



# **2014 SEC Government-Business Forum on Small Business Capital Formation**

**Secondary Market Liquidity for Securities of Small Businesses**

November 20, 2014

- Problem: Market structure presents challenges for the trading of small companies
- Solution: Develop more hospitable trading market for small companies
- Catalyst: Change in SEC regulatory policy
- Beneficiary: Pool of small companies nurtured by new trading market

# Market Structure Presents Challenges for the Trading of Small Companies

- Today's trading market is inhospitable for small companies
  - High Frequency Trading
    - (*Flash Boys*, Brad's problem bedevils small companies)
  - Stock exchange companies' share of revenue earned from US trading of small capitalization stocks is minuscule!
    - No economic incentive to foster development of new market
  - Decimalization disincentivized market makers from making markets
- Solution requires a “Mindshift” in SEC regulatory policy

# Develop a More Hospitable Trading Market for Small Companies

- Choice for new trading market: national securities exchange or alternative trading system
  - Each requires policy accommodation
- Mindshift in SEC regulatory policy is key to solution
  - SEC policy accommodation can spur private sector development of hospitable trading market
- SEC can signal to market participants:
  - It is open to rethinking Regulation NMS as it relates to new trading market
    - Not the only framework that can achieve policy goals (i.e fair, orderly and transparent trading markets)
  - It invites market participants to advance trading technology solutions that achieve policy goals

## Pool of small companies nurtured by new trading market

- Need critical mass of small public companies to incentivize development of new trading market
  - Regulation A+ Tier 2 issuers with periodic and current reporting obligations under proposed Rule 257(b) should be conditionally exempt from Section 13(a) reporting
    - Allows ongoing reduced disclosure avoiding the significant disclosure burdens of Section 12 registrants
  - Allow OTC Section 12 registered small emerging growth companies (defined as companies with less than \$250 million in revenues) to migrate to the Regulation A+ reporting system
  - Allow listed Section 12 registered small emerging growth companies to delist and migrate to the Regulation A+ reporting system

# Eliminate Blue Sky Restraint on Trading of Regulation A+ Tier 2 Issuers

- Development of a liquid trading market for Regulation A+ Tier 2 Issuers will be impeded unless resale trading benefits from preemption of Blue Sky qualification and registration laws
  - Regulation A+ Tier 2 issuers subject to periodic and current reporting obligation pursuant to proposed Rule 257(b) should benefit from preemption
  - SEC should expand the proposed definition of “qualified purchaser” to include any offeree/purchaser of a security offered and sold pursuant to Securities Act Section 4(a)(1) or (3), provided that, the issuer is current in its periodic and current reporting obligations under proposed Rule 257(b)

- Recommendation 1
  - The SEC’s should adopt exemptions to permit existing Section 12(g) registrants and Section 15(d) filers that qualify as smaller emerging growth companies (defined as companies with less than \$250 million in revenues) to migrate to the periodic and current reporting system implemented for Regulation A+ Tier 2 issuers under proposed Rule 257(b).
- Recommendation 2
  - SEC should expand the category of the proposed “qualified purchaser” to include any purchaser of a class of security which has been offered and sold pursuant to Section 4(a)(1) or (3), provided that, the issuer is a Regulation A+ Tier 2 reporting issuer under proposed Rule 257(b); or alternatively, the SEC should seek any necessary legislation to implement Blue Sky preemption for trading of Regulation A+ Tier 2 offered securities.