February 2, 2021

Ms. Vanessa A. Countryman
Secretary
U.S Securities and Exchange Commission
100 F. Street, NE
Washinton, DC 20549

Subject: SR-NASDAQ-2021-045 Notice of Filing of Proposed Rule Change, as Modified by Amendment No. 2, to Modify Certain Pricing Limitations for Companies Listing in Connection with a Direct Listing Primary Offering

Dear Ms. Countryman,

I am writing to express my strong support for the Nasdaq's proposed rule changes that would facilitate a Direct Listing with a primary capital raise. I have spent the past two decades as a venture capitalist at Benchmark and have had the good fortune to work with many great companies on their Initial Public Offerings. Prior to my career as a venture capitalist, I spent four years working on Wall Street as a sell-side equity analyst, including having a front row seat on the Amazon IPO. These experiences have given me a unique lens to see many facets of the IPO process and to see them from multiple points of perspective. As I will discuss further, adding a primary capital raise to the Direct Listing would represent a major step forward in the efficiency and openness of the U.S. capital markets, as well as solve a key "conflict of interest" problem that has not only festered but has unfortunately become much worse over the past several years.

There are two fundamental flaws with the current U.S. IPO process which are both addressed with the Direct Listing. First, the IPO process does not use a market mechanism to determine price or allocation to shareholders. An agent with a clear conflict of interest is charged with choosing both price and allocation. Second, and equally troubling, only a handful of the largest institutional investors are given access to even participate in the IPO. Most professional investors and nearly all retail clients are left completely out of the process. The retail clients that are invited to participate in a standard IPO are simply the high-net-worth clients of the underwriters.

As a result of these limitations, conflicts, and lack of availability to all investors, the inefficiencies in the IPO process are quite extraordinary. Based on data aggregated by Professor Jay Ritter at the University of Florida, over the past 41 years and across 9,084 IPOs, first-day underpricing has resulted in $229.72 billion "left on the table" from corporate issuers.

Unfortunately, this problem has been getting worse. In the past two years alone, these underwriter-orchestrated "pops" have totaled $57.64 billion in one-day wealth transfers to those lucky enough to participate in the IPO process. This represents an average of $121 million underpricing/wealth-transfer for each of the 474 IPOs in 2020 and 2021. In 2020, the average IPO was underpriced by 47.9%. These numbers are not congruent with the SEC objective of "efficient markets."

What is the systemic problem here? As mentioned, there are two key issues: that pricing/allocation is done without the use of a market mechanism and that preferential treatment is given to only a handful of potential buyers. When one looks at the structure of the market and the current IPO process, this mispricing and inefficiency should be expected. In a normal IPO process, there are

three constituents: (1) the issuing company and its investors, (2) the institutional investors that are prospective buyers of the offering, and (3) the underwriter. With this structure, the underwriter is asked to serve as an impartial “agent” for both the issuing company and potential investors at the same time -- an arguably impossible task. In what other high dollar value transaction does a single agent represent both sides? This multi-agency risk is well understood in the economic literature, and a conflict of interest should be assumed as a result.

During the dot-com boom (1999-2001) many journalists and regulators became concerned about conflicts that arose from underwriters giving “hot-stock” to executives at companies in Silicon Valley. This practice — also labeled “spinning” — was considered by all to be an obvious conflict of interest. What is remarkable is that giving this same “hot-stock” to institutional investors in much larger allocations has not to date raised the same red flags. *But why not?* We all know that underwriters have an alternate business relationship with these same institutional investors through Prime Brokerage services. In 2019, Morgan Stanley CFO Jonathan Pruzan noted, “Prime brokerage is our biggest business,” and “It’s the centre of the machine, if you will...It’s a very strong and powerful business.” The importance of Prime Brokerage is a much stronger argument for conflict between the underwriter and the institutional investor than there ever was between the executive and the underwriter. In 2020, each of the 165 IPOs represented $121 million in one-day gains for the underwriter’s institutional clients. Over the course of that same year, $29.66 billion was passed to these “allocated” investors in one-day gains. That is a staggering amount of money and clear opportunity for conflict. One could also argue that this reality even distorts the efficiency of the Prime Brokerage market itself.

The inefficiency and mispricing of the traditional IPO has become much worse over the last decade. When I worked on Wall Street 20 years ago, the equity sales force at a leading Wall Street bank was 10 times the size that they are today. In those days when an investment bank pitched for an IPO mandate, they highlighted their prowess in “marketing and distribution.” They would brag about the large number of accounts you could “get your story in front of.” In a modern IPO, they focus on as few as 20-30 core accounts. The CEO and CFO are also told they have two key objectives — to secure a 30x over-subscription in the order book and to have a 90%+ commitment hit rate for 1-1 meetings. I would encourage you to ask around, as this is the current “best practice.” It should be quite evident that running a process where your starting plan is to ignore 97% of demand (this is the 29/30 overage) will result in systemic underpricing. This process is clearly failing the corporate issuers.

Some people would argue that the corporate CEO and CFO should be more experienced than to be taken advantage of this way. As someone that has watched this process many times, I would offer the following perspective. Most CEO and CFOs go public once in their career. They rely heavily on the advice they are given from both underwriters and institutional investors. The underwriters and investors may work on 20-40 offerings a year. This lopsided experience mismatch is remarkably hard to overcome. Occasionally you will have an experienced player on the corporate side, as you did with Barry McCarthy on the pioneering Spotify Direct Listing, but it is very rare. Additionally, once a company is “in the process” they are very reluctant to go against the advice of the underwriter. They would rather settle for being underpriced than risk the stigma of a “pulled deal.” The uniqueness and importance of this critical corporate event creates immense leverage for an advisor.

Thankfully, there is now a super-efficient and elegant way to go public that avoids these two key problems — the Direct Listing. With the Direct Listing, pricing and allocation are both determined by the blind eye of the market. No one party has an “advantage” in the process because everyone is on a level playing field. Additionally, because the Direct Listing process leverages existing brokerages systems, the new issue opportunity is open to ANY and ALL shareholders. You can

have an account on Schwab, E-Trade or Robinhood, and if you bid a $0.01 over the settled price, you are 100% guaranteed to be filled. This seems highly consistent with the SEC's interest in empowering individual investors. With a traditional IPO, the retail investor has zero chance at getting allocation in the IPO. In fact, they are more likely to set the "pop" price on the next day open and may even "top-tick" the market. The Direct Listing puts Joe Investor on an equal footing with the likes of Fidelity. Also, because the price discovery and allocation process are "blind" to the names of the bidding investors, the Direct Listing is outside the bias of agency. This is the ultimate in fairness. All conflict is avoided.

Many will make the argument that supporting Direct Listings is supporting innovation. I cannot make that claim, but I *would* argue the Direct Listing is a massive improvement and makes unquestionable progress against the traditional IPO. The reason it cannot be called innovative is these electronic matching systems are not new. Electronic order matching systems were first used in the 1980s, over 40 years ago. The Midwest Stock Exchange first launched the "MAX system" in 1982. The price-time allocation algorithm inherent in the Direct Listing has been used for decades. These processes were innovative years ago, they simply have not been applied to this process until now. To be clear, it would represent massive progress to bring these proven tools to the public offering process.

Notably, the electronic processes behind the Direct Listing are "tried and true." They have been tested and optimized for years and years. All stocks open every day with this same process. When a company "spins out" a division through a stock-dividend, price is determined with this same process. And perhaps most ironically, the very next day after a traditional IPO, the "true" market price is determined with the exact Direct Listing process. That's right — every company that does a traditional IPO in effect does a Direct Listing the very next morning. The day after an IPO placement, when you are waiting for the company to "open," that is what is happening. Interestingly, this means doing a Direct Listing has fewer steps than a traditional IPO. You simply skip the part where the conflicted agent makes pricing and allocation decisions.

One quick note on some of the objections brought against Direct Listings. Almost all the objections involve esoteric differences in the two process that are completely off the radar of a typical CEO or CFO. I can assure you that no founder is choosing or has chosen a Direct Listing to take advantage of these small esoteric differences. They simply want a market approach and an open approach. I would urge the Commission to find a way to have "parity" on these issues relative to a traditional IPO. Stopping the progress to a more elegant approach for these reasons really would be "throwing the baby out with the bath water."

Lastly, I want to touch on the critical importance of supporting a primary capital raise with an efficient Direct Listing process. The number one reason I hear that CEOs and CFOs are still choosing a traditional IPO over a Direct Listing is the need to raise capital. As such, adding this key feature will have a profound impact on all the issues I herein outlined. Based on numerous discussions with those on the front lines, there are zero concerns about the technical implementation of such a feature. Currently, regulatory support is the critical limiting factor.

I sincerely appreciate your consideration of these comments. If you would like more information, or if I can be helpful in any way, please feel free to contact me at your convenience.

Sincerely,

Bill Gurley
General Partner
Benchmark