

SECURITIES AND EXCHANGE COMMISSION  
(Release No. 34-88315; File No. SR-NASDAQ-2019-091)

March 4, 2020

Self-Regulatory Organizations; The Nasdaq Stock Market LLC; Order Instituting Proceedings To Determine Whether To Approve or Disapprove a Proposed Rule Change To Adopt a New Rule Concerning Nasdaq's Ability To Request Information From a Listed Company Regarding the Number of Unrestricted Publicly Held Shares in Certain Circumstances and Halt Trading in the Company's Security Upon the Request, and in Certain Circumstances Request a Plan To Increase the Number of Unrestricted Publicly Held Shares To an Amount That is Higher Than the Applicable Publicly Held Shares Requirement

I. Introduction

On November 22, 2019, The Nasdaq Stock Market LLC ("Nasdaq" or the "Exchange") filed with the Securities and Exchange Commission ("Commission"), pursuant to Section 19(b)(1) of the Securities Exchange Act of 1934 ("Act")<sup>1</sup> and Rule 19b-4 thereunder,<sup>2</sup> a proposed rule change to adopt a rule specifying Nasdaq's ability to request information from a listed company regarding the number of unrestricted publicly held shares when Nasdaq observes unusual trading characteristics in a security or a company announces an event that may cause a contracting in the number of unrestricted publicly held shares, halt trading in such company's securities upon such a request, and potentially request a listed company to increase its number of unrestricted publicly held shares. The proposed rule change was published for comment in the Federal Register on December 12, 2019.<sup>3</sup> On January 24, 2020, pursuant to Section 19(b)(2) of the Act,<sup>4</sup> the Commission designated a longer period within which to either approve the proposed rule change, disapprove the proposed rule change, or institute proceedings to determine

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<sup>1</sup> 15 U.S.C. 78s(b)(1).

<sup>2</sup> 17 CFR 240.19b-4.

<sup>3</sup> See Securities Exchange Act Release No. 87677 (December 6, 2019), 84 FR 67974 (December 12, 2019) ("Notice").

<sup>4</sup> 15 U.S.C. 78s(b)(2).

whether to disapprove the proposed rule change.<sup>5</sup> The Commission received no comment letters on the proposed rule change. This order institutes proceedings under Section 19(b)(2)(B) of the Act<sup>6</sup> to determine whether to approve or disapprove the proposed rule change.

## II. Description of the Proposal

Nasdaq's current continued listing standards require a listed company to maintain a minimum number of Publicly Held Shares,<sup>7</sup> without excluding Restricted Securities<sup>8</sup> from such calculation.<sup>9</sup> In contrast, for initial listing, Nasdaq's current rules, as amended in 2019,<sup>10</sup> require that a company seeking to be listed on Nasdaq have, among other things, a minimum number of Unrestricted Publicly Held Shares.<sup>11</sup>

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<sup>5</sup> See Securities Exchange Act Release No. 88028 (January 24, 2020), 85 FR 5500 (January 30, 2020). The Commission designated March 11, 2020, as the date by which it should approve, disapprove, or institute proceedings to determine whether to disapprove the proposed rule change.

<sup>6</sup> 15 U.S.C. 78s(b)(2)(B).

<sup>7</sup> "Publicly Held Shares" is defined as "shares not held directly or indirectly by an officer, director or any person who is the beneficial owner of more than 10 percent of the total shares outstanding." See Rule 5005(a)(35).

<sup>8</sup> "Restricted Securities" is defined as "securities that are subject to resale restrictions for any reason, including but not limited to, securities: (1) acquired directly or indirectly from the issuer or an affiliate of the issuer in unregistered offerings such as private placements or Regulation D offerings; (2) acquired through an employee stock benefit plan or as compensation for professional services; (3) acquired in reliance on Regulation S, which cannot be resold within the United States; (4) subject to a lockup agreement or a similar contractual restriction; or (5) considered 'restricted securities' under Rule 144." See Rule 5005(a)(37).

<sup>9</sup> See proposed Rule 5120. See also Notice, *supra* note 3, 84 FR at 67974. For the continued listing requirements relating to Publicly Held Shares, see Rules 5450(b)(1)(B), (2)(B), and (3)(B), 5460(a)(1), 5550(a)(4), 5555(a)(3), and 5565(a).

<sup>10</sup> See Securities Exchange Act Release No. 86314 (July 5, 2019), 84 FR 33102 (July 11, 2019) (SR-NASDAQ-2019-009) (approving Nasdaq's proposal to, among other things, require that Restricted Securities be excluded from Nasdaq's calculation of Publicly Held Shares for purposes of meeting initial listing requirements).

<sup>11</sup> "Unrestricted Publicly Held Shares" is defined as "Publicly Held Shares that are Unrestricted Securities." See Rule 5005(a)(45). "Unrestricted Securities" is defined as

Nasdaq has proposed to adopt new Rule 5120, which would provide that, while Nasdaq would not ordinarily consider the number of Unrestricted Publicly Held Shares of a listed company's security, Nasdaq may request information from a company regarding the number of Unrestricted Publicly Held Shares if (1) Nasdaq observes unusual trading characteristics in the security; or (2) the company has announced an event that may cause a contraction in the number of Unrestricted Publicly Held Shares.<sup>12</sup> Proposed Rule 5120 also sets forth that pursuant to Nasdaq's authority under Rule 4120(a)(5),<sup>13</sup> Nasdaq may halt trading in the security in connection with such a request.<sup>14</sup> When considering whether a security has unusual trading characteristics, the proposed rule provides that Nasdaq may review volume, price movements, spread, and the presence or absence of any news.<sup>15</sup> Furthermore, the proposed rule specifies the events that may cause a contraction in the number of Unrestricted Publicly Held Shares, thereby possibly triggering a request for additional information, to include reverse stock splits, tender offers, stock buybacks, or entering into contractual agreements such as standstills or lockups.<sup>16</sup>

Further, proposed Rule 5120 provides that if information provided by the company or otherwise obtained by Nasdaq indicates that the number of Unrestricted Publicly Held Shares for

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“securities that are not Restricted Securities.” See Rule 5005(a)(46). For the initial listing requirements relating to Unrestricted Publicly Held Shares, see Rules 5315(e)(2), 5405(a)(2), 5415(a)(1), 5505(a)(2), 5510(a)(3), and 5520(g)(3).

<sup>12</sup> See proposed Rule 5120.

<sup>13</sup> Rule 4120(a)(5) provides that Nasdaq “may halt trading in a security listed on Nasdaq when Nasdaq requests from the issuer information relating to: (A) material news; (B) the issuer’s ability to meet Nasdaq listing qualification requirements, as set forth in the Listing Rule 5000 Series; or (C) any other information which is necessary to protect investors and the public interest.”

<sup>14</sup> See proposed Rule 5120.

<sup>15</sup> See proposed Rule 5120.

<sup>16</sup> See proposed Rule 5120.

the security is below the applicable Publicly Held Shares requirement for continued listing of the security, Nasdaq generally would use its authority under Rule 5101<sup>17</sup> to apply more stringent criteria and request a plan to increase the number of Unrestricted Publicly Held Shares to an amount that is higher than the applicable Publicly Held Shares requirement.<sup>18</sup> Such a plan would generally be required to be provided within 45 calendar days of the request, as provided in the Rule 5800 Series.<sup>19</sup>

In support of its proposal, Nasdaq stated that it believes that its previously revised initial listing standards do not sufficiently address listed companies that may have Restricted Securities, which could potentially result in a security that is illiquid.<sup>20</sup> Nasdaq noted that illiquid securities may trade infrequently and in a more volatile manner, change hands at a price that may not

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<sup>17</sup> Rule 5101 states, in part, that Nasdaq “has broad discretionary authority over the initial and continued listing of securities in Nasdaq . . . [and] may use such discretion to . . . apply additional or more stringent criteria for the initial or continued listing of particular securities, or suspend or delist particular securities based on any event, condition, or circumstance that exists or occurs that makes initial or continued listing of the securities on Nasdaq inadvisable or unwarranted in the opinion of Nasdaq, even though the securities meet all enumerated criteria for initial or continued listing on Nasdaq.”

<sup>18</sup> See proposed Rule 5120.

<sup>19</sup> See proposed Rule 5120. Nasdaq has proposed to make conforming changes to Rule 5810(c)(2)(A) to add a deficiency under proposed Rule 5120 to the list of deficiencies for which a company may submit to the Exchange’s Listing Qualifications Department a plan to regain compliance. Nasdaq has also proposed to make other conforming and non-substantive changes to Rule 5810(c)(2). See proposed Rule 5810(c)(2). In addition, Nasdaq has proposed non-substantive changes to Rule 5810(c)(3)(A) (which deals with a company’s failure to meet the continued listing requirement for minimum bid price) to revise the phrase “market value of publicly held shares” to utilize the terms “Market Value” and “Publicly Held Shares,” which are defined in Rule 5005(a). See proposed Rule 5810(c)(3)(A)(i) and (ii).

<sup>20</sup> See Notice, supra note 3, 84 FR at 67974. For example, Nasdaq stated that companies that were not required to meet the newer initial listing requirements may still have Restricted Securities that are not freely tradeable, and a listed company may conduct a transaction that decreases its number of Unrestricted Publicly Held Shares. See id.

reflect their true market value, and may be more susceptible to price manipulation.<sup>21</sup> According to Nasdaq, the proposal would enhance transparency<sup>22</sup> and ensure that securities listed on Nasdaq are liquid and have sufficient freely tradeable shares to meet investor demand, thereby reducing trading volatility and price manipulation.<sup>23</sup>

III. Proceedings to Determine Whether to Approve or Disapprove SR-NASDAQ-2019-091 and Grounds for Disapproval Under Consideration

The Commission is instituting proceedings pursuant to Section 19(b)(2)(B) of the Act to determine whether the proposal should be approved or disapproved.<sup>24</sup> Institution of such proceedings is appropriate at this time in view of the legal and policy issues raised by the proposed rule change, as discussed below. Institution of disapproval proceedings does not indicate that the Commission has reached any conclusions with respect to any of the issues involved.

Pursuant to Section 19(b)(2)(B) of the Act, the Commission is providing notice of the grounds for disapproval under consideration. The Commission is instituting proceedings to allow for additional analysis and input concerning the proposed rule change's consistency with

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<sup>21</sup> See Notice, supra note 3, 84 FR at 67974. Nasdaq stated that it has observed problems with a small number of listed companies that have a large number of Restricted Securities, and that such companies may not have sufficient liquidity to meet investor demand, particularly upon announcement of material news, which may result in unusual trading characteristics, such as extreme price movements and unusually large bid-ask spreads. See id.

<sup>22</sup> According to Nasdaq, its existing rules would currently allow it to apply additional criteria to a listed company that satisfies all of the continued listing requirements where there are indications that there is insufficient liquidity in the security to support fair and orderly trading. See Notice, supra note 3, 84 FR at 67974, n.7 (citing Rule 5101).

<sup>23</sup> See Notice, supra note 3, 84 FR at 67975.

<sup>24</sup> 15 U.S.C. 78s(b)(2)(B).

the Act<sup>25</sup> and, in particular, with Section 6(b)(5) of the Act, which requires, among other things, that the rules of a national securities exchange not be designed to permit unfair discrimination between customers, issuers, brokers, or dealers.<sup>26</sup>

Nasdaq is proposing to adopt a new rule to specifically permit it to request additional information from a listed company regarding its number of Unrestricted Publicly Held Shares if Nasdaq observes unusual trading characteristics in a listed company's security or if the listed company has announced an event that may cause a contraction in the number of Unrestricted Publicly Held Shares. Nasdaq acknowledges that its continued listing standards currently require a minimum number of Publicly Held Shares, but not a minimum number of Unrestricted Publicly Held Shares. Nasdaq specifies, in the proposed rule, that in considering whether there are unusual trading characteristics in a security for purposes of requesting additional information on the number of Unrestricted Publicly Held Shares, Nasdaq may review volume, price movements, spread, and the presence or absence of any news. However, Nasdaq does not state how these broad factors would be considered in its determination of whether there are unusual trading characteristics to trigger a request for additional information, other than to note that the "unusual trading characteristics" it has observed in the past include "extreme price movements" and "unusually large bid ask spreads."<sup>27</sup> In any case, whether unusual trading characteristics, however determined, would cause Nasdaq to request additional information from a listed company on the number of Unrestricted Publicly Held Shares appears to be subject to wide discretion under the proposed rule.

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<sup>25</sup> 15 U.S.C. 78f(b)(5).

<sup>26</sup> Id.

<sup>27</sup> See Notice, supra note 3, 84 FR at 67974.

Similarly, under the proposed rule, Nasdaq may also request information on the number of Unrestricted Publicly Held Shares if the listed company has announced an event that may cause a contraction in the number of such unrestricted shares, such as a reverse stock split, tender offer, or stock buyback. The Exchange has not provided any specific explanation of when such events would or would not trigger a request for the number of Unrestricted Publicly Held Shares, but rather just provided that such events “may” trigger such a request, with the result that this provision also appears to be subject to wide discretion by Nasdaq.

Upon Nasdaq requesting additional information on the number of Unrestricted Publicly Held Shares, the proposed rule then states that if the information indicates the number of such unrestricted shares are below the applicable minimum number of Publicly Held Shares continued listing standard, Nasdaq generally will use its authority under Rule 5101 to apply more stringent criteria and request a plan to increase the number of Unrestricted Publicly Held Shares to an amount that is higher than the applicable minimum number of Publicly Held Shares continued listing standard. Nasdaq does not provide any information in its filing regarding when it generally will or will not use its authority to request such a plan. Moreover, should Nasdaq ask the listed company to provide a plan to increase the minimum number of Unrestricted Publicly Held Shares, Nasdaq provides no guidance on how it would determine such minimum number, with the result that this provision appears to be subject to wide discretion by Nasdaq as well.

Nasdaq stated that its proposal is not designed to permit unfair discrimination between customers, issuers, brokers, or dealers because, while the proposed changes will only apply to securities exhibiting unusual trading characteristics and companies that announce an event that may cause a contraction in the number of Unrestricted Publicly Held Shares, Nasdaq will apply

this standard to all such securities listed on Nasdaq.<sup>28</sup> As discussed above, however, the Exchange’s proposal provides it wide discretion both (1) to determine whether to request additional information from a listed company on the number of Unrestricted Publicly Held Shares; and (2) if it does so, and that number is less than the minimum number of Publicly Held Shares, to establish the more stringent requirements with respect to the minimum number of Unrestricted Publicly Held Shares. Accordingly, the Commission believes there are questions as to whether the proposal is consistent with Section 6(b)(5) of the Act and its requirement, among other things, that the rules of a national securities exchange not be designed to permit unfair discrimination.

The Commission notes that under the Commission’s Rules of Practice, 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 [‘SRO’] that proposed the rule change.”<sup>29</sup> 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,<sup>30</sup> and 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.<sup>31</sup>

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<sup>28</sup> See Notice, supra note 3, 84 FR at 67975-76.

<sup>29</sup> Rule 700(b)(3), Commission Rules of Practice, 17 CFR 201.700(b)(3).

<sup>30</sup> See id.

<sup>31</sup> See id.



For these reasons, the Commission believes it is appropriate to institute proceedings pursuant to Section 19(b)(2)(B) of the Act to determine whether the proposal should be approved or disapproved.

#### IV. Commission's Solicitation of Comments

The Commission requests that interested persons provide written submissions of their views, data, and arguments with respect to the issues identified above, as well as any other concerns they may have with the proposal. In particular, the Commission invites the written view of interested persons concerning whether the proposal is consistent with Section 6(b)(5) or any other provision of the Act, or the rules and regulations thereunder. Although there do not appear to be any issues relevant to approval or disapproval that would be facilitated by an oral presentation of views, data, and arguments, the Commission will consider, pursuant to Rule 19b-4, any request for an opportunity to make an oral presentation.<sup>32</sup>

Interested persons are invited to submit written data, views, and arguments regarding whether the proposal should be approved or disapproved by [insert date 21 days from publication in the Federal Register]. Any person who wishes to file a rebuttal to any other person's submission must file that rebuttal by [insert date 35 days from publication in the Federal Register]. The Commission asks that commenters address the sufficiency of the Exchange's statements in support of the proposal which are set forth in the Notice,<sup>33</sup> in addition to any other comments they may wish to submit about the proposed rule change.

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<sup>32</sup> Section 19(b)(2) of the Exchange Act, as amended by the Securities Act Amendments of 1975, Pub. L. 94-29 (June 4, 1975), grants the Commission flexibility to determine what type of proceeding—either oral or notice and opportunity for written comments—is appropriate for consideration of a particular proposal by a self-regulatory organization. See Securities Act Amendments of 1975, Senate Comm. on Banking, Housing & Urban Affairs, S. Rep. No. 75, 94th Cong., 1st Sess. 30 (1975).

<sup>33</sup> See Notice, supra note 3.

Comments may be submitted by any of the following methods:

Electronic comments:

- Use the Commission's Internet comment form (<http://www.sec.gov/rules/sro.shtml>); or
- Send an email to [rule-comments@sec.gov](mailto:rule-comments@sec.gov). Please include File Number SR-NASDAQ-2019-091 on the subject line.

Paper comments:

- Send paper comments in triplicate to Secretary, Securities and Exchange Commission, 100 F Street, NE, Washington, DC 20549-1090.

All submissions should refer to File Number SR-NASDAQ-2019-091. This file number should be included on the subject line if e-mail is used. To help the Commission process and review your comments more efficiently, please use only one method. The Commission will post all comments on the Commission's Internet website (<http://www.sec.gov/rules/sro.shtml>). Copies of the submission, all subsequent amendments, all written statements with respect to the proposed rule change that are filed with the Commission, and all written communications relating to the proposed rule change between the Commission and any person, other than those that may be withheld from the public in accordance with the provisions of 5 U.S.C. 552, will be available for website viewing and printing in the Commission's Public Reference Room, 100 F Street, NE, Washington, DC 20549, on official business days between the hours of 10:00 a.m. and 3:00 p.m. Copies of such filing also will be available for inspection and copying at the principal office of the Exchange. All comments received will be posted without change.

Persons submitting comments are cautioned that we do not redact or edit personal identifying information from comment submissions. You should submit only information that you wish to

make available publicly. All submissions should refer to File Number SR-NASDAQ-2019-091 and should be submitted on or before [insert date 21 days from publication in the Federal Register]. Rebuttal comments should be submitted by [insert date 35 days from publication in the Federal Register].

For the Commission, by the Division of Trading and Markets, pursuant to delegated authority.<sup>34</sup>

J. Matthew DeLesDernier  
Assistant Secretary

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<sup>34</sup> 17 CFR 200.30-3(a)(57).