



December 22, 2014

Brent J. Fields
Secretary
Securities and Exchange Commission
100 F Street NE
Washington, DC 20549-1090

Re: File No. 4-657; Release No. 34-73511: *Proposed National Market System Plan to Implement a Tick Size Pilot Program on a One-Year Pilot Basis*

To whom it may concern:

The Biotechnology Industry Organization (BIO) is pleased to submit comments to the Securities and Exchange Commission (SEC) on the proposed national market system plan to implement a tick size pilot program. BIO applauds the SEC and the plan participants for taking steps to address the trading needs of emerging companies on the public market, and we look forward to working to ensure that the pilot is successful for job-creating American small businesses.

BIO is a not-for-profit trade association that represents more than 1,100 biotechnology companies, academic institutions, state biotechnology centers, and related organizations in all 50 states. BIO members are working toward groundbreaking cures and treatments for devastating diseases, developing technologies for advanced biofuels and renewable chemicals, and researching novel gene traits for identifying food sources that could help combat global hunger.

In the biotechnology industry, it can take more than a decade and over \$1 billion to bring a single lifesaving treatment from laboratory bench to hospital bedside. Further, the entire process is undertaken without the benefit of product revenue. Early-stage biotech companies do not have the luxury of using the sale of one product to finance the development of another. Rather, the entire cost of drug development is borne by external investors.

As companies near the later stages of research and begin conducting expansive clinical trials in human patients, they often turn to an IPO for capital formation. As such, a functioning public market is vital to the success of the biotech industry and the development of lifesaving treatments for patients. When effective, the markets provide innovation capital through an IPO, stimulate a liquid and profitable trading environment for investors, offer growing companies important leverage in M&A negotiations, and create an exit for early-stage venture capitalists.

The recent surge of biotech IPOs has shown the importance of public financing to emerging innovators. Since the passage of the Jumpstart Our Business Startups (JOBS) Act in April 2012, more than 130 small biotech companies have used the law's IPO On-Ramp to go public. The capital from their offerings is supporting research and spurring job creation, and the re-opened market has the potential to inspire growth in innovative companies at all stages of development. However, emerging issuers still face the challenges inherent to trading as a public company. Stagnant liquidity can stall their progress and decrease the

appeal of an IPO for other growing companies. BIO applauds the SEC and the national securities exchanges for taking steps to support small company growth and maintain the essential role of the public market in biotech capital formation. BIO is hopeful that an effective tick size pilot program will build on the success of the JOBS Act and support company growth, job creation, and groundbreaking R&D at small business innovators across the country.

Decimalization, Tick Size, and Small Issuer Liquidity

The one-size-fits-all tick size imposed by decimalization has hampered small company growth since it was implemented in 2000. When the SEC adopted decimalization, the goal was to increase trading activity for large issuers with millions of shares traded each day. However, as large companies enjoyed an influx of new investors, small issuers experienced a corresponding decrease in liquidity. Without strong liquidity available for small public companies, the public market ceases to be an effective source of capital formation for emerging biotechs to raise the funds necessary to support the decade-long, billion-dollar development timeline intrinsic to groundbreaking R&D.

The proposing release solicits comment on whether small cap stocks would benefit from the proposed pilot program. BIO believes that small companies will see an increase in liquidity under a more flexible tick size regime, and thus that the pilot will benefit small companies and their investors alike.

Thinly traded stocks, like those of most small biotechs, often need market-makers to stimulate trading activity, and a decreased tick size removes their incentive to do so. Market-makers face a limited upside when trading in small spreads, so a reduced tick diminishes their potential profit margin, changing their market-making habits and leaving small cap stocks stagnant. The public market plays a vital role in financing next generation R&D, but a sluggish market bereft of liquidity does nothing to spur capital formation or fund research. The current one-size-fits-all approach to tick size does not reflect the realities of the market and subjects smaller issuers to the same trading framework as large, multinational corporations with exponentially higher revenues, trading volumes, and market capitalizations.

BIO supports flexibility in tick size for smaller issuers in order to address the needs of growing companies hamstrung by decimalization. A pilot program to allow small cap stocks to be traded in larger trading increments would meet this problem head on and give the SEC the opportunity to study the effects of an increased tick on small company trading. Allowing growing companies to trade at \$0.05 increments would stimulate market-making activity in small company stocks and lead to a corresponding increase in liquidity for growing issuers. Similarly, an increased tick would group bids and offers at the nickel rather than spreading them across the existing penny options, facilitating trading volume vital to the health of many emerging companies on the market.

This increased trading volume would benefit issuers and investors alike. The proposing release specifically solicits comments on the investor impact of the pilot, and BIO believes that biotech investors, and investors across various segments of the market, will thrive under a more liquid trading environment. Liquidity is essential for investors to gain benefit from stock ownership, and a successful pilot will stimulate trading activity – increasing the potential upside for investors and preventing them from being trapped holding illiquid stocks.

The proposed tick size pilot program has the potential to stimulate growth among American small businesses and reward the investors who support them. BIO strongly supports the efforts of the SEC and the national exchanges to implement this important reform.

Pilot Program Length

The proposing release solicits comment on whether the pilot period is too long or too short. BIO emphatically believes that, at one year, the program will be far too short to achieve its desired goals.

Trading behaviors are deeply entrenched among the decision-makers targeted by the pilot. Developed over time in response to the existing trading paradigm, these behaviors are embedded in the day-to-day activities of market participants from brokers to bankers, active investors to algorithmic traders, and investors to issuers. The choices made by these market participants are guided by a set of rules and norms that govern the marketplace and inform America's capital formation ecosystem.

The tick size pilot proposes a sea change to the very structure of the market, but gives little to no time for participants to react to that change. BIO's strong belief in the potential for tick size flexibility to positively impact the market is shared by the small cap investment universe, but are market participants with millions of dollars on the line going to spend precious time and resources adjusting their research, algorithms, processes, and behaviors only to have the trading paradigm revert back to the status quo after a year? If it takes two or five or seven months to fully adjust to the new tick size rules, wouldn't it be simpler for a trader to just ignore the whole thing? If the possible benefits of modifying small company tick size – of which BIO believes there are many – are time-limited to half a year or so, is the proposed pilot really going to change anyone's trading behavior?

BIO is deeply concerned that a one-year pilot will really mean that nothing changes for emerging companies. The limited amount of time available for the proposed study will not incentivize new trading behaviors because it is not long enough for the traders to reap any rewards. Absent the financial incentive that would build over time, market makers can just ignore the pilot – or, worse, the small cap market entirely – and wait for the clock to run out. Such a scenario would waste the progress that the SEC, Congress, and industry stakeholders have made on tick size flexibility, returning subpar pilot results and condemning innovative small businesses to continue their struggle against a market structure that benefits large cap stocks at the expense of emerging companies.

Similarly, to the extent that analyst research could support knowledge flow and therefore liquidity for small cap stocks, a one-year pilot program is unlikely to cause a brokerage house to build a research effort to cover stocks that it might previously have ignored. If the market is going to revert to its pre-pilot structure after just a year, there will not be enough incentive to get an expanded small cap research effort off the ground because it will be rendered useless at the end of such a short pilot. Simply put, a one-year study may fall short in terms of providing a true signal as to what market structure would benefit small businesses because it may not provide ample incentives for the appropriate research and trading infrastructure to be built.

BIO believes that the proposed tick size pilot program should last for longer than one year. A three- or five-year pilot would provide enough time for market participants to modify their trading behaviors and give the SEC enough true data to analyze the impact of the proposed tick size change. In order for the pilot to succeed, it must be in existence long enough to incentivize true change and allow investors and issuers alike to fully secure its benefits.

Pilot Structure

The proposing release solicits comment on the necessity of Test Group Two to the pilot. BIO believes that this test group is vital to the pilot's success, and that the SEC and plan participants should maintain it in the finalized program.

It is likely that Test Group One, despite being an important control for the later test groups, will not have much impact on the pilot. Because securities in that test group can be traded at any increment permitted today (despite being quoted at \$0.05), BIO is concerned that trading behavior will not change enough to stimulate the needed liquidity. Traders will continue to operate at the sub-penny margins, once again eschewing trading activity that would support the small cap market.

Test Group Two, on the other hand, puts limits on trading as well as quoting, restricting trades to \$0.05 increments (with certain exceptions). Ideally, these rules will stimulate market-making activity and generate a change in liquidity for the small cap stocks in Test Group Two. Because it will actually test the impact of nickel trading, Test Group Two is essential to the proposed pilot program. BIO believes it should be maintained in the finalized pilot.

Similarly, BIO believes that Test Group Three will provide important information to the SEC and market participants. The proposing release specifically notes that a trade-at requirement, as instituted in Test Group Three, could "stem the possible migration of trading volume away from 'lit' venues to 'dark' venues." BIO members have voiced some concern about the growth of trading in the dark, so testing the impact of trade-at on dark vs. lit trading is an excellent use of the proposed pilot. BIO believes that Test Group Three should maintain its trade-at requirement.

Across all test groups, BIO urges the SEC to be mindful of the impact that short selling could have on the pilot securities. It would be appropriate for the SEC to ensure that its various short selling restrictions apply to the stocks within the pilot program. In particular, BIO believes that Rule 201, restricting short selling when a stock's price has dropped more than 10 percent, is a key protection to maintain. Addressing short selling at the outset of the pilot will go a long way toward ensuring the integrity of the program.

Pilot Data Analysis

BIO applauds the SEC and the plan participants for committing to a full analysis of the pilot results. In any pilot, comprehensive analysis *and concrete action based on that analysis* are vital for success. BIO urges the SEC to study the pilot results closely and, if small cap stocks thrive under the pilot rules, take steps to make the most effective rules permanent.

BIO would also be interested in reviewing the pilot results on an industry-by-industry basis. The JOBS Act, for instance, has had an outsize impact on the biotech industry, and BIO's members would be well-served by a breakdown of the impact of the pilot on various segments of the market.

Regardless of what data analysis efforts the SEC and the exchanges decide to implement, it is vital that they lead to concrete rulemaking action. The exchanges' report to the SEC described in the proposing release will do little good if it sits on a shelf gathering dust while the market readjusts to a one-size-fits-all \$0.01 tick.

Other Issues

As mentioned, BIO strongly supports the SEC in its implementation of a tick size pilot program aimed at increasing the liquidity of small cap stocks. The proposing release also solicits comment on any additional initiatives that the SEC could consider to address the needs of small public companies. BIO urges the SEC to consider proposals to reduce the regulatory burden on emerging innovators, which currently face an array of costly rules leading to a damaging diversion of capital from science to compliance.

For emerging biotech companies, most of which undertake their costly R&D without the benefit of product revenue, expensive and excessive regulatory requirements can slow the research process and delay the development of lifesaving treatments and breakthrough medicines. As such, BIO supports changes to the non-accelerated filer definition and the eXtensible Business Reporting Language (XBRL) reporting regime in order to institute commonsense compliance rules for small businesses.

Currently, SEC Rule 12b-2 caps non-accelerated filers at companies with a public float of \$75 million. These small businesses are subject to a reduced regulatory burden, including an exemption from the costly external auditor attestation requirement in Sarbanes-Oxley (SOX) Section 404(b). However, many biotech companies exceed the \$75 million cap because of their high R&D costs and are therefore forced to pay for an expensive compliance regime, despite their simple corporate structure and lack of product revenue. Changing the non-accelerated filer definition to include companies with a public float up to \$250 million or revenues below \$100 million would institute right-sized regulations for these growing companies and allow them to focus on innovative R&D rather than unnecessary red tape.

Similarly, there are no small company allowances for XBRL reporting, meaning that growing businesses are forced to divert resources to producing complicated, technical reports that are not utilized by investors or regulators. BIO supports an exemption from XBRL compliance for emerging growth companies and other small businesses until the SEC can improve the costly and ineffective reporting mechanism.

BIO applauds the SEC for understanding that there should not be a one-size-fits-all approach to public company regulation. Targeted reforms to the compliance burdens placed on America's small businesses would build on the proposed tick size pilot program by recognizing the unique nature of our nation's emerging innovators and ensuring that capital is available to fund their groundbreaking R&D.

Conclusion

Allowing for tick size flexibility will increase the effectiveness of the public market as a capital formation tool and speed the development of cures and breakthrough medicines. As the JOBS Act continues to spur IPOs in the biotech industry, changes to the current one-size-fits-all trading regime must be made in order to alleviate the ongoing struggle to maintain healthy trading activity in small company stock.

BIO supports an effective tick size pilot program that will enhance small company liquidity, stimulate job creation, and maintain the vital role that public financing plays in the ongoing search for lifesaving therapies.

BIO looks forward to working with the SEC to implement the proposed pilot so that it will spur capital availability, company growth, and next generation research at innovative small



businesses. If you have further questions or comments, please contact me or Charles Crain, Senior Manager of Tax & Financial Services Policy, at (202) 962-9218.

Sincerely,

A handwritten signature in black ink, which appears to read "E. Cartier Esham". The signature is fluid and cursive, with a large initial "E" and a stylized "Esham" that ends in a long, sweeping underline.

E. Cartier Esham
Executive Vice President, Emerging Companies
Biotechnology Industry Organization (BIO)