January 28, 2025

VIA ELECTRONIC SUBMISSION

Jennifer Piorko Mitchell
Office of the Corporate Secretary
FINRA
1735 K Street, NW
Washington, DC 20006-1506

Re: Regulatory Notice 24-13; FINRA Requests Comment on the Effectiveness and Efficiency of its Requirements Relating to Day Trading

Dear Ms. Piorko Mitchell:

FINRA is requesting comment on various trading requirements including the Rule 4210 framework governing day trading requirements to assess its effectiveness and efficiency.[1] As the operator of six national securities exchanges and a leader in exchange-traded derivatives, Cboe Global Markets, Inc. ("Cboe")[2] appreciates the opportunity to provide feedback on this topic.

In addition to operating six national securities exchanges, among other venues, Cboe also has a longstanding commitment to empowering investors through education. Cboe's Options Institute is highly regarded as an important educational resource and has been dedicated to educating investors for over 35 years. As the markets have become increasingly more accessible, education continues to play a key role in that accessibility.

It's through the lens of the importance of expanding access to the markets for a wider range of investors that Cboe wishes to share its views on the current day trading requirements – specifically the pattern day trader requirements – and how those requirements can be modernized to ensure their relevance and keep pace with the technological advancements that have occurred since Rule 4210 was put in place in 2001.

<u>**Summary**</u>

- **There have been many technological and industry advancements since 2001 that render the pattern day trader requirements outdated. Updates taking into account those advancements are in order and will help realign the rule with its original intent.**

[1] Regulatory Notice 24-13 (FINRA Requests Comment on the Effectiveness and Efficiency of its Requirements Relating to Day Trading) (October 29, 2024).
[2] Cboe operates six national securities exchanges (Cboe Exchange, Cboe C2 Exchange, Cboe BYX Exchange, Cboe BZX Exchange, Cboe EDGA Exchange, and Cboe EDGX Exchange), including the largest U.S. options exchange.

- **Smaller investors with modest account balances are being inadvertently penalized by Rule 4210 and needlessly locked out of the market.**
- **The current pattern day trader margin requirements are no longer reflective of today's trading environment and risks. Brokerage firms with real-time risk monitoring and the ability to automatically block trades if a client's activity exceeds targeted risk parameters should be exempt from needing to apply the rudimentary pattern day trader designation to clients.**
- **In all other instances, modernization of the pattern day trader requirements, as suggested below, will prevent investors with modest account balances from being shut out from the markets while staying consistent with the risk mitigating aims of the rule when it was conceived.**

Discussion

History of Rule 4210

The margin requirements associated with pattern day trading under Rule 4210 were put in place over 20 years ago to address clearing firm risk while also protecting investors. Specifically, if an account makes four or more day trades (roundtrip trades) within five business days and those trades account for more than 6% of the account's total trading activity for that period, that margin account will be flagged as a "pattern day trader" account. These requirements require accounts deemed to be pattern day traders to maintain minimum equity of $25,000 in their margin accounts to avoid trading restrictions when their accounts fall below that amount.[3]

Additionally, pattern day trader accounts cannot trade in excess of their day-trading buying power ("DTBP"). DTBP is defined as the equity in a customer's account at the close of business of the previous day, less any maintenance margin requirement, multiplied by four for equity securities. If a pattern day trader exceeds their DTBP, the account will be margined based on the cost of all the day trades made during the day and the customer's day-trading buying power will be limited to the equity in the customer's account at the close of business of the previous day, less the maintenance margin required, multiplied by two for equity securities. These requirements, which were put in place in 2001, have remained largely unchanged for the last two decades and counting.

Industry Advancements

The industry itself has also grown and seen many advancements since 2001. For example, there are now dozens of securities exchanges providing ample investor choice while most investors are also able to enjoy zero commission trading. Additionally, the standard for settlement moving to the next business day after a trade (T+1) in May 2024 "reflects improvements in technology that allow trades to settle more quickly."[4] One of the goals of the original rule was to protect clearing firms (along with investors) and the move to T+1 settlement allows those clearing firms to have less exposure to risk while trades

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[3] Accounts under $25,000 that have been tagged as pattern day trader accounts are technically able to open positions, but they are unable to day trade. However, oftentimes for a firm to make sure a client does not day trade, all trades need to be blocked to help ensure compliance with Rule 4210.

[4] "Understanding Settlement Cycles: What Does T+1 Mean for You?" Understanding Settlement Cycles: What Does T+1 Mean for You? | FINRA.org (January 30, 2024).

are being settled as the settlement timeframe has shortened dramatically from when Rule 4210 was put in place.[5]

Notably, while the importance of the goals behind the original implementation of the margin requirements associated with pattern day trading has not changed, the technology and the industry have evolved greatly. Specifically, broker-dealers are now able to calculate risk in real-time via robust risk controls that are able to block trades that would exceed the firm's risk parameters for the client. This important technological evolution makes elements of Rule 4210 in need of modernization to accurately reflect the technological and market developments and the existence of real-time risk monitoring tools that were not available two decades ago.

While these positive developments have led to greater democratization of the markets, they have also resulted in an increased number of accounts being designated as pattern day trader accounts. This means that while an unprecedented number of investors are able to realize the benefits of participating in the securities markets – some for the first time – those with smaller accounts that are below $25,000 are being unnecessarily locked out of the markets and penalized simply for having accounts with smaller balances even though firms are now able to monitor risk in real-time and block trades that exceed that risk tolerance. Importantly, considering the aforementioned advancements, these smaller investors are not imposing the same systemic risk as was the case when the requirements were first enacted. Modernizing the pattern day trader margin requirements would help ensure the markets are able to remain accessible to improve the overall investor experience.

Negative Implications of the Current Pattern Day Trader Margin Requirements for Investors

Unfortunately, considering the technological advancements that allow firms to utilize real-time risk controls, the current Rule 4210 margin requirements for accounts that are deemed pattern day traders have become outdated. These requirements are no longer consistent with their original intent of protecting investors and clearing firms and fail to recognize that brokers now have robust, real-time risk control capabilities to block certain trades and limit risk. Currently, if an account that is deemed a pattern day trader account has an equity minimum that falls below $25,000, that account holder is effectively locked out of the markets even though their broker has real-time risk controls that allow the firm to properly limit this customer's risk. This creates the perception of an unlevel playing field for investors while also creating a financial barrier to actively participating in the financial markets.

Notably, because retail investors often roll their options positions and engage in spread trading, the pattern day trader provisions of Rule 4210 can disincentivize retail investors from taking risk off in order to avoid such a designation. It is a bad development for the entire ecosystem when the outcome of a particular rule is that it actually discourages investors from reducing their overall risk profile.

The unintended consequences of the current pattern day trader designation are that it causes investor frustration and confusion and results in retail investors being discouraged from investing in ways that were not contemplated by the rule when it was originally adopted in 2001. Rule 4210 limits investors' ability to manage risk – retail investors may hesitate to close out positions to avoid receiving the pattern day trader designation, which may increase position risk. This unforeseen outcome negatively impacts

[5] From 2001-2017 the standard settlement cycle was T+3.

both the investor, and their firm as intra-day risk management is preferred to reduce overnight risk for both.

Cboe's Recommendations

Cboe believes that the pattern day trader margin requirements associated with Rule 4210 are outdated and no longer reflective of the current trading environment and risks. Brokerage firms with real-time risk monitoring and the ability to automatically block trades if a client's activity exceeds targeted risk parameters should be exempt from needing to apply the pattern day trader designation to clients. Ultimately, if the risk profile is adequately covered by the firm's risk management tools and associated technology, account balance should be inconsequential – as opposed to an arbitrary threshold that negatively impacts smaller investors.

If FINRA believes that some type of pattern day trader requirements and minimum equity amount is still necessary, our recommendation would be to let each individual brokerage firm set their own minimum equity amount for their customers trading in margin accounts. That account would then only receive the pattern day trader designation after surpassing a predetermined threshold set by the firm. The various brokerage firms should be able to have flexibility and different processes to determine pattern day trader account thresholds because firms serve different customer bases characterized by distinct sophistication levels, needs, and ultimately, risk tolerances.

At the very least, if the $25,000 minimum equity threshold is retained, Rule 4210 should be modernized to reflect the previously mentioned technological and industry advancements to allow firms to utilize the Regulation T overnight buying power of 2x day trader buying power (2x DTBP)[6] rather than locking these investors out of the market.

Consider a PDT retail investor with excess maintenance margin of $4,000, but with an account equity that is below the $25,000 PDT minimum

	Under Current Rule	Under Proposed Change
Pattern day trader DTBP?	Excess maintenance margin = $4,000 DTBP = $0 The investor is prevented from entering opening orders (DTBP goes to zero) because they are a PDT and FINRA Rule 4210 prohibits opening orders until a $25,000 minimum equity requirement is met.	Excess maintenance margin = $4,000 DTBP = $8,000 (2 x $4,000) FINRA Rule 4210 is amended to permit day trading without the minimum equity of $25,000, but only at one-half of the regular DTBP. Thus, there would be two classes of PDTs; those that wish to have DTBP of 4x and must meet the $25,000 minimum equity requirement and those that wish to have DTBP of 2x and have no minimum equity requirement. PDTs with a DTBP of 4x and $25,000 minimum equity would automatically be limited to DTBP of 2x if their account equity falls below $25,000.

Note: "Excess maintenance margin" is the investor's equity in their margin trading account above other margin requirements. i.e., FINRA rules require investors have at least $2,000 to open a margin account and set minimum initial margin requirements (up to 50% of security's price) and maintenance margin requirements (at least 25% equity percentage). Brokers may set higher requirements.

[6] Day trader buying power is calculated using the excess margin – the amount of cash and equity remaining in the trading account above the minimum requirements – as of the close of business of the previous day.

This modest change allows firms to reduce the DTBP to Regulation T margin levels and use their dynamic real-time risk monitoring tools in a way that recognizes firms' real-time risk controls instead of completely blocking investor access to the markets until their account has at least $25,000. Updating Rule 4210 to limit the trading that can be done by these investors to two times their excess margin (rather than four times, which is what pattern day traders with accounts over $25,000 are permitted to do) would at least allow the unintended capture of smaller investors under the rule to maintain market access rather than continue to be disadvantaged by the current margin requirements.

Cboe Responses to Specific Questions Raised in the Request for Comment

Question 1 *– Have the original purposes of and need for the day trading requirements (including the day-trading account approval and risk disclosure requirements, and the pattern day trading requirements) been affected by changes to technology, types of securities available, firms' capabilities for monitoring and assessing intra-day risk, the business environment, or customer behavior? What are the relevant risks that should be addressed by these requirements in the current environment? Are there alternative or additional ways to protect customers that FINRA should otherwise consider? If so, please explain.*

Cboe Response: Yes, the broker technological advancements discussed in this letter have rendered the pattern day trader requirement outdated and less necessary. The rule modifications we suggest would realign the rule with the original intent.

Moreover, Cboe supports the idea that if the risk profile is adequately covered by the firm's risk management tools and associated technology, the account balance is inconsequential. If FINRA believes that a minimum equity requirement is still needed, we recommend allowing each brokerage firm to determine its own minimum equity threshold for customers trading in margin accounts. Once an account falls below this threshold after completing the required number of roundtrip trades, it would then receive the pattern day trader designation. Each individual firm is best positioned to know the specific behavior, risk profile, and general makeup of their customer base and this would avoid widespread restrictions on accessing the market for smaller investors who simply have less equity in their accounts but may not actually impose any additional risk to the firms due to their ability to monitor risk intra-day and in real time.

Alternatively, if the pattern day trader requirements as well as the $25,000 minimum equity threshold are retained, Rule 4210 should be modernized to reflect the previously mentioned technological and industry advancements to allow firms to utilize the Regulation T overnight buying power of 2x day trader buying power (2x DTBP) rather than locking these investors out of the market.

Question 12 *– Have changes in the business and market environments altered the risks that the pattern day trading requirements are intended to address? For example, have developments such as zero commission trading or narrowing bid-offer spreads in certain securities in the equity markets affected the need for the pattern day trading requirements?*

Cboe Response: Yes, in addition to the technological and industry advancements that have taken place since the pattern day trading requirements were put into effect, changes in the overall business and market environments have also altered the risks meant to be captured by the original intent of Rule 4210. As mentioned previously, a key objective of the original rule was to protect both clearing firms

and investors. The adoption of T+1 settlement has reduced the risk exposure for clearing firms during trade settlements, as the settlement period has been considerably shortened since Rule 4210 was implemented.

Question 14 *- In a margin account, a day trade can count toward a customer's pattern day trading designation regardless of whether the trade uses margin. With T+1 settlement, it is possible that day trading-type activity, without using margin, might move to cash accounts. There are no restrictions on paying for a security and selling it the same day in a cash account, and the proceeds would be available to pay for purchases the next day. What changes in the pattern day trading requirements would be warranted if such trading moves to cash accounts?*

Cboe Response: If such trading moves to cash accounts, we do not believe any changes in the pattern day trading requirements would be warranted. It would be problematic if day trading requirements that are largely based on day trading buying power associated with margin requirements were imposed on cash accounts that do not involve margin trading. FINRA's day trading requirements state that "all securities purchased in the cash account must be paid for in full before they are sold...purchasing a security, paying for it in full as required by Regulation T, and then selling the same security is not considered a day trade."[7] Imposing pattern day trader rules to cash accounts would be a negative outcome that would likely have many unintended consequences for investors – including, but not limited to, restricting access to the market for even more investors than are currently restricted today.

Cboe also wishes to clarify that short-dated options trades (also known as zero days to expiration or "0DTE" trades) should, by their very nature, not be considered a trade for purposes of counting roundtrips for pattern day trader requirements. Short-dated options positions often expire on the same day of purchase rather than the investor buying and selling (or selling and buying) the same security pursuant to the day trading definition[8] and therefore should not be viewed as constituting a day trade for purposes of determining if an investor's account needs to be deemed a pattern day trading account.

Question 20 *- What changes, if any, should FINRA consider for the pattern day trading requirements?*

Cboe Response: See Cboe's recommendations discussed earlier in the letter as well as the response to Question 1.

Conclusion

Cboe respectfully requests that FINRA modernize the pattern day trader requirements to properly reflect the technological and industry advancements that have taken place since the rule was introduced over twenty years ago.

Specifically, we urge FINRA to exempt brokerage firms that employ real-time risk monitoring that can systematically block trades when a client's activity exceeds targeted risk parameters from having to apply the pattern day trader designation to clients. Alternatively, firms should be permitted to either (1)

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[7] Day Trading | FINRA.org

[8] FINRA defines day trading as "where an individual buys and sells (or sells and buys) the same security in a margin account on the same day in an attempt to profit from small movements in the price of the security."

reduce the day-trading buying power to Regulation T margin levels and utilize their real-time calculations for pattern day trading accounts with less than $25,000 or (2) determine their own minimum equity threshold – instead of restricting those with smaller accounts from participating in the market and disincentivizing these investors from properly taking risk off their positions (especially with respect to options trades).

Any of these sensible solutions would spare investors from experiencing the problematic and unintended consequences associated with the outdated nature of Rule 4210 while still properly accounting for firms' real-time risk. These solutions would also align the requirements with what was envisioned when they were first developed (i.e., to minimize clearing firm risk). Importantly, updating the pattern day trader requirements as recommended above would bring the U.S. securities markets in line with the U.S. futures markets as well as other countries where retail investors do not face similar constraints.

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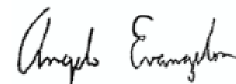
Cboe appreciates the opportunity to share its views on the request for comment. Cboe welcomes the opportunity to discuss these comments further.

Sincerely,



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