Regulatory Notice 21-13

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Notice Type
- Guidance

Suggested Routing
- Compliance
- Institutional
- Legal
- Margin
- Operations
- Registered Representatives
- Risk
- Senior Management
- Systems
- Trading

Key Topics
- Day Trading
- Margin
- Multiple Purchases and Sales
- Pattern Day Trader

Referenced Rules & Notices
- Rule 4210

Margin Interpretation Updates

FINRA Announces Updates to the Interpretations of FINRA's Margin Rule for Day Trading

Summary

This *Notice* announces, effective immediately, clarifications of interpretations of FINRA margin requirements regarding day trading (Rule 4210(f)(8)(B)(ii)).

Questions concerning this *Notice* should be directed to:

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- Kathryn Moore, Associate General Counsel, Office of General Counsel, at (202) 728-8200 or *kathryn.moore@finra.org*.

Background & Discussion

FINRA Rule 4210 (Margin Requirements) specifies the margin requirements applicable to securities held in margin accounts, including both strategy-based margin accounts and portfolio margin accounts. FINRA maintains interpretations regarding FINRA Rule 4210, available on the Interpretations of FINRA's Margin Rule webpage, in a portable digital format (PDF) document where the interpretations immediately follow the section of the rule to which they relate. This *Notice* clarifies and updates the interpretations as discussed below.

Day Trading

FINRA Rule 4210(f)(8)(B)(i) defines "day trading" to mean the purchasing and selling or the selling and purchasing of the same security on the same day in a margin account except for positions held overnight. FINRA Rule 4210(f)(8)(B)(ii) defines a "pattern day trader" as a customer who executes four or more day trades within five business days.[1] Firms have raised questions about the determination of when multiple purchases and sales of the same security on the same day are considered a single day trade. Current Interpretation /01 provides guidance for such determination. To provide additional flexibility and guidance, FINRA is adding new Interpretation /02, which provides an alternative method to calculate the number of day trades when there are multiple purchases and sales of the same security on the same day.

In addition to the numerical determinations of when a customer is classified as a "pattern day trader," FINRA Rule 4210(f)(8)(B)(ii) provides that if a member knows or has reasonable basis to believe that a customer will engage in pattern day trading, then the pattern day trading requirements of the rule will apply. Investors and firms have raised questions about how to terminate a customer's "pattern day trader" classification if the investor no longer wishes to engage in such trading. To provide clarity and guidance for firms, FINRA is adding new Interpretation /03 regarding terminating pattern day trader status.

New Interpretations of FINRA Rule 4210(f)(8)(B)(ii)

/02 Multiple Purchases and Sales – Alternative Method

Rather than counting day trades based on the number of transactions a customer executes to establish or increase a position that is liquidated on the same day (as set out in Interpretation /01 above) a firm may instead count day trades based on the number of times during the day that the day trading customer changes its trading direction (*i.e.*, changes from buying a particular security to selling it, or changes from selling a particular security to buying it).

Example A:

09:30 Buy 250 ABC
09:31 Buy 250 ABC
13:00 Sell 500 ABC
The customer has executed one day trade.

Example B:
09:30 Buy 100 ABC
09:31 Sell 100 ABC
09:32 Buy 100 ABC
13:00 Sell 100 ABC
The customer has executed two day trades.

Example C:
09:30 Buy 500 ABC
13:00 Sell 100 ABC
13:01 Sell 100 ABC
13:03 Sell 300 ABC
The customer has executed one day trade.

Example D:
09:30 Buy 250 ABC
09:31 Buy 300 ABC
13:01 Buy 100 ABC
13:02 Sell 150 ABC
13:03 Sell 175 ABC
The customer has executed one day trade.

Example E:
09:30 Buy 199 ABC
09:31 Buy 142 ABC
13:00 Sell 1 ABC
13:01 Buy 45 ABC
13:02 Sell 100 ABC
13:03 Sell 200 ABC
The customer has executed two day trades.

Example F:
09:30 Buy 200 ABC
09:30 Buy 100 XYZ
13:00 Sell 100 ABC
13:00 Sell 100 XYZ
The customer has executed two day trades

/03 Terminating Pattern Day Trader Status

A customer that has been classified as a pattern day trader under paragraph (f)(8)(B)(ii) of this Rule is presumed to remain a pattern day trader. However, if a customer seeks to terminate its pattern day trader classification, a member may so accommodate such request after the member determines in good faith, as defined in Section 220.2 of Regulation T, that the customer will no longer engage in pattern day trading.

A member may, for example, base its good faith determination on providing the definition of pattern day trader to the customer and receiving a written certification from the customer that (1) the customer understands the definition of pattern day trading and (2) the customer will not engage in future pattern day trading.

As an alternative, a good faith determination that a customer will not engage in future pattern day trading may be based on the member's application of technological restrictions on such customer's trading activity that effectively prevent the customer from engaging in pattern day trading.

If, after a termination of pattern day trader status, a customer again engages in pattern day trading, such customer's pattern day trader status may not be terminated absent extraordinary circumstances.

Interpretation Updates

These interpretation updates are available in portable digital format (PDF) on the Interpretations of FINRA's Margin Rule web page.

FINRA member firms and others that maintain the hardcopy version of the Interpretations of FINRA's Margin Rule may refer to the accompanying updated pages, containing the aforementioned interpretation updates, which are being made available to enable the replacement of existing pages in the hardcopy version of the Interpretations of FINRA's Margin Rule. The filing instructions for the new pages are as follows:

- Remove old pages 174 to 179 and insert new pages 174 to 181.

Endnote

1. A customer is not considered a "pattern day trader" if the number of day trades is 6 percent or less of the total trades for a five business day period.