

FEDERAL RESERVE SYSTEM

12 CFR Part 220

Regulation T; Docket No. R-1131 Credit by Brokers and Dealers; Security Futures

AGENCY: Board of Governors of the Federal Reserve System.

ACTION: Proposed rule.

SUMMARY: The Board of Governors is publishing for comment proposed amendments to Regulation T to clarify the treatment of stock futures held by customers at a security futures intermediary. The proposed amendments would permit the withdrawal of cash from an otherwise restricted margin account if required to satisfy maintenance margin requirements. The proposed amendments also would explicitly permit stock futures to be carried in a good faith account as is currently done with other futures.

DATES: Comments on the proposed rule must be received not later than November 15, 2002.

ADDRESSES: Comments should refer to docket number R-1131 and should be sent to Ms. Jennifer J. Johnson, Secretary, Board of Governors of the Federal Reserve System, 20th Street and Constitution Avenue, N.W., Washington, D.C., 20551 or mailed electronically to regs.comments@federalreserve.gov. Comments addressed to Ms. Johnson also may be delivered between 8:45 a.m. and 5:15 p.m. to the Board's mail facility in the west courtyard of the Eccles Building, located on 21st Street between Constitution Avenue and C Street, N.W. Members of the public may inspect comments in accordance with the Board's Rules Regarding the Availability of Information (12 CFR Part 261) in Room MP-500 of the Martin Building on weekdays between 9:00 a.m. and 5:00 p.m.

FOR FURTHER INFORMATION CONTACT: Scott Holz, Senior Counsel (202/452-2966) or Thomas Scanlon, Senior Attorney (202/452-3594), Legal Division; for users of Telecommunication Devices for the Deaf (TDD) only, contact 202/263-4869.

SUPPLEMENTARY INFORMATION:

1. Background

The Commodity Futures Modernization Act of 2000¹ ("CFMA") lifted the ban on futures on single stocks and narrow-based stock indexes, as well as options on these futures (hereinafter "stock futures").² The CFMA required the Board either to adopt margin rules for stock futures or to delegate its authority jointly to the Commodity Futures Trading Commission and Securities and Exchange Commission. The Board delegated its authority to the Commissions in a letter dated March 6, 2001. The Commissions published proposed margin rules for public comment in the Federal Register on October 4, 2001³ and published joint final margin rules in the Federal Register on August 14, 2002.⁴

¹ Pub. L. No. 106-554, Appendix E

² The CFTC and SEC have adopted rules for futures on single stocks and narrow-based stock indexes. The CFMA does not authorize the trading of options on these futures before late 2003. The Board is today proposing amendments that would cover all stock future products, including options. If the CFTC and SEC adopt additional margin rules for stock futures options (under the authority delegated by the Board in 2001), the Board may wish to propose further amendments to Regulation T.

³ 66 FR 50720.

⁴ 67 FR 53146.

Brokers and dealers are generally subject to the Board's Regulation T⁵ when they effect transactions for customers. Although the Board has delegated its authority over margin requirements for stock futures to the Commissions, these transactions will be effected in one or more securities accounts described in Regulation T. The Board is proposing amendments to Regulation T to eliminate potential conflicts between the regulation and the Commissions' joint margin rules. We invite your comments on all aspects of the proposal.

2. Stock futures held in a securities margin account

A. Margin requirements for stock futures

Margin requirements for stock futures are established by the Commissions' joint margin rules, and stock futures may be subject to additional requirements of the self-regulatory organizations (SROs). The Board is proposing to amend section 220.4(b)(1) of Regulation T ("Margin Account – Applicability) to state explicitly that stock futures are not subject to the margin requirements of Regulation T found in section 220.12 ("Supplement: margin requirements").

B. Withdrawals to meet variation settlement obligations

Although positions in futures and securities are marked-to-market daily to determine if additional margin is required, the procedures for the two markets differ. With futures contracts, the daily marked-to-market amount, known as "variation settlement" is paid by customers with positions that have declined in value to customers on the other side of the contract whose positions have risen in value. With securities, customers whose positions have declined in value are not required to post additional collateral unless the decline is large enough to trigger the maintenance margin requirements of the SROs. The securities margining system has nothing comparable to the payment that occurs between customers under the futures margining system.

Section 220.4(e) of Regulation T prohibits a customer from withdrawing cash or securities from a margin account if there is an outstanding Regulation T margin call or if the withdrawal, together with other transactions on the same day, would create or increase a margin deficiency. The Board believes this restriction should not apply to a customer who is required to make a variation settlement payment under the Commissions' joint margin rules or SRO margin rules. The Board is therefore proposing an exception to the withdrawal provision for such customers. Withdrawals permitted under the proposed amendment would not be made available to the customer whose account is debited as the funds will be used exclusively to pay the customer on the other side of the stock futures contract.

3. Stock futures held in a futures account

Stock futures are securities under the Securities Exchange Act of 1934 ("SEA") and contracts of sale for future delivery under the Commodities Exchange Act ("CEA"). The Commissions' joint margin rules provide that stock futures may be held in either a securities or a futures account. Under Regulation T, stock futures transactions may be effected and carried in a margin account because they are securities under the SEA. Under Regulation T, transactions involving contracts of sale for future delivery are recorded in the good faith account,⁶ which is not subject to the restrictions of the margin account. The Board is proposing to amend section 220.6(e) of Regulation T to provide explicitly that stock futures may be effected and carried in the good faith account.

Paperwork Reduction Act

In accordance with the Paperwork Reduction Act of 1995 (44 U.S.C. 3506; 5 CFR 1320 Appendix A.1), the Board reviewed the proposed rule under the authority delegated to the Board by the Office of Management and Budget. No collections of information pursuant to the Paperwork Reduction Act are contained in the proposed rule.

⁵ 12 CFR Part 220.

⁶ Section 220.6(e).

Regulatory Flexibility Act

The Board certifies that the proposed amendments, if adopted, will not have a significant economic impact on a substantial number of small entities. The only substantive effect of the proposed amendments is to eliminate a potential conflict with other federal margin regulations promulgated by the CFTC and SEC.

List of Subjects in 12 CFR Part 220

Brokers, Reporting and recordkeeping requirements, Securities.

AUTHORITY AND ISSUANCE

For the reasons set forth in the preamble, the Board proposes to amend 12 CFR Part 220 to read as follows:

PART 220 -- CREDIT BY BROKERS AND DEALERS (REGULATION T)

- 1. The authority citation for Part 220 continues to read as follows:

Authority: 15 U.S.C. 78c, 78g, 78q, and 78w.

- 2. Section 220.4 is amended as follows:
 - a. by revising paragraph (b)(1); and
 - b. by adding a new paragraph (e)(4).

The revision and addition read as follows:

§ 220.4 Margin Account.

* * * * *

(b) Required margin. — (1) Applicability. The required margin for each long or short position in securities (except for security futures products) is set forth in § 220.12 (the Supplement) and is subject to the following exceptions and special provisions.

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(e) Withdrawals of cash or securities.

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(4) The provisions of this paragraph (e) shall not apply to a withdrawal of cash to meet variation settlement obligations for security futures products held in a margin account.

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- 3. Section 220.6(e)(1) introductory text and (i) are revised to read as follows:

§ 220.6 Good faith account.

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(e) Nonpurpose credit and security futures products. (1) A creditor may:

- (i) Effect and carry transactions in commodities, including transactions in security futures products;

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By order of the Board of Governors of the Federal Reserve System, September 30, 2002.

Jennifer J. Johnson
Secretary of the Board.