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SECURITIES AND EXCHANGE COMMISSION  
WASHINGTON, D.C. 20549  
Form 19b-4

File No. \* SR 2022 - \* 007

Amendment No. (req. for Amendments \*)

Filing by Financial Industry Regulatory Authority

Pursuant to Rule 19b-4 under the Securities Exchange Act of 1934

Initial \*

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Amendment \*

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Withdrawal

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Section 19(b)(2) \*

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Section 19(b)(3)(A) \*

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Section 19(b)(3)(B) \*

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Pilot

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Extension of Time Period for  
Commission Action \*

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Date Expires \*

Rule

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19b-4(f)(1)

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19b-4(f)(4)

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19b-4(f)(2)

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19b-4(f)(5)

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19b-4(f)(3)

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19b-4(f)(6)

Notice of proposed change pursuant to the Payment, Clearing, and Settlement Act of 2010

Section 806(e)(1) \*

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Section 806(e)(2) \*

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Security-Based Swap Submission pursuant to the  
Securities Exchange Act of 1934

Section 3C(b)(2) \*

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Exhibit 2 Sent As Paper Document

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Exhibit 3 Sent As Paper Document

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## Description

Provide a brief description of the action (limit 250 characters, required when Initial is checked \*).

Proposed Rule Change to Amend FINRA Rule 2360 (Options) to Increase the Position and Exercise Limits for Conventional Options on certain Exchange-Traded Funds

## Contact Information

Provide the name, telephone number, and e-mail address of the person on the staff of the self-regulatory organization prepared to respond to questions and comments on the action.

First Name \*

Faisal

Last Name \*

Sheikh

Title \*

Principal Counsel

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## Signature

Pursuant to the requirements of the Securities Exchange of 1934, Financial Industry Regulatory Authority has duty caused this filing to be signed on its behalf by the undersigned thereunto duty authorized.

Date

03/29/2022

(Title \*)

By

Racquel Russell

(Name \*)

Senior Vice President and Director of Capital M

Racquel  
Russell

Digitally signed by Racquel  
Russell  
Date: 2022.03.29 12:40:06  
-04'00'

NOTE: Clicking the signature block at right will initiate digitally signing the form. A digital signature is as legally binding as a physical signature, and once signed, this form cannot be changed.

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SECURITIES AND EXCHANGE COMMISSION  
WASHINGTON, D.C. 20549

For complete Form 19b-4 instructions please refer to the EDFS website.

**Form 19b-4 Information \***

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FINRA-2022-007 19b-4.docx

The self-regulatory organization must provide all required information, presented in a clear and comprehensible manner, to enable the public to provide meaningful comment on the proposal and for the Commission to determine whether the proposal is consistent with the Act and applicable rules and regulations under the Act.

**Exhibit 1 - Notice of Proposed Rule Change \***

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FINRA-2022-007 Exhibit 1.docx

The Notice section of this Form 19b-4 must comply with the guidelines for publication in the Federal Register as well as any requirements for electronic filing as published by the Commission (if applicable). The Office of the Federal Register (OFR) offers guidance on Federal Register publication requirements in the Federal Register Document Drafting Handbook, October 1998 Revision. For example, all references to the federal securities laws must include the corresponding cite to the United States Code in a footnote. All references to SEC rules must include the corresponding cite to the Code of Federal Regulations in a footnote. All references to Securities Exchange Act Releases must include the release number, release date, Federal Register cite, Federal Register date, and corresponding file number (e.g., SR-[SRO]-xx-xx). A material failure to comply with these guidelines will result in the proposed rule change being deemed not properly filed. See also Rule 0-3 under the Act (17 CFR 240.0-3)

**Exhibit 1A - Notice of Proposed Rule Change, Security-Based Swap Submission, or Advanced Notice by Clearing Agencies \***

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The Notice section of this Form 19b-4 must comply with the guidelines for publication in the Federal Register as well as any requirements for electronic filing as published by the Commission (if applicable). The Office of the Federal Register (OFR) offers guidance on Federal Register publication requirements in the Federal Register Document Drafting Handbook, October 1998 Revision. For example, all references to the federal securities laws must include the corresponding cite to the United States Code in a footnote. All references to SEC rules must include the corresponding cite to the Code of Federal Regulations in a footnote. All references to Securities Exchange Act Releases must include the release number, release date, Federal Register cite, Federal Register date, and corresponding file number (e.g., SR-[SRO]-xx-xx). A material failure to comply with these guidelines will result in the proposed rule change being deemed not properly filed. See also Rule 0-3 under the Act (17 CFR 240.0-3)

**Exhibit 2- Notices, Written Comments, Transcripts, Other Communications**

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Copies of notices, written comments, transcripts, other communications. If such documents cannot be filed electronically in accordance with Instruction F, they shall be filed in accordance with Instruction G.

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Exhibit Sent As Paper Document

**Exhibit 3 - Form, Report, or Questionnaire**

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Copies of any form, report, or questionnaire that the self-regulatory organization proposes to use to help implement or operate the proposed rule change, or that is referred to by the proposed rule change.

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Exhibit Sent As Paper Document

**Exhibit 4 - Marked Copies**

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The full text shall be marked, in any convenient manner, to indicate additions to and deletions from the immediately preceding filing. The purpose of Exhibit 4 is to permit the staff to identify immediately the changes made from the text of the rule with which it has been working.

**Exhibit 5 - Proposed Rule Text**

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FINRA-2022-007 Exhibit 5.docx

The self-regulatory organization may choose to attach as Exhibit 5 proposed changes to rule text in place of providing it in Item I and which may otherwise be more easily readable if provided separately from Form 19b-4. Exhibit 5 shall be considered part of the proposed rule change

**Partial Amendment**

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If the self-regulatory organization is amending only part of the text of a lengthy proposed rule change, it may, with the Commission's permission, file only those portions of the text of the proposed rule change in which changes are being made if the filing (i.e. partial amendment) is clearly understandable on its face. Such partial amendment shall be clearly identified and marked to show deletions and additions.

**1. Text of the Proposed Rule Change**

(a) Pursuant to the provisions of Section 19(b)(1) of the Securities Exchange Act of 1934 (“Act” or “Exchange Act”),<sup>1</sup> the Financial Industry Regulatory Authority, Inc. (“FINRA”) is filing with the Securities and Exchange Commission (“SEC” or “Commission”) a proposed rule change to amend Rule 2360 (Options) to increase the position and exercise limits for conventional options on certain exchange-traded funds (“ETFs”).<sup>2</sup>

The text of the proposed rule change is attached as Exhibit 5.

(b) Not applicable.

(c) Not applicable.

**2. Procedures of the Self-Regulatory Organization**

The Chief Legal Officer of FINRA authorized the filing of the proposed rule change with the SEC pursuant to delegated authority. No other action by FINRA is necessary for the filing of the proposed rule change.

FINRA has filed the proposed rule change for immediate effectiveness and has requested that the SEC waive the requirement that the proposed rule change not become operative for 30 days after the date of the filing, so FINRA can implement the proposed rule change immediately.

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<sup>1</sup> 15 U.S.C. 78s(b)(1).

<sup>2</sup> Rule 2360(b)(4) sets forth exercise limits through incorporating by reference options position limits under the rule. Accordingly, although the proposed rule change would not amend the text of Rule 2360(b)(4), the proposed rule change also would correspondingly raise exercise limits on the option.

**3. Self-Regulatory Organization's Statement of the Purpose of, and Statutory Basis for, the Proposed Rule Change**

(a) Purpose

FINRA Rule 2360(b)(3)(A) imposes a position limit on the number of equity options contracts in each class on the same side of the market that can be held or written by a member, a person associated with a member, or a customer or a group of customers acting in concert. Position limits are intended to prevent the establishment of options positions that can be used to manipulate or disrupt the underlying market or might create incentives to manipulate or disrupt the underlying market so as to benefit the options position. In addition, position limits serve to reduce the potential for disruption of the options market itself, especially in illiquid options classes.<sup>3</sup> This consideration has been balanced by the concern that the limits “not be established at levels that are so low as to discourage participation in the options market by institutions and other investors with substantial hedging needs or to prevent specialists and market makers from adequately meeting their obligations to maintain a fair and orderly market.”<sup>4</sup>

Rule 2360(b)(3)(A)(i) does not independently establish a position limit for standardized equity options. Rather, the position limit established by the rules of an options exchange for a particular equity option is the applicable position limit for purposes of Rule 2360.<sup>5</sup> Rule 2360(b)(3)(A)(iii) provides that conventional equity

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<sup>3</sup> See Securities Exchange Act Release No. 40969 (January 22, 1999), 64 FR 4911, 4912-13 (February 1, 1999) (Order Approving File No. SR-CBOE-98-23) (citing H.R. No. IFC-3, 96<sup>th</sup> Cong., 1<sup>st</sup> Sess. at 189-91 (Comm. Print 1978)).

<sup>4</sup> See supra note 3, at 4913.

<sup>5</sup> See e.g., Cboe Rule 8.30; ISE Options 9 Section 13; Nasdaq PHLX Options 9 Section 13; NYSE American Rule 904; NYSE Arca Rule 6.8-0; MIAX Rule 307;

options<sup>6</sup> are subject to a basic position limit of 25,000 contracts or a higher tier for conventional option contracts on securities that underlie exchange-traded options qualifying for such higher tier as determined by the rules of the options exchanges. In addition, FINRA lists position limits for options on securities that have higher position limits – currently, only the ETFs listed in Rule 2360(b)(3)(A)(iii)a.6. – that also generally mirror the options exchange position limits. At this time, FINRA proposes to conform its conventional options position limits to the Cboe Exchange, Inc.’s (“Cboe”) recent amendments that increased the position limit options due to an ongoing increase in demand in options on the following ETFs: (1) iShares iBoxx \$ Investment Grade Corporate Bond ETF (“LQD”), and (2) VanEck Vectors Gold Miners ETF (“GDX”) (together, the “Underlying ETFs”).<sup>7</sup>

The proposed rule change would add to the table provided in Rule 2360(b)(3)(A)(iii)a.6. as follows, with the effect of each ETF being increased from the current position limit of 250,000 contracts:

- The position limit for options on LQD would be increased to 500,000 contracts.
- The position limit for options on GDX would be increased to 500,000 contracts.

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BOX Rule 3120 and IM-3120-2; Nasdaq Options 9 Section 13; BX Options 9 Section 13; and BZX Rule 18.7.

<sup>6</sup> Conventional options are over-the-counter options and are defined in Rule 2360(a)(9) as “(A) any option contract not issued, or subject to issuance, by The Options Clearing Corporation; or (B) an OCC Cleared OTC Option.”

<sup>7</sup> See Securities Exchange Act Release No. 93525 (November 4, 2021), 86 FR 62584 (November 10, 2021) (Order Approving File No. SR-CBOE-2021-029).

FINRA notes the proposed position limits for options on LQD and GDX are consistent with current position limits for options on the iShares MSCI Brazil Capped ETF (“EWZ”), iShares 20+Year Treasury Bond Fund ETF (“TLT”), iShares MSCI Japan ETF (“EWJ”), and iShares iBoxx High Yield Corporate Bond Fund (“HYG”).

In support of the proposed rule change, as noted by Cboe, position limits are determined by the option exchange’s rules.<sup>8</sup> The ETFs that underlie options subject to the proposed rule change are highly liquid and are based on a broad set of highly liquid securities and other reference assets. The above listed ETFs are listed on various national securities exchanges and meet their listing standards.

In supporting the proposed position limit increases, FINRA considered the liquidity of the Underlying ETFs, the value of the underlying securities or index components and relevant marketplace, the share and option volume for the Underlying ETFs, and, where applicable, the availability or comparison of economically equivalent products to options on the Underlying ETFs.

FINRA notes that Cboe has compiled the following trading statistics regarding shares of and options on the Underlying ETFs and the values of the Underlying ETFs and their component securities or index components, as applicable:

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<sup>8</sup> See e.g., CBOE Rule 8.30, Interpretation and Policy .02.

Product	ADV <sup>9</sup> (ETF shares millions)	ADV (option contracts)	Shares Outstanding <sup>10</sup> (millions)	Fund Market Capitalization <sup>11</sup> (USD millions)	Share Value <sup>12</sup> (USD)
LQD	14.1	30,300	308.1	54,113.7	130.13 (NAV)
GDX	39.4	166,000	419.8	16,170.5	33.80 (NAV)

FINRA notes Cboe collected the same trading statistics, where applicable, as above regarding a sample of other ETFs, as well as the current position limits for options on such ETFs, to draw comparisons in support of proposed position limit increases for options on the Underlying ETFs (see further discussion below):

Product	ADV (ETF shares millions)	ADV (option contracts)	Shares Outstanding (millions)	Fund Market Capitalizat ion (USD millions)	Share Value (USD)	Current Position Limit
EWZ	29.2	139,400	173.8	6,506.8	33.71 (NAV)	500,000
TLT	11.5	111,800	103.7	17,121.3	136.85 (NAV)	500,000
EWJ	8.2	15,500	185.3	13,860.7	69.72 (NAV)	500,000
HYG	30.5	261,600	254.5	24,067.5	86.86 (NAV)	500,000

<sup>9</sup> Average daily volume (ADV) data for ETF shares and option contracts, as well as for ETF shares and options on the comparative ETFs presented below, are for all of 2020. Additionally, reference to ADV in ETF shares and ETF options, and indexes herein this proposal are for all of calendar year 2020, unless otherwise indicated.

<sup>10</sup> Shares Outstanding and Net Asset Values (“NAV”), as well as for the comparative ETFs presented below, are as of April 5, 2021.

<sup>11</sup> Fund Market Capitalization data, as well as for the comparative ETFs presented below, are as of January 14, 2021.

<sup>12</sup> See supra note 10.

FINRA echoes the Cboe's belief that, overall, the liquidity in the shares of the Underlying ETFs and in their overlying options, the larger market capitalizations for each of the Underlying ETFs, and the overall market landscape relevant to each of the Underlying ETFs support the proposal to increase the position limits for each option class. Given the robust liquidity in and value of the Underlying ETFs and their component securities, FINRA does not anticipate that the proposed increase in position limits would create significant price movements as the relevant markets are large enough to adequately absorb potential price movements that may be caused by larger trades.

The following analyses for the Underlying ETFs, which FINRA agrees with in support of the proposed rule change, as well as the statistics presented in support thereof, were presented by Cboe in their rule filing, which was approved by the Commission.

LQD tracks the performance of the Markit iBoxx USD Liquid Investment Grade ("IBOXIG") Index, which is an index designed as a subset of the broader U.S. dollar-denominated corporate bond market which can be used as a basis for tradable products, such as ETFs, and is comprised of over 8,000 bonds.<sup>13</sup> From 2019 through 2020, ADV has grown significantly in shares of LQD and in options on LQD, from approximately 9.7 million shares in 2019 to 14.1 million through 2020, and from approximately 8,200 option contracts in 2019 to 30,300 through 2020. LQD also continued to experience significant growth in ADV in the first quarter of 2021 with an ADV of approximately 140,200 option contracts. Further, LQD generally experiences higher ADV in shares

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<sup>13</sup> See Markit iBoxx USD Liquid Investment Grade Index, available at <https://cdn.ihsmarkit.com/www/pdf/MKT-iBoxx-USD-Liquid-Investment-Grade-Index-factsheet.pdf> (March 3, 2021).

than both TLT (11.5 million shares) and EWJ (8.2 million shares) and almost double the ADV in option contracts than EWJ (15,500 option contracts). Options on each EWZ, TLT and EWJ are currently subject to a position limit of 500,000 contracts—the proposed limit for options on LQD. The NAV of LQD is also higher than, or comparable to, that of the NAV of the ETFs underlying the options that are currently subject to a position limit of 500,000 option contracts (as presented in the table above), which is indicative that the total value of its underlying components is generally higher or comparable. Per the tables above, LQD’s total market capitalization of approximately \$54.1 billion is also higher than or comparable to the total market capitalization of the ETFs underlying the options currently subject to a position limit of 500,000 contracts. In addition to this, although there are currently no options listed for trading on the IBXIG Index, the components<sup>14</sup> of the IBXIG Index, which can be used in creating a basket of securities that equate to the LQD ETF, are made up of over 8,000 bonds for which the outstanding face value of each must be greater than or equal to \$2 billion.<sup>15</sup> FINRA echoes Cboe’s belief that the total value of the bonds in the IBXIG Index, coupled with LQD’s share and option volume, total market capitalization, and NAV price indicates that the market is large enough to absorb potential price movements caused by a large trade in LQD. Also, as evidenced above, trading volume in LQD shares has increased over the past few years and market participants’ need for options have continued to grow alongside the ETF. Particularly, Cboe notes in its filing that in the last year, market

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<sup>14</sup> Investment grade corporate bonds.

<sup>15</sup> See supra note 13.

participants have sought more cost-effective hedging strategies through the use of LQD options as a result of the borrow on other fixed income ETFs, such as HYG. Therefore, FINRA agrees with Cboe's belief that because LQD options are being increasingly utilized as an alternative to similar products, such as HYG options, then it is appropriate that options on LQD be subject to the same 500,000 contract position limit that currently exists for options on HYG.

GDX seeks to replicate as closely as possible the price and yield performance of the NYSE Arca Gold Miners ("GDMNTR") Index, which is intended to track the overall performance of companies involved in the gold mining industry.<sup>16</sup> ADV in GDX options has increased from 2019 through 2020, with an ADV of approximately 117,400 option contracts in 2019 to an ADV of approximately 166,000 option contracts in 2020.

ADV in GDX shares did not increase from 2019 to 2020. GDX options also experienced an ADV of approximately 287,800 option contracts in the first quarter of 2021. The ADV in GDX shares (39.4 million) and options on GDX (166,000 option contracts) are greater than the ADV in EWZ (29.2 million shares and 139,300 option contracts), TLT (11.5 million shares and 111,800 option contracts), EWJ (8.2 million shares and 15,500 option contracts) and HYG (30.5 million shares and 261,600 option contracts), each of which is currently subject to a position limit of 500,000 option contracts – the proposed limit for options on GDX. GDX also experiences a comparable, or higher, market capitalization (approximately \$16.2 billion) than EWZ, TLT and EWJ. Cboe noted that many of the Brazil-based gold mining constituents included in GDX are also included in

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<sup>16</sup> See VanEck Vectors Gold Miners ETF, available at <https://www.vaneck.com/library/vaneck-vectors-etfs/gdx-fact-sheet-pdf> (February 28, 2022).

EWZ, which tracks the investment results of an index composed of Brazilian equities, and that there have been no identified issues with the continued listing and trading of EWZ options or any adverse market impact on EWZ in connection with the current 500,000 position limit in place for EWZ options. Additionally, like that of LDQ above, there is currently no index option analogue for the GDX ETF on the GDMNTR Index approved for options trading, however, the components of the GDMNTR Index, which can be used to create the GDX ETF, currently must each have a market capitalization greater than \$750 million, an ADV of at least 50,000 shares, and an average daily value traded of at least \$1 million in order to be eligible for inclusion in the GDMNTR Index. FINRA echoes Cboe's belief that the GDMNTR Index component inclusion requirements, as well as GDX's share and option volume and total market capitalization, indicate that the GDX market is sufficiently large and liquid enough to absorb price movements as a result of potentially oversized trades.

FINRA believes that increasing the position limits for conventional options subject to the proposed rule change would lead to a more liquid and competitive market for these options, which will benefit customers interested in these products.

#### Creation and Redemption for ETFs

FINRA believes that the creation and redemption process for ETFs subject to this proposed rule change will lessen the potential for manipulative activity with options on the Underlying ETFs. Regarding ETFs, when an ETF provider wants to create more shares, it looks to an Authorized Participant (generally a market maker or other large financial institution) to acquire the securities the ETF is to hold. For instance, when an ETF is designed to track the performance of an index, the Authorized Participant can

purchase all the constituent securities in the exact same weight as the index, then deliver those shares to the ETF provider. In exchange, the ETF provider gives the Authorized Participant a block of equally valued ETF shares, on a one-for-one fair value basis. The price is based on the net asset value, not the market value at which the ETF is trading. The creation of new ETF units can be conducted during an entire trading day, and is not subject to position limits. This process works in reverse where the ETF provider seeks to decrease the number of shares that are available to trade. The applicable creation and redemption processes for the Underlying ETFs creates a direct link to the underlying components of the ETF and serves to mitigate potential price impact of the ETF shares that might otherwise result from increased position limits for the options on the Underlying ETFs.

FINRA understands that the ETF creation and redemption process seeks to keep an ETF's share price trading in line with the product's underlying net asset value. Because an ETF trades like a stock, its share price will fluctuate during the trading day, due to simple supply and demand. If demand to buy an ETF is high, for instance, the ETF's share price might rise above the value of its underlying securities. When this happens, the Authorized Participant or issuer believes the ETF may now be overpriced, so it may buy shares of the component securities and then sell ETF shares in the open market. This may drive the ETF's share price back toward the underlying net asset value or indicative index value. Likewise, if the ETF share price starts trading at a discount to the securities it holds or its index components, the Authorized Participant or issuer can buy shares of the ETF and redeem them for the underlying securities or index component instruments. Buying undervalued ETF shares may drive the share price of the ETF back

toward fair value. This arbitrage process helps to keep an ETF's share price in line with the value of its underlying portfolio or index components.

#### Surveillance and Reporting

FINRA believes that the increased position limits provisions are appropriate in light of the existing surveillance procedures and reporting requirements at FINRA,<sup>17</sup> the options exchanges, and at the several clearing firms, which are capable of properly identifying unusual or illegal trading activity. These procedures use daily monitoring of market movements by automated surveillance techniques to identify unusual activity in both options and underlying stocks.<sup>18</sup>

In addition, large stock holdings must be disclosed to the Commission by way of Schedules 13D or 13G.<sup>19</sup> Options positions are part of any reportable positions and cannot legally be hidden. Moreover, the previously noted Rule 2360(b)(5) requirement that members must file reports with FINRA for any customer that held aggregate large long or short positions of any single class for the previous day will continue to serve as an important part of FINRA's surveillance efforts.

Finally, FINRA believes that the current financial requirements imposed by FINRA and by the Commission adequately address financial responsibility concerns that a member or its customer will maintain an inordinately large unhedged position in any option with a higher position limit. Current margin and risk-based haircut methodologies

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<sup>17</sup> See Rule 2360(b)(5) for the options reporting requirements.

<sup>18</sup> These procedures have been effective for the surveillance of options trading and will continue to be employed.

<sup>19</sup> 17 CFR 240.13d-1.

serve to limit the size of positions maintained by any one account by increasing the margin or capital that a member must maintain for a large position. Under Rule 4210(f)(8)(A), FINRA also may impose a higher margin requirement upon a member when FINRA determines a higher requirement is warranted. In addition, the Commission's net capital rule<sup>20</sup> imposes a capital charge on members to the extent of any margin deficiency resulting from the higher margin requirement.

As noted in Item 2 of this filing, FINRA has filed the proposed rule change for immediate effectiveness and has requested that the SEC waive the requirement that the proposed rule change not become operative for 30 days after the date of the filing, so FINRA can implement the proposed rule change immediately.

(b) Statutory Basis

FINRA believes that the proposed rule change is consistent with the provisions of Section 15A(b)(6) of the Act,<sup>21</sup> which requires, among other things, that FINRA rules must be designed to prevent fraudulent and manipulative acts and practices, to promote just and equitable principles of trade, and, in general, to protect investors and the public interest. FINRA believes that the proposed rule change promotes consistent regulation by harmonizing position limits with those of the other self-regulatory organizations. FINRA further believes that increasing the position limit on conventional options promotes consistent regulation by harmonizing the position limit with its standardized counterpart. In addition, FINRA believes the proposed rule change will be beneficial to large market makers and institutions (which generally have the greatest ability to provide

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<sup>20</sup> 17 CFR 240.15c3-1.

<sup>21</sup> 15 U.S.C. 78o-3(b)(6).

liquidity and depth in products that may be subject to higher position limits as has been the case with recently approved increased position limits),<sup>22</sup> as well as retail traders and public customers, by providing them with a more effective trading and hedging vehicle.

In addition, FINRA believes that the structure of the Underlying ETFs, the considerable market capitalization of the funds, underlying component securities and indexed component securities, and the liquidity of the markets for the applicable options and underlying component securities will mitigate concerns regarding potential manipulation of the products or disruption of the underlying markets upon increasing the relevant position limits. As a general principle, increases in market capitalizations, active trading volume, and deep liquidity of securities tend to deter manipulation or disruption. This general principle applies to the recently observed increased levels of market capitalization, trading volume, and liquidity in shares of and options on the Underlying ETFs (as described above). FINRA does not believe that the options markets or underlying markets would become susceptible to manipulation or disruption as a result of the proposed position limit increases.

Increased position limits for select actively traded options, such as those proposed herein, are not novel and have been previously approved by the Commission.<sup>23</sup>

Furthermore, FINRA notes that the proposed position limits for options on LQD and

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<sup>22</sup> See supra note 7.

<sup>23</sup> See supra note 7. See also Securities Exchange Act Release Nos. 88768 (April 29, 2020), 85 FR 26736 (May 5, 2020) (Order Approving File No. SR-CBOE-2020-015); 83415 (June 12, 2018), 83 FR 28274 (June 18, 2018) (Notice of Filing and Immediate Effectiveness of File No. SR-CBOE-2018-042); and 68086 (October 23, 2012), 77 FR 65600 (October 29, 2012) (Order Approving File No. SR-CBOE-2012-066).

GDX are consistent with existing position limits for options on comparable ETFs in Rule 2360(b)(3)(A)(iii)a.6.

FINRA's existing surveillance and reporting safeguards are designed to deter and detect possible manipulative behavior that might arise from changing position and exercise limits.

#### **4. Self-Regulatory Organization's Statement on Burden on Competition**

FINRA does not believe that the proposed rule change will result in any burden on competition that is not necessary or appropriate in furtherance of the purposes of the Act.

#### **Economic Impact Analysis**

FINRA has undertaken an economic impact assessment, as set forth below, to analyze the potential economic impacts, including anticipated costs, benefits, and distributional and competitive effects, transfers of wealth, relative to the current baseline, and the alternatives FINRA considered in assessing how to best meet its regulatory objectives.

#### **Regulatory Objective**

FINRA is proposing to amend Rule 2360 to harmonize FINRA's position limits for conventional options with the position limit for standardized options.<sup>24</sup>

#### **Economic Baseline**

Per FINRA Rule 2360(b)(3)(A)(iii) conventional equity options are subject to a basic position limit of 25,000 contracts or higher for conventional option contracts on

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<sup>24</sup> See supra note 7.

securities that underlie exchange-traded options qualifying for a higher tier as determined by option exchange rules. The existing position limits for conventional options on LQD and GDX are 250,000 contracts. Cboe has recently increased position limits for options on these ETFs.

#### Economic Impact

##### Benefits

As noted above, the proposed rule change would amend Rule 2360 to harmonize FINRA's position limits for conventional options with the position limits for standardized options.<sup>25</sup> If the existing position limits for conventional equity options on select ETFs constrains trading in these ETFs, then investors may be able to better manage risk and trade on information when the position limit is relaxed. In general, the improvement in risk management and informational efficiency may increase more when position limits are increased. We acknowledge, however, that the conventional options on these ETFs, the ETFs themselves, and the securities underlying these ETFs are liquid, so improvements in informational efficiency may be relatively small.

For investors that trade conventional equity options, there is likely to be a natural size for an executed order that minimizes fixed and variable transaction costs, including but not limited to, the bid-ask spread, price impact, and transaction fees. If the existing position limits for conventional equity options on select ETFs constrains the order size such that fixed and variable transaction costs are higher than optimal, then investors may benefit if the new position limit is no less than the natural size. In such an event, the cost to hedge an ETF would decline, thereby making it less costly to manage downside risk.

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<sup>25</sup>

See supra note 7.

In addition, if the existing position limits serve as a constraint, then an increase in the position limits for conventional options on select ETFs could permit investors to more easily find a counterparty. If the number of counterparties increases, then the cost of hedging should decline as the half-spread narrows, thereby making it less expensive to manage downside risk.

The extent of the constraint imposed by the current limit on conventional options is related to the ability of an investor to achieve similar economic exposure through other means. If there are other securities, such as an option on a closely related index, that exist and provide similar economic exposure less expensively, then the value of lessening the position limits on conventional options on ETFs is lower.

Members may rely on information and data feeds from the Options Clearing Corporation to assist in their monitoring position limits. Because position limits on the standardized and conventional side have traditionally been consistent, members have relied on this feed for both standardized and conventional options. If the position limits between standardized and conventional options are conformed, then the cost from monitoring position limits should decline for member firms. Having the same position limits on standardized and conventional options, reduces the potential for excess loss that may be incurred when different limits are applied to the standardized versus conventional options on the same ETF. The economic loss may arise from building and maintaining trading and compliance systems to support the different regimes. Furthermore, the harmonization of position limits on standardized and conventional options eliminates the potential risk and cost arising from regulatory arbitrage.

### Costs

The proposed rule change may impose limited operational cost on member firms that trade conventional options on ETFs, as these same firms would need to revise position limits that are used in trading systems. However, the proposed rule change should not impose additional costs, because it is difficult to disrupt or manipulate the underlying market, create an incentive to disrupt or manipulate the underlying market for the purpose of profiting from the options position, or disrupt or manipulate the options market for conventional options on ETFs affected by this proposed rule. ETFs that underlie options subject to the proposed rule change are highly liquid and are based on a broad set of highly liquid securities, which makes the market difficult to manipulate or disrupt. In fact, options on certain broad-based security indexes have no position limits. Furthermore, the applicable creation and redemption process for these ETFs reduces the potential for disruptive or manipulative activity. New ETF units may be created at any time during the trading day and are not subject to position limits. Consequently, there is a direct link between the underlying components of the ETF, which keeps ETF's share prices trading in line with the ETF's underlying net asset value.

### Alternatives

No further alternatives are under consideration.

5. **Self-Regulatory Organization's Statement on Comments on the Proposed Rule Change Received from Members, Participants, or Others**

Written comments were neither solicited nor received.

6. **Extension of Time Period for Commission Action**

Not applicable.

**7. Basis for Summary Effectiveness Pursuant to Section 19(b)(3) or for Accelerated Effectiveness Pursuant to Section 19(b)(2) or Section 19(b)(7)(D)**

The proposed rule change is effective upon filing pursuant to Section 19(b)(3) of the Act<sup>26</sup> and paragraph (f)(6) of Rule 19b-4 thereunder,<sup>27</sup> in that the proposed rule change does not significantly affect the protection of investors or the public interest; does not impose any significant burden on competition; and does not become operative for 30 days after filing or such shorter time as the Commission may designate. The proposed rule change is based on the Cboe rule as noted in Item 8 below, and thus would ensure consistent regulation with respect to position limits (and exercise limits)<sup>28</sup> for ETF options noted above as such may be established by an options exchange as approved by the SEC for the protection of investors and the public interest.

FINRA requests that the Commission waive the requirement that the rule change, by its terms, not become operative for 30 days after the date of the filing as set forth in Rule 19b-4(f)(6)(iii),<sup>29</sup> so FINRA may immediately harmonize position limits with those of other self-regulatory organizations to ensure consistent regulation for the protection of investors and the public interest. In accordance with Rule 19b-4(f)(6),<sup>30</sup> FINRA submitted written notice of its intent to file the proposed rule change, along with a brief

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<sup>26</sup> 15 U.S.C. 78s(b)(3).

<sup>27</sup> 17 CFR 240.19b-4(f)(6).

<sup>28</sup> See *supra* note 7. Rule 2360(b)(4) sets forth exercise limits through incorporating by reference options position limits under the rule. Accordingly, although the proposed rule change would not amend the text of Rule 2360(b)(4), the proposed rule change also would correspondingly raise exercise limits on the option.

<sup>29</sup> 17 CFR 240.19b-4(f)(6)(iii).

<sup>30</sup> 17 CFR 240.19b-4(f)(6).

description and text of the proposed rule change, at least five business days prior to the date of filing, or such shorter time as the Commission may designate, as specified in Rule 19b-4(f)(6)(iii) under the Act.<sup>31</sup>

**8. Proposed Rule Change Based on Rules of Another Self-Regulatory Organization or of the Commission**

See Cboe Rule 8.30.

**9. Security-Based Swap Submissions Filed Pursuant to Section 3C of the Act**

Not applicable.

**10. Advance Notices Filed Pursuant to Section 806(e) of the Payment, Clearing and Settlement Supervision Act**

Not applicable.

**11. Exhibits**

Exhibit 1. Completed notice of proposed rule change for publication in the Federal Register.

Exhibit 5. Text of the proposed rule change

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<sup>31</sup> 17 CFR 240.19b-4(f)(6)(iii).

EXHIBIT 1

SECURITIES AND EXCHANGE COMMISSION  
(Release No. 34- ; File No. SR-FINRA-2022-007)

Self-Regulatory Organizations; Financial Industry Regulatory Authority, Inc.; Notice of Filing and Immediate Effectiveness of a Proposed Rule Change to Amend FINRA Rule 2360 (Options) to Increase the Position and Exercise Limits for Conventional Options on certain Exchange-Traded Funds

Pursuant to Section 19(b)(1) of the Securities Exchange Act of 1934 (“Act”)<sup>1</sup> and Rule 19b-4 thereunder,<sup>2</sup> notice is hereby given that on , the Financial Industry Regulatory Authority, Inc. (“FINRA”) filed with the Securities and Exchange Commission (“SEC” or “Commission”) the proposed rule change as described in Items I, II, and III below, which Items have been prepared by FINRA. FINRA has designated the proposed rule change as constituting a “non-controversial” rule change under paragraph (f)(6) of Rule 19b-4 under the Act,<sup>3</sup> which renders the proposal effective upon receipt of this filing by the Commission. The Commission is publishing this notice to solicit comments on the proposed rule change from interested persons.

I. Self-Regulatory Organization’s Statement of the Terms of Substance of the Proposed Rule Change

FINRA is proposing to amend Rule 2360 (Options) to increase the position and exercise limits for conventional options on certain exchange-traded funds (“ETFs”).

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<sup>1</sup> 15 U.S.C. 78s(b)(1).

<sup>2</sup> 17 CFR 240.19b-4.

<sup>3</sup> 17 CFR 240.19b-4(f)(6).

The text of the proposed rule change is available on FINRA's website at <http://www.finra.org>, at the principal office of FINRA and at the Commission's Public Reference Room.

II. Self-Regulatory Organization's Statement of the Purpose of, and Statutory Basis for, the Proposed Rule Change

In its filing with the Commission, FINRA included statements concerning the purpose of and basis for the proposed rule change and discussed any comments it received on the proposed rule change. The text of these statements may be examined at the places specified in Item IV below. FINRA has prepared summaries, set forth in sections A, B, and C below, of the most significant aspects of such statements.

A. Self-Regulatory Organization's Statement of the Purpose of, and Statutory Basis for, the Proposed Rule Change

1. Purpose

FINRA Rule 2360(b)(3)(A) imposes a position limit on the number of equity options contracts in each class on the same side of the market that can be held or written by a member, a person associated with a member, or a customer or a group of customers acting in concert. Position limits are intended to prevent the establishment of options positions that can be used to manipulate or disrupt the underlying market or might create incentives to manipulate or disrupt the underlying market so as to benefit the options position. In addition, position limits serve to reduce the potential for disruption of the options market itself, especially in illiquid options classes.<sup>4</sup> This consideration has been balanced by the concern that the limits "not be established at levels that are so low as to

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<sup>4</sup> See Securities Exchange Act Release No. 40969 (January 22, 1999), 64 FR 4911, 4912-13 (February 1, 1999) (Order Approving File No. SR-CBOE-98-23) (citing H.R. No. IFC-3, 96<sup>th</sup> Cong., 1<sup>st</sup> Sess. at 189-91 (Comm. Print 1978)).

discourage participation in the options market by institutions and other investors with substantial hedging needs or to prevent specialists and market makers from adequately meeting their obligations to maintain a fair and orderly market.”<sup>5</sup>

Rule 2360(b)(3)(A)(i) does not independently establish a position limit for standardized equity options. Rather, the position limit established by the rules of an options exchange for a particular equity option is the applicable position limit for purposes of Rule 2360.<sup>6</sup> Rule 2360(b)(3)(A)(iii) provides that conventional equity options<sup>7</sup> are subject to a basic position limit of 25,000 contracts or a higher tier for conventional option contracts on securities that underlie exchange-traded options qualifying for such higher tier as determined by the rules of the options exchanges. In addition, FINRA lists position limits for options on securities that have higher position limits – currently, only the ETFs listed in Rule 2360(b)(3)(A)(iii)a.6. – that also generally mirror the options exchange position limits. At this time, FINRA proposes to conform its conventional options position limits to the Cboe Exchange, Inc.’s (“Cboe”) recent amendments that increased the position limit options due to an ongoing increase in demand in options on the following ETFs: (1) iShares iBoxx \$ Investment Grade

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<sup>5</sup> See supra note 4, at 4913.

<sup>6</sup> See e.g., Cboe Rule 8.30; ISE Options 9 Section 13; Nasdaq PHLX Options 9 Section 13; NYSE American Rule 904; NYSE Arca Rule 6.8-0; MIAX Rule 307; BOX Rule 3120 and IM-3120-2; Nasdaq Options 9 Section 13; BX Options 9 Section 13; and BZX Rule 18.7.

<sup>7</sup> Conventional options are over-the-counter options and are defined in Rule 2360(a)(9) as “(A) any option contract not issued, or subject to issuance, by The Options Clearing Corporation; or (B) an OCC Cleared OTC Option.”

Corporate Bond ETF (“LQD”), and (2) VanEck Vectors Gold Miners ETF (“GDX”) (together, the “Underlying ETFs”).<sup>8</sup>

The proposed rule change would add to the table provided in Rule 2360(b)(3)(A)(iii)a.6. as follows, with the effect of each ETF being increased from the current position limit of 250,000 contracts:

- The position limit for options on LQD would be increased to 500,000 contracts.
- The position limit for options on GDX would be increased to 500,000 contracts.

FINRA notes the proposed position limits for options on LQD and GDX are consistent with current position limits for options on the iShares MSCI Brazil Capped ETF (“EWZ”), iShares 20+Year Treasury Bond Fund ETF (“TLT”), iShares MSCI Japan ETF (“EWJ”), and iShares iBoxx High Yield Corporate Bond Fund (“HYG”).

In support of the proposed rule change, as noted by Cboe, position limits are determined by the option exchange’s rules.<sup>9</sup> The ETFs that underlie options subject to the proposed rule change are highly liquid and are based on a broad set of highly liquid securities and other reference assets. The above listed ETFs are listed on various national securities exchanges and meet their listing standards.

In supporting the proposed position limit increases, FINRA considered the liquidity of the Underlying ETFs, the value of the underlying securities or index components and relevant marketplace, the share and option volume for the Underlying

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<sup>8</sup> See Securities Exchange Act Release No. 93525 (November 4, 2021), 86 FR 62584 (November 10, 2021) (Order Approving File No. SR-CBOE-2021-029).

<sup>9</sup> See e.g., CBOE Rule 8.30, Interpretation and Policy .02.

ETFs, and, where applicable, the availability or comparison of economically equivalent products to options on the Underlying ETFs.

FINRA notes that Cboe has compiled the following trading statistics regarding shares of and options on the Underlying ETFs and the values of the Underlying ETFs and their component securities or index components, as applicable:

Product	ADV <sup>10</sup> (ETF shares millions)	ADV (option contracts)	Shares Outstanding <sup>11</sup> (millions)	Fund Market Capitalization <sup>12</sup> (USD millions)	Share Value <sup>13</sup> (USD)
LQD	14.1	30,300	308.1	54,113.7	130.13 (NAV)
GDX	39.4	166,000	419.8	16,170.5	33.80 (NAV)

FINRA notes Cboe collected the same trading statistics, where applicable, as above regarding a sample of other ETFs, as well as the current position limits for options on such ETFs, to draw comparisons in support of proposed position limit increases for options on the Underlying ETFs (see further discussion below):

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<sup>10</sup> Average daily volume (ADV) data for ETF shares and option contracts, as well as for ETF shares and options on the comparative ETFs presented below, are for all of 2020. Additionally, reference to ADV in ETF shares and ETF options, and indexes herein this proposal are for all of calendar year 2020, unless otherwise indicated.

<sup>11</sup> Shares Outstanding and Net Asset Values (“NAV”), as well as for the comparative ETFs presented below, are as of April 5, 2021.

<sup>12</sup> Fund Market Capitalization data, as well as for the comparative ETFs presented below, are as of January 14, 2021.

<sup>13</sup> See supra note 11.

Product	ADV (ETF shares millions)	ADV (option contracts)	Shares Outstanding (millions)	Fund Market Capitalizat ion (USD millions)	Share Value (USD)	Current Position Limit
EWZ	29.2	139,400	173.8	6,506.8	33.71 (NAV)	500,000
TLT	11.5	111,800	103.7	17,121.3	136.85 (NAV)	500,000
EWJ	8.2	15,500	185.3	13,860.7	69.72 (NAV)	500,000
HYG	30.5	261,600	254.5	24,067.5	86.86 (NAV)	500,000

FINRA echoes the Cboe's belief that, overall, the liquidity in the shares of the Underlying ETFs and in their overlying options, the larger market capitalizations for each of the Underlying ETFs, and the overall market landscape relevant to each of the Underlying ETFs support the proposal to increase the position limits for each option class. Given the robust liquidity in and value of the Underlying ETFs and their component securities, FINRA does not anticipate that the proposed increase in position limits would create significant price movements as the relevant markets are large enough to adequately absorb potential price movements that may be caused by larger trades.

The following analyses for the Underlying ETFs, which FINRA agrees with in support of the proposed rule change, as well as the statistics presented in support thereof, were presented by Cboe in their rule filing, which was approved by the Commission.

LQD tracks the performance of the Markit iBoxx USD Liquid Investment Grade ("IBOXIG") Index, which is an index designed as a subset of the broader U.S. dollar-denominated corporate bond market which can be used as a basis for tradable products,

such as ETFs, and is comprised of over 8,000 bonds.<sup>14</sup> From 2019 through 2020, ADV has grown significantly in shares of LQD and in options on LQD, from approximately 9.7 million shares in 2019 to 14.1 million through 2020, and from approximately 8,200 option contracts in 2019 to 30,300 through 2020. LQD also continued to experience significant growth in ADV in the first quarter of 2021 with an ADV of approximately 140,200 option contracts. Further, LQD generally experiences higher ADV in shares than both TLT (11.5 million shares) and EWJ (8.2 million shares) and almost double the ADV in option contracts than EWJ (15,500 option contracts). Options on each EWZ, TLT and EWJ are currently subject to a position limit of 500,000 contracts—the proposed limit for options on LQD. The NAV of LQD is also higher than, or comparable to, that of the NAV of the ETFs underlying the options that are currently subject to a position limit of 500,000 option contracts (as presented in the table above), which is indicative that the total value of its underlying components is generally higher or comparable. Per the tables above, LQD’s total market capitalization of approximately \$54.1 billion is also higher than or comparable to the total market capitalization of the ETFs underlying the options currently subject to a position limit of 500,000 contracts. In addition to this, although there are currently no options listed for trading on the IBOXIG Index, the components<sup>15</sup> of the IBXIG Index, which can be used in creating a basket of securities that equate to the LQD ETF, are made up of over 8,000 bonds for which the

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<sup>14</sup> See Markit iBoxx USD Liquid Investment Grade Index, available at <https://cdn.ihsmarkit.com/www/pdf/MKT-iBoxx-USD-Liquid-Investment-Grade-Index-factsheet.pdf> (March 3, 2021).

<sup>15</sup> Investment grade corporate bonds.

outstanding face value of each must be greater than or equal to \$2 billion.<sup>16</sup> FINRA echoes Cboe's belief that the total value of the bonds in the IBOXIG Index, coupled with LQD's share and option volume, total market capitalization, and NAV price indicates that the market is large enough to absorb potential price movements caused by a large trade in LQD. Also, as evidenced above, trading volume in LQD shares has increased over the past few years and market participants' need for options have continued to grow alongside the ETF. Particularly, Cboe notes in its filing that in the last year, market participants have sought more cost-effective hedging strategies through the use of LQD options as a result of the borrow on other fixed income ETFs, such as HYG. Therefore, FINRA agrees with Cboe's belief that because LQD options are being increasingly utilized as an alternative to similar products, such as HYG options, then it is appropriate that options on LQD be subject to the same 500,000 contract position limit that currently exists for options on HYG.

GDX seeks to replicate as closely as possible the price and yield performance of the NYSE Arca Gold Miners ("GDMNTR") Index, which is intended to track the overall performance of companies involved in the gold mining industry.<sup>17</sup> ADV in GDX options has increased from 2019 through 2020, with an ADV of approximately 117,400 option contracts in 2019 to an ADV of approximately 166,000 option contracts in 2020.

ADV in GDX shares did not increase from 2019 to 2020. GDX options also experienced an ADV of approximately 287,800 option contracts in the first quarter of 2021. The

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<sup>16</sup> See supra note 14.

<sup>17</sup> See VanEck Vectors Gold Miners ETF, available at <https://www.vaneck.com/library/vaneck-vectors-etfs/gdx-fact-sheet-pdf> (February 28, 2022).

ADV in GDX shares (39.4 million) and options on GDX (166,000 option contracts) are greater than the ADV in EWZ (29.2 million shares and 139,300 option contracts), TLT (11.5 million shares and 111,800 option contracts), EWJ (8.2 million shares and 15,500 option contracts) and HYG (30.5 million shares and 261,600 option contracts), each of which is currently subject to a position limit of 500,000 option contracts – the proposed limit for options on GDX. GDX also experiences a comparable, or higher, market capitalization (approximately \$16.2 billion) than EWZ, TLT and EWJ. Cboe noted that many of the Brazil-based gold mining constituents included in GDX are also included in EWZ, which tracks the investment results of an index composed of Brazilian equities, and that there have been no identified issues with the continued listing and trading of EWZ options or any adverse market impact on EWZ in connection with the current 500,000 position limit in place for EWZ options. Additionally, like that of LDQ above, there is currently no index option analogue for the GDX ETF on the GDMNTR Index approved for options trading, however, the components of the GDMNTR Index, which can be used to create the GDX ETF, currently must each have a market capitalization greater than \$750 million, an ADV of at least 50,000 shares, and an average daily value traded of at least \$1 million in order to be eligible for inclusion in the GDMNTR Index. FINRA echoes Cboe's belief that the GDMNTR Index component inclusion requirements, as well as GDX's share and option volume and total market capitalization, indicate that the GDX market is sufficiently large and liquid enough to absorb price movements as a result of potentially oversized trades.

FINRA believes that increasing the position limits for conventional options subject to the proposed rule change would lead to a more liquid and competitive market for these options, which will benefit customers interested in these products.

#### Creation and Redemption for ETFs

FINRA believes that the creation and redemption process for ETFs subject to this proposed rule change will lessen the potential for manipulative activity with options on the Underlying ETFs. Regarding ETFs, when an ETF provider wants to create more shares, it looks to an Authorized Participant (generally a market maker or other large financial institution) to acquire the securities the ETF is to hold. For instance, when an ETF is designed to track the performance of an index, the Authorized Participant can purchase all the constituent securities in the exact same weight as the index, then deliver those shares to the ETF provider. In exchange, the ETF provider gives the Authorized Participant a block of equally valued ETF shares, on a one-for-one fair value basis. The price is based on the net asset value, not the market value at which the ETF is trading. The creation of new ETF units can be conducted during an entire trading day, and is not subject to position limits. This process works in reverse where the ETF provider seeks to decrease the number of shares that are available to trade. The applicable creation and redemption processes for the Underlying ETFs creates a direct link to the underlying components of the ETF and serves to mitigate potential price impact of the ETF shares that might otherwise result from increased position limits for the options on the Underlying ETFs.

FINRA understands that the ETF creation and redemption process seeks to keep an ETF's share price trading in line with the product's underlying net asset value.

Because an ETF trades like a stock, its share price will fluctuate during the trading day, due to simple supply and demand. If demand to buy an ETF is high, for instance, the ETF's share price might rise above the value of its underlying securities. When this happens, the Authorized Participant or issuer believes the ETF may now be overpriced, so it may buy shares of the component securities and then sell ETF shares in the open market. This may drive the ETF's share price back toward the underlying net asset value or indicative index value. Likewise, if the ETF share price starts trading at a discount to the securities it holds or its index components, the Authorized Participant or issuer can buy shares of the ETF and redeem them for the underlying securities or index component instruments. Buying undervalued ETF shares may drive the share price of the ETF back toward fair value. This arbitrage process helps to keep an ETF's share price in line with the value of its underlying portfolio or index components.

#### Surveillance and Reporting

FINRA believes that the increased position limits provisions are appropriate in light of the existing surveillance procedures and reporting requirements at FINRA,<sup>18</sup> the options exchanges, and at the several clearing firms, which are capable of properly identifying unusual or illegal trading activity. These procedures use daily monitoring of market movements by automated surveillance techniques to identify unusual activity in both options and underlying stocks.<sup>19</sup>

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<sup>18</sup> See Rule 2360(b)(5) for the options reporting requirements.

<sup>19</sup> These procedures have been effective for the surveillance of options trading and will continue to be employed.

In addition, large stock holdings must be disclosed to the Commission by way of Schedules 13D or 13G.<sup>20</sup> Options positions are part of any reportable positions and cannot legally be hidden. Moreover, the previously noted Rule 2360(b)(5) requirement that members must file reports with FINRA for any customer that held aggregate large long or short positions of any single class for the previous day will continue to serve as an important part of FINRA's surveillance efforts.

Finally, FINRA believes that the current financial requirements imposed by FINRA and by the Commission adequately address financial responsibility concerns that a member or its customer will maintain an inordinately large unhedged position in any option with a higher position limit. Current margin and risk-based haircut methodologies serve to limit the size of positions maintained by any one account by increasing the margin or capital that a member must maintain for a large position. Under Rule 4210(f)(8)(A), FINRA also may impose a higher margin requirement upon a member when FINRA determines a higher requirement is warranted. In addition, the Commission's net capital rule<sup>21</sup> imposes a capital charge on members to the extent of any margin deficiency resulting from the higher margin requirement.

FINRA has filed the proposed rule change for immediate effectiveness and has requested that the SEC waive the requirement that the proposed rule change not become operative for 30 days after the date of the filing, so FINRA can implement the proposed rule change immediately.

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<sup>20</sup> 17 CFR 240.13d-1.

<sup>21</sup> 17 CFR 240.15c3-1.

2. Statutory Basis

FINRA believes that the proposed rule change is consistent with the provisions of Section 15A(b)(6) of the Act,<sup>22</sup> which requires, among other things, that FINRA rules must be designed to prevent fraudulent and manipulative acts and practices, to promote just and equitable principles of trade, and, in general, to protect investors and the public interest. FINRA believes that the proposed rule change promotes consistent regulation by harmonizing position limits with those of the other self-regulatory organizations.

FINRA further believes that increasing the position limit on conventional options promotes consistent regulation by harmonizing the position limit with its standardized counterpart. In addition, FINRA believes the proposed rule change will be beneficial to large market makers and institutions (which generally have the greatest ability to provide liquidity and depth in products that may be subject to higher position limits as has been the case with recently approved increased position limits),<sup>23</sup> as well as retail traders and public customers, by providing them with a more effective trading and hedging vehicle.

In addition, FINRA believes that the structure of the Underlying ETFs, the considerable market capitalization of the funds, underlying component securities and indexed component securities, and the liquidity of the markets for the applicable options and underlying component securities will mitigate concerns regarding potential manipulation of the products or disruption of the underlying markets upon increasing the relevant position limits. As a general principle, increases in market capitalizations, active trading volume, and deep liquidity of securities tend to deter manipulation or disruption.

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<sup>22</sup> 15 U.S.C. 78o-3(b)(6).

<sup>23</sup> See supra note 8.

This general principle applies to the recently observed increased levels of market capitalization, trading volume, and liquidity in shares of and options on the Underlying ETFs (as described above). FINRA does not believe that the options markets or underlying markets would become susceptible to manipulation or disruption as a result of the proposed position limit increases.

Increased position limits for select actively traded options, such as those proposed herein, are not novel and have been previously approved by the Commission.<sup>24</sup> Furthermore, FINRA notes that the proposed position limits for options on LQD and GDX are consistent with existing position limits for options on comparable ETFs in Rule 2360(b)(3)(A)(iii)a.6.

FINRA's existing surveillance and reporting safeguards are designed to deter and detect possible manipulative behavior that might arise from changing position and exercise limits.

B. Self-Regulatory Organization's Statement on Burden on Competition

FINRA does not believe that the proposed rule change will result in any burden on competition that is not necessary or appropriate in furtherance of the purposes of the Act.

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<sup>24</sup> See supra note 8. See also Securities Exchange Act Release Nos. 88768 (April 29, 2020), 85 FR 26736 (May 5, 2020) (Order Approving File No. SR-CBOE-2020-015); 83415 (June 12, 2018), 83 FR 28274 (June 18, 2018) (Notice of Filing and Immediate Effectiveness of File No. SR-CBOE-2018-042); and 68086 (October 23, 2012), 77 FR 65600 (October 29, 2012) (Order Approving File No. SR-CBOE-2012-066).

### Economic Impact Analysis

FINRA has undertaken an economic impact assessment, as set forth below, to analyze the potential economic impacts, including anticipated costs, benefits, and distributional and competitive effects, transfers of wealth, relative to the current baseline, and the alternatives FINRA considered in assessing how to best meet its regulatory objectives.

#### Regulatory Objective

FINRA is proposing to amend Rule 2360 to harmonize FINRA's position limits for conventional options with the position limit for standardized options.<sup>25</sup>

#### Economic Baseline

Per FINRA Rule 2360(b)(3)(A)(iii) conventional equity options are subject to a basic position limit of 25,000 contracts or higher for conventional option contracts on securities that underlie exchange-traded options qualifying for a higher tier as determined by option exchange rules. The existing position limits for conventional options on LQD and GDX are 250,000 contracts. Cboe has recently increased position limits for options on these ETFs.

#### Economic Impact

##### Benefits

As noted above, the proposed rule change would amend Rule 2360 to harmonize FINRA's position limits for conventional options with the position limits for standardized

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<sup>25</sup> See supra note 8.

options.<sup>26</sup> If the existing position limits for conventional equity options on select ETFs constrains trading in these ETFs, then investors may be able to better manage risk and trade on information when the position limit is relaxed. In general, the improvement in risk management and informational efficiency may increase more when position limits are increased. We acknowledge, however, that the conventional options on these ETFs, the ETFs themselves, and the securities underlying these ETFs are liquid, so improvements in informational efficiency may be relatively small.

For investors that trade conventional equity options, there is likely to be a natural size for an executed order that minimizes fixed and variable transaction costs, including but not limited to, the bid-ask spread, price impact, and transaction fees. If the existing position limits for conventional equity options on select ETFs constrains the order size such that fixed and variable transaction costs are higher than optimal, then investors may benefit if the new position limit is no less than the natural size. In such an event, the cost to hedge an ETF would decline, thereby making it less costly to manage downside risk.

In addition, if the existing position limits serve as a constraint, then an increase in the position limits for conventional options on select ETFs could permit investors to more easily find a counterparty. If the number of counterparties increases, then the cost of hedging should decline as the half-spread narrows, thereby making it less expensive to manage downside risk.

The extent of the constraint imposed by the current limit on conventional options is related to the ability of an investor to achieve similar economic exposure through other means. If there are other securities, such as an option on a closely related index, that

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<sup>26</sup> See supra note 8.

exist and provide similar economic exposure less expensively, then the value of lessening the position limits on conventional options on ETFs is lower.

Members may rely on information and data feeds from the Options Clearing Corporation to assist in their monitoring position limits. Because position limits on the standardized and conventional side have traditionally been consistent, members have relied on this feed for both standardized and conventional options. If the position limits between standardized and conventional options are conformed, then the cost from monitoring position limits should decline for member firms. Having the same position limits on standardized and conventional options, reduces the potential for excess loss that may be incurred when different limits are applied to the standardized versus conventional options on the same ETF. The economic loss may arise from building and maintaining trading and compliance systems to support the different regimes. Furthermore, the harmonization of position limits on standardized and conventional options eliminates the potential risk and cost arising from regulatory arbitrage.

#### Costs

The proposed rule change may impose limited operational cost on member firms that trade conventional options on ETFs, as these same firms would need to revise position limits that are used in trading systems. However, the proposed rule change should not impose additional costs, because it is difficult to disrupt or manipulate the underlying market, create an incentive to disrupt or manipulate the underlying market for the purpose of profiting from the options position, or disrupt or manipulate the options market for conventional options on ETFs affected by this proposed rule. ETFs that underlie options subject to the proposed rule change are highly liquid and are based on a

broad set of highly liquid securities, which makes the market difficult to manipulate or disrupt. In fact, options on certain broad-based security indexes have no position limits. Furthermore, the applicable creation and redemption process for these ETFs reduces the potential for disruptive or manipulative activity. New ETF units may be created at any time during the trading day and are not subject to position limits. Consequently, there is a direct link between the underlying components of the ETF, which keeps ETF's share prices trading in line with the ETF's underlying net asset value.

Alternatives

No further alternatives are under consideration.

C. Self-Regulatory Organization's Statement on Comments on the Proposed Rule Change Received from Members, Participants, or Others

Written comments were neither solicited nor received.

III. Date of Effectiveness of the Proposed Rule Change and Timing for Commission Action

Because the foregoing proposed rule change does not: (i) significantly affect the protection of investors or the public interest; (ii) impose any significant burden on competition; and (iii) become operative for 30 days from the date on which it was filed, or such shorter time as the Commission may designate, it has become effective pursuant to Section 19(b)(3)(A) of the Act<sup>27</sup> and Rule 19b-4(f)(6) thereunder.<sup>28</sup>

At any time within 60 days of the filing of the proposed rule change, the Commission summarily may temporarily suspend such rule change if it appears to the Commission that such action is necessary or appropriate in the public interest, for the

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<sup>27</sup> 15 U.S.C. 78s(b)(3)(A).

<sup>28</sup> 17 CFR 240.19b-4(f)(6).

protection of investors, or otherwise in furtherance of the purposes of the Act. If the Commission takes such action, the Commission shall institute proceedings to determine whether the proposed rule should be approved or disapproved.

#### IV. Solicitation of Comments

Interested persons are invited to submit written data, views and arguments concerning the foregoing, including whether the proposed rule change is consistent with the Act. Comments may be submitted by any of the following methods:

##### Electronic Comments:

- Use the Commission's Internet comment form (<http://www.sec.gov/rules/sro.shtml>); or
- Send an e-mail to [rule-comments@sec.gov](mailto:rule-comments@sec.gov). Please include File Number SR-FINRA-2022-007 on the subject line.

##### Paper Comments:

- Send paper comments in triplicate to Secretary, Securities and Exchange Commission, 100 F Street, NE, Washington, DC 20549-1090.

All submissions should refer to File Number SR-FINRA-2022-007. This file number should be included on the subject line if e-mail is used. To help the Commission process and review your comments more efficiently, please use only one method. The Commission will post all comments on the Commission's Internet website (<http://www.sec.gov/rules/sro.shtml>). Copies of the submission, all subsequent amendments, all written statements with respect to the proposed rule change that are filed with the Commission, and all written communications relating to the proposed rule change between the Commission and any person, other than those that may be withheld

from the public in accordance with the provisions of 5 U.S.C. 552, will be available for website viewing and printing in the Commission's Public Reference Room, 100 F Street, NE, Washington, DC 20549, on official business days between the hours of 10 a.m. and 3 p.m. Copies of such filing also will be available for inspection and copying at the principal office of FINRA. All comments received will be posted without change. Persons submitting comments are cautioned that we do not redact or edit personal identifying information from comment submissions. You should submit only information that you wish to make available publicly. All submissions should refer to File Number SR-FINRA-2022-007 and should be submitted on or before [insert date 21 days from publication in the Federal Register].

For the Commission, by the Division of Trading and Markets, pursuant to delegated authority.<sup>29</sup>

Jill M. Peterson  
Assistant Secretary

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<sup>29</sup> 17 CFR 200.30-3(a)(12).

## EXHIBIT 5

Below is the text of the proposed rule change. Proposed new language is underlined; proposed deletions are in brackets

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### 2300. SPECIAL PRODUCTS

\* \* \* \* \*

#### 2360. Options

(a) No Change.

##### (b) Requirements

(1) through (2) No Change.

##### (3) Position Limits

(A) Stock Options —

(i) through (ii) No Change.

(iii) Conventional Equity Options

a. For purposes of this paragraph (b), standardized equity option contracts of the put class and call class on the same side of the market overlying the same security shall not be aggregated with conventional equity option contracts or FLEX Equity Option contracts overlying the same security on the same side of the market. Conventional equity option contracts of the put class and call class on the same side of the market overlying the same security shall be subject to a position limit of:

1. through 5. No Change.

6. for selected conventional options on  
exchange-traded funds (“ETF”), the position limits  
are listed in the chart below:

<b>Security Underlying Option</b>	<b>Position Limit</b>
The DIAMONDS Trust (DIA)	300,000 contracts
The Standard and Poor's Depository Receipts Trust (SPY)	3,600,000 contracts
The iShares Russell 2000 ETF (IWM)	1,000,000 contracts
The PowerShares QQQ Trust (QQQ)	1,800,000 contracts
The iShares MSCI Emerging Markets ETF (EEM)	1,000,000 contracts
iShares China Large-Cap ETF (FXI)	1,000,000 contracts
iShares MSCI EAFE ETF (EFA)	1,000,000 contracts
iShares MSCI Brazil Capped ETF (EWZ)	500,000 contracts
iShares 20+ Year Treasury Bond Fund ETF (TLT)	500,000 contracts
iShares MSCI Japan ETF (EWJ)	500,000 contracts
iShares iBoxx High Yield Corporate Bond Fund (HYG)	500,000 contracts
<u>iShares iBoxx \$ Investment Grade Corporate Bond ETF (LQD)</u>	<u>500,000 contracts</u>
Financial Select Sector SPDR Fund (XLF)	500,000 contracts
<u>VanEck Vectors Gold Miners ETF (GDX)</u>	<u>500,000 contracts</u>

b. No Change.

(B) through (D) No Change.

(4) through (24) No Change.

(c) No Change.

• • • **Supplementary Material:** -----

.01 through .03 No Change.

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