The Honorable Jay Clayton
Chairman
Securities and Exchange Commission
100 F Street, NE
Washington, DC 20549-1090

May 10, 2018

Re: Market Structure for Thinly-Traded Securities

Dear Chairman Clayton:

I am Don Ross, chief executive officer of PDQ Enterprises, LLC. PDQ's CODA Markets subsidiary aims, as our web site says, to assist investors by "reducing market fragmentation and eliminating flaws in conventional trading platforms." This aim is particularly relevant to the subject of thinly-traded securities, so I appreciate the opportunity to comment on this topic and my firm applauds the efforts of the Securities and Exchange Commission to highlight existing problems and examine potential solutions.

As was emphasized repeatedly in the Commission's April 23 Roundtable on Market Structure for Thinly-Traded Securities, the root problem behind small-cap illiquidity is "temporal fragmentation." That is, buy and sell orders don't match owing to arrival at different points in time. Of course, investors can always place limit orders and wait, but the costs of information leakage and adverse selection typically outweigh the benefits of displayed patience.

Market intermediaries are only too happy to suggest regulatory interventions as solutions, as these have the tendency of benefiting their proposers unambiguously while bearing only a tenuous hypothetical relationship with lowering issuer cost of capital and raising investor returns. Most notably, the broker community successfully lobbied the House of Representatives into passing 2014 legislation backing their long-standing goal of widening small-cap tick sizes from one cent to five.

Since 2016, the Commission has allowed 1200 companies with market caps below $3 billion to trade at a 5 cent tick. Despite the self-interested and logically dubious claims that brokers would plow higher profits into analyst research, which would—in textbook virtuous-cycle fashion—stimulate investors to buy small caps, trading volumes have not increased. The only beneficiaries have, not surprisingly, been the brokers whose round-tripping profits potentially quintupled.

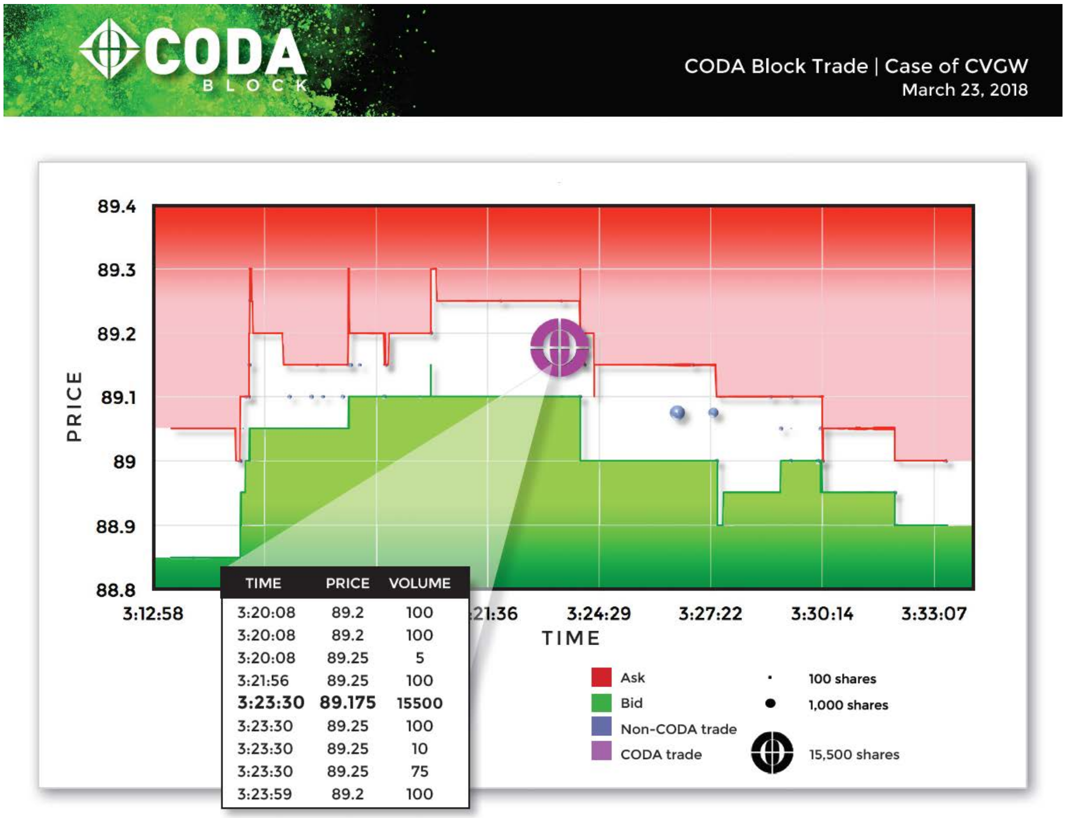
Not to worry, say the exchanges. We too have a suggestion: prohibit the trading of small caps outside their listing venue. Liquidity will then cease fragmenting spatially—across trading venues. Never mind that the small-cap problem is *temporal*, and not spatial,[i] and that the proposal is only sure to increase trading and market-data fees on the beneficiary exchanges. They are now selling the putative public benefits of such government-granted monopolies under the guise of "company choice." Yet since listed companies are owned by shareholders, the proposal amounts to nothing more than a denial of shareholder choice.

I would, in short, urge the Commission to reject transparently self-interested proposals from intermediaries, such as widening spreads and lessening competition, and to consider instead whether the market model relied upon by such intermediaries—displayed liquidity in continuous markets—is actually appropriate for all small companies. Some may simply be better off trading through private negotiation;

others—the type on which my young firm has focused its R&D—are better off trading in public auctions that mitigate temporal fragmentation.

CODA Markets runs a market structure very different from those we see on the exchanges. We run auctions—all day, on demand. Without having to reveal how much one wishes to buy or sell, or even whether one is a buyer or a seller, investors can initiate CODA auctions that *summon forth and aggregate new liquidity*—liquidity not residing anywhere else. As one might expect, our market structure is tailored to the trading of both *large blocks* of securities and *thinly-traded* ones—trading for which temporal fragmentation is problematic.

It is important to stress that in the absence of competitors like CODA, the market would simply not see such innovations. The NYSE has, for example, rejected mid-day auctions owing to member fears of information leakage and interference with continuous-trading activity.[ii] Yet our CODA Block platform, recognized as the "Best New Block Trading Product" at the recent 2018 Markets Choice Awards, was shown, in a recent independent study of nearly 100,000 CODA Block auctions, to create no material information leakage or adverse-selection costs. Meanwhile, our trade size for small-cap issues averages 4 times larger than the total size displayed by exchanges at the NBBO at the time of the trade.[iii] Below you can see how a recent small-cap trade on our market compared with others elsewhere just before and after. Our experience demonstrates that the market is capable of manufacturing small-cap liquidity on its own—without special advantages or protections for middlemen.



At the April 23 Roundtable, Director Redfearn indicated that the Commission did not wish to rely on a rule-heavy approach to improving small-cap trading, but rather only to ensure that innovation could do its necessary work. I enthusiastically agree. To this end, however, the rules can be improved. In particular, the order-protection rules in Reg NMS are a costly and anachronistic substitute for best-execution obligations. Reg NMS treats each exchange's top of book, however trivially sized, as if it were a valuable, unique liquidity pool that would not exist outside its host, requiring costly spaghetti-bowl market networking to keep it alive. For systems built on different premises—that the price and quantity traders are willing to *display* bears little relation with what they are willing to *transact*—these rules amount to a misguided tax on innovation. They should therefore be eliminated.

Sincerely yours,

Don Ross, III
Chief Executive Officer
PDQ Enterprises, LLC

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[i] For the least active securities, those trading under 50,000 shares a day, the average number of exchanges quoting at the NBBO is only 1.8 [https://www.sec.gov/files/thinly_traded_eqs_data_summary.pdf].
[ii] See comments of the NYSE's Stacey Cunningham at the April 23 Roundtable.
[iii] [http://www.viablemkts.com/coda-block-auction-analysis/]