



RIA User Guide

Freeride Trades

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Introduction

In a cash account, an investor must pay for the purchase of a security (meaning, the trade must settle) prior to selling that security. If an investor buys a security and then sells that same security without paying for the security in full by settlement date, the investor is considered to be “freeriding.”

“Freeriding” is not permitted under Regulation T (Reg T) and may require the investor’s broker to “freeze” the investor’s account. During this “freeze” period, an investor may still purchase securities with the cash account, but the investor must fully pay for any purchase on the date of the trade. An investor may avoid having a “freeze” placed on his cash account by fully paying for the securities by the settlement date with funds that do not come from the sale of the securities.

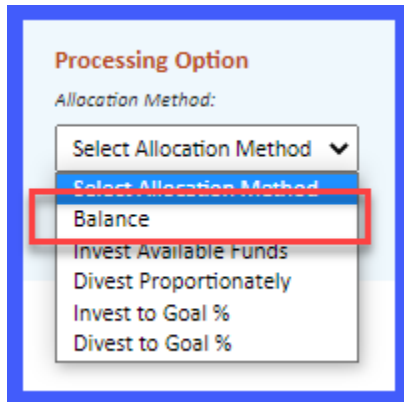
The duration of the “freeze” placed on the client account is based on the number of violations occurring in a rolling 1-year period.

- For violation #1: 90 calendar days
- For violation #2: 180 calendar days
- For violation #3: 365 calendar days

Preventing a Freeride

Model Processing (Balance)

Model processing poses a unique challenge when it comes to freeriding and the possible restrictions to be applied once a freeride occurs. As a result, AAS has taken the approach of erring on the side of preventing the freeride by disallowing any sell that may violate this policy. When this occurs, the RIA will be notified of the exclusion(s) at the time of trade creation or approval.

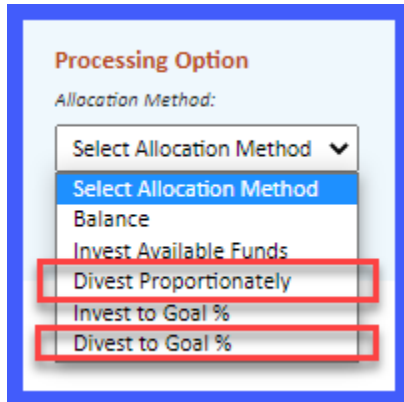


When model processing (balance) goes to sell shares, it checks to see if there are settled shares. If so, they can be sold without any further analysis. If there are not settled shares then model processing will compare the purchase price of the unsettled shares to the current cash in the account (the settled/posted cash, not including any pending events)

- If the cost of the unsettled shares is **MORE** than the cash in the account, then the shares cannot be sold as it would cause a freeride violation.
- If the cost of the unsettled shares is **LESS** than the "uncommitted" cash in the account, then the sale of the unsettled shares can occur as there is sufficient cash to cover.

Model Processing (Divest)

The Divesting to Goal and Divesting Proportionately model processing methods follow the same framework as Balancing, with any sells that may violate the freeride policy being disallowed.



When this occurs, we will display an error message which reads: "Account 123456 could not sell XXYYY due to the freeride rule resulting in the account not being fully balanced."

What happens when a sell trade is identified that would result in a freeride violation?

The offending account/ticker combination will be disallowed from participating in the model processing event and an error message is presented to the user:

"Account 123456 – Potential Free-Riding Violation in XXYYY – Sale of this security was disqualified."

The user always has the option of creating a Block Trade (sell) or account level Trade Order those accounts where he/she wants to proceed with the sell, understanding that the action could result in a freeride and a restriction being applied to the account.

Model Process Summary

0 Alerts

2 Messages

1 Completed

Completed Trade Order #	Model	Symbol
20456435	137-Free-Free Ride Model	SPY

Messages and Alerts

Alerts

No Alerts

Messages

Model 137 - Account 684094 - Potential Free-Riding Violation in 60263 ISHARES TR BARCLAYS 1-3 TREAS BD ETF - Sale of this security was disqualified

Model 137 - 1 trades created or modified

Close Continue To Blotter Create Report

Limiting Trading on Restricted Accounts

Accounts violating the freeride policy will be restricted to using **settled cash** for any purchases. The duration of the “freeze” placed on the client account is based on the number of violations occurring in a rolling 1-year period.

- For violation #1: 90 calendar days
- For violation #2: 180 calendar days
- For violation #3: 365 calendar days

Should the user attempt to make a purchase on the account with unsettled cash (while it is restricted) we will disallow the trade and return a message. The good order check occurs both at the time the trade is recommended and again at the point of approval.

Message to display for Block Trade (buy), manual TOR or Trade Upload:

- "Account 123456 has freeride restriction in effect which limits purchases to using settled cash only. You may initiate additional purchase orders once settled funds are available. The freeride restriction expires on mm/dd/yyyy."

Messages to display for Model Processing:

- “Account 123456 could not sell XYYYY due to the freeride rule resulting in the account not being fully balanced.”
- “Account 123456 has a freeride restriction in effect which limits purchases to using settled cash only. As a result, the account may not be fully balanced. You may want to initiate model processing again once settled funds are available. The freeride restriction expires on mm/dd/yyyy.”

Reporting: Accounts with Violations

A must-read bulletin will be created daily listing all accounts that have freeride restriction in effect. Accounts will be displayed in chronologic order based on the date freeride restriction was added, with the most recently added accounts listed first.

A bulletin will not be generated if there are no accounts subject to a freeride restriction.

The screenshot displays a web application interface with a navigation bar at the top containing 'Analytics', 'Trading', 'Client Management', 'Documents', and 'My Profile'. Below the navigation bar, there are tabs for 'Completed Reports', 'Standard Reports', 'Custom Reports', 'Bulletins', 'Reminders', and 'Document Upload'. The main content area is titled 'BULLETINS' and shows 'Viewing 123 results'. A table lists various bulletins with columns for 'All', 'Must Read', 'Date', and 'Subject'. One bulletin is highlighted: 'Accounts with a Free Ride Restriction' on 10/20/2021 at 01:02:25am. To the right, a 'Bulletin Details' panel shows the bulletin's metadata and a table of affected accounts. The table has columns for 'Number', 'Type', 'Name', 'Restriction Date', 'Restriction Expiration Date', 'Rep ID', 'Rep Name', and 'Value'.

Number	Type	Name	Restriction Date	Restriction Expiration Date	Rep ID	Rep Name	Value
123456	IRA	Billy Client	10/18/2021	1/18/2022	11223	Russel Crow	14,918.22
456789	IN	Jamie Investor	10/10/201	1/18/2021	33445	Marlon Brandow	256,587.32
147369	JT	Billy Client & Jamie Investor JTWRDS	9/30/2021	12/30/2021	45654	Donald McFarland	100,123.78

Examples

The SEC website provides good examples of freeride scenarios (and permissible trades)

https://www.sec.gov/oiea/investor-alerts-and-bulletins/ib_cashaccounts

Permitted Trade Examples

Examples of trading that would be permitted in a cash account include:

1. An investor has \$10,000 in cash and no securities in a cash account. The investor buys \$10,000 worth of ABC stock on Monday and sells it the same day.

These transactions are permissible since the investor purchased the ABC stock on Monday with the \$10,000 in cash that the investor had in the cash account. Since the investor purchased the ABC stock with cash, the investor may sell this stock at any time.

2. An investor holds \$10,000 of fully paid for and settled ABC stock in a cash account. The investor does not hold any additional cash or securities in the cash account. The investor sells all the ABC stock on Monday. On Friday, the investor buys \$10,000 worth of XYZ stock.

These transactions are permissible because an investor can sell a fully-paid for and settled security held in a cash account. The \$10,000 proceeds from the sale of the ABC stock would have settled on Wednesday. Therefore, the investor would have “sufficient funds” in the cash account on Friday to purchase the XYZ stock.

3. An investor holds \$10,000 of fully paid for and settled ABC stock in a cash account. The investor does not hold any additional cash or securities in the cash account. The investor sells all the ABC stock on Monday and buys \$10,000 worth of XYZ stock the same day. The investor sells the XYZ stock on Friday.

The sale of the ABC stock is permissible because an investor can sell a fully-paid for and settled security held in a cash account. The purchase of the XYZ stock is also permissible. The investor may purchase the XYZ stock with the proceeds from the sale of the ABC stock as long as the investor does not sell the XYZ stock prior to the settlement of the ABC stock sale, which is Wednesday. By doing this, the investor will have made full cash payment for the XYZ stock before selling it on Friday.

Freeride Trade Example

The following example illustrates “freeriding” per the SEC website:

An investor holds \$10,000 of fully paid for and settled ABC stock in a cash account. The investor does not hold any additional cash or securities in the cash account. The investor sells all the ABC stock on Monday and buys \$10,000 worth of XYZ stock on the same day. On Tuesday, the investor sells all of the XYZ stock without adding any additional cash to the account.

The settlement date on the sale of the ABC stock that the investor used to pay for the purchase of the XYZ stock would be Wednesday (two business days after the date of the sale). Since the investor used the proceeds from a sale of securities that has not settled yet, to purchase the XYZ stock, the investor cannot not sell the XYZ stock prior to Wednesday without adding additional cash to the account to cover the purchase price of the XYZ stock. Since the investor sold the XYZ stock on Tuesday without adding any additional cash to the account, the investor’s actions constitute freeriding.

“Freeriding” is not permitted under Regulation T, and may require the investor’s broker to [“freeze”](#) the investor’s account for 90 days. During this 90-day period, an investor may still purchase securities with the cash account, but the investor must fully pay for any purchase on the date of the trade. An investor may avoid having a “freeze” placed on his cash account by fully paying for the securities by the settlement date with funds that do not come from the sale of the securities.