

# Senator Ted Kaufman (D-DE) Letter to SEC Chairman Mary Schapiro

**June 25, 2009**

Dear Chairman Schapiro:

We are writing to urge that the Commission consider the establishment of a pilot program to study whether a strict pre-borrow requirement would work effectively to end the problem of naked short selling. Such a pilot program would lead to the collection of data about stock lending and borrowing and the costs and benefits of imposing a pre-borrow requirement on all short sales.

Recently, Senators Carl Levin (D-MI), Charles Grassley (R-IA) and Arlen Specter (D-PA) - in connection with the release of a General Accountability Office study analyzing recent SEC actions to curb naked short selling -- called for the SEC to consider imposing a strict pre-borrow requirement on short sales as the best way of ending abusive short selling. We strongly agree. A pre-borrow requirement would seem to address the problem at its most fundamental level and should be seriously and urgently considered by the SEC as it rethinks its regulations and enforcement approach in this area.

As we have consistently maintained in our communications with the Commission and its Staff, reinstating some form of the "uptick" rule may also be beneficial. We are pleased that the Commission has outlined five options in a proposed rule and will consider comments currently being submitted. We look forward to the Commission moving forward on that front.

Focusing on the uptick rule alone, however, puts too narrow a frame on the problems associated with naked short selling. The problem at its root may be that the current rules against naked short selling are both inadequate and impossible to enforce.

Moreover, the other half of the problem may be that the systems by which stocks currently are loaned and borrowed can and should be greatly improved, leading to greater efficiency and cost savings. For example, centralized systems for loaning and borrowing stocks might better enable the SEC to impose fair rules on stock loans and borrows in connection with short sales as well as enhance the SEC's ability to provide regulatory oversight to prevent naked short selling.

A possible next step would be for the SEC to immediately propose a pre-borrow pilot program because to our knowledge such a requirement has never been formally proposed. As the Commission did with the uptick proposal, the Commission might then immediately hold a Roundtable to discuss the need for fundamental solutions that would address naked short selling, most especially the imposition of a strict pre-borrow requirement and the design and utility of a pre-borrow pilot program.

We urge the Commission to invite a balanced group of commentators including specifically members of the investing public to fully air these issues publicly as the Commission continues its efforts to draft and promulgate additional rules to end naked short selling.