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Congress of the United States
House of Representatives

July 28, 2006

Chairman Christopher Cox
Securities and Exchange Commission
100 F Street, NE
Washington, DC 20549

Dear Chairman Cox,

I write to you with concern over the impact that abusive naked short selling could have on our capital markets and individual companies and their shareholders within these markets. To this end, I commend the Commission for its proposal to amend Regulation SHO by repealing the grandfather provision and narrowing the options market maker exception. However, I believe these changes are only the first steps toward reducing persistent fails to deliver and other associated abuses.

Thank you also for the opportunity to provide further ideas for modifications to Regulation SHO. I suggest that the Commission take two additional steps:

First, I reiterate Commissioner Atkins' statement that aggregate fail data should be disclosed. Without full disclosure, it is difficult to know the level of "naked shorting" and its risk to the capital markets. More transparency will lead to the elimination of abuses and to more investor confidence and security. I suggest that the Commission amend Regulation SHO so that the volume of failures to deliver are reported daily of each threshold security.

Second, to further curb the potential for market manipulation and protect investors, if a stock is sold, that stock should either be in the seller's possession or the seller should have entered into a bona fide contract to borrow the stock in advance of the sale. Current rules allowing the stock to be simply located allows for one share to be "located" multiple times without it actually being borrowed. Moreover, as an alternative to the regulatory requirement of a "bone fide agreement" to borrow the stock, a broker need only have "reasonable grounds to believe that the security can be borrowed" a phrase that in practice has become a serious loophole in the regulatory scheme. Using these loose standards, abusive short-sellers frequently never deliver the stocks they are selling, but rather postpone trade closures indefinitely.

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Recently, hedge funds filed a class action lawsuit against the major prime brokers alleging that the prime brokers told the hedge funds clients they had stock, allowed these hedge fund clients to short the stock, then did not deliver the stock as promised, leading to failure to deliver and a naked short position. In the meantime, the hedge funds paid the brokers lending fee for stock the brokers did not lend or even have to lend.

If a provision were added to Regulation SHO simply requiring a bona fide contract to borrow stock before selling it, and eliminating the "reasonable grounds to believe" loophole, this problem would diminish.

It is imperative that we strive to protect our investors and public companies by minimizing the manipulation of our capital markets. The interests of short-sellers must not be placed ahead of our duty to protect the small investors and employees who often depend on these companies for their livelihood and retirement.

Mr. Chairman, I look forward to working with you and your staff in this effort. Should you have any questions, please contact Jodee Niswanger on my staff at 202-225-8490.

Sincerely,

Rodney Alexander

RODNEY ALEXANDER
Member of Congress

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• **Comments:**

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