

SECURITIES AND EXCHANGE COMMISSION
(Release No. 34-65086; File No. SR-FINRA-2011-036)

August 10, 2011

Self-Regulatory Organizations; Financial Industry Regulatory Authority, Inc.; Notice of Filing and Immediate Effectiveness of Proposed Rule Change to Increase the Position Limit for Options on the Standard and Poor's Depository Receipts Trust

Pursuant to Section 19(b)(1) of the Securities Exchange Act of 1934 ("Act")¹ and Rule 19b-4 thereunder,² notice is hereby given that, on July 29, 2011, 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 and II 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,³ 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 the Substance of the Proposed Rule Change

FINRA is proposing to amend FINRA Rule 2360 (Options), Supplementary Material .03 to increase the position limit for options on the Standard and Poor's Depository Receipts Trust ("SPY").

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.

¹ 15 U.S.C.78s(b)(1).

² 17 CFR 240.19b-4.

³ 17 CFR 240.19b-4(f)(6).

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

The purpose of the proposed rule change is to amend FINRA Rule 2360, Supplementary Material .03 to increase the position limit applicable to options on the Standard and Poor's Depository Receipts Trust, which trade under the symbol SPY, from 300,000 to 900,000 contracts⁴ to conform to a recent rule change by other self-regulatory organizations⁵ as well as [sic] the reasons discussed below.

Currently, SPY options have a position limit of only 300,000 contracts on the same side of the market while Power Shares QQQ Trust, based on the Nasdaq 100 Index[®] ("QQQ")

⁴ The exercise limits on SPY options set forth in FINRA Rule 2360(b)(4), which is not amended by this filing, but which incorporate by reference options position limits, would correspondingly increase to 900,000 contracts.

⁵ See Securities Exchange Act Release No. 64695 (June 17, 2011) 76 FR 36942 (June 23, 2011) (SEC order approving File No. SR-Phlx-2011-58); Securities Exchange Act Release No. 64760 (June 28, 2011) 76 FR 39143 (July 5, 2011) (Notice of Filing and Immediate Effectiveness of File No. SR-ISE-2011-34); Securities Exchange Act Release No. 64928 (July 20, 2011) (File No. SR-CBOE-2011-065); Securities Exchange Act Release No. 64966 (July 26, 2011) (File No. SR-NYSEAmex-2011-50); and Securities Exchange Act Release No. 64945 (July 21, 2011) (File No. SR-NYSEArca-2011-47).

options, which are comparable to SPY options but have lesser volume,⁶ have a position limit of 900,000 contracts on the same side of the market. Given the high volume and continuous demand for trading SPY options, FINRA believes that the current position limit of 300,000 contracts is inadequate, and that such options should, like options on QQQ, have a position limit of 900,000 contracts.

The position limit on SPY options has remained flat for more than five years, despite the options being the most actively traded options for the last two years, and is no longer sufficient for optimal trading and hedging purposes. SPY options are used by large institutions and traders as a means to invest in or hedge the overall direction of the market. The restrictive option position limit prevents large customers, such as mutual funds and pension funds, from using options to gain meaningful exposure to, and hedging protection through the use of, SPY options. Restrictive options position limits also can result in lost liquidity in both the options market and the equity market. The proposed position limit increase will remedy this situation to the benefit of large as well as retail traders, investors, and public customers. FINRA also believes that increasing position and exercise limits for SPY options would lead to a more liquid and competitive market environment that would benefit customers interested in this product.

In addition, FINRA believes that the options on SPY position and exercise limits, at their current levels, no longer serve their stated purpose. There has been a steadfast and significant increase over the last decade in the overall volume of exchange-traded options; position limits,

⁶ For example, options on SPYs, the most actively traded options in the U.S. in terms of volume, traded a total of 33,341,698 contracts across all exchanges from March 1, 2011 through March 16, 2011. In contrast, over the same time period options on the QQQ traded a total of 8,730,718 contracts (less than 26.2% of the volume of options on SPYs). In addition, for 2010, options on SPY had an average daily trading volume of 3.63 million contracts, while options on QQQs had an average daily trading volume of 963,502. See supra note 5 PHLX rule filing, at 36942.

however, have not kept up with the volume. Part of this volume is attributable to a corresponding increase in the number of overall market participants, which has, in turn, brought about additional depth and increased liquidity in exchange-traded options.⁷

FINRA believes that the existing surveillance procedures and reporting requirements at FINRA,⁸ the options exchanges, and at the several clearing firms are capable of properly identifying unusual and/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.⁹

Furthermore, large stock holdings must be disclosed to the Commission by way of Schedules 13D or 13G.¹⁰ 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 who 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.

⁷ The Commission has previously observed that: "Since the inception of standardized options trading, the options exchanges have had rules imposing limits on the aggregate number of options contracts that a member or customer could hold or exercise. These rules are intended to prevent the establishment of options positions that can be used or might create incentives to manipulate or disrupt the underlying market so as to benefit the options position. In particular, position and exercise limits are designed to minimize the potential for mini-manipulations and for corners or squeezes of the underlying market. In addition such limits serve to reduce the possibility for disruption of the options market itself, especially in illiquid options classes." See Securities Exchange Act Release No. 39489 (December 24, 1997), 63 FR 276, 278 (January 5, 1998) (File No. SR-CBOE-97-11) (order approving increased OEX position and exercise limits).

⁸ See FINRA Rule 2360(b)(5) for the reporting requirements.

⁹ These procedures have been effective for the surveillance of SPY options trading and will continue to be employed.

¹⁰ 17 CFR 240.13d-1.

FINRA believes that the current financial requirements imposed by FINRA and by the Commission adequately address concerns that a member or its customer may try to maintain an inordinately large unhedged position in an option, particularly on SPY. Current margin and risk-based haircut methodologies serve to limit the size of positions maintained by any one account by increasing the margin and/or capital that a member must maintain for a large position held by it or by its customer. It also should be noted that FINRA has the authority under FINRA Rule 4210(f)(8)(A) to impose a higher margin requirement upon a member when FINRA determines a higher requirement is warranted. In addition, the Commission's net capital rule, Rule 15c3-1 under the Act,¹¹ imposes a capital charge on members to the extent of any margin deficiency resulting from the higher margin requirement.

Finally, FINRA believes that while the position limit on options on QQQs, which as noted are similar to SPY options, has been gradually expanded from 75,000 contracts to the current level of 900,000 contracts, there have been no adverse affects on the market as a result of this position limit increase. Likewise, there have been no adverse affects on the market from expanding the position limit for SPY options from 75,000 contracts to the current level of 300,000 contracts.

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, such that FINRA can implement the proposed rule change immediately.

¹¹ 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,¹² 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 filing promotes consistent regulation by harmonizing FINRA's position limits for options on SPYs with those of the other self-regulatory organizations. In addition, FINRA believes this proposal will be beneficial to large market makers (which generally have the greatest potential and actual ability to provide liquidity and depth in this product), as well as retail traders, investors and public customers.

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.

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 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 prior to 30 days from the date on which it was filed, or such shorter time as the Commission may designate, if consistent with the protection of investors and the public interest, provided that the self-regulatory organization has given the Commission written notice of its intent to file the proposed rule change at least five business days prior to the date of filing of the proposed

¹² 15 U.S.C. 78o-3(b)(6).

rule change or such shorter time as designated by the Commission, the proposed rule change has become effective pursuant to Section 19(b)(3)(A) of the Act¹³ and Rule 19b-4(f)(6)(iii) thereunder.¹⁴

A proposed rule change filed under Rule 19b-4(f)(6)¹⁵ normally does not become operative prior to 30 days after the date of the filing. However, pursuant to Rule 19b-4(f)(6)(iii),¹⁶ the Commission may designate a shorter time if such action is consistent with the protection of investors and the public interest. FINRA has requested that the Commission waive the 30-day operative delay so that the proposal may become operative immediately upon filing. The Commission believes that waiving the 30-day operative delay is consistent with the protection of investors and the public interest, because increasing position and exercise limits for SPY options would lead to a more liquid and competitive market environment that would benefit customers interested in this product. Additionally, it would allow FINRA to seamlessly continue to offer traders and the investing public the ability to use this product as an effective hedging and trading vehicle. Lastly, it will enable FINRA's position and exercise limits for SPDR® options to be consistent with those of other exchanges that have already adopted the higher position and exercise limits. Therefore, the Commission designates the proposal operative upon filing.¹⁷

¹³ 15 U.S.C. 78s(b)(3)(A).

¹⁴ 17 CFR 240.19b-4(f)(6).

¹⁵ 17 CFR 240.19b-4(f)(6). In addition, Rule 19b-4(f)(6)(iii) requires that a self-regulatory organization submit to the Commission written notice of its intent to file the proposed rule change, along with a brief description and text of the proposed rule change, at least five business days prior to the filing of the proposed rule change, or such shorter time as designated by the Commission. The Commission notes that FINRA has satisfied this requirement.

¹⁶ 17 CFR 240.19b-4(f)(6)(iii).

¹⁷ For purposes only of waiving the 30-day operative delay, the Commission has considered the proposed rule's impact on efficiency, competition, and capital formation. See 15 U.S.C. 78c(f).

At any time within 60 days of the filing of such 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 protection of investors, or otherwise in furtherance of the purposes of the Act.

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. Please include File Number SR-FINRA-2011-036 on the subject line.

Paper Comments:

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

All submissions should refer to File Number SR-FINRA-2011-036. 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 10:00 a.m. and 3:00 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; the Commission does not edit personal identifying information from submissions. You should submit only information that you wish to make available publicly. All submissions should refer to File No. SR-FINRA-2011-036 and should be submitted on or before [insert date 21 days from date of publication in the Federal Register].

For the Commission, by the Division of Trading and Markets, pursuant to delegated authority.¹⁸

Elizabeth M. Murphy
Secretary

¹⁸ 17 CFR 200.30-3(a)(12).