Biotechnology Innovation Organization

March 11, 2016

Brent J. Fields
Secretary
Securities and Exchange Commission
100 F Street NE
Washington, DC 20549-0609

Re: File No. 4-691: *Request to require disclosure of short positions in parity with required disclosure of long positions*

To whom it may concern:

The Biotechnology Innovation Organization (BIO) appreciates the opportunity to provide comment to the Securities and Exchange Commission (SEC) on File No. 4-691, the December 7, 2015, petition for rulemaking submitted by Nasdaq, Inc. Nasdaq's petition requests that the SEC "take swift action to promulgate rules to require public disclosure by investors of short positions in parity with the disclosure regime applicable to long positions." BIO strongly supports the short disclosure framework proposed by Nasdaq, and we similarly urge the SEC to promulgate rules to ensure parity between the public disclosures required of investors taking long and short positions.

BIO represents more than 1,100 biotechnology companies, academic institutions, state biotechnology centers, and related organizations in all 50 states. Because of the unique capital needs of biotech research (it can take more than a decade and upwards of $1 billion to bring a single product to patients), growing companies often turn to the public market for financing. Fair, liquid, and efficient capital markets are vital to their success. Emerging biotechs do not generate product revenue, but a strong public market gives them access to capital formation that supports the groundbreaking R&D being conducted by BIO member companies.

BIO applauds Nasdaq for proposing parity between short and long disclosure requirements. BIO also agrees that any short disclosure framework should include not just traditional short sales, but the full range of agreements that allow an investor to profit from a security's loss in value. We encourage the SEC to take action on this important rulemaking petition.

The Lack of Short Transparency Impacts the Entire Biotech Industry

Like Nasdaq, BIO acknowledges that appropriate shorting can support the stable, liquid markets that fuel the growth of emerging biotech innovators. However, BIO members strongly believe that the current lack of transparency around short positions is enabling trading behaviors that unfairly harm growing companies and their investors.

A healthy market allows for either a long or a short investor to "put his money where his mouth is" and bet on the future success or failure of a company. Long investors believe a company is promising, while short investors believe there are hazards in its path. If both long and short investors are required to disclose their bets, all market actors have the full range of information necessary to make informed trading decisions. However, the current regulations only require long disclosures, leading to information asymmetry and a lack of transparency that can be harmful to emerging issuers and their investors.

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The unique business model of groundbreaking innovation leaves emerging biotechs particularly vulnerable to stock manipulation via short selling and associated activities. It frequently takes years to conduct a single clinical trial, and the extended time between trial results is essentially a dark period in terms of the company's public information flow. A company's stock may jump significantly following the public release of clinical trial data, but the months and years spent conducting the *next* trial do not yield much, if any, information that should change the investing public's view of the value of a company or move its stock price. To put it bluntly, there are no quarterly sales numbers (most biotechs do not yet have a product on the market), no declining or rising profits to report (almost all growing biotechs are pre-revenue), and no interim trial results (trial data remains blinded until the research is finalized and the results are released).

Opportunistic short investors are able to use this information vacuum to their advantage by filling it with "information" of their own – usually dire warnings about the state of the company and the quality of the management that have little to no relation to the actual prospects of the business. This steady information drip can drive down the stock price, harming long investors who want to see the company succeed and generating a tidy profit for investors who took short positions before generating the negative publicity. This strategy is additionally effective because most small biotech stocks are thinly traded, so the rumors do not have to gain all that much traction to drive the stock down a few points and generate a return for short investors.

BIO's larger members also fall prey to similar shorting strategies because they face the same iterative clinical trial and FDA approval process as BIO's emerging company members. Though these large companies do have a revenue stream, their investors focus on future growth and clinical progress. Poor trial results or delayed decisions from the FDA still dramatically impact a company's stock performance – so even a rumor of clinical delays (substantiated or not) can produce a stock dive that benefits investors who have taken a short position. It is very easy for a rumor to spread because a company's actual trial results remain blinded and the FDA does not release information on its deliberations. These rumors and insinuations can drive down the stock price, divert long investors away from potentially life-saving therapies, and harm the ability of biotech companies to advance innovative treatments. This type of shorting behavior can also prevent growing companies from raising valuable innovation capital, often placing an additional discount on the equity pricing of a financing round. Without short transparency, market participants cannot judge rumors fairly, and are forced to make investment decisions without all of the relevant information.

BIO members do not object to short investors taking an objective look at a company, making a prediction about its future prospects, and taking a short position if they think the company is unlikely to meet expectations. The issue lies with investors who take short positions and then immediately take action to make those short positions turn a profit. Transparency is the easiest and most direct way to combat these trading behaviors – a short disclosure regime on par with long disclosures would shine light on the motivations of short investors and provide valuable information to issuers and the public. BIO is aware that the SEC has focused on so-called "short and distort" manipulation from an enforcement standpoint, but we believe that robust transparency is the first step to ensuring fair and efficient markets.

Short Manipulation via the Patent System

Short selling has come under increased scrutiny in the biotech industry over the past year in the wake of actions by a few hedge fund managers who abuse the U.S. patent system in order to inflate their own profits. Briefly, these individuals take short positions in a company's stock and then immediately file a series of challenges through the Patent Office's inter partes review (IPR) process. They do not have a competing patent, or indeed any specific stake in the company's science, yet the IPR process allows them to file a challenge – which naturally impacts the company's stock price as news spreads that its patents may be in jeopardy. The short investors' goal is not to actually impact the long-term standing of the patent (nor the long-term health of patients), but rather to initiate a short-term drop in the stock. The lack of transparency around short selling enables this behavior, which is extraordinarily damaging to the financial health of companies of all sizes in our industry. A commonsense disclosure regime for short positions would shine a light on manipulative practices, including abuses of the patent system, while giving investors and companies the information they need to make informed market decisions.

Conclusion

BIO believes that the lack of transparency around short positions is having a damaging impact on companies of all sizes across the biotech industry. Our members see no public policy justification for the existing disparity between the disclosures required of long and short investors – both groups are making predictions based on the risk and/or reward a given company presents, but only one group is required to disclose its holdings and transactions. As the Nasdaq petition notes, this discrepancy deprives "companies of insights into trading activity and limits their ability to engage with investors, the market of information to ensure it functions efficiently and fairly, and investors of information to use to make meaningful investment decisions." For biotechs specifically, this information asymmetry gives rise to certain trading behaviors that could make long investors skittish about providing the capital necessary to fund the decades-long, billion-dollar development pathway intrinsic to life-saving research.

An enhanced short disclosure regime that institutes parity with the disclosure requirements faced by long investors would shine a light on manipulative behavior, allow market participants to make informed trading decisions, and ensure fair rules for all types of investments. Nasdaq's petition notes that "transparency, fairness, and efficiency" underlie the existing long disclosure regime, and BIO sees no reason that these principles should not equally apply to short disclosures.

BIO applauds Nasdaq for proposing this important reform to the short disclosure regime, and we also commend the New York Stock Exchange (NYSE) and the National Investor Relations Institute (NIRI) for filing a similar petition (File No. 4-689). BIO urges the SEC to take action on these petitions in order to fulfill its mission of maintaining fair, orderly, and efficient markets. We look forward to working with the SEC as it considers how to bring parity to the short and long disclosure requirements in such a way that enhances transparency and encourages investment in innovative companies that are leading the search for next generation medical advances. If you have further questions or comments, please contact me or Charles Crain, Senior Manager of Tax & Financial Services Policy, at [redacted].

Sincerely,

E. Cartier Esham
Executive Vice President, Emerging Companies
Biotechnology Innovation Organization (BIO)