

BOARD OF GOVERNORS
OF THE
FEDERAL RESERVE SYSTEM

STATEMENT FOR THE PRESS

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Saturday, April 30, 1938.

The following ruling will appear in the Federal Reserve Bulletin.

Effect of Purchase and Sale of Same Securities
on Given Day

The Board recently considered a case under Regulation F in which transactions effected on Monday in a general account resulted in a requirement of \$100 margin, and on the day following, Tuesday, a certain quantity of a particular stock was purchased and later in the day the same quantity of the same security was sold, resulting in a net profit of \$150. There were no other transactions in the account on Tuesday.

The question presented was whether this purchase and sale could be treated, to the extent of \$100, as a liquidation pursuant to section 3(e) of the regulation in lieu of a deposit of that amount of margin, and as also permitting a withdrawal of \$50 on Tuesday pursuant to the second paragraph of section 3(b).

Sections 3(b) and 3(e) of the regulation read in part as follows:

"(b) General rule. - A creditor shall not effect for or with any customer in a general account any transaction which, in combination with the other transactions effected in the account on the same day, creates an excess of the adjusted debit balance of the account over the maximum loan value of the securities in the account, or increases any such excess, unless in connection therewith the creditor obtains, as promptly as possible and in any event before

the expiration of three full business days following the date of such transaction, the deposit into the account of cash or securities in such amount that the cash deposited plus the maximum loan value of the securities deposited equals or exceeds the excess so created or the increase so caused.

"A transaction consisting of a withdrawal of cash or registered or exempted securities from a general account shall be permissible only on condition that no cash or securities need be deposited in the account in connection with a transaction on a previous day and that, in addition, the transactions (including such withdrawal) on the day of such withdrawal would not create an excess of the adjusted debit balance of the account over the maximum loan value of the securities in the account or increase any such excess.

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"(e) Liquidation in lieu of deposit.* - In any case in which the deposit required by section 3(b), or any portion thereof, is not obtained by the creditor within the three-day period specified in that section, securities shall be sold or covering or other liquidating transactions shall be effected in the account, prior to the expiration of such three-day period, in such amount that the resulting decrease in the adjusted debit balance of the account exceeds, by an amount at least as great as such required deposit or the undeposited portion thereof, any resulting decrease in the maximum loan value of the securities in the account.

* This requirement relates to the action to be taken when a customer fails to make the deposit required by section 3(b), and it is not intended to countenance on the part of customers the practice commonly known as 'free-riding' or 'three-day riding', to prevent which the principal national securities exchanges have adopted certain rules. See the rules of such exchanges and section 7(e) of this regulation."

The Board expressed the view that the purchase and sale of the same securities on Tuesday could be so treated. This follows from the fact that such purchase and sale would reduce by \$150 any excess of the

adjusted debit balance of the account over the maximum loan value of the securities in the account. It seems proper to treat such reduction as consisting of two portions in the manner suggested.

As indicated in the footnote to section 3(e), that provision was not intended to countenance on the part of customers the practice commonly known as "free-riding" or "three-day riding", to prevent which the principal national securities exchanges have adopted certain rules. If the transactions on Tuesday were treated as indicated above, the liquidation in lieu of a deposit of margin would, of course, have to be considered in connection with such exchange rules.