September 17, 2007

Securities and Exchange Commission
100F Street, NE
Washington D. C., 20549-1090

Mr. Chairman & Commissioners,

Now that we have officially received commentary from two of Wall Street’s most elite (Citigroup and UBS) lets discuss openly the issues they bring to the table.

Both firms are opposed to any modifications to the existing Options Market Making exemptions because each feels that they add the necessary liquidity required for the options market. Neither firm however provides any insight as to how much revenue they create by adding such liquidity into the markets. Hence, is it the liquidity for others they speak for or is it the revenues they receive that motivate such a response?

“CDMI believes that the proposed elimination of the OMM exception would significantly harm the ability of OMMs to provide liquidity and would widen the bid offer quotation for options on the affected securities to the detriment of investors, as detailed below.”

Question: How much liquidity are you willing to accept for fraud?

While the options market has a limited investor base, the equities market is open to nearly 96 Million investors who invest through equity purchases, mutual funds, and IRA portfolio’s sponsored by their employers. Citigroup (CDMI) nor UBS once spoke of what impact such liquidity and persistent settlement failure has to the underlying equity for which so many are directly or indirectly invested.

Question: Should an options market maker be afforded the luxury of creating failures to levels reaching the entire public float simply to close the bid offer quotation? Should every investor that wants to purchase an option be allowed to do so without market controls?

“While the Commission’s stated goal of "requiring that all fails to deliver be closed out within a reasonable time period" is worthy, CDMI believes that the elimination of the OMM exception will have the opposite effect by reducing liquidity in both the threshold security and the overlaying option, to the ultimate detriment of the investor.”

CDMI is obviously misunderstanding the process of a threshold security and the mandatory closeout provisions set forth by the Commission.

To continue to allow the options market maker to naked short hedge into the equity market during a threshold period for which mandatory closeout requirements are in play creates an inefficient market. The liquidity they say they bring to the threshold security is one-sided liquidity that goes against the very nature of the closeout itself. The mandatory buy-in attempts to close out an equity trade will fail due to the inability of a share available to purchase if the best offers represented in the market are merely hedged sales based on an optioned position taken.

It is abundantly clear that Citigroup has openly abused such closeout requirements in the short sale process as they have abused much of the short sale regulations that have existed in these capital markets for decades.
To support such claims, I refer the Commission to the July 2006 NYSE enforcement case in which Citigroup Global Markets was fined $250,000 for clear violations of Regulation SHO and the close-out provisions of SHO. Not to be outdone, FINRA fined Citigroup Global Markets an additional $87,700 last month for selling short out of proprietary accounts without conducting the proper affirmative determinations that such trades can settle. The FINRA complaint also alleged that Citigroup was selling naked short out of their market making account when they held customer orders that could have been executed in their place (front running trades).

I believe that this is the liquidity Citigroup continues to refer to despite the fact that such liquidity being detrimental to the actual equity market and those who invest in such a market.

UBS on the other hand is not only opposed to the elimination of the options market making exemption, UBS is also opposed to the requirement that those selling shares long properly mark where such shares exist to insure the client is in fact long.

The Commission proposes a requirement that broker-dealers executing sell “long” orders document the present location of the securities being sold. UBS is strongly opposed to this requirement as unnecessary, redundant to existing regulation, unduly burdensome, inefficient and costly to implement.

Apparently UBS continues to fail to monitor the level of mis-marked trades that are executed into the marketplace on a month-by-month basis by firms across the country. In many cases the FINA enforcement action results in a compliance fine imposed for the failure to mark a short sale a short, instead marking such a long transaction. By making such an error the firm will equally be in violation of the affirmative determination rules of the short sale as firms like UBS will simply execute the order on behalf of a client that does not really own the shares to sell.

Such a violation is exposed in the March 2007 enforcement case against Goldman Sachs for allowing clients to illegally short the equity markets through Goldman’s electronic trade system while marking such sales as long sales. While Goldman was fined $2 Million, the value of profits to the clients and the impact such trades had on the underlying equity were never revealed and most likely never calculated.

The costs of implementation, ongoing compliance, surveillance and enforcement of the new marking requirements greatly outweigh any incremental benefit of the proposed amendments.

Before the SEC considers this statement by UBS at face value I would urge the SEC to provide the investing public with what they perceive to be the accepted level of collateral damage (fraud) that will be accepted by not taking such appropriate actions.

In an industry that does out $27 Billion in annual bonuses and whose corporate executives are receiving compensation packages nearing $60 Million annually, would the one-time cost of putting in compliance systems and the yearly maintenance really be that dramatic? By UBS’s own estimates, Even at the Commission’s estimate of .5 seconds per trade, the annual hourly burden on the industry would be 268,688 hours. At $100.00/hour that is $26 Million distributed equally across this multi-trillion dollar industry. This actually assumes that every 0.5 second of time is fully burdened before such value is fully loaded.

As has been stated many times over, the Commission is at a cross road where they must decide which direction they choose to take. Will the Commission draft rules that focus on maintaining business revenues for Wall Street firms that are routinely found to willfully violate such rules or, will
the Commission chose a path that clearly puts the interests of the 96 Million investors above such a revenue stream.

Liquidity is a valuable tool in our markets but liquidity, the right for anybody that wants in to get in, is meaningless if such a right has a direct impact on the players that presently exist in such a market. Clearly the right to liquidity comes to varying degrees depending on who the investor is where the greatest benefit comes to those institutions and wealthy funds/investors who use such leveraged positions to dictate our markets today.

In closing the SEC must consider their own position to regulatory enforcement as an example of how the average investor is protected in these capital markets. As seen in the John Mack case, the SEC clearly felt underpowered and thus was willing to walk away from a potential confrontation. Wealth buys political clout and an indefinite pool to legal spending. The average investor sees that similar wealth drowns out our ability to invest in a safe and protected market place and witness continued regulatory actions that add more protection to the already leveraged positions of the institutions and wealthy investors.

The Options Market is already tailored to a higher class of investor and thus must be considered a “minority market” The Commission is urged to consider the players in the Options market and decide whether such players should be given the added leverage to trade a fully saturated market in a means that continues to impact that equity markets position. There must be boundaries and limitations to how far these leveraged investors can go. Clearly today there are no such limitations as hedged options positions have created fails equal to deliver greater than a majority of the entire public float in some companies.

The Commission needs to decide whom they decide they will protect under such circumstance.

As a representative of the investor class, I urge you to deny your urge to protect these firms with the right to expect riskless trading strategies. Neither Citigroup nor UBS provided a modicum of proof that such changes will impact anything other than their right to riskless revenues in a market whose foundation is risk. The Commission must also carefully avoid the trap being set by these market participants whereby the Commission is threatened by the commentary where the participants claim they will simply stop making a market in securities. It is an idle threat and, in a worst case, a situation that may be required under circumstances of extreme excess in fails.

Remember: EVERYBODY HAS A RIGHT TO INVEST SAFELY – NOT JUST THE MEMBERS.

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