

February 29, 2024

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

Hon. Gary Gensler, Chair
Hon. Hester Peirce, Commissioner
Hon. Caroline Crenshaw, Commissioner
Hon. Mark Uyeda, Commissioner
Hon. Jaime Lizarraga, Commissioner

Securities and Exchange Commission
100 F Street, NE
Washington, DC 20549-1090

Re: File No. SR-Phlx-2024-04; File No. SR-BX-2024-004; and File No. SR-NASDAQ-2024-005¹

Dear Commissioners:

The Healthy Markets Association² writes to object to the Nasdaq Penny Stock Tiering Proposal,³ which has purportedly already been implemented on the Nasdaq Stock Market LLC, Nasdaq BX Inc., and Nasdaq PHLX LLC. The Nasdaq Penny Stock Tiering Proposal did not include sufficient data or analysis with which the Commission could conclude that the filing complies with the Exchange Act or Commission Rules, and therefore should be suspended and disapproved.

¹ Notice of Filing and Immediate Effectiveness of Proposed Rule Change to Amend Equity 7, Section 3(a), SEC, Exch. Act Rel. No. 99537, Feb. 14, 2024, available at <https://www.sec.gov/files/rules/sro/phlx/2024/34-99537.pdf>; Notice of Filing and Immediate Effectiveness of Proposed Rule Change to Amend Equity 7, Section 118, SEC, Exch. Act Rel. No. 99534; File No. SR-BX-2024-004, Feb. 14, 2024, available at <https://www.sec.gov/files/rules/sro/bx/2024/34-99534.pdf>; and Notice of Filing and Immediate Effectiveness of Proposed Rule Change to Amend Equity 7, Section 118, SEC, Exch. Act Rel. No. 99535, Feb. 14, 2024, available at <https://www.sec.gov/files/rules/sro/nasdaq/2024/34-99535.pdf> (collectively, “Nasdaq Penny Stock Tiering Proposal”).

² The Healthy Markets Association is a not-for-profit member organization focused on improving the transparency, efficiency, and fairness of the capital markets. Healthy Markets promotes these goals through education and advocacy to reduce conflicts of interest, improve timely access to market information, modernize the regulation of trading venues and funding markets, and promote robust public markets. Its members include public pension funds, investment advisers, broker-dealers, exchanges, and data firms. To learn about HMA or our members, please see our website at <http://healthymarkets.org>.

³ HMA submitted two prior comment letters detailing specific concerns with the ADF Proposal. Letter from Tyler Gellasch, HMA, to Vanessa Countryman, SEC, Jan. 13, 2023, available at <https://www.sec.gov/comments/sr-finra-2022-032/srfinra2022032-20154755-323003.pdf> (“First HMA Letter”); Letter from Tyler Gellasch, HMA, to Vanessa Countryman, SEC, Mar. 14, 2023, available at <https://www.sec.gov/comments/sr-finra-2022-032/srfinra2022032-20159679-327732.pdf> (Second HMA Letter”).

Standard of Commission Review and Consideration

The Commission is obligated to review exchange filings and determine that those filings are consistent with the Exchange Act,⁴ including that an exchange's rules:

- “provide for the equitable allocation of reasonable dues, fees, and other charges;”⁵
- not be “designed to permit unfair discrimination”;⁶
- “not impose any burden on competition not necessary or appropriate in furtherance of the purposes of” the Act;⁷ and
- be designed “to protect investors and the public interest.”⁸

As the Commission has previously acknowledged:

Rule 700(b)(3) of the Commission's Rules of Practice states that the “burden to demonstrate that a proposed rule change is consistent with the [Exchange Act] and the rules and regulations issued thereunder . . . is on the self-regulatory organization that proposed the rule change” and that a “mere assertion that the proposed rule change is consistent with those requirements . . . is not sufficient.” Rule 700(b)(3) also states that “the description of a proposed rule change, its purpose and operation, its effect, and a legal analysis of its consistency with applicable requirements must all be sufficiently detailed and specific to support an affirmative Commission finding.” Any failure of an SRO to provide this information may result in the Commission not having a sufficient basis to make an affirmative finding that a proposed rule change is consistent with the Exchange Act and the applicable rules and regulations. **Moreover, “unquestioning reliance” on an SRO's representations in a proposed**

⁴ See *Susquehanna Int'l Grp., LLP v. SEC*, 866 F.3d 442 (D.C. Cir. 2017) (“The SEC “shall approve” a self regulatory organization’s proposed rule change only “if it finds that such proposed rule change is consistent with” provisions of the Exchange Act.”). *Accord*, Remarks of Brett Redfearn, SEC, before the SEC Roundtable and Market Access and Market Data, Oct. 26, 2018, *available at* <https://www.sec.gov/news/public-statement/statement-redfearn-102518> (declaring that in order for the Commission to “meet our obligations under the Exchange Act, we also need to ensure that the fees that are being charged for such important market services are fair and reasonable, not unreasonably discriminatory, and do not impose an undue or inappropriate burden on competition.”).

⁵ 15 U.S.C. § 78f(b)(4).

⁶ 15 U.S.C. § 78f(b)(5).

⁷ 15 U.S.C. § 78f(b)(8).

⁸ 15 U.S.C. § 78f(b)(5).



rule change is not sufficient to justify Commission approval of a proposed rule change.⁹

Proposal

At root, the Nasdaq Penny Stock Tiering Proposal would distinguish trading volumes in penny stocks from other NMS stocks, and offer preferential pricing tiers based upon adjusted aggregated volumes. As Nasdaq explained in its notice to trading firms on January 31st:

Starting February 1, 2024, the Nasdaq Exchanges will evaluate the two calculations below in determining a member's qualification for all Add equity pricing tier/incentives and will apply the most advantageous pricing tier/incentives for which the member qualifies:

1. Firm or MPID's volumes expressed as a percentage of Total Consolidated Volume inclusive of volume pertaining to securities priced below \$1
2. Firm or MPID's volumes expressed as a percentage of Total Consolidated Volume exclusive of volume pertaining to securities priced below \$1 and increasing the distinct volume percentage thresholds (as set forth in Equity 7, Section 118(a) [Nasdaq and BX] / Equity 7, Section 3(a)(1) [PSX]) by 10%

In attempting to explain why it made the filing to the Commission, Nasdaq asserted that:

Anomalous rises in sub-dollar volume stand to have a material adverse impact on members' qualifications for pricing tiers/incentives because such qualifications depend members upon achieving threshold percentages of volumes as a percentage of Consolidated Volume, and an extraordinary rise in sub-dollar volume stands to elevate Consolidated Volume. As a result, members may find it more difficult, if not practically impossible, to qualify for or to continue to qualify for their existing incentives during months where there are such rises in sub-dollar volumes, even if their dollar plus volumes have not diminished relative to prior months.

⁹ *Order Disapproving Proposed Rule Change To Introduce a Liquidity Provider Protection Delay Mechanism on EDGA*, SEC, Exch. Act Rel. No. 34-88261, Feb. 21, 2020, available at <https://www.sec.gov/files/rules/sro/cboeedga/2020/34-88261.pdf> (emphasis added) (citing 17 C.F.R. § 201.700(b)(3)).

The Exchange believes that it would be unfair for its members that execute significant dollar plus volumes on the Exchange to fail to achieve or to lose their existing incentives for such volumes due to anomalous behavior that is extraneous to them. Therefore, the Exchange wishes to amend its Rules to help avoid extraordinary spikes in sub-dollar volumes from adversely affecting a member's qualification of incentives for their dollar plus stock executions.¹⁰

Analysis

The Nasdaq Penny Stock Tiering Proposal is yet another exchange filing that lacks basic information that would be essential to understand its impact.

While the Proposal acknowledges the “anomalous rise” in sub-\$1 stock trading, it declines to offer any explanation of it, or how it impacts trading on the venue. We can speculate that Nasdaq may want to avoid the topic, however, given the reality that so many of these penny stocks are, in fact, listed on Nasdaq.¹¹ And while we think that its role in listing and trading in companies with very low dollar prices should give rise to separate, independent Commission investigations and examinations (including for compliance with its obligations under the Exchange Act), Nasdaq cannot reasonably avoid the topic when it is expressly changing its trading tier pricing as a result.

At face value, the filing appears to be customized to benefit a select customer or customers of Nasdaq, who are themselves not identified. We may speculate that the filings would benefit one or more of Citadel and Virtu Financial, but we do not know. The number or nature of the obviously very small number of firms that would benefit from the Proposal are not identified.

And while the Proposal would clearly confer preferential pricing upon these favored firms, the Proposal does not explain whether it expects the new tiering thresholds to change routing behavior or execution quality, or what the impact of the change is expected to be. For example, does Nasdaq expect the Proposal to lead to more penny stock trading on Nasdaq, or in the markets overall? Other than one or more firms not enjoying greater incentives, what has been the impact on Nasdaq or the markets of the rise in sub-dollar price stock trading? For example, did the targeted customer or customers of Nasdaq change their routing behavior to route to other venues? Has that impacted the execution quality of trading on Nasdaq for those securities? How about any impacts on trading volumes or execution quality in other securities, given that the

¹⁰ Proposal, at 3

¹¹ Alexander Osipovich, *As Trading Frenzies Grip Penny Stocks, Criticism of Nasdaq Grows*, Wall St. Journal, Feb. 23, 2024, available at <https://www.wsj.com/finance/stocks/as-trading-frenzies-grip-penny-stocks-criticism-of-nasdaq-grows-8bd4118b>.



volumes are all aggregated? We are not aware of any discernible variations during the period prior to this Proposal that would provide any evidentiary support to the Proposal's necessity – other than a desire by Nasdaq to offer an undisclosed, but clearly targeted firm or firms – preferential treatment.

Notably, HMA is not aware of prior communications to the vast majority of market participants regarding this fee change prior to it being first communicated to the public just hours before it went into effect.¹² If this was an issue that was intended to impact the pricing of a significant number of firms, of course, we would expect the exchange to communicate that change broadly. It did not. To the contrary, it likely only notified the customers that were specifically targeted for the preferential treatment.

As we have shared with the Commission before, we believe that not just written, but rather a summary of all communications between an exchange and its customers related to transaction pricing prior to a filing that is intended to impact those customers should be included in the filing itself, as it would provide essential context for regulators and other market participants. And while the Commission's Rules require exchanges to include prior written communications, Nasdaq has declined in the filing to include any reference to any of its pre-filing discussions with its intended impacted customer or customers. The Commission should insist on this extremely important information.

Apart from providing the Commission with an informed basis to understand what is motivating the Proposal, without this additional basis, we do not see how Nasdaq could reasonably conclude, as it purports to have done, that the change will not have a material impact on competition and will not unreasonably discriminate among its members.

Ultimately, Nasdaq has failed to provide any data about how the rise of sub-penny trading has impacted its operations or the markets, as well as any analysis or predictions about the potential impact of its Proposal. If the filing is to comply with the Exchange Act and Commission Rules, it must. But further, the Commission itself cannot simply rely on that information, either. The Commission must itself have command of the relevant facts and analysis in order to fulfill its own duties. None of this is evidenced in the scant record.

Titling Filings With Obscure References Reduces Transparency and Engagement

Lastly, we were disappointed that the Commission submitted the proposed rule change under title that references the obscure section of Nasdaq's rulebook that would be amended, as opposed to the substance of the change. The title of the filing put out for comment by the Commission staff obfuscates the substance of the filing, and makes it

¹² Nasdaq, *Equity Trader Alert #2024 - 10*, Jan. 31, 2024, available at <https://www.nasdaqtrader.com/TraderNews.aspx?id=ETA2024-10>.



materially less likely for market participants or commenters to quickly scan the filing and have any reasonable understanding of what it does.

The title of the release “*Notice of Filing and Immediate Effectiveness of Proposed Rule Change to Amend Equity 7, Section 3(a)*,” could easily be adjusted to read in plain language, “... to Amend Aggregate Volume Calculations for Pricing Tiers.” The latter format would allow commenters who do not know, off the top of their heads, what “Equity 7, Section 3(a)” of the Nasdaq Rulebook is. Further, a revised title should also inform the reader and public of the nature of the change.

We at HMA read all the filings of the exchanges, and we quickly try to sort and analyze them so that we may share information with our members and subscribers. Clearly identifying the substance of the rule change in the title of the release – as has been done for years – helps us and others navigate the deluge of dozens of filings each month. Removing that information, and instead just referencing numeric sections of the rulebook being modified, makes the review and analysis of filings much more time consuming and error-prone. Put simply, we are more likely to miss important filings because we are unfamiliar with the obscure references.

We urge the Commission to revise the titles of its releases to ensure that market participants and experts can have a reasonable basis to understand what a proposal would do, based upon its plain language title.

Conclusion

Given the paucity of information provided by Nasdaq, the Commission has no choice but to suspend and disapprove the Nasdaq Penny Stock Tiering Proposal. Further, if Nasdaq seeks to refile the proposal or something similar, the Commission should ensure that such proposal is thoroughly assessed and found to be consistent with the Exchange Act and Commission Rules prior to its implementation.

If you have any questions, please contact me at (202) 909-6138 or ty@healthymarkets.org. Thank you for your consideration.

Sincerely,

President and CEO
Healthy Markets Association