



Edward S. Knight
Executive Vice President,
General Counsel and
Chief Regulatory Officer
One Liberty Plaza, 165 Broadway
New York, NY 10006 / USA
(212) 401-8906
Edward.knight@nasdaq.com

Nasdaq.com

By Electronic Mail

December 7, 2015

Mr. Brent J. Fields
Secretary
U.S. Securities and Exchange Commission
100 F Street, NE
Washington, DC 20549-1090

Re: Petition for Rulemaking to Require Disclosure of Short Positions in Parity with Required Disclosure of Long Positions

Dear Mr. Fields:

By this Petition, and in accordance with Rule 192 of the Securities and Exchange Commission (the "Commission") Rules of Practice,¹ the Nasdaq, Inc. ("Nasdaq"), as a public company and on behalf of our clients who are also public companies, respectfully requests that the Commission, pursuant to Sections 10 and 13 of the Securities Exchange Act of 1934, as amended, and Section 929X of the Dodd-Frank Wall Street Reform and Consumer Protection Act of 2010 ("Dodd-Frank"), 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, including the timing for such disclosure and when updates are required.²

¹ 17 CFR 201.192.

² Specifically, Section 929X(a) of Dodd-Frank provides that "[t]he Commission shall prescribe rules providing for the public disclosure of the name of the issuer and the title, class, CUSIP number, aggregate amount of the number of short sales of each security, and any additional information determined by the Commission following the end of the reporting period. At a minimum, such public disclosure shall occur every month." See Pub. L. No.

To be clear, we are not suggesting limitations or restrictions on short sale activities. There is ample evidence that legitimate short selling contributes to efficient price formation, enhances liquidity, and facilitates risk management.³ Evidence also shows that short sellers benefit the market and investors in other important ways, including by identifying and ferreting out instances of fraud and other misconduct at public companies.⁴

Nevertheless, there is a serious gap in the regulation of short sellers related to their disclosure obligations. As Congress recognized, it is incongruous that certain investors who accumulate long positions are required to publicly disclose their holdings, but there is no corresponding obligation for short sellers to do so, including synthetic or derivative instruments that allow an investor to profit from a loss in value of the underlying security. This asymmetry has several deleterious effects: it 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. The Commission's Dodd-Frank rulemaking over the last several years has made important enhancements to transparency and deserves credit. However, Dodd-Frank provides the Commission with the mandate to make further enhancements and lift the veil of secrecy behind which short sellers operate. It must do so.⁵

The obligation of investors to disclose long positions and when they must do it is part of a 47-year old regulatory disclosure regime and stems from amendments to the Securities Exchange Act of 1934 set forth in the Williams Act, adopted by Congress in 1968. As currently enacted, these rules require, among other things, investment managers and funds that own or have discretion over prescribed amounts of equity securities, regardless of whether they are registered

111-203, Section 929X(a), codified as amended at 15 U.S.C. 78m(f)(2). The Commission has not yet taken action pursuant to this provision.

³ See Securities Exchange Act Release No. 48709 (Oct. 28, 2003), 68 FR 62972 (Nov. 6, 2003); Commission's website, "Key Points About Reg SHO," available at: <http://www.sec.gov/investor/pubs/regsho.htm>; and Katherine McGavin, *Short Selling in a Financial Crisis: The Regulation of Short Sales in the United Kingdom and the United States*, 30 Nw. J. Int'l L. & Bus. 201 (2010) ("McGavin"), available at: <http://scholarlycommons.law.northwestern.edu/njilb/vol30/iss1/7/> ("In a well-regulated market with minimal risk of abuse, the liquidity and information efficiency benefits of short selling far outweigh its potential harm.")

⁴ Owen A. Lamont, Yale School of Management, "Go Down Fighting: Short Sellers vs. Firms," available at <http://www.nber.org/papers/w10659.pdf> ("The evidence suggests that short-sellers play an important role in detecting not just overpricing, but fraud,"). See, also, "Probe Gotham? Er, no. Gowex is Bust," *Financial Times* (Alphaville blog), July 6, 2014, available at: <http://ftalphaville.ft.com/2014/07/06/1893582/probe-gotham-er-no-gowex-is-bust/>

⁵ This is not the first time Nasdaq has called for increased transparency around short selling activity. See Testimony of Nelson Griggs, Executive Vice President, Nasdaq, Before the Senate Banking, Housing and Urban Affairs Committee, Subcommittee on Securities, Insurance and Investments, Venture Exchanges and Small Cap Stocks, March 10, 2015, available at: http://www.banking.senate.gov/public/index.cfm?FuseAction=Files.View&FileStore_id=eeb822ac-fba1-448d-a57e-5a1a6941d4e8 ("We also recommend consideration of disclosures of short positions in smaller companies that are similar to the disclosures required of long positions, providing companies and other investors with transparency.")

with the Commission, to disclose their long positions on Form 13F, Schedule 13D and/or Schedule 13G, depending on the circumstances. Such investors must generally disclose their long positions on Schedule 13F within 45 days of the end of each calendar quarter, subject to delays based on requests for confidentiality. Further, when such investors acquire beneficial ownership of more than five percent of the voting class of a company's equity securities, they are generally required to file a Schedule 13D with the Commission. This filing must be made within ten days after the five percent threshold is exceeded.⁶ However, if such investors are either Qualified Institutional Investors or Passive Investors, they may make such disclosure on Schedule 13G within 45 days of the end of a calendar year, subject to updated disclosure based changes in ownership positions.⁷

There are no comparable public disclosure requirements in the U.S. applicable to the accumulation of short positions.⁸ Instead, short sellers can amass short positions secretly, abetted by increased use of derivatives and other synthetic instruments. This is particularly untenable in light of the fact that in recent years, investors with short positions, or derivative equivalents, have taken a more activist role in corporate policy and governance. Because there is

⁶ The ten day window has come under increased scrutiny amid calls for reform. In 2011, the law firm Wachtell, Lipton, Rosen & Katz petitioned the Commission to reduce the ten day period to one-day, citing the potential for market manipulation and abusive tactics during this period ("Wachtell Petition"). The Wachtell Petition, available at: <http://www.sec.gov/rules/petitions/2011/pctn4-624.pdf>, also urged the Commission to expand the definition of "beneficial ownership" for Section 13 reporting purposes to "encompass ownership of any derivative instrument which includes the opportunity, directly or indirectly, to profit or share in any profit derived from any increase in the value of the subject security." In a recent letter to Congress, ethics and watchdog groups urged Congress to act in this area. Letter from Citizens for Responsibility and Ethics in Washington, Government Accountability Project and New Rules for Global Finance to Hon. Richard Shelby, Chairman and Hon. Sherrod Brown, Ranking Member, U.S. Senate Committee on Banking, Housing and Urban Affairs; Hon. Jeb Hensarling, Chairman, and Hon. Maxine Waters, Ranking Member, U.S. House Committee on Financial Services, Apr. 15, 2015 ("Loopholes in federal securities laws are allowing activist investors to secretly buy large stakes in companies before initiating hostile take overs, depriving the market of material information and significantly disadvantaging ordinary investors."), available at: http://www.citizensforethics.org/page/-/PDFs/Legal/Letters/4-15-15-10_Day_Rule_Banking_Letter.pdf?nocdn=1. See, also, David A. Katz and Laura A. McIntosh, "Corporate Governance Update: 13(d) Reporting Inadequacies in an Era of Speed and Innovation," *New York Law Journal*, September 24, 2015 ("Katz and McIntosh"), available at: <http://www.newyorklawjournal.com/id=1202737986585/13d-Reporting-Inadequacies-in-an-Era-of-Speed-and-Innovation>; and "SEC Is Urged to Shorten Window for Investor Tip-Offs," *Wall Street Journal*, March 27, 2014, available at: <http://www.wsj.com/articles/SB10001424052702304688104579465661917560346>.

⁷ In addition, every director, officer or owner of more than 10% of a class of equity securities registered under Section 12 of the Securities Exchange Act of 1934 must file with the Commission a statement of ownership regarding such security.

⁸ In the U.S., self-regulatory organizations (SROs) are required to provide on their websites daily aggregate short selling volume information for individual equity securities. The SROs also provide website disclosure on a one-month delayed basis of information regarding individual short sale transactions in all exchange-listed equity securities. You can find that information here: <http://www.sec.gov/answers/shortsalevolume.htm>. On June 5, 2014, as required by Section 417 of Dodd-Frank, the Staff of the Commission's Division of Economic and Risk Analysis published a study on "Short Sale Position and Transaction Reporting." The Study left open the question of whether the Commission should require disclosure of individual short positions.

no disclosure required of short positions, the investing public and issuers do not know when such circumstances exist or whether the incentives of these investors are inconsistent with corporate policies and objectives.⁹ As a result, without full information about short positions maintained by individual market participants, investors and companies are left to speculate on the extent of short activity, to the detriment of market efficiency, price discovery and shareholder engagement. This information deficiency potentially subjects a company's stock price to trading and volatility based on rumor, speculation and innuendo, not facts or substantive analysis.

Trading in Herbalife Ltd. stock surrounding speculation about the intentions of a well-known short seller is a case in point. As highlighted in a New York Times article, gyrations in the company's stock price followed the short seller asking a few questions on an analyst call and, in a separate instance, his mere physical presence at an investor conference where he made no mention of the company.¹⁰ Further, the stock of two companies he mentioned at this conference declined significantly following his comments, even though it was unknown whether he had a position in any of these companies or not.¹¹ These examples demonstrate why it is so important to lift the veil of secrecy behind which short sellers operate in order to temper speculation and over-reaction by markets to short selling-induced volatility.¹² Without such action, stocks will continue to be buffeted by rumor, speculation and innuendo, and companies, investors and the market will continue to be deprived of important information.

There are other important reasons to increase transparency in this area. Net short positions can have a direct and material impact on trading in securities, including when short positions are established through derivative instruments.¹³ Further, enhancing transparency would minimize the opportunity for some market participants to engage in manipulative or abusive conduct that

⁹ Theodore N. Mirvis, Adam O. Emmerich and Adam M. Gogolak, "Beneficial ownership of Equity Derivatives and Short Positions – A Modest Proposal to Bring the 13D Reporting System into the 21st Century," Wachtell, Lipton, Rosen & Katz (2008) ("Mirvis, Emmerich and Gogolak"), available at: <http://www.wlrk.com/webdocs/wlrknew/WLRKMemos/WLRK/WLRK.15395.08.pdf> ("For example, a shareholder in a company who has spoken out against an acquisition requiring the vote of the acquiring company's shareholders could have a net short position in the target company. Or more directly, net short shareholders may speak out against legislation or other regulatory actions that would be beneficial to the company whose shares they have shorted.")

¹⁰ Steven Davidoff, "Disclosure by Short-Sellers Would Improve Market Clarity," New York Times, May 22, 2012 ("Davidoff"), available at: http://dealbook.nytimes.com/2012/05/22/disclosure-by-short-sellers-would-improve-market-clarity/?_r=0. See, also, Alexandra Stevenson and Ben Protess, "Bruised, Herbalife Swings Back at an Accuser," New York Times, June 2, 2015, available at: <http://www.nytimes.com/2015/06/03/business/dealbook/herbalife-steps-up-lobbying-to-counter-ackmans-attacks.html>

¹¹ See Davidoff.

¹² See McGavin at 237.

¹³ Counterparties to such derivative instruments may hedge their position through market transactions. Puts or equity swaps that replicate short positions may lead to sales in the underlying security. See Mirvis, Emmerich and Gogolak, *supra* note 9.

can potentially result from large, undisclosed short interests, particularly where investors have taken a public and vocal role in corporate policy.¹⁴

In a survey of its members about their views on short sale reporting, the National Investors Relations Institute found strong support for greater transparency of short positions.¹⁵ The respondents also identified a number of benefits from increased transparency: heightened confidence in the markets, enhanced ability to identify market abusers, more informed investment decisions by investors, improved ability of companies to react to potentially manipulative rumors, and greater clarity and insight into investment activity.¹⁶

While the U.S. has focused on disclosure of aggregated data on short sales, starting in 2008, the U.K., France and Spain in turn adopted and implemented enhanced disclosure requirements for short positions applicable to individuals.¹⁷ In a February 2009 Discussion Paper on Short Selling (the "FSA Discussion Paper"), the FSA, after considering the benefits of disclosure (including detection of market abuse and visibility of unusual short selling activity that could otherwise

¹⁴ See, e.g., "Activist Investors Often Leak Their Plans to A Favored Few," *Wall Street Journal*, March 26, 2014 ("For a new breed of "activist" investors, tipping other investors is part of the playbook"), available at: <http://www.wsj.com/articles/SB10001424052702304888404579381250791474792> and Joseph Walker and Rob Copeland, "New Hedge Fund Strategy: Challenge the Patent, Short the Stock," *Wall Street Journal*, April 7, 2015, available at: <http://www.wsj.com/articles/hedge-fund-manager-kyle-bass-challenges-jazz-pharmaceuticals-patent-1428417408>; and Leo E. Strine, Jr., Can We Do Better By Ordinary Investors? A Pragmatic Reaction to the Dueling Ideological Mythologists of Corporate Law, 114 Col L.Rev. 495 (2014) ("[T]he voting electorate should have up-to-date, complete information about the economic interests of a hedge fund holding a large bloc of a corporation's shares and proposing that the corporation make business strategy changes it is suggesting."), available at: <http://columbialawreview.org/wp-content/uploads/2014/03/Strine-L..pdf>

¹⁵ Letter from Jeffrey D. Morgan, President and Chief Executive Officer, National Investor Relations Institute, to Elizabeth Murphy, Secretary, Securities and Exchange Commission, dated June 21, 2011, available at: <http://www.sec.gov/comments/4-627/4627-134.pdf>

¹⁶ Id.

¹⁷ The UK Financial Services Authority ("FSA") was the first, requiring disclosures starting in June 2008 in stocks undergoing rights issues, which it subsequently expanded to financial stocks. See "Financial Services Authority introduces disclosure regime for significant short positions in companies undertaking rights offerings," FSA/PN/057/2008 dated June 13, 2008, available at: <http://www.fsac.org.uk/library/communication/pr/2008/057.html>; FSA's policy statement "Temporary Short Selling Measures," January 2009, available at: http://www.fsa.gov.UK/pubs/policy/ps09_01.pdf; and "FSA confirms extension of short selling disclosure regime," FSA/PN/009/200, January 14, 2009, available at: <http://www.fsa.gov.UK/pages/Library/Communication/PR/2009/009.shtml>. The FSA has since become two separate regulatory authorities, the Financial Conduct Authority and the Prudential Regulation Authority. See <http://www.fsa.gov.uk/>. See also Charles M. Jones, Adam V. Reed and William Waller, "Revealing shorts: An examination of large short position disclosures," June 28, 2014 ("Jones Reed Waller"), available at: http://business.gwu.edu/wp-content/uploads/2015/02/Finance_Seminars_Revealing-Shorts_2.20.2015.pdf (finding next-day disclosure requirements reduced bid-ask spreads)

cause an over-reaction) against the possible harm to asset managers and the costs to asset managers of compliance, concluded that an individualized disclosure regime was appropriate.¹⁸

Thereafter, in November 2012, the E.U. Short Selling Regulation (“SSR”) came into effect, superseding and expanding on the existing requirements in the U.K., France and Spain.¹⁹ The E.U. SSR provides for a public and private notification regime for investors who hold net short positions. It requires -- for all shares admitted to trading on a trading venue in the E.U. -- public disclosure of net short positions of 0.5% and above of outstanding shares (the “Initial Public Disclosure Threshold”), when there is a 0.1% increase and decrease in net short position above the Initial Public Disclosure Threshold, and when the net short position falls below the Initial Public Disclosure Threshold. It further requires that net short positions of 0.2% and above be disclosed to the relevant competent authority. Calculation of net short positions must include indirect holdings through related financial instruments including derivatives (including index derivatives), baskets, depository receipts and exchange-traded funds.

Disclosures must be made the day after a threshold is crossed, and, with some exceptions for market makers and stocks with a primary listing outside the E.U., must include the name of the entity that has the position, the amount of the position and the name of the company in which it has a position.

The E.U. SSR cites several benefits to requiring this disclosure:

“Enhanced transparency relating to significant net short positions in specific financial instruments is likely to be of benefit to both the regulator and market participants. For shares admitted to trading on a trading venue in the Union, a two-tier model that provides for greater transparency of significant net short positions in shares at the appropriate level should be introduced. At the lower threshold, notification of a position should be made privately to the regulators concerned to enable them to monitor and, where necessary,

¹⁸ In the FSA Discussion Paper, the FSA noted that “[t]he question is therefore whether the indirect costs of requiring public disclosures outweigh the benefits. We acknowledge that some market participants would prefer for any disclosures to be done privately to the FSA, arguing that public disclosure might have potentially harmful commercial effects. They are concerned that disclosures might make themselves vulnerable to being squeezed by competitors when it comes time to cover their short position. Against this, without any form of public disclosure, much of the benefit of disclosure as a potential constraint on aggressive large-scale short selling leading to disorderly markets would be lost. In addition, the informational benefits to the wider market of having transparency of information on significant short positions would also be lost. ... On balance, we consider that the benefits of having public disclosure of significant short positions outweigh the costs and that the short selling disclosure regime should be on this basis.” Quoted in McGavin at 236, citing the FSA Discussion Paper at 29.

¹⁹ Regulation (EU) No. 236/2012, available at: <http://eur-lex.europa.eu/legal-content/EN/TXT/?uri=CELEX:32012R0236>; see also “The EU Short Selling Regulation Comes Into Force,” White & Case LLP Client Alert, November 2012, available at: <http://www.whitecase.com/files/Publication/83a9ff70-03f5-46d4-a282-6ee1f2cf7662/Presentation/PublicationAttachment/f2a3c609-c0f9-465a-b5a8-95c38775137e/alert-eu-short-selling-regulation.pdf>

investigate short selling that could create systemic risks, be abusive or create disorderly markets; at the higher threshold, positions should be publicly disclosed to the market in order to provide useful information to other market participants about significant individual short positions in shares.”

We agree. To be meaningful, however, consideration should also be given to the types of instruments and trading activity encompassed by such a disclosure regime. To this end, “short interest” should include all agreements and understandings that allow an investor to profit from a loss in value of the subject security, thereby capturing traditional short sales as well as derivative positions.²⁰ This is consistent with the approach of the E.U. SSR, which provides:

“In order to ensure comprehensive and effective transparency, it is important that the notification requirements cover not only short positions created by trading shares or sovereign debt on trading venues but also short positions created by trading outside trading venues and net short positions created by the use of derivatives, such as options, futures, index-related instruments, contracts for differences and spread bets relating to shares or sovereign debt.”

There has been opposition to these and other proposals and regulations to enhance transparency around short positions. Some argue that disclosure of short positions could act as a coordination device enabling manipulative short sellers to act in concert and facilitating herding behavior. A recent study of the disclosure regime in Europe rebuts this argument, finding no evidence of manipulative short selling or that “these disclosures provide a coordination device for predatory short selling[.] ...[M]ore generally, we find no deleterious unintended consequence associated with the short disclosure regime”²¹

Others including investment funds argue for an alternative proposal that disclosure should be made only to regulators on a confidential basis, if at all.²² The FSA rejected this approach, noting that: “For the sake of completeness we should also note that we see little value in a regime which required disclosure of individual positions to the regulator and then ... publishing aggregate information about those positions. It would only give partial and arguably misleading information about the extent of short positions in individual stocks.”²³

Further, some argue that disclosure would impede investors’ ability to execute short trading strategies and that if disclosure is required, other investors will match their trading positions,

²⁰ See Mirvis, Emmerich and Gogolak at 4, *supra* note 9.

²¹ Jones Reed Waller at 5-6. 33. The FSA also concluded that it had not seen any evidence of coordinated behavior. FSA, FS09/04, “Feedback on DP09/01” October 2009, available at: http://www.centerforfinancialstability.org/forum/fsa_feedback_on_short_selling_limits_200910.pdf

²² Letter from Stuart J. Kaswell, Executive Vice President and General Counsel, Managed Funds Association, to Elizabeth Murphy, Secretary, Securities and Exchange Commission, dated June 22, 2011, available here: <http://www.sec.gov/comments/4-627/4627-137.pdf>

²³ McGavin at 236, citing FSA Discussion Paper at 29.

undermine their strategies, and remove opportunities and incentives to profit that do not benefit the market or participants.²⁴ But for decades, long investors have executed trading strategies notwithstanding Section 13 disclosure obligations. Furthermore, the disclosure regime (or lack thereof) is not intended to grant a license to investors to make money, for example, by trading ahead of undisclosed market moving information regarding short positions.²⁵

The Commission itself, through recent enforcement actions and reported investigations related to Section 13(d), has implicitly acknowledged the inadequacies of the Section 13(d) disclosure regime.²⁶ But to ensure uniform transparency and market integrity, meaningful reform cannot be accomplished through enforcement. The United States long ago determined that investor protection and market integrity merit safeguarding through regulation and disclosure. This history commands that the disclosure regime keep pace with today's rapid fire flow of information, innovations in financial instruments and ever more sophisticated trading strategies. Failure to act will not only reinforce the notion that the market is skewed to the benefit of those with an informational advantage, but will also embolden some investors to continue to operate in the dark and profit at the expense of public shareholders.²⁷

There is no policy or practical reasons to maintain the current disparity and differentiated disclosure regimes in the U.S. for long and short positions. Indeed, the policies that underlie Section 13 disclosure requirements applicable to investors with long positions -- transparency, fairness and efficiency -- apply equally to investments with short positions.²⁸ Dodd-Frank demands the Commission to close this gap in the regulatory disclosure regime and level the playing field. By this Petition, we are asking the Commission to promptly do so by requiring disclosure of net short positions and their economic equivalents on an individualized basis in parity with the required disclosure of long positions, including the timing for such disclosure and when updates are required.

²⁴ See Katz and MacIntosh, *supra* note 6.

²⁵ Wachtell Petition at 7.

²⁶ Securities and Exchange Commission, Press Release, "Corporate Insiders Charged for Failing to Update Disclosures Involving "Going Private" Transactions," March 13, 2015, available at: <http://www.sec.gov/news/pressrelease/2015-47.html>; "SEC Probes Activist Funds Over Whether They Secretly Acted in Concert," *Wall Street Journal*, June 4, 2015, available at: <http://www.wsj.com/articles/sec-probes-activist-funds-over-whether-they-secretly-acted-in-concert-1433451205?KEYWORDS=activist+hedge+funds>

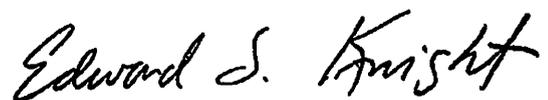
²⁷ See Katz and MacIntosh, *supra* note 6.

²⁸ Such a disclosure requirement should exclude net short positions accumulated in connection with bona fide market making activities, as is the case in the E.U. SSR.

Mr. Brent J. Fields
December 7, 2015
Page 9

If you have any questions, or if we can provide any additional information that would be helpful to the Commission or its staff, please feel free to call me.

Sincerely,

A handwritten signature in black ink that reads "Edward S. Knight". The signature is written in a cursive style with a large, prominent "E" and "K".

Edward S. Knight