



March 5, 2020

The Honorable Jay Clayton  
Chairman  
U.S. Securities and Exchange Commission  
100 F Street, NE  
Washington, DC 20549

**Re: New York Stock Exchange 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; Release No. 34-87821; File No. SR-NYSE-2019-67**

Dear Chairman Clayton:

This letter is a follow-up to the American Securities Association (ASA)<sup>1</sup> letter dated December 12, 2019 regarding a proposal by the New York Stock Exchange (NYSE) to expand the use of direct listings to include primary offerings to the general public<sup>2</sup> (NYSE Proposal). We support innovative ideas to promote capital formation for businesses across America so long as they have the appropriate investor protections that have surrounded the initial public offering (IPO) process for over eight decades. The ASA continues to be concerned that if the NYSE Proposal were adopted in its current form by the Securities and Exchange Commission (SEC), then those protections would be significantly undermined.

The Securities Act of 1933 and Securities Exchange Act of 1934 established regulatory oversight for the offering and trading of securities, which up until that point had been virtually nonexistent. Widespread fraud and self-dealing related to the public trading of stocks directly led to the 1929 market crash and shattered the public's trust in our financial markets. The passage of the securities laws and creation of the SEC helped restore the faith of the American people in our capital markets because its mandate was to hold market participants liable for any wrongdoing they may perpetrate. This system has worked remarkably well, and it has made America's capital markets the envy of the world.

A core component of the securities laws – and an indispensable tool necessary to protect investors – is the imposition of liability of on issuers and underwriters under Sections 11 and 12

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<sup>1</sup> The ASA is a trade association that represents the retail and institutional capital markets interests of regional financial services firms who provide Main Street businesses with access to capital and advise hardworking Americans how to create and preserve wealth. The ASA's mission is to promote trust and confidence among investors, facilitate capital formation, and support efficient and competitively balanced capital markets. This mission advances financial independence, stimulates job creation, and increases prosperity. The ASA has a geographically diverse membership base that spans the Heartland, Southwest, Southeast, Atlantic, and Pacific Northwest regions of the United States.

<sup>2</sup> <https://www.nyse.com/publicdocs/nyse/markets/nyse/rule-filings/filings/2019/SR-NYSE-2019-67,%20Re-file.pdf>



of the Securities Act for any material misrepresentations or omissions they make related to an IPO. Interestingly, it remains unclear under the NYSE Proposal whether issuers that pursue a direct listing, or the financial advisors that assist them, would retain liability under Sections 11 and 12. This question is critical to maintain investor trust and confidence in the markets and it is one that the SEC must address before allowing the expanded use of direct listings.

The ASA echoes many of the concerns raised by the Council of Institutional Investors (CII) in its January 16<sup>th</sup>, 2020 comment letter.<sup>3</sup> The CII letter points out that certain shareholder legal rights under Section 11 could be weakened under direct listings and cites ongoing litigation in California regarding Slack's direct listing in June 2019.

In the Slack case, shareholders are alleging that Slack – whose stock price remains roughly 30% below its direct listing in June – failed to disclose certain risks to its business. Slack is making the remarkable argument that it should not be held liable because investors bought a mix of shares when the company listed publicly. They argue that in this mix of shares some were covered by the company's registration statement, while others that were sold by insiders of Slack are not covered because they are not registered with the SEC.

Slack is effectively taking the position that it should not be held liable under Section 11 for false or omitted statements regarding shares that are sold through a direct listing. This alarming argument can't be what the SEC or the broader investing public had in mind when the Slack direct listing was approved.

As reported by the Wall Street Journal in December, the SEC is currently probing some of the trading surrounding Slack's first day of trading. The investigation is part of a larger probe into the communications and practices of certain hedge funds involved in "unicorn" IPOs. The SEC probe into trading activity underscores some of the risks associated with foregoing the traditional underwriting process.

Rather than offering an alternative path forward for more businesses to go public, the Slack offering is a serious warning sign for investors. If the company is successful in its California lawsuit, then investors will have diminished and uneven rights for claims against issuers.

Given that Slack – along with Spotify – is one of the two high-profile companies that have added momentum to the call for direct listings in the U.S., it behooves the SEC to refrain from any further regulatory changes until the California litigation and SEC probe are concluded.

We would also like to highlight Professor John Coffee of Columbia University, who posed a number of important questions regarding investor protections if direct listings were approved as an end-run around the IPO process in the United States.<sup>4</sup> In particular, Prof. Coffee questions whether financial advisors to a direct listing can or should be held liable under Sections 11 and

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<sup>3</sup> <https://www.sec.gov/comments/sr-nyse-2019-67/srnyse201967-6660338-203855.pdf>

<sup>4</sup> <https://clsbluesky.law.columbia.edu/2018/01/16/the-spotify-listing-can-an-underwriter-less-ipo-attract-other-unicorns/>



12 as an underwriter would in a traditional IPO. Prof. Coffee also raises concerns over short-sellers exploiting pricing uncertainties at the time of a direct listing. In a traditional IPO, underwriters typically act as a stabilizer against “bear raids” in the period immediately following the listing – a practice that does not exist in a direct listing.

The wild fluctuations in “unicorn” valuations over the last several years should give the SEC pause as it considers approving direct listings. Certain companies, such as WeWork, demonstrate the real risks companies would pose to Main Street investors if they were permitted to sell shares at unvetted valuations. In other words, direct listings without the appropriate protections could provide a strong incentive and an easier path for company insiders to cash out at inflated valuations, leaving “Mr. and Mrs. 401k” holding the bag.

The NYSE Proposal is not consistent with the Commission’s overarching mission of (1) protecting investors and (2) maintaining fair, orderly and efficient markets and (3) facilitating capital formation. Investors would be exposed to companies with unsustainable valuations and have little legal recourse if an issuer engages in wrongdoing. Short sellers could exploit price inefficiencies associated with direct listings, and confidence in our public markets would likely be eroded as investors get burned by the absence of lock-ups, due diligence, and liability for issuers and underwriters.

Ferdinand Pecora, the lawyer who led the Senate’s investigation into the financial abuses that contributed to the 1929 market crash and Great Depression, stated that his investigation uncovered a “shocking disclosure of low standards in high places.” The SEC should not encourage the lowering of standards for IPOs because this will put investors at risk and increase the chances of fraud in our markets.

We reiterate the position in our December letter: at a minimum, the SEC should make clear that financial advisors, exchanges, control shareholders, and directors involved in a direct listing automatically incur statutory underwriter liability under the 1933 Securities Act and be required to hold the regulatory capital necessary to act as a de facto underwriter.

Sincerely,

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