April 10, 2020

Via Electronic Mail (rule-comments@sec.gov)

Vanessa Countryman
Office of the Secretary
Securities and Exchange Commission
100 F Street, NE
Washington, DC 20549-1090

Re: *Commission Statement on Market Structure Innovation for Thinly Traded Securities (File No. S7–18–19)*[1] and *Nasdaq Application to Permit Issuer Choice to Consolidate Liquidity by Terminating Unlisted Trading Privileges*[2]

Dear Ms. Countryman:

The Healthy Markets Association[3] appreciates the opportunity to offer our comments to the above-referenced application by Nasdaq to create a new opportunity to suspend unlisted trading privileges in certain securities.

As an initial matter, we appreciate Nasdaq's efforts to promote liquidity and ease trading in thinly-listed securities.[4] We share those objectives. However, the 2020 Nasdaq Application should be denied because it does not provide sufficient information to establish its compliance with the Exchange Act and Commission rules.

Further, we question whether the 2020 Nasdaq Application could ever warrant approval, in part because it would directly impose an unreasonable burden on competition --

[1] *Commission Statement on Market Structure Innovation for Thinly Traded Securities,* Sec. and Exch. Comm'n, Exch. Act Rel. No. 34-87327, 84 Fed. Reg. 56856 (Oct. 24, 2019), *available at* https://www.govinfo.gov/content/pkg/FR-2019-10-24/pdf/2019-22994.pdf ("2019 Commission Statement").
[2] Letter from John A. Zecca, Nasdaq, to Hon. Jay Clayton, Sec. and Exch. Comm'n, Feb. 5, 2020, *available at* https://www.sec.gov/comments/s7-18-19/s71819-6848219-209750.pdf ("2020 Nasdaq Application").
[3] The Healthy Markets Association is an investor-focused not-for-profit coalition working to educate market participants and promote data-driven reforms to market structure challenges. Our members, who range from a few billion to hundreds of billions of dollars in assets under management, have come together behind one basic principle: Informed investors and policymakers are essential for healthy capital markets. To learn more about Healthy Markets or our members, please see our website at http://healthymarkets.org.
[4] We also wish to thank Nasdaq executives for speaking with us at length regarding its application. Teleconference between John Zecca and Jeffrey Davis, Nasdaq, and Tyler Gellasch and Chris Nagy, Healthy Markets Association, Apr. 6, 2020.

directly in contravention of the clear intent of Congress, the plain meaning of the text of the Exchange Act, and longstanding Commission policy. The proposal is facially inconsistent with decades of market structure law and policy designed to promote competition, and would instead permit the creation of government-sanctioned monopolies.

The proposal is little more than an attempt to turn back the clock to a time when listing exchanges faced less competition for trading, and investors were forced to absorb higher trading costs and lower execution quality. The Exchange has boldly asserted that granting it a monopoly for exchange trading in each of potentially hundreds of securities would somehow benefit investors. These claims are both unsupported, but also contrary to decades of experience.

If Nasdaq is granted the ability to operate as a trading venue monopoly, it should be expected that it will attempt to exploit that monopoly for its own benefit.[5] Thus, if the Commission were to grant the 2020 Nasdaq Application despite our objections, we urge it to limit the limitations on UTP to last for not more than 12 months, as well as establish safeguards to ensure that the exchange does not abuse the new monopoly powers. These safeguards would necessarily include pricing and other limitations on trading and market data, as well as criterion for measuring the "success" or "failure" of the proposal, and detailed procedures for having such suspensions or terminations revoked.

Background On Recent Proposals to Promote Liquidity in Thinly-Traded Securities

Policymakers, regulators, and market participants have long struggled to promote liquidity in thinly-traded securities. And several ideas have been attempted over the years. These ideas haven't generally worked out well for investors.

Most recently, former Nasdaq senior executive David Weild and others pressed Congress and the Commission to artificially widen stock trading tick sizes. The rationale the former Nasdaq official offered was that by widening the spreads, brokers would be able to make larger profits trading in those securities, and thus would be more

[5] As a for-profit entity, one would expect Nasdaq's executives to take seriously their fiduciary obligations to their shareholders, and maximizing shareholder value is often cited as a key tenet of modern corporate governance theory.

incentivized to provide investment research in those names.[6] It was a ridiculously flawed argument when made,[7] but it unfortunately carried the day.[8]

At the urging of Congress,[9] The Commission ultimately implemented a two-year Tick Size Pilot.[10] By the time the pilot mercifully ended, investors had lost an estimated more than $300 million.[11] There was no measured enhancement in liquidity or expansion of investment research.

Despite this disaster, calls for reforms to "promote liquidity" in thinly-traded securities have continued. Some commenters and regulators have suggested efforts to "boost liquidity" in less-liquid names could include instituting dynamic tick sizes, conducting periodic batch auctions, or consolidating trading on a single venue.[12]

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[6] *See, e.g.*, David Weild, Edward Kim and Lisa Newport, *The trouble with small tick sizes Larger tick sizes will bring back capital formation, jobs and investor confidence*, Grant Thornton, at 3, Sept. 2012, *available at* https://www.sec.gov/info/smallbus/acsec/acsec-backgroundmaterials-090712-weild-article.pdf ("higher tick sizes will … lead to investment in the ecosystem (research, stock sales, investment banking and capital commitment to provide institutional liquidity) required to successfully take companies public and support them in the aftermarket; favor long-term investors and stock pickers over short-term traders; and increase investor confidence by reducing the number of price points at which stocks are traded and by limiting computer trading behaviors.").

[7] Many market participants questioned the wisdom of the pilot. For example, the modern market makers in many securities (e.g., VirtuFinancial) are typically not providers of fundamental research. Thus, increasing market maker profitability still would not necessarily provide greater revenues to the firms who provide fundamental research. But even further, even if the two were the same entities, it's not entirely clear why profits from one business activity (i.e., market making) would necessarily be plowed back into subsidizing a different, and unrelated business activity, as opposed to any other way those profits could be spent (e.g., buybacks, dividends, executive compensation, etc.).

[8] While working as a United States Senate aide at the time, I met with Weild and others who were then pressing Congress and the Commission for a tick size pilot. Notably, after the pilot was a resounding failure, Weild later explained that it needed to be longer, and that "Nobody's going to hire research analysts on the basis of a two-year pilot." Alexander Osipovich, *SEC's Stock Trading Experiment Cost Investors Over $300 Million, Study Finds*, Wall St. Journal, Sept. 6, 2018, *available at* https://www.wsj.com/articles/secs-stock-trading-experiment-cost-investors-over-300-million-study-finds-1536206461.

[9] Jumpstart Our Business Startups Act, Pub. L. 112–106, 126 Stat. 306 (2012).

[10] *Order Approving the National Market System Plan To Implement a Tick Size Pilot Program by BATS Exchange, Inc., BATS YExchange, Inc., Chicago Stock Exchange, Inc., EDGA Exchange, Inc., EDGX Exchange, Inc., Financial Industry Regulatory Authority, Inc., NASDAQ OMX BX, Inc., NASDAQ OMX PHLX LLC, The Nasdaq Stock Market LLC, New York Stock Exchange LLC, NYSE MKT LLC, and NYSE Arca, Inc., as Modified by the Commission, for a Two-Year Period,* Sec. and Exch. Comm'n, Exch. Act Rel. No. 34-74892, 80 Fed. Reg. 27514 (May 13, 2015), *available at* https://www.govinfo.gov/content/pkg/FR-2015-05-13/pdf/2015-11425.pdf.

[11] Pragma Securities, *SEC Tick Size Pilot cost investors over $300 million*, Sept. 6, 2018, *available at* https://www.pragmatrading.com/wp-content/uploads/2018/09/SEC-Tick-Size-Pilot-cost-investors-over-US300-million.pdf.

[12] Proposals to consolidate trading for less-liquid securities have appeared to gain traction as the number of exchanges, ATSs, and broker-dealer internalizers has grown, further fragmenting the number of places where stocks may trade. In fact, excessive fragmentation of liquidity is a concern generally for investors, brokers, and other key market participants--irrespective of whether a security is heavily traded or not.

In October of 2017, the Treasury Department's Capital Markets report called on the Commission to allow:

> issuers of less-liquid stocks, in consultation with their underwriter and listing exchange, be permitted to partially or fully suspend UTP for their securities and select the exchanges and venues upon which their securities will trade… [and] choose to have their stock trade only on a smaller number of venues until liquidity in the stock reaches a minimum threshold.[13]

Notably, the Treasury Capital Markets Report recommended suspending UTP, but still permitting broker-dealer internalization, in an effort to continue some "competition."[14]

In the Spring of 2018, Nasdaq joined several other trade organizations in releasing a report, *Expanding the On-Ramp*, which called for, amongst other things, allowing Emerging Growth Companies or "small issues" with "distressed liquidity" to opt-out of unlisted trading privileges.[15]

Commission Invitations for Proposals and Nasdaq Applications

On April 23, 2018, the Commission held a Roundtable on Market Structure for Thinly Traded Securities, which also explored the issues. Two days after that Roundtable, Nasdaq filed the 2018 Nasdaq Application.[16]

The 2018 Nasdaq Application formally asked the Commission to utilize its Section 12(f) authority to suspend unlisted trading privileges in

> Nasdaq-listed securities that: (1) are issued by an operating company; (2) have an initial market capitalization of $700 million or less or a continued market capitalization of $2 billion or less; (3) have an initial Average Daily Volume

[13] *A Financial System That Creates Economic Opportunities Capital Markets*, U.S. Dep't of the Treasury, Oct. 2017, at 60, *available at* https://www.treasury.gov/press-center/press-releases/Documents/A-Financial-System-Capital-Markets-FINAL-FINAL.pdf ("Treasury Capital Markets Report").

[14] Treasury Capital Markets Report, at 60. As discussed in greater detail below, this was essentially industry practice for decades.

[15] Nasdaq *et al.*, *Expanding the On-Ramp*, Spring 2018, *available at* https://www.uschamber.com/sites/default/files/ipo_report_expanding_the_on-ramp.pdf.

[16] Letter from Edward Knight, Nasdaq to Hon. Jay Clayton, Sec. and Exch. Comm'n, Apr. 25, 2018, *available at* https://www.sec.gov/comments/265-31/26531-3515735-162293.pdf ("2018 Nasdaq Application.").

("ADV") of 100,000 shares or less; and (4) have a bid price greater than $1 ("Subject Securities").[17]

According to the 2018 Nasdaq Application, the suspension would only last for not more than twelve months, and would only occur for corporate stock issuers that "opt in" to the suspension.[18] The proposal asserted that:

- "UTP may exacerbate market fragmentation and thereby negatively impact market quality for less liquid issuers;"[19]
- "suspending UTP trading in the Subject Securities will promote market quality by, among other things, promoting the submission of displayed limit orders in those securities;"[20]
- "the absence of UTP trading will foster innovations in market structure that may not be feasible in an environment where stocks trade via UTP. Suspending UTP trading for the Subject Securities would provide Nasdaq with the opportunity to create functional and financial incentives for displayed limit orders in the Subject Securities that are closely tailored to the trading characteristics of those securities, and thereby encourage additional trading, including the increased submission of displayed limit orders, in these securities;"[21] and
- "suspending UTP for the Subject Securities would reduce market complexity, promote market stability, and promote efficiency."[22]

While the Commission didn't grant the 2018 Nasdaq Application, in March 2019, Chairman Clayton and the Director of the Division of Trading and Markets offered joint remarks at Fordham University in which they suggested strongly that the Commission was considering whether to allow for the suspension of UTP in less-liquid securities so as to aggregate liquidity.[23] The Commission also subsequently released a statement[24] and a paper by the Division of Trading and Markets staff considering methods to

[17] 2018 Nasdaq Application, at 3.
[18] 2018 Nasdaq Application, at 3.
[19] 2018 Nasdaq Application, at 4.
[20] 2018 Nasdaq Application, at 5.
[21] 2018 Nasdaq Application, at 5.
[22] 2018 Nasdaq Application, at 5.
[23] Remarks of Hon. Jay Clayton and Brett Redfearn, Equity Market Structure 2019: Looking Back & Moving Forward before Fordham University, Mar. 8, 2019, *available at* https://www.sec.gov/news/speech/clayton-redfearn-equity-market-structure-2019 ("A potential initiative to address illiquidity, which was discussed at length at the Roundtable, is the Department of the Treasury's recommendation in its Capital Markets Report to allow issuers of thinly-traded securities to suspend unlisted trading privileges for non-listing exchanges, while continuing to allow off-exchange trading in these securities as a means to maintain competition among trading venues. … I have asked our Division of Trading and Markets staff to explore this issue, including considering whether primary listing exchanges should develop pilot programs that would allow us, and market participants, to explore the effects of restricting unlisted trading privileges for certain classes of thinly-traded stocks.").
[24] 2019 Commission Statement.

improve trading in thinly traded securities.[25] In that 2019 Commission Statement, the Commission expressed a willingness to explore proposals to suspend or terminate UTP for thinly traded securities,[26] provide exemptive relief from Regulation NMS,[27] increase incentives for market makers;[28] hold periodic auctions;[29] and introduce non-automated markets.[30]

At that time, the 2019 Commission Statement expressly noted that an "application to suspend or terminate UTP for thinly traded securities under Section 12(f) of the Exchange Act and the rules thereunder may be submitted to the Commission."[31] The 2020 Nasdaq Application appears to be made in response to that invitation.

Substantively, the 2020 Nasdaq Application is remarkably similar to the 2018 Nasdaq Application. However, unlike the 2018 Nasdaq Application, the current one isn't a suspension of UTP for up to one year, but is instead a complete termination of UTP.[32]

Further, we note that Nasdaq has outlined its longer-term objective of creating a new "tier" of securities, where trading would occur outside of the normal investor protections afforded by the Exchange Act and Commission Rules. In fact, this "vision" includes not just denying investors basic trading protections, but also information and rights. We also note that Nasdaq has proposed that executives for companies in these tiers also be provided greater transparency into who's trading in those securities. Fortunately, while we are deeply troubled by Nasdaq's vision, the issue before the Commission at the moment is application itself.

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[25] *Background Paper on the Market Structure for Thinly Traded Securities*, Sec. and Exch. Comm'n Division of Trading and Markets, Oct. 17, 2019, *available at* https://www.sec.gov/rules/policy/2019/thinly-traded-securities-tm-background-paper.pdf ("2019 Staff Paper"). According to the staff paper, "one-half of all NMS stocks have an average daily trading volume ("ADV") of less than 100,000 shares and constitute less than two percent of all daily share volume." 2019 Staff Paper, at 1. In fact, that paper cited to an earlier staff paper, which also found that nearly one-fifth of NMS common stocks and two-thirds of ETPs traded less than 50,000 shares a day, and comprised less than one-fourth of one percent of the average daily volumes. *Empirical Analysis of Liquidity Demographics and Market Quality For Thinly-Traded NMS Stocks*, Sec. and Exch. Comm'n Office of Analytics and Research, Division of Trading and Markets, at 2, Apr. 10, 2018, *available at* https://www.sec.gov/files/thinly_traded_eqs_data_summary.pdf.

[26] 2019 Commission Statement, at 56957 (noting that the Commission "believes that certain market structure innovations that may provide benefits to thinly traded securities, when applied on one given exchange, may be less likely to succeed if the securities are subject to concurrent trading on multiple exchanges with different trading models. Accordingly, to be effective, these innovations may require the suspension or termination of UTP.").

[27] 2019 Commission Statement, at 56956.

[28] 2019 Commission Statement, at 56957.

[29] 2019 Commission Statement, at 56957-58.

[30] 2019 Commission Statement, at 56958.

[31] 2019 Commission Statement, at 56957, n.13 (internal citations omitted).

[32] We noticed that the only changes in the justifications between what would be a temporary change and permanent change was the replacement of the word "suspend" with "terminate."

At root, the 2020 Nasdaq Application is simply a proposal to permit the reinstatement of monopoly exchange trading in listed securities. This isn't a new concept. In fact, it's similar to how the world used to be. Congress and the Commission have spent decades trying to change that.

Background on Consolidation of Trading

For decades, policymakers and regulators have wrestled with how to promote liquidity and reduce transaction costs for investors. In the mid-1990s, as technological changes were revolutionizing trading, Congress conducted a series of hearings on a number of key market structure issues ranging from decimalization and limit order display rules to conflicted order routing practices, payments for order flow, and best execution obligations.[33]

One of the key issues was where stocks could trade. At that time, nearly all exchange trading occurred on the exchanges where those securities were listed. While NASD and brokers could freely execute trades away from the listing exchange, other exchanges (i.e., the regional exchanges) could not. Historically, the Securities Exchange Act of 1934 required stock exchanges to ask the Commission for permission before beginning to trade securities listed elsewhere. And while the approval process could take months, the Commission had not once, since 1939, denied a request by a regional exchange for UTP.[34]

In 1993, Representative (now Senator) Ron Wyden drafted legislation that would immediately provide UTP to regional exchanges.[35] In 1994, the bill was revised, reintroduced as the Unlisted Trading Privileges Act of 1994, and adopted by voice vote in both the House and Senate.[36] That law provided for UTP within two days of an IPO, while also ensuring that the Commission could suspend or terminate UTP.[37]

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[33] See, e.g., *Hearing Before the Subcommittee on Telecommunications and Finance, Committee on Energy and Commerce on H.R. 4535*, 103rd Cong. 83 (1994) (Statement of James F. Duffy, American Stock Exchange, Inc.), *available at* https://babel.hathitrust.org/cgi/pt?id=uc1.31210013511603&view=1up&seq=1 ("We are concerned, for example, that the practice of cash payments for order flow could induce brokers to route orders for execution to markets or market makers based on maximizing broker profits rather than providing a customer order with the best possible price."); see also, Id., at

[34] See, *Hearing Before the Subcommittee on Telecommunications and Finance, Committee on Energy and Commerce on H.R. 4535*, 103rd Cong. 5 (1994) (Statement of Hon. Ron Wyden), *available at* https://babel.hathitrust.org/cgi/pt?id=uc1.31210013511603&view=1up&seq=1.

[35] H.R. 2515, 103rd Cong. (1993), *available at* https://www.govtrack.us/congress/bills/103/hr2515/text/ih.

[36] *Unlisted Trading Privileges Act of 1994.* Public L. 103-389 (1994), *available at* https://www.congress.gov/103/bills/hr4535/BILLS-103hr4535enr.pdf. Legislative actions available at https://www.congress.gov/bill/103rd-congress/house-bill/4535/actions?KWICView=false.

[37] *Unlisted Trading Privileges Act of 1994.* Public L. 103-389 (1994),

After the revised, compromise language had been hammered out, the House of Representatives held one last hearing on the bill.[38] Republican Representative Jack Fields, Jr., explained that the legislation would direct the Commission to "modernize these rules to ensure that monopolies are not being protected and that competition, not regulation, determines where stocks will trade."[39]

Nevertheless, this statutory change, and the Commission's subsequent rulemaking, were inadequate to successfully promote competition between exchanges for either listings or trading. There were, it turns out, other barriers. Perhaps one of the most obvious was NYSE Rule 390. Rule 390 and its predecessor originally prohibited trading in all securities by NYSE members and their affiliates, but was later modified to prohibit just trading in some historical NYSE-listed securities.[40]

As recently as September 1999, about 84% of share volume in NYSE-listed equities were traded on the exchange and about 71% of the share volume in Amex listed securities were traded on Amex.[41] This monopoly position gave rise to significant concerns for investors, and enabled significant abuses by specialists and other market makers. Nevertheless, NYSE defended its efforts to restrict trading to its listing exchange on the grounds that it reduced fragmentation and promoted liquidity and price formation by aggregating orders on a single venue--essentially the same arguments that Nasdaq is making now.

After years of complaints and enforcement actions, NYSE finally rescinded Rule 390.[42] In approving the change, the Commission explained

> Off-board trading restrictions such as Rule 390 have long been questioned as attempts by exchanges with dominant market shares to prohibit competition from other market centers. On their face, such restrictions run contrary to the Exchange Act's objectives to assure fair competition among

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[38] *Hearing Before the Subcommittee on Telecommunications and Finance, Committee on Energy and Commerce on H.R. 4535*, 103rd Cong. 5 (1994), *available at* https://babel.hathitrust.org/cgi/pt?id=uc1.31210013511603&view=1up&seq=1.
[39] Id. (Statement of Hon. Jack Fields, Jr.), at 3.
[40] *Notice of Filing of Proposed Rule Change by the New York Stock Exchange, Inc. to Rescind Exchange Rule 390; Commission Request for Comment on Issues Relating to Market Fragmentation*, Sec. and Exch. Comm'n, Exch. Act Rel. No. 34-42450, Feb. 23, 2000, *available at* https://www.sec.gov/rules/sro/ny9948n.htm.
[41] *Notice of Filing of Proposed Rule Change by the New York Stock Exchange, Inc. to Rescind Exchange Rule 390; Commission Request for Comment on Issues Relating to Market Fragmentation*, (citing NYSE and Amex).
[42] *Notice of Filing of Proposed Rule Change by the New York Stock Exchange, Inc. to Rescind Exchange Rule 390; Commission Request for Comment on Issues Relating to Market Fragmentation*, Sec. and Exch. Comm'n, Exch. Act Rel. No. 34-42450, Feb. 23, 2000, *available at* https://www.sec.gov/rules/sro/ny9948n.htm.

> market centers and to eliminate unnecessary burdens on competition.[43]

Despite the repeal of Rule 390, there have remained some material monopolies in trading, most notably the opening and closing auctions. Again, the arguments in support of those temporary monopolies has been that the aggregation of orders at the listing venues at those two critical points in the day allows for the most robust price discovery mechanism.

However, particularly as trading has begun to aggregate towards the open and close of the day, market participants have begun to look for alternatives. Why? Because the listing exchanges have come to increasingly exploit their monopolies on trading during those times. The listing exchanges impose higher trading costs for those periods.

In response to pleas from market participants for ways to avoid those higher trading costs, approximately three years ago, Bats BZX Exchange, Inc. (now known as Cboe BZX Exchange, Inc.) applied to the Commission for approval to match market-on-close orders for securities not listed on the exchange.[44] Not surprisingly, both Nasdaq and NYSE objected to the proposal. After years of comments, modifications, an initial approval, and an appeal, the Commission ultimately approved that proposal just a few months ago.[45] In approving the proposal, the Commission concluded that it "should introduce and promote competitive forces among national securities exchanges for the execution of MOC orders [and] should not disrupt the closing auction price discovery process nor should it materially increase the risk of manipulation of official closing prices."[46]

Put simply, while the exchanges have a long history of seeking to promote monopoly trading, Congress and the Commission have now spent decades slowly breaking up those monopolies to promote competition.

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[43] *Order Approving Proposed Rule Change to Rescind Exchange Rule 390*, Sec. and Exch. Comm'n, Exch. Act Rel. No. 34-42758, May 5, 2000, *available at* https://www.sec.gov/rules/sro/ny9948o.htm.

[44] *Notice of Filing of a Proposed Rule Change to Introduce Bats Market Close, a Closing Match Process for Non-BZX Listed Securities Under New Exchange Rule 11.28*, Sec. and Exch. Comm'n, Exch. Act Rel. No. 34-80683, May 16, 2017, *available at* https://www.sec.gov/rules/sro/batsbzx/2017/34-80683.pdf.

[45] *Order Setting Aside Action by Delegated Authority and Approving a Proposed Rule Change, as Modified by Amendments No. 1 and 2, to Introduce Cboe Market Close, a Closing Match Process for Non-BZX Listed Securities under New Exchange Rule 11.28*, Sec. and Exch. Comm'n, Exch. Act Rel. No. 34-88008, Jan. 21, 2020, *available at* https://www.sec.gov/rules/sro/batsbzx/2020/34-88008.pdf?mod=article_inline.

[46] Id., at 6. We note that this venue has not yet attracted signficiant volume. However, we believe that this may be, in part, due to changes instituted by the listing exchanges so as to keep from losing trading to the new offering.

The 2020 Nasdaq Application Is Inconsistent with Congressional Intent, the Exchange Act, and Commission Policy

Congress imbued the Exchange Act with a strong mandate to promote -- not inhibit -- competition. The Commission is acutely aware of the monopoly positions exchanges have over trading (such as on the closing auctions) and over market data. Repeatedly, over many years and many actions, the Commission has chipped away at those monopolies in efforts to promote competition and more efficient, fair, and transparent markets. We have generally applauded these efforts.

The 2020 Nasdaq Application would explicitly seek to go in the opposite direction -- and create a government-sanctioned monopoly -- ostensibly to aggregate liquidity for less-liquid securities. This proposal raíses many, many questions that are not answered in its application, but the first question has to be:

What is the objective for terminating UTP?

Is the objective of terminating UTP to promote more trading in those securities? Is it to reduce trading costs for market makers? Is it to promote more fundamental investment in those securities? Unfortunately, these questions are not answered in the proposal.

Instead, we are left to speculate that the objectives are to promote trading and reduce investor trading costs. Assuming that those are the objectives, there are then several critical questions that arise. For example:

- Would terminating UTP encourage market makers to offer more quote depth? If so, how?
- Would terminating UTP encourage market makers to offer more size at the top-of-book? If so, how?
- Would terminating UTP make quotes more accessible for investors? If so, how?
- Would terminating UTP increase investor demand in thinly-traded securities? If so, how?

Put simply, what is the mechanism for how aggregating liquidity onto a single venue would achieve more liquidity or lower trading costs? In today's marketplace, stocks can trade on numerous venues, and market participants typically have data feeds from and connections to all major trading venues. Thus, to a market participant, it may be irrelevant if it sees 1000 shares posted on the NBO at one exchange, or spread over five different exchanges. But even if there were a material difference to investors, the Exchange has offered no data or factual analysis to suggest that the spreads would be

narrower, the liquidity would be more or less “accessible”, or other trading costs would be lower if all of the shares were posted on one exchange, as opposed to several.

Importantly, the 2020 Nasdaq Application does not directly address off-exchange trading. In many of the securities that would be covered by the proposal, off-exchange trading may comprise 50% or more of daily volume. What would the impact of the new monopoly on exchange trading be? While we aren’t required to provide analysis, our expectation would be that overall exchange quoting and trading would actually decrease as a result of the termination of UTP. Market makers, instead of posting quotes on multiple exchanges would instead by quoting on one, thus showing a lesser number of shares to trade at any given time. Nasdaq has offered no details or analysis on this important market impact. It must.

Further, the overall market share for exchange trading in a security may be 50% today, but that may be spread over multiple exchanges. If all exchange liquidity is consolidated onto Nasdaq, we would expect that percentage of exchange trading marketshare to fall -- decreasing displayed liquidity, widening spreads, and more. Again, the Exchange has not provided any analysis of how its termination of UTP would impact the percentage of quote and trading activity that is in the lit, versus dark, markets. It must.

While the 2020 Nasdaq Application observes low trading volumes and relatively high costs for trading in less-liquid securities, it has offered no evidence to relate its proposed “solution” to those concerns. Nasdaq argues that terminating UTP “promotes economic and pricing efficiency by focusing the listing and trading of securities,” but fails to explain how. It must.

But Nasdaq needs to offer more than just a theory of how it *could work*. It needs to show that its proposal *would protect investors*. That requires not just cocktail party theories, but data. To approve the application, the Commission would need to conclude that the elimination of exchange trading competition would -- in fact -- improve investors’ execution quality, lower investors’ costs, or otherwise improve their experience. The 2020 Nasdaq Application offers none of that information.

Somewhat amazingly, nothing in the 2020 Nasdaq Application materially limits the ability of the Exchange to exploit its position as a newly government-sanctioned monopoly. For example, would Nasdaq charge investors more for trading in securities for which UTP is suspended, as it currently does in closing auctions? Would Nasdaq charge more for market data in those securities, as it would be essentially the sole source exchange market information? We recognize that Nasdaq has admitted that, if granted, it would have some of these powers. And we understand that the Exhange may be willing to limit its pricing powers, but we have not yet seen any details. If the Exchange is granted monopoly powers over exchange trading in a security, it will have tremendous power over costs for both the trades, and more importantly, the data. While the trading costs may be partially limited by the ability to execute at off-exchange

trading venues, we nevertheless believe that the pricing powers may be significant. Further, the data for these securities would be essential for any market participants looking to trade in any of these securities--especially since that is the only source for displayed prices. Put another way, why wouldn't the for-profit Exchange seek to exploit its newly-minted monopoly powers?

The 2020 Nasdaq Application also doesn't justify its choices. For example, why did it determine that more than half of its listed securities should qualify for the termination of UTP? What is the basis for that determination? Why is the termination at the option of the issuer? Why don't investors get a say? The markets are not just for issuers, but for investors as well. The choices made in its proposal appear to be justified only by Nasdaq's self-interest in re-establishing monopolistic powers for exchange trading and market data in a broad swath of its listed securities. Again, the Exchange needs to offer facts and a reasonable basis for its choices.[47] It hasn't done that. And without that information, the Commission cannot lawfully approve the proposal.[48]

As the Court of Appeals for the District of Columbia reiterated in *Susquehanna*,[49] the Administrative Procedure Act (APA) makes agency action unlawful if it is "arbitrary, capricious, an abuse of discretion, or otherwise not in accordance with law" or that is "unsupported by substantial evidence."[50] Furthermore, "[t]o satisfy the "arbitrary and capricious" standard, "the agency must examine the relevant data and articulate a satisfactory explanation for its action including a 'rational connection between the facts found and the choice made.'"[51]

Without details about (1) what Nasdaq is trying to accomplish, (2) how permitting issuers to "opt in" to terminate UTP would accomplish those goals, (2) the respective impacts on other market participants, including investors, and (4) the impacts on the markets overall, the Commission simply cannot lawfully grant the application.

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[47] In addition to information about the proposal and its impacts, we also note that the 2018 Nasdaq Application for exemptive relief was not granted. Now, the Exchange has come back with no new information, and yet a bolder request. Instead of a suspension of UTP, it is now proposing a permanent termination of UTP. The Exchange should explain why it thinks the Commission should -- instead of temporarily suspending UTP -- terminate it.

[48] We question whether the Commission has authority to suspend or terminate UTP broadly, as Nasdaq has asserted. The legislative history of the Unlisted Trading Privileges Act of 1994 contemplates UTP suspensions and grants being made on a per security basis (including around the time of those securities' IPOs. Congress did not appear to ever contemplate, and the Commission did not appear to ever seek to assert, authority to suspend UTP writ large for a swath of securities.

[49] *Susquehanna Int'l Grp., LLP v . SEC*, 866 F.3d 442 (D.C. Cir. 2017).

[50] Id., at 445 (citing 5 U.S.C. § 706(2)(A), (E)).

[51] Id., at 445 (citing *Motor Vehicle Mfrs. Ass'n v. State Farm Mut. Auto. Ins. Co.*, 463 U.S. 29, 43, (1983) (quoting *Burlington Truck Lines, Inc. v. United States* , 371 U.S. 156, 168, (1962)).

Data and Anaylsis -- An "Off-Switch"

The 2020 Nasdaq Application, if approved, would allow the Exchange to permit issuers to "opt in" to a world without UTP. But the application does not detail how "success" or "failure" would be measured. It offers no new data collection or analysis of the impacts of its proposal, once undertaken. Nor does it detail the procedures through which market participants -- or the Commission -- could or should reconsider the termination of UTP. What happens if the immediate impact is to shrink displayed liquidity in the covered securities? What if the issuers don't seem to mind? What if investor's trading costs materially rise? What recourse would investors have?

Essentially, Nasdaq is looking to engage in a massive experiment with as much as half of its issuers, but has not built in any appropriate metrics to study, or scoped its experiment so as to avoid negative impacts on investors or the markets. If the Commission decides to approve the 2020 Nasdaq Application in whole or in part, we urge it to impose significant data collection and reporting, as well as install automatic "off switches" or triggers to reduce potentially negative impacts on investors or the markets.

Conclusion

To be approved, the Commission would need to determine that the 2020 Nasdaq Application "is necessary or appropriate in the public interest or for the protection of investors."[52] Further, the Commission would have to itself "examine the relevant data and articulate a satisfactory explanation for its action including a 'rational connection between the facts found and the choice made.'"[53] Nothing in the record provides sufficient information for the Commission to make that determination. Accordingly, we urge the Commission to deny the 2020 Nasdaq Application.

If the Commission nevertheless determines to permit the limitation of UTP, we urge it to limit the restrictions to not more than 12 months, and to impose such limitations and restrictions as may be necessary to prevent Nasdaq from exploiting the government-sanctioned monopoly pricing power to maximize its profits at the expense of other market participants. Lastly, the Commission should impose data collection and analysis to measure "success" or "failure" of the initiative, and should take such necessary actions so as to ensure that the termination or suspension of UTP does not -- in fact -- harm investors or the markets overall.

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[52] Securities Exchange Act, Section 12(f).

[53] *Susquehanna*, at 445 (citing *Motor Vehicle Mfrs. Ass'n v. State Farm Mut. Auto. Ins. Co.*, 463 U.S. 29, 43, (1983) (quoting *Burlington Truck Lines, Inc. v. United States* , 371 U.S. 156, 168, (1962)).

Thank you for your consideration. Should you have any questions or would like to discuss these matters further, please contact me at (202) 909-6138.

Sincerely,

Tyler Gellasch
Executive Director