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Securities and Exchange Commission
100 F St. NW
Washington, DC 20549-9303
Rule-comments@sec.gov

Re: Virtu Petition for Rulemaking on Exchange Listing of Penny Stocks PETN 4-830

Dear SEC:

[1] All opinions are strictly my own and do not necessarily represent those of Georgetown University or anyone else. I am very grateful to Georgetown University for financial support. Over the years I have served as a Visiting Academic Fellow at the NASD (predecessor to FINRA), served on the boards of the EDGX and EDGA stock exchanges, served as Chair of the Nasdaq Economic Advisory Board, and performed consulting work for brokerage firms, stock exchanges, other self-regulatory organizations, government agencies, market makers, industry associations, and law firms. I am the academic director for the FINRA Certified Regulatory and Compliance Professional (CRCP®) program at Georgetown University. I've also visited over 85 stock and derivative exchanges around the world. As a finance professor, I practice what I preach in terms of diversification and own modest and well-diversified holdings in most public companies, including brokers, asset managers, market makers, and exchanges.

- This is a good request and should be addressed quickly.
- Many low-quality IPOs have recently been listed on our exchanges.
- Many dodgy issuers engage in repeated reverse splits.
- These damage index fund investors in our 401-Ks.
- The SEC should require stronger listing standards for IPOs.
- The SEC should require tougher rules around reverse splits
- The SEC should pay more attention to reverse mergers.
- The SEC should be tougher on foreign issuers
- The SEC should be tougher on selling syndicates for defective IPOs.
- The SEC should be nicer to US biotech companies.
- SEC should also begin a measured review of gatekeeping for all assets, from cryptos to crowdfunding to institutional 144A deals.

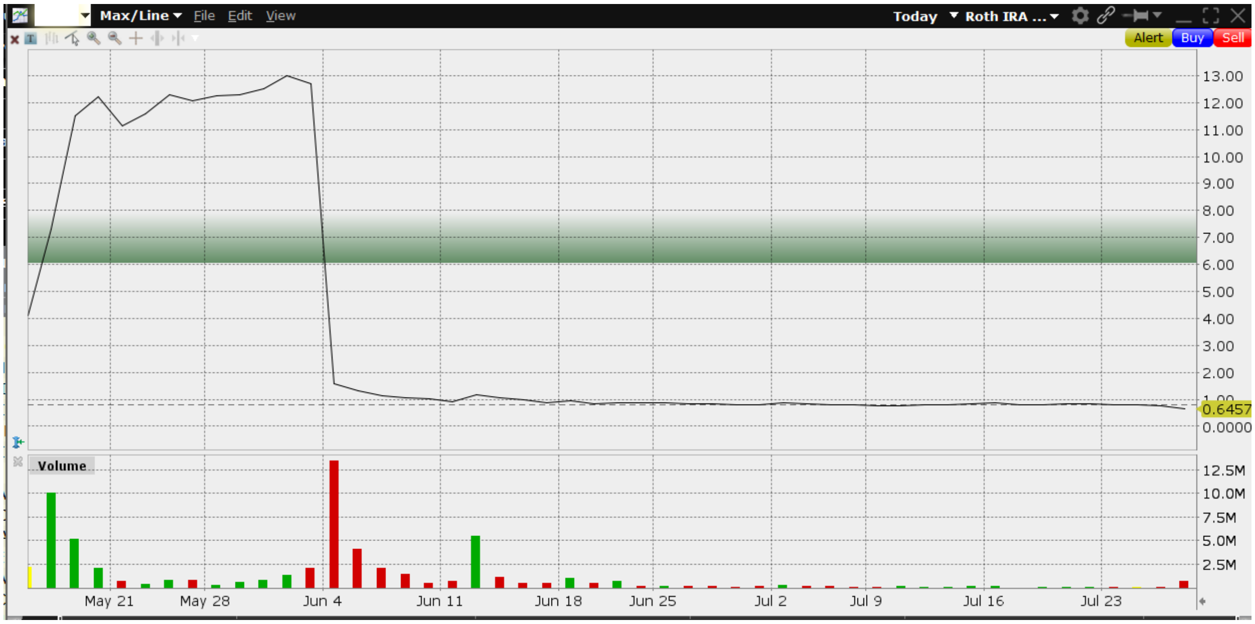
<u>Background</u>

Virtu Financial has submitted a request for rulemaking asking the SEC to clean up the mess in penny stocks that have found their way onto our national securities exchanges. They seek stronger listing standards. I strongly support this request. Cleaning up this mess will do more to protect investors, promote capital formation, and provide for fair and efficient markets than all four of the big 2022 equity market structure proposals combined.

<u>We are experiencing a wave of crappy IPOs!</u>

So far this year through July 26, 2024, we have had 99 IPOs, of which 46 were priced below $10. The median return of those 46 IPOs from their offering date through July 26 has been -31.16%. Nine of them are already selling below $1.00 per share and are in danger of delisting. Only eight (17.4%) of those 46 IPOS are selling above their offering price.

Here is an example: Jiade Ltd, a foreign issuer, went public on May 15, 2024 at $4.00 per share. Within a few days it more than quadrupled to $13 per share, before collapsing down to penny stock levels. Can you say “pump and dump?”



In contrast, of the 53 IPOs priced at $10 and above, the median return through July 26 has been a positive 6.41%. The majority of those IPOs (34, or 64.2%) are selling at or above their offering price.

Something is clearly wrong here. The majority of the low-priced IPOs tank, often on the day of the offering, while the higher-priced ones generally do OK.

Here is another example: Bloomz, Inc., another foreign issuer, went public on July 24 at $4.30. By the end of the day it was in the $2 range.

Clearly, the current listing policies and procedures are not sufficient enough to keep defective offerings from listing on our exchanges.

<u>Index investors are harmed.</u>

It may be tempting to think that the only people harmed are careless idiots who chase after the latest IPO without doing their homework. Unfortunately, the harm is spread much further. In particular, an index fund ends up having to purchase these stocks when they end up in that fund's index. Dodgy companies will wind up in some indices as long as they are listed on our exchanges.

Here is an example. Several very large index funds attempt to track the entire US market. The Vanguard Total Stock Market Index Fund tracks an index that includes all US exchange-listed companies. Among its other holdings, it owns 1,763,201 shares of Next Bridge Hydrocarbons, a non-tradeable spinoff created out of Meta Materials that was itself a reverse merger listing. Meta Materials was involved in an alleged pump and dump scheme that is being prosecuted by the

SEC.[2] Vanguard now reports a value of zero for these now completely illiquid Next Bridge Hydrocarbons shares.

		Shares	Market Value ($000)
*	Clean Energy Technologies Inc.	8,777	9
*,1	Vivakor Inc.	6,500	5
			40,578,370
Total Common Stocks (Cost $706,524,265)			1,595,666,791
Preferred Stocks (0.0%)			
*,1,2	Next Bridge Hydrocarbons Inc. Preference Shares	1,763,201	—

<u>The market's reputation is harmed</u>.

When investors lose money on investments in dodgy companies, they cry that the market is "rigged" and demand revenge. It is all too easy for them to buy into conspiracy theories about the naked short sellers who cavort in dastardly dark pools with the demonic high-frequency market makers from outer space. Investors rightfully demand that regulators and Congress DO SOMETHING. Tightening listing standards and their enforcement is the right SOMETHING to do.

<u>The SEC's reputation is harmed.</u>

One doesn't have to look very hard to see dozens of offensive memes on social media critical of the SEC. Most of them are a result of investors losing money, often when they have been drawn into various market manipulations. The manipulators have become quite good at deflecting blame for investor losses onto other market participants, including regulators. Rather than blame the masterminds of the manipulation schemes, the bag holders often blame the SEC for allowing the manipulation to have occurred as well as for the SEC's lack of visible effort in going after the bad guys.[3]

[2] For more on the background to this soap opera, see https://www.wsj.com/articles/how-the-stock-ticker-mmtlp-became-an-anti-wall-street-rallying-cry-3e2a512a For details of the SEC enforcement case around the reverse merger, see https://www.sec.gov/enforcement-litigation/litigation-releases/lr-26035.

[3] For very good reason, the SEC does not generally comment on the existence or nonexistence of an investigation. This lengthy quiet period creates the impression that the SEC is not doing its fundamental job of enforcing our

Cleaning up the penny stock mess will go a long way to preventing these manipulations and rebuilding the SEC's reputation as an effective regulator.

"Protection of investors" is the core mandate for the SEC. The phrase is mentioned 211 times in the Securities Exchange Act of 1934. To allow this situation to fester is a dereliction of the SEC's fundamental duty to protect investors. The SEC's scarce resources have often been diverted into areas with little benefit to investors to the detriment of its core mandate.

It will be a much more effective use of the SEC's scarce resources to prevent fraud by tightening the rules on listings, reverse mergers, and reverse splits rather than to chase after the miscreants one at a time after the fact.

Toughening the one-dollar rule makes sense, but there needs to be a grace period during times of hardship.

Currently, when the stock price of an exchange-listed company drops below a dollar for a period of time, delisting proceedings begin. The company has a long grace period to take whatever actions are needed, including a reverse split, to retain its exchange listing.

When the share price of a common stock goes down to one dollar, it indicates that something has gone dreadfully wrong with the company. For a $4 penny stock IPO, dropping to one dollar indicates a 75+% drop in the market's valuation of the company's prospects. This can occur for two reasons: The first and most likely is that something is dreadfully wrong with the company's business model. Unless major changes are made, the company is likely to continue to flounder and

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securities laws. As one who has submitted complaints to the SEC about apparent violations of our securities laws, the lack of response and timely follow up to the complainant is very frustrating. The SEC in general does a very poor job of communicating the good reasons behind this policy to complainants or to the general public.

Chair Gensler's flub when asked by Congress about MMTLP was a classic job of poor communication. With 20-20 hindsight, a better response would have been:

"As a matter of policy, the SEC does not comment on specific investigations. Just stating that something is under investigation could cause serious harm to innocent people. For example, suppose that we receive a complaint about a particular Congressman's stock trading that is totally unfounded. Just announcing that we are doing what we are legally bound to do –examine the complaint to assess its validity – could damage an innocent party by putting them under a public cloud of suspicion. Let me assure you we examine every complaint to determine its validity. Then we follow up to the maximum extent our limited resources allow. When there is a serious issue in the market of the type that creates numerous complaints to Congress, we investigate, quietly at first. This does take time to do it right. We understand how frustrating this quiet period can be. We then take whatever public action is in the public interest for the protection of investors. Stay tuned."

eventually perish. There is no reason to prolong the agony for investors or for the company. Flushing such companies off of our exchange in a timelier manner is the right thing to do.

The second possible reason is that something has gone dreadfully wrong with the economy. The one-dollar rule was rightly relaxed after the dot-com bust as well as during the Great Recession in order to prevent mass delisting of otherwise viable firms. For this reason, there should be a mechanism for the exchanges to grant a longer grace period to all firms during times of economic distress.

Maintenance rules should be tougher for reverse split companies.

When a company does a reverse split to avoid delisting, it is a response to a major fall in its share price. As discussed above, this means that something has gone seriously wrong. Just raising more capital is usually not going to fix the problem. It would just throw good money after bad. Serious changes need to be made. A company seeking to do a reverse split to maintain its listing should be required to meet at least all of the standards for a new listing, not just the maintenance standards.

Consideration should be given to making the standards even tougher, both quantitatively and qualitatively. For example, a company engaging in a reverse split should be required to file a new registration statement similar to an S1 that would explain the company's plans to fix the underlying problems with the company.

Be more vigilant with foreign companies.

A casual examination of many of the problem companies reveals that many of them are foreign-based companies. The listing requirements for foreign issuers should have a requirement for independent third-party due diligence to assure that the companies are legitimate and really do meet U.S. listing standards, including internal controls.

Be tougher on the underwriters and the syndicates of low-quality IPOs.

Again, a casual examination of the underwriters for many of the problem IPOs reveals the same names coming up over and over again. The SEC should make it clear that when a dodgy IPO hits the market, the underwriters will immediately experience a long, protracted, and painful proctological examination from the SEC. Similarly, the selling syndicates should also be aware that all its members will experience excruciating scrutiny when they participate in selling crap to investors.

Back in the bad old days, the underwriters of an IPO would "stabilize" or support the price of the offering when it was launched. The usually did this by utilizing the "green shoe" option to sell additional shares (usually up to 15%) of the offering. For example, they would sell 115% of the offering to investors. If the stock rose upon the commencement of trading, the underwriter would exercise the green show option to deliver the 15% of the offering it oversold. Everyone lived happily ever after. If the market price came under pressure, the underwriter could buy back up to the 15% oversold shares to support the price. It was considered a black mark on the reputation of the underwriter for the share price to fall quickly below the offering price.

Apparently, the underwriters of these penny stock IPOs don't care about reputation. The SEC needs to explore how these underwriters are able to continually bring more of these poor offerings to market.

One thing that would be helpful in IPO registration statements (and any marketing material) would be a clear and prominent table or better yet an infographic showing the results of the underwriter's last 10 IPOs.

<u>Be nicer to US biotech companies.</u>

One of the amazing features of our capital markets is how they fund risky research to create modern miracle cures. We now have hundreds of biotech companies that have raised funds through the public markets. Many of them are at the pre-revenue stage. Their ability to make these cures happen is dependent on their ability to raise the enormous sums of money needed to finish the job of getting new treatments through the slow and expensive regulatory process. Many of them have gone through serious ups and downs. Sometimes their stocks fall below a dollar, not because their treatments are not promising, but because they have run low on capital due to the many delays in getting regulatory approval.

The SEC should do all it can to help the many legitimate US biotech companies retain their listings and their access to capital. We are all depending on these biotech firms to create and deliver badly needed treatments for awful diseases.

Take a holistic approach to access to US markets.

We have problems in our capital markets that go well beyond just penny stock IPOs. The cost of compliance has been so great that entire industries have grown up around capital raising methods that avoid full-blown SEC registration. Over the years, an unwieldy agglomeration of exceptions to registration has evolved. We have created, with all good intentions, a wealth-based caste system of who can invest in what. This has the unfortunate unintended consequence of preventing poorer people from building wealth. Rich people get access to the early stages of value creation while the great masses only get access to the exhaust when the VCs exit in an IPO.

The SEC should begin a thorough and holistic review of access to our markets, and the types of protections needed for different groups of investors. Technology has changed dramatically since the passage of the 1933 Act, but regulatory thinking has not. We need to figure out how to use technology to cut compliance costs while improving investor protection. The old caste system is obsolete and needs to be re-engineered for the modern world.

Care is needed, as delisting affects the ability of firms to raise additional capital.

Capital formation is an important statutory mandate of the SEC. When a company is delisted from an exchange, it becomes harder and more expensive for that company to raise capital. The SEC thus has to balance the need to protect investors with the need to promote efficiency, competition, and capital formation. The SEC needs to be very careful to make sure that it does not make it harder and more expensive for legitimate productive enterprises to grow in our capital markets.

Access to our capital markets should be the same for IPOs, SPACs, and reverse mergers.

The SEC also needs to pay close attention to why companies seek to access our capital markets through artifices such as reverse mergers and SPACs rather than traditional offerings. The reasons generally come down to cost, speed, and disclosure requirements. Differences in the requirements create a fertile ground for regulatory arbitrage. Since the end result is the same, the cost, speed, and disclosure requirements should be the same.

The SEC should pay attention to the high cost of public listings.

The SEC has always faced a painful dilemma. Protecting investors involves rules and required compliance activities. This required compliance costs money and drives up the cost of being a public company. Higher costs raise the threshold at which the public markets become open to issuers, raising the cost of capital for the small and growing enterprises that we depend upon to grow the economy and create jobs.

The SEC has struggled over the years to create less costly compliance regimes for smaller issuers that still provide sufficient communication (notice I am not saying disclosure) to investors

Just because it is difficult to come up with cost-effective compliance regimes for smaller issuers does not mean that the SEC should not try. Congress has mandated this in SBREFA. These considerations need to be part of the fundamental thinking of any potential rule or policy change.

More "disclosure" is not the answer. Communication is.

If all you have is a hammer, then everything looks like a nail. The general theme of US securities regulation is "disclosure." As long as investors have complete information, they should be able to make up their own minds. This sounds good in theory. Some would say that as long as investors are informed, they should be able to buy any piece of crap they want. I am very sympathetic to this view.

However, the disclosure-is-all-we-need paradigm evolved in a time when information was scarce and very expensive to transmit or obtain. We now live in a world in which we are drowning in data. The miscreants take advantage of this data overload and bury required disclosures in an ocean of legalbabble. When was the last time *you* read a prospectus or 10-K from cover to cover?

The investor protection focus needs to be on both *communicating* relevant material information to investors and ensuring that the information they do receive is complete and not misleading. This has to apply to both official channels such as SEC filings and unofficial channels such as social media.

Conclusion

The SEC should move quickly to address the current problem with defective IPOs. Listing procedures for IPOs have to be improved, and quickly. Companies seeking to do a reverse split to stay listed should be required to go through an S1-type registration process demonstrating the changes it will make.

However, the SEC must not stop there. It needs to think holistically about how different kinds of issuers access the various segments of the US capital markets with an eye towards modernizing our regulatory processes. It should move methodically with a series of round tables to generate needed input before attempting any rulemaking.

Respectfully submitted,

James J. Angel,

Georgetown University