

Via Email

July 28, 2022

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

*Re: File Number SR-NYSE-2022-14.*

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 \$40 trillion in assets under management.<sup>1</sup>

## **The Order**

The purpose of this letter is to respond to the Securities and Exchange Commission’s (SEC or Commission) solicitation of comments with respect to the *Order Instituting Proceedings to Determine Whether To Approve or Disapprove a Proposed Rule Change To Modify Certain Pricing Limitations for Securities Listed*

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<sup>1</sup> 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>.

*on the Exchange Pursuant to a Primary Direct Floor Listing (Order).*<sup>2</sup> Under the proposed rule change, the New York Stock Exchange LLC (Exchange) would:

[M]odify certain pricing limitations for securities listed on the Exchange pursuant to a direct listing with a primary offering in which the company will sell shares itself in the opening auction on the first day of trading on the Exchange.<sup>3</sup>

As the leading voice for effective corporate governance and strong shareholder rights, CII respectfully recommends that the SEC disapprove the Exchange's proposed rule.

### **The SEC Does Not Have a Sufficient Basis to Make an Affirmative Finding**

The Commission has indicated a proposed rule 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 Section 6(b)(5) of the Securities and Exchange Act of 1934 (Exchange Act).<sup>4</sup> The Exchange Act requires, among other things, that the rules of a national securities exchange be designed to: 1) prevent fraudulent and manipulative acts and practices; 2) promote just and equitable principles of trade; 3) remove impediments to, and perfect the mechanism of, a free and open market and a national market system; 4) protect investors and the public interest; and 5) prohibit unfair discrimination between customers, issuers, brokers, or dealers.<sup>5</sup> In addition, the Commission's Rules of Practice<sup>6</sup> provide that:

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<sup>2</sup> See Self-Regulatory Organizations; New York Stock Exchange LLC; Order Instituting Proceedings To Determine Whether To Approve or Disapprove a Proposed Rule Change To Modify Certain Pricing Limitations for Securities Listed on the Exchange Pursuant to a Primary Direct Floor Listing, Exchange Act Release No. 95,301, 87 Fed. Reg. 43,931 (July 21, 2022), <https://www.federalregister.gov/documents/2022/07/22/2022-15656/self-regulatory-organizations-new-york-stock-exchange-llc-order-instituting-proceedings-to-determine>.

<sup>3</sup> 87 Fed. Reg. at 43,914.

<sup>4</sup> See National Securities Exchanges § 6(b)(5), 15 U.S.C. §78(f)(b)(5) (1934), available at <https://www.law.cornell.edu/uscode/text/15/78f> ("The rules of the exchange are designed to prevent fraudulent and manipulative acts and practices, to promote just and equitable principles of trade, to foster cooperation and coordination with persons engaged in regulating, clearing, settling, processing information with respect to, and facilitating transactions in securities, 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, or to regulate by virtue of any authority conferred by this chapter matters not related to the purposes of this chapter or the administration of the exchange").

<sup>5</sup> *Id.*

<sup>6</sup> See Rules of Practice Governing Disapproval Proceedings for SRO Proposed Rule Change Filings and For Proposed NMS Plans and Plan Amendments §201.701(b)(3)(i), available at <https://www.sec.gov/files/tm/no-action/rules-practice-disapproval-proceedings-02192021.pdf> (describing rules demonstration of consistency with the Exchange Act).

[T]he “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.” 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, 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>7</sup>

CII notes that the SEC has raised multiple questions in the Order as to whether provisions of the proposed rule are consistent with the protection of investors under Section 6(b)(5) of the Exchange Act.<sup>8</sup> We are particularly concerned about the following SEC staff observations and related questions about the proposed rule’s disclosure of information to investors about the final offering price when the price falls outside of the range disclosed in the registration statement:

Given the possibility under the proposed rules that the offering might price far outside the disclosed price range, would issuers be less likely to update their disclosed price ranges, compared to firm commitment underwritten initial public offerings? Similarly, would disclosed price ranges for direct listings be less reliable as indicators of management’s perceived valuation of the issuer? How would the ability to ultimately conduct the auction up to 20% below or anywhere above the disclosed price range affect issuer decisions as to what price range to disclose in the registration statement? *Would this impact the usefulness of price range disclosure to potential investors or market analysts? If so, this raises concerns about the consistency of the proposal with investor protection and the public interest under Section 6(b)(5) of the Exchange Act.*<sup>9</sup>

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<sup>7</sup> 87 Fed. Reg. at 43,921 (footnotes omitted).

<sup>8</sup> *See id.* at 43,918-21.

<sup>9</sup> *Id.* at 43,920 (footnotes omitted); cf. Letter from Jeffrey P. Mahoney, General Counsel, Council of Institutional Investors to Secretary, Securities and Exchange Commission 2 (Oct. 21, 2021), [https://www.cii.org/files/issues\\_and\\_advocacy/correspondence/2021/October%2021%202021%20Nasdaq%20letter%20\(final\).pdf](https://www.cii.org/files/issues_and_advocacy/correspondence/2021/October%2021%202021%20Nasdaq%20letter%20(final).pdf) (“We are particularly concerned about the following SEC staff observations that the [Nasdaq Stock Market LLC] (Exchange) proposal lacks required company disclosure of material information about the final offering price prior to the time of the sale of shares in a direct listing with a capital raise . . .”).

Our sensitivity to this lack of disclosure under the proposed rules is heightened by our broader and repeated concerns about the loss of investor protections relating to direct listings generally, primarily focused on the difficulties investors face in effectively bringing claims under Section 11 of the Securities Act of 1933<sup>10</sup> for material misstatements or omissions in primary direct listing registration statements.<sup>11</sup> In that regard, we commend the SEC staff for explicitly raising the following two Section 11-related issues in the Order:

- “While the Exchange has indicated that the proposal is intended to treat like cases alike with respect to pricing flexibility, it has not addressed certain differences between listings that would occur under this proposed rule change and firm commitment underwritten initial public offerings on the Exchange that may affect investor protection, including the lack of a named underwriter, any challenges to bringing claims under Section 11 of the Securities Act due to the potential assertion of tracing defenses, and how those differences could affect the consistency of the proposal with Section 6(b)(5) of the Exchange Act. It is not clear from the proposal what consideration, if any, the Exchange has given to addressing these issues, or why it believes the proposal is consistent with investor protection, as required by Section 6(b)(5) of the Exchange Act, in light of the pricing flexibility proposed by the Exchange.”<sup>12</sup>
- “Given the limited judicial precedent addressing tracing requirements in the context of direct listings, and the typical absence of lock-up arrangements in connection with direct listings to date, we are considering whether the Exchange has met its burden of establishing that the proposal to allow a direct listing to proceed at a price outside of the disclosed price range is consistent with Section 6(b)(5) of the Exchange Act that requires the rules of the Exchange be designed to protect investors and the public interest.”<sup>13</sup>

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<sup>10</sup> See Civil liabilities on account of false registration statement, 15 U.S. Code § 77k (1933) (Section 11 of the Securities Act of 1933), available at <https://www.law.cornell.edu/uscode/text/15/77k>.

<sup>11</sup> See, e.g., Petition of Council of Institutional Investors for Review of an Order, Issued by Delegated Authority, Granting Approval of a Proposed Rule 8-13 (Sept. 8, 2020) (footnotes omitted), <https://www.sec.gov/rules/sro/nyse/2020/34-89684-petition.pdf> (describing in detail how direct listings with a capital raise “compounds the problems shareholders face in tracing their share purchases to a registration statement.”).

<sup>12</sup> 87 Fed. Reg. at 49,919.

<sup>13</sup> Id. at 43,919 n.79.

Finally, if the Exchange chooses to address those critical investor protection issues, we believe its consideration should also include responding to a recent analysis in a forthcoming law review article by Professor Brent J. Horton, *Direct Listings and the Weakening of Investor Protections*.<sup>14</sup> The article concludes:

*One of the primary remedies for harmed investors--Section 11 of the Securities Act--is largely unworkable in the context of a direct listing.*<sup>15</sup>

[I]n the case of a Direct Listing, a harmed investor faces two impediments to recovery under Section 11. The first impediment is the tracing requirement. The second impediment is the absence of the [traditional] underwriter as a defendant.<sup>16</sup>

For all these reasons, we believe the proposed rules are not consistent with Section 6(b)(5) of the Act and should be disapproved.<sup>17</sup>

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<sup>14</sup> See Brent J. Horton, *Direct Listings and the Weakening of Investor Protections*, 50 Fla. St. University L. Rev. (forthcoming 2023), available at <https://ssrn.com/abstract=4081399/>.

<sup>15</sup> *Id.* at 1.

<sup>16</sup> *Id.* at 30.

<sup>17</sup> We believe the following facts may also be relevant to the consideration of whether the proposed rules are consistent with Section 6(b)(5) of the Securities and Exchange Act of 1934: In calendar 2021, CII tracked 287 traditional initial public offerings (IPOs), 6 direct listings and 121 special purpose acquisition (de-SPAC) mergers. See Council of Institutional Investors, *Newly Public Operating Companies Snapshot: 2021*, [https://www.cii.org/Files/issues\\_and\\_advocacy/Dual%20Class%20post%206-25-19/2022\\_1\\_19%20Dual-Class%20IPO%20Snapshot%202021\\_.pdf](https://www.cii.org/Files/issues_and_advocacy/Dual%20Class%20post%206-25-19/2022_1_19%20Dual-Class%20IPO%20Snapshot%202021_.pdf). Out of these 415 companies, 94 had dual class structures in violation of a core principle of good corporate governance—the principle of one share, one vote. See Council of Institutional Investors, *Corporate Governance Policies § 3.3 One Share, One Vote* (Updated Mar. 7, 2022), [https://www.cii.org/files/03\\_07\\_22\\_corp\\_gov\\_policies.pdf](https://www.cii.org/files/03_07_22_corp_gov_policies.pdf). Of those 94 companies with poor corporate governance due to dual class stock: 62 were traditional IPOs (21.6% of all traditional IPOs), 6 were direct listings (100% of all direct listings), and 25 de-SPAC mergers (21.3% of all de-SPAC mergers). From this data, CII perceives that among those three paths of entry to the public markets, direct listings may have the highest risk of creating public companies that violate a core principle of good corporate governance.

We appreciate your consideration of our comments. Please let me know if you have any questions.

Sincerely,

A handwritten signature in cursive script that reads "Jeff Mahoney". The signature is written in black ink and is positioned above the printed name.

Jeffrey P. Mahoney  
General Counsel