

Via Email to submissions@banking.senate.gov

June 3, 2022

The Honorable Patrick Toomey, Ranking Member
U.S. Senate Banking Committee

Re: JOBS Act 4.0

Dear Ranking Member Toomey,

OTC Markets Group Inc. operates the OTCQX[®] and OTCQB[®] markets for over 1,700 public companies that provide current disclosure and meet financial standards, including over 500 small and emerging companies here in the United States. These U.S. companies are based across 47 states, have over 80,000 employees and represent a wide variety of industries, including technology, financial services, healthcare, real estate and consumer goods.

We are firm believers in the value that our public markets provide to small and growing business, American workers and the economy at large. In advance of the 10th anniversary of the landmark Jumpstart Our Business Startups (JOBS) Act, we want to thank you and your Senate Banking Committee colleagues for continuing to focus on serving these constituencies and improving our public markets. We support the overarching goals of the JOBS Act 4.0 to encourage companies to be publicly traded, improve small company capital raising tools and enhance retail investor access to investment opportunities, while maintaining robust investor protection and regulatory oversight.

In an effort to further these goals, we respectfully submit the feedback below with respect to a number of provisions that would impact the hundreds of small public companies on our markets.

Section 107: The Main Street Growth Act (S.3097)

The Main Street Growth Act would allow the creation of “Venture Exchanges” with rules and regulatory privileges tailored for venture stage companies. While we support legislation that helps smaller public companies, the current text of the Main Street Growth Act takes a misguided approach towards creating and regulating U.S. venture markets. We suggest two changes below that would address these issues.

First, the Main Street Growth Act should create *Venture Markets*, not just *Venture Exchanges*. The Act should include a section permitting *Alternative Trading Systems* that operate as *Qualified Interdealer Quotation Systems* subject to Rule 15c2-11 under the *Securities and Exchange Act of 1934* to elect to be treated as a “*Venture Market*.”

The Main Street Growth Act focuses solely on national securities exchanges, limiting the ability of “*Venture Securities*” to trade on other venues. This excludes existing venture markets, such

as our OTC Link ATS that operates as an Alternative Trading Systems (“ATS”) and Qualified Interdealer Quotation System.¹

Prescribing an exchange-only solution for venture-stage companies stifles the type of innovative, tailored market structure that already supports small company trading. Over 500 U.S.-based companies that trade on our OTCQX and OTCQB markets would fall within the bill’s definition of “venture security.”² Approximately 65 companies graduate from our markets to an exchange listing each year, making them the most successful “venture” markets in the world. Many domestic OTCQX and OTCQB companies do not seek to graduate and instead choose to maintain a thriving secondary market on our ATS platform without the cost and complexity of listing on an exchange. These companies have previously expressed concern over earlier introductions of the Main Street Growth Act.³ Failure to recognize non-exchange market models under this bill would effectively exclude over 500 American public companies, and others like them, from being granted “venture” status.

The successes of our markets are in part due to a decentralized “interdealer quotation system” model. This model works well for smaller, thinly traded securities because it allows broker-dealers to communicate with one another and provide liquidity as a service on an as-needed basis. This structure differs from the exchange model, which operates as a centralized trading facility designed to automatically match and execute orders.⁴ High-speed exchange matching engines can capture the substantial existing liquidity and efficiently process large trading volumes in the largest public companies, but they are not designed to create liquidity for smaller companies.

Second, paragraph (3)(B) of the Main Street Growth Act should be removed. The extension of Unlisted Trading Privileges (UTP) is vital to promoting fair and efficient market trading. In an apparent attempt to consolidate liquidity, the Main Street Growth Act would not permit Venture Exchanges to offer UTP to the securities traded there. Unlisted Trading Privileges allow securities to trade across multiple venues and were originally adopted, in large part, to facilitate competition between markets and deter monopolistic practices by the

¹ OTC Link ATS operates as a Qualified Interdealer Quotation System (“Qualified IDQS”) subject to Exchange Act Rule 15c2-11 and direct FINRA oversight. In its capacity as a Qualified IDQS, OTC Link ATS is responsible for, among other things, confirming that companies meet the ongoing disclosure requirements for public quoting under Rule. OTC Link ATS is also regulated as an Alternative Trading System (ATS) subject to direct regulatory oversight by the Securities Exchange Commission and FINRA.

² The definition of “venture security” under the Main Street Growth Act would include “emerging growth companies” with revenues under \$1.07 billion. Nearly all U.S. based companies traded on the OTCQX and OTCQB markets as of June 1, 2022, would fall within this definition.

³ Nine OTCQX companies submitted letters to members of the House Committee on Financial Services expressing their concern over the Main Street Growth Act in May 2018 and 11 OTCQX companies submitted similar letters to the Senate Banking Committee members in February 2019.

⁴ National securities exchanges cannot operate as interdealer quotation systems that have historically benefited smaller public company trading. See Reena Aggarwal & James J. Angel, *The Rise and Fall of the Amex Emerging Company Marketplace*, 52 J. FIN. ECON. 257, 271 (1999) (noting that small firms in the United States have traditionally chosen to be traded on dealer markets). Nasdaq, regulated by NASD (now FINRA), operated as the primary over-the-counter interdealer quotation system serving smaller public companies until 2006 when it registered as a national securities exchange. OTC Markets Group, regulated by FINRA, now serves as the primary interdealer quotation system.

exchanges.⁵ Removing these privileges incentivizes anti-competitive behavior that far outweighs the potential benefits of consolidated liquidity.⁶ Forcing these participants to use a venue type prescribed by regulators is not in the best interest of any market, particularly one intended to support smaller companies and their investors.

All market participants should be permitted to choose the type of trading venue that best suits their needs:

- Companies should be free to choose their listing or designation based on value and cost,
- Broker-dealers should be free to seek best execution from the market or broker-dealer of their choice, and
- Investors should benefit from competition between multiple market options for buying and selling company stock.

The two changes suggested above can help to achieve the underlying objectives of the Main Street Growth Act, while ensuring healthy competition and choice for market participants.

Section 307: Facilitating Main Street Offerings Act (S.3966)

We support the preemption of state securities laws for secondary transactions in Regulation A securities, as proposed in Section 307 of JOBS Act 4.0.

State law compliance is a significant concern for companies that are not traded on an exchange. When a security transaction is deemed out of compliance with state laws for secondary trading, broker-dealers are unable provide investment advice, distribute research to retail customers or facilitate trading in managed accounts on behalf of investors. These restrictions ultimately impact market liquidity and reduce investor access to information. The OTCQX market is exempt under state laws concerning secondary trading in 37 states and the OTCQB market is exempt in 33 states. We have achieved this status largely by engaging with individual state regulators over the past five years with the goal of recognizing the current disclosure provided by OTCQX and OTCQB companies.

We support extending “covered security” status to secondary transactions in Regulation A securities and would further advocate for extending that status to certain other qualified companies that provide current disclosure to the public. This relief would enhance improve secondary liquidity for shareholders and recognize the efforts of issuers that make current disclosure available to investors.

⁵ See Yakov Amihud & Haim Mendelson, *A New Approach to the Regulation of Trading Across Securities Markets*, 71:6 N.Y.U. L. REV 1411,1425 (1996) (“Congressman Markey's comments also illustrated the prevailing view that multimarket trading should be encouraged because of its competitive effect[.]”), available at <https://www.nyulawreview.org/wp-content/uploads/2018/08/NYULawReview-71-6-Amihud-Mendelson.pdf>.

⁶ A study examining trading costs across multiple equity trading venues found, among other things, that “[c]osts decline with OTC trading, number of LIT venues, and fragmentation, because these features help provide more competitive quotes.” See Andrea Frazzini, Ronen Israel & Tobias J. Moskowitz, *Trading Costs* 22 (2018), <https://ssrn.com/abstract=3229719>.

Beyond state securities law issues, Regulation A should be examined as a viable capital raising alternative for small public companies. When public companies raise funds in private transactions, the cost of such capital often comes at a significant discount to the public market price, hurting the company and the public shareholders. Companies that undertake the work and cost of providing quarterly, annual or semi-annual reports to the public should be able to access the public markets to raise capital. This can be achieved by permitting public companies to sell Regulation A shares directly into the market through a regulated broker-dealer.⁷

Sec. 401: Small Entity SEC Update Act

We support directing the SEC to conduct a study of the definition of “small entities” every five years. Many companies trading on our OTCQB Venture market would qualify as small entities under the definition in Section 601 of the Regulatory Flexibility Act. These are small public companies that the SEC should actively consider in its periodic regulatory impact reviews. This would contribute to a thoughtful, targeted regulatory framework for these companies, which would evolve in tandem with market conditions.

Sec. 403: Tracking Bad Actors Act of 2022 (S.3716)

We support the creation of a public database identifying bad actors as proposed in Section 403 of JOBS Act 4.0. The SEC can further these investor protection initiatives by also naming non-defendant individuals and corporate entities mentioned in enforcement actions.⁸ Individuals willing to act at the behest of bad actors should be publicly identified so that brokers, compliance teams, transfer agents and the investing public can make informed investment decisions. Greater transparency will enhance industry accountability and incentivize reputable professionals to avoid engagement with bad actors.

At OTC Markets Group, we make significant efforts to promote transparency, deter fraudulent trading activities and identify bad actors. For example, all OTCQX and OTCQB companies are subject to the OTC Markets Group Stock Promotion Policy,⁹ which, along with our Best Practices for Issuers,¹⁰ establishes a framework that allows market participants to easily identify and respond to fraudulent promotional activities.

We also designate certain securities with compliance risk flags, such as the “Caveat Emptor” skull and crossbones, when we become aware of certain public interest concerns, including promotional activities without adequate disclosure, fraudulent or criminal investigations, trading suspensions and undisclosed corporate actions, among others.

⁷ Letter from OTC Markets Group Inc. to the Securities and Exchange Commission 8-10 (Sept. 24, 2019) (on file with author), *available at* <https://www.sec.gov/comments/s7-08-19/s70819-6193364-192517.pdf>.

⁸ For example, in SEC v. Coldicutt, concerning various securities law violations against named attorney Andrew Coldicutt, the Complaint obscures certain related parties as “Attorney D”, “Issuer A” and “Audit Firm C.” See Complaint, SEC v. Coldicutt, No. 22CV0274MMAKSC (S.D. Cal. filed March 1, 2022), *available at* <https://www.sec.gov/litigation/complaints/2022/comp25338.pdf>.

⁹ OTC Markets Group Policy on Stock Promotion, https://www.otcmarkets.com/files/OTC_Markets_Group_Policy_on_Stock_Promotion.pdf.

¹⁰ OTC Markets Group Stock Promotion: Best Practices for Issuers, https://www.otcmarkets.com/files/Best_Practices_for_Issuers_Stock_Promotion.pdf.

Moreover, we publish and maintain a “Prohibited Service Providers” list on our website,¹¹ which includes attorneys, accountants, auditors, investor relations firms and other service providers that have been convicted of criminal activity, are subject to SEC sanctions, or that have raised questions regarding the reliability of their work such that OTC Markets Group has determined not to accept their professional affirmations.

We believe that critical information about investment risk empowers regulators to protect investors so they can make informed decisions. Market participants and regulators must work together to develop solutions that can efficiently identify, stop and ultimately prevent fraud in our capital markets.

Conclusion

We thank the Committee for the opportunity to provide feedback on this important legislation and we believe that Congress can work together to provide smaller, venture companies with the tools necessary to foster their growth and development. Please let us know if we can provide any additional information or insight in furtherance of that shared goal.

Very truly yours,



Daniel Zinn
General Counsel



Cass Sanford
Deputy General Counsel

¹¹ OTC Markets Group-Prohibited Service Providers, <https://www.otcmarkets.com/learn/prohibited-service-providers>.