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ACCOUNTS, MARGIN, RULES & TAXES

The boring stuff that protects you — margin, day-trading rules, and taxes.

Alpha Academy · Team Alpha Trading

Accounts, Margin, Rules & Taxes: The Boring Stuff That Protects You

Nobody opens a brokerage account dreaming about settlement rules and tax forms. But here is a secret experienced traders know: more beginner accounts are damaged by boring rule mistakes than by bad stock picks. People get accounts restricted for breaking a rule they never heard of, pay interest they did not know they owed, and get a tax surprise in April for trades they made in June.

This chapter explains the machinery under your trading: the two kinds of accounts, how borrowing from your broker really works, the day-trading rule, settlement, and the basic tax rules every US trader must know exist.

After reading it, you will be able to choose between a cash and margin account with your eyes open, and explain a margin call in plain words.

> **NOTE**
> This chapter is education only, from Team Alpha Trading. It is not financial, tax, or legal advice. Tax rules change, broker rules change, and your situation is your own. Use a qualified tax professional for anything that touches your real money and your real tax return.

The Two Kinds of Brokerage Accounts

A **brokerage account** is an account at a licensed company — a **broker** — that lets you buy and sell investments like stocks. You choose between two basic types.

Cash Accounts: Your Money Only

In a **cash account**, you can only trade with money that is actually in the account and fully settled (we explain "settled" below). It is like a prepaid debit card: load $1,000, buy up to $1,000 of stock, and when the money is spent, it is spent. You can never owe the broker money or be charged interest. For most beginners, this is the right starting account — its one main limit, waiting for sale money to settle, is covered in the settlement section below.

Margin Accounts: Your Money Plus a Loan

In a **margin account**, the broker lets you borrow money to trade bigger. **Margin** is the name for trading with borrowed money: you deposit your own money, and the broker adds a loan on top. For US stocks, a federal rule called **Regulation T** (often shortened to **Reg T**) says your first purchase can be up to 50% borrowed — with $10,000 of your own money, you could buy up to $20,000 of stock on day one.

Bigger buying power sounds great. Remember what it is, though: a loan, with interest, secured by your investments. If the investments fall, the debt stays.

How Margin Borrowing Works: A Worked Example

Let's walk through real numbers, slowly.

You deposit $10,000 into a margin account. You buy $20,000 of a stock — $10,000 of your cash plus a $10,000 loan from the broker.

- **If the stock rises 10%:** your position is worth $22,000. Sell, repay the $10,000 loan, and you have about $12,000 (minus interest and fees) — a gain of about $2,000, or 20%, from a 10% move. That doubling is the attraction of margin. It is called **leverage** — using borrowed money to control a bigger position than your cash alone could.
- **If the stock falls 10%:** your position is worth $18,000. Sell, repay the loan, and you have about $8,000 — a loss of about $2,000, or 20%.

Leverage is a multiplier: it multiplies wins, losses, and speed. Beginners usually need *less* speed, not more.

The Interest Nobody Mentions

Borrowed money is not free. Brokers charge **margin interest** — a yearly percentage rate charged on your loan balance. Rates vary by broker and loan size, and they change over time, so check your broker for the current number.

On a $10,000 loan, even a moderate yearly rate means hundreds of dollars a year quietly leaving your account — win or lose. Hold a losing position on margin for months and you are paying rent on a loss.

> **RISK**
> Margin interest is owed in winning months and losing months alike. Many beginners discover it only on a monthly statement. Read your broker's margin rate before you borrow a single dollar.

Maintenance Margin and the Margin Call

Your **equity** is what you actually own: the current value of your investments minus what you borrowed. In our example, if the position is worth $22,000 and the loan is $10,000, your equity is $12,000. Your broker watches that number every day.

Maintenance margin is the minimum equity, as a percentage of the position's value, that your broker requires you to keep. Regulators set a floor (25% for most stocks); most brokers require more — 30%, 40%, sometimes higher for risky stocks.

If your equity falls below that line, you get a **margin call**: a demand to fix the account *now*, by depositing cash or selling positions. Here is the part beginners miss: if you do not act fast enough, the broker may legally sell your investments for you, at whatever price the market offers, without asking — and they will sell the positions they choose, not the ones you would choose.

Worked example: the stock falls 40%. The position is worth $12,000; your equity is $12,000 − $10,000 = $2,000 — only about 17% of the position's value, below the maintenance line. Margin call. And notice: the stock fell 40%, but your own money fell from $10,000 to $2,000 — an 80% loss.

> **RISK**
> With margin, a bad week can end with the broker selling your stocks at the bottom while you are at work. You cannot "wait for it to come back" if the account is no longer yours to wait with. This is why Team Alpha tells beginners: learn in a cash account first.

Margin accounts also unlock advanced features in many brokers — like **short selling** (betting a stock will fall) and some options strategies — which carry their own large risks and get their own chapters. Having the account does not mean you must use them.

The Pattern Day Trader Rule

A **day trade** is buying and selling the same stock (or option) on the same day. Do it a lot in a margin account and an old US rule may apply to you.

The classic rule is called the **Pattern Day Trader** rule (often shortened to **PDT**). Under it, four or more day trades within five business days in a margin account gets you flagged as a pattern day trader — and you must then keep at least **$25,000 in equity** in the account to keep day trading. Drop below $25,000 and the broker can block your day trades until the balance is restored.

Two things every beginner must know now:

- **The rule has been changing.** US regulators have been replacing the old PDT system with new intraday-margin standards — rules based on the risk you actually take during the day instead of one flat $25,000 line — and brokers have been transitioning on their own schedules.
- **Your broker is the final word.** Because of that transition, the exact limits in *your* account depend on *your* broker *right now*. Before placing a fourth day trade, read your broker's current day-trading page or call and ask.

One point has stayed simple through every version: these day-trader rules apply to **margin accounts**. Cash accounts are not flagged — though they have their own settlement limits, next.

Settlement: T+1 and the Good Faith Violation

When you sell a stock, the money does not fully become "yours to reuse" that same second. **Settlement** is the short official waiting period for a trade to be finalized — money and shares formally change hands. Since May 2024, US stock and options trades settle in one business day: **T+1**, trade date plus one business day. In a margin account the broker's loan bridges the gap, so settlement barely matters. In a cash account, it matters a lot.

The plain-words rule: **only trade with money that has settled.** Break it and you can earn a **good faith violation** — you bought a stock with unsettled money, then sold it before that money settled. You sold something you had not fully paid for yet.

Concrete example: On Monday you sell Stock A for $500; that $500 settles Tuesday (T+1). Also on Monday, impatient, you use the $500 to buy Stock B and sell Stock B that same afternoon. You sold before the funds settled: good faith violation.

Brokers track these; a common policy restricts an account to settled-cash-only trading for 90 days after several violations in 12 months. The fix is easy: in a cash account, wait until sale money settles (usually the next business day) before buying something you might sell quickly. Money deposited from your bank and left to settle is always safe to trade with.

Taxes: The Basics Every Trader Must Know Exist

This section is a map, not a manual — it names the tax ideas that exist so nothing ambushes you.

Every Sale Is a Taxable Event

When you sell an investment for more than you paid, you have a **capital gain** — a profit the US government taxes. Sell for less and you have a **capital loss**, which can reduce your taxes in ways a professional can explain. Buying is not taxed; selling is the taxable moment. Every trade you close can show up on your tax return — hundreds of trades means hundreds of line items to handle.

Short-Term vs. Long-Term

How long you held the investment changes how a gain is taxed:

- **Short-term:** you held it for **one year or less**. Day trades and swing trades (trades held days or weeks) are almost always short-term.
- **Long-term:** you held it for **more than one year**.

The two are taxed differently: long-term gains generally get a lower, preferential rate, while short-term gains are generally taxed like regular income from a job. Exact rates depend on your income, filing situation, and current law — and they change — so never plan around a rate from a book or video.

For active beginners the lesson is simple: nearly all your gains will be short-term, and a profitable year of day trading comes with a real tax bill. Set money aside as you go instead of spending every dollar of profit.

The Wash Sale Rule

A **wash sale** is a tax rule that disallows a loss — for now — in a specific situation. If you sell an investment at a loss and then buy a **substantially identical** security (usually the same stock, or an option on it) within 30 days before or after that sale, the IRS (the US tax agency, the **Internal Revenue Service**) says the loss cannot be claimed yet. The window is 61 days total: 30 days before the sale, the sale day, and 30 days after.

Example: You sell 100 shares at a $400 loss on June 10. On June 25 you buy the same stock again because "now it looks good." That is a wash sale. The $400 loss is disallowed for this year's taxes; in many cases it is added to the cost of your new shares, so you may effectively claim it later when you sell for good — but the timing surprise is what hurts beginners.

Day traders hit this rule constantly, because they rebuy the same tickers every day. Worse, your broker's software only sees its own accounts — buy the same stock in a *different* account (including a spouse's, or an IRA retirement account) and the rule can still apply, sometimes permanently with an IRA. This is exactly where a tax professional earns their fee.

Year-End Forms: The 1099

After the year ends, your broker sends a **Form 1099** package (the key part is usually the 1099-B) listing every sale you made: what, when, for how much, and what you paid. The broker sends a copy to the IRS too. Keep yours, expect it in the first months of the year, and do not file before it arrives — corrected versions sometimes follow.

> **NOTE**
> Everything in this tax section is general education, not tax advice. Tax law changes, state taxes differ, and details like wash sales across accounts are genuinely tricky. Before your first serious year of trading, pay for an hour with a tax professional who works with traders — some of the best money a trader spends.

Common Beginner Mistakes

- Opening a margin account because it was the default, without knowing borrowing was turned on.
- Being surprised by margin interest on a monthly statement.
- Thinking a margin call is negotiable — it is not; the broker can sell your positions without asking.
- Making a fourth day trade in a small margin account without checking the broker's current day-trader policy.
- In a cash account, repeatedly buying with unsettled sale money and collecting good faith violations.
- Assuming profits are "tax-free until I withdraw them" — they are taxable when you sell, withdrawal or not.
- Rebuying a stock days after selling it at a loss and expecting to claim that loss this year.
- Trading all year with no money set aside for the tax bill.

Chapter Summary

- A cash account trades only your own settled money: no borrowing, no interest, no margin calls.
- A margin account adds a broker loan: Reg T allows up to 50% borrowing on initial stock purchases, and interest is charged on what you borrow.
- Leverage multiplies outcomes: a 10% move can become roughly a 20% gain — or a 20% loss — on your own money.
- Maintenance margin is the minimum equity you must keep; fall below it and a margin call can force sales at the worst moment.
- The classic Pattern Day Trader rule required $25,000 minimum equity for frequent day traders in margin accounts, but regulators have been replacing it with intraday-margin standards and brokers are transitioning — always check your broker's current rule.
- US trades settle T+1, the next business day. In a cash account, buying with unsettled money and selling before it settles is a good faith violation.
- Every sale is a taxable event. Gains on investments held one year or less are short-term, over one year long-term, and the two are taxed differently.
- The wash sale rule disallows a loss if you buy a substantially identical security within 30 days before or after selling at a loss.
- Your broker sends a Form 1099 after year-end listing your sales; the IRS gets a copy too.

Check Yourself

1. What is the biggest practical difference between a cash account and a margin account?
2. You buy $20,000 of stock using $10,000 of your own money and a $10,000 loan. The stock falls 10%. Roughly how much of your own money have you lost, before interest and fees?
3. What is a margin call, and what can the broker do if you do not respond?
4. In a cash account, what is a good faith violation? Give the plain-words version.
5. You sell a stock at a $400 loss on June 10 and buy the same stock again on June 25. What rule applies, and what happens to the loss?

Answers: 1) A cash account trades only your own settled money; a margin account lets you borrow from the broker — with interest, and with the broker able to force sales if your equity falls too low. 2) About $2,000, or 20%: the position drops to $18,000, you still owe the $10,000 loan, leaving about $8,000. 3) A margin call is the broker's demand to restore your equity when it falls below the maintenance requirement; if you do not act in time, the broker may sell your positions without your permission. 4) You bought a stock with money from a sale that had not settled, then sold it before the money settled — you sold something you had not fully paid for. 5) The wash sale rule: the $400 loss is disallowed for now because you rebought a substantially identical security within 30 days after the sale (inside the 61-day window).

> **RULE**
> Boring is protective. Know which account you have, know what you owe, know the day-trading and settlement rules at your broker, and let a tax professional handle April. The traders who last are the ones the fine print never surprises.