

Via Email

July 16, 2020

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

Re: File Number SR-NYSE-2019-67

Dear Madam Secretary:

I am writing on behalf of the Council of Institutional Investors (CII), a nonprofit, nonpartisan association of U.S. public, corporate and union employee benefit funds, other employee benefit plans, state and local entities charged with investing public assets, and foundations and endowments with combined assets under management of approximately \$4 trillion. Our member funds include major long-term shareowners with a duty to protect the retirement savings of millions of workers and their families, including public pension funds with more than 15 million participants – true “Main Street” investors through their pension funds. Our associate members include non-U.S. asset owners with about \$4 trillion in assets, and a range of asset managers with more than \$35 trillion in assets under management.¹

The purpose of this letter is to respond to the Securities and Exchange Commission (SEC or Commission) request for comments in response to a New York Stock Exchange LLC (NYSE or Exchange) proposal that would “(1) amend Chapter One of the Listed Company Manual . . . to modify the provisions relating to direct listings to permit a primary offering in connection with a direct listing and to specify how a direct listing qualifies for initial listing if it includes both sales of securities by the company and possible sales by selling shareholders, (2) modify the definition of ‘Direct Listing’ in Rule 1.1, (3) add a definition of Issuer Direct Offering . . . Order to Rule 7.31 and describe how it would participate in a Direct Listing Auction in Rule 7.35A, and (4) remove references to Direct Listing Auctions from Rule 7.35C”² (NYSE Proposal).³

¹ For more information about the Council of Institutional Investors (“CII”), including its board and members, please visit CII’s website at <http://www.cii.org>.

² Self-Regulatory Organizations; New York Stock Exchange LLC; Notice of Filing of Proposed Rule Change, as Modified by Amendment No. 2, To Amend Chapter One of the Listed Company Manual To Modify the Provisions Relating to Direct Listings, Exchange Act Release No. 89,148, 85 Fed. Reg. 39,246, 39,246 (June 24, 2020), <https://www.federalregister.gov/documents/2020/06/30/2020-14013/self-regulatory-organizations-new-york-stock-exchange-llc-notice-of-filing-of-proposed-rule-change>.

³ *Id.*

As you are aware, most commentators have opposed the NYSE's previous proposals to expand direct listings.⁴ As indicated in our letter of April 16, 2020 in response to the Commission's related proceedings to determine whether to approve the proposed rule change, as modified by Amendment No. 1⁵ (April Letter),⁶ our January 16, 2020 letter in response to the NYSE Amendment No.1 to the proposed rule change⁷ (January Letter)⁸ and as discussed further in this letter, CII believes the SEC should disapprove the NYSE Proposal.

SEC Does Not Have A Sufficient Basis to Make an Affirmative Finding

The SEC has indicated that a proposal must be disapproved if the SEC does not have “a sufficient basis to make an affirmative finding that a proposed rule change is consistent with the . . . [Securities and Exchange Act of 1934 (Exchange Act)] and the applicable rules and regulations.”⁹ More specifically, the SEC has stated that a proposal must be consistent with:

Section 6(b)(5) of the Exchange Act, which requires, among other things, that the rules of a national securities exchange be designed to *prevent fraudulent and manipulative acts and practices*, to promote just and equitable principles of trade, to remove impediments to and perfect the mechanism of a free and open market and a national market system, and, in general, *to protect investors and the public interest*; and are not designed to permit unfair discrimination between customers, issuers, brokers, or dealers.¹⁰

⁴ See Cydney Posner, Cooley LLP, Blog: NYSE takes another crack at primary direct listings—will it succeed? (July 29, 2020), JDSUPRA, available at <https://www.jdsupra.com/legalnews/blog-nyse-takes-another-crack-at-92073/> (“the majority of comment letters opposed the proposal”).

⁵ Self-Regulatory Organizations; New York Stock Exchange LLC; Order Instituting Proceedings to Determine Whether to Approve or Disapprove a Proposed Rule Change, as Modified by Amendment No.1, To Amend Chapter One of the Listed Company Manual To Modify the Provisions Relating to Direct Listings, Exchange Act Release No. 88,485, 85 Fed. Reg. 18,292, 18,292 (Mar. 26, 2020), available at <https://www.federalregister.gov/documents/2020/04/01/2020-06732/self-regulatory-organizations-new-york-stock-exchange-llc-order-instituting-proceedings-to-determine>.

⁶ See Letter from Jeffrey P. Mahoney, General Counsel, Council of Institutional Investors to Secretary, Securities and Exchange Commission (Apr. 16, 2020), [https://www.cii.org/files/issues_and_advocacy/correspondence/2020/April%2016%202020%20NYSE%20direct%20listing%20\(final\).pdf](https://www.cii.org/files/issues_and_advocacy/correspondence/2020/April%2016%202020%20NYSE%20direct%20listing%20(final).pdf).

⁷ Self-Regulatory Organizations; New York Stock Exchange LLC; Notice of Filing of Proposed Rule Change, as Modified by Amendment No. 1, To Amend Chapter One of the Listed Company Manual To Modify the Provisions Relating to Direct Listings, Exchange Act Release No. 87,821, 84 Fed. Reg. 72,065 (Dec. 20, 2019), <https://www.govinfo.gov/content/pkg/FR-2019-12-30/pdf/2019-28029.pdf>.

⁸ See Letter from Jeffrey P. Mahoney, General Counsel, Council of Institutional Investors to Secretary, Securities and Exchange Commission (Jan. 16, 2020), <https://www.sec.gov/comments/sr-nyse-2019-67/srnyse201967-6660338-203855.pdf>.

⁹ See, e.g., 85 Fed. Reg. at 18,296.

¹⁰ *Id.* at 18,295 (emphasis added).

CII believes the NYSE Proposal to expand direct listings may lessen investor protections in a number of ways, including the following:¹¹

Investors may have fewer legal protections.

In a recent article discussing the NYSE Proposal, Lise Buyer of Class V Group, a Silicon Valley consultant for companies going public, indicated that: “[L]iability ‘would be an issue’ in a direct listing combined with a primary share offering.”¹²

As described in our January Letter, investors that purchase shares from issuers that have conducted direct listings may have fewer legal protections from damages caused by untrue statements of fact or material omissions of fact.¹³ More specifically, investors in direct listings may not be able to directly trace their shares to a misrepresented registration statement to support a meritorious claim.¹⁴

As discussed in our April Letter, the NYSE has previously dismissed our concerns claiming that “it should have no bearing on the Commission’s decision as to whether the [NYSE] Proposal is consistent with the Exchange Act.”¹⁵ The NYSE appears to support the absence of traceable shares in a direct listing as an appropriate defense to investor losses caused by public companies’ untrue statements of fact or material omissions of fact.¹⁶ We respectfully disagree.

Our view is consistent with an April 2020 decision of first impression by a judge in the Northern District of California who declined to impose a tracing requirement for Section 11 claims under the Securities Act of 1933 (Securities Act) concerning a direct listing, holding that there was a “good reason” for dispensing with the tracing requirement in that context in order to avoid

¹¹ We note that investor protections in direct listings may be particularly vulnerable during a down or volatile market. See Crystal Tee & Katie Roof, Direct Listings Fall From Favor With Tech Cash Crunch Deepening, Yahoo! Fin. (Mar. 25, 2020) (on file with CII) (“the lack of visibility on the supply of shares on the first trading day, the absence of a target price range and the loose framework make it difficult to guide investors in an unstable market”); Cromwell Schubarth, The Funded: Direct listings, ‘blank check’ IPOs look less likely in age of COVID-19, Silicon Valley Bus. J. (Mar. 25, 2020), <https://www.bizjournals.com/sanjose/news/2020/03/25/the-funded-direct-listings-blank-check-ipos-look.html> (“current market volatility makes it too hard to guide investors on the proper pricing and valuation of companies that skip traditional investor road shows before they trade”).

¹² Ines Ferré, Proposed direct listing change would ‘encourage more companies to go public’: IPO expert, Yahoo Fin., (June 29, 2020), <https://finance.yahoo.com/news/proposed-direct-listing-change-will-encourage-more-companies-to-go-public-ipo-expert-130008146.html>.

¹³ See Letter from Jeffrey P. Mahoney, General Counsel, Council of Institutional Investors to Secretary, Securities and Exchange Commission at 2 (“investors in direct listing companies may have fewer legal protections than investors in IPOs”).

¹⁴ See, e.g., Alexander Osipovich, *Investor Advocates See Risks in Silicon Valley’s Favorite IPO Alternative*, Wall St. J., Jan. 3, 2020 (on file with CII).

¹⁵ Letter from Elizabeth K. King, Chief Regulatory Officer, ICE, General Counsel & Corporate Secretary, NYSE to Ms. Vanessa Countryman, Secretary, Securities and Exchange Commission 4 (Mar. 16, 2020) <https://www.sec.gov/comments/sr-nyse-2019-67/srnyse201967-6960395-212779.pdf>.

¹⁶ See *id.* at 4-5 (“The methods used by a plaintiff to establish Securities Act liability for offering participants may well vary depending upon the facts of the specific transaction, and securities law liability has always distinguished between investors who purchase in the market and investors who purchase directly from underwriters.”).

“completely obviat[ing] the remedial penalties” of the Securities Act.¹⁷ The decision, however, may not be adopted by other courts. As some legal experts have explained:

[G]iven that *Slack* considered an issue of first impression, departed from the well-established traceability requirement under Section 11, and recognized that district courts have reached differing conclusions regarding the activities that constitute active solicitation under Section 12(a)(2), it is possible that the decision will receive appellate review or that other courts will disagree with its holdings. *In this respect, it is notable that many of the concerns expressed by the District Court are similar to other situations where courts have uniformly declined to dispense with the existing standing requirements of the Securities Act, including secondary offerings.*¹⁸

Thus, we concluded in the January Letter and we continue to believe that “SEC approval of the [NYSE Proposal] . . . before fixing our system of share ownership would follow the same disordered approach that the Commission has taken to fixing problems in proxy plumbing.”¹⁹

We are pleased that the SEC has recently added “proxy process amendments” to its short-term agenda.²⁰ We look forward to supporting proposed rulemaking and other SEC actions that will move the U.S. to a system of traceable shares that could better support the expansion of direct listings in a manner that would not lessen investor protections.²¹

¹⁷ See *Dennee v. Slack Technologies Inc.*, No. 19-cv-05857-SI at 12, 13 (N.D. Cal. Apr. 21, 2020), available at <https://cases.justia.com/federal/district-courts/california/candce/3:2019cv05857/348463/74/0.pdf?ts=1587547235>.

¹⁸ Nicolas Grabar et al., *Cleary Gottlieb Discusses How Court Allowed Securities Liability for Slack’s Direct Listing*, CLS Blue Sky Blog (May 4, 2020) (footnotes omitted and emphasis added), <https://clsbluesky.law.columbia.edu/2020/05/04/cleary-gottlieb-discusses-how-court-allowed-securities-liability-for-slacks-direct-listing/>.

¹⁹ Letter from Jeffrey P. Mahoney, General Counsel, Council of Institutional Investors to Secretary, Securities and Exchange Commission at 3 (footnotes omitted).

²⁰ See Betty Moy Huber & Paula H. Simpkins, *Briefing: Governance, SEC’s Spring 2020 Reg Flex Agenda Indicates Universal Proxy Rule May Be Coming Soon*, DavisPolk (July 1, 2020), <https://www.briefinggovernance.com/2020/07/secs-spring-2020-reg-flex-agenda-indicates-universal-proxy-rule-may-be-coming-soon/> (“Worth noting is that the potential rulemaking related to universal proxies, proxy process amendments (a.k.a. ‘proxy plumbing’) and mandated electronic filings have moved up to the short-term agenda; formerly these were on the 2019 fall long-term agenda.”); Agency Rule List – Spring 2020, SEC, Proxy Process Amendments (last visited July 10, 2020), <https://www.reginfo.gov/public/do/eAgendaViewRule?pubId=202004&RIN=3235-AM16>.

²¹ See, e.g., Letter from Kenneth A. Bertsch, Executive Director, Council of Institutional Investors et al. to Brent J. Fields, Secretary, Securities and Exchange Commission 2, 8 (Jan. 31, 2019), <https://www.cii.org/files/20190131%20CII%20Follow%20Up%20Letter%20to%20SEC%20on%20Proxy%20Mechanics%20FINAL.pdf> (“Technological change now offers the opportunity to construct a better system of share ownership based on traceable shares . . . investors bringing Section 11 claims fall susceptible to chain of custody opacities when they cannot demonstrate, as is required, that they purchased shares that were issued in connection with a misrepresented registration statement. These practical obstacles present in the current system needlessly delay or prevent investors from proceeding with legitimate claims and receiving compensation, which harms the health and fairness of the capital markets. Intuitively, blockchain-based traceable shares would provide an immutable chain of custody ledger and enable investors to supply evidence of their provenance and voting decisions as necessary”).

Investors may be subject to greater risk because of the potential for insufficient size and liquidity.

NYSE listing standards generally require that a company may list on the NYSE in connection with its initial public offering with a market value of publicly-held shares of \$40 million.²² Under the NYSE Proposal, however, a company may list on the NYSE in connection with a “Primary Direct Floor Listing”^[23] if it: “(1) sell[s] at least \$100 million of its listed securities in the opening auction, or (2) ha[s] an aggregate market value of publicly-held shares immediately prior to listing together with the market value of shares the company sells in the opening auction total at least \$250 million, with such market value calculated using a price per share equal to the lowest price of the price range established by the issuer in its registration statement.”²⁴ The NYSE argues that this provision is “consistent with the protection of investors” because:

*[I]n the Exchange’s experience in listing IPOs, a liquid trading market develops after listing for issuers with a much smaller value of publicly-held shares than the Exchange anticipates would exist after the opening auction in a Primary Direct Floor listing under the proposed market value of publicly-held shares requirements. Consequently, the Exchange believes that these requirements would provide that any company conducting a Primary Direct Floor Listing would be of a suitable size for Exchange listing and that there would be sufficient liquidity for the security to be suitable for auction market trading.*²⁵

The NYSE, however, provides no data to support its argument, but rather asks that the Commission rely on its *experience* in listing IPOs and its *belief* that the proposed requirement will result in a suitable size with sufficient liquidity. We do not believe the NYSE’s claim of experience and beliefs are a sufficient basis to make an affirmative finding in support of the NYSE Proposal.

²² See NYSE, Listing Company Manual § **102.01B** (“A Company must demonstrate an aggregate market value of publicly-held shares of \$40,000,000 for companies that list either at the time of their initial public offerings . . . (C) or as a result of spin-offs or under the Affiliated Company standard or, for companies that list at the time of their Initial Firm Commitment Underwritten Public Offering (C), and \$100,000,000 for other companies (D)(E).”), https://nyseguide.srorules.com/listed-company-manual/document?searchId=362512045&treeNodeId=csh-da-filter!WKUS-TAL-DOCS-PHC-%7B0588BF4A-D3B5-4B91-94EA-BE9F17057DF0%7D--WKUS_TAL_5667%23teid-5.

²³ 85 Fed. Reg. at 39,247 (“Primary Direct Floor Listing” defined as a “listing in which either (i) only the company itself is selling shares in the opening auction on the first day of trading or (ii) the company is selling shares and selling shareholders may also sell shares in such opening auction”).

²⁴ *Id.* at 39,250.

²⁵ *Id.*

For all the above reasons, we respectfully request that the Commission disapprove the NYSE Proposal. Thank you for considering our views on this matter. Please contact me with any questions.

Sincerely,

A handwritten signature in black ink that reads "Jeff Mahoney". The signature is written in a cursive style with a large, stylized "J" and "M".

Jeffrey P. Mahoney
General Counsel