April 2, 2008

Securities and Exchange Commission
100 F Street NE
Washington DC

Subject: Rule 10b-21 (File S7-08-08)

Mr. Chairman,

I would say that it is a pleasure to draft comment to the Commissions proposed 10b-21 anti-fraud provisions but it is not. Instead, it is becoming more and more frustrating how the investing public is subjected to such regulatory irresponsibility. Never before in the history of rulemaking has so many partial steps been taken to address market fraud without ever coming to a decisive end. This proposal simply represents the latest volley in public deception by the SEC.

"I was just wondering if there's any precedent for the Commission proposing rules prohibiting behavior that is already illegal?"[1]

The reason such a question is even being asked, by a member of the Commission staff no less, is due to the lack of responsibility taken by the SEC's Division of Enforcement. Had the Division of Enforcement acted upon the rules provided by the Division of Market Trading in previous rule making the Commission staff would not be sitting before the public wasting more time creating layer upon layer of rules regarding the same illegal trading activities.

The first round of duplicative rules came during the release of Regulation SHO in 2004. Regulation SHO was drafted into law simply because Wall Street Regulators and member firms were not abiding by the rules presently in place.

"To give you that brief introduction in Reg SHO, the history (of) how we got to where we are today. For the past few years we have been hearing from many different regulators regarding their concerns about the increase in the level of fails that they are seeing. They believe, and they have stated on numerous occasions, that one of the primary causes of the high level of fails was that various participants in the short sale process, prime brokers, executing brokers, clients, were not following already established rules."[2]

But when SHO was released it was done so not as a definitive measure to stop fraud but to cultivate a bailout of those that committed prior acts of fraud to excessive levels. Commissioner Annette Nazareth stated in an e-Mail while referring to the grandfather clause;

"We believed in good faith that the provision was a cautious first step with respect to serious short sale reform."[3]

We later came to learn that the grandfather clause, as part of the 2004 version of regulation SHO, was not a cautious first step but an appeasement to Wall Street. The clause was not part of the language up for public comment, as one would expect. Instead, the grandfather clause was the off record brainchild of industry lobbyist Securities Industry Financial and Markets Association (SIFMA). The

[1] Comments by Commissioner Casey March 4, 2008 during the proposal of Rule 10b-21
[2] Statement by Bear Stearns General Counsel during a December 13, 2004 Conference Call on Regulation SHO Audio available at: http://investigatethesec.com/drupal-5.5/node/153
[3] e-Mail dated 1/2/2007 from Commissioner Annette Nazareth to a concerned investor.

proposal was presented to the SEC during a private meeting held between the lobbyist for Wall Street and the SEC's Division of Market Regulation.

Convinced that Wall Street would abide by the rules in the future despite years of past abuse, the SEC agreed to the compromise being presented by SIFMA. The grandfather clause would allow the members to reduce their financial liabilities associated with failed trades slowly and over an extended period in time. To the investing public's prediction it didn't work. Investors stated as early as June 2004, before Reg. SHO was enacted, that the clause would be a failure. As predicted, the grandfather clause simply became yet another industry loophole used to manipulate markets.

"Reg SHO, has proven insufficient to stop the problem. One of the reasons is the Grandfather provision in the rule as it was originally adopted…And I know that people victimized by it have a great deal of right on their side to complain about it."[4]

How out of control did it get?

Consider the numbers as reported in public filings by the Depository Trust Clearing Corporation for the years 2005 thru 2007.

	2005	2006	2007	Diff	% change
FTD	$3,423,028,000	$3,749,160,000	$7,454,648,000	$4,031,620,000	117.78%
FTR	$2,445,326,000	$2,643,433,000	$5,761,192,000	$3,315,866,000	135.60%
SBP	$977,702,000	$1,105,727,000	$1,693,456,000	$715,754,000	73.21%
Open	$6,846,056,000	$7,498,320,000	$14,909,296,000	$8,063,240,000	117.78%

Note: FTD – Fail to Deliver; FTR – Fail to Receive; SBP – Covered Trades through Stock Borrow Program; % Change is the % Dollar Value Change between 2005 and 2007

So despite the Commissions public assertions that SHO was in fact working,[5] SHO was never actually working. It was getting worse. The level of aggregate fails to deliver, in dollar value, continued to increase despite the financial markets entering into a bear market period. The $3 Billion mark to market problem of 2004/5 was approaching a $7 Billion problem by 4th Quarter 2007.[6]

"Manipulating the price for security is a serious fraud, and the SEC can investigate and punish it. Reg SHO needs teeth, and this recommendation is aimed at providing them…Reg SHO has accomplished a good deal, but our experience has shown that Reg SHO can't be effective without enforcement."[7]

Mr. Chairman, no rule will be effective if the Division of Enforcement does not take such rules seriously which is the responsibility of the Commission staff to insure happens. So far, Reg. SHO has never been taken seriously by Linda Thomsen and the Division of Enforcement. And with a doubling of the dollar value in aggregate fails I beg to differ on what if anything Reg. SHO has accomplished.

Prior to SHO pre-existing securities laws contained anti-fraud provision and anti-manipulation provisions. As Commissioner Casey implies, this does not alter those laws in any way, it simply parallels what pre-exists. The SEC likewise has rules 15c6-1 and 15c3-3 that can be enforced when contracts for trade were entered into illegally but history has shown no SEC enforcement has ever taken place.

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[4] Chairman Chris Cox before the US Chamber Summit on Capital Markets February 2007
[5] Fails to Deliver Pre- and Post-Regulation SHO, a Study by the OEA http://www.sec.gov/spotlight/failstodeliver082106.pdf
[6] Vodia Group Report February 26, 2008; Short First, Ask Questions Later; An Analysis of SEC Fails to Deliver Data http://investigatethesec.com/drupal-5.5/files/Vodia%20Group.pdf
[7] Chairman Cox March 4, 2008 Opening remarks to proposed Rule 10b-21

Rules without enforcement might just as well not exist and when it comes to the rules of trade contract and trade settlement the member internal compliance systems, market self-regulatory agencies, and the Commission failed to enforce such pre-existing rules. The SEC and SRO audit teams rarely drill down into such trade contracts to understand how each was executed and how each was handled when such a contract violation appears. Such failures in auditing exacerbated the fraud.

Rule 10b-21 will not solve this problem alone and as drafted will not solve it at all. In part it won't solve this problem because 10b-21 does nothing to address the general enforcement philosophy of present director of enforcement Linda Thomsen nor that of any of her predecessors.

"When we hear complaints about short selling-and, frankly, it is both short and naked short, it is a combination of both-we routinely hear from companies who've come in, who worry that they're being shorted in an illegal way. We routinely take all that information in and look into it. And often times, as I think many defense counsel would be happy to tell you, when we dig in, what we find is that some of the information that has caused people to be shorting is actually true as to the company, and we may very well be confronted with two issues, one on the company and its disclosure side as well as on the trading side."[8]

In this declaration Director Thomsen has now publicly admitted that one of the first activities of the Division of Enforcement is to investigate the complaintent, to decide whether short sellers are justified in shorting the equity. This is irresponsible and harassing.

If trading irregularities are taking place in the issuer market it would take place independent of how a business operates. Trading irregularities in the open market never involve company accounting practices, how press releases are made, or what a CEO may declare. Trading irregularities involve the investing public and member firms. The fact that the SEC seeks to investigate the issuer when an issuer comes to them with trading concerns is irresponsible. Issuers who take their companies public will issue shares into the open market and thereafter relinquish all rights to the public trading of those shares. The SEC, in 2004 proposed and released a rule that restricted the authority an issuer has over their shares and how such shares are trade.[9]

History has instead shown that the announcement of the investigation by the SEC into the complaintent simply aides in the manipulation of the stock price and that rarely does such investigation yield anything of significance. Such is a well-known and understood practice of the short seller. Typically, only a portion of what was being touted by the short seller was in fact accurate. Much of what is identified by a Commission audit are minor issues typical of any audit. Yet the negativity placed upon the issue continues and is used to manipulate the markets perceptions. An example of the relationship between a short seller, Regulation SHO fails, and the SEC is provided in the backup data provided in the Appendix to this memo.

Trading violations by members and member short sale clients are thus excused based on a small fraction of accurate perceptions by the short seller. The fact that the SEC even investigates the issuer upon complaint disrupts the open door policies needed by the agency. Shooting each messenger who walks through the door will quickly insure than none come knocking again and fraud is never exposed.

So now on to the specifics of what is wrong with Rule 10b-21 and responses to the questions posed by the Division of Market trading.

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[8] SEC Director of Enforcement Linda Thomsen testimony before US Chamber Summit on Capital Markets 3/26/08

[9] Issuer Restrictions or Prohibitions on Ownership by Securities Intermediaries Release No. 34-49804; File No. S7-24-04

Market Collusion

A proposed in 10b-21, the SEC is of the opinion that clients are deceiving members regarding their ability to deliver shares. Whether the client provided a false locate, identified a long position when no such long shares existed, etc… the presumption is that the client is a guilty party and that the Broker-Dealer (BD) is innocent to such acts of fraud.

Wrong!

Broker-Dealers are many times fully aware of the potential failures by their preferred clients. These firms take such risk because of the revenues generated by such clientele. Consider that, to date, violations in the short sale process have been treated as simple compliance violations netting trivial fines of $10K, $20,K or even $30K. When calculating risk, the BD will calculate the potential lost revenues vs. the potential sanctions if caught and will trade make that illegal trade 99 out of 100 times.

Broker-Dealers additionally collude with other member firms once such a trade is executed and that fail is in the marketplace. Proof lies with the response to the failed trade itself.

In a failed trade the liability of the fail rests with the Broker-Dealer and not the client. In fact the buy side and sell side broker dealer must put up capital to cover the potential of the failed trade. In an illegal trade the BD can act in several different ways.

1. If the error was based on the client's misrepresentations the BD can buy in the trade on behalf of the client to settle the trade. The client would then be billed for any costs associated with such a transaction. The client misrepresented the parameters of the trade. In taking this approach the BD is without liability and the client pays for their misrepresentations.
2. The BD can buy in the trade from the house account and lend out the share for settlement. This allows the client to maintain their short, and pay the lending fee to the BD leaving the BD long the stock. This likewise would eliminate any liability on the books of the firm and would insure safe and prompt delivery to the buy side BD representing the long shareholder.
3. The BD can take no steps leaving the illegal trade to remain on the books of the firm.

Option 3 is typically what takes place. Both the buy side and sell side BD agree to hold this open as a fail, and set aside net capital to cover the fail, because it is financially beneficial to do so. Both owe each other shares and both have shares owed to them and thus participating parties excuse the cost liability of a buy-in.

The fact that the receiving firm has failed to act in the best interest of their client is evidence of the collusion between firms since, as a stand-alone transaction, the failed trade is neither in their best interest or that of their client.

"Proposed Rule 10b-21 is narrowly tailored to apply when a seller, including a broker-dealer trading for its own account, deceives specified persons about its ability or intention to deliver securities in time for settlement, or about its locate source or ownership of shares and that fails to deliver securities by settlement date."

By "narrowly" tailoring this rule the Commission sets themselves up for future loopholes used to circumvent the fraud as specifically defined in 10b-21. Instead fraud should apply to all trade executions as they apply specifically to the intent of settlement defined in 15c6-1.

Solution:

Rule 10b-21 must make it mandatory that in the event of a failed trade, where a client misrepresented the locate or the ownership of such shares, that the broker dealer representing that client immediately, and without interruption, engage in a guaranteed delivery buy in. No compliance or exclusion from this violation will be provided for efforts that fail because there were no guaranteed shares available at the market pricing offered. If the shares being offered in the market cannot be delivered on time there is a problem with the market and how it is being represented.

Failure to take such immediate steps would result in aiding and abetting charges filed against the BD representing such client.

Zero tolerance to these activities may be accepted.

One way to insure such compliance is to create a mandatory pre-borrow into the short sale process instead of simply a mandatory locate. Simply requiring a locate allows for an unlimited number of short sellers to stake claim on the same located share providing repeated opportunity for a failure to occur.

Market Making

Rule 10b-21 and other similar regulatory rules fail to accurately define fraud as it pertains to bona fide market making. How and where naked short liquidity is injected into the marketplace.

"Last summer at a Securities Traders Association Conference, NASD Vice President Tom Gira expressed concern stub quotes were a sign 'that people are registering as market makers just to get the exemption' from rules prohibiting shorting stocks on a down tick, according to the Web site of Traders' Magazine"[10]

and

"Our concern is that people are registering as market makers just to get the [short sale] exemption," said Tom Gira at the Security Traders Association's annual conference. "But the exemption is limited to bona fide market making."[11]

Finally,

The rule, eliminated in 1997, banned dealers from entering quotes whose spreads the NASD deemed too wide.'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.'[12]

As Mr. Gira clearly recognized in 2006, bona fide market making was not all market makers were engaged in and yet, despite this admittance to areas of fraud and abuse no significant enforcement actions relating to manipulation and fraud has been undertaken. Instead failures to deliver increased.

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[10] TheStreet.com Aaron Trask Is Electronic Trading Adding to the Carnage – 8/3/07
[11] Financial Times 2006
[12] Peter Chapman Market Makers Under Short Sale Scrutiny 2006 Trader Magazine
http://www.tradersmagazine.com/magazine2.cfm?id=1&aid=2657&year=2006

In each trade executed by a market maker, where the exemption was used in a manner not consistent with bona-fide market making, that trade is illegal and most likely manipulative. Rule 10b-21 does not specifically address such activity nor provide a mechanism to take such as a manipulative task.

Solution:

Rule 10b-21 must better define the rules in which market makers can engage in such market making activity. The rule must clearly address what is considered market making and what will be considered fraud. Can a market maker objectively naked short into a market with a mandatory buy in to their account occurring at the same time? Certainly not as the naked short will simply take out demand and force a lower offering.

Present rules are ambiguous which is why Mr. Gira admits that such ambiguity is being used to commit fraud. Market makers have been known to loan out their exemptions and used such to raid pubic issues and drive out investors later covering prior failed trades from the selloff. Present auditing by regulators does not easily identify such activity, which is why it continues unabated. The vary fact that such activity takes place over a short period in time can allow the client or firm to execute such a raid within a window that would not be picked up by the Regulation SHO threshold status system. Investors can be easily manipulated out of their positions in the timeframe allowed for a company to be listed on the threshold security publication.

Ultimately, with the growth of the hedge fund industry and the liquidity such provides, market making liquidity at any level must be seriously re-evaluated. Is the market really illiquid and for those that are, is marking making really necessary or does the activity simply bring in additional victims? The market has changed this past decade and the need for the number of market makers and the level of market making activity taking place should now be better evaluated.

Response to SEC Questions;

1. Should we narrow the scope of the proposed rule to apply only to sales of “threshold securities” as that term is defined in Rule 203(c)(6) of Regulation SHO or to certain types of securities?

No, fraud and manipulation can take place before a company achieves threshold status and manipulation can specifically occur in a manner intended to deceive regulators regarding threshold status. From trading ex-clearing, to inducing fails, to raiding markets to prevent threshold status, member firms and clients can engage in fraud before the pre-defined SEC abuse levels. Quick hits have replaced long drawn out abuses.

Furthermore, Federal Regulations and subsequent rule making promulgated from Federal Regulations do not provide the Commission with the authority to arbitrarily excuse a certain threshold of fraud. Section 17A of the Exchange Act of 1934, along with Rules 15c3-3, 15c6-1, and Section 8 of the UCC demand that trades settle promptly and require that those entering into such trades do so with the intent of prompt settlement. Failures ignored by the Commission that accumulate to threshold levels simply allow the first abusers a free pass on fraud. The Commission is asking whether a client who deceives a BD in a non-threshold security should be considered in violation of fraud.

2. The proposed rule highlights the specific liability of persons that deceive broker-dealers, participants of a registered clearing agency, or purchasers about their intention or ability to deliver securities in time for settlement. Are there other entities that could be deceived about a seller’s intention or ability to deliver securities in time for settlement that should be included in the proposed rule?

The Rule fails to address the deception both the seller and the participating Broker-Dealers play on the investor who purchases such a share. When a trade fails settlement there becomes an implied counter party liability by the participating broker dealers. Such liability is not in the best interests of the investor and that investor is unaware that such liability has been taken. From a confirmed account statement highlighting the settlement of a trade to the debit of monies from the buyers account, the buyer is deceived into believing they have custody of a share when in fact they do not.

Upon the occurrence of a settlement failure, the buyer's monies should be placed into escrow accruing interest until such time as a share is delivered or a trade is executed to sell the security.

At the present time the commission received by the trade as well as the use of the capital as leverage until such time as the trade is settled offsets the counter party liability. Such benefit should not be to the BD but to the shareholder who purchased shares under the guidelines of 15c3-3. The BD has deceived the shareholder through a course of false indicators (Account balance, account statement)

3. What are the costs and benefits, including to broker-dealers or customers, for including delivery as an element of the violation? Would the inclusion of a fail to deliver as an element of the proposed rule encourage broker-dealers, as a service to customers, to deliver securities on behalf of customers to prevent customers from failing to deliver securities by settlement date?

Broker-Dealers are responsible for the acts of their clients when they trade on behalf of their clients. The BD's ultimately carry the liability of their client's failures and such can be construed as aiding and abetting when the BD fails to follow established securities laws because of failures of the client. Any costs incurred are done so with the open eyes of the firms involved.

4. Should we instead no longer permit a broker-dealer to rely on such customer assurances in satisfying the locate requirement of Regulation SHO?

The NASD proposed in 2001 that member firms must be responsible for affirmative determination for all non-member firms. The proposal was based on the naked shorting entering US markets by non-member firms. NASD Rule 3370 was modified in November 2003 to address this. The SEC killed Rule 3370 with SHO and in the process allowed US and International Clients the right to conduct their locates without responsibility of the selling member firm.

In the case of 10b-21 and the locate requirements of Regulation SHO, similar interpretation to Rule 3370 should apply. Clients who are not registered with the Commission or SRO's can not use their own locates in the act of a short sale. The member firm responsible for the execution of such trading must be likewise responsible for confirming the affirmative determination.

There is no reason legal reason to allow clients of member firms a freedom different than that of a non-member firm. Certainly the client's right to fail a trade and potentially manipulate a market should not override the right of an investor to receive a share they purchased in good faith expecting it to be delivered.

5. To what extent, if any, might the proposed rule result in short squeezes? What costs, if any, would the potential for short squeezes have on the efficiency of the market?

I must remind the Commission that the Commission holds no legal grounds in defining how a market trades as long as such trades are done legally. Preventing any kind of a short covering by forcing trades to settle under the legal rules as defined by Federal and Market Regulations is not for the Commission to determine one way or another. Taking steps to prevent the free trade of a market is instead the very definition of market manipulation.

Failing to settle trades because to settle trades would cause a price appreciation is accepting that unsettled trades have essentially manipulated the price of a security. Under that premise, the Commission has authority under pre-existing law to take appropriate enforcement action.

"Regulation SHO does not require the close-out of fails to deliver that existed before a stock became a threshold security (known as "grandfathered" securities) because the Commission was concerned about creating volatility through short squeezes if existing positions had to be closed out quickly."[13]

I request that before the Commission seek out to protect those that committed these crimes in the first place (extensive levels and duration of failed trades) that the Commission provide the public with a through study on how the existing failed trades have not already negatively impacted these same public markets the SEC shows concern about having appreciate.

Who defines the natural pricing of an issue? Is it the Commission? Is it the short seller who has been provided means to sell off any upside demand or sell down a thinly demanded market? Is it the market maker who can legally sell short and then manage the future market to insure the house fails [liabilities] are covered at a profit?

In the market today we see massive swings of volatility much being attributed to the Commissions removal of the tick test. Somehow the Commission does not have any issue with highly leveraged short sales taking out the demand in a market and raiding such a market down.

Consider for example that in the market volatility seen since Bear Stearns collapsed, and factoring in the 8 trade days between a trade and the SHO listing, 89 new Companies were added to the Regulation SHO list in a single day (April 2, 2008). Eighty-nine new companies had reached settlement failures above an abusive level and all did so based on trading for a single trade day - March 20, 2008.

Does the Commission know what impact such trading had on these markets? Is the Commission as equally concerned about such impact, as they are the potential of a short squeeze induced by the past regulatory neglect to settlement failures? Would the short squeeze be a non-event should the failures in the system not exist? Finally, who has a greater right in the trade execution the buyer who purchased and fully paid for securities or the seller who sold something they could not deliver and then had no future intention of delivering?

6. To what extent, if any, would the proposed rule induce short sellers to execute trades in overseas markets?

Who cares where illegal short sales move to, they are illegal?

Trading offshore into the US markets would require member firms to insure affirmative determination and insure settlement could be made or they would not accept the trade. Trading offshore into non-US markets would cost the brokerage firms a commission on trades that would otherwise not be legal to make. Having a short seller move their business offshore because they want to be able to deceive a BD about what they have available is only telling the short seller that the US markets will no longer accept the fraud.

There would be no incentive for short sellers executing legal short sales to move offshore.

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[13] e-Mail dated July 27, 2005 from SEC Division of Market Regulation to David Patch Subject: Your correspondence to Congressman Tierney – Copy in Appendix A of this memo

Conclusions:

The Commission must decide and decide quickly where they stand on investor protection. Presently the Commission continues to add layer after layer of rules on top of pre-existing rules hoping that with each new layer the fraud will cease to exist. The Commission is wrong. The fraud exists not because of a lack of rule making [teeth] but because of a lack of commitment by the Commission staff and a lack of Commitment by the Division of Enforcement to consider taking action.

Rule 10b-21 will not resolve this underlying issue. Chairman Cox speaking publicly about how serious a problem this is, without evidence of any real enforcement action, does not put the investing public at ease. The public is becoming smarter and more aware and the political rants of the SEC Chairman carry little weight today. Such commentary only really separates the public from their trust and belief in the regulatory system.

Beyond the ultimate lack of commitment by the Commission, Rule 10b-21 lacks the language to call out the fraud accepted at the self-regulatory levels of market participants and regulators. When money is involved the industry runs a risk v. reward analysis and has figured out that the risk is well worth the reward. Fraud is long confused with compliance violations and therefore the risk of engaging in fraud is minimal. The teeth of rule 10b-21 is in the level of enforcement that can be imposed and such penalties must be significant enough to sway the risk v. reward pendulum.

With the collapse of Bear Stearns last month the Commission was provided yet another snapshot of how such abuses can impact a market. The trading in Bear Stearns leading into that final day resulted in Bear Stearns becoming a short lived SHO threshold company. Did the unsettled trades consume a large portion of natural demand and blow out the bids in the market? How much of that was highly leveraged short sale executed through the options market where the option market making hedge flooded the equity market and propelled the collapse?

The confidence is being lost, will the Commission respond with appropriate rule making or will investor protection take a back seat to the needs of Wall Street once again?

In closing I ask the Commission to cease with the smoke screen created by their public comment process. The Commission will most likely hold private sessions with member firms while the general public will be forced to provide all comment and public debate through paper submission. It is understood that the inception of the grandfather clause was an option presented to the Commission by SIFMA and the public was not afforded the luxury of understanding that such an option was presented privately and thus open for return comment.

If the Commission is to hold such meetings it is imperative that meeting minutes be taken and published for the public to view and comment on. By holding these types of private meetings the industry is being afforded the luxury of holding back on sensitive issues awaiting private non-public communications to address their concerns and options. The fact that the grandfather clause was a bust is proof positive that these private meetings and sensitive proposals are not always in the best interests of the investing public.

David E. Patch
Investor Advocate
www.investigatethesec.com

See Attached Appendix for additional supporting documents.

Appendix A
Background Info

2nd Annual Capital Markets Summit: Strengthening U.S. Capital Markets for All Americans
Date: 26-Mar-2008 8:30 AM EST - 26-Mar-2008 4:30 PM EST -
Location: U.S. Chamber of Commerce, 1615 H Street, NW, Washington, DC 20062

2:15 p.m. – 2:45 p.m.
Hall of Flags
Keynote Address: A New World Order for Capital
Markets: How Consolidation, Regulation, and Technology are Reshaping Exchanges Worldwide
Robert Greifeld, President and Chief Executive Officer, The Nasdaq Stock Market, Inc.
Introduced and moderated by: David T. Hirschmann, President and Chief Executive Officer, Center for Capital Markets Competitiveness

AUDIENCE MEMBER: "You mentioned clearance and settlement. As an SRO, what is NASDAQ doing to properly police its members and protect issuers from excessive settlement failures."

ROBERT GREIFELD: "Well that's obviously a hot topic with our issuers. It's centered around the question of short selling and failing to deliver on a short sale. So we think, one, that the Commission is on the right path to solving the vast majority of the problems. When you have to locate before you sell short, we think that is a positive outcome. What you need, eventually, in the system, is coordination. So if you are going to sell short, you have to then secure that inventory of the stock and make sure it is locked in. So I think we'll get there. I think the interim step the Commission is taking now, that is going to be something sort of a regulatory regime or penalty associated with failing to deliver is the end step. So, I think we're getting there."

AUDIENCE MEMBER: "Would you be in favor of a pre-borrow requirement?"

ROBERT GREIFELD: "What I'm in favor of is a system hopefully developed by private industry—and I in a past life was in this type of business, so I certainly recognize great opportunity—so any time you try to go short you have to have a system that is connected to all of the sources of liquidity of the stock available to borrow, and that stock available to borrow, and that stock available to borrow is then decremented based upon people making a contractual economic commitment to it. So it's a lock-in system much like today, on a front-end trading system, you go to hit the bid in Apple, you own Apple at that point in time. So it would be the same methodology for the end state for people wanting to short."

DAVID HIRSCHMANN: "In the technology area, where do you think we are in the evolutionary process…"

ROBERT GREIFELD: "… going back to the question before, picture the electronic world today where some people are shorting stock without any tie to a physical inventory system. So if you think about it in general terms, the development of a physical inventory system for shares available for borrow is not a technological challenge that would be breaking any new ground. So to think that we don't have that system in place, and the users who want to borrow either short or long can tie to that, so that's certainly something that's there. Uh, 3 day settlement. So we have certainly taken great pride in the fact that our system broad defined in the settlement system is working very well, but in 2008 it's hard to think we still need 3 day settlement. You know, the only thing that comes to mind, 8 years ago we talked about T plus 1, and that hasn't happened, so those would be two things we could talk about."

3:00 p.m. – 3:30 p.m.
Regulatory Keynote Address: A View from the Division of Enforcement: Perspectives and Priorities
Linda C. Thomsen, Director of the Division of Enforcement, U.S. Securities and Exchange Commission
Introduced and moderated by: Michael J. Ryan, Senior Vice President and Executive Director, Center for Capital Markets Competitiveness

AUDIENCE MEMBER: "You spent a lot of time talking about insider trading and penny stock fraud, but you failed to mention an issue that's of great concern to the Chamber, and that is naked short selling and the unsettled trades that can result from that. How can the Commission claim that it is serious about enforcement when millions of trades fail to settle every day and companies remain on Reg SHO Threshold Lists for years and years? And, second part of the question, why is the new rule 10b-21 necessary when, as Commissioner Casey pointed out, it makes illegal activity that is already illegal?"

LINDA THOMSEN: "Um… I didn't hear all of it, unfortunately, but as to the issue of short selling, we recognize that short selling is…

AUDIENCE MEMBER: "My question was not about short selling. We all know that short selling is legal, and a necessary and efficient part of the market process. I'm talking about naked short selling—the selling of shares one does not have in inventory and probably has no intention of locating or borrowing."

LINDA THOMSEN: "As to naked short selling, and more generally market manipulation generally (sic), it is an area we are focused on. We have seen fewer cases in that arena because, often times, this is not necessarily with respect to naked shorts, but shorting or market manipulation more generally, because often the components of something that might look to be manipulative are all legal trades as you point out. So it's a hard case to bring, which is not to say that it isn't something that we don't investigate, because we do. So I .. hear and understand the frustration of many on the subject of short selling generally. When we hear complaints about short selling—and, frankly, it is both short and naked short, it is a combination of both—we routinely hear from companies who've come in, who worry that they're being shorted in an illegal way. We routinely take all that information in and look into it. And often times, as I think many defense counsel would be happy to tell you, when we dig in, what we find is that some of the information that has caused people to be shorting is actually true as to the company, and we may very well be confronted with two issues, one on the company and its disclosure side as well as on the trading side. But they're very difficult cases, which is not to say that we aren't focused on them and interested in them and indeed this new focus that we have on some smaller companies and smaller issuers will wrap some of those concerns into their focus as well.

November 2006 Form 13F Edgar Filing of Copper River

American Capital Strate	PUT		24937954	1,808	45,800	SH	PUT	OTHER	45,800			
American Tower Corp	PUT		29912951	44,530	1,220,000	SH	PUT	OTHER	1,220,000		SHO	
AMR Corp	PUT		1765956	4,628	200,000	SH	PUT	OTHER	200,000		SHO	
Annaly Cap Mgt Inc	COM		35710409	95,063	7,234,629	SH		OTHER	7,234,629			
C-COR Inc	COM		125010108	38,002	4,429,163	SH		OTHER	4,429,163			
Digital Riv Inc	PUT		25388b954	30,672	600,000	SH	PUT	OTHER	600,000			
Fairfax Financial Holdings	SUB	VTG	303901102	39,033	300,000	SH		OTHER	39,454	260,546		
Fairfax Financial Holdin	PUT		303901952	54,672	420,200	SH	PUT	OTHER	420,200		SHO	SEC
Gartner Inc	COM		366651107	85,523	4,862,000	SH		OTHER	4,862,000			
Interwoven Inc	COM	NEW	46114t508	45,590	4,133,238	SH		OTHER	4,133,238			
IShares Russell 2000 Inde	RUS	SELL 2000	464287655	127,256	1,767,445	SH		OTHER	1,767,445			
Krispy Kreme Doughnut	PUT		501014954	9,068	1,119,500	SH	PUT	OTHER	1,119,500		SHO	
Navarre Corp	PUT		639208957	9,809	2,440,000	SH	PUT	OTHER	2,440,000		SHO	SEC
Novastar Finl Inc	PUT		669947950	43,371	1,485,800	SH	PUT	OTHER	1,485,800		SHO	SEC
Omnivision Technolgies	PUT		682128953	66,910	4,688,900	SH	PUT	OTHER	4,688,900		SHO	SEC
Overstock Com Inc Del	PUT		690370951	8,362	477,000	SH	PUT	OTHER	477,000		SHO	SEC
Powerwave Technologies I	COM		739363109	84,307	#########	SH		OTHER	11,092,972			
Powerwave Technologies I	CAL	L	739363909	1,689	222,200	SH	CALL	OTHER	222,200			
PW Eagle Inc	PUT		69366y958	11,314	377,000	SH	PUT	OTHER	377,000		SHO	
Safeway Inc.	COM	NEW	786514208	106,043	3,494,000	SH		OTHER	3,494,000			
Sealy Corp	COM		812139301	65,791	5,037,600	SH		OTHER	5,037,600			
Source Interlink Cos Inc	PUT		836151959	1,659	174,600	SH	PUT	OTHER	174,600			
Take-Two Interactive So	PUT		874054959	100,884	7,074,600	SH	PUT	OTHER	7,074,600		SHO	SEC
Taser Intl Inc	PUT		87651b954	8,654	1,129,700	SH	PUT	OTHER	1,129,700		SHO	SEC
Tempur Pedic Intl Inc	PUT		88023u951	25,095	1,461,600	SH	PUT	OTHER	1,461,600		SHO	SEC
Thor Inds Inc	PUT		885160951	10,696	259,800	SH	PUT	OTHER	259,800		SHO	

This Edgar filing illustrates how the SEC aids short sellers in depressing markets. This filing illustrates short positions taken up in the options market, the number of short positions held by this fund that were on the Reg. SHO threshold list, and finally, the number of issuers involved in an SEC investigation. How many of these investigations were initiated after the company took their concerns public or after the fund involved petitioned the SEC to investigate these companies? How many investigations yielded nothing significant?

The SEC must understand, even a company found at fault can likewise have their markets manipulated.

From: marketreg [mailto:marketreg@SEC.GOV]
Sent: Wednesday, July 27, 2005 4:24 PM
To:
Subject: Your correspondence to Congressman Tierney

Dear Mr. Patch:

Your March 31, 2005, letter to Congressman John F. Tierney, was sent to the Chairman by Congressman Tierney via letter dated June 20, 2005. The correspondence was forwarded to the Division of Market Regulation for a response.

In your letter, you expressed your concerns regarding abusive naked short selling. On April 11, 2005, which was after you sent your letter to Congressman Tierney, the staff of the Division of Market Regulation posted on the Commission's website a document entitled "Key Points About Regulation SHO." This document is available at http://www.sec.gov/spotlight/keyregshoissues.htm.

This document provides a detailed response to many of the concerns expressed in your letter. For example, it appears from your letter that you misunderstand "grandfathering" under Regulation SHO. Regulation SHO does not require the close-out of fails to deliver that existed before a stock became a threshold security (known as "grandfathered" securities) because the Commission was concerned about creating volatility through short squeezes if existing positions had to be closed out quickly. SEC staff is working closely with the SROs to monitor whether "grandfathered" fails are being closed out in due course. In fact, the SROs are closely scrutinizing all sizeable fails, whether or not they reach the threshold securities levels, to assess whether broker-dealers are taking steps to close them out. In addition, the SEC and the SROs are currently examining firms for compliance with Regulation SHO.

The "grandfathering" clause of the Regulation does not affect the Commission's ability to prosecute violations of law that may involve such securities or violations that may have occurred before the adoption of Regulation SHO or that occurred before the security became a threshold security. Thus, you are mistaken when you state in your letter that "grandfathering" under Regulation SHO "accept[s] the prior abuses."

You also state that you may have evidence of manipulation. If you have specific enforcement-related information, you should forward that information in an email to enforcement@sec.gov. The staff of the Commission's Division of Enforcement carefully considers any comments it receives. As you may be aware, however, the Commission will neither confirm nor deny the existence of an investigation unless, and until, it becomes a matter of public record as the result of a court action or administrative proceeding. In addition, Commission investigations are conducted on a non-public and confidential basis to help assure the integrity of the investigative process.

As we have informed you in our previous discussions with you, the Commission takes naked short selling concerns seriously and pursues allegations vigorously where warranted. We believe that Regulation SHO is a significant and balanced measure and will be effective in curtailing potentially abusive naked short selling. In addition, the Commission staff is closely monitoring all aspects of the operation of Regulation SHO. As we learn more about how Regulation SHO is working, we will consider whether any adjustments to the rules are necessary. In addition, the SEC will continue to investigate complaints about abusive short selling, and will not hesitate to bring enforcement actions where violations of the law can be proven.

We hope the information provided is helpful.

Sincerely,

Office of Trading Practices

Division of Market Regulation

History

- As early as 1980's the SEC and SRO's were aware of organized crime infiltration on Wall Street. Starting with the Genovese family and Alphonse Malangone the penny stock market became a haven for fraud. The family had control of Brokerage Hanover Sterling and engaged in the illegal marketing of securities. The Mob short sales were represented through Falcon Trading Group and Sovereign Equity Management Corp. In 1995 Hanover Sterling went belly up and due to inadequate capital to cover naked short positions caused the collapse of Clearing Firm Adler Coleman. The NASD banned short seller John Fiero in early 2000 based on his illegal shorting practices.

- Between 1996 and 2001 the SEC and FBI were tracking illegal money laundering through Canada. Working through Pacific International the authorities determined that the major crime families were trading naked short through Canada because Canada had no affirmative determination laws. The fails were entering the US Markets and creating fails at the receiving brokers on publicly traded US companies.

- In 1998 The SEC proposed short sale reforms through a concept release. The SEC received over 3000 comment letters (by the Commissions admission) regarding the abuses of naked short selling and short sale abuses in general. The Concept release went nowhere.

- In 2001 the NASD presented to the SEC a proposal to modify Rule 3370. The proposal was to "eliminate a loophole" associated with the naked shorting through Canada. The SEC ignored the proposal until November 2003 when the SEC approved the closure of this loophole – Effective date April 2004. Better than 2 years after the NASD attempted to address fraud and address money-laundering issues.

- By October 2003, with extreme pressure from investors and issuers, the SEC proposed Regulation SHO. By now, fails to deliver in the markets had reached unhealthy levels as Wall Street and regulators ignored compliance with and enforcement of present short sale laws. The rule was approved in June 2004 with a stipulation; the grandfather clause.
    - The grandfather clause was the brainchild of SIFMA
    - The GF clause excused much of the past abuses by clients and member firms citing the need to maintain market stability and efficiency.

- August 2006 SEC OEA published a findings report citing the success of Reg SHO. The Division of Market regulation imbedded the analysis into a proposed rule to eliminate the GF clause presented in June 2006.
    - Analysis claimed success despite market fail data revealing an increase in companies listed on SHO and revealing a significant rise in aggregate FTD's.
    - GF clause was identified as a problem in reducing abuses by Chairman Cox
    - GF Clause removed effective 4Q 2007.

- August 2007 SEC publishes proposed rule to eliminate Options Market Making Exemption. Exemption has been used by clients to manipulate the equity market through concentrated large short positions in the options market.
    - SEC has not voted on a rule on this issue
    - Options Market has increasingly been shown to be where insider trading and short sale abuse now originate.
    - Recent Bear raids of Lehman and Bear Stearns were based on massive short sale abuse through the options market.