

July 8, 2008

Securities and Exchange Commission  
100 F Street NE  
Washington, DC

REF: File No.: S7-19-07 34-58107

Mr. Chairman, members of the Commission Staff,

For the second time in as many years the Division of Market Trading has delayed submission of a proposal to the Commission staff for approval and in the process the team has inflicted unnecessary and irreparable financial damage to millions of investors and hundreds of public companies. This most recent delay in the proposal to reform the Options Market Making exemption is in direct conflict with the mission of the Commission which is to insure the highest levels of investor protection.

July 2006 the Division of Market Trading identified several loopholes created in the initial release of Regulation SHO and in response proposed two changes be made to correct these loopholes. First was the move to eliminate the ill-advised grandfather clause and the second was to address the issue of the Options Market Making exemption and the increasing level of fails seen in this area.

Behind those supporting the elimination of the OMM exemption are present laws passed down by Congress. Present law does not even recognize the options market making exemption as an alternative to the demands of prompt and accurate trade settlement defined in Section 17A of the securities Act of 1934.

Within the hundreds of public comments submitted, the SEC received commentary from Mr. Keith Higgins of the American Bar Association. While the memo never clearly addressed the underlying issues needing reform nor does it address the abusive nature to unsuspecting individuals, Mr. Higgins did feel compelled to challenge the lack of empirical data supporting the elimination of the grandfather clause. The Higgins memo was drafted on ABA letterhead and talks of an ABA Committee consensus but those of the media that questioned Mr. Higgins on this memo found that the letter was not drafted with staff approval of the ABA nor did it represent a majority consensus of the Committee for which Mr. Higgins spoke.

The SEC obliged Mr. Higgins none-the-less with a delay in action through a re-proposal of the rule including some conclusive data.

With data now available, as benign as it was, Mr. Higgins and his Committee never responded on the re-proposed rule change.

Did the data suddenly support or refute the SEC's proposal? The 8-month delay created to placate this individual cost investors and issuers billions in fraudulent trades with the rule outcome ultimately remaining unchanged. Most would have expected that during this period of delay a key individual responsible for the delay would have the courage to comment on the rule change itself.

Word is, Mr. Higgins admitted that he held no particular interest in the rule change whatsoever.

In other words, Mr. Higgins was simply acting out the agitator in disrupting critical rule changes affecting millions of peoples and hundreds of communities. Agitator for whom?

August 2007 the SEC re-proposed the elimination of the Options Market Making exemption and again public comments were overwhelmingly one sided. The public spoke and wanted the exemption eliminated.

Mr. Higgins again opined on this proposal but not the underlying subject. Higgins again requesting the release of more empirical data beyond that already presented so that informed decisions could be made. Nearly one year later the Division of Market Trading has elected to respond to Mr. Higgins with yet another delay and is using old data as the empirical information Mr. Higgins sought.

Mr. Higgins has once again thrown a wrench in the system and done so for disingenuous reasons. Clearly his interests in maintaining investor protection are misguided and based on his failure to provide a response to the previous data created on his behalf the SEC should have considered the source before impacting so many.

I ask, with the data now being provided being of a vintage representing nearly one year why is it that this data could not have been presented at any time over these past 9 months? Didn't the SEC have data that supported the origination of the proposal?

It was 9 months ago that the comment period ended and 9 months since Higgins questioned the lack of data. Is it too much to expect the Commission to act responsibly when it comes to investor protection? Does it really take 9 months to analyze old data?

With respect to the very data provided, it is for all practical purposes garbage. It will placate Mr. Higgins however since it is clear that all he wants is numbers – bogus or not.

Unfortunately this data is similar in structure to that provided previously. The data only provides SEC conclusions without the raw materials behind the conclusions making it possible for others to analyze and come to similar or dissimilar conclusion. Somehow the SEC expects that investors and issuers should trust their analysis despite decades of failure by the Commission staff.

The SEC's Office of Economic Analysis has already been questioned once on the constraints of their analysis and has been proven to have taken unreasonable methods in coming to their conclusions. Similarly the data provided today is meaningless based on the level of information provided. Information, pertinent information, is being excluded. The filters used in presenting this data filters out the evidence necessary to understand the abusive mechanics behind the trading.

Ultimately the data provided is irrelevant and had Mr. Higgins done his own research he would have understood that.

By definition SHO companies have mandatory close-out provisions of all fails to deliver once a company reaches threshold levels. Under these provisions the level of fails to deliver in SHO threshold securities would significantly decrease once achieving such levels unless the fails were exempt from settlement. Companies would not continue to see an accumulation of fails while under SHO due to the pre-borrow restrictions and other secondary stop gaps put in place.

The data provided by the SEC on their web site illustrates significant increases in fails in many threshold securities and, without enforcement actions being taken, such increases imply exemption from settlement. The only trades exempt from immediate close-out and trade restrictions are those affiliated with the Options Market Making exemption. Thus it does not take a genius to conclude that the new explosion in failed trades is affiliated with this specific exemption.

Better yet, let's take a look at the numbers the SEC provides in a raw data set. The CNS fails data now archived on the SEC site dating back to 2004

The average daily fails to deliver, by Month, are:

December 2004	747 Million	Month preceding Regulation SHO
December 2005	509 Million	One Year into SHO
July 2006	577 Million	Proposed elimination of GF Clause & OMM Exemption
August 2007	1,295 Million	Re-Proposed elimination of OMM Exemption
October 2007	1,071 Million	Elimination of Grandfather Clause
November 2007	1,070 Million	First Full Month w/o Grandfather Clause
March 2008	1,303 Million	Last Published Data Point

By these numbers alone, the level of fail shares in the system have more than doubled since Regulation SHO became law and have risen more than 30% since the grandfather clause was eliminated. The only plausible reason for this explosion in fails is the Options Market Making exemption. Any other cause for such a rise in fails during a Bear Market would be abusive stock manipulation and being void of any regulatory actions to date we must exclude that causation.

Clearly the SEC would not be turning their backs on the responsibilities of enforcement actions associated with market manipulation and fraud.

Today, short sellers who are finding it more difficult to short securities limited in available shares to borrow simply moved their trades to the options market renting out the OMM exemption to short the underlying equity. The short seller wants the position and the OMM wants the liquidity (trade commission) and thus it is a perfect marriage. The OMM is not required to adjust their offerings to balance their books; they simply hedge the imbalance through the naked short of the underlying equity. Pricing of that underlying equity is not of interest. The need for a locate in a hard to borrow market eludes the short seller when the OMM can short the equity for them.

This data is irrefutable in its raw and analyzed form.

And who pays the price for this negligence at the SEC staff levels? The investing public, public companies, and ultimately the US Economy pay the price.

The most public example of how victims are created would be that of Bear Stearns.

In the days leading up to the collapse of Bear Stearns the fails to deliver in that security were barely 19,000 shares. Those net fails exploded to 200,000 shares and then to 1.2 Million shares (\$64 Million) on the first day of the rumors. By the time the collapse was announced on Monday March 17 the trade fails for that Monday peaked at over 13 million shares. From 19,000 to 13 Million shares in a matter of 5 trade days. By the time the SEC blinked the damage is done and by the time the SEC has figured this out the money is re-invested making the trader more money or moved off-shore, immune from the SEC's grasp.

For those not understanding what these numbers mean, these are net fails. Intraday fails are not accounted for in this data and during a highly volatile trading period intraday fails covered by business close are not accounted for. Those intraday fails could be multiples of the final net fails posted as profit taking took over and could be part of the catalyst that creates the panic selling of eventual long shareholders.

The intraday Bear Raid.

And while the World is looking closely at exactly how and why Bear Stearns became a manipulated company with hundreds of billions in investor losses, and with the attention focused squarely at the Securities and Exchange Commission for answers, it is the SEC that again drops the ball. There is no rational reason to continue to allow predatory trading into a free falling market. Predatory trading that result in buyers failing to acquire in a timely manner the very securities they purchased to protect that market. There is no need to continue to allow the abuses attached to the OMM exemption.

In the mean time, Maybe Mr. Higgins could explain to all these victims what his intentions are in working the SEC into delaying this proposal once again. Certainly we can all hope that this man has the courage to now speak out on the underlying policy itself since the SEC was so kind as to put our financial safety at risk to appease this misguided individual.

The only response the SEC really needs: The Options Market Making exemption is illegal as it stands today. It violates Section 17A of the Exchange Act of 1934 as it relates to the prompt and accurate settlement of equity transactions. Risking the safety of the equity market and equity market investor for the sole purpose of creating a revenue stream for the Options Market Maker is in violation of the law. The OMM exemption is unnecessary as responded to by Citadel when questioned by the SEC over this matter.

David Patch  
[www.investigatethesecc.com](http://www.investigatethesecc.com)

Or for better insight and discussion of this issue; [www.deepcapture.com](http://www.deepcapture.com).