01-18
(11)

1221 Avenue of the Americas
New York, NY 10020

Morgan Stanley

COMMENT

RECEIVED C.F.T.C.
'01 DEC 10 AM 11 58
RECEIVED C.F.T.C.
RECORDS SECTION

December 5, 2001

Commodity Futures Trading Commission
Three Lafayette Centre
1155 21st Street, N.W.
Washington D.C. 20581

Securities and Exchange Commission
450 Fifth Street, N.W.
Washington D.C. 20549-0609

Re: Customer Margin Rules Relating to Security Futures, 17 CFR Part 41, 17 CFR Part 242; Release No. 34-44853; SEC File No. S7-16-01

Ladies and Gentlemen,

Morgan Stanley appreciates the opportunity to comment on the joint proposed rules (the "Proposed Rules") of the Commodity Futures Trading Commission (the "CFTC") and the Securities and Exchange Commission (the "SEC" and together with the CFTC, the "Commissions") for customer margining of security futures. Morgan Stanley is a diversified financial services firm comprised of several regulated broker-dealers ("B/Ds"), some of which are also registered as Futures Commission Merchants ("FCMs"), and numerous other regulated entities globally serving a diverse retail and institutional clientele.

Morgan Stanley supports, in many respects, the comments outlined by the joint committee (the "Committee") of the Futures Industry Association and the Securities Industry Association in a letter dated December 5, 2001 (the "FIA/SIA Letter"). We believe that the Proposed Rules, with those modifications outlined in the FIA/SIA Letter as well as some additional changes which we have outlined below, could be applied in a cost effective manner to security futures booked in a margin account at a B/D. With respect to security futures booked in a futures account, like the Committee, we believe that a separate margining regime, utilizing the regime currently in place for FCMs in respect of customer margin for non-security futures, should be implemented by the Commissions. Such a dual margining regime is consistent with the dual customer protection and insolvency regimes advocated by the Commissions for security futures in their Release on Customer Protection and Record Keeping. We believe that having two separate margining regimes, each of which builds upon the expertise and systems already in place at FCMs and B/Ds, is the most prudent and cost effective approach and provides

this new product with its greatest chance for success from both a commercial and a safety and soundness perspective.[1]

In drafting the Proposed Rules, the Commissions strove to provide equal treatment for security futures, whether booked at an FCM or a B/D. We believe that this concern can be best addressed by developing a risk-sensitive, portfolio-based approach, such as that currently used in customer futures accounts at FCMs, for margining securities (including security futures) held by a B/D. Under a comprehensive, portfolio margining system, not only would margin accounts be margined in the same manner as futures accounts (which currently utilize a portfolio approach to margining), but all financial instruments, whether regulated by the CFTC or the SEC, could be evaluated and risk managed in accordance with their true economic risk profile, taking account of liquidity, volatility, correlations between instruments and concentration risks. Adoption of a portfolio margining system to the margining of customer securities positions would ensure that margin levels across different types of financial instruments are adequate and proportionate to the inherent risks in a given portfolio. We encourage the Commissions, together with the various securities exchanges and clearing houses, to work together with the securities industry to develop rules based upon portfolio margining principles for the securities margin account.

We recognize that it may not be possible to implement portfolio margining in a customer securities account prior to the launch of trading of security futures in April 2002. Accordingly, we believe that the right approach for the Commissions to follow at this time is to apply Regulation T and the applicable margin rules of the New York Stock Exchange (the "NYSE") and of the National Association of Securities Dealers, Inc. (the "NASD") to security futures booked in the securities margin account and to apply the existing margin rules of the futures exchange as well as a new CFTC Rule (to ensure uniformity in treatment under the various exchange rules) to the margining of security futures booked in a customer futures account. Unlike the Committee, which advocates creation of a new rule, we believe that these changes can be best implemented by amending the existing securities margin rules, including Regulation T, NYSE Rule 431 and NASD Rule 2520 ("Rule 2520") (collectively, "SRO Margin Rules"), in respect of customer positions booked in a B/D margin account, and by creating a new CFTC Rule to govern margin on security futures booked in a futures account, in respect of customer security futures positions booked in a futures account at an FCM.

In order to properly recognize the risks inherent in the product as well as to achieve parity in treatment for the product as between the futures account and the customer margin account, we believe that the following are necessary and appropriate:

- *Subject Security Futures to Minimum Initial and Maintenance Margin of 25%.*
- *Amend Regulation T to, among other things, prohibit withdrawals of cash or securities if there are unsatisfied maintenance margin calls with respect to*

[1] In order to assist the Staffs in evaluating the potential costs involved in applying Regulation T to the futures account at an FCM, we intend to submit, under separate cover, a confidential filing which details our internal estimates of what those costs would be.

security futures, permit the debiting of daily mark-to-market losses on security futures and costs and other charges incurred by the B/D in carrying security futures and permitting the withdrawal of daily mark-to-market gains with respect to security futures.

- *Do not change the timing of margin calls under the existing regulations applicable to the futures account and the securities margin account.*

In addition, because we believe that it will be difficult for either the futures or the securities self regulatory organizations ("SROs") to amend their rules in time to meet the April 2002 launch of the product, we respectfully request that the CFTC, in a new CFTC Rule, and the SEC, in Regulation T, provide guidance regarding how security futures ought to treated for maintenance margin purposes, including, in the case of security futures booked in the margin account, under Rule 431 and Rule 2520.

Our recommendations to the Commissions are as follows:

1. *Application of a Risk-Sensitive, Portfolio-Based Approach to Security Margin Accounts.*

   Prudential risk management of leveraged positions held in a customer's securities account requires an evaluation of both the riskiness of the particular instruments and an analysis of the portfolio in which the instruments are carried. We believe that portfolio-based margining regimes, such as the Standard Portfolio Analysis of Risk ("SPAN"™), currently used for establishing customer margin requirements for futures contracts, and the Theoretical Intermarket Margin System ("TIMS"™), currently used for establishing clearinghouse margin requirements for listed options, are better able to analyze those risks than a "one size fits all" approach, like that in Regulation T and the SRO Margin Rules.

   Regulation T and the SRO Margin Rules do not differentiate between high volatility and low volatility instruments or between the riskiness of exposure to a single name as compared to a diverse portfolio. Accordingly, the results produced by the regulations are often disproportionate to the actual risk inherent in a position. Although the 50% long-side margin requirement of Regulation T often results in margin requirements that are substantially higher than would appear to be required based on an economic analysis of the liquidation risk[2], in some cases (particularly those involving high volatility, low priced stocks), the regulations may result in margin levels that are lower than those which would be produced by a risk-sensitive model.

   As a result of the failure of the regulations to address adequately the actual risk inherent in customer portfolios, Morgan Stanley's internal policies often impose

[2] One noted academic study pointed to this tendency to call for more margin than is economically required and argued that it creates an inappropriate "regulatory tax" on U.S. capital markets participants. *See* "Regulatory Competition and the Efficiency of Alternative Derivative Product Margining Systems," Paul H. Kupiec and A. Patricia White, June 11, 1996.

"house margin" requirements substantially in excess of the regulatory minimum in respect of marginable equities. We believe that the failure to have a uniform margin level that adequately measures the risk of loss in the face of a sudden change in market conditions exposes the market to systemic risk, since not all market participants will elect to impose higher "house margin" requirements for competitive reasons. We believe that these risks are heightened in the case of a levered product such as security futures, which potentially may also lack liquidity. In our view, this systemic risk could and should be addressed through a system under which margin requirements are derived based on the greatest projected net loss in an account given a variety of underlying price increases and decreases and implied volatility changes. SPAN™ and TIMS™ both provide this type of analysis and either could be adopted to cover security futures as well as other U.S. instruments held by customers in a securities margin account, such as equities and listed options. The methodology used by these regimes is understandable and relatively easy to administer. Application of a portfolio based margining regime would still offer B/Ds flexibility to apply higher margin requirements if desired.[3]

Regulation T has permitted portfolio margining since April 1998, subject to approval by the SEC of an appropriate methodology. The Board of Governors of the Federal Reserve System (the "Board"), in its Letter to the Commissions, dated March 6, 2001 (the "Delegation Letter"), delegating authority to the Commissions under Section 7(c)(2) of the Securities Exchange Act to set customer margin requirements for security futures, expressly requested that the Commissions "provide an assessment of progress toward adopting more risk-sensitive, portfolio-based approaches to margining security futures products." The Board endorsed a portfolio-based approach and believes that the Commissions' evaluation of margining for security futures "will provide another opportunity to develop more risk-sensitive, portfolio-based approaches for *all securities*" (emphasis added).

We agree that the regulators and the industry should use the opportunity that introduction of security futures affords us to develop a risk-based margining system to apply to margining of customer security positions. Morgan Stanley agrees with the SIA Credit Division that portfolio margining in the margin account is not necessarily appropriate for all customers. However, we believe that it is essential that any portfolio margining regulation give discretion to B/Ds to apply portfolio margining as they deem appropriate for their businesses. In our view, the proper approach to implementing such a system would be to establish a committee made up of representatives of all of the U.S. securities exchanges (including the options exchanges), the NASD, the Options Clearing Corporation (the "OCC") and members of the industry to recommend uniform rules which could be adopted by all the applicable SROs for securities margin accounts. We note that staff members of the Chicago Board Options Exchange, who were instrumental in the application of TIMS™ to market maker capital haircuts, have

[3]As an example, Morgan Stanley does, from time to time, apply higher "house margin" requirements to futures customers which are subject to portfolio margining.

particular expertise with respect to portfolio margining and should be closely involved with the initiative. We would be pleased to work with the Commissions to develop specific parameters for a risk-based, portfolio margining proposal for the securities margin account. We look forward to having an opportunity to work with the Board, the various U.S. securities exchanges, the SROs and the Commissions to implement a workable risk-based regime that will apply to all listed security products, including security futures.

2. *Approach should Modify Existing Margin Rules Rather than Adopting a New, Stand-Alone Rule.*

While we agree with the basic message of the FIA/SIA Letter that Regulation T should not be applied to security futures held in a futures account, we do not believe that creating and implementing a stand-alone rule for security futures products, as detailed in the FIA/SIA Letter, is the simplest and most efficient way to achieve the desired result. Instead, we believe it would be simpler to amend the existing margin regulations under each regime to incorporate any necessary modifications/amendments required to implement new margin requirements for securities futures. In the case of the futures account, we believe that the CFTC will need to adopt a new rule covering initial and maintenance margining of security futures since there is not currently one central rule, as there is for securities under Regulation T (in respect of initial margin) and Rule 431 and Rule 2520 (in respect of maintenance margin). This new CFTC Rule should establish a minimum initial and maintenance margin level for security futures and clarify how the mechanics of SPAN margining as well as other details provided by applicable exchange rules should be applied.

Putting the margin regulations for all securities credit transactions (including credit with respect to security futures) into a single regulation rather than two separate regulations should facilitate greater compliance by B/Ds with such regulations. Not only would B/Ds have only one place to go to find the applicable federal regulation, but interpretative issues as to whether one regulation is "inconsistent" with the other would be avoided. Moreover, a single regulation should facilitate the implementation of future amendments and interpretations by focusing regulatory and public attention on the impact of any amendment or interpretation on the whole scheme of federal securities credit regulation.
The Commissions have the authority, pursuant to the delegation by the Board[4] in the Delegation Letter as well as, indirectly, by Congress in the Commodity Futures Modernization Act of 2000 (the "CFMA"), to establish margin rules for securities futures products.[5] Although the delegation of authority does not

---

[4] The Board has the authority to set margin requirements for securities futures products under Section 7(c)(2) of the Securities Exchange Act of 1934 ("Exchange Act") and expressly delegated authority to the Commissions to prescribe initial and maintenance margin levels under the Delegation Letter.
[5] Section 206 of the CFMA states that the Board has authority to "establish margin requirements, including the establishment of levels of margin (initial and maintenance) for security futures products under such terms, and at such levels, as the Board deems appropriate" and that the Board may delegate such authority to the Commissions.

indicate how this should be done, we believe it allows the Commissions to achieve this goal by adopting amendments to Regulation T for securities futures products. We urge the Commissions to exercise this authority.

3. *Adopting a Minimum Initial and Maintenance Margin Level of 25%.*

Morgan Stanley urges the Commissions to adopt a 25% minimum initial and maintenance margin requirement for security futures. We believe that the proposed 20% minimum level is insufficient to satisfy the statutory mandate that the levels "preserve the financial integrity of markets" and "prevent systemic risk". We also believe that the 20% minimum margin level fails to satisfy the comparability standard in Section 206 of the CFMA.[6]

Since strategy-based margin regulations (*e.g.*, those set forth in Regulation T and the SRO Margin Rules) do not take account of the volatilities of the underlying instruments, we believe that the minimum margin level ought to be high enough to protect carrying B/Ds against loss assuming a volatility level that is high enough to include a substantial majority of the available underlying listed equities. The OCC does periodic reviews of historic price data for all 2,239 classes of equity options in order to set the parameters for the TIMS™ portfolio margining system. Using data through August 31, 2001, for the 1,650 equity option classes on which there was four years of historical price data, the average margin interval was 20.66 percent. For the 502 additional classes on which there was at least one year of data, the average margin interval was 22.66 percent. Margin intervals for equity options range between 3.39 percent and 85.38 percent, with a mean of 22.66 percent, a median of 21.44 percent, and a standard deviation of 10.56.

Large volume equity option classes with margin intervals materially higher than 20 percent (data through September, 2001) include Ciena Corp (35.05%), BEA Systems (30.34%) and QUALCOMM Incorporated (28.47%). If a broker/dealer were only collecting the proposed regulatory minimum of 20% from its customers for positions in these securities, it would be required to finance a portion of the clearinghouse margin that is required to be posted. We assume that the OCC or other clearinghouses will impose clearinghouse margin for security futures based upon the methodology in TIMS™ or SPAN™. Accordingly, we would expect that the sorts of margin intervals described above for equity options would be applicable for security futures. This would mean that clearinghouse margin levels for security futures should be expected to be materially higher, on average, than customer margin levels if the 20% minimum level is applied.

---

[6] Section 206(2)(B)(ii) provides that levels of margin for security futures, both initial and maintenance, must be "consistent with margin requirements for comparable option contracts traded on any exchange registered pursuant to section 6(a)…[and] …not be lower than the lowest level of margin, exclusive of premium, required for any comparable option contract traded on any exchange registered pursuant to section 6(a)". We believe that put/call pairs of listed options should be considered to be the "comparable option contract."

Morgan Stanley believes that a customer margin policy that consistently requires the financing of customer positions at the clearinghouse level is inconsistent with prudent safety and soundness considerations. The implementation of risk-based portfolio margining for customer securities accounts would remove this inconsistency between customer and clearinghouse level minimum requirements. Until such time as customer level portfolio margining is approved for securities accounts, a higher minimum level in the "one size fits all" regime is necessary.

A 20% minimum margin level would also create an advantage for security futures as compared to listed option put/call pairs. Based on an analysis of existing minimum margin levels on listed put/call pairs under Regulation T and the SRO Margin Rules (*see* Annex A) using actual premiums and contracts, customer margin levels for combinations based on relatively high volatility stocks (*see, e.g.*, options for Broadcom Corp.) were in excess of 30%. Even in the case of combinations based on relatively low volatility stock (*see, e.g.*, options for Chevron Texaco Corp), margin levels were in excess of 20%. Imposition of a lower minimum margin level on security futures could be expected to incentivize customers to invest in security futures rather than listed options which would be contrary to the requirement of "comparability" established by Congress in the CFMA.

There is some ambiguity regarding how to calculate what the "comparable" margin would be for an options contract given the statement in the CFMA that the calculation should be "exclusive of premium". Regardless of how this provision is read, we believe that the result clearly shows that Congress intended the minimum level to be substantially higher than 20%.

The minimum customer margin level for a listed option is defined under Rule 431(f). Margin is 100% of the "current market value" of the option plus the percentage of the current value of the underlying component specified (*i.e.*, 20% in the case of single equities). Current market value means "the total cost or net proceeds of the option contract" in respect of initial margin and "the preceding business day's closing price of that option…as shown by any regularly published reporting or quotation service" in respect of maintenance.

Applying this definition to a put/call option pair, we believe that even if the CFMA's directive to "exclude" the premium means that the current market value of the option for purposes of *initial* margin would be 20%, since the definition of "current market value" for *maintenance* purposes references the prior day's closing price, the maintenance amount (assuming an efficient market and no market movement of the underlying stock) would be well in excess of the 20% level since it would take into account the embedded value of the net short premium on top of the value of the underlying stock (as well as the carrying cost of the underlying and time to maturity).

We believe that the appropriate minimum margin level should be 25%. This level is consistent with the minimum margin level applied by the SRO Margin Rules to long equity positions. This level has also proven to be a prudential standard with respect to that market, which provides comparable exposure to a long security futures contract.

4. *Amendments to Regulation T.*

We suggest, in addition to inclusion of related definitions in Section 220.2 and the required customer margins in Section 220.12 of Regulation T, that the following amendments to Regulation T would be necessary or appropriate:

- Section 220.4(c)(1) to add a reference to security future maintenance margin requirements as a "transaction" that may give rise to a maintenance margin call;
- Section 220.4(e)(1) to prohibit withdrawals of cash or securities if there are unsatisfied maintenance margin calls with respect to security futures, or if a maintenance margin requirements with respect to security futures creates or increases a margin deficiency;
- Section 220.4(f)(1) to permit the debiting thereunder of daily mark-to-market losses with respect to security futures and costs and other charges incurred by the B/D in carrying such security futures, including costs associated with meeting delivery obligations and exchange or clearinghouse fees associated with the positions;
- Section 220.4(f)(2) to permit the withdrawal thereunder of daily mark-to-market gains with respect to security futures;
- Section 220.5(b)(1) to refer to the crediting of daily mark-to-market gains with respect to security futures;
- Section 220.5(b)(2) to clarify that it does not permit crediting of maintenance margin required under Regulation T;
- Section 220.5(b)(3) to permit the credit of margin released upon the liquidation of a security futures position; and
- Section 220.6(e)(1)(i) to recognize a customer futures trading account, including one holding security futures.

Because it is important to make clear that the margin treatment accorded to security futures in the futures account is comparable to that accorded to security futures in the margin account, we believe that the Commissions should clarify in Regulation T that appreciation in a security futures position may be directly applied to a customer's net equity. This clarification ensures that appreciation is treated in a similar manner to "open trade equity" in a futures account. Morgan

Stanley would be happy to consult with the Staffs of Commissions to assist in further identifying and drafting the necessary amendments to Regulation T.

5. *Clarifications to SRO Margin Rules.*

We believe that it is important for the Commissions to clarify how maintenance margin will apply to security futures. In that respect, we urge the Commissions to amend Regulation T to clarify how the applicable SRO Margin Rules would apply to security futures. These changes would allow B/Ds to margin security futures in accordance with the existing SRO Margin Rules applicable to securities except that the minimum margin levels otherwise provided by the rules (*see, e.g.,* Rule 431 (b) and (c)) would be replaced by the Commissions' designated minimum initial and maintenance margin requirements for security futures.

After trading has commenced in the product, we would urge the Commissions, together with the applicable SROs and the industry to evaluate the existing maintenance rules and determine whether or not additional changes would be required. As an initial matter, however, we urge the Commissions to adopt procedures that utilize the existing procedures, to the greatest extent possible, since that will be most cost effective for the industry and minimize the possibility of errors.

6. *Adoption of a CFTC Rule governing Security Futures and Changes to SPAN.*

In order to provide for uniform treatment of security futures traded on different exchanges and to provide a minimum initial and maintenance margin level for the product, we recommend that the Commissions adopt a new rule to govern margining of the product in the futures account. In that regard, we urge the Commissions to reference existing mechanics and definitions provided by exchange and clearinghouse rules to the greatest extent possible, in order to minimize the amount of operational work that will be required to margin the product.

We do not believe that SPAN™ or TIMS™ would require a substantial amount of quantitative retooling or programming work in order to integrate the minimum margin levels for security futures into either of those methodologies. SPAN™ and TIMS™ derive the margin requirement for the portfolio based on a set of product specific parameters. Of these parameters, the most important is the "price scan range", sometimes referred to as the "margin interval". In determining the price scan range for equity related products, both the futures exchanges (for SPAN™) and the OCC (for TIMS™) set a price scan range that covers at least the 99th percentile of observed close-to-close price changes for the underlying product for the analyzed period of time (*i.e.,* not less than one year for futures exchanges and four years for the OCC).

In the interim period of time prior to the implementation of portfolio margining for customer securities accounts, we suggest that the price scan range or margin

interval be set at the greater of: (i) 25% of the current market value of the underlying instrument and (ii) an amount that will cover the 99th percentile of observed close-to-close price changes.

Implementation of this approach will assure reasonable consistency between futures and securities accounts while at the same time preserving the operational integrity of the portfolio margining systems. If, at some point in the future, the Commissions approve trading in options on securities futures, this approach will continue to function appropriately.

Another operational difference between the current securities margin rules and regulations and portfolio margining as it operates for futures accounts is the recognition of risk offsets among different underlying instruments with highly correlated price movements (*i.e.*, "inter-commodity spreads"). In order for these offsets to be recognized by the SPAN™ system, they must be specifically entered into a table that governs their operation. If the Commissions determine that the requisite level of comparability do not allow for recognition of such offsets, it would be a simple matter to keep this table empty. It would also be possible for the Commissions to mandate a minimum level of correlation (*e.g.*, 85 percent over a specified time period) before the table is populated for a given pair of underliers. Either approach would fully preserve the operational integrity of the SPAN™ or TIMS™ portfolio margining system. We would also suggest that, at such time as portfolio margining is approved for customer securities accounts, at least the first of these restrictions be lifted.

7. *Changes are not required to change the timing of Margin Calls made in the Futures Account or the Margin Account.*

Morgan Stanley believes that the timing of margin calls should be tied to existing statutory standards. We do not believe that the timing provisions of either one of the two margining regimes provide a regulatory or prudential advantage over the other.

Although the timing provisions contained in Regulation T are different from those set forth in applicable CFTC and exchange requirements, the result achieved by the two requirements is substantially similar. Under current CFTC rules as well as rules of the applicable futures exchanges, margin calls must be made on T+1 and customer are generally expected to satisfy margin calls on a same day basis. If a margin call remains unsatisfied after T+5, the carrying FCM is required to deduct the deficiency in computing its net capital under CFTC Rule 1.17. There are no CFTC, exchange or SRO provisions for extending the collection period. There is also no statutory requirement that an FCM liquidate a customer's position if the margin call is not satisfied in full by T+5, although a number of FCMs provide for such a liquidation right by contract. Under Regulation T, margin must be calculated on trade date and additional margin must be called for on the next day. *See* Regulation T, Section 220.4(c). Until a margin call is satisfied, the customer is generally not permitted to borrow or withdraw cash or

securities from the account. In the event that a margin call has not been met by T+5, the B/D must liquidate the position or get an extension. Under Exchange Act Rule 15c3-1, a B/D must take a capital charge with respect to customer margin calls not met by T+5. As a practical matter, under both regimes, margin calls are generally made and satisfied on T+1. In any event,we believe that the carrying FCM or B/D has sufficient safe guards in place under a T+5 margin collection regime (through capital charges and mandatory or optional liquidation rights) to protect against systemic risk. Morgan Stanley recommends that the Commissions follow the margin collection periods set forth in the applicable regulations for each of the two margining regimes.

We appreciate the effort that the Commissions have given to formulating clear, workable margining rules for security futures that satisfy the statutory mandate. We believe that the proposal, as modified to take account of the comments outlined in the Committee's letter as well as in this letter, would provide a strong springboard from which to launch the product. We believe that the soundest way to margin security futures is under a risk-sensitive, portfolio-based approach, such as that currently utilized in the futures account which we believe should be available for security futures. Until a portfolio margining regime can be developed for the securities margin account, we urge the Commissions to amend Regulation T to allow security futures to be booked and margined in the margin account using the rules generally applicable to the margin account. We endorse the Commission's use of a minimum margin level for both accounts; however, we believe that a 25% minimum margin level is necessary and appropriate to prevent systemic risk and provide comparability between security futures and cash equities, which are economically equivalent to security futures.[7] Once a sound portfolio margining regime has been developed for the securities margin account, that minimum margin level can be dispensed with.

We believe that security futures could be an important and beneficial new product. The product may provide a useful tool for hedging and carrying out arbitrage and trading strategies. Notwithstanding the potential benefits to be provided by the product, it presents a number of risks given its leveraged structure and the volatility of the underlying securities. In light of these risks, it is critical that the product be subject to a sound, workable and efficient margining system.

---

[7] We urge both Commissions to analyze and rectify all regulatory disparities between the products. For example, the exemption enjoyed by security futures from Exchange Act Rule 10a-1 provides an economic incentive to investors to transact in security futures rather than cash equities. As a policy matter, this advantage does not make sense. Security futures do not perform a more important role than cash equities in the capital markets. In fact, there are some arguments that cash equities ought to be accorded better regulatory treatment since they perform an important capital raising function for public companies.

We appreciate your providing us with an opportunity to comment on the Commissions' proposal. If it would be beneficial to the Staff of the Commissions, we would be happy to facilitate an opportunity for Commission Staff to sit with our margin personnel.

Should you have any questions, please feel free to contact the undersigned, at (212) 537-1456, Jonathan Barton, at (212) 761-8805, James Barry, at (212) 762-5254, or Georgia Bullitt, at (212) 762-6859.

Sincerely yours,

John P. Davidson III
Managing Director

Synthetic Futures - All Prices Close of Business November 15, 2001

Stock 111320107 BROADCOM CORP CLASS A COM STK **Stock Price** 44.49
Stock Notional: 4,449.00 **Short Margin Req:** 889.80 **Barra GEM Vol:** 94.116

Expiry	Strike	Call Premium	Put Premium	Long Synthetic	Notional %	Short Synthetic	Notional %
20011222	45	460.00	510.00	1,349.80	30.34%	1,399.80	31.46%

Stock 48203R104 JUNIPER NETWORKS INC COM STK **Stock Price** 25.12
Stock Notional: 2,512.00 **Short Margin Req:** 502.40 **Barra GEM Vol:** 87.864

Expiry	Strike	Call Premium	Put Premium	Long Synthetic	Notional %	Short Synthetic	Notional %
20011222	25	310.00	300.00	812.40	32.34%	802.40	31.94%

Stock 171779101 CIENA CORP COM **Stock Price** 19.09
Stock Notional: 1,909.00 **Short Margin Req:** 381.80 **Barra GEM Vol:** 85.506

Expiry	Strike	Call Premium	Put Premium	Long Synthetic	Notional %	Short Synthetic	Notional %
20011222	20	190.00	285.00	571.80	29.95%	666.80	34.93%

Stock 71366Q101 PEREGRINE SYSTEMS INC COM **Stock Price** 17.15
Stock Notional: 1,715.00 **Short Margin Req:** 343.00 **Barra GEM Vol:** 84.82

Expiry	Strike	Call Premium	Put Premium	Long Synthetic	Notional %	Short Synthetic	Notional %
20011222	17.5	170.00	215.00	513.00	29.91%	558.00	32.54%

Stock 04644A101 ASTRO POWER COM STK **Stock Price** 34.25
Stock Notional: 3,425.00 **Short Margin Req:** 685.00 **Barra GEM Vol:** 84.526

Expiry	Strike	Call Premium	Put Premium	Long Synthetic	Notional %	Short Synthetic	Notional %
20011222	35	300.00	350.00	985.00	28.76%	1,035.00	30.22%

Stock 826170102 SIEBEL SYS INC COM **Stock Price** 25.29
Stock Notional: 2,529.00 **Short Margin Req:** 505.80 **Barra GEM Vol:** 83.524

Expiry	Strike	Call Premium	Put Premium	Long Synthetic	Notional %	Short Synthetic	Notional %
20020119	25	370.00	335.00	875.80	34.63%	840.80	33.25%

Synthetic Futures - All Prices Close of Business November 15, 2001

Stock 278642103 EBAY INC COM STK **Stock Price** 60.07

Stock Notional: 6,007.00 **Short Margin Req:** 1,201.40 **Barra GEM Vol:** 80.709

Expiry	Strike	Call Premium	Put Premium	Long Synthetic	Notional %	Short Synthetic	Notional %
20011222	60	430.00	420.00	1,631.40	27.16%	1,621.40	26.99%
20020119	60	670.00	630.00	1,871.40	31.15%	1,831.40	30.49%

Stock 25243Q205 DIAGEO PLC SPONS ADR NEW **Stock Price** 43.57

Stock Notional: 4,357.00 **Short Margin Req:** 871.40 **Barra GEM Vol:** 24.532

Expiry	Strike	Call Premium	Put Premium	Long Synthetic	Notional %	Short Synthetic	Notional %
20020119	45	125.00	282.50	996.40	22.87%	1,153.90	26.48%

Stock 002824100 ABBOTT LABS USD COM NPV **Stock Price** 52.9

Stock Notional: 5,290.00 **Short Margin Req:** 1,058.00 **Barra GEM Vol:** 24.318

Expiry	Strike	Call Premium	Put Premium	Long Synthetic	Notional %	Short Synthetic	Notional %
20020119	55	145.00	370.00	1,203.00	22.74%	1,428.00	26.99%

Stock 98389B100 XCEL ENERGY INC COM STK **Stock Price** 28.7

Stock Notional: 2,870.00 **Short Margin Req:** 574.00 **Barra GEM Vol:** 24.278

Expiry	Strike	Call Premium	Put Premium	Long Synthetic	Notional %	Short Synthetic	Notional %
20011222	30	37.50	162.50	611.50	21.31%	736.50	25.66%

Stock 166764100 CHEVRON TEXACO CORP (EX CHEVRON CORP) SHS **Stock Price** 83.8

Stock Notional: 8,380.00 **Short Margin Req:** 1,676.00 **Barra GEM Vol:** 23.914

Expiry	Strike	Call Premium	Put Premium	Long Synthetic	Notional %	Short Synthetic	Notional %
20011222	85	237.50	335.00	1,913.50	22.83%	2,011.00	24.00%
20020119	80	640.00	230.00	2,316.00	27.64%	1,906.00	22.74%

Stock 035229103 ANHEUSER BUSCH COS INC COM **Stock Price** 43.7

Stock Notional: 4,370.00 **Short Margin Req:** 874.00 **Barra GEM Vol:** 23.241

Expiry	Strike	Call Premium	Put Premium	Long Synthetic	Notional %	Short Synthetic	Notional %
20011222	45	80.00	205.00	954.00	21.83%	1,079.00	24.69%
20020119	45	120.00	255.00	994.00	22.75%	1,129.00	25.84%