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Mr. Jonathan G. Katz, Secretary
Securities and Exchange Commission
450 Fifth Street NW
Washington, DC 20549-0609

August 15, 2005
Petition 4-500

Dear Mr. Katz:

I strongly support this petition to require short interest reporting for OTCBB and Pink Sheets stocks.

As you are aware, there are numerous allegations of short selling abuses in this sector of the marketplace. It is difficult for investors to determine whether these allegations are legitimate or whether they are merely cover-ups by the pump and dump operators. Better transparency in this marketplace is essential for investors to make informed investment decisions.

At the very least, the short interest reporting should be the same as for stocks listed on the major marketplaces.

I am also in favor of increased transparency regarding short selling in general. It should also be noted that the NYSE has started selling daily short selling statistics on a stock-by-stock basis, and that the Reg SHO pilot data on short selling are now available for stocks listed on major markets. The release of this data has not caused any noticeable perturbations in the market. The Commission should move to make similar data available for the OTCBB and Pink Sheets markets as well.

There is another problem in this sector of the marketplace that also needs attention. The experience so far with the threshold list of Reg SHO has shown that the list has not cleaned up the problems with failures to deliver. Indeed, the seemingly permanent tenure of dozens of stocks on the list is an embarrassment to the U.S. capital markets.

The reason for these failures to deliver is that there are regulatory impediments in the U.S. stock lending market. If investors or their brokers could borrow stocks on reasonable terms, there would be far fewer failures.

This problem is particularly acute in the OTCBB and Pink Sheets sector of the market. OTCBB and Pink Sheets stocks are not widely held by institutions. Such stocks are usually not marginable under Federal Reserve Regulation T. Because the primary sources of borrowing stocks are institutional investors and margin accounts, this means that it is often very difficult to find such stocks to borrow.

Alas, it is very difficult to lend stocks out of cash accounts or fully paid margin accounts. In particular, SEC Rule 15c3-3 -- Customer Protection--Reserves and Custody of Securities, provides severe regulatory hurdles to lending out fully paid or excess margin securities. In particular, section b.3 of the rule provides the conditions under which a brokerage firm may lend out fully paid or excess margin securities. These conditions include:

- A written agreement that contains the specific basis for compensation.
- Notification at the time of the loan of the specific securities borrowed.
- Notification that provisions of the Securities Investor Protection Act may not apply.
- Delivery to the lender of collateral or a letter of credit.

The practical impact of these well-intentioned requirements is that many practitioners in the back office tell me that “You just can’t lend out shares from cash accounts.” The problems inherent in negotiating trade-by-trade deals with numerous small retail accounts, and dealing with collateral and letters of credit, means that the cost of lending securities out of such accounts is prohibitive.

It should be noted that brokerage firms routinely lend out margined shares without notice or compensation to investors, and that this system works very smoothly. Opening up fully paid shares to the stock lending market would help the stock lending market work much more smoothly.

Short sellers are our first line of defense against securities manipulators who would pump and dump worthless securities. It is important that the stock lending market work efficiently in order for the short sellers to be able to do their job. By preventing fraudulent manipulators from hyping overpriced stocks to the stratosphere, they can prevent investors from buying overpriced stocks.

The Commission should immediately examine the stock lending market in order to see how it can improve the efficiency and transparency of the stock lending marketplace.

The requirements of section 15c3-3(b)3 can be relaxed in a manner that still protects consumers. In particular, b.3 could be relaxed in the following ways for lending from cash accounts:

- The written agreement could be a blanket agreement as part of the customer account agreement. The written agreement could leave the basis of compensation, if any, to be determined later. For example, “Compensation for the lending of a particular security, if any, will be 25% of any compensation received by us for lending out your stock."

- The written agreement would have plain English disclosures indicating that the securities could be loaned to short sellers and that this could have an impact on the price of the stock.
- Customers would have the right to prevent the lending of any particular security or to immediately recall a particular security at no charge.
- Customers would not be required to agree to stock lending in order to open or maintain an account.
- Notification of a borrowing transaction would not have to be made immediately, but could be on the customer's next regular statement.
- The letter of credit could be a blanket letter of credit that would protect all of the customers of the broker-dealer. The broker-dealer would only have to deliver a copy of the letter of credit upon request.
- The customer would have the right to know about any compensation received by the broker-dealer for lending the securities.

These enhancements would have many benefits:

- By improving the stock lending market, it would virtually eliminate problems with failures to deliver of securities.
- By making it easier to borrow shares, it would become easier for short sellers to stabilize prices and prevent the dangerous overvaluation of shares.
- It would make it easier for retail investors to lend out their shares and receive compensation for doing so.

Respectfully submitted,

James J. Angel

Rule 15c3-3 -- Customer Protection--Reserves and Custody of Securities

b. Physical possession or control of securities.

1. A broker or dealer shall promptly obtain and shall thereafter maintain the physical possession or control of all fully-paid securities and excess margin securities carried by a broker or dealer for the account of customers.

2. A broker or dealer shall not be deemed to be in violation of the provisions of paragraph (b)(1) of this section regarding physical possession or control of customers' securities if, solely as the result of normal business operations, temporary lags occur between the time when a security is required to be in the possession or control of the broker or dealer and the time that it is placed in his physical possession or under his control, provided that the broker or dealer takes timely steps in good faith to establish prompt physical possession or control. The burden of proof shall be on the broker or dealer to establish that the failure to obtain physical possession or control of securities carried for the account of customers as required by paragraph (b)(1) of this section is merely temporary and solely the result of normal business operations including same day receipt and redelivery (turnaround), and to establish that he has taken timely steps in good faith to place them in his physical possession or control.

3. A broker or dealer shall not be deemed to be in violation of the provisions of paragraph (b)(1) of this section regarding physical possession or control of fully-paid or excess margin securities borrowed from any person, provided that the broker or dealer and the lender, at or before the time of the loan, enter into a written agreement that, at a minimum;

    i. Sets forth in a separate schedule or schedules the basis of compensation for any loan and generally the rights and liabilities of the parties as to the borrowed securities;

    ii. Provides that the lender will be given a schedule of the securities actually borrowed at the time of the borrowing of the securities;

    iii. Specifies that the broker or dealer:

        A. Must provide to the lender, upon the execution of the agreement or by the close of the business day of the loan if the loan occurs subsequent to the execution of the agreement, collateral, which fully secures the loan of securities, consisting exclusively of cash or United States Treasury bills and Treasury notes or an irrevocable letter of credit issued by a bank as defined in section 3(a)(6)(A)-(C) of the Act or such other collateral as the Commission designates as permissible by order as necessary or appropriate in the public interest and consistent with the protection of investors after giving consideration to the collateral's liquidity, volatility, market depth and location, and the issuer's creditworthiness; and

B. Must mark the loan to the market not less than daily and, in the event that the market value of all the outstanding securities loaned at the close of trading at the end of the business day exceeds 100 percent of the collateral then held by the lender, the borrowing broker or dealer must provide additional collateral of the type described in paragraph (b)(3)(iii)(A) of this section to the lender by the close of the next business day as necessary to equal, together with the collateral then held by the lender, not less than 100 percent of the market value of the securities loaned; and

iv. Contains a prominent notice that the provisions of the Securities Investor Protection Act of 1970 may not protect the lender with respect to the securities loan transaction and that, therefore, the collateral delivered to the lender may constitute the only source of satisfaction of the broker's or dealer's obligation in the event the broker or dealer fails to return the securities.