



January 8, 2018

**VIA Electronic Submission**

*pubcom@finra.org*

Jennifer Piorko Mitchell  
Office of the Corporate Secretary  
FINRA  
1735 K Street, NW  
Washington, DC 20006-1506

**Re: FINRA Regulatory Notice 17-14  
Response to FINRA's Request for Comments on FINRA Rules Impacting  
Capital Formation**

Dear Ms. Mitchell:

OTC Markets Group Inc.<sup>1</sup> ("OTC Markets Group"), on behalf of its wholly owned subsidiary OTC Link LLC ("OTC Link"), respectfully submits to the Financial Industry Regulatory Authority, Inc. ("FINRA") the following comments on FINRA Rule 6432 ("Rule 6432") in response to FINRA's request for comments in FINRA Regulatory Notice 17-14. OTC Link is a FINRA member broker-dealer operating an SEC registered ATS that provides a network facilitating broker-dealer trading in OTCQX®, OTCQB®, OTC Pink® and other securities.

**INTRODUCTION**

OTC Markets Group made comments to the Securities and Exchange Commission (the "SEC") on Rule 6432 when it was last amended in 2014.<sup>2</sup> We continue to believe that the cumbersome operational processes around Rule 6432, and the related Rule 15c2-11 ("Rule 15c2-11") under the Securities Exchange Act of 1934 (the "Exchange Act"), unnecessarily impede capital formation by small issuers. As a result, these rules contribute to the unnecessary difficulties faced by smaller companies seeking to access public equity markets in the United States.

---

<sup>1</sup> OTC Markets Group Inc. operates the OTCQX® Best Market, the OTCQB® Venture Market, and the Pink® Open Market for 10,000 U.S. and global securities. Through OTC Link® ATS, we connect a diverse network of broker-dealers that provide liquidity and execution services. We enable investors to easily trade through the broker of their choice and empower companies to improve the quality of information available for investors.

To learn more about how we create better informed and more efficient markets, visit [www.otcmarkets.com](http://www.otcmarkets.com).

OTC Link ATS is operated by OTC Link LLC, member FINRA/SIPC and SEC regulated ATS.

<sup>2</sup> See, OTC Markets Group Inc. Comment Letter on Proposed Amendments to FINRA Rule 6432; File No. SR-FINRA-2014-011, available at <https://www.sec.gov/comments/sr-finra-2014-011/finra2014011-1.pdf>, (the "2014 Comment Letter").

The recent boom in unregistered initial coin offerings (“ICOs”) appears to be a natural reaction to the increasing regulatory barriers and burdens impacting startups and smaller companies using FINRA member broker-dealers to raise capital and facilitate secondary trading. Early-stage companies and broker-dealers face a host of administrative hurdles in the way of accessing price transparency and secondary market liquidity. From clearing a FINRA Form 211, to obtaining DTC eligibility, to a shareholder’s ability to deposit securities, outdated regulations have driven small companies out of the regulated and transparent trading market. Through a thoughtful reevaluation of Rule 6432, FINRA can help clear a path for its member firms to provide more efficient secondary market trading for small cap issuers that have freely tradable securities, as well as better quality, transparent order handling and trade executions for investors.

The core principals of Rule 15c2-11 – that adequate current information is available when a security enters the market – still hold true. However, the world has changed dramatically since this rule was first adopted over 45 years ago, when the Internet did not exist, and investors and brokers often struggled to access company disclosure.

We encourage FINRA to work with the SEC to develop common sense operational solutions that will allow small companies to provide their investors with public disclosure of adequate current information, support competitive secondary trading markets and ultimately improve access to capital. An efficient on-ramp is key to making public markets more attractive to smaller companies. A number of these objectives can be achieved by more thoughtful administration of Rule 6432.

With the overarching goal of making the process of filing a Form 211 more transparent and efficient, we propose the following changes to improve the administration of Rule 6432:

1. **Make the Form 211 Review Process More Objective and Efficient:** FINRA’s involvement in the Form 211 process reaches beyond the scope of Rule 6432 and has become a practical impediment to small companies seeking to access secondary market liquidity. Accordingly, FINRA should make the following changes to its administration of Rule 6432:
  - a. **Objective Notice Filing:** FINRA’s role should not be a gatekeeper performing merit review of each issuer, but instead an industry regulator ensuring that the filing broker-dealer has complied with the objective information criteria required under Rule 15c2-11.
  - b. **Three-Day Turnaround:** As the language of Rule 6432 suggests, a broker-dealer should be able to submit a quotation three days after filing a Form 211, whether or not FINRA has provided a response.
2. **Form 211 Materials Should be Made Public and Issuers Should be Liable for Any Misrepresentations:** FINRA should adopt a disclosure-based approach to Rule 6432 and require that all information submitted in connection with a Form 211 be made publicly available. Additionally, to

- facilitate broker-dealer engagement with small-cap companies, the ultimate responsibility for the accuracy of information provided during this process should lie with the issuer, rather than the broker-dealer.
3. **Outsource Form 211 Processes to IDQs:** Modern day trading venues have become public repositories for information about the securities that trade there. A broker filing a Form 211 should send it directly to the interdealer quotation system (“IDQS”) on which it plans to quote the security. The IDQS should review the filing for completeness, and submit it to FINRA within three days. An IDQS that is a FINRA member should be permitted to file a Form 211 for quotations on its own system of issuers that meet recognized standards, and for certain other “lower risk” securities, as long as the IDQS otherwise complies with Rule 15c2-11. Lower risk securities may include, for example, those listed on a Qualified Foreign Exchange.
  4. **Allow IDQs to Monitor Ongoing Disclosure and Institute Trading Halts:** FINRA member IDQs should be responsible for developing a regime that monitors the ongoing disclosure of securities quoted. Securities of issuers that fail to meet their disclosure obligations should be publicly labeled as late or deficient. The market must be empowered to respond to indications of fraud in a timely manner. As a start, FINRA should give more authority to market operators to initiate trading halts.
  5. **Allow Broker-Dealer Compensation for Form 211 Filing:** In the interest of transparency and price discovery, FINRA Rule 5250 should be amended such that broker-dealers are able to accept compensation from issuers for the preparation and filing of a Form 211, provided that the relationship is disclosed pursuant to Exchange Act Rule 17(b).
  6. **Allow Multiple Market Makers to Quote a Security after a Form 211 is Cleared:** To promote quote competition amongst market makers and price discovery for investors, FINRA should allow multiple market makers to quote a security immediately upon clearing a Form 211 if the information required by Rule 15c2-11 is publicly available. This would replace the current practice where only the sponsoring broker-dealer may publish quotations for the first 30 days after a Form 211 is cleared and cumbersome operational practice of FINRA reviewing multiple Form 211 filings in the same security.

## BACKGROUND

Rule 15c2-11 was promulgated in 1970, long before the Internet provided easy access to company information. The basic idea is sound: proper pricing of a security on the public markets requires a baseline of available issuer information to support the development of an efficient market pricing process. In 2018, the public accessibility of information via the Internet, combined with a requirement that the information required under Rule 15c2-11 be made publicly available, could empower all investors with current information at the start of trading. This would lead to more efficient pricing, less susceptibility to fraud, and ultimately greater confidence in the markets.

Rule 15c2-11 governs the submission and publication of quotations to an IDQS by broker-dealers in securities not listed on a national securities exchange. The rule

requires broker-dealers to review and maintain specified information about the issuer of a security before publishing a quotation for that security in any IDQS, including our OTC Link® ATS.

Unless an exception to Rule 15c2-11 is available, the rule requires a broker-dealer to gather and review, and maintain in its files, one of the following five sets of information: (1) a prospectus specified by Section 10(a) of the Securities Act of 1933 (the “Securities Act”) that has been filed with the SEC and been in effect less than 90 calendar days; (2) an offering circular provided for under Regulation A of the Securities Act, the effective date of which must be within the preceding 40 days; (3) if the issuer is current in its SEC filing obligations, the issuer's latest Form 10-K and all subsequent Form 10-Qs and Form 8-Ks; (4) if the issuer is exempt from Section 12(g) of the Exchange Act pursuant to Rule 12g3-2(b), all the information the issuer has published pursuant to that rule since the beginning of its last fiscal year; or (5) a collection of sixteen items of information about the issuer, including financial information that is reasonably current on the day the quotation is submitted.

Rule 6432 is intended to ensure broker-dealer compliance with Rule 15c2-11. Under Rule 6432, a FINRA member firm must file with FINRA a Form 211 that contains the information required under Rule 15c2-11, as well as the price at which the broker intends to initiate quotations and the basis upon which such price was determined.

According to Rule 6432(a), a broker-dealer may submit quotations three days after a Form 211 is filed with FINRA. In practice, however, FINRA will not issue a trading symbol or otherwise permit trading until it has completed a review of the filing, which generally includes requests for additional information. FINRA’s additional information requests frequently include non-public information and, in some cases, *material* non-public information beyond the scope of the information required under Rule 15c2-11. As a result, it may take weeks or longer from the time of filing before a FINRA member firm may submit a quotation.

For 30 days after the Form 211 has been cleared by FINRA, only the broker-dealer that filed the Form 211 may publicly quote the security. Under the “Piggyback” exemption, other broker-dealers may enter quotations in the security only after the filing broker has quoted the security on at least 12 business days during the preceding 30 days, with not more than four consecutive business days without quotations. This practice interferes with the creation of a larger, more efficient public market for the security.

Finally, FINRA Rule 5250<sup>3</sup> prohibits broker-dealers from accepting any payments from an issuer for, among other things, the preparation and filing of a Form 211, and further requires a certification that no such payments have been made or will be accepted.

---

<sup>3</sup> FINRA Rule 5250(a) provides that “[no] member or person associated with a member shall accept any payment or other consideration, directly or indirectly, from an issuer of a security, or any affiliate or promoter thereof, for publishing a quotation, acting as market maker in a security, or submitting an application in connection therewith.” Certain “bona fide” services are exempt from Rule 5250, including underwriting and other investment banking services.

This frustrates the ability of broker-dealers to form a relationship with the issuer and perform the due diligence and information gathering required by Rule 15c2-11 and Rule 6432.

## **WHY RULE 15c2-11 AND RULE 6432 FAIL TO ACHIEVE THEIR STATED PURPOSES**

The purpose of Rule 15c2-11 and Rule 6432 is to prevent and deter “microcap fraud.” In its 1998 rule proposal to amend Rule 15c2-11, the SEC stated that “[m]icrocap fraud frequently involves issuers for which public information is limited, especially when issuers are not subject to reporting requirements” and further noted that “[w]ithout information, it is difficult for investors, securities professionals, and others to evaluate the risks presented by microcap securities.”

While we have no doubt that “sunlight is said to be the best of disinfectants; electric light the most efficient policeman” the fact is that Rule 15c2-11 – as currently implemented – is not a disclosure rule. While broker-dealers must gather information about an issuer, there is no requirement that the information be shared with the investing public. Broker-dealers are required to provide the information gathered to investors on request, but investors are unlikely to go through the trouble to make such requests because the information supplied on Form 211, and much more, is readily available on the OTC Markets Group website, issuers’ own websites and other online sources. Similarly, Rule 6432 does not require FINRA to share the information provided on Form 211s with the public, and there is no existing procedure in place to disseminate this information to investors. It follows that the information gathering requirements of Rule 15c2-11 do not enable “investors, securities professionals and others to evaluate the risks presented by microcap securities,” because the information is not required to be made publicly available through FINRA or the filing broker-dealer.

Rule 15c2-11 would have significantly greater utility if it required that, when a security is newly traded, adequate current information must be publicly available. That would allow investors to make an informed assessment of the financial position and prospects of the issuer.

It is certainly true that broker-dealers control access to the markets for OTC equity securities. Some aspects of Rule 15c2-11 suggest that broker-dealers assume additional responsibility in performing this role. Accordingly, broker-dealers are required to form a “reasonable basis under the circumstances” for believing that the information gathered under Rule 15c2-11 is accurate.

Broker-dealers undertake that task, and review the source of the information to make the “reasonable basis” determination. IPO underwriters have a contractual agreement with the issuer and a significant financial stake in the offering, but FINRA Rule 5250 prohibits broker-dealers filing a Form 211 from receiving any compensation for their work in compiling and reviewing issuer information. As a result, Rule 15c2-11 provides a good baseline for ensuring that issuer information exists, but does not facilitate

broker-dealer engagement with issuers, ensure investor access to in-depth information that would help investors make an investment decision, or help regulators prevent and detect fraud.

Rule 15c2-11 and Rule 6432 are not designed to be merit review or gatekeeper rules for determining what securities can be quoted publicly. Public quotes provide additional information to investors in the form of price discovery. Securities that are not ‘approved’ for quoting under Rule 6432 may still be traded on the opaque Grey Market<sup>4</sup>, where spreads are wider, volatility is higher, and investors have even less information available. Rule 6432 can best serve the market by ensuring (i) that a quoting broker has formally reviewed and confirmed that a baseline of company information, (ii) that the company information is made publicly available, and (iii) that investors have access to market pricing information. OTC Markets Group and others can then categorize the degree of information made available by the company, providing yet another layer of valuable market transparency.

We share FINRA and the SEC’s interest in protecting against microcap fraud. However, Rule 15c2-11 and Rule 6432 are not the right tools with which to pursue this goal. They also present the added burdens of negatively impacting capital raising by smaller U.S. companies, and preventing U.S. investors from investing in well-respected foreign companies that might help them to better diversify their investment portfolios.

For these reasons, we encourage FINRA and the SEC to work with operators of IDQs and modernize the operational process of Rule 6432 in ways that would encourage small companies to engage with regulated public marketplaces and benefit the investing public.

### **OTC MARKETS GROUP: MAKING THE FORM 211 PROCESS MORE EFFICIENT**

OTC Markets Group is the operator of OTC Link ATS, the primary IDQS for broker-dealers to quote and trade securities that are the subject of a Form 211. For many smaller companies, the markets provided by OTC Link ATS are their first introduction to the public securities markets.

Investors are much more likely to participate in capital raising initiatives if they know their securities will have easy access to a secondary market when the securities have become seasoned or are freely tradable. Secondary markets, such as those provided by OTC Markets Group, and national securities exchanges, therefore indirectly facilitate capital raising by enabling investors to resell securities in public trading markets. *Any rule that unnecessarily restricts the ability of investors to purchase and sell securities in public trading markets inhibits capital raising and hampers the proper allocation of capital in the nation’s economy.*

---

<sup>4</sup> “Grey Market” refers to securities that broker-dealers are not willing or able to publicly quote because of a lack of investor interest, company information availability or regulatory compliance.

Recent years have seen fewer small company IPOs, as underwriting a registered securities offering has become much more complicated, expensive and time consuming. Consider that maintaining a listing on a national securities exchange costs an average of over \$1,000,000 per year.<sup>5</sup> These economics have made public offerings on a national securities exchange unsustainable for a small company seeking to raise \$10 million to finance a promising new software venture, build a small 3D printing establishment or fund other small commercial ventures.

### Incentivizing Company Disclosure

OTC Markets Group is central to any thoughtful analysis of Rule 6432 and how information about OTC securities is obtained and made publicly available. Our tiered market system incentivizes companies to make consistent, high-quality regulatory reporting and disclosure freely available to the public directly on our website. The SEC has recognized our OTCQX and OTCQB markets as “Established Public Markets” for the purpose of determining a public market price when registering securities for resale in equity line financings.<sup>6</sup> State regulators across 28 states have recognized the disclosure required by OTCQX and OTCQB, and have made those markets exempt for the purpose of their blue sky secondary trading registration requirements. As a result of these recognitions, among other factors, companies are incentivized to qualify for the highest possible market tier, which in turn leads companies to improve the quality and increase the frequency of their initial and ongoing public disclosure.

OTC Markets Group operates under the standard proposed herein: to ensure that adequate current information is made available to investors so that they can make an informed investment decision. We maintain objective standards for our three market tiers, based on the quality and quantity of information that companies make publicly available on our website:

- OTCQX® Best Market – To qualify, companies must meet high financial standards, Penny Stocks, shells and companies in bankruptcy cannot qualify for OTCQX.
  - U.S. companies must provide PCAOB audited financials
  - International companies must be listed on a Qualified Foreign Exchange
  - All companies must be current in their reporting requirements
  - Must follow best practice corporate governance standards
  - Must have a professional third-party sponsor introduction
- OTCQB® Venture Market – To be eligible, companies must be current in their reporting must meet \$0.01 bid test and may not be in bankruptcy.
  - U.S. companies must provide PCAOB audited financials
  - International companies must be listed on a Qualified Foreign Exchange
  - All companies must be current in their reporting requirements

---

<sup>5</sup> IPO Task Force, Rebuilding the IPO On-Ramp, at 9 (Oct. 20, 2011), available at: [https://www.sec.gov/info/smallbus/acsec/rebuilding\\_the\\_ipo\\_on-ramp.pdf](https://www.sec.gov/info/smallbus/acsec/rebuilding_the_ipo_on-ramp.pdf).

<sup>6</sup> SEC Compliance and Disclosure Interpretations, Question 139.13 (May 16, 2013).

- Must undergo an annual verification and management certification process
- Pink® Open Market – With no minimum financial standards, this market includes foreign companies that limit their disclosure, penny stocks and shells, as well as distressed, delinquent, and dark companies not willing or able to provide adequate information to investors.
  - Pink Current Information: Companies that are current in their reporting requirements under the OTC Markets Group Alternative Reporting Standard or SEC, International, Regulation A or U.S. Bank reporting standards
  - Pink Limited Information: Companies with financial reporting problems, in economic distress, or bankruptcy, that make limited information publicly available are marked with a red “YIELD” symbol
  - Pink No Information: companies that do not provide disclosure are marked with a red “STOP” sign

OTC Markets Group monitors OTCQX and OTCQB company disclosure and removes companies that become delinquent in providing the required information. In addition to the above designations, OTC Markets Group also designates certain securities as “Caveat Emptor” and places a skull and crossbones icon next to the stock symbol when it becomes aware of certain suspicious activities, including promotional activities without adequate disclosure, fraudulent or criminal investigation, trading suspensions, undisclosed corporate actions and other public interest concerns.

OTC Markets Group has successfully harnessed market forces to incentivize issuers to provide current disclosure. In fact, Pink securities that have been identified as “Pink Limited Information” or “Pink No Information” represent a very small portion of the OTC marketplace, making up just 1% of the total dollar volume traded on OTC Markets Group’s various markets in 2016.

Often, despite otherwise complying with the robust standards and disclosure requirements outlined above, small companies are deterred or prevented from accessing public markets due to roadblocks or lengthy delays in the Form 211 process.

As the primary market for OTC securities, we implore FINRA to work with the SEC to provide a streamlined and transparent Form 211 process, which would free up FINRA’s valuable staff resources and allow investors increased access to new investment opportunities.

## **THE ADMINISTRATION OF RULE 6432 SHOULD ENCOURAGE PUBLIC DISCLOSURE**

FINRA should take care in its administration of Rule 6432 to ensure it encourages company disclosure without unnecessarily stifling capital formation and the development of small company public trading markets. The Rule should provide a cost effective on-ramp to public markets for companies that make adequate current



information available. Accordingly, we propose the following changes to Rule 6432 and its administration:

**(1) FINRA Should Make the Form 211 Process Objective and Efficient by Adopting an Objective Review Standard and a Three-Day Notice Filing**

The Form 211 process has become a drawn-out “approval” decision made by FINRA staff on undefined company “merits.” The process often takes months, rather than the three-day objective review process to determine that the appropriate information has been gathered, as contemplated by Rule 6432. Accordingly, Form 211s should only be reviewed to ensure that the required information is available, and broker-dealers should be able to begin publishing quotations in the security within 3 days of filing the Form 211 with FINRA.

Regulation A offers a prime example of how FINRA’s Form 211 review process has fallen behind the times. The recent improvements to Regulation A better accommodate the needs of smaller public companies, and early results show promise. But, securities issued under Regulation A, although immediately freely tradable under the SEC’s regulation, cannot be quoted by broker-dealers until and unless a Form 211 is submitted and approved by FINRA. The 211 “approval” process for Regulation A securities often takes much longer than securities issued under more familiar regulations. The delays by FINRA in approving Form 211s therefore serve to hinder capital raising by small companies seeking to finance their operations or expansion using Regulation A.

This inhibits small company capital raising on its own, and is particularly frustrating because ***under Rule 15c2-11(a)(2), a Regulation A offering statement is sufficient information to allow a broker to publicly quote a security.*** Therefore, Regulation A offerings should be among the *fastest* Form 211 reviews, with FINRA just checking the SEC’s EDGAR system to ensure that the Form 1-A is posted and has been cleared by the SEC. Unnecessarily hindering secondary market trading of securities issued under a qualified Regulation A offering undermines the goals of the JOBS Act.

U.S. investors also remain interested in companies listed in foreign markets. Many of these companies, such as BMW and Roche, have substantial operations in the United States and employ thousands of U.S. employees. In the U.S. markets, most of the securities issued by these well-known global companies cannot be traded in the United States until a Form 211 has been filed and approved by FINRA. FINRA’s Form 211 reviews of these companies have been known to take well more than the 3 days outlined in Rule 6432. It is difficult to understand what regulatory goal is being accomplished with such lengthy reviews of companies listed on Qualified Foreign Exchanges. Delays by FINRA in approving Form 211s for these companies inhibits U.S. investor access to global investment and limits the ability of these companies to build and expand their operations in the United States.

Our federal securities laws do not contemplate that securities regulators will decide which securities should be offered to the public or publicly traded. Instead, we rely entirely on investors to make appropriate decisions when they have received adequate

disclosure. In administering Rule 6432, FINRA should take heed of this disclosure-based approach. When all the information specifically required under the rule has been provided, there is no reason why the Form 211 review period should take any longer than the prescribed three-day notice period.

FINRA regularly asks issuers for additional information that is not otherwise required under Rule 6432. This supplemental information may include material non-public information, which is never disclosed to other broker-dealers and the investing public. Broker-dealers and investors with no relationship to the issuer should be able to access the same information that FINRA and the sponsoring broker have access to.

Accordingly, FINRA should scale back its Form 211 review process and implement the following changes: (a) all information provided pursuant to Rule 6432 is reviewed and approved under an objective standard; and (b) Rule 6432 should be a “notice” filing whereby broker-dealers are permitted to quote a security within three days of filing a complete Form 211.

## **(2) Information Collected During the Form 211 Process Should be Made Publicly Available and Issuers Should be Responsible for the Accuracy of Disclosure**

Rule 15c2-11 and Rule 6432 require broker-dealers to certify that they have a reasonable belief the issuer information is accurate and from reliable sources. For companies listed on a foreign stock exchange, current in their SEC reporting, or publicly disclosing financial statements audited by a PCAOB registered accounting firm, this should be a relatively straightforward, formal review process.<sup>7</sup> This information has been produced by the issuer and reviewed by a regulator or qualified third party, and broker-dealers should not be responsible for performing a quasi-merit review of the issuer’s honesty or uncovering fraudulent disclosure.

FINRA’s rules should focus on an objective, disclosure-based approach premised on the public availability of adequate current information. This would facilitate investors making an informed judgment about risks and whether to invest in the security. Under this policy, the issuer should be ultimately responsible for the accuracy of information provided to FINRA, broker-dealers and the public.

The European Securities and Markets Authority (“ESMA”) takes a similar holistic regulatory approach to non-exchange markets that serve smaller companies. The revised Markets in Financial Instruments Directive (“MiFID II”) establishes a new SME Growth Market designation (“SME-GM”) and regulatory regime aimed at facilitating access to capital for early-stage companies with a dual objective of (1) minimizing administrative burdens for smaller companies, while (2) promoting investor protection and confidence in SME markets.

---

<sup>7</sup> In addition, it may be more complicated to collect the information if a company has recently issued securities under a confirmed plan of bankruptcy reorganization, however there should be little question that such information is accurate and reliable since a Federal Bankruptcy court has approved it.

ESMA advocates for a disclosure-based framework where SME-GM market operators are responsible for ensuring that sufficient information is made publicly available, enabling investors to make an informed investment decision. Rather than a one-size-fits all approach, operators of SME-GMs are afforded the flexibility to choose a model best-suited to serve the market's investors and issuers. In determining whether a company qualifies for trading on an SME-GM, ESMA believes that the market operator is in the best position to define how the admission materials should be appropriately reviewed. However, ESMA has been very clear that the issuer is ultimately responsible for the accuracy of the information provided and neither market operators nor regulators should be required to formally "approve" the information provided. Once admitted for trading, issuers must make ongoing disclosures and are encouraged to do so directly on the SME-GM website, creating a one-stop-shop for investors seeking information on SME companies.

OTC Markets Group offers a similar disclosure-based model with straightforward, objective criteria for admission to trading on the OTCQX and OTCQB markets. After companies begin trading, they are required to disclose current information, either on EDGAR, with their local regulator or directly on the OTC Markets Group website under our Alternative Disclosure Guidelines, all of which is made publicly accessible on the issuer's quote page on the OTC Markets Group website.

Keeping Form 211 information private and attempting to make anyone other than the issuer responsible for the accuracy of disclosure hinders small company capital formation and serves no purpose in an era where company information is easily accessible. Rule 15c2-11 and the Form 211 process under Rule 6432 should be used to help bring transparency and price efficiency for securities newly entering public markets. Once a quote is published, the market can better categorize the disclosure made available by the subject company and put the appropriate risk protections in place.

Accordingly, all information related to a Form 211 filing should be made publicly available and the issuer, not the broker-dealer, should be responsible for its accuracy and completeness.

### **(3) FINRA Should Allow an IDQS to Take on the Administration of Rules 15c2-11 and Rule 6432**

FINRA should bring Rule 15c2-11 and Rule 6432 into the digital age by allowing FINRA-registered trading systems to participate in the Form 211 process. Specifically, with respect to securities to be quoted on an IDQS, the FINRA member operating the IDQS should be permitted to file its own Form 211 and to review Form 211 filings from other broker-dealers. In each case, the Form 211s should be limited to securities issued by companies that meet recognized standards, and certain other "lower risk" securities.

As to an IDQS filing its own Form 211, Rule 6432 does not prohibit a FINRA member market operator from filing a Form 211. In fact, the "reasonable basis" standard under Rule 15c2-11 could be more effectively employed if an IDQS was able to participate in

the process. Rule 15c2-11 includes in the definition of a quotation “any indication of interest by a broker or dealer in receiving bids or offers from others for a security.”<sup>8</sup> An IDQS filing a Form 211 would be indicating its interest in having other broker-dealers submit bids or offers in the subject security. An IDQS filing a 211 would be obligated to make the company information publicly available, which would ensure that other broker-dealers have full and complete access to the information, thereby fulfilling their own Rule 15c2-11 requirements. This practice would help consolidate valuable information and eliminate the redundant practice of requiring each individual broker dealer to collect and maintain the same records about a security. Given the clear increases in market efficiency and access to information that would stem from this proposal, we ask that FINRA and the SEC reconsider their previously stated positions and work with us to craft the best possible rule for investors, companies and broker-dealers.

Other broker-dealers filing a Form 211 in similarly low risk securities should submit the form the IDQS that will ultimately accept the resulting broker-dealer quotation on its system. The type of review called for by Rule 6432 can best be performed by an IDQS, such as OTC Link ATS. Companies with securities quoted on the OTCQX and OTCQB markets have comprehensive agreements with OTC Markets Group that outline the company’s obligation to comply with certain disclosure requirements and make certain information available on [www.otcm Markets.com](http://www.otcm Markets.com). OTC Link ATS, as a FINRA member broker-dealer, could easily perform reviews under the Rule 15c2-11 standard with respect to companies that qualify for the OTCQX and OTCQB markets and other “lower risk” securities subject to established disclosure requirements, including companies that report to the SEC, companies that have an SEC qualified Form 1-A, or those that list on a foreign exchange and comply with Exchange Act Rule 12g3-2(b).

This would be similar to the European system. Under EU regulations and the ESMA SME-GM regulatory framework, the operator of a multilateral trading facility (the European equivalent of an ATS) handles the initial market entrance requirements and qualifications to initiate trading.<sup>9</sup> We firmly believe that allowing an IDQS to file and review Form 211s for low risk securities will vastly improve the trading and informational experience for investors. Prior to adopting those proposals, at a minimum FINRA should require that Form 211 disclosure materials be provided to, and made publicly available by, the applicable IDQS.

Rule 6432 should therefore be amended to provide that (i) IDQSs may file Form 211s, provided that the applicable information is made publicly available, (ii) Broker-dealer Form 211s will be reviewed by the applicable IDQS, and (iii) Form 211s, and supporting documentation, will be provided to the IDQS on which the broker chooses to quote the security.

---

<sup>8</sup> Rule 15c2-11(e)(3).

<sup>9</sup> “[T]he right balance is struck by giving to the SME-GM operator the ability to define how the admission document should be appropriately reviewed. Key is, however that the admission document clearly states whether or not it has been reviewed or approved and by whom. In this way, admission document readers will not be misled as to the status of the mentioned document.” See, Final Report: ESMA’s Technical Advice to the Commission on MiFID II and MiFIR, p. 361, ESMA/2014/1569 (December 19, 2014).

#### **(4) To Combat Fraudulent Trading Practices, IDQSs Should Implement Ongoing Disclosure Regimes and Have the Authority to Issue Trading Halts**

A majority of the fraudulent activity in microcap securities occurs after a Form 211 has been cleared and the security begins trading. If a trading platform has a contractual agreement with an issuer, the platform is in the best position to monitor and suspend trading when it suspects that the market pricing process in a security has broken down due to misleading disclosure or fraudulent market manipulation.

With the goal of efficiently and effectively preventing microcap fraud, an IDQS should be delegated some authority to monitor the securities trading on its system and, if necessary, halt trading in a security that demonstrates fraudulent activity. For issuers under a contractual agreement, the IDQS should also be able to halt trading on the issuer's request, in circumstances such as news dissemination.

This more dynamic and real-time concept is applied to mitigate ongoing fraud risks in other industries. For example, to apply for a credit card, a user must first meet objective standards and provide certain information. After the user has been approved and the card is issued, activity on the card is monitored by the credit card company. If the credit card company suspects that the holder is engaged in fraudulent activity, is no longer creditworthy, or the account has been hijacked by a third party, the credit card company will temporarily freeze the user's account.

In the context of small company trading, OTC Markets Group is often first to be notified of manipulative trading activity or fraudulent promotional campaigns involving the securities that trade on our markets. In response, OTC Markets Group has developed disclosure-based practices that use visual risk warnings – such as our “Pink No Information” stop sign and “Caveat Emptor” skull and crossbones – to signal to investors that a security may involve a greater degree of risk.

However, only the SEC and FINRA have the authority to halt or suspend trading in an OTC security. Stock promotion schemes can quickly hijack the price of a security, and by the time a regulatory halt becomes effective weeks later, much of the damage has already been done. For example, out of 522 securities identified as being promoted in 2016,<sup>10</sup> only 9 were suspended, often well after the promotional campaign was over and the price had corrected. The ability of an IDQS to quickly implement trading halts and suspensions would greatly reduce the profits reaped from fraudulent promotion and other manipulative trading activities.

We also recognize the need for companies to be able to adequately recover from a trading suspension. Companies that are subject to an unrelated third party promotional scheme and respond appropriately (i.e. by issuing a press release confirming that they have no affiliation with the promoters and correcting any misstatements) should be able

---

<sup>10</sup> This data was provided by [www.theOTC.today](http://www.theOTC.today), a website that monitors and analyzes stock promotion campaigns. The website was independently owned and operated during 2016, and was purchased by OTC Markets Group in 2017.

to quickly rehabilitate and resume trading privileges without suffering devastating consequences that often follow a trading halt or SEC suspension, including the loss of a public quoting and trading market. Just as an IDQS should be able to halt or suspend trading quickly, it must have a path to quickly lift the halt or suspension if the underlying issue is appropriately addressed. Restoring public trading of securities is also key to rebuilding shareholder value when, for example, a new management team is turning around a company harmed by former officers or directors.

Similarly, FINRA could further incentivize issuers to make timely and accurate disclosures by imposing limits on the types of investors that may purchase securities providing less than full disclosure. The limitation on resale to Qualified Institutional Buyers under Rule 144A provides a useful guideline. In the OTC context, issuers that fall behind in their reporting obligations or otherwise fail to make consistent public disclosures could be limited to selling their securities only to accredited investors. Similarly, investors in delinquent reporting OTC companies could be subject to a risk tolerance/sophistication test similar to that used in the options market. Another option would be modifying FINRA's rules governing penny stock and OTC securities to tie an issuer's disclosure activity to investor limitations.

FINRA should adopt disclosure-based policies which grant an IDQS the authority to implement a disclosure regime, identify issuers that fail to comply with requirements, and issue trading halts if the IDQS suspects an issuer is engaged in fraudulent trading activity.

#### **(5) Issuer Payments for Information Gathering and Review Should Be Allowed**

Rule 5250 prohibits issuers from paying for secondary trading services, including services related to the significant information gathering and due diligence review required under Rule 15c2-11 and Rule 6432. This blanket prohibition is based on the policy that broker-dealers should remain independent and unbiased when publishing a quotation or making a market in a security.

This policy is well-intentioned, but ultimately harms small company capital raising.<sup>11</sup> The information gathering and review process required under Rule 15c2-11 cannot be performed without cost. Information gathered by firms during the Form 211 process would be of higher quality and more useful to investors if the sponsoring broker-dealer could be paid for these services. Firms would be incentivized to interact with small cap issuers and provide the much-needed guidance and access to public markets. Rather than prohibiting all payments, FINRA should require that details about the relationship between the issuer and the market maker be fully disclosed to the public.

Accordingly, Rule 5250 should be amended to allow broker-dealers to receive reimbursements for the reasonable out-of-pocket expenses incurred in connection with information gathering and review under Rule 15c2-11 and Rule 6432, provided that the

---

<sup>11</sup> We previously raised these concerns in our 2014 Comment Letter, at pgs 5-7, available at <https://www.sec.gov/comments/sr-finra-2014-011/finra2014011-1.pdf>.

amount of such reimbursements is fully disclosed to investors, as required by Section 17(b) under the Exchange Act.

### **(6) FINRA Should Allow Multiple Market Makers to Quote a Security After the Form 211 is Cleared**

For the first 30 days after a Form 211 has been cleared, only the sponsoring broker-dealer that filed the Form 211 may publicly quote the security. After 30 days, the piggyback exception of Rule 15c2-11 allows additional broker-dealers to enter quotes, thereby creating a larger public market for the securities. If another broker dealer wishes to quote the security during this preliminary 30-day period, it must file a separate Form 211 with FINRA.

Once a competitive market price has been established in a security, the price is a good indicator to investors of the quality of the information available. Healthy secondary markets exist where adequate current information is publicly available and multiple market makers can compete with one another on price, execution quality and liquidity.

Commenters have suggested doing away with the piggyback exemption and requiring all market makers to file a Form 211 before quoting a security. In 1991, and then again in 1998 and 1999, the SEC proposed comprehensive amendments to Rule 15c2-11 – including eliminating the piggyback exemption – to address concerns about fraud and manipulation in the OTC market. The 1991 proposals to do away with the piggyback exemption were based on the belief that the underlying assumption of the piggyback provision – that regular and frequent quotations in a security reflect independent pricing decisions – were no longer valid after Nasdaq exited the OTC market. The 1998 proposed amendments and 1999 re-proposal relied on microcap fraud prevention as a justification for eliminating the piggyback exemption.

This is the wrong approach<sup>12</sup> and would provide a great disservice to small companies seeking an active secondary market. An efficient public trading market provides the best estimate of a security's value based on publicly available information. Price competition increases market efficiency. Removing the piggyback exemption would

---

<sup>12</sup> See SEC Release No. 34-39670 (Feb. 17, 1998) ("The Commission received 75 comment letters from 74 commenters in response to the 1991 Proposing Release. The vast majority of commenters opposed the Commission's proposal. These commenters believed that the proposal would discourage, or even eliminate, market making for many non-Nasdaq OTC securities. They claimed that the proposed amendments would have impaired liquidity, reduced market value, and harmed the capital-raising process. Several commenters believed that the proposed changes would have hurt the market for the securities of many substantial and legitimate companies, but would have little effect on fraud in worthless stocks."); see also, SEC Release No. 34-41110 (Feb. 25, 1999) ("In response to the [1998] Proposing Release, we received 199 comment letters from 193 commenters. Most commenters, which included broker-dealers, issuers, attorneys, and individuals, opposed many of the proposed changes. Broker-dealers were especially concerned that they would be exposed to potential liability in civil actions because of their increased review obligations under the proposal. Commenters also expressed views about the possibility of: reduced liquidity in covered OTC securities if broker-dealers stopped making markets; less transparent markets if broker-dealers did not publish priced quotes to avoid the annual review requirement; less competitive pricing for covered OTC securities; impaired access to capital by issuers; and increased compliance costs for broker-dealers.").

diminish price competition and severely harm capital formation by raising the costs and risks of market making. This would reduce the number of market makers and lower the quality of firms providing market making services.

The piggyback exemption makes it easier for firms to quote and make a market in a security. If a security exhibits certain red flags, more broker-dealers shorting the security will create a more efficient market for the security.

Similarly, allowing multiple broker-dealers to begin publishing quotations in a security immediately after the Form 211 has cleared would remove an artificial barrier to price transparency and promote quote competition. If all the information required under Rule 15c2-11 is made publicly available (e.g. published by an IDQS as contemplated in Section 3 herein) and the quoting broker-dealer has retained such information in its records, there should be no limit on the number of broker dealers permitted to enter a quote in that security. This would do away with the current inefficient practice whereby FINRA can review multiple Form 211 filings in the same security.

Accordingly, FINRA should seek to improve price transparency and liquidity by allowing multiple market maker quoting three days after a Form 211 has been filed.

## **CONCLUSION**

The operational implementation of Rule 15c2-11 is slow, cumbersome and outdated, from a time when information about smaller companies was scarce and difficult to obtain. FINRA has been overly focused on preventing any possible risk of fraud, and as a result Rule 6432 has become a burdensome merit review mechanism for Rule 15c2-11. The Rule 6432 process introduces needless delays into an already difficult process. This creates an undue burden on FINRA member firms, inhibits small company capital formation, and diminishes execution quality and liquidity of freely tradable U.S. and global securities traded by regulated FINRA members.

The time has come to harness modern technology to maximize public information availability, which would empower investors and market participants. In a dynamic world, regulators should look to existing market practices and the wealth of company information and market data already available online to create real-time risk mitigation tools. This will allow regulators to build faster processes to approve securities for trading, ensure that investors have access to adequate current disclosure, and respond to fraud or manipulation.

We recommend that FINRA work with the SEC to make Rule 6432 more efficient and regulatorily relevant by adopting a disclosure-based approach and promoting the public availability of information. As set forth above in greater detail, we believe that the following simple modifications to the administration of Rule 6432 would provide immense benefits to smaller companies looking to access well-regulated secondary markets:



- (1) Making the Form 211 review process more efficient by adopting an objective review standard and implementing a three-day turnaround;
- (2) Requiring that Form 211 materials be made public and issuers (not broker-dealers) be liable for any misrepresentations;
- (3) Outsourcing certain Form 211 functions to IDQs, including allowing an IDQ to file a Form 211 directly with FINRA and to review Form 211 filings submitted by other broker-dealers;
- (4) Allowing IDQs the authority to develop disclosure regimes and initiate trading halts;
- (5) Amending FINRA Rule 5250 to allow broker-dealer compensation for information gathering and Form 211 filing, provided that all such payments are fully disclosed; and
- (6) Allowing multiple market makers to quote a security immediately after a Form 211 is cleared.

We appreciate the opportunity to comment on FINRA's rules regarding capital formation. Please contact me at (212) 896-4413 or [dan@otcm Markets.com](mailto:dan@otcm Markets.com) with any questions.

Very truly yours,

A handwritten signature in black ink, appearing to read 'Dan Zinn', with a stylized flourish at the end.

Daniel Zinn  
General Counsel  
OTC Markets Group Inc.