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August 13, 2009

Ms. Elizabeth M. Murphy
Secretary
U.S. Securities and Exchange Commission
100 F Street, NE
Washington, DC 20549

RE: Release No. 34-59748; File No. S7-08-09 and
Release No. 34-60388; File No. S7-30-08

Dear Ms. Murphy:

The Securities and Exchange Commission's recent actions adopting Rule 204T on a permanent basis is a significant advance in the effort to control abusive short selling. Rule 204T is a measured and targeted regulation that places the regulatory burden primarily upon those market participants that engage in short selling. It is an effective regulation that has significantly reduced the number of issues on the threshold lists and reduced overall fails to deliver by over 50%. This rule works. The deliberative open process used to vet this rule is most effective for considering complex issues. The Security Traders Association congratulates the Commission on this exemplary rulemaking effort.

The Security Traders Association (STA) has been involved in the short sale discussions for decades. We have long viewed short sales as a valid investment alternative and we have held equally strong support for strict enforcement of locate and delivery rules that serve to eliminate illegal naked and abusive short selling. The STA has also long shared its concerns about abusive short selling. We continue to believe that short sale regulations should concentrate on the clearing and settlements processes.

We absolutely concur with Commissioner Paredes' remarks at the Security Traders Association's 13th Annual Washington Conference on May 6, 2009:

> Much attention has focused on concerns with short selling, but it is equally important to emphasize the benefits of short selling. Short selling makes significant contributions to the effective operation of securities markets, benefiting all market participants and the economy overall. Short selling contributes to liquidity, capital formation, and more efficiently allocated risk. Short selling can buttress buying by allowing investors going long to hedge their positions; and short selling can

> encourage market participation by leading to improved price discovery. Short selling helps ensure that securities prices are not systematically biased higher than the fundamentals warrant, as could be the case if prices did not reflect the less optimistic views of short sellers. Price discovery matters because investors would be less willing to invest if the contrarian views of short sellers were not fully incorporated into securities prices. Furthermore, when price discovery is compromised, we run the risk that our securities markets allocate capital inefficiently.[1]

Rule 204

Final adoption of the amendments to Regulation SHO making permanent amendments contained in Interim Final Rule 204T of Regulation SHO is a positive step in the regulation of short selling and one for which the Securities and Exchange Commission (SEC) should be commended. Rule 204T moved resolving persistent fails to deliver from a "should" to a "must."

The amazing results produced by this Rule are hard to overlook. Strict enforcement of Rule 204T has reduced the number of stocks on the threshold lists from 582 in July of 2008 to 63 issues one year later, a reduction of over 89%. While STA did not file a comment letter for this particular action, we lauded the effectiveness of Rule 204T in all three short sale comment letters we filed this year. It is unfortunate that there seems to be a lack of recognition in the popular media of the success of this rule.

As Kevin Cronin, Global Head of Trading at INVESCO Capital Management accurately predicted at the May 5, 2009 SEC Roundtable, recent market advances and the absence of popular media provocateurs have all but erased the public ardor for the short selling debate. Traders, however, remain intensely focused on the issue, committed to an outcome which promotes fair and robust price discovery in an efficient and transparent market structure. While adoption of Rule 204T is an important step, we believe that there are other areas of concern that must be addressed and areas where additional regulation should be avoided.

In previous comment letters, the STA has suggested that the:

> SEC needs to clearly and unambiguously communicate to all market participants that naked short selling is illegal, and any transgressions will be prosecuted to the fullest extent of the law… without an unambiguous definition of naked short selling and a clear pronouncement that it is illegal from the regulators, this problem will persist."[2]

The definition of "naked" short sales that the SEC provided in the press release heralding the new Rule 204T did not escape our attention. We agree that "naked" short selling is technically not illegal, but making that sale without a locate is. We feel that the latter point needs to be communicated more clearly to market participants.

The STA is encouraged by the level of cooperation currently exhibited between the SEC and the CFTC, but we believe the SEC needs to be given clear authority to regulate markets where equity equivalent investments can be created. This is particularly evident in the discussion of short sale regulation, as most large short positions are actually created through the use of derivative products. Trading the derivative is less expensive and provides less information leakage to other market participants, making these strategies

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[1] Commissioner Troy A. Paredes, May 6, 2009, < http://www.securitytraders.org/conference-presentations/troy-paredes>.

[2] STA Comment Letter: Short Sale Circuit-Breaker Proposal, May 4, 2009, p. 4, < http://www.securitytraders.org/file_download/199>.

very efficient. The STA continues to believe that the unregulated OTC derivatives area is a fertile field for market manipulators.

Short Sale Disclosure with Appropriate Protections for Market Participants
The SEC should also develop an appropriate short sale disclosure regime. Sunlight is the best disinfectant, but many market participants prefer to remain in the shadows, making a voluntary disclosure system ineffective. The SEC should develop and mandate a disclosure system that employs the appropriate protections for market participants, whether in the form of delayed publication or participant anonymity. By all accounts, from the SEC press release and various news outlets, the SEC appears to be on track with the disclosure regime it is currently vetting with the various self-regulatory organizations.

Price Test and Circuit-Breaker Proposals
The STA continues to believe that the reincarnation of previously discredited rules, such as the price tests employed in the past, would be a grave mistake. Decrementing the robust price discovery process to achieve an un-measurable goal would be an extreme solution to the abusive short selling problem. Economic sanctions on the clearing and settlements area and strict enforcement of current regulations would produce the desired results.

The STA also commends the SEC for its handling of this rulemaking. As we have previously commented, we are fervent believers in the regular rulemaking notice and comment process. We continue to stress the importance of these procedures, as we commented in our January 12, 2009 comment letter on due process:

> This required comment period permits the collection of informed opinions regarding how the proposed regulation might work and also serves as a cooling off period, allowing for deliberative review and limiting political influence. The notice and comment process improves regulations by testing them "by exposure to diverse public comment," and by providing "fairness to affected parties."[3]

We would further commend the SEC for scheduling a roundtable to discuss additional measures to bring a greater degree of transparency to the markets, focusing on the securities-lending market. The STA suggested in our May 4, 2009 comment letter on the short sale circuit-breaker proposal that bringing transparency and price discovery to the securities-lending market would greatly benefit this traditionally opaque marketplace by introducing real competition and reducing lending costs.

In the May 4, 2009 comment letter, the STA also offered an alternative circuit-breaker proposal which would impose a pre-borrow requirement once a security hit the breaker level. We have previously questioned the appropriateness of certain interpretations of the locate rules and would respectfully suggest that these interpretations are a probable cause for the same piece of stock being used for multiple locates. The multiple locate issue is believed to be the source of much of the "phantom share" creation problem and thus excess share available to borrow. In order to alleviate the severe selling pressure that "phantom shares" generate on targeted stocks, we proposed the pre-borrow circuit breaker to circumnavigate the locate issues and impose economic sanctions on any additional short sells.

> The process of entering into an enforceable borrow agreement prior to making any further short sales will provide the desired "timeout" for the distressed issue, giving time for rational participants to evaluate what

[3] STA Comment Letter: Robust Regulation and Market Quality: The Importance of Due Process in the Course of Self Regulatory Rulemaking, January 12, 2009, p. 3, < http://www.securitytraders.org/file_download/176>.

> price the issue should be trading at. This timeout period is actually scalable, as an issue becomes harder to borrow, the process of borrowing shares becomes more onerous and time consuming. There is also a real and significant cost associated with entering into the borrowing agreement on trade date. Normally a short seller would locate shares to borrow on trade date and not enter into the borrowing agreement until settlement. Only when the short seller actually enters into the borrow agreement does he begin to pay for the borrowed shares. Forcing short sellers to enter into these borrow agreements three days earlier than they would normally borrow securities will change the profit/loss relationship of the proposed short sale, compelling less confident short sellers to abandon the trade and find greener pastures elsewhere, while allowing short sellers with conviction in their strategy to enter into the trade at a higher cost. Market participants understand the economics of trading and react quickly to avoid economic hardship; this proposal would literally hit them in the pocketbook. Quick-buck artists would be discouraged as their profits dwindled and other market participants would not even know this was happening. The mandatory pre-borrow would also immediately reduce the pool of shares available to borrow, thus making an issue more difficult to borrow and raising the borrowing costs.[4]

Phase-in or Pilot Program

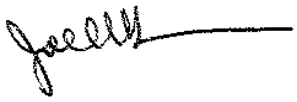
While we are encouraged by the announcement of a roundtable to discuss clearing and settlement solutions to the short sale problem, we anticipate that many organizations who currently profit from the opacity of the stock lending markets will be sharing opinions that these markets are not ready for a pre-borrow requirement. We heard these comments back in May when we announced our circuit-breaker proposal. Additional investigation convinced us that a limited pre-borrow requirement is feasible and may encourage development of systems compatible with the new infrastructure. Thus, we would encourage the Commission to phase in any pre-borrow requirement, either through our circuit-breaker proposal, which would target the pre-borrow requirement directly where it would be most needed, or through a pilot program.

> The STA has long held that the key to strong and efficient markets rests on the appropriate balance between regulation and competition. As regulations are developed they should be phased in to allow market participants to judge their effectiveness – how the new rules change the competitive dynamic and uncover any unintended consequences the new regulation may usher in. We further believe that it is more appropriate to attempt to accomplish the goals of regulation without disrupting the natural interaction of supply and demand or price discovery as much as possible.[5]

The STA would further encourage the SEC to postpone any final decision on price tests currently under consideration until it can consolidate and digest the comments produced by the announced roundtable into the current short sale discussions and evaluate for themselves where it would be most appropriate to target regulations. This approach would allow the Commission to evaluate the costs, benefits and effectiveness of all the regulatory alternatives and truly adopt a comprehensive measured response that would be effective at stopping the short sale abuses.

Sincerely,

Peter J. Driscoll
Chairman



John C. Giesea
President & CEO

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[4] STA Comment Letter: Short Sale Circuit Breaker Proposal, May 4, 2009, p. 5, < http://www.securitytraders.org/file_download/199>.

[5] STA Comment Letter: SEC Proposal on Short Sale Price Test , March 18, 2009, p. 2, < http://www.securitytraders.org/file_download/192>.

cc: The Hon. Mary L. Schapiro
The Hon. Luis A. Aguilar
The Hon. Kathleen L. Casey
The Hon. Troy A. Paredes
The Hon. Elisse B. Walter
James Brigagliano, Co-Acting Director Division of Trading and Markets
Daniel Gallagher, Co-Acting Director, Division of Trading and Markets