I am the former founder and manager of Fidelity’s NASDAQ Trading Department, and had managed and/or started five other trading departments during my extensive career on Wall St. Currently, as President of Matthew B. Management, Inc., a consulting firm, I provide expert/consulting services to securities attorneys, and to the financial service community with regard to trading or compliance related issues.

I am quite familiar with short selling techniques, and have advocated short selling as an intrinsic part of the portfolio hedge, while managing my various departments. I am sensitive, however, to the potential disruption caused by aggressive, non compliant short sellers, and am particularly sensitive to the potential disruption this behavior might have caused during the recent market swoon.

In my opinion, the imposition of some type of short sale restriction will likely enhance liquidity and restore confidence. However, the wrong restriction may ultimately reduce liquidity and negatively impact investor confidence.

The idea that only certain industries be susceptible to short sale restrictions is unworkable. In some multinational conglomerates whose businesses span several industries, how would you label such a complex company? I think it would only lead to confusion and/or funnel short sellers into particular conglomerates in order to short industries deemed unable to be shorted.

I also believe that in the current pricing environment, characterized by decimalization, both a bid test, and a last tick test are almost meaningless, can be “gamed”, and ultimately will unnecessarily tax the computer systems of all participants, attempting to comply while living in the world of flickering quotes. I have witnessed, when spreads were wider, less ethical participants post bids through Electronic Communication
Networks (ECNs) in an attempt to appear anonymous, while creating higher bids for 100 share orders, in an attempt to force executions of their “real” short sale orders. In the world of decimal quotes, this illegal gaming of the system would be virtually financially painless for the manipulating party.

My vote is to impose circuit breakers, on a per stock basis, after declining a fixed percentage. This could be easily determined and complied with in today’s environment, and does not readily provide a haven for unethical participants to manipulate the system. During the restricted period, I believe that there should also be a restriction on the creation of synthetic shorts, through the sale of deep in the money calls, or the purchase of particular puts, those with little or no premium. Any attempt to address the short selling issue without recognizing the derivative side of the equation, would simply hamper the unsophisticated short seller, but merely re-direct the professional, who would seemingly comply, without missing a beat. Sales of deep in the money calls by those looking to subvert the restrictions, can create the same disproportionate supply issues that the non compliant, aggressive short seller is currently responsible for.

Therefore, I propose one hour circuit breakers, after 10% declines of individual issues as determined by last sale, accompanied by restrictions on selling deep in the money calls or buying in the money puts.

Sincerely,

Leslie Seff
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