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September 21, 2009

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

**RE: Release No. 34-60509; File No. S7-08-09
Proposed Price Test Amendments to Regulation SHO**

Dear Ms. Murphy:

The Security Traders Association (STA or the "Association") welcomes the opportunity to respond to questions posed by the Securities and Exchange Commission ("SEC" or "the Commission") in SEC File 34-60509, Proposed Amendments to Regulation SHO.

The STA is a professional trade organization that works to improve the markets, ethics, business standards, and working environment for our members. There are approximately 5,200 members across North America, all engaged in the buying selling and trading of securities. The STA provides a forum for our traders, representing institutions, broker-dealers, ECNs, exchanges, market makers and floor brokers to share their unique perspective on issues facing the securities markets. Our members work together to promote investor protection and efficient, liquid markets.

A major fact that many market observers fail to recognize is that the equity markets have functioned efficiently throughout the recent financial meltdown and subsequent recovery. At times the equity markets were the last frontier of liquidity. When investors wanted liquidity they turned to the equity markets which were not frozen, unlike some other markets. When they did, the equity markets were functioning, providing bids and offers to facilitate investor transactions.

The STA has been involved in the discussion and debate about short sales for decades. Our members are actively involved in the business of trading securities and are therefore uniquely qualified to discuss regulations concerning the purchase and sales of securities. We believe that short selling is a legitimate and economically important activity that fosters price discovery and provides additional liquidity to the markets. The STA supports legitimate short selling as a critical component of overall liquidity. We applaud the SEC for focusing on balancing the costs

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and benefits of any additional short selling restrictions at both the April 8, 2009 open meeting and the May 5, 2009 Roundtable. We are not aware of any evidence produced at these meetings or in all the subsequent comment letters that showed restricting short selling would have eliminated naked or abusive short selling, increased investor confidence in any meaningful fashion or that the benefits of these regulations would outweigh the additional costs they would impose.

The STA supports strict enforcement of locate and delivery rules that have been proven to substantially reduce illegal and abusive short selling, including naked shorts. We believe that Rule 204 has produced empirical evidence that the clearing and settlement function is the appropriate area on which to concentrate short sale regulations. The significant reduction in the number of issues experiencing chronic failures to deliver is a result of Rule 204. Implementation and enforcement of Rule 204 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%. The STA specifically cites the effectiveness of Rule 204 in all three short sale comment letters we filed this year, however, there is a lack of attention to the success of the rule in the popular media.

If the Commission believes that additional corrective action is necessary in this area, the STA suggests that focusing on the locate provisions of Regulation SHO could tighten the locate process (Rule 203) and produce the desired results. In previous communications with the SEC the Association expressed its concerns about the interpretation and operation of this rule.

The STA identified one such interpretation which creates ambiguities in the locate process on page 18 in our recent *Special Report: The STA's Perspective on U.S. Market Structure* (May 2008).

Footnotes in the Regulation SHO release and the responses to the SEC's frequently asked questions, which address how broker-dealers satisfy the "locate requirement" under Rule 203(b)(3), serve to create more uncertainty. These interpretations seem to allow registered broker/dealers to rely on other entities, some of which are not registered with the SEC, for their performance under the rule. These nonregistered entities have become some of the broker/dealers largest customers making it more probable that the broker/dealer would readily accept any assurances provided to them.

This interpretation of Rule 203(b) appears in the Frequently Asked Questions Release even though the final rule release states: "As proposed, Rule 203(b) would have allowed the "person for whose account the short sale is executed" to perform a locate. We agree with commenters that the locate requirement should apply to a regulated entity -- the broker-dealer effecting the sale -- and have modified the adopted rule accordingly. Therefore, the rule as adopted makes clear that the broker-dealer effecting the short sale has the responsibility to perform the locate."

We also question the enforceability of Reg SHO Rule 203(b)(2) which "requires a broker-dealer, prior to effecting a short sale in any equity security, ...[to have]... reasonable grounds to believe that the security can be borrowed so that it can be delivered on the date delivery is due". The "reasonable grounds to believe" provision defies objective measurement and could provide an avenue to circumvent the intent of the locate rule. The "reasonableness" standard is even more impaired by the answer to question 4.1 in the Division of Market Regulation "Answers to Frequently asked Questions Concerning Regulation SHO" release regarding how broker/dealers should satisfy the reasonableness requirement. The division responds that "'Reasonableness" is determined based on the facts and circumstances of the particular transaction. What is reasonable in one context may not be reasonable in another context." We believe that

the Commission should tighten the abstract language in the rule and provide some concrete examples of how broker/dealers are expected to perform under this provision.

The STA also has concerns about whether the requirement of 203(b)(2) has been strictly complied with, namely that “The locate must be made and documented prior to effecting a short sale, regardless of whether the seller's short position may be closed out by purchasing securities the same day.” The high volumes in “targeted” issues, some being over 100% of the current float of the issue, leads to the conclusion that more than the available number of shares are being traded. Extreme trading volumes occurring as fails to delivers have come down significantly lead us to believe that there must be significant intraday short selling activity that is either not locating shares to deliver or receiving one of multiple locates being issued on the same shares.

The STA recommends that the SEC undertake a review of Rule 203 of Regulation SHO and its interpretations to amend language to address any circumvention of the intent of the rule. Surgically altering that language and strict enforcement could provide significant results in the effort to control improper and abusive short selling.

Short selling is a small segment of the overall equity marketplace and active short sellers are an even smaller group of participants. A recent study of trading data by Deutsche Bank shows that “as stocks plunged in September (2008), fewer than 8 percent of trades for companies in the S&P 500 Financials Index were done on consecutive downticks.”¹ Another recent study of exchange data by Bloomberg reveals, “When Citigroup plunged 26 percent on Nov. 20, (2008) the steepest drop on record for the New York-based bank, downticks represented 7.1 percent of trades.”²

The limited nature of the alleged problem of abusive short selling argues against imposition of trading restrictions on a permanent market-wide basis. Even bid and tick tests, including the alternative uptick rule, implemented on a circuit breaker basis would require all market participants to retool their systems at significant expense. Circuit breaker trading restrictions, while less intrusive than their market-wide permanent brethren, would also represent burdensome regulations and an unnecessary interference with price discovery mechanisms that, for the most part, are functioning with historical efficiency. This is especially true when other rules and regulations already on the books could be used to curtail this perceived problem. We believe clear and concise language in Rule 203 would offer a significant advance in addressing short selling issues.

Regulations should be designed to curb identifiable and measurable inappropriate behavior while encouraging the most robust price discovery possible. None of the proposals set forth in this release or the prior release meet those criteria. These proposals denigrate the price discovery process in an attempt to increase investor confidence. Offering less efficient price discovery will not restore investor's faith in the markets.

The STA agrees that the “alternative uptick rule” discussed in the August 20, 2009, Release 34-60509 removes the major difficulty of identifying an appropriate benchmark off which to price short sales. This alternative, however, would be much more restrictive for short sellers, significantly denigrating the price

¹ STA Comment Letter: Short Sale Circuit Breaker Proposal, May 4, 2009, p. 2,
< http://www.securitytraders.org/file_download/199>.

² Ibid.

discovery process. Requiring that all short sales be “passive” orders ineligible for immediate execution reduces the certainty that the trade will be executed. The alternative uptick rule could be much easier and less costly to implement than the other alternatives that required sequencing of bid data or tick data, but it would be a great deal more costly for the investing public. This alternative is more restrictive in how it allows short sales to execute and would therefore, severely restrict liquidity and widen spreads. Wider spreads and reduced liquidity will cost investors every time they trade through market impact (execution price).

If the Commission believes that additional regulation is absolutely necessary, then the Association would suggest the Commission review our circuit breaker elected hard borrow proposal sent May 4, 2009. In our letter, we suggest that an alternative short sale circuit breaker be used when a security declines to a given threshold (e.g. 10%), a hard borrow requirement would go into effect with the appropriate exemptions including an exemption for bona fide market makers and options market makers. If the security were to decline further (e.g.20%) the mandatory pre-borrow would apply to all short sales, no exemptions. And if the stock declined even further (e.g. 30%), short sales in that stock would be banned for the remainder of the day. The STA stands by our initial recommendation of clarifying existing regulation, and we believe our alternative circuit breaker presents a reasonable solution if additional short sale restrictions are necessary.

The STA stands ready to answer any questions you may have about these comments and answers many of the specific questions asked in the release below. If the Association can provide any additional information or assistance please do not hesitate to contact us through the Security Traders Association office at 212-867-7002.

Sincerely,



Peter J. Driscoll
Chairman



John C. Giese
President & CEO

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

**Responses to Specific Comment Requests Contained in SEC File Number 34-60509
Questions from Proposing Release**

1. Would the alternative uptick rule be more effective at preventing short selling, including potentially manipulative or abusive short selling, from being used as a tool to drive down the market or from being used to accelerate a declining market than the approach set forth in the proposed modified uptick rule or proposed uptick rule? If so, how? If not, why not?

The alternative uptick rule would be extremely effective in preventing short selling from being used as a tool to drive down the market because it does not allow short sellers to sell stock at the bid; however, we have yet to see any evidence that abusive short selling was a problem during the recent downturn. The STA believes that rules should be promulgated to resolve problematic behavior but abusive short selling has not been identified as part of the problem by any academic studies or other reliable evidence. The Deutsche Bank and Bloomberg statistics cited above demonstrate that short selling was a de minimus amount of the selling pressure that the markets experienced recently; it was certainly not the main selling force.

2. What effect would the alternative uptick rule have on the benefits of short selling, such as providing price efficiency and liquidity?

The alternative uptick rule would basically nullify any benefits of short selling. Price efficiency would be compromised because the informational content that short sales contain would be restricted to passive orders and not be communicated in the price discovery process. Liquidity would be reduced significantly and spreads would widen forcing investors to receive inferior executions.

3. Would the alternative uptick rule be easier to program into trading and surveillance systems than the approach in the proposed modified uptick rule or proposed uptick rule? If so, why? If not, why not?

Surveillance of the alternative uptick rule would be much easier than surveilling a bid test or tick test. Compliance officers would only need to look at the NBBO to ensure compliance with the alternative uptick rule, rather than comparing the bid or tick with the previous bid or tick under the other alternatives.

The alternative uptick rule would be much easier and probably cost less for the industry to implement because it does not require the sequencing of tick or bid data. Ongoing costs to the industry should also be significantly reduced as firms would not be required to maintain huge storage facilities for the required data. Investors, however, would pay a substantial price tag through wider spreads and less available liquidity.

4. If adopted, should the alternative uptick rule be combined with a policies and procedures approach similar to that discussed under the proposed modified uptick rule or a prohibition approach similar to that discussed under the proposed uptick rule? What would be the advantages and disadvantages, including costs and benefits of each of these approaches as combined with the alternative uptick rule?

The alternative uptick rule should not be adopted. If the Commission does go ahead with this proposal it should be implemented with policies and procedures rather than prohibitions. While the prohibition approach could apply Regulation SHO is a statement of policies and procedures and for consistency it would be advisable to maintain that approach.

5. If the Commission were to adopt a circuit breaker rule, should the circuit breaker, when triggered, result in the alternative uptick rule? If so, why? If not, why not?

As the Association communicated above, the breadth of the perceived problem does not rise to the level that would require a market wide permanent rule. We believe that trading restrictions are the wrong approach to solve this problem, however, if the Commission decides that a trading restriction is warranted, that trading restriction should be a circuit breaker. A circuit breaker leaves the majority of issues priced efficiently by not interfering with the price discovery process for those issues that have not tripped the circuit breaker.

Supplemental Comment Request

1. How effective would the alternative uptick rule be at helping to prevent short selling, including potentially abusive or manipulative short selling, from being used as a tool for driving the market down or from being used to accelerate a declining market by exhausting all remaining bids at one price level? Please explain and provide empirical data in support of any arguments and/or analyses. Could the alternative uptick rule be modified to better meet these goals? If so, how? Please explain and provide empirical data in support of any arguments and/or analyses.

The STA is unaware of any evidence that short sellers accelerated the market declines of last year. The fact that the markets continued to decline during the period covered by the emergency order halting short sales demonstrates the impact of short selling on the market decline was minimal. The STA believes that long sellers deleveraging and anticipating withdrawals and redemptions were largely responsible for the declines. Regulations should be designed to curb identifiable and measurable problems and abusive short selling has not been identified through any academic studies or other credible evidence as a major problem during the recent downturn.

2. How would the alternative uptick rule affect short selling in an advancing market? How would the alternative uptick rule affect short selling in a declining market? Please explain and provide empirical data in support of any arguments and/or analyses.

If the alternative uptick rule were adopted on a permanent market-wide basis, it would restrict short sellers to passive orders, allowing inflated equity prices to persist. In declining markets the inability to execute short sale orders would deprive the price discovery process of the informational content the short sale contained, thus allowing overpriced situations to persist. Short sellers would peg their orders to offer at one minimum price variation above the bid and ratchet those offers down as the bids exhausted. While this would slow executions of short sales it would also prolong and deepen downward moves by forcing there to be overhanging, passive supply.

If a circuit breaker version of the proposal is adopted there would be no effect in a rising market because the circuit breaker would not be triggered. In declining markets the stock would trade without restriction until the circuit breaker was triggered and then the price discovery process would be denigrated as described above. While we continue to believe that price restrictions are unwarranted, if price restrictions are to be implemented the circuit breaker approach would be less intrusive for the markets. The STA believes that regulatory intervention in the markets should not be done in such a way as to inhibit competitive market forces and practices which otherwise would have determined prices.

3. To the extent that there are concerns regarding investor confidence based on the numerous requests for reinstatement of short sale price test restrictions, would adopting the alternative uptick rule help restore investor confidence? If so, why? If not, why not? Please explain and provide empirical data or other specific information in support of any arguments and/or analyses.

The Security Traders Association shares the concerns of regulators about the effects recent precipitous and rapid equity price declines have had on investor confidence. Many have commented that the re-imposition of a price test will “slow” the declines and restore investor confidence. The STA is unaware of any empirical evidence establishing this causal relationship and would caution the Commission against acting rashly to correct this problem with intrusive price tests, especially when rising markets have already resulted in a significant improvement in investor confidence.

4. In addition to investor confidence and market volatility, we have stated that we are concerned about potentially abusive short selling. Would the alternative uptick rule help address potentially abusive short selling? If so, how? If not, why not? Please explain and provide empirical data in support of any arguments and/or analyses.

The STA is also concerned about abusive short selling. If the Commission is referring to short selling on continuous downticks in an effort to manipulate the price of a stock, we believe that the alternative uptick rule would be very effective in preventing this behavior because under this proposal participants would be precluded from hitting a bid let alone consecutive bids.

5. In the Proposal, we also noted that short selling may be used to illegally manipulate stock prices. What impact, if any, would the alternative uptick rule have on short selling used to illegally manipulate stock prices? Please explain and provide empirical data in support of any arguments and/or analyses.

While there has been a good deal of innuendo and supposition that manipulative activity contributed to the market’s recent declines, the STA is not aware of any credible evidence having been produced to support those claims. Market manipulation is already illegal and examinations and enforcement actions brought pursuant to existing regulations are adequate to address the problem.

6. What impact, if any, would the alternative uptick rule have on “bear raids?” Please explain and provide empirical data in support of any arguments and/or analyses.

Again, the STA is unaware of any credible evidence pointing to bear raids as the cause of recent declines and has repeatedly pointed to the balance sheets of many of the “targeted companies” as the real culprit.

7. Would the alternative uptick rule be an appropriate short sale price test in the current decimals environment? Would the alternative uptick rule be more suitable than the proposed modified uptick rule or the proposed uptick rule in a decimals environment with multiple trading centers? Please explain and provide empirical data in support of any arguments and/or analyses.

While STA does not believe that any price tests are required, we believe that the alternative uptick rule would rise above the benchmarking problems inherent in the other price test proposals. Our concern is that the investing public would receive worse executions should this rule be implemented.

8. How would trading systems and strategies used in today's marketplace be affected by the alternative uptick rule? How might market participants alter their trading systems and strategies in response to the alternative uptick rule, if adopted?

Traders wishing to employ hedging strategies that include a short sale leg could not be certain that the short sale would be executed. They would then be in the position of having established an un-hedged long position which was not their intent. To avoid this situation, unless the certainty of the execution of the short leg can be assured, traders are unlikely to execute the purchase and liquidity would be lost in both issues.

9. What impact, if any, would the trading requirements of Regulation NMS have on implementing the alternative uptick rule?

We do not see any conflicts with Regulation NMS.

10. The proposed modified uptick rule and the proposed uptick rule have as their reference point for a permissible short sale the current national best bid, and the last sale price, respectively, in relation to the last differently priced national best bid, and the last differently priced sale price, respectively. In contrast, the alternative uptick rule would have as its reference point the current national best bid. Accordingly, the sequence of bids would not play a role in determining when short sales are permissible. How would removing bid or sale price sequencing from the requirements of a short sale price test restriction, if adopted, affect implementation costs, ongoing costs, the effectiveness of the restriction in achieving the Commission's goals, market liquidity, pricing efficiency, and investor confidence?

Removing the sequencing requirements would significantly improve the ease of implementation and probably reduce the costs as well. Restrictive rules will result in wider spreads and lost liquidity. We also have serious concerns about the effect of this proposal on investor confidence. Markets move up and down and investors need to be prepared for downtrends and the availability of short selling provides them with that opportunity. There are no regulations that can insulate investors from losses when significant parts of the economy sour.