



# GATE GLOBAL IMPACT

February 20, 2015

FEB 24 2015

Hon. Luis A. Aguilar,  
Commissioner  
Securities and Exchange Commission  
100 F Street, NE  
Washington, DC 20549

Re: Letter to Director Higgins regarding Proposal to Amend Regulation ATS to Address the Sale of Unregistered Securities

Dear Commissioner Aguilar,

Please find enclosed letter to Director Higgins

We hope that you, the Commission, and the staff find these comments useful and productive as part of a review of the new model of capital formation. As the operator of a trading platform designed to address some of the issues facing small private companies, we welcome the opportunity to discuss with you how the SEC may amend Regulation ATS to facilitate a model that promotes the orderly sale of unregistered securities. If GATE or I can be of further assistance to you in this matter, please do not hesitate to contact me at the address above or [REDACTED].

Very truly yours,

Vincent R. Molinari  
Chief Executive Officer  
GATE Global Impact Inc.  
[REDACTED]

Joseph K. Latona Jr.  
President and Chief Operating Officer  
GATE Global Impact Inc.  
[REDACTED]



# GATE GLOBAL IMPACT

February 20, 2015

**VIA FEDERAL EXPRESS AND  
ELECTRONIC MAIL**

Mr. Keith F. Higgins  
Director - Division of Corporation Finance  
Securities and Exchange Commission  
100 F Street, NE  
Washington, DC 20549

**Re: Proposal to Amend Regulation ATS to Address the Sale of Unregistered Securities**

Dear Mr. Higgins:

GATE Global Impact, Inc. ("GATE") writes this letter to encourage the Securities and Exchange Commission (the "SEC") to review and revise Regulation Alternative Trading System ("ATS") of the Securities Exchange Act of 1934 (the "Exchange Act") and the rules and regulations under the Securities Act of 1933 (the "Securities Act") that address the sale of unregistered securities. While the Jumpstart Our Business Startups Act of 2012 (the "JOBS Act") represents a meaningful step to improve the capital formation process, Regulation ATS has grown increasingly ill-suited to the new model for capital formation that could rely on the internet to facilitate the sale of unregistered securities.

We offer the following comments in the hope of promoting a solution that will best serve the capital formation process, promote economic expansion and job creation.

## **I. Background**

A central element of the investor protection scheme established by the federal securities laws is the comprehensive framework for the registration and regulation of persons engaged in the business of buying and selling securities for the account of others. The Exchange Act is the primary federal legislation governing "brokers" and "dealers" in securities. With certain exceptions, section 15 of the Exchange Act requires registration with the SEC of all broker-dealers using interstate commerce or the facilities of any national securities exchange to effect transactions in securities (other than exempted securities and certain short-term debt instruments). The Exchange Act, SEC rules thereunder, and the rules of self-regulatory organizations ("SROs") prescribe an extensive scheme of regulation for broker-dealers.

The underlying policy for the broker-dealer registration requirement and associated regulatory framework is to provide important safeguards to investors. The Exchange Act's regulatory scheme is designed to ensure that all registered broker-dealers and their associated persons

satisfy professional standards, have adequate capital, treat their customers fairly, and provide adequate disclosures to investors.

#### **A. Section 15**

Originally enacted in 1934, Section 15 of the Exchange Act did not impose specific registration requirements on broker-dealers. Section 15 delegated to the SEC the authority to prescribe rules regulating over-the-counter ("OTC") transactions. Under this authority, the SEC promulgated rules requiring the registration of all broker-dealers involved in OTC transactions. Regulation of transactions on national securities exchanges was primarily granted to registered exchanges. As part of regulatory reforms following the paperwork crisis of 1968–1970, Congress passed the Securities Acts Amendments of 1975, which enacted Section 15(a) in its current form.

#### **B. Duties of Broker-dealers**

Section 15(a)(1) compels registration of most broker-dealers by prohibiting the use by any broker or dealer of the mails or any means or instrumentality of interstate commerce to effect any transactions in, or to induce or attempt to induce the purchase or sale of, any security (other than an exempted security or commercial paper, bankers' acceptances, or commercial bills) unless such broker or dealer is registered with the SEC in accordance with the Exchange Act.

Once registered, a broker-dealer is subject to numerous compliance requirements and obligations under the Exchange Act, as well as rules and regulations promulgated thereunder. The compliance requirements include:

- Meeting certain standards of operational capability and standards of training, experience, competence, and other qualifications established by the SEC;
- Being subject to investigations, inspections, and disciplinary actions by the SEC;
- Complying with minimum net capital requirements, customer protection rules, specific recordkeeping, financial compliance, and financial reporting requirements.

Registered broker-dealers are also:

- Subject to the general antifraud and anti-manipulation provisions of the federal securities laws;
- Required to establish, maintain, and enforce policies and procedures reasonably designed to prevent insider trading;
- Subject to anti-money laundering regulations.

One of the most important requirements for registered broker-dealers is the obligation to be a member of an SRO.

### C. Exchanges

Over the last twenty years, as the roles of broker-dealers and exchanges have blurred, the SEC has sought to distinguish these roles. Section 3(a)(1) of the Exchange Act defines an "exchange" as:

any organization, association, or group of persons, whether incorporated or unincorporated, which constitutes, maintains, or provides ***a market place or facilities for bringing together purchasers and sellers of securities*** or for otherwise performing with respect to securities the functions commonly performed by a stock exchange . . .

Exchange Act Rule 3b-16(a) interprets the Section 3(a)(1) definition to mean any organization, association, or group of persons that:

- Brings together the orders of multiple buyers and sellers; and
- Uses established, nondiscretionary methods (whether by providing a trading facility or by setting rules) under which such orders interact with each other, and the buyers and sellers entering such orders agree to the terms of a trade.

Absent an exemption, an exchange must register as a national securities exchange pursuant to Section 6 and Section 19(a) of the Exchange Act.

Beginning in the early 1970s with Instinet and in the 1990s following the adoption of the Order Handling Rules, a number of broker-dealer hosted crossing engines or electronic communications networks ("ECNs"), lead to the SEC adopting a new model for the regulation of ECNs and crossing engines.

### D. Regulation ATS

In 1998, the SEC adopted Regulation ATS, which required ECNs and crossing engines to choose whether to register as national securities exchanges *or* to register as broker-dealers that host ATs and comply with additional requirements of Regulation ATS depending on their activities and trading volume. An ATS means any organization, association, person, group of persons, or system:

- That constitutes, maintains, or provides ***a market place or facilities for bringing together purchasers and sellers of securities*** or for otherwise performing with respect to securities the functions commonly performed by a stock exchange within the meaning of Rule 3b-16 under the Exchange Act, and
- That does not set rules governing the conduct of subscribers other than the conduct of such subscribers' trading on such organization, association, person, group of persons, or system; or
- Discipline subscribers other than by exclusion from trading.

Any system exercising self-regulatory powers, such as regulating its members' or subscribers' conduct when engaged in activities outside of that trading system, must register as an exchange or be operated by a national securities association.

However, in the 1998 adopting release to Regulation ATS, the SEC noted:

**While the revised regulatory scheme implemented today is designed to address changes in the way securities are traded, *the Commission's assessment of the impact that these systems may have on the trading of unregistered securities* . . . and of the appropriate regulatory posture to these developments, is still ongoing.<sup>1</sup>**

GATE believes the time has come for the SEC to resume the work it commenced in 1998 and consider how best to regulate the sales of unregistered securities through an ATS.

#### **E. Sales of Unregistered Securities**

Section 4(a)(2) of the Securities Act exempts from registration "transactions by an issuer not involving any public offering." Section 4(a)(2) permits an issuer to sell securities in a "private placement" without registration under the Securities Act. Section 4(a)(2), however, is only available to the issuer, and not to persons who have acquired securities from the issuer and who want to resell the securities.

Section 4(a)(1) of the Securities Act exempts from registration "transactions by any person other than an issuer, underwriter, or dealer." A holder of securities who is not an issuer or a dealer can sell securities in a private sale without registration if the holder is not an underwriter. Under Section 2(a)(11) of the Securities Act, a person is an "underwriter" if he or she acquires securities with a view to "distribution" or is participating in a "distribution."

A holder of securities that were issued in a private placement may resell the securities on a *public trading market*, after a holding period, pursuant to Rule 144. A seller who complies with Rule 144 is deemed not to be an "underwriter" under the Securities Act and therefore may sell the restricted shares without registration. "Restricted securities" are defined in Securities Act Rule 144(a)(3) to include, in part, "securities acquired directly or indirectly from the issuer, or from an affiliate of the issuer, in a transaction or chain of transactions not involving any public offering."

There is not, however, a similar rule for the private resale of restricted securities. A holder of securities who wishes to resell them privately under section 4(a)(1) therefore must sell in a transaction that is sufficiently "private" to avoid being considered an underwriter. Over time, the various restrictions on sales considered by the SEC and securities lawyers to permit a resale under 4(a)(1) has been referred to as section 4(1-1/2).

---

<sup>1</sup> *Regulation of Exchanges and Alternative Trading Systems*, Securities Exchange Act Release No. 40760, 63 Fed. Reg. 60,844 (Dec. 22, 1998) (emphasis added).

It is generally considered that for a resale to be private for purposes of section 4(1-1/2), the following conditions apply:

- The sale should be limited to less than 25 purchasers;
- The securities should be ***offered without public advertising or general solicitation***;
- The seller should provide the purchaser with such information about the issuer as is available to the seller, although a seller that is not affiliated with the issuer may not be able to provide anything like the disclosures that would be made in a private placement by the issuer;
- If the seller is affiliated with the issuer, purchasers generally should be limited to those who are sophisticated enough to be able to evaluate the risks of the investment;
- Although no specific holding period is required before the resale of the securities, the seller must not have purchased the securities with a view to resale, and it generally is considered that a holding period of six months or more will evidence the seller's original investment intent; and
- The purchaser should represent that it is acquiring the securities for investment, and not for resale.

While there are a number of regulatory mechanisms to address the sale of unregistered securities, those mechanisms are ill-suited to the use of an ATS or the new platforms that are designed to democratize the capital formation process.

#### **F. JOBS Act and Rule 144A**

In July 2013 the SEC approved a rule proposal to amend Rule 506 of Regulation D and Rule 144A under the Securities Act. The amendments lifted the ban on general solicitation in offerings under Rule 506 and 144A (and added Rule 144A requirements to initial sales thereunder). Rule 144A is a non-exclusive safe harbor exemption from the registration requirements of the Securities Act for sales of certain securities to qualified institutional buyers, or QIBS.<sup>2</sup> Prior to the amendments to Rule 144A, *offers* of securities under Rule 144A were required to be limited to QIBs, which effectively prohibited the use of general solicitation under Rule 144A.

Amended Rule 506 and Rule 144A represent an important change to the process by which issuers may offer securities to potential investors. However, the amendments required by the JOBS Act failed to address secondary sales through ATSs of unregistered securities to investors that do not meet the QIB standard.

---

<sup>2</sup> The term "qualified institutional buyer" is defined in Rule 144A(a)(1) and includes specified institutions that, in the aggregate, own and invest on a discretionary basis at least \$100 million in securities of issuers that are not affiliated with such institutions. Banks and other specified financial institutions must also have a net worth of at least \$25 million. A registered broker-dealer qualifies as a QIB if it, in the aggregate, owns and invests on a discretionary basis at least \$10 million in securities of issuers that are not affiliated with the broker-dealer.

## **II. The Current Model for Registration of Exchanges, Broker-dealers, and ATSS Is Ill-Suited to Secondary Sales of Unregistered Securities**

Private companies are critical to the U.S. economy and their ability to access capital is an important driver for growth, job creation and government tax revenues. These smaller companies have turned to new methods of capital formation, and looked increasingly to private market funding alternatives, while the public market's appetite for new listings waned. New platforms offer small private companies and investors an increasingly transparent model to access capital. As these platforms become more broadly accepted, they will also become increasingly robust and transparent through technological advances. Recently, the spotlight has fallen on the new platforms that are designed to bring finance to the masses and the sale under a new paradigm.<sup>3</sup>

We appreciate the efforts of the SEC, FINRA, and state securities regulators to develop a model for the proper regulation of the use of general solicitation under Rule 506(c), and crowdfund investing. However, the SEC has not addressed how best to regulate platforms that facilitate the sale of unregistered securities. Such platforms are currently required to register with the SEC and FINRA as broker-dealers and ATSS under a regulatory model that was developed in 1934, amended in 1975, and enhanced in 1998. As noted by the SEC in 1998, Regulation ATS did not address the regulation of platforms that facilitate the sale of unregistered securities.

This lack of a suitable regulatory model for ATSS that focus on the sale of unregistered securities has limited investor's access to high-growth investments, and the ability of accredited investors to more efficiently redeploy capital from more mature private companies to early stage companies. We believe that the evolution of the private equity market is unlikely to stop and more issuers will inevitably be limited in their ability to raise capital through platforms that attempt comply with unfinished requirements of Regulation ATS. We encourage the SEC to resume the work it started in 1998 and implement amendments to Regulation ATS to address the sale of unregistered securities through an ATS.

## **III. Conclusion**

GATE believes that while Regulation ATS has played an important role in preserving the integrity of the financial markets and has helped to promote transparency and efficiency in the trading of registered securities, the present regulatory model does not properly address the unique characteristics of new platforms that are designed to democratize the capital formation process. The value of the sale of unregistered securities in an orderly manner that serves to protect the investing public is a cornerstone of the U.S. capital formation process. While the amendments to Rule 506 and Rule 144A permit the use of general solicitation in the offering of unregistered securities, the changes do not address the issue that Regulation ATS failed to properly address in 1998 – how the regulation should apply to the sale of unregistered securities.

GATE encourages the SEC to review and revise Regulation ATS and the rules and regulations under the Securities Act that address the regulation of marketplaces that focus on the sale of unregistered securities. Such regulations will enable the SEC and FINRA to use currently

---

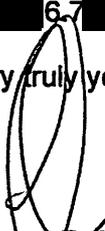
<sup>3</sup> Patrick Jenkins, *Democratizing Finance: Big banks eye peer-to-peer lending push*, Financial Times (Jan. 28, 2015), available at: <http://www.ft.com/cms/s/0/93837c4a-a6db-11e4-9c4d-00144feab7de.htm#slide0>.

available surveillance tools in a manner that will enhance market transparency and liquidity, and that will promote investor protection. We encourage the SEC to address these issues as promptly as possible in order to spur the capital formation process and the growth of small private companies.

We hope that you, the Commission, and the staff find these comments useful and productive as part of a review of the new model of capital formation. As the operator of a trading platform designed to address some of the issues facing small private companies, we welcome the opportunity to discuss with you how the SEC may amend Regulation ATS to facilitate a model that promotes the orderly sale of unregistered securities. If GATE or I can be of further assistance to you in this matter, please do not hesitate to contact me at the address above or

██████████ 67 ██████████

Very truly yours,

  
Vincent R. Molinari  
Chief Executive Officer  
GATE Global Impact Inc.  
██

  
Joseph K. Latona Jr.  
President and Chief Operating Officer  
GATE Global Impact Inc.  
██

cc: Hon. Mary Jo White, Chair  
Hon. Luis A. Aguilar, Commissioner  
Hon. Daniel M. Gallagher, Commissioner  
Hon. Michael S. Piwowar, Commissioner  
Hon. Kara M. Stein, Commissioner  
Robert L.D. Colby, Esq. – Chief Legal Officer - FINRA