March 27, 2007

Ms. Nancy M. Moms
Securities and Exchange Commission
100F Street, NE
Washington D. C., 20549-1090

Ms. Norris,

It was October 2003 that the Securities and Exchange Commission came to their senses and admitted what small investors have discussed openly for years – naked short selling abuses can have a detrimental impact on those select companies whose shares are being traded under abusive settlement failure principles. Since that point in time in which the SEC made such admissions nearly every act thereafter was to derail any type of investor security that the practice would be stopped.

This most recent action, to re-open the comment period of a near year old proposal, is a perfect illustration of the lack of commitment by this staff, the staff of the SEC's Division of Market Regulations to address this problem. In June 2006 the Chairman and his staff praised this group of individuals for maintaining their promise to evaluate the progress of Reg SHO and yet 9 months after that proposal was submitted for comment we are exactly where we started, back for public comment.

The difference between March 2007 and June 2006 are the nine months of additional victims the Commission allowed to be abused by the system. Victims this staff should take full accountability for.

According to the document release by James Brigagliano and his staff, the SEC is re-opening for public comment this proposal based on concerns raised by a small minority of comments [3 to be precise] that solid empirical data was not provided to properly evaluate the need for reforms. Each of those response memo's coming weeks after the SEC did in fact publish the analysis by the OEA with very little additional insight being provided in the documents that the SEC has registered as part of this latest action.

First about the minority trio of commenters who have stalled this reform package:

- American Bar Association submitted their comment memo on September 27, 2007. The ABA had no opinion memo presented during the original 2003/2004 comment phase of SHO where the SEC had provided far less data relative to settlement abuses yet in this proposal the ABA claims the SEC has no right to impose additional changes without providing the evidence to support such changes. If concern over empirical data is at issue, where was the ABA in 2003 and who has lobbied for their support here today?

- Alan Schwartz submitted his comment memo on September 19, 2007 whereby the commenter also stated "There is no rationale for providing explicit regulatory protection to companies which are chronically and/or grossly delinquent with regard to public disclosure."

  While Mr. Schwartz has blocked this reform because of his request for empirical data, this individual lacked the empirical data that would support his accusations that those issuers with settlement failures are in fact "companies which are chronically and/or grossly delinquent."

  Mr. Schwartz provided comment on Reg. SHO as originally presented in 2003. He opposed such regulations at that time claiming that the short sale restrictions were already overly prohibitive.

- CTC LLC submitted their comment memo on September 28, 2007. CTC LLC is an options broker-dealer who has identified in their memo that they are unaware of any direct correlation to options settlement failures and market abuses. For the record, there is no record of CTC having an opinion to present at the time SHO was first up for public comment in 2003.

Of significance to these commenter claims is that the SEC provided the results of their analysis in August of 2006 and therefore made available to these individuals at the time of their comment memo. The SEC, in this re-proposal references that document.

Enough with the overview of who it was the SEC has appeased by this delay. Instead, lets take a closer look at the detail of data that the SEC chooses to put up for public comment and the ultimate value of that data. Each of the three comment memo's published requested specific and clear empirical data that either confirmed or refuted a problem existed. Lets see how well the SEC fared relative to data already in existence.

Data Point #1:

Prior to the Commission's Proposal, the New York Stock Exchange LLC (the "NYSE") informed the Commission that it conducted a review of five securities with substantial aged fail positions from July 1, 2005 through September 23, 2005. The NYSE found that the aged fail positions in these five securities were attributable to one broker-dealer. This broker-dealer informed the NYSE that the fail positions were not being closed out because it was relying on the options market maker exception.

This is statement is hardly strong empirical data. This is summary data similar to the August report by the SEC's OEA without the supporting facts to make any validations one way or another.

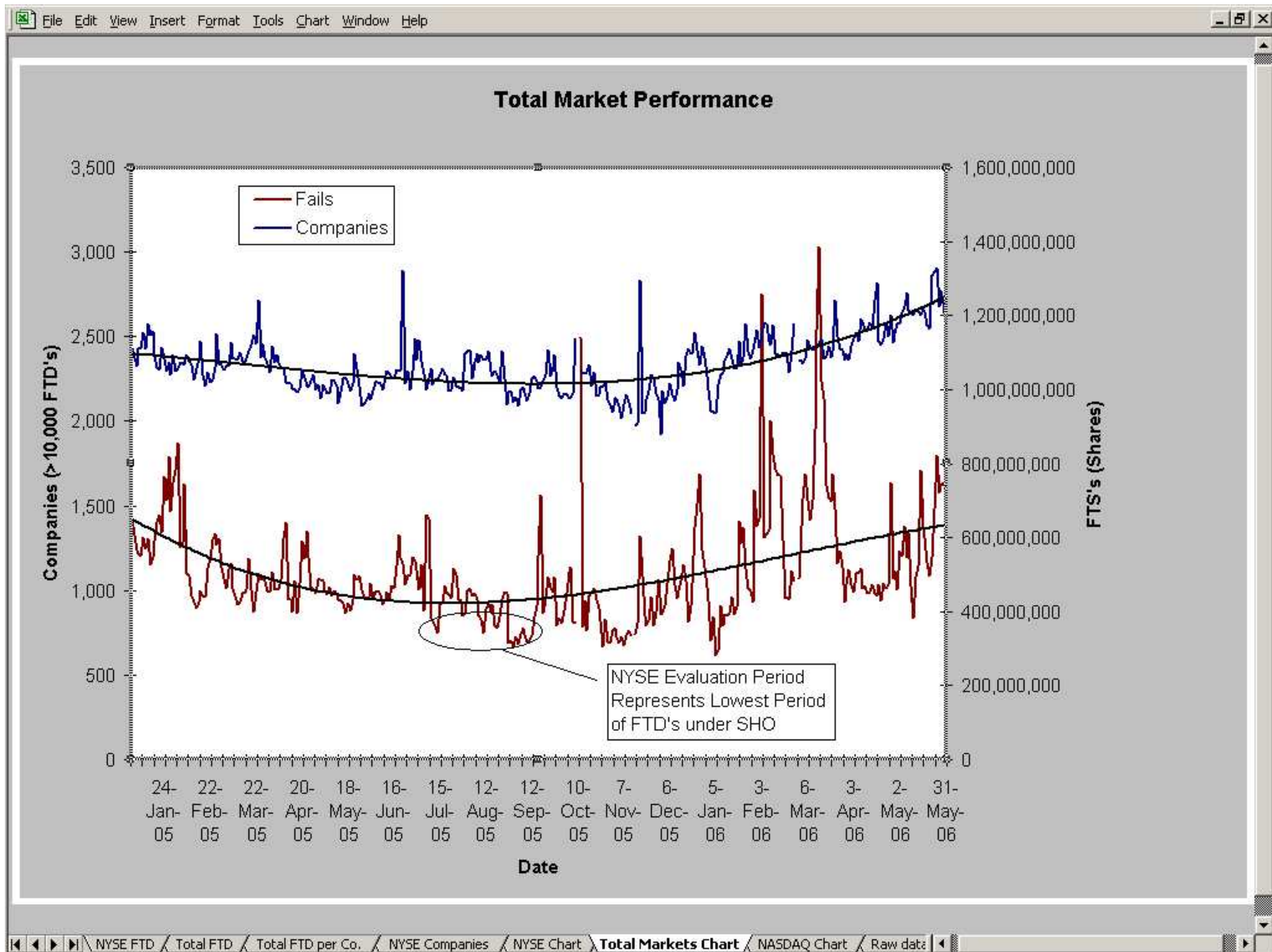
1. The aged options fails relying on the options exemption; did those fails have a negative impact on the underlying value of the equity and were the option positions used as leverage to impact that underlying equity?

2. Was the basis of these large levels of options fails attributed to a large variety of investors or were the fails attributed to a limited small "focus group" of investors?

Please note that the data being presented is based on a period in time nearly 2 years ago and by the Commissions admission, information the Commission has had access to since well before June 2006. This is thus not new data. The NYSE data is also data that is associated with a mere 3-month window of time on a program that has been in existence for over 2 years.

1. How does this correlate to present day as future data supplied by the SEC under FOIA request has identified that the July – September timeframe was an improving period under SHO before the fails again escalated to levels exceeding the original levels seen in January 2005.

Below is a Chart based on data provided by the SEC under FOPIA request. As the chart will illustrate, the period of evaluation by the NYSE represents the best performance period under SHO during the period in which the FOIA Covered (January 2005 – May 2006)



Data Point #2.

Prior to the Commission's Proposal, the Commission's Office of Compliance and Inspections ("OCIE") conducted some examinations for Regulation SHO compliance and found that some broker-dealers were still carrying a significant amount of fails to deliver in securities that they were not closing out because they were relying on the grandfather provision. One broker-dealer indicated that it had not closed out several persistent fails in threshold securities because it was relying on the options market maker exception.

Again I must inform the Commission that this is not strong enough empirical data to dictate a delay in implementing change.

1. The inspection found a "significant amount of fails to deliver" utilizing the grandfather clause as cause for not closing out the fails. Could the commission elaborate on the initial cause of the failure and whether such cause was of legal or illegal standing? By law all trade executions must take place under a contract obligation that requires the intent of 3-day settlement. Did the members ignore this law once the grandfather clause permitted them to do so?

2. Did the Commission investigate a pattern of offenders associated with such trades to determine possible patterns of abuse?

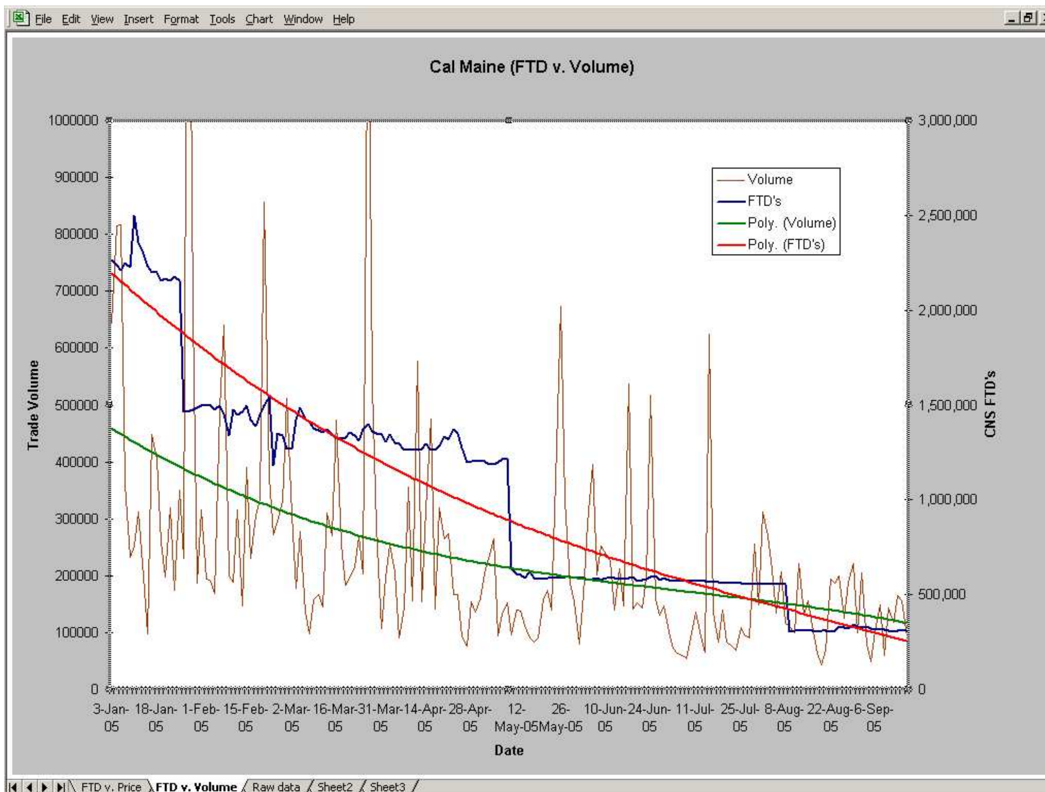
3. Were the fails exempted under the grandfather clause fails that were relative to market making exemptions and if so, what was the market making history of that firm relative to the particular issuer?

   Recently, during a Security Traders Association seminar NASD Executive Vice President Tom Gira identified the awareness that market makers were setting up shop specifically to take advantage of the market making exemption providing sell only liquidity to the markets. *"It's very easy to hang on the box and never really provide liquidity, yet benefit by being an exempt market maker,"* Gira said. A true market maker is *not "somebody who goes in the box and all they do is sell."* Was any of this the case before us here?

All of these delays are taking place at a time where public awareness is at its highest point. Bloomberg TV presented an expose on this subject matter where specific companies were highlighted as being abused, or potentially abused. The Chairman of the SEC spoke before a US Chamber Summit and again made claim that SHO was not working as intended and that investors and issuers remained victims of the abuse. And finally, CNBC personality Jim Cramer spoke out about how hedge funds would manufacture liquidity (illegally) to move market in order to close out of necessary positions.

Such claims are of concern to me personally based on the actual data I had put forth to the Commission under previous comment memos of which the SEC did not afford me the similar courtesy of a response.

In one memo I suggested that the high level of fails in Cal Maine (NASDAQ: CALM) were being closed out by a manipulative tactic of sell side volume to drive investors out. Fraudulent liquidity was put into the market to drive out fails and as the fails reduced so did the level of liquidity required to close out the fails.



As fails became reduced, daily volume also reduced and so did the market value. In January 2005 the stock trading near $11.00/share but falling to below $6.00/share by the time the fails and the volume came out of play.

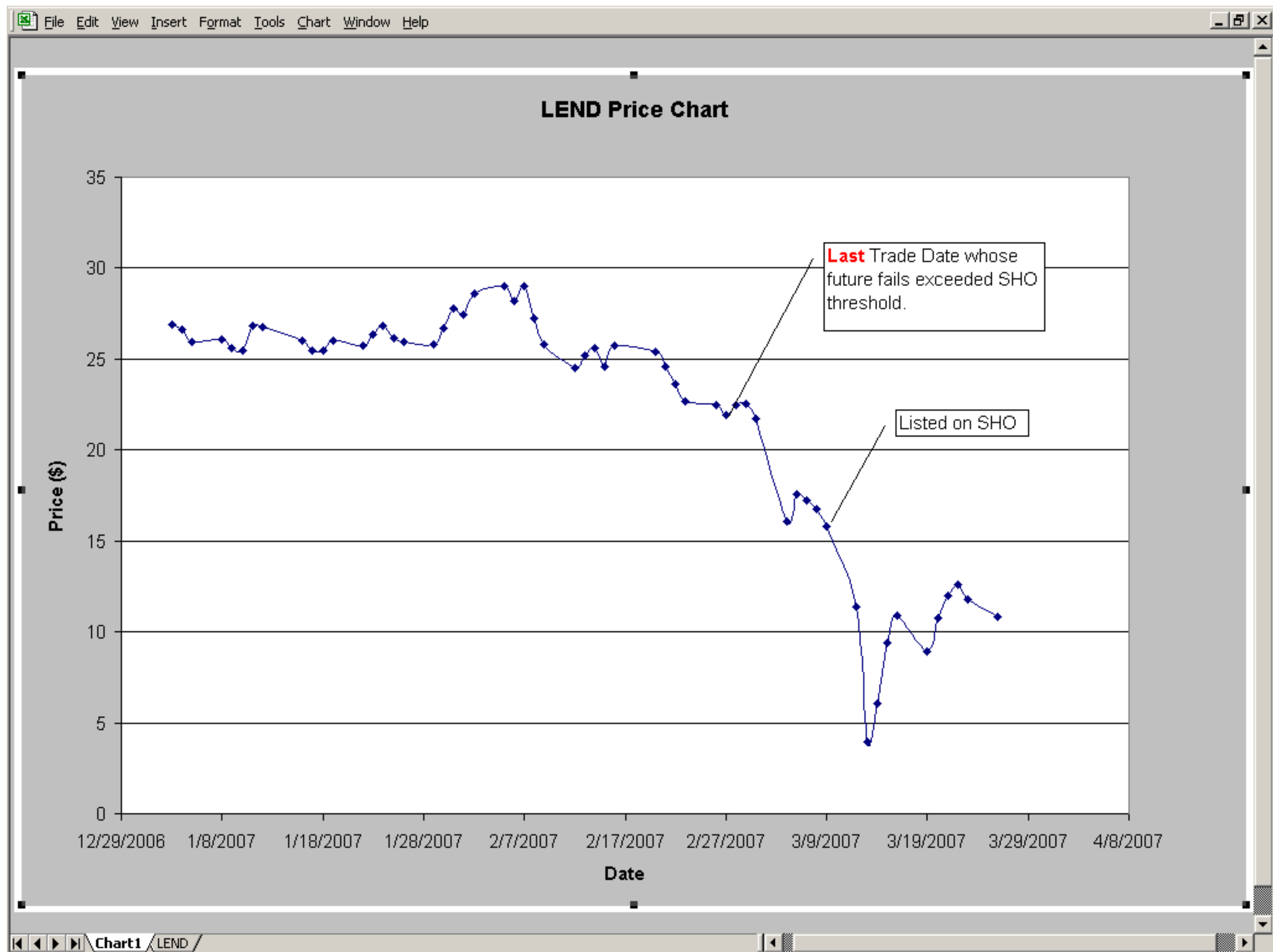
How much of that trade volume was market driven by those holding the fails?

More concerning is that this pattern is not new and SHO did not alter this market anomaly.

Recently the sub-prime industry came down with a crash. Prior to this collapse only one sub-prime lender had been bestowed the honor of being a threshold security, Novastar Financial (NYSE: NFI). Novastar was a well known short of David Rocker.

But while Novastar was the only sub-prime threshold security, this collapse brought more to the table as each collapsing stock was quickly followed with a position on the list. In fact, Accredited Home Lenders (NASDAQ: LEND) first became a threshold security on March 9, 2007 while New Century (NYSE: NEW) was listed only one trade day later, March 12, 2007.

Both LEND and NEW have near identical charts as seen by the LEND chart below.

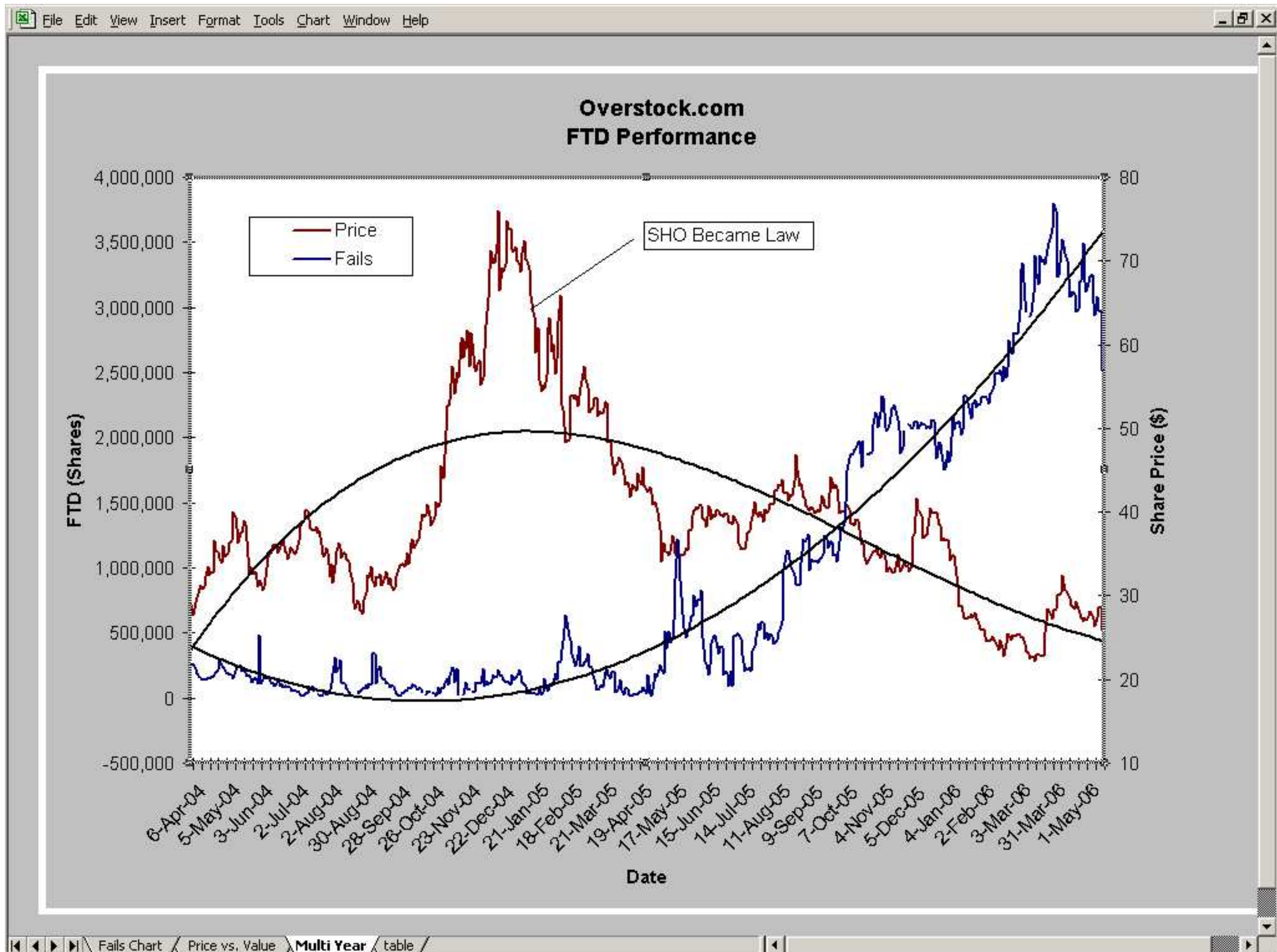


The question some is whether the bounce at the bottom, seen in both LEND and NEW, is not in fact the response to the fails being covered at the bottom of the market after securing a profit on the failed trades.

For the record, the Airline Industry saw an additional spike in companies reaching threshold levels in fails as the industry succumbed to tough times in the markets. Delta, UAL, Northwest, and US Air

along with a range of smaller airlines were all listed on SHO at one time and at a time when each was involved in a collapsing market.

Other similar charts that provide into SHO include:



Overstock.com spending nearly the entire SHO period on the threshold security list and despite patterns of buy side interest the level of fails, presumably executed through the options market, would overcome any type of buy side exuberance and drive the market down.

As Jim Cramer pointed out recently in his “bag of tricks” to manipulate markets:

“The great thing about the market is it has nothing to do with the actual stocks. Now, maybe two weeks from now, the buyers will come to their senses and realize that everything that they heard was a lie, but then again, Fannie Mae lied about their earnings for $6 billion, so there's just fiction and fiction and fiction.

I think it's important for people to recognize that the way that the market really works is to have that nexus of: Hit the brokerage houses with a series of orders that can push it down, then leak it to the

press, and then get it on CNBC—that's also very important. And then you have a kind of a vicious cycle down. It's a pretty good game. It can pay for a percentage or two."

And when the pushdowns result in settlement failures it simply requires a succession of fails be delivered to insure each level of capital at risk.

And then we have Refco Securities whose collapse over a matter of days drove the $30.00 stock to less than $1.00 and on the day of the news the fails come out in big numbers.

File Edit View Insert Format Tools Data Window Help

Refco Securities at Time of Collapse

	A	B	C	D	E	F	G	H	I	K
28	21-Sep-05									
29	22-Sep-05									
30	23-Sep-05									
31	26-Sep-05									
32	27-Sep-05									
33	28-Sep-05									
34	29-Sep-05									
35	30-Sep-05	**Open**	**High**	**Low**	**Close**	**Volume**	**Adj. Close**	**Fails Reported**		
36	3-Oct-05									
37	4-Oct-05									
38	5-Oct-05							41276		
39	6-Oct-05							44876		
40	7-Oct-05	28.46	28.65	28.2	**28.56**	169300	28.56	45676		
41	**10-Oct-05**	**20.1**	**20.25**	**15.6**	**15.6**	**2.4E+07**	**15.6**	<10,000	**Trade**	**Refco debacle Announced Sunday October 9, 2005**
42	11-Oct-05	15.6	15.61	12.79	**13.85**	1.7E+07	13.85	<10,000	T+1	
43	12-Oct-05	11.8	11.9	9.9	**10.85**	3.5E+07	10.85	<10,000	T+2	
44	13-Oct-05	7.84	7.9	7.84	**7.9**	2768300	7.9	**313944**	**T+3**	**Refco Shares Halted On NYSE**
45	14-Oct-05	7.9	7.9	7.9	**7.9**	0	7.9	257414		
46	17-Oct-05	7.9	7.9	7.9	**7.9**	0	7.9	303645		
47	18-Oct-05							15392	**Trade**	**Refco Resumes trading - Pink Sheets** **shares of**
48	19-Oct-05				**0.75**			<10,000	T+1	**Refco shares plunged when they resumed trading yeste**
49	20-Oct-05							504912	T+2	
50	21-Oct-05							**638448**	**T+3**	
51	24-Oct-05							481983	**Trade**	**4 More Bidders Interested in Refco Assets**
52	25-Oct-05							946177	T+1	
53	26-Oct-05							765149	T+2	
54	27-Oct-05							**1209276**	**T+3**	
55	28-Oct-05							1228405		Ex-Clearing Shuffle? Pretty
56	31-Oct-05							1223331		significant drop in one day.
57	1-Nov-05							1219342		
58	2-Nov-05							10822		
59	3-Nov-05							23290		
60	4-Nov-05									
61	7-Nov-05							28907		
62	8-Nov-05							44939		
63	9-Nov-05							37192		
64	10-Nov-05							39993		
65	14-Nov-05									
66	15-Nov-05							10300		
67	16-Nov-05							128847		
68	17-Nov-05							120303		
69	18-Nov-05							166086		
70	21-Nov-05							138846		
71	22-Nov-05							200566		
72	23-Nov-05							45853		

Sheet1 / Sheet2 / Sheet3

From less than 10,000 FTD's to greater than 300,000 in a single day while the stock collapsed from a previous day close of $28.00 to $15.00.

I would ask this Commission to seriously consider their alliances as this latest reform is finally to be taken for consideration of change. Going back are re-reading the statements made by the Commission staff under the original proposal such comments as this below puts significant doubt as to whether the Commission is serious about protecting investors.

"Although we believe that no failure to deliver should last indefinitely, we note that requiring delivery without allowing flexibility for some failures may impede liquidity for some securities. For instance, if faced with a high probability of a mandatory close out or some other penalty for failing to deliver, market makers may find it more costly to accommodate customer buy orders, and may be less willing to provide liquidity for such securities. This may lead to wider bid-ask spreads or less depth. Allowing flexibility for some failures to deliver also may deter the likelihood of manipulative short squeezes because manipulators would be less able to require counterparties to purchase at above-market value."

Such a position presents a conflict of interest over the rights of an investor to receive what they fully purchase over the rights of a market maker to fulfill an obligation to an investor where no shares exist to fulfill. Later providing accommodations to the market maker to insure that such activity does not come at a loss to their proprietary book.

1. Is the Commission stating that the right of an investor to obtain profitability is less than the right of a member firm? Doesn't such an execution create dilution and such dilution could be harmful to the investor.

2. Would the Commission agree that every investor should have the right to know that they are being sold a share that does not presently exist with a seller of securities and thus they are increasing the level of shares in circulation?

3. By the conditions presented here by the Commission, would it not be a simple line of theory to believe that if the market maker would not be closing out such a transaction due to the potential of purchasing shares at above market value from when the originating trade transpired that it would also be in the best interests of that market maker to create a market value that protects their liabilities?

   The Commission staff appears concerned about "manipulative short squeezes" that come from the purchase of fails "above market value" and yet when market making activities take place market values can be made at the buy side or sell side levels in a gap market. Such conditions, and market making exemptions can easily create a conflict of interest by the market maker as to whether they sell into the buyer or buy into the seller in creating such a market.

4. The Commission, in documents to myself, as stated here, and as stated in other public forums, has expressed this obsession with "manipulative short squeezes." Can the Commission elaborate on how it differentiates between a "manipulative short squeeze" and a set of market conditions that result in those holding the short position simply being on the wrong side of a trade?

   As was shown with just a few of the dozens of examples I have regarding stock raids where rapid stock declines are coincident to rapid increases in settlement failures. The Commission has excused each of these raids as simple market events where long shareholders were simply on the wrong side of a market. The SEC has not taken any steps to address the lack of market making during these critical events nor has the Commission sought evidence as to whether these raids were legal raids or stock manipulation. Yet, the Commission has become so concerned with a "manipulative short squeeze" that the Commission has allowed shorting abuses to exist to drive away even legal short squeezes caused by market events.

Evidence of such fears by regulators about a market appreciation is what was in the news today:

Mac-Gray won't comment on unusual market activity

By Gabriel Madway
Last Update: 12:52 PM ET Mar 26, 2007

SAN FRANCISCO (MarketWatch) -- Mac-Gray Corp. (TUC) said Monday the New York Stock Exchange contacted the company and requested that it issue a public statement on whether there are any corporate developments that might explain the unusual activity in its stock. Mac-Gray shares were up nearly 14% at $15.85 in early afternoon trade. Waltham, Mass.-based Mac-Gray, which provides laundry facilities management, said it is company policy not to comment on unusual market activity.

There have been similar type PR's that have come out recently where the SEC has contacted companies regarding a sudden rise in stock price as if the company must be responsible for such activity. Never seen are PR's where the SEC or SRO contacts a company when a stock suddenly collapses 10, 20, 30% on no news.

Conclusion:

There is not direct response to this issue because the investing public, on both sides of this argument, are forced to live with the total lack of transparency by the SEC and SRO's relative to market trading activities. The public's concern however is the clear transparency of the Commission staff working this issue and their objectivity at looking carefully at how these markets really trade.

James Brigagliano, the supervisor responsible for this reform and this latest delay, informed a group of Hedge Fund Managers at a recent Managed Fund Association seminar that "The Securities and Exchange Commission is stepping gingerly into the issue of short-selling abuse and is following a "carefully honed approach" so that it does not impose too many restrictions on prime users of short-selling, namely hedge funds."

By all accounts Mr. Brigagliano's role is not to insure that the fast moving hedge funds, for which Jim Cramer claims are manipulating our markets, are provided all the luxuries of liquidity freedoms they need in order make a profit. No, Mr. Brigagliano's role is to insure that the public issuers and public investors are fully protected from ALL market abuses that will impact investor confidence and eventually the formation of these capital markets.

I ask that if the Commission plans on continuing with this ruse that the Commission addresses the specific questions raised in this memo. How detailed an analysis did the Commission conduct and what were those results?

In closing, my parting shot will come from former Hedge Fund Manager Jim Cramer who claims stock manipulation is easy "because the SEC doesn't get it," To date Cramer has proven to be 100% accurate with his statements.

David Patch
www.investigatethesec.com