Testimony of Edward S. Knight
Executive Vice President
Global Chief Legal and Policy Officer
Nasdaq, Inc.
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Subcommittee on Capital Markets and GSEs
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Chairman Huizenga and Ranking Member Maloney,

Thank you for the opportunity to testify in support of legislation designed to improve economic growth, create jobs, and provide investors with more opportunity to grow their savings. That is what we can expect if we modernize the public company model, while preserving critical investor protections.

Nasdaq recently noted the one-year anniversary of launching its Revitalize Initiative (business.nasdaq.com/revitalize) aimed at highlighting a set of ideas that our listed companies, stakeholders and investors tell us will restore the vibrancy of the capital markets. These ideas are broadly grouped around three areas of the securities law: the proxy process, the disclosure rules, and the market structure that applies to the U.S. equity markets.

A little over a year ago, I testified on a similar topic, "The JOBS Act at Five", as Congress began its deliberations concerning how best to build on the foundation of the JOBS Act. Since then, Congress, the SEC, and the Administration — acting largely on a bipartisan basis — have made progress in seeking to improve economic conditions, without new appropriations or changes to the tax code. That is the beauty of the capital markets: by making them more efficient and modern, we stimulate growth and job creation, and the fiscal impact is positive.

And when the business community understands policymakers are willing to work alongside them to effect change, there are other less tangible results. As one economist observed: "business confidence is the cheapest form of economic stimulus."[1]

We are encouraged the following has occurred since the JOBS Act hearing:

[1] Lawrence H. Summers (see, e.g., The Business Roundtable's Outlandish Tax Cut Claims, The Washington Post (October 23, 2017)).

- The U.S. Department of the Treasury issued a comprehensive Capital Markets Report that supported disclosure reform, proxy advisory firm reform, and market structure reform for small cap stocks.[2]

- The House passed the Budd / Meeks legislation, H.R. 3903, extending confidential filing provisions. The Senate has offered a bipartisan companion bill.[3]

- Separately, the SEC has acted to broaden confidential filings.[4]

- The House passed the Duffy / Meeks proxy advisory firm reform bill, H.R. 4015.

- Chairman Huizenga's conflict minerals bill, H.R. 4248, passed the full House Financial Services Committee.

- The SEC held a "Roundtable" on April 23 that addressed the market structure for thinly-traded, exchange-listed securities, both equities and exchange-traded products.[5]

- The SEC moved forward with proposed rulemaking to modernize and simplify Regulation S-K, as instructed in the FAST Act.[6]

- The SEC issued Staff Bulletin 14I reducing burdens of proxy access.[7]

Equally important, a broad coalition of interests, from the Chamber of Commerce and the National Venture Capital Association to the Biotechnology Innovation Organization (BIO) and TechNet to SIFMA, the American Securities Association and the Equity Dealers of America, have come forward to embrace this agenda.[8]

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2 U.S. Department of the Treasury, A Financial System That Creates Economic Opportunities: Capital Markets (October 6, 2017), available at https://www.treasury.gov/press-center/press-releases/Documents/A-Financial-System-Capital-Markets-FINAL-FINAL.pdf.

3 Encouraging Public Offerings Act of 2018, S. 2347, 115th Congress.

4 SEC Press Release, Draft Registration Statement Processing Procedures Expanded (June 29, 2017), available at https://www.sec.gov/corpfin/announcement/draft-registration-statement-processing-procedures-expanded.

5 Roundtable on Market Structure for Thinly-Traded Securities, available at https://www.sec.gov/video/webcast-archive-player.shtml?document_id=042318-roundtable-thinly-traded-securities. See also SEC Press Release 2018-65, available at https://www.sec.gov/news/press-release/2018-65.

6 FAST Act Modernization and Simplification of Regulation S-K, Securities Exchange Act Release No. 34-81851 (October 11, 2017), 82 FR 50988 (November 2, 2017).

7 Available at https://www.sec.gov/interps/legal/cfslb14i.htm.

8 Expanding the On-Ramp: Recommendations to Help More Companies Go and Stay Public, available at https://www.centerforcapitalmarkets.com/wp-content/uploads/2018/04/IPO-Report_EXPANDING-THE-ON-RAMP.pdf.

I want to focus my comments today on five initiatives that we believe are worthy of the Subcommittee's favorable consideration:

- Rep. Tom Emmer's H.R. 5877, regarding Venture Exchanges, which would allow certain smaller publicly-listed companies to choose to aggregate the trading of their securities on a single exchange to enhance liquidity and reduce fragmentation in the market;

- Legislation to simplify the quarterly filing financial reporting regime, including Rep. Ann Wagner's legislation to allow Form 10-Q optionality;

- Legislation that matches short selling disclosure with disclosure required of other investors;

- Proxy process reform legislation, including Rep. Sean Duffy's H.R. 5756, designed to modernize the submission of proposals for inclusion on corporate proxies; and

- Legislation expanding testing the waters and confidential filing exemptions.

**Venture Exchange Legislation**

As the founder of electronic trading, Nasdaq views market innovation as a tremendous force for good, unlocking competition and unleashing the flow of capital to catalyze economic activity. Yet, as markets have advanced, the fundamental structure that underpins them has not evolved to benefit all market segments equally.

Despite incremental improvements to markets in recent years, liquidity and the trading experience for small and medium growth companies, and investors in these companies, still lags far behind that of larger issuers. For small and medium growth companies—those with a market capitalization below $1 billion, particularly when the lower market cap is accompanied by low daily trading volume—relatively small orders can create dramatic price movements. This increases costs for both the companies and their investors. For example, regardless of the listing market that a company may choose, small and medium growth companies have shown a worsening incidence of high-volatility days, which increases investor confusion and undermines confidence in our markets.

This liquidity dilemma stems from a long-term trend towards fragmentation, where liquidity has spread across an increasing number of trading venues. As recently as 15 years ago, more than 90% of liquidity was often concentrated in a single market with the small remainder spread over an additional eight to ten other exchanges and electronic communications networks. Today, liquidity is spread thinly across fifty or more venues.

Nasdaq believes allowing smaller issuers to choose to concentrate that disaggregated liquidity onto a single exchange, with limited exceptions, will allow investors to better source liquidity. In addition, investors will enjoy a higher level of transparency because exchanges are required to display their best quotes to the public, and most exchanges

choose also to publish full supply and demand information (i.e. order book depth information) within their markets.

Thus, Nasdaq recommends permitting issuers to choose to trade in an environment with consolidated liquidity as would be allowed under the Venture Exchange Legislation. By creating a market for smaller issuers that is voluntary for issuers to join and largely exempt from the UTP obligations—subject to key exemptions—we can concentrate liquidity, to reduce volatility and improve the trading experience. Exchange trading would likely further concentrate liquidity and limit fragmentation. The net effect would be a substantial "thickening" of the liquidity crust on the exchange that lists the security.

Nasdaq has made an application at the SEC, which would adopt elements of this idea on our exchange, and we are proud this proposal has attracted wide support, including from the Chamber of Commerce and SIFMA. The legislation would expand this idea for a larger number of companies across existing and new exchanges. The Venture Exchange legislation provides a comprehensive framework, which will ensure that the benefits are realized in the near term. We appreciate the thoughtful diligence of Rep. Tom Emmer and his staff for the constructive balance contained in H.R. 5877 and look forward to this Subcommittee moving forward with consideration of this innovative proposal.

**Form 10-Q Optionality**

The Securities Exchange Act of 1934 (1934 Act) and the rules adopted thereunder require most SEC registrants to file a quarterly report with the SEC on Form 10-Q. The Form 10-Q includes condensed financial information and other data prepared by a company and reviewed by its independent auditors. The purpose of Form 10-Q is to update information included in annual Form 10-Ks or, for new companies, in securities registration statements previously filed under the 1934 Act or the Securities Act of 1933 (Securities Act or 1933 Act). The SEC's integrated disclosure system is designed so that the instructions in the various forms under the 1933 and 1934 Acts refer to Regulation S-X for financial statement disclosures and Regulation S-K for the required nonfinancial statement disclosures.

In today's market, to reach investors quickly, companies provide key data via an earnings press release each quarter. For virtually all investors, the press release is the quarterly report where they obtain key information and on which they make investment decisions. Yet companies are then required to file a formal Form10-Q document with the SEC, which is complex, time-consuming, and provides little additional actionable information that cannot be found in the press release. By establishing simple guidelines, the press release can replace the Form 10-Q entirely for issuers that prefer to report quarterly information in that format, aligning regulatory and shareholder interests and significantly decreasing corporate reporting red tape. The current two-step process frustrates the goals of modern disclosure since retail investors rely on the press release that may be missing some important information, which appears buried in the Form 10-Q. The legislation would move all the disclosure into single press release and accompanying Form 8-K. And, it can be done without reducing the key disclosures that investors rely upon or changing the materiality standard that has been the compass for investors for nearly a century.

We understand that Rep. Ann Wagner will offer draft legislation that would address this issue and allow public companies to have optionality with respect to Form 10-Q filings. We support the Wagner legislation and look forward to working with the Subcommittee to see that bill move forward.

**Short Selling Transparency**

As Congress has recognized, it is incongruous that certain investors who accumulate long positions are required to publicly disclose their holdings, but there is no corresponding obligation for short sellers to do so, including those using synthetic or derivative instruments, which allow an investor to profit from a loss in value of the underlying security. This asymmetry has several deleterious effects: it deprives investors of information they can use to effect meaningful investment decisions, it deprives companies of insights into trading activity and limits their ability to engage with investors, and it deprives the market of information to ensure it functions efficiently and fairly. The Commission's Dodd-Frank rulemaking made important enhancements to transparency, and it deserves credit. However, Dodd-Frank provides the Commission with the mandate to make further enhancements, and lift the veil of secrecy behind which short sellers operate, and the SEC has not yet done so.

The obligation of investors to disclose long positions, and when they must do it, is part of a 49-year old regulatory disclosure regime and stems from amendments to the Securities Exchange Act of 1934 set forth in the Williams Act, adopted by Congress in 1968. As currently enacted, these rules require, among other things, investment managers and funds that own or have discretion over prescribed amounts of equity securities, regardless of whether they are registered with the Commission, to disclose their long positions on Form 13F, Schedule 13D and/or Schedule 13G, depending on the circumstances. Such investors must generally disclose their long positions on Schedule 13F within 45 days of the end of each calendar quarter, subject to delays based on requests for confidentiality. Further, when such investors acquire beneficial ownership of more than five percent of the voting class of a company's equity securities, they are generally required to file a Schedule 13D with the Commission. This filing must be made within ten days after the five percent threshold is exceeded.

However, if such investors are either Qualified Institutional Investors or Passive Investors, they may make such disclosure on Schedule 13G within 45 days of the end of a calendar year, subject to updated disclosure-based changes in ownership positions.

There are no comparable public disclosure requirements in the U.S. applicable to the accumulation of short positions. Instead, short sellers can amass short positions secretly, abetted by increased use of derivatives and other synthetic instruments. This is particularly untenable in light of the fact that in recent years, investors with short positions, or derivative equivalents, have taken a more activist role in corporate policy and governance. Because there is no disclosure required of short positions, the investing public and issuers do not know when such circumstances exist or whether the incentives of these investors are inconsistent with corporate policies and objectives. As a result, without full

information about short positions maintained, investors and companies are left to speculate on short positions, to the detriment of market efficiency, price discovery and shareholder engagement. This information deficiency potentially subjects a company's stock price to trading and volatility based on rumor, speculation and innuendo, not facts or substantive analysis.

In December of 2015, I wrote to the SEC outlining these points and requested that the Commission promulgate rules for a short selling regime. This position has been echoed by other organizations such as BIO, NYSE and others. It is time for Congress to step in and require it.

**Proxy Access Reform**

Nasdaq supports shareholder-friendly regulations that provide healthy interactions between public companies and shareholders. However, current regulations governing the way shareholders access a company's proxy statement can poison the company-shareholder relationship by amplifying the voice of a tiny minority, over the best interests of the vast majority. The cost to public companies, and their shareholders, in legal expense, let alone the time and attention of management and boards, is real and significant.

According to The New York Times, three individuals were responsible for 70% of all proposals sponsored by individuals among Fortune 250 companies in 2014.[9] The current process is costly, time-consuming and frustrating for companies, which in aggregate each year must address hundreds of such proposals plus address the many others threatened. Recent action by the SEC to clarify when an initial proposal can be excluded as an ordinary business matter is helpful, but Congress should adopt the proposed legislation to modestly increase the shareholder support that a proxy proposal must receive before a properly introduced proposal can be reintroduced, time after time, at future meetings. We support the alternatively proposed thresholds of 6 percent, 15 percent, and 30 percent of shareholder support for the first, second, and third time a matter is considered within five years before the same proposal can be reintroduced.

In addition, we continue to monitor opportunities to improve the initial thresholds for proxy access. For instance, the $2,000 in market value threshold seems out of date and ill-suited for most companies.

The SEC should study the categories of topics suitable for shareholder proxies and modify its rules accordingly, to ensure proposals considered at annual meetings are properly placed before shareholders and are meaningful to the business of the company, and not related to ordinary business matters.

[9] Grappling With the Cost of Corporate Gadflies by Steven Davidoff Solomon (August 19, 2014), available at https://dealbook.nytimes.com/2014/08/19/grappling-with-the-cost-of-corporate-gadflies/.

Rep. Sean Duffy has proposed legislation that we support to adjust the resubmission thresholds for proxy proposals. H.R. 5756 offers a fair and balanced approach for companies and those seeking proxy access.

**Testing the Waters and Confidential Filing Exemptions**

There are two draft bills before us that deal with the important topics of testing the waters and confidential filings at the SEC.

The ability to file draft registration statements confidentiality at the SEC, which was first mandated for Emerging Growth Companies (EGCs) through the JOBS Act, would be expanded to all companies by statute in one bill. We support this legislation.

The JOBS Act confidential filing provision removed an impediment to going public that resulted in many new, successful public companies, without any loss of investor protections. The historical process included associated costs in terms of the loss of business confidential information that caused many companies to defer going public, unless all other options were exhausted. Now, companies can explore all capital raising opportunities simultaneously.

The SEC under Chairman Clayton quickly recognized the benefits of expanding the opportunity to file confidentially, and acted through its use of staff discretion. The proposed legislation would wisely codify this action.

The legislation would also allow all companies, not just Emerging Growth Companies, to test the waters. Again, this provision originally found in the JOBS Act has proven to facilitate companies going public without harming investors. The new bill allows the SEC to issue regulations to impose terms and conditions on issuers, other than Emerging Growth Companies, that take advantage of the ability to test to the waters in order to ensure investors are protected. We support this protective provision.

The second bill would codify a rule the SEC proposed in 2010 that would allow well-known, seasoned issuers to authorize an underwriter to act as its representative in communicating about an offering of the issuer's securities prior to the filing of a registration statement. We believe this is a modest proposal that practically extends the benefits of an existing capital-raising provision to an issuer's agents or representatives.

**Other Proposals Noticed by the Subcommittee**

The Subcommittee is also considering several legislative items on which we have worked with a broad coalition. These bills make XBRL optional for EGCs, increase research coverage for smaller companies, direct the SEC to align several smaller reporting definitions, expand the JOBS Act by eliminating certain phase outs, and increase the ability of mutual funds to invest in EGCs. We join our coalition partners at BIO, the U.S. Chamber, Equity Dealers of America, National Venture Capital Association, SIFMA, TechNet and the American Securities Association and others to support this legislation.

**Conclusion**

We appreciate the opportunity to present Nasdaq's views on a set of proposals that preserve critical investor protections, while facilitating capital formation, job growth and innovation.

These are not partisan bills. They should not be viewed as controversial. They are part of the natural process of responding to the ever-changing economy and adjusting rules based upon years of experience. This is a healthy process that has served to keep our markets modern and competitive.

Thank you Mr. Chairman and Members of the Subcommittee.