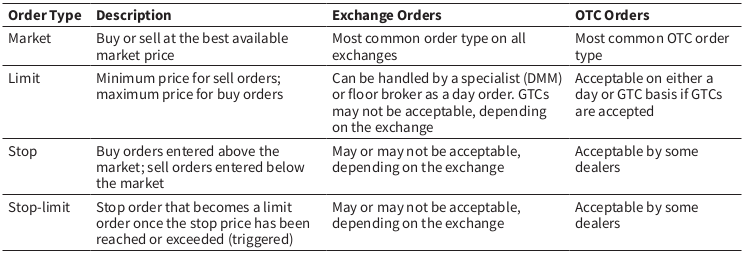
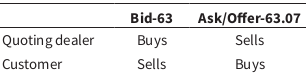
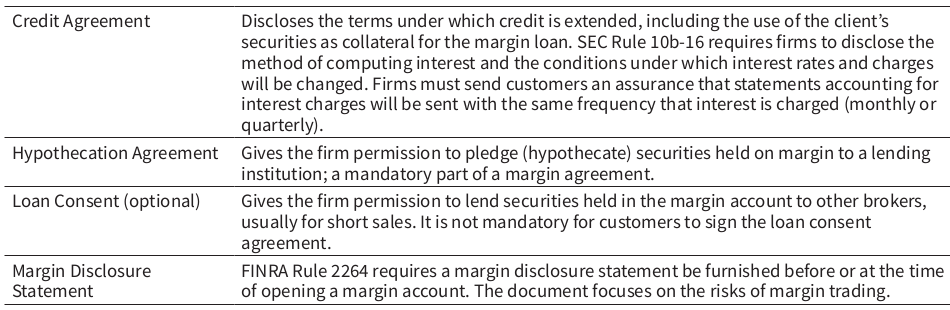
# C16:TYPES OF ORDERS AND QUOTATIONS

1. Name the different types of orders available to customers
   1. Price Restricted Orders
      1. Market Orders – immediate execution, priority over all other types of orders, order to buy at lowest price possible, order to sell at highest price available, inside quote, highest bid-lowest ask *(highest buy price – lowest sell price)*
      2. Limit Orders – customer limits the acceptable purchase or selling price. Limit order can be executed only at the specified price or better
         1. if the order cannot be executed at the limit price immediately, it is placed on the designated market maker’s (DMM) book and executed when/if the market price matches the limit price
         2. Buy Limit → placed below the current market **(SLoBS/BLiSS)**
            1. buy limits set by investors who believe a stock is currently overpriced, and they wish to buy at a dip
         3. Sell Limit → placed above the market **(SLoBS/BLiSS)**
            1. investors who own a stock and believe it is currently undervalued turn in sell limit orders getting them out of the position should the stock rise
         4. Length of Limit Orders – 2 time restrictions, day order, or GTC
         5. Risks – sometimes limit orders are not executed, even if the stock trades at the limit price
            1. stock ahead – first come, first served on DMM’s book, there was stock ahead of your order, also called time priority
      3. Stop Orders – AKA stop loss order, designed to protect a profit or prevent a loss if the stock begins to move in the wrong direction
         1. Becomes market order once the stock trades at or *moves through* the stop price. Stop Orders take two trades to execute – Trigger, and Execution (at execution, the stop order becomes a market order and executes at the next available price)
         2. Buy Stop Order **(SLoBS/BliSS)** – protects a profit or limits a loss in a *short* stock positions
         3. Sell Stop Order **(SLoBS/BliSS) –** protects a profit or limits a loss in a *long* stock position and entered at a price below the current market
         4. Stop Limit – stop order that turns into a limit order
      4. Reducing Orders – certain orders on a DMM are reduced when a stock goes ex-dividend
         1. all orders enetered below the market are reduced on the ex-date. We know that on the ex-date the stock price opens lower by the amt of the distributions
         2. Orders reduced include buy limits and sell stops, (including sell stop limit orders). These orders are reduced by the div amt. Without this reduction, trading at the lower price on the ex-date could cause an inadvertent execution
         3. DNR- Do Not Reduce order – not reduced by an ordinary cash div, the customer does not care if there’s an execution due solely to the ex-date reduction
         4. Recall that only those placed below the mkt price are automatically reduced. (BLiSS only). All orders are adjusted for stock div and stock splits whether placed above or below the mkt.
            1. *E.g*: There is an open GTC order to sell 100 XYZ @ 50 stop; 2:1 split; Order becomes: 200 XYZ @ 25 stop;
            2. *E.g*:Open order to buy 500 XYZ @ 30; 20% stock div;500\*1.2=600, 30/1.2=25;600 XYZ @ 25;
            3. *E.g*: (Round Lot Issue): Open order to buy 100 XYZ @ 30; 20% stock div; 100\*1.2=120, 30/1.2=25; 100 XYZ @ 25 ***NOT*** 120; Only round lots are allowed on the order book. Additional 20 shares are in the customer account, but can’t be part of an open order. For reverse splits, all open orders are canceled
         5. Standard trading unit for stocks is normally 100 shares (round lot). Any quantity less = odd-lot
      5. Time-Sensitive Orders
         1. Day Order – unless marked to contrary, an open order is assumed to be a day order, valid until the close of trading on the day it’s entered. If not filled by close of trading, it’s canceled
         2. GTC – valid until executed or canceled, Auto canceled if unexecuted for 30d or 90d, depending on what the indiv BD chooses. If the customer wishes to have the order remain working beyond those specific days, cust. Must re-enter the order.
         3. At-the-Open and Market-On-Close – At the Open = executed at the opening of the mkt, partial execs are allowable, must reach the post by the open of trading in that sec, or they will be cancelled. Market On Close = executed at or near as possible to closing price in OTC mkt, on the NYSE, however, a mkt on close order must be entered before 3:40pm ET, will be executed at Closing Price
         4. Not Held – market order NH indicates that the customer agrees not to hold the floor broker or BD to a particular time or price of execution. This provides the floor broker with the authority to decide the best time or price at which to execute the trade. May not be placed with the NYSE DMM
            1. Under FINRA Rule 3260, market NH orders in which a retail customer gives you authority over price or timing, are limited to the day the order is given. In other words, they are day orders. An exception is granted if the customer, in writing, states that the order is GTC.
         5. Fill-Or-Kill – commission house broker is instructed to fill an entire FOK order immediately at the limit price or better. If the entire order cannot be filled, it has to be canceled and the broker who couldn’t fill has to notify the originating branch office
         6. Immediate-or-cancel – FOK, except partial execution is acceptable, portion not executed is not canceled
         7. All-or-None – must be executed in their entirety or not at all, GTC or Day Order, they do not have to be filled immediately
         8. Alternative (OCO) – OCO = one cancels the other – If one of the orders is executed, the other one is immediately canceled.
            1. *E.g*: A customer is long stock at $50 that was purchased six months earlier at $30. To protect his unrealized gain, the customer might enter a sell stop at $48. Alternatively, if the stock continues to rise, he wants out at $53. What he miSght do is enter both orders with the notation, one cancels the other (OCO).
   2. Comparison of order characteristics
2. Name the different types of quotes
   1. Bids, Offers, and Quotes - available for both listed and unlisted secs, for stocks traded on NYSE, quotes come from DMM; These are available elextronically, even to retail investors. On OTC mkts, quotation originates with the market makers. OTC has no DMMs.
      1. Bid
         1. Bidder says “I will buy this stock at this price”
         2. Investor wants to sell, she sells to the bidder at that price
         3. *price at which a seller receives*
      2. Ask
         1. Buyer says “I will sell this stock at this price”
         2. Investor wants to buy, she buys from the buyer at that price
         3. *price at which buyer pays*
      3. Multi-quote bid-ask: highest bid-lowest ask *(highest buy price – lowest sell price)*
      4. Customer’s and Market Maker’s relationship to the quote:
      5. Note: A BD can never charge a mark up/down and a commission on the same trade
   2. Types of Quotes – In OTC Mkt (Negotiated mkt) BDs trade w/ other BDs. Several diff types of quotes
      1. Firm Quote – mkt maker stands ready to buy/sell >=1 trading unit (100 sh. Stock, or 5 bonds) at the quoted price, w other member firms
         1. All quotes are firm quotes unless otherwise indicated. In almost all cases, the quote size will be more than 1 round lot.
         2. One function of an employee of a broker-dealer is that of *OTC trader*.
            1. This individual is responsible for taking customer orders received in the trading department and getting them executed at the best possible price.
            2. This trader may attempt to negotiate a better price with a market maker by making a counteroffer or a counter-bid, especially if the spread between the market maker’s bid and ask is fairly wide.
            3. However, the only way to guarantee an immediate execution is to buy stock at the market maker’s ask price or sell at the bid price.
            4. In a typical bond transaction, a trader at one BD/market maker, calls a trader at another to buy a specific bond. A market maker might give another BD a quote that is *firm for an hour w 5-min recall*.

This is a firm quote that remains good for an hour. If, within that hour, the market maker receives another order for the same sec, the trader calls the BD back and gives it 5-min to confirm its order or lose its right to buy that sec at the price quoted. (\*\*out-firm)

* + - 1. Backing Away -- bad
    1. Subject Quote – opposite of a firm quote, firm quote = prices the dealer will honor, a subject quote requires further confirmation. Rare situation.
    2. Qualified Quotes – a quote given with qualifiers intended to allow the dealer to back away if the market conditions change
       1. Workout Quote – reserved for situations where a market maker knows that special handling will be required to accommodate a particular trade. Either the order size is too big for the market to absorb without disruption, or the market is too thin or temporarily unstable – a workout quote is an approximate figure used to provide the buyer or the seller with an indication of price, not a firm quote
       2. Nominal Quote – someone’s assessment of where a sec might trade in an active market – used to give customers an idea of market value of an inactively traded security – *not firm quotes –* must be clearly labled as nominal, -- common with municipal bonds
  1. Quotation Spread – difference between bid and offer/ask price, many factors influence a spread’s size including: issue size, issuer’s financial condition, the amt of market activity in the issue, and the market conditions – “The more active a security, the narrower the spread”
  2. Best Execution of Customer Orders – using reasonable diligence to find the best market for the subject sec. FINRA Rule 5310’s reasonable diligence:
     1. the character of the market for the security (price, volatility, relative liquidity, pressure on available communications)
     2. Size and type of transaction
     3. The number of markets checked
     4. Accessibility of the quotations
     5. the terms and conditions of the order that result in the transaction as communicated to the member and persons associated with the member -- *fin*
     6. Orders involving secs with limited quotations or pricing info:
        1. Interpositioning – a member firm cannot place a 3rd party between itself and the best available market
        2. Markups and markdowns are charged when a market maker is acting as a principal (dealing from inventory with financial risk).
        3. Unless stated otherwise, firm quotes are good for a round lot only. A quote of 11 –11.50, 3 × 5 is firm between dealers for 300 shares at the bid price of 11 and 500 shares at the ask price of 11.50.
        4. Nominal quotes can be given for informational purposes and can be printed only if clearly labeled as such.

1. Define short sale strategies and requirements – bearish strategy, selling before owning/borrowing the secs, the risk is the price of the borrowed sec shares increases. Unlimited Loss. To make delivery, the BD lends the sec to its customer. After settlement of the trade, the BD credits the proceeds to the customer’s account – Short Selling is the “Sell High, Buy Low” principle
   1. Regulation SHO – mandates a locate requirement, before the short sale of any equity security, firms must locate the secs for borrowing to ensure that delivery will be made on the settlement date – regulators refer to this as **affirmative determination** – not doing this is naked short selling, not permitted
   2. Insider Short Sale Regulations – SEC 1934 prohibits directors, officers, and principal stockholders (insiders) from selling short stock in their own companies
   3. Sell Order Tickets – SEC requires that all sell orders be identified as either long or short – no sale can be marked long unless the sec to be delivered is in the customer’s account or is owned by the customer and will be delivered to the broker by the settlement date; A person is long a sec if:
      1. has title to it
      2. has purchased the sec or has entered into an unconditional contract to purchase the sec but has not yet received it
      3. owns a sec convertible into or exchangeable for the sec and has tendered such sec for conversion or exchange or
      4. has an option to purchase the security and has exercised that option
      5. 1 or more of the conditions have to be met:
   4. Borrowing Secs – Secs can be borrowed from:
      1. the member firm executing the short sale on behalf of the customer
      2. margin customers of that member firm
      3. other member firms
      4. institutional investors, such as pension plans and custodial banks
   5. Note: A buyer has no idea that shares purchased were sold short, but the order ticket prepared by the brokerage firm representing the seller must indicate that the sale is short. Also note: Short sales may be executed at any time during the trading day, including the opening and closing.
   6. Mark to Market – making daily adjustments to the customer’s margin accnt as the price of the underlying sec changesr. In a short pos, where the stock’s price increases, the equity in the account goes down
   7. Shorting Bonds – It is not easy to cover shorts for most muni bonds because the limited number of bonds available in each issue could make it difficult to buy back the short position – muni market is too thin – short selling muni bonds is almost never done
2. Compute margin requirements
   1. Types of Margin Accounts – Long (LMA, customers purchase secs and pay interest on the borrowed until the loan is repaid) and Short (SMA, the stock is borrowed and then sold short, enabling the customer to profit if its value declines)
   2. Margin Account Agreements – customers who open margin accounts must sign a margin agreement before trading can begin – 3 parts – the credit agreement, the hypothecation agreement, and loan consent form
      1. Credit Agreement – discloses the terms of the credit extended by the BD, includes the method of interest computation, and situtations under which interest rates may change
      2. Hypothecation Agreement – gives permission to the BD to pledge customer margin secs as collat – the firm hypothecates customer secs to the bank, and the bank loans money to the BD on the bases of the loan value of these secs
         1. all customer secs must be held in street name to facilitate this process – BD is known as the nominal/named/owner -- customer is known as beneficial owner, he retains all rights of ownership
         2. BD rehypothecation covered by Regulation U, BD are limited to pledging 140% of a customer’s debit balance as collat – any customer secs over this amt must be physically segregated
         3. The firm cannot commingle customer secs with secs owned by the firms
      3. Loan Consent Form – optional, gives permission to the firm to lend out customer margin secs to other customers or BDs, usually for short sales
      4. Risk Disclosure – member firm must provide customers with a margin disclosure statement, info must also be provided to margin customers on an annual basis
         1. customers can lose more $$ than initially deposited
         2. customers not entitled to choose which securities or other assets in their account(s) are liquidated or sold to meet a call for additional funds
         3. customers are not entitled to an extension of time to meet a margin call
         4. firms can increase their in-house margin requirements without advance notice



* 1. Regulation T – Sec act of 1934 gives the FRB the authority to regulate the extension of credit in the securities industry. -- customers must deposit a minimum of 50% of the price of the transaction within S+2 time (T+4 time)
     1. Marginable Secs:
        1. May be purchased on margin and used as collateral
           1. Exchange Listed Stocks, bonds
           2. Nasdaq stocks
           3. Non-Nasdaq OTC issues approved by the FRB
           4. Warrants
        2. *Cannot* be purchased on margin and *cannot* be used as collateral
           1. Call/Put options
           2. Rights
           3. Non-Nasdaq OTC issues *not* approved by the FRB
           4. Insurance Contracts
        3. Cannot be bought on margin but can be used as collateral after 30 days
           1. MFs
           2. New Issues
     2. Deadlines for meeting margin calls – deadline is S+2, deposit may be made in cash or paid in fully marginable secs valued at 2x (200%) the amt of the Reg T cash call\*\*
        1. If pmt late, dealer may apply to its DEA (designated examining authority) for an extension, DEA – FINRA, exchange, or even FRB – For introducing BDs, the request is made by the firm that does their clearing (back-office work)
        2. a BD may disregard any sum due from the customer not > $1k – sell out and freeze (freeriding)
        3. Freeriding – secs are purchased and then sold without making payment for the purchase on settlement date – how do day traders handle avoiding freeriding? -- they may have sufficient funds in their acccount before making the trade – “Swaps” checks on settlement date – pay the BD and then receive payment for the sale
     3. exempt secs – exempt from Reg T Margin reqs, subject to firm’s determination of Init. Req.; Secs exempt include US T-Bills, Notes, and Bonds, Gov’t agency Secs, and Muni Secs
  2. Initial Requirements → *x* = MAX($2000,init amt);if *x* ==$2000, then init deposit = Min($2000,50%\*init amt)
  3. Margin Accounting – for active margin accounts, BDs must verify that the equity in the account still meets minimum requirements following fluctuations in market value – marking to market is a recalculation to check the status of the equity in the account, done every B-Day on the basis of the closing price of the stock
     1. Long Margin Accounting – The customer owns the security
        1. LMV = Long Market Value = the CMV of the stock position the investor purchased
        2. DR = Debit Register = the amt of money borrowed by the customer
        3. EQ = equity = the customer’s net worth in the margin account; it represents the portion of the securities the customer fully owns
           1. LMV – DR = EQ
           2. *Note*: When the market value of securities goes up, the debit balance stays the same, whiel the equity increases (and vice versa)
           3. v small balance sheet – LMV is an asset, DR is liability, equity is equity ***[DRAW BELOW]***
           4. Note: We know that Reg T requires 50% deposit when buying/selling short on margin; Note that the regulation assigns a loan value to securities (loan val will be 50%)….***[NEEDS MORE]***
           5. when the market value of secs changes, the BD must mark to market the positions to ensure that enough equity remains in the accounts – must always meet the maintenance requirement of FINRA –maintenance margin is 25% of LMV
     2. Restricted Accounts
        1. If the equity in the account is less than the Reg T requirement but greater than the min Maintenance Requirement, the account is *restricted* **[min Maintenance Req < EQ < Reg T req ===> *restricted*]**
        2. the following rules would apply
           1. to purchase additional secs, put up 50%
           2. to withdraw secs from the account, the customer must deposit cash equal to 50% of the value of the securities to be withdrawn
           3. if secs are sold in a restricted account, >=50% of the proceeds must be retained in the account to reduce the debit balance (retention requirement) → 50% of the proceeds are credited to SMA (special memorandum account)
        3. *Note*: SMA used much like a line of credit with a bank – SMA preserves the customer’s right to use excess equity
     3. Maintenance Requirements
        1. Maintenance Call
  4. Excess Equity and the SMA
     1. Using SMA
  5. Pattern Day Traders
     1. Approval for Day Trading Accounts
  6. Short Sales and Margin Requirements
     1. Margin Deposits
     2. Analyzing Short Margin Account Activity
     3. Minimum Maintenance
  7. Short Margin Account Math
     1. Minimum Maintenance in a Short Account
  8. Combined (Mixed) Margin Accounts
  9. Options and Margin
  10. Customer Portfolio Margining

1. Determine the rules and regulations pertaining to trading securities