Lek Securities Corporation

House Requirements

Portfolio Margin Accounts
Day Trading Accounts with Equity in excess of $5,000,000
All other accounts

In connection with the newly approved Portfolio Margin rules and the elimination of the day trading restriction on accounts with equity in excess of $5MM, LSC has established certain risk parameters to protect the firm and its clients. All traders are expected to be able to monitor their own risk – in real time – and be in continuous compliance with these restrictions.

Although our house requirements will likely only be relevant for Portfolio Margin Accounts ("PMAs"), because the traditional maintenance requirement and day trading restrictions often will be more restrictive, it is important to note that the house requirements apply to all accounts. For example, under traditional day trading rules, an account with $1MM cash, could at any time during the day be long as much as $4MM of just one stock. Our house restrictions on undue concentration would not permit this.

As a prerequisite to opening a PMA, the account must maintain a minimum equity of $250,000. Moreover, we will only open a PMA for traders that have three years experience in trading derivatives.

Portfolio margin rules require LSC to download so-called TIMS data from the OCC. The OCC data evaluates the theoretical P&L for each symbol for moves up and down 15%. For each underlying, the worst P&L is taken and the margin requirement is the aggregate of the worst position for all underlying symbols combined. The OCC allows offsets between indices that are largely overlapping, such as, for example the S&P 500 and the OEX. However, no offset is allowed for offsetting positions in different symbols, even if one can show a historically high degree of correlation. Every option contract has a minimum margin requirement of $37.50, which was designed to be reflective of the transaction costs of liquidating the position.

One of LSC's concerns with the exchange mandated portfolio margin rules is that there are little restrictions on long gamma positions and there is virtually nothing to prevent a trader from being unduly concentrated in just a few symbols. The latter is of particular concern. LSC is willing to allow day traders to trade as high as 20:1, which is very aggressive when compared to the old restrictions that limited intra-day exposure to 4:1. However, in lieu of the arcane day trading rules, LSC has put in place restrictions that prevent traders from being too long or too short the market and discourage highly concentrated positions. We also evaluate time-decay (Theta) and overall shifts in volatility (Vega).

Specifically all traders are expected to remain within the following risk parameters:

Short Gamma Restriction

LSC will evaluate a 6 vol. move in each underlying, i.e. a one through 6 vol. move up and down. For each underlying symbol the worst result is taken. The minimum equity requirement is the aggregate worst move for all symbols combined. This calculation mimics the OCC calculation, except that for more volatile stocks, a wider range is evaluated; for less volatile stocks, we look at a narrower range. For example, if the 60 day implied volatility of at the money options in XYZ is 30%, then a one vol. move would be .3 * √[1/252] or a daily move of 1.88%. A six vol. move would equal a daily move 1 plus 1.88% to the sixth power, or a 11.82% daily move. Indices and ETFs are excluded from this calculation. This calculation is not performed for day trading accounts. In lieu thereof, we use a 20:1 maximum.

Theta and Vega Restrictions

For each underlying symbol the above described calculations are repeated with volatilities marked up and down 20% respectively. If either way the potential loss is greater, the more unfavorable number is taken to compute the minimum margin requirement. The calculations are also repeated 1, 2, 3, 5, 19, 15, 20 and 30 days in the future to evaluate time decay. Once again, if the number is worse, the more unfavorable figure is used.

Net Market Long/Short Restriction

It makes an enormous difference if a trader has a large position if he is just long or short the market or evenly balanced. LSC allows traders to take on large positions, provided the portfolio is relatively evenly divided between long and short positions. To measure how well a portfolio is balanced, we evaluate 10 single vol. up and down moves in each underlying symbol. We then sum each column and an account must have equity to cover the worst loss. Unlike the short gamma restriction, we do not look at the worst case scenario for each underlying. In this analysis, we assume that all stocks move up or down in the same direction as a function of a move in the overall market, and that the size of each symbol’s move is proportional to its market implied volatility.

Concentration Restriction

To avoid excessive concentration, we look at a 16 vol. move in each underlying symbol and select the four symbols that could produce the largest loss. Equity must be sufficient to cover 100% of the loss in the symbol that could produce the largest loss, plus 50% of the loss in underlying that could bring about the second largest loss, plus 25% of the third and 10% of the fourth largest loss that could occur after a 16 vol. move. Indices and ETFs are excluded from this calculation.

Subjective Restrictions/Exemptions

The Chief Credit Officer may grant exemptions from our house requirements, if a trader can point to a legitimate special hedge that we might not have taken into account when evaluating portfolio risk. However, no exemption will be granted simply because a trader might find our requirements to be too burdensome. Exemptions from exchange mandated requirements are never permitted. Traders are required to be in continuous compliance with these restrictions, and any intraday violation will be considered the equivalent of a “liquidation”.

LSC reserves the right to require additional collateral from any account if it deems itself insufficiently secured, even if an account is in compliance with the above requirements.

(Execution on next page)

Agreed and Accepted this ___ day of _______, 200__

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(Account Title)

____
(Signature)

____
(Print Name)

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(Title)