10/11/2018

Jennifer Piorko Mitchell
Office of the Corporate Secretary
Financial Industry Regulatory Authority
1735 K Street, NW
Washington, DC 20006-1506

Re: Financial Technology Innovation - FINRA Requests Comment on Financial Technology Innovation in the Broker-Dealer Industry

> *"…supervisory processes concerning the use of artificial intelligence…*
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> *…Applications for artificial intelligence tools… trading,*
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> *…FINRA has also previously stated that: "[A]s the use of algorithmic strategies has increased, the potential of such strategies to adversely impact market… has likewise grown…*
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> *…FINRA is requesting comment on any measures that FINRA could take to clarify or adapt its rules and processes in light of the evolving uses of such tools.14 By asking these questions, FINRA intends to develop a deeper understanding of how artificial intelligence may affect the industry and the steps that FINRA may take to facilitate its use in ways that enhance investor protection and market integrity..."*

Ms. Mitchell,

HFT, A/I, Algos exist for one reason. To harvest cash from the markets more efficiently than the last improvement in technology. They've done a great job. The balance in our ecosystem is slightly out of whack. The path toward restoring the balance for sustainability likely should be initiated in the supervisory process.

We find ourselves in an investment environment whereby companies would rather stay private than list. In 2000 there were 12,000+ companies trading between NASDAQ, NYSE and AMEX. Now there are 4800. GDP is 80% higher. This is a reflection on FINRA and the SEC. People have money. Companies need capital. They just don't find value participating in this automated environment.

The public markets are no longer a venue for capital formation. If a company is under $500,000,000 in market cap and is cash tight, they will likely become a target of a systematic prolonged short attack simply because they are unable to use cash to perform a share buyback defending against strategies which create some volatility and then trade down through the thinned bids.

It's not Sarbanes which prevents companies from doing small IPO's. It's the inability to get a second or a third round off once public. CEOs don't want to subject their life's work to paying exorbitant fees and costs to see their stocks get punished by liquidity shares filling every buyer or HFT's running short ladder strategies.

We've written rules which enable this automated self-destructive behavior. Odd lot price improvement, and removal of the uptick rule both directly benefit automated strategies which destroy investor value.

We also write rules that clearly are devised for the sole purpose to try to favor one group of participants over the rest such as the beloved 5c spread tic trial which recently ended.

Now we are allowing "Artificial Intelligence" to provide a layer of plausible deniability between strategy programmer and the actual order flow. "Sure I wrote it, but who knew the A/I would mark the close?"

The question about supervisory procedures concerning the use of A/I is as relevant as the horse being out of the barn, across the pasture, stolen, slaughtered for glue, finding some meat making it into the food chain, and then asking about a policy and procedure manual outlining the process for oiling the automated gate latch.

FINRA has just proudly announced the new SIE. Made easier to get more humans back into the industry. In changing the exam to hopefully increase the number of people testing and passing, FINRA admits by its action human participation is now our focus.

As an industry, we are at the point where we are laughed at and shunned because of the predatory environment. There's more respect in being a used car salesman, than in being a used stock salesman. Everything is tracked and illuminated. All truths are known. It's time we actually provide value instead of sucking the life out of developing companies and their human investors.

How about we take this opportunity to shift the tone just a bit?

If someone employs HFT, or A/I they need to justify how it benefits the market as a whole. "Liquidity" is not an acceptable answer. Their liquidity can and should be able to evaporate. How do the strategies they employ enhance the listing environment for capital needy companies? Remember, if companies don't want to list, you and I have no job.

If we want to return the US public markets into being the premier venue for capital formation, we need to create an environment where little companies can become big companies. We need to create an environment where loud mouth, low IQ, risk takers can have some prolific wins in tiny companies growing 10x instead of being snuffed because the company can't cashflow a buy back. Right now, the loud mouth, low IQ, risk takers are our carnival barkers until we find a way for humans with their Series 7 to profit from transactions selling individual issues instead of trying to survive on ever shrinking fees for conveying to retail human investors, "we are not smart enough to know our core product, so index".

This redevelopment of sales positions for individual stocks is ultimately FINRA's responsibility. You write the rules. Participants respond. What are you going to create whereby humans can have fun making money selling individual issues? The SIE being a more relevant test is nice. Can these guys have fun making money selling stocks??

The search for balance can start with supervision of process of A/I.

FINRA/SEC can prohibit A/I strategies from shorting companies under $500,000,000 in market cap. They can act long but not short. Same thing can be applied to non-intelligent automated strategies. Anyone who has been subject to compliance exams knows you don't need a rule. The examiner needs tone and tenacity. If the examiner makes the oversight of A/I short strategies under $500,000,000 market cap so cost and time painful, the strategy operators will focus on long only at that market cap range.

The greater you shift the balance away from short selling companies under $500,000,000 in market cap the quicker you will repopulate the markets. I know its blasphemy, but eliminate the use of liquidity shares in the market making of options and stocks for companies under $500,000,000 in market cap. Sure, you'll have companies rise in valuation very quickly. And, yes, they will get 2nd and 3rd rounds off before they hit $500 million.

If companies can raise capital here, more will come. If humans can purchase shares of a small company in which they believe, and have it go well, they'll brag and bring in friends. It becomes a virtuous cycle.

We have Reg FD. We want fair dissemination of information. It's about time. Processing time. Time to act. Time to position for events. Where we are right now with automated strategies vs human participation can be likened to 30 years ago when market makers and certain well moneyed participants would have huge information time advantages on just the regular dissemination of news. Automated strategies provide a time advantage in aggregating, digesting and acting on the information at hand. Great for the guys who've taken the time to develop their personal skill sets to create the strategies. The rest of the humans, issuers and speculators alike, have simply voted with their feet. As regulators you are on a path to ending up with having just 6 surviving tech firms fighting for 401k inflows to harvest.

These are your markets. You regulate. You write the rules. What do you want to structure? You really get to choose. If you are happy with the path of the US financial markets, do nothing differently. If you are happy with a landscape where money is pooled in family offices and they skew toward private equity to avoid what the public markets have become, then do nothing you are doing brilliantly fine.

One knee jerk response would be to mandate all orders be placed, modified, cancelled by a human hand. It would repopulate human market makers for you to register and regulate. It would dramatically increase the amount of human prop traders. These guys all have golfing buddies they would cajole into being investors. Is that a practical shift? Likely not. Fintech strategies are here. What's the balance?

Drawing from the above thought cluster to service the original request for comment:

In our current market environment, fintech strategies as implemented have had the same capital removal effect as casinos developed in small towns. They are very efficient at removing cash from the ecosystem. Good for them. The people designing the strategies have worked very hard to create that success for themselves.

For the health of the markets, there needs to be a small shift in tone towards fostering human participant growth. The implementation of this tone would obviously be structured into the supervision processes employed by the operators of A/I and then flowing over into the operators of un-artificially-intelligent automated strategies.

> Examination question: Please explain how the application of your fintech strategy promotes human participation growth within the US public markets.
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> Examination tone: We want you to harvest well. The pond needs to be continually stocked with guppies that grow to 12 inches before you can catch and keep.
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> Examination mantra: Sustainable Fintech

Logically, you simply have to prime the virtuous cycle. If you turn the US markets into a place where $25 million companies can raise capital and have a clean path toward becoming $500 million companies, it becomes self-perpetuating. Companies will come here because they can raise and prosper. Investors push money into developing companies because the companies receive reduced headwinds if they develop and grow publicly in the US. The cycle repeats. That then becomes a marketable process for Series 7 holders into high risk tolerant investors.

Thanks for the opportunity to respond,

Todd Krajniak
Krajniak Capital Management