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Securities and Exchange Commission
100 F St. NW
Washington, DC 20549-9303
Rule-comments@sec.gov

Re: Request to require the periodic public disclosure of short-sale activities by institutional investment managers

File 4-689

Dear Securities and Exchange Commission:

I support this very reasonable petition and urge the SEC to promptly commence the requested rulemaking.

Summary

- Forced disclosure is an expropriation of intellectual property and a breach of privacy.
- The same logic that drives disclosure requirements of long positions also applies to short positions.
- While most shorts benefit the market, some are actively harmful.
- Better disclosure of short positions will leverage SEC enforcement resources.

Introduction

The NYSE and the National Investor Relations Institute (NIRI) have submitted a petition for rulemaking calling upon the SEC to utilize its statutory authority to bring disclosures of short positions in line with disclosures of long positions.[1] Currently, certain investment managers such as mutual funds are required to periodically disclose their holdings. Furthermore, officers and directors of public companies as well as 5% holders are also required to disclose holding and transactions.

In Europe, net short interest must be disclosed to regulators when it exceeds 0.1% of shares outstanding and to the public when it exceeds 0.2%. [2] Currently, there is no similar requirement in the U.S. The implementation of this requirement does not seem to have caused any damage to the EU market.[3]

Short selling is not necessarily bad. Indeed, most short selling is not "directional" short selling in which the short is betting that the stock will decline precipitously. Short selling is an important tool for market makers and arbitrageurs, neither of whom are making large directional bets.

Forced disclosure is an expropriation of intellectual property and a breach of privacy.

Any recommendation for further disclosure must overcome a basic hurdle: Information is the intellectual property of the people who have created that information. Forcing disclosure is an expropriation (without compensation) of that property. Furthermore, forced disclosure is a breach of the financial privacy of the owner of that information. Only if there is an overriding public interest should those intellectual property rights be breached. I believe the NYSE/NIRI proposal easily clears this high hurdle.

The same logic that drives disclosure requirements of long positions also applies to short positions.

These rationales include:

- Monitoring investment managers. Large investment managers are required to disclose their holdings for several good reasons. As they are the stewards of assets belonging to others, public

[1] http://www.sec.gov/rules/petitions/2015/petn4-689.pdf

[2] For details see https://www.esma.europa.eu/page/Short-selling and http://eur-lex.europa.eu/LexUriServ/LexUriServ.do?uri=OJ:L:2012:086:0001:0024:en:PDF

[3] For an analysis of the EU experience, see Panagiotis K. Staikouras, 'The EU Short Selling Regulation Revisited: New Evidence, Different Perspective?' (2015) 26 European Business Law Review, Issue 4, pp. 531–553. For ESMA's take, see http://www.esma.europa.eu/system/files/2013-614_final_report_on_ssr_evaluation.pdf

disclosure makes it possible for their beneficiaries to better understand their performance. It is illogical and inconsistent to make them disclose only long positions but not short positions.

- Concerns about the systemic risk of large institutional activities also motivate calls for disclosure. Furthermore, institutional ownership of positions is information that investors often find useful in their investment decisions. One of the legislative goals of §13(f) of the Securities Exchange Act was to "increase investor confidence in the integrity of the U.S. securities markets."[4] Given never ending allegations of abusive "short and distort" campaigns by shadowy manipulators, additional disclosure around short selling would certainly help to "increase investor confidence in the integrity of the U.S. securities markets."

- Monitoring insiders. It is well known that the buying and selling actions of insiders convey important information regarding the firms. Although insiders are often prohibited from selling short, some of them may effectively do so by hedging their positions in various novel ways. Effective reporting of short activity through hedging by insiders would provide an additional disincentive to insiders seeking to circumvent restrictions on their shorting by using derivatives.

- Control battles. One of the rationales for reporting long holdings is that the accumulation of a large holding may be the prelude to a control battle. Similarly, large short positions may indicate the possibility of empty voting in a control battle by a long shareholder who has hedged their position.

<u>While most shorts benefit the market, some are actively harmful.</u>

One of the reasons that blanket bans on short selling are harmful to the market is that most of the uses of short selling are beneficial to the market:

- Market makers often go short in order to accommodate customer orders. Their business model is to earn small amounts on large quantities of trades. Their willingness to buy and sell at any time based purely on price helps to hold down transactions costs for retail investors like me.

- When arbitrageurs find mispriced sets of securities, they buy low and short high. This keeps the prices of related securities in their proper alignment. For this reason, long-term retail investors like me can purchase ETFs confident that the ETF price will closely track the price of the ETF's underlying portfolio.

[4] See U.S. SEC, Office of Inspector General, Review of the SEC's Section 13(f) Reporting Requirements, http://www.sec.gov/oig/reportspubs/480.pdf See also https://www.sec.gov/divisions/investment/13ffaq.htm.

- Other short sellers bring important information to the market regarding overpriced securities. By bringing down the price of an overpriced security, they protect uninformed retail investors like me from paying too much.

However, not every short seller is an angel. There have been shorts who disseminate false or misleading information about their targets. Even worse, there are shorts who actively seek to interfere with the operations of the companies they have shorted. Perhaps the worst example is that of the famous Contac poisoning case. [5] Edward Arlen Marks put rat poison into packages of Contac cold medicine and then hoped to profit from the negative publicity by purchasing large quantities of put options on the manufacturer's stock. He was caught and convicted upon the tip of an options trader who noticed unusual trading in the put options. However, no one was ever convicted of murder in the famous Tylenol poisoning cases.[6] Was that also a scheme motivated by potential short selling profits?

Some short sellers actively attempt to reduce the cash flows of the companies they short. As corporate cash flows are usually a good thing for the economy, actions by short sellers to harm their target companies may not only harm the investors in those companies, but also inhibit capital formation and economic growth. For this reason, their activities deserve more scrutiny than that of long investors. For example some short sellers seek to invalidate the patents owned by their target companies.[7]

There are many other anecdotal stories about manipulative false information disseminated by short sellers. Also, there are many situations where issuers have blamed short sellers when the short sellers were correct, such as in the case of Enron. It is often difficult for investors to determine the truth amidst the media storms during the colorful battles that rage between short sellers and long investors. Having better information about who is short will help investors better interpret information releases during such battles.

Better disclosure of short positions will leverage SEC enforcement resources.

It is no secret that the SEC is not properly funded. If one adds up all of the dollars in the SEC budget from 1934 through 2015 ($19.9 billion), that is less than investor losses from one Enron. The SEC just

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[5] See "Californian Gets 27 years in Drug Tampering Case," Los Angeles Times October 31, 1986, http://articles.latimes.com/1986-10-31/local/me-8417_1_drug-capsules . He was released on 2002 according to http://www.bop.gov/inmateloc/. Also see http://www.businessinsider.com/our-interview-with-rick-ackerman-the-man-who-helped-helped-the-fbi-catch-a-criminal-merrill-lynch-trader-2010-5 and http://www.nytimes.com/1986/06/08/us/drug-tampering-suspect-has-long-arrest-record.html

[6] For an update, see http://www.pbs.org/newshour/updates/tylenol-murders-1982/

[7] For example, see Joseph Walker and Aaron Copeland, New Hedge Fund Strategy: Dispute the Patent, Short the Stock, *The Wall Street Journal*, April 7, 2015. http://www.wsj.com/articles/hedge-fund-manager-kyle-bass-challenges-jazz-pharmaceuticals-patent-1428417408.

does not have enough boots on the ground to properly investigate all violations of our securities laws. Although any artifice to deceive is a violation of the anti-fraud provision of §10(b) of the '34 Act, it is very difficult to identify and prosecute malicious rumor mongers, let alone product tamperers. Information related to the identity and size of economic short positions – whether in cash equities or derivatives would help to identify those with a motive to engage in defamatory practices.

The holes in the current reporting regime mean that no one – not even the SEC – really knows who the short sellers are. This clearly slows down and increases the cost of any SEC investigation into manipulative short selling. Requiring large short sellers – including those who short via derivatives – to report to the SEC would substantially reduce the time and effort that the SEC would have to expend to identify short sellers when investigating alleged abuses. As the SEC does not have the wherewithal to thoroughly investigate as much as it should, public disclosure will allow the victims of manipulative campaigns – the issuers and investors in unfairly attacked companies – to do some of the investigation themselves. As Justice Brandeis is often quoted in securities regulation, "Sunlight is said to be the best of disinfectants; electric light the most efficient policeman."[8] By providing more sunlight onto those with an economic motive opposite that of the issuer and its investors, better disclosure will inhibit some of the abuses that can occur.

Respectfully submitted,

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[8] Louis D. Brandeis, *Other People's Money, and How the Bankers Use It*, Frederick A Stokes Co., New York, 1913, Chapter V.