

## Covered Agency Transactions

### SEC Approves Amendments to FINRA Rule 4210 (Margin Requirements) to Establish Margin Requirements for Covered Agency Transactions

Effective Date of Risk Limit Determination Requirements:  
December 15, 2016

Effective Date of All Other Requirements: December 15, 2017

#### Executive Summary

The SEC has approved<sup>1</sup> FINRA's rule change amending FINRA Rule 4210 to establish margin requirements for Covered Agency Transactions. Covered Agency Transactions include (1) To Be Announced (TBA) transactions, inclusive of adjustable rate mortgage (ARM) transactions, (2) Specified Pool Transactions and (3) transactions in Collateralized Mortgage Obligations (CMOs), issued in conformity with a program of an agency or Government-Sponsored Enterprise (GSE), with forward settlement dates, as discussed more fully in this *Notice*.

This *Notice* provides an overview of the rule change. The rule change becomes effective in two phases:

- ▶ The amendments relating to the risk limit determination requirements are effective on December 15, 2016. These are shown in Appendix A.
- ▶ All other amendments pursuant to the rule change go into effect on December 15, 2017. Appendix B shows the complete text of the amendments as effective on that date.

Questions regarding this *Notice* should be directed to:

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## August 2016

#### Notice Type

- ▶ New Rule

#### Suggested Routing

- ▶ Compliance
- ▶ Legal
- ▶ Margin Department
- ▶ Operations
- ▶ Regulatory Reporting
- ▶ Risk Management
- ▶ Senior Management

#### Key Topics

- ▶ Covered Agency Transactions
- ▶ Margin
- ▶ TBA Market

#### Referenced Rules & Notices

- ▶ FINRA Rule 4210
- ▶ FINRA Rule 6710
- ▶ SEA Rule 15c3-1

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- ▶ Adam Arkel, Associate General Counsel, Office of General Counsel, at (202) 728-6961 or [Adam.Arkel@finra.org](mailto:Adam.Arkel@finra.org).

Questions may also be directed to [covered.agency.margin@finra.org](mailto:covered.agency.margin@finra.org). FINRA will publish additional guidance as appropriate to address questions that FINRA receives.

## Background & Discussion

### Overview

The SEC has approved FINRA's amendments<sup>2</sup> to FINRA Rule 4210 to establish margin requirements for Covered Agency Transactions.

- ▶ Broadly, under the rule change, unless the rule provides for an exception:
  - ▶ members are required to collect daily mark to market margin from all counterparties for their Covered Agency Transactions; and
  - ▶ in addition to the daily mark to market margin, maintenance margin of two percent is required for accounts that are not "exempt accounts" as that term is defined in FINRA Rule 4210(a)(13) (see note 3 for more information).
- ▶ Members that engage in Covered Agency Transactions with any counterparty must make and enforce a written risk limit determination for each such counterparty. Risk limit determinations may be made at the investment adviser level if a member engages in transactions with advisory clients of a registered investment adviser.
- ▶ Broadly, under the rule change, members are required to include any mark to mark loss or maintenance margin deficiency from their Covered Agency Transactions toward the concentration thresholds specified under paragraph (e)(2)(l), as redesignated by the amendments.
- ▶ The rule change provides for several exceptions or allowances, including:
  - ▶ the new margin requirements do not apply to transactions that are cleared through a registered clearing agency and are subject to the margin requirements of that clearing agency;
  - ▶ the new margin requirements (both daily mark to market and maintenance margin) do not apply to any counterparty that has gross open positions in Covered Agency Transactions with the member amounting to \$10 million or less if the counterparty regularly settles its Covered Agency Transactions on a Delivery Versus

Payment (DVP) basis or for cash and meets other specified conditions. However, members should be aware that any amounts excepted pursuant to this exclusion must be included toward the concentration thresholds specified in redesignated paragraph (e)(2)(I);

- ▶ similarly, a non-exempt account is excepted from the two percent maintenance margin requirement if the non-exempt account regularly settles its Covered Agency Transactions on a DVP basis or for cash and meets other specified conditions;
- ▶ the rule change provides an aggregate \$250,000 *de minimis* transfer amount with a single counterparty, so that if the aggregate required but uncollected maintenance margin or mark to market loss does not exceed that amount, the margin need not be collected or charged to net capital. However, members should be aware that any amounts allowed pursuant to this exclusion must be included toward the concentration thresholds specified in redesignated paragraph (e)(2)(I);
- ▶ a member is not required to apply the new margin requirements to transactions in multifamily housing securities or project loan program securities, provided the member makes and enforces a written risk limit for each counterparty in these transactions;
- ▶ subject to specified conditions, members may treat mortgage bankers that hedge their pipeline of mortgage commitments as exempt accounts;
- ▶ a member may elect not to apply the new margin requirements to any counterparty that is a Federal banking agency, central bank, or other similar instrumentality of sovereign governments, as specified by the rule, provided the member makes and enforces a written risk limit determination for each such counterparty.

FINRA is implementing the rule change in two phases. First, the requirements to make and enforce written risk limit determinations as specified by the rule become effective on December 15, 2016. Second, the remainder of the rule change becomes effective on December 15, 2017.

## Detailed Discussion

The core requirements of the rule change are intended to reach members engaging in Covered Agency Transactions with counterparties as specified in the rule. New paragraph (e)(2)(H) establishes a set of definitions and addresses the types of counterparties that are subject to the new requirements, risk limit determinations, specified exceptions or allowances, transactions with exempt accounts,<sup>3</sup> transactions with non-exempt accounts, and the treatment of standbys. As discussed further below, the rule change also includes revisions to the concentration limit provisions under newly redesignated paragraph (e)(2)(I) as well as conforming revisions to paragraphs (a)(13)(B)(i), (e)(2)(F), (e)(2)(G) and (f)(6).

## Definitions Established for Purposes of Paragraph (e)(2)(H)

### ▶ Covered Agency Transactions

Paragraph (e)(2)(H)(i)c. of the rule defines Covered Agency Transactions to mean:

- ▶ TBA transactions, as defined in FINRA Rule 6710(u),<sup>4</sup> inclusive of ARM transactions, for which the difference between the trade date and contractual settlement date is greater than one business day;
- ▶ Specified Pool Transactions, as defined in FINRA Rule 6710(x),<sup>5</sup> for which the difference between the trade date and contractual settlement date is greater than one business day; and
- ▶ CMOs, as defined in FINRA Rule 6710(dd),<sup>6</sup> issued in conformity with a program of an agency, as defined in FINRA Rule 6710(k),<sup>7</sup> or a GSE, as defined in FINRA Rule 6710(n),<sup>8</sup> for which the difference between the trade date and contractual settlement date is greater than three business days.

In addition to Covered Agency Transactions, the rule change establishes the following other key definitions:<sup>9</sup>

- ▶ **Bilateral transaction:** a Covered Agency Transaction that is not cleared through a registered clearing agency as defined in paragraph (f)(2)(A)(xxviii) of Rule 4210;<sup>10</sup>
- ▶ **Counterparty:** any person that enters into a Covered Agency Transaction with a member and includes a “customer” as defined in paragraph (a)(3) of Rule 4210;
- ▶ **Deficiency:** the amount of any required but uncollected maintenance margin and any required but uncollected mark to market loss;
- ▶ **Gross open position:** with respect to Covered Agency Transactions, the amount of the absolute dollar value of all contracts entered into by a counterparty, in all CUSIPs; provided, however, that such amount shall be computed net of any settled position of the counterparty held at the member and deliverable under one or more of the counterparty’s contracts with the member and which the counterparty intends to deliver;
- ▶ **Maintenance margin:** margin equal to two percent of the contract value of the net long or net short position, by CUSIP, with the counterparty;
- ▶ **Mark to market loss:** the counterparty’s loss resulting from marking a Covered Agency Transaction to the market;
- ▶ **Mortgage banker:** an entity, however organized, that engages in the business of providing real estate financing collateralized by liens on such real estate;
- ▶ **Round robin trade:** any transaction or transactions resulting in equal and offsetting positions by one customer with two separate dealers for the purpose of eliminating a turnaround delivery obligation by the customer; and
- ▶ **Standby:** contracts that are put options that trade OTC, as defined in paragraph (f)(2)(A)(xxvii) of Rule 4210, with initial and final confirmation procedures similar to those on forward transactions.

### Requirement to Make and Enforce Risk Limits

Paragraph (e)(2)(H)(ii)b. of the rule provides that members that engage in Covered Agency Transactions with any counterparty shall make a determination in writing of a risk limit for each such counterparty that the member shall enforce.<sup>11</sup> The rule provides that the risk limit determination shall be made by a designated credit risk officer or credit risk committee in accordance with the member's written risk policies and procedures. Further, in connection with risk limit determinations, the rule establishes new Supplementary Material .05, which provides that, for purposes of any risk limit determination pursuant to paragraphs (e)(2)(F), (e)(2)(G)<sup>12</sup> or (e)(2)(H) of the rule:

- ▶ If a member engages in transactions with advisory clients of a registered investment adviser, the member may elect to make the risk limit determination at the investment adviser level;<sup>13</sup>
- ▶ Members of limited size and resources that do not have a credit risk officer or credit risk committee may designate an appropriately registered principal to make the risk limit determinations;
- ▶ The member may base the risk limit determination on consideration of all products involved in the member's business with the counterparty, provided the member makes a daily record of the counterparty's risk limit usage; and
- ▶ A member shall consider whether the margin required pursuant to the rule is adequate with respect to a particular counterparty account or all its counterparty accounts and, where appropriate, increase such requirements.

Members should note that the risk limit determination requirements under the rule change become effective on December 15, 2016. *See* Implementation Phases below.

### Margin Requirements for Covered Agency Transactions

#### Key Exceptions or Allowances

Paragraph (e)(2)(H)(ii)a. provides that all Covered Agency Transactions with any counterparty, regardless of the type of account to which booked, are subject to the provisions of paragraph (e)(2)(H) of the rule. The rule change specifies several exceptions or allowances (*see also further discussion in* Margin Requirements for Exempt Accounts *and* Margin Requirements for Non-Exempt Accounts below):

- ▶ **Federal banking agencies and other entities:** Paragraph (e)(2)(H)(ii)a.1. of the rule provides that with respect to Covered Agency Transactions with any counterparty that is a Federal banking agency, as defined in 12 U.S.C. 1813(z) under the Federal Deposit Insurance Act,<sup>14</sup> central bank, multinational central bank, foreign sovereign, multilateral development bank, or the Bank for International Settlements, a member may elect not to apply the margin requirements specified in paragraph (e)(2)(H) provided the member makes a written risk limit determination for each such counterparty that the member shall enforce pursuant to paragraph (e)(2)(H)(ii)b. (*see* Requirement to Make and Enforce Risk Limits above).

- ▶ **Multifamily housing securities and project loan program securities:** Paragraph (e)(2)(H)(ii)a.2. of the rule provides that a member is not required to apply the margin requirements of paragraph (e)(2)(H) with respect to Covered Agency Transactions with a counterparty in multifamily housing securities or project loan program securities, provided that:
  - a. such securities are issued in conformity with a program of an agency, as defined in FINRA Rule 6710(k),<sup>15</sup> or a GSE, as defined in FINRA Rule 6710(n),<sup>16</sup> and are documented as Freddie Mac K Certificates, Fannie Mae Delegated Underwriting and Servicing bonds, or Ginnie Mae Construction Loan or Project Loan Certificates, as commonly known to the trade, or are such other multifamily housing securities or project loan program securities with substantially similar characteristics, issued in conformity with a program of an agency or a GSE, as FINRA may designate by *Regulatory Notice* or similar communication; and
  - b. the member makes a written risk limit determination for each such counterparty that the member shall enforce pursuant to paragraph (e)(2)(H)(ii)b. (*see Requirement to Make and Enforce Risk Limits above*).
- ▶ **Registered Clearing Agencies:** Paragraph (e)(2)(H)(ii)c.1. provides that the margin requirements specified in paragraph (e)(2)(H) of the rule shall not apply to Covered Agency Transactions that are cleared through a registered clearing agency, as defined in FINRA Rule 4210(f)(2)(A)(xxviii),<sup>17</sup> and are subject to the margin requirements of that clearing agency.
- ▶ **Gross Open Positions of \$10 Million or Less:** Paragraph (e)(2)(H)(ii)c.2. provides that the margin requirements specified in paragraph (e)(2)(H) of the rule shall not apply to any counterparty that has gross open positions in Covered Agency Transactions with the member amounting to \$10 million or less in aggregate, if the original contractual settlement for all such transactions is in the month of the trade date for such transactions or in the month succeeding the trade date for such transactions and the counterparty regularly settles<sup>18</sup> its Covered Agency Transactions on a Delivery Versus Payment (DVP) basis or for cash; provided, however, that such exception from the margin requirements shall not apply to a counterparty that, in its transactions with the member, engages in dollar rolls, as defined in FINRA Rule 6710(z),<sup>19</sup> or round robin trades, or that uses other financing techniques<sup>20</sup> for its Covered Agency Transactions. *Members should be aware that amounts excepted pursuant to the \$10 million exclusion must be included toward the concentration thresholds as set forth under redesignated paragraph (e)(2)(l), as discussed below.*

*Note: Members should note that the above-described exceptions are exceptions to the margin requirements under paragraph (e)(2)(H). The requirement to determine risk limits pursuant to paragraph (e)(2)(H)(ii)b. applies.*

- ▶ **De Minimis Transfer Amounts:** Paragraph (e)(2)(H)(ii)f. of the rule provides that any deficiency, as set forth in paragraph (e)(2)(H)(ii)e. of the rule, or mark to market losses, as set forth in paragraph (e)(2)(H)(ii)d. of the rule, with a single counterparty (whether an exempt or non-exempt account) shall not give rise to any margin requirement, and as such need not be collected or charged to net capital, if the aggregate of such amounts with such counterparty does not exceed \$250,000 (referred to as “the *de minimis* transfer amount”). The rule provides that the full amount of the sum of the required maintenance margin and any mark to market loss must be collected when such sum exceeds the *de minimis* transfer amount. *Members should note that amounts excepted as de minimis transfer amounts must be included toward the concentration thresholds as set forth under redesignated paragraph (e)(2)(l), as discussed below.*

### Margin Requirements for Exempt Accounts

Paragraph (e)(2)(H)(ii)d. of the rule provides that, on any net long or net short position, by CUSIP, resulting from bilateral transactions with a counterparty that is an exempt account,<sup>21</sup> no maintenance margin<sup>22</sup> shall be required. However, the rule provides that such transactions must be marked to the market daily and the member must collect any net mark to market loss,<sup>23</sup> unless otherwise provided under paragraph (e)(2)(H)(ii)f. of the rule.<sup>24</sup> The rule provides that if the mark to market loss is not satisfied by the close of business on the next business day after the business day on which the mark to market loss arises, the member shall be required to deduct the amount of the mark to market loss from net capital as provided in SEA Rule 15c3-1 until such time the mark to market loss is satisfied. The rule requires that if such mark to market loss is not satisfied within five business days from the date the loss was created, the member must promptly liquidate positions to satisfy the mark to market loss, unless FINRA has specifically granted the member additional time. FINRA expects to establish a process that members may use to request extensions of time specifically related to Covered Agency Transactions.<sup>25</sup>

Paragraph (e)(2)(H)(ii)d. further provides that members may treat mortgage bankers that use Covered Agency Transactions to hedge their pipeline of mortgage commitments as exempt accounts for purposes of paragraph (e)(2)(H). In this regard, the rule change adds new Supplementary Material .02, which provides that, for purposes of paragraph (e)(2)(H)(ii)d. of the rule, members must adopt written procedures to monitor the mortgage banker’s pipeline of mortgage loan commitments to assess whether the Covered Agency Transactions are being used for hedging purposes. FINRA has noted that this is intended to ensure that, if a mortgage banker is permitted exempt account treatment, the member has conducted sufficient due diligence to determine that the mortgage banker is hedging its pipeline of mortgage production.<sup>26</sup>

Members should note that the exception under the rule change for gross open positions of \$10 million or less is available to exempt accounts that meet the specified conditions under the rule. See Gross Open Positions of \$10 Million or Less above.

### Margin Requirements for Non-Exempt Accounts

Paragraph (e)(2)(H)(ii)e. of the rule provides that, on any net long or net short position, by CUSIP, resulting from bilateral transactions with a counterparty that is not an exempt account, maintenance margin, plus any net mark to market loss on such transactions, shall be required margin, and the member shall collect the deficiency, as defined in paragraph (e)(2)(H)(i)d. of the rule,<sup>27</sup> unless otherwise provided under paragraph (e)(2)(H)(ii)f. of the rule. The rule provides that if the deficiency is not satisfied by the close of business on the next business day after the business day on which the deficiency arises, the member shall be required to deduct the amount of the deficiency from net capital as provided in SEA Rule 15c3-1 until such time the deficiency is satisfied.<sup>28</sup> Further, the rule provides that if such deficiency is not satisfied within five business days from the date the deficiency was created, the member shall promptly liquidate positions to satisfy the deficiency, unless FINRA has specifically granted the member additional time. As noted earlier, FINRA expects to establish a process that members may use to request extensions of time specifically related to Covered Agency Transactions.<sup>29</sup>

The rule makes an exception available to non-exempt accounts with respect to the maintenance margin requirement. Specifically, the rule provides that no maintenance margin is required if the original contractual settlement for the Covered Agency Transaction is in the month of the trade date for such transaction or in the month succeeding the trade date for such transaction and the customer regularly settles<sup>30</sup> its Covered Agency Transactions on a DVP basis or for cash; provided, however, that such exception from the required maintenance margin shall not apply to a non-exempt account that, in its transactions with the member, engages in dollar rolls, as defined in FINRA Rule 6710(z), or round robin trades, as defined in paragraph (e)(2)(H)(i)i., or that uses other financing techniques<sup>31</sup> for its Covered Agency Transactions.

Members should note that the exception under the rule change for gross open positions of \$10 million or less is available to non-exempt accounts that meet the specified conditions under the rule. *See Gross Open Positions of \$10 Million or Less above.*

### Unrealized Profits; Standbys

Paragraph (e)(2)(H)(ii)g. of the rule provides that unrealized profits in one Covered Agency Transaction position may offset losses from other Covered Agency Transaction positions in the same counterparty's account and the amount of net unrealized profits may be used to reduce margin requirements. The rule provides that, with respect to standbys, only profits (in-the-money amounts), if any, on long standbys shall be recognized.

### Limits on Net Capital Deductions – Redesignated Paragraph (e)(2)(I)

Current (prior to the rule change) paragraph (e)(2)(H) of FINRA Rule 4210 imposes upon members a specified obligation to notify FINRA and refrain from new transactions if the member's net capital deductions as a result of marked to the market losses incurred under paragraphs (e)(2)(F) and (e)(2)(G) of the rule exceed specified thresholds. The rule change



redesignates current paragraph (e)(2)(H) as new paragraph (e)(2)(I) and makes conforming revisions to include Covered Agency Transactions and to reflect the requirements of new paragraph (e)(2)(H). Specifically, new, redesignated paragraph (e)(2)(I)(i) of the rule provides that, in the event that the net capital deductions taken by a member as a result of deficiencies or marked to the market losses incurred under paragraphs (e)(2)(F) and (e)(2)(G) of the rule (exclusive of the percentage requirements established thereunder), plus any mark to market loss as set forth under paragraph (e)(2)(H)(ii)d. of the rule and any deficiency as set forth under paragraph (e)(2)(H)(ii)e. of the rule, and inclusive of all amounts excepted from margin requirements as set forth under paragraph (e)(2)(H)(ii)c.2. of the rule or any *de minimis* transfer amount as set forth under paragraph (e)(2)(H)(ii)f. of the rule, exceed:

- ▶ for any one account or group of commonly controlled accounts, 5 percent of the member's tentative net capital (as such term is defined in SEA Rule 15c3-1), or
- ▶ for all accounts combined, 25 percent of the member's tentative net capital (as such term is defined in SEA Rule 15c3-1), and,
- ▶ such excess as calculated in paragraphs (e)(2)(I)(i)a. or b. of the rule continues to exist on the fifth business day after it was incurred,

the member must give prompt written notice to FINRA and shall not enter into any new transaction(s) subject to the provisions of paragraphs (e)(2)(F), (e)(2)(G) or (e)(2)(H) of the rule that would result in an increase in the amount of such excess under, as applicable, paragraph (e)(2)(I)(i) of the rule.

*As discussed earlier, members should note that, under the new rule, de minimis transfer amounts must be included toward the five percent and 25 percent thresholds, as specified, as well as amounts pursuant to the specified exception under new paragraph (e)(2)(H) for gross open positions of \$10 million or less in aggregate.*

#### Implementation Phases

- ▶ The risk limit determination provisions under the rule change become effective on December 15, 2016. These provisions include new paragraph (e)(2)(H)(ii)b., new Supplementary Material .05, and the second text paragraph under paragraph (e)(2)(F) and paragraph (e)(2)(G), each as revised by the rule change. To help effectuate the application of these provisions, the definition of "counterparty," as set forth in paragraph (e)(2)(H)(i)b., and the definition of "Covered Agency Transaction," as set forth in paragraph (e)(2)(H)(i)c., also become effective on December 15, 2016. In addition, to ensure clarity, FINRA has specified cross-references, text and headers in the rule change that become effective on December 15, 2016.<sup>32</sup> Appendix A of this *Notice* shows the text of the rule change as effective on that date.
- ▶ All other provisions of the rule change become effective on December 15, 2017. Appendix B of this *Notice* shows the text of the rule change as effective on that date.

## Endnotes

1. See Securities Exchange Act Release No. 78081 (June 15, 2016), 81 FR 40364 (June 21, 2016) (Notice of Filing of Amendment No. 3 and Order Granting Accelerated Approval to a Proposed Rule Change To Amend FINRA Rule 4210 (Margin Requirements) To Establish Margin Requirements for the TBA Market, as Modified by Amendment Nos. 1, 2, and 3; File No. SR-FINRA-2015-036). The rule change redesignates current (prior to the rule change) paragraph (e)(2)(H) of FINRA Rule 4210 as new paragraph (e)(2)(I), adds new paragraph (e)(2)(H), makes conforming revisions to paragraphs (a)(13)(B)(i), (e)(2)(F), (e)(2)(G), (e)(2)(I) (as redesignated by the rule change), and (f)(6), and adds to the rule new Supplementary Materials .02 through .05.
2. See note 1.
3. The term “exempt account” is defined under FINRA Rule 4210(a)(13). Broadly, an exempt account means a FINRA member, non-FINRA member registered broker-dealer, account that is a “designated account” under FINRA Rule 4210(a)(4) (specifically, a bank as defined under SEA Section 3(a)(6), a savings association as defined under Section 3(b) of the Federal Deposit Insurance Act, the deposits of which are insured by the Federal Deposit Insurance Corporation, an insurance company as defined under Section 2(a)(17) of the Investment Company Act, an investment company registered with the Commission under the Investment Company Act, a state or political subdivision thereof, or a pension or profit sharing plan subject to the Employee Retirement Income Security Act or of an agency of the United States or of a state or political subdivision thereof), and any person that has a net worth of at least \$45 million and financial assets of at least \$40 million for purposes of paragraphs (e)(2)(F) and (e)(2)(G) of the rule, as currently set forth under paragraph (a)(13)(B)(i) of Rule 4210, and meets specified conditions as set forth under paragraph (a)(13)(B)(ii). FINRA notes that the rule change makes a conforming revision to paragraph (a)(13)(B)(i) so that the phrase “for purposes of paragraphs (e)(2)(F) and (e)(2)(G)” as revised reads “for purposes of paragraphs (e)(2)(F), (e)(2)(G) and (e)(2)(H).”
4. FINRA Rule 6710(u) defines “TBA” to mean a transaction in an Agency Pass-Through Mortgage-Backed Security (“MBS”) or a Small Business Administration (“SBA”)-Backed Asset-Backed Security (“ABS”) where the parties agree that the seller will deliver to the buyer a pool or pools of a specified face amount and meeting certain other criteria but the specific pool or pools to be delivered at settlement is not specified at the Time of Execution, and includes TBA transactions for good delivery and TBA transactions not for good delivery. Agency Pass-Through MBS and SBA-Backed ABS are defined under FINRA Rule 6710(v) and FINRA Rule 6710(bb), respectively. The term “Time of Execution” is defined under FINRA Rule 6710(d).
5. FINRA Rule 6710(x) defines Specified Pool Transaction to mean a transaction in an Agency Pass-Through MBS or an SBA-Backed ABS requiring the delivery at settlement of a pool or pools that is identified by a unique pool identification number at the Time of Execution.
6. FINRA Rule 6710(dd) defines CMO to mean a type of Securitized Product backed by Agency Pass-Through MBS, mortgage loans, certificates backed by project loans or construction loans, other types of MBS or assets derivative of MBS, structured in multiple classes or tranches with each class or tranche entitled to receive distributions of principal or interest according to the requirements adopted for the specific class or tranche, and includes a real estate mortgage investment conduit (“REMIC”).

## Endnotes

7. FINRA Rule 6710(k) defines “agency” to mean a United States executive agency as defined in 5 U.S.C. 105 that is authorized to issue debt directly or through a related entity, such as a government corporation, or to guarantee the repayment of principal or interest of a debt security issued by another entity. The term excludes the U.S. Department of the Treasury in the exercise of its authority to issue U.S. Treasury Securities as defined under FINRA Rule 6710(p). Under 5 U.S.C. 105, the term “executive agency” is defined to mean an “Executive department, a Government corporation, and an independent establishment.”
8. FINRA Rule 6710(n) defines GSE to have the meaning set forth in 2 U.S.C. 622(8). Under 2 U.S.C. 622(8), a GSE is defined, in part, to mean a corporate entity created by a law of the United States that has a Federal charter authorized by law, is privately owned, is under the direction of a board of directors, a majority of which is elected by private owners, and, among other things, is a financial institution with power to make loans or loan guarantees for limited purposes such as to provide credit for specific borrowers or one sector and raise funds by borrowing (which does not carry the full faith and credit of the Federal Government) or to guarantee the debt of others in unlimited amounts.
9. These are found in paragraphs (e)(2)(H)(i)a. through (H)(i)b. and (H)(i)d. through (H)(i)j. of the new rule. See Appendix A and Appendix B.
10. FINRA Rule 4210(f)(2)(A)(xxviii) defines registered clearing agency to mean a clearing agency as defined in SEA Section 3(a)(23) that is registered with the SEC pursuant to SEA Section 17A(b)(2).
11. FINRA notes that the rule is intended to require a member to make, and enforce, a written risk limit determination *for each counterparty* with which the member engages in Covered Agency Transactions.
12. Paragraph (e)(2)(F) addresses transactions with exempt accounts involving certain good faith securities. Paragraph (e)(2)(G) addresses transactions with exempt accounts involving highly rated foreign sovereign debt securities and investment grade debt securities. With regard to risk limit determinations, members should note that the rule change makes revisions to both these paragraphs. Specifically, current (prior to the rule change) paragraph (e)(2)(H)(i) provides that members must maintain a written risk analysis methodology for assessing the amount of credit extended to exempt accounts pursuant to paragraphs (e)(2)(F) and (e)(2)(G) which shall be made available to FINRA upon request. The rule change moves this language to paragraphs (e)(2)(F) and (e)(2)(G) and adds to each the requirement that the risk limit determination shall be made by a designated credit risk officer or credit risk committee in accordance with the member’s written risk policies and procedures. FINRA notes that the rule change also makes other conforming revisions to paragraphs (e)(2)(F) and (e)(2)(G) in the interest of clarifying the rule’s structure and otherwise conforming the rule in light of new paragraph (e)(2)(H). See Appendix A and Appendix B.
13. FINRA has noted that it expects members to be mindful of their obligations as to making and enforcing risk limits under the rule. In making risk limit determinations as to advisory accounts, FINRA expects members to exercise appropriate diligence in understanding the extent of their risk and to craft their risk limit determinations accordingly. See [SR-FINRA-2015-036](#), Partial Amendment No. 3.
14. 12 U.S.C. 1813(z) defines “Federal banking agency” to mean the Comptroller of the Currency, the Board of Governors of the Federal Reserve System, or the Federal Deposit Insurance Corporation.

15. See note 7.
16. See note 8.
17. See note 10.
18. FINRA has noted that the term “regularly settles” is meant to provide scope for flexibility on members’ part as to how they implement the requirement. FINRA expects that members are in a position to make reasonable judgments as to the observed pattern and course of dealing in their customers’ behavior by virtue of their interactions with their customers. FINRA views the term “regularly” as conveying the prevailing or dominant pattern and course of the customer’s behavior. FINRA would not view, for instance, “substantial portion of the time” as equivalent to “regularly.” In ascertaining the customer’s regular pattern, a member may use the customer’s history of transactions with the member, as well as any other relevant information of which the member is aware. Further, FINRA believes members should be able to rely on the reasonable representations of their customers for purposes of the requirement. See [SR-FINRA-2015-036](#), Partial Amendment No. 1 and Partial Amendment No. 2.
19. FINRA Rule 6710(z) defines “dollar roll” to mean a simultaneous sale and purchase of an Agency Pass-Through MBS for different settlement dates, where the initial seller agrees to take delivery, upon settlement of the re-purchase transaction, of the same or substantially similar securities.
20. FINRA has noted that it believes the term “other financing techniques” should be clear as a matter of plain language, that is, transactions other than on a DVP basis or for cash suggest the use of financing. FINRA does not expect that a customer that engages in a single dollar roll or round robin trade would be denied access to the specified exception provided the member can reasonably demonstrate a regular pattern by the customer of settling its Covered Agency Transactions on a DVP basis or for cash. Again, FINRA has noted a member may use the customer’s history of transactions with the member, as well as any other relevant information of which the member is aware. Further, FINRA believes that members should be able to rely on the reasonable representations of their customers where necessary for purposes of the requirement. See [SR-FINRA-2015-036](#), Partial Amendment No. 1.
21. The rule change adds to FINRA Rule 4210 new Supplementary Material .04, which provides that, for purposes of paragraph (e)(2)(H) of the rule, the determination of whether an account qualifies as an exempt account must be based upon the beneficial ownership of the account. The rule provides that sub-accounts managed by an investment adviser, where the beneficial owner is other than the investment adviser, must be margined individually. As discussed earlier, the new rule provides that risk limit determinations may be made at the investment adviser level. See Requirement to Make and Enforce Risk Limits above.
22. As discussed earlier, the definition of “maintenance margin” specifies margin equal to two percent of the contract value of the net long or net short position, by CUSIP, with the counterparty.
23. As discussed above, “mark to market loss” means the counterparty’s loss resulting from marking a Covered Agency Transaction to the market.
24. As discussed above, paragraph (e)(2)(H)(ii)f. addresses the treatment of *de minimis* transfer amounts.

25. Current (prior to the rule change) paragraph (f)(6) of FINRA Rule 4210 permits up to 15 business days for obtaining the amount of margin or mark to market, unless FINRA has specifically granted the member additional time. The rule change makes a conforming revision to paragraph (f)(6) so as to accommodate the five days specified under the new rule. See Appendix B. Members should note that FINRA maintains, and regularly updates, the Regulatory Extension System (REX) for purposes of granting additional time pursuant to Rule 4210. FINRA will announce updates to REX to accommodate firms' requests for extensions of time related to Covered Agency Transactions prior to the effective date of the new margin requirements. FINRA has noted that the Regulatory Extension System does not grant waivers from requirements under Rule 4210, whether permanent or temporary. FINRA grants additional time, pursuant to the rule, for meeting specified obligations and, consistent with longstanding practice under the rule, FINRA may limit or restrict the extensions granted. See [SR-FINRA-2015-036](#), Partial Amendment No. 2.
26. See 80 FR 63603, 63607 n. 54. FINRA has noted that it believes members should be able to rely on the reasonable representations of their mortgage banker customers where necessary for purposes of this requirement. See [SR-FINRA-2015-036](#), Partial Amendment No. 1.
27. As discussed above, "deficiency" means the amount of any required but uncollected maintenance margin and any required but uncollected mark to market loss.
28. The rule change adds to FINRA Rule 4210 new Supplementary Material .03, which provides that, for purposes of paragraph (e)(2)(H) of the rule, to the extent a mark to market loss or deficiency is cured by subsequent market movements prior to the time the margin call must be met, the margin call need not be met and the position need not be liquidated; provided, however, if the mark to market loss or deficiency is not satisfied by the close of business on the next business day after the business day on which the mark to market loss or deficiency arises, the member shall be required to deduct the amount of the mark to market loss or deficiency from net capital as provided in SEA Rule 15c3-1 until such time the mark to market loss or deficiency is satisfied.
29. See note 25.
30. See note 18.
31. See note 20.
32. See 81 FR 40364, 40370 n. 65.

## APPENDIX A

Following shows the text of the rule change pursuant to SR-FINRA-2015-036 that becomes effective on December 15, 2016. Language that becomes effective on that date is underlined; deletions are in brackets. (For language pursuant to the rule change that becomes effective on December 15, 2017, see Appendix B.)

\* \* \* \* \*

### 4210. Margin Requirements

(a) through (d) No Change.

#### (e) Exceptions to Rule

The foregoing requirements of this Rule are subject to the following exceptions:

(1) No Change.

#### (2) Exempted Securities, Non-equity Securities and Baskets

(A) through (E) No Change.

#### **(F) Transactions with Exempt Accounts Involving Certain “Good Faith” Securities**

On any “long” or “short” position resulting from a transaction involving exempted securities, mortgage related securities, or major foreign sovereign debt securities made for or with an “exempt account,” no margin need be required and any marked to the market loss on such position need not be collected. However, the amount of any uncollected marked to the market loss shall be deducted in computing the member’s net capital as provided in SEA Rule 15c3-1 and, if applicable, Rule 4110(a), subject to the limits provided in paragraph (e)(2)([H]I) [below] of this Rule.

Members shall maintain a written risk analysis methodology for assessing the amount of credit extended to exempt accounts pursuant to paragraph (e)(2)(F) of this Rule which shall be made available to FINRA upon request. The risk limit determination shall be made by a designated credit risk officer or credit risk committee in accordance with the member’s written risk policies and procedures.

#### **(G) Transactions With Exempt Accounts Involving Highly Rated Foreign Sovereign Debt Securities and Investment Grade Debt Securities**

On any “long” or “short” position resulting from a transaction made for or with an “exempt account” (other than a position subject to paragraph (e)(2)(F), the margin to be maintained on highly rated foreign sovereign debt and investment

grade debt securities shall be, in lieu of any greater requirements imposed under this Rule, (i) 0.5 percent of current market value in the case of highly rated foreign sovereign debt securities, and (ii) 3 percent of current market value in the case of all other investment grade debt securities. The member need not collect any such margin, provided the amount equal to the margin required shall be deducted in computing the member's net capital as provided in SEA Rule 15c3-1 and, if applicable, Rule 4110(a), subject to the limits provided in paragraph (e)(2)([H]) [below] of this Rule.

Members shall maintain a written risk analysis methodology for assessing the amount of credit extended to exempt accounts pursuant to paragraph (e)(2)(G) of this Rule which shall be made available to FINRA upon request. The risk limit determination shall be made by a designated credit risk officer or credit risk committee in accordance with the member's written risk policies and procedures.

#### **(H) Covered Agency Transactions**

##### **(i) Definitions**

For purposes of paragraph (e)(2)(H) of this Rule:

**a. (To be implemented on December 15, 2017.)**

b. The term "counterparty" means any person that enters into a Covered Agency Transaction with a member and includes a "customer" as defined in paragraph (a)(3) of this Rule.

c. The term "Covered Agency Transaction" means:

1. To Be Announced ("TBA") transactions, as defined in Rule 6710(u), inclusive of adjustable rate mortgage ("ARM") transactions, for which the difference between the trade date and contractual settlement date is greater than one business day;

2. Specified Pool Transactions, as defined in Rule 6710(x), for which the difference between the trade date and contractual settlement date is greater than one business day; and

3. Transactions in Collateralized Mortgage Obligations ("CMOs"), as defined in Rule 6710(dd), issued in conformity with a program of an Agency, as defined in Rule 6710(k), or a Government-Sponsored Enterprise, as defined in Rule 6710(n), for which the difference between the trade date and contractual settlement date is greater than three business days.

d. through j. **(To be implemented on December 15, 2017.)**

**(ii) Margin Requirements for Covered Agency Transactions**

**a. (To be implemented on December 15, 2017.)**

b. A member that engages in Covered Agency Transactions with any counterparty shall make a determination in writing of a risk limit for each such counterparty that the member shall enforce. The risk limit determination shall be made by a designated credit risk officer or credit risk committee in accordance with the member's written risk policies and procedures.

c. through g. **(To be implemented on December 15, 2017.)**

**([H]) Limits on Net Capital Deductions for Exempt Accounts**

(i) through (ii) No Change.

(3) through (8) No Change.

(f) through (h) No Change.

**• • • Supplementary Material: -----**

**.01** No Change.

**.02 through .04 (To be implemented on December 15, 2017.)**

**.05 Risk Limit Determination.**

(a) For purposes of any risk limit determination pursuant to paragraphs (e)(2)(F), (e)(2)(G) or (e)(2)(H) of this Rule:

(1) If a member engages in transactions with advisory clients of a registered investment adviser, the member may elect to make the risk limit determination at the investment adviser level;

(2) Members of limited size and resources that do not have a credit risk officer or credit risk committee may designate an appropriately registered principal to make the risk limit determinations;



(3) The member may base the risk limit determination on consideration of all products involved in the member's business with the counterparty, provided the member makes a daily record of the counterparty's risk limit usage; and

(4) A member shall consider whether the margin required pursuant to this Rule is adequate with respect to a particular counterparty account or all its counterparty accounts and, where appropriate, increase such requirements.

\* \* \* \* \*

## APPENDIX B

Following shows the text of the rule change pursuant to SR-FINRA-2015-036 that becomes effective on December 15, 2017. Language that becomes effective on that date is underlined; deletions are in brackets. (Language that becomes effective on December 15, 2016 is shown without underlining as effective. *See* Appendix A.)

\* \* \* \* \*

### 4210. Margin Requirements

#### (a) Definitions

For purposes of this Rule, the following terms shall have the meanings specified below:

(1) through (12) No Change.

(13) The term “exempt account” means:

(A) No Change.

(B) any person that:

(i) has a net worth of at least \$45 million and financial assets of at least \$40 million for purposes of paragraphs (e)(2)(F), [and] (e)(2)(G)[.] and (e)(2)(H), and

(ii) No Change.

(14) through (16) No Change.

(b) through (d) No Change.

#### (e) Exceptions to Rule

The foregoing requirements of this Rule are subject to the following exceptions:

(1) No Change.

#### (2) Exempted Securities, Non-equity Securities and Baskets

(A) through (E) No Change.

#### (F) Transactions with Exempt Accounts Involving Certain “Good Faith” Securities

Other than for Covered Agency Transactions as defined in paragraph (e)(2)(H) of this Rule, [O]n any “long” or “short” position resulting from a transaction involving exempted securities, mortgage related securities, or major foreign sovereign debt securities made for or with an “exempt account,” no margin

need be required and any marked to the market loss on such position need not be collected. However, the amount of any uncollected marked to the market loss shall be deducted in computing the member's net capital as provided in SEA Rule 15c3-1 and, if applicable, Rule 4110(a), subject to the limits provided in paragraph (e)(2)(I) of this Rule.

Members shall maintain a written risk analysis methodology for assessing the amount of credit extended to exempt accounts pursuant to paragraph (e)(2)(F) of this Rule which shall be made available to FINRA upon request. The risk limit determination shall be made by a designated credit risk officer or credit risk committee in accordance with the member's written risk policies and procedures.

**(G) Transactions With Exempt Accounts Involving Highly Rated Foreign Sovereign Debt Securities and Investment Grade Debt Securities**

On any "long" or "short" position resulting from a transaction made for or with an "exempt account" (other than a position subject to paragraph (e)(2)(F) or (e)(2)(H) of this Rule), the margin to be maintained on highly rated foreign sovereign debt and investment grade debt securities shall be, in lieu of any greater requirements imposed under this Rule, (i) 0.5 percent of current market value in the case of highly rated foreign sovereign debt securities, and (ii) 3 percent of current market value in the case of all other investment grade debt securities. The member need not collect any such margin, provided the amount equal to the margin required shall be deducted in computing the member's net capital as provided in SEA Rule 15c3-1 and, if applicable, Rule 4110(a), subject to the limits provided in paragraph (e)(2)(I) of this Rule.

Members shall maintain a written risk analysis methodology for assessing the amount of credit extended to exempt accounts pursuant to paragraph (e)(2)(G) of this Rule which shall be made available to FINRA upon request. The risk limit determination shall be made by a designated credit risk officer or credit risk committee in accordance with the member's written risk policies and procedures.

**(H) Covered Agency Transactions**

**(i) Definitions**

For purposes of paragraph (e)(2)(H) of this Rule:

a. The term "bilateral transaction" means a Covered Agency Transaction that is not cleared through a registered clearing agency as defined in paragraph (f)(2)(A)(xxviii) of this Rule.

b. The term “counterparty” means any person that enters into a Covered Agency Transaction with a member and includes a “customer” as defined in paragraph (a)(3) of this Rule.

c. The term “Covered Agency Transaction” means:

1. To Be Announced (“TBA”) transactions, as defined in Rule 6710(u), inclusive of adjustable rate mortgage (“ARM”) transactions, for which the difference between the trade date and contractual settlement date is greater than one business day;

2. Specified Pool Transactions, as defined in Rule 6710(x), for which the difference between the trade date and contractual settlement date is greater than one business day; and

3. Transactions in Collateralized Mortgage Obligations (“CMOs”), as defined in Rule 6710(dd), issued in conformity with a program of an Agency, as defined in Rule 6710(k), or a Government-Sponsored Enterprise, as defined in Rule 6710(n), for which the difference between the trade date and contractual settlement date is greater than three business days.

d. The term “deficiency” means the amount of any required but uncollected maintenance margin and any required but uncollected mark to market loss.

e. The term “gross open position” means, with respect to Covered Agency Transactions, the amount of the absolute dollar value of all contracts entered into by a counterparty, in all CUSIPs; provided, however, that such amount shall be computed net of any settled position of the counterparty held at the member and deliverable under one or more of the counterparty’s contracts with the member and which the counterparty intends to deliver.

f. The term “maintenance margin” means margin equal to 2 percent of the contract value of the net “long” or net “short” position, by CUSIP, with the counterparty.

g. The term “mark to market loss” means the counterparty’s loss resulting from marking a Covered Agency Transaction to the market.

h. The term “mortgage banker” means an entity, however organized, that engages in the business of providing real estate financing collateralized by liens on such real estate.

i. The term “round robin” trade means any transaction or transactions resulting in equal and offsetting positions by one customer with two separate dealers for the purpose of eliminating a turnaround delivery obligation by the customer.

j. The term “standby” means contracts that are put options that trade OTC, as defined in paragraph (f)(2)(A)(xxvii) of this Rule, with initial and final confirmation procedures similar to those on forward transactions.

**(ii) Margin Requirements for Covered Agency Transactions**

a. All Covered Agency Transactions with any counterparty, regardless of the type of account to which booked, shall be subject to the provisions of paragraph (e)(2)(H) of this Rule, except:

1. with respect to Covered Agency Transactions with any counterparty that is a Federal banking agency, as defined in 12 U.S.C. 1813(z), central bank, multinational central bank, foreign sovereign, multilateral development bank, or the Bank for International Settlements, a member may elect not to apply the margin requirements specified in paragraph (e)(2)(H) of this Rule provided the member makes a written risk limit determination for each such counterparty that the member shall enforce pursuant to paragraph (e)(2)(H)(ii)b.; and

2. a member is not required to apply the margin requirements specified in paragraph (e)(2)(H) of this Rule with respect to Covered Agency Transactions with a counterparty in multifamily housing securities or project loan program securities, provided:

A. such securities are issued in conformity with a program of an Agency, as defined in Rule 6710(k), or a Government-Sponsored Enterprise, as defined in Rule 6710(n), and are documented as Freddie Mac K Certificates, Fannie Mae Delegated Underwriting and Servicing bonds, or Ginnie Mae Construction Loan or Project Loan Certificates, as commonly known to the trade, or are such

other multifamily housing securities or project loan program securities with substantially similar characteristics, issued in conformity with a program of an Agency or a Government-Sponsored Enterprise, as FINRA may designate by Regulatory Notice or similar communication; and

B. the member makes a written risk limit determination for each such counterparty that the member shall enforce pursuant to paragraph (e)(2)(H)(ii)b.

b. A member that engages in Covered Agency Transactions with any counterparty shall make a determination in writing of a risk limit for each such counterparty that the member shall enforce. The risk limit determination shall be made by a designated credit risk officer or credit risk committee in accordance with the member's written risk policies and procedures.

c. The margin requirements specified in paragraph (e)(2)(H) of this Rule shall not apply to:

1. Covered Agency Transactions that are cleared through a registered clearing agency, as defined in paragraph (f)(2)(A)(xxviii) of this Rule, and are subject to the margin requirements of that clearing agency; and

2. any counterparty that has gross open positions in Covered Agency Transactions with the member amounting to \$10 million or less in aggregate, if the original contractual settlement for all such transactions is in the month of the trade date for such transactions or in the month succeeding the trade date for such transactions and the counterparty regularly settles its Covered Agency Transactions on a Delivery Versus Payment ("DVP") basis or for "cash"; provided, however, that such exception from the margin requirements shall not apply to a counterparty that, in its transactions with the member, engages in dollar rolls, as defined in Rule 6710(z), or "round robin" trades, or that uses other financing techniques for its Covered Agency Transactions.

d. Transactions with Exempt Accounts: On any net “long” or net “short” position, by CUSIP, resulting from bilateral transactions with a counterparty that is an “exempt account” no maintenance margin shall be required. However, such transactions shall be marked to the market daily and the member shall collect any net mark to market loss, unless otherwise provided under paragraph (e)(2)(H)(ii)f. of this Rule. If the mark to market loss is not satisfied by the close of business on the next business day after the business day on which the mark to market loss arises, the member shall be required to deduct the amount of the mark to market loss from net capital as provided in SEA Rule 15c3-1 until such time the mark to market loss is satisfied. If such mark to market loss is not satisfied within five business days from the date the loss was created, the member shall promptly liquidate positions to satisfy the mark to market loss, unless FINRA has specifically granted the member additional time. Members may treat mortgage bankers that use Covered Agency Transactions to hedge their pipeline of mortgage commitments as exempt accounts for purposes of paragraph (e)(2)(H) of this Rule.

e. Transactions with Non-Exempt Accounts: On any net “long” or net “short” position, by CUSIP, resulting from bilateral transactions with a counterparty that is not an “exempt account,” maintenance margin, plus any net mark to market loss on such transactions, shall be required margin, and the member shall collect the deficiency, as defined in paragraph (e)(2)(H)(i)d. of this Rule, unless otherwise provided under paragraph (e)(2)(H)(ii)f. of this Rule. If the deficiency is not satisfied by the close of business on the next business day after the business day on which the deficiency arises, the member shall be required to deduct the amount of the deficiency from net capital as provided in SEA Rule 15c3-1 until such time the deficiency is satisfied. If such deficiency is not satisfied within five business days from the date the deficiency was created, the member shall promptly liquidate positions to satisfy the deficiency, unless FINRA has specifically granted the member additional time. No maintenance margin is required if the original contractual settlement for the Covered Agency Transaction is in the month of the trade date for such transaction or in the month succeeding the trade date for such transaction and

the customer regularly settles its Covered Agency Transactions on a DVP basis or for “cash”; provided, however, that such exception from the required maintenance margin shall not apply to a non-exempt account that, in its transactions with the member, engages in dollar rolls, as defined in Rule 6710(z), or “round robin” trades, or that uses other financing techniques for its Covered Agency Transactions.

f. Any aforementioned deficiency, as set forth in paragraph (e)(2)(H)(ii)e. of this Rule, or mark to market losses, as set forth in paragraph (e)(2)(H)(ii)d. of this Rule, with a single counterparty shall not give rise to any margin requirement, and as such need not be collected or charged to net capital, if the aggregate of such amounts with such counterparty does not exceed \$250,000 (“the de minimis transfer amount”). The full amount of the sum of the required maintenance margin and any mark to market loss must be collected when such sum exceeds the de minimis transfer amount.

g. Unrealized profits in one Covered Agency Transaction position may offset losses from other Covered Agency Transaction positions in the same counterparty’s account and the amount of net unrealized profits may be used to reduce margin requirements. With respect to standbys, only profits (in-the-money amounts), if any, on “long” standbys shall be recognized.

#### **(I) Limits on Net Capital Deductions [for Exempt Accounts]**

[(i) Members shall maintain a written risk analysis methodology for assessing the amount of credit extended to exempt accounts pursuant to paragraph (e)(2)(F) and (e)(2)(G) which shall be made available to FINRA upon request.]

[(ii)] In the event that the net capital deductions taken by a member as a result of deficiencies or marked to the market losses incurred under paragraphs (e)(2)(F) and (e)(2)(G) of this Rule (exclusive of the percentage requirements established thereunder), plus any mark to market loss as set forth under paragraph (e)(2)(H)(ii)d. of this Rule and any deficiency as set forth under paragraph (e)(2)(H)(ii)e. of this Rule, and inclusive of all amounts excepted



from margin requirements as set forth under paragraph (e)(2)(H)(ii)c.2. of this Rule or any de minimis transfer amount as set forth under paragraph (e)(2)(H)(ii)f. of this Rule, exceed:

a. [on] for any one account or group of commonly controlled accounts, 5 percent of the member's tentative net capital (as such term is defined in SEA Rule 15c3-1), or

b. [on] for all accounts combined, 25 percent of the member's tentative net capital (as such term is defined in SEA Rule 15c3-1), and,

c. such excess as calculated in paragraphs (e)(2)(l)(i)a. or b. of this Rule continues to exist[s] on the fifth business day after it was incurred,

the member shall give prompt written notice to FINRA and shall not enter into any new transaction(s) subject to the provisions of paragraphs (e)(2)(F), [or] (e)(2)(G) or (e)(2)(H) of this Rule that would result in an increase in the amount of such excess under, as applicable, [subparagraph (ii)] paragraph (e)(2)(l)(i) of this Rule.

(3) through (8) No Change.

**(f) Other Provisions**

(1) through (5) No Change.

(6) Time Within Which Margin or "Mark to Market" Must Be Obtained

The amount of margin or "mark to market" required by any provision of this Rule, other than that required under paragraph (e)(2)(H) of this Rule, shall be obtained as promptly as possible and in any event within 15 business days from the date such deficiency occurred, unless FINRA has specifically granted the member additional time.

(7) through (10) No Change.

(g) through (h) No Change.

• • • **Supplementary Material:** -----

**.01** No Change.

**.02 Monitoring Procedures.** For purposes of paragraph (e)(2)(H)(ii)d. of this Rule, members shall adopt written procedures to monitor the mortgage banker's pipeline of mortgage loan commitments to assess whether the Covered Agency Transactions are being used for hedging purposes.

**.03 Mark to Market Loss/Deficiency.** For purposes of paragraph (e)(2)(H) of this Rule, to the extent a mark to market loss or deficiency is cured by subsequent market movements prior to the time the margin call must be met, the margin call need not be met and the position need not be liquidated; provided, however, if the mark to market loss or deficiency is not satisfied by the close of business on the next business day after the business day on which the mark to market loss or deficiency arises, the member shall be required to deduct the amount of the mark to market loss or deficiency from net capital as provided in SEA Rule 15c3-1 until such time the mark to market loss or deficiency is satisfied.

**.04 Determination of Exempt Account.** For purposes of paragraph (e)(2)(H) of this Rule, the determination of whether an account qualifies as an exempt account shall be made based upon the beneficial ownership of the account. Sub-accounts managed by an investment adviser, where the beneficial owner is other than the investment adviser, shall be margined individually.

**.05 Risk Limit Determination.**

(a) For purposes of any risk limit determination pursuant to paragraphs (e)(2)(F), (e)(2)(G) or (e)(2)(H) of this Rule:

(1) If a member engages in transactions with advisory clients of a registered investment adviser, the member may elect to make the risk limit determination at the investment adviser level;

(2) Members of limited size and resources that do not have a credit risk officer or credit risk committee may designate an appropriately registered principal to make the risk limit determinations;

(3) The member may base the risk limit determination on consideration of all products involved in the member's business with the counterparty, provided the member makes a daily record of the counterparty's risk limit usage; and

(4) A member shall consider whether the margin required pursuant to this Rule is adequate with respect to a particular counterparty account or all its counterparty accounts and, where appropriate, increase such requirements.

\* \* \* \* \*