

September 7, 2022

Mr. Robert W. Cook
President and Chief Executive Officer
Financial Industry Regulatory Authority
1735 K Street, NW
Washington, D.C., 20006

Dear Mr. Cook:

We write to express our concerns with the recent Financial Industry Regulatory Authority (“FINRA”) Regulatory Notice 22-08, which solicits public comment on a number of questions and policy considerations regarding retail investors’ access to “complex products” and options (the “Reg Notice”).¹ As you know, the Reg Notice raises potential regulatory changes that, if implemented, would raise costs and limit retail investors’ access to financial products and investment strategies that are widely available to other investors. A number of these changes could prohibit retail investors from trading in certain products, including options on registered securities.

In particular, we are concerned that FINRA is acting as a “merit” regulator by considering prohibiting or unduly restricting the sale of registered securities to specific investors, even when these investors have access to full and fair disclosure. Both FINRA and the Securities and Exchange Commission (“SEC”) have long avoided this approach. In fact, SEC Chair Gensler recently stated that, “[g]oing back to the 1930s, we have a disclosure-based regime, not a merit-based one.”²

In addition, we are concerned that FINRA is effectively seeking to propose a backdoor accredited investor standard on certain regulated securities that it deems unsuitable for retail customers. While such a change may be acceptable to the wealthiest customers of many FINRA member firms, it would only impede the progress of financial inclusion made possible through increased retail investor participation in our markets. In fact, a 2021 report prepared with the

¹ FINRA Regulatory Notice 22-08, “FINRA Reminds Members of Their Sales Practice Obligations for Complex Products and Options and Solicits Comment on Effective Practices and Rule Enhancements,” May 9, 2022, *available at* <https://www.finra.org/rules-guidance/notices/22-08#notice>.

² SEC Chair Gary Gensler, “A Century with a Gold Standard,” May 6, 2022, *available at* https://www.sec.gov/news/speech/gensler-acfmr-20220506?utm_medium=email&utm_source=govdelivery. *See, also*, Richard Ketchum, Chairman and CEO, FINRA, “Remarks from the SIFMA Complex Products Forum,” Sept. 27, 2012, (stating that, “merit regulation ... would be a significant departure from the product disclosure model on which the federal securities laws are based.”), *available at* <https://www.finra.org/media-center/speeches-testimony/remarks-sifma-complex-products-forum-0>.

FINRA Investor Collaboration Foundation showed that new investors entering the market as retail investors are more ethnically and racially diverse.³ According to the report, 17 percent of new investors in 2020 were African American, and 15 percent were Hispanic or Latino.⁴ Any attempts to limit these investors' access to investment opportunities would only narrow one important avenue towards their economic inclusion.

Moreover, retail investors' access to, and trading in, options has been highly regulated for decades. As you know, the existing regulatory framework includes shared responsibility by the SEC, FINRA, and the options exchanges. Those who trade in options are also afforded broad anti-fraud protections under the federal securities laws. Despite the robust regulatory framework already in place, the Reg Notice fails to adequately justify why new regulations are needed, or why existing regulations are no longer sufficient, to oversee the options markets and protect retail investors. A general increase in retail trading volume is not enough to justify restricting such investors' access to widely used and regulated financial products.

Nevertheless, the Reg Notice outlines several potential reforms that are problematic. For example, it questions whether broker-dealers should be required to conduct a "suitability review" for each level of options trading or to have a conversation with each customer before approving an account to trade options, regardless of whether an account is self-directed or options are being recommended by the firm.⁵ Not only would this impose a costly and unnecessary responsibility on firms, but it would also limit retail investors' ability to make their own investment decisions.

Similarly, the Reg Notice questions whether broker-dealers should require a customer to have a specific amount of equity in their account prior to trading options. Such a requirement would effectively impose an accredited investor standard on basic options. Together, these policies wrongly place FINRA's thumb on the scale against even the most basic options trading for retail investors. In doing so, they limit retail investors' access to important, widely available tools to hedge risk and generate income.

Decades of securities regulation demonstrates that retail investors are best protected when they have access to a variety of financial services and products with accurate disclosure, adequate educational resources, and vigorous enforcement of the law. We caution FINRA against acting

³ Mark Lush, *et al.*, "Investing 2020: New Accounts and the People Who Opened Them," NORC at the University of Chicago and FINRA Investor Education Foundation, Feb. 2021, at 3, *available at* https://www.finrafoundation.org/sites/finrafoundation/files/investing-2020-new-accounts-and-the-people-who-opened-them_1_0.pdf.

⁴ *Id.* at 4.

⁵ See SEC Release No. 34-86031, "Regulation Best Interest: The Broker-Dealer Standard of Conduct," Jun. 5, 2019, at 299 ("Nor does Regulation Best Interest apply to self-directed or otherwise unsolicited transactions by a retail customer, whether or not he or she also receives separate recommendations from the broker-dealer."), *available at* <https://www.sec.gov/rules/final/2019/34-86031.pdf>.

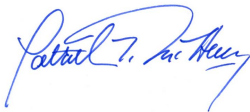
as a merit regulator and limiting retail investors' access to options trading, especially without evidence demonstrating that current regulations are inadequate.

To help the Committee on Financial Services further understand FINRA's objectives in advancing the Reg Notice, we would request answers to the following questions:

1. What evidence does FINRA have indicating that the current rules and regulations governing access to options and options trading are insufficient to protect retail investors?
2. What does FINRA view as the potential benefits of options trading for retail investors? What impact would the proposals included in the Reg Notice, including (but not limited to) the proposals referenced herein, have on retail investors' access to options?
3. Does FINRA believe that its appropriate role is to act as a merit regulator, limiting retail investors' access to options? If not, please detail measures FINRA has taken to enhance retail investors' access to capital markets, options trading and other investment and trading products.
4. Chair Gensler has indicated that the SEC may also seek to impose more stringent rules on so-called "complex products."⁶ Is FINRA coordinating with the SEC on these efforts? Specifically, has Robert Cook discussed these issues directly with Chair Gensler? Please describe any collaboration or joint efforts focused on the regulation of retail investor access to options and options trading.

Please provide written responses no later than September 30, 2022. We look forward to continuing our discussion on these critical issues.

Sincerely,



Patrick McHenry
Ranking Member



Bill Huizenga
Ranking Member of the Subcommittee
on Investor Protection, Entrepreneurship,
and Capital Markets



Ann Wagner
House Committee on Financial Services



French Hill
House Committee on Financial Services

⁶ See Tobias Salinger, "SEC's Gensler sees 'opportunity for tougher complex product rules,'" *Financial Planning*, May 16, 2022, available at <https://www.financial-planning.com/news/secs-gary-gensler-sees-opportunity-for-rules-on-complex-products>.



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House Committee on Financial Services



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