MANAGED FUNDS ASSOCIATION
The Voice of the Global Alternative Investment Industry
WASHINGTON, DC | NEW YORK

October 1, 2009

Via Electronic Mail: rule-comments@sec.gov

Ms. Elizabeth M. Murphy
Secretary
U.S. Securities and Exchange Commission
100 F Street, NE
Washington DC 20549-1090

Re: Amendments to Regulation SHO; File No. S7-08-09

Dear Ms. Murphy:

Managed Funds Association ("MFA")[1] welcomes the opportunity to provide additional comments on the Securities and Exchange Commission's ("Commission" or the "SEC") proposed amendments to Regulation SHO contained in Securities Exchange Act Release No. 59748, 74 FR 18042 (Apr. 20, 2009) (the "Proposal"). This letter supplements our prior comment letter dated June 22, 2009 ("Initial Comment"), which we incorporate by reference and as an attachment, and focuses specifically on the alternative uptick rule.

In MFA's Initial Comment, we underscored our central concerns regarding the Proposal to reinstate a price test:

- First, we believe that liquidity benefits the market, and therefore investors, and that short selling is a legitimate and critical market activity that contributes such liquidity and capital formation, price discovery, and pricing efficiency.

- Second, we recognize that there has been a loss of investor confidence that is more accurately attributed to poor economic fundamentals rather than incorrectly linked to legitimate short selling, which has served as a scapegoat in the public debate. As the SEC's Office of Economic Analysis found, episodes of extreme negative returns last September were not the result of short selling activity, but from selling activity by sellers who own the stock (long sellers).[2]

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[1] MFA is the voice of the global alternative investment industry. Its members are professionals in hedge funds, funds of funds and managed futures funds, as well as industry service providers. Established in 1991, MFA is the primary source of information for policy makers and the media and the leading advocate for sound business practices and industry growth. MFA members include the vast majority of the largest hedge fund groups in the world who manage a substantial portion of the approximately $1.5 trillion invested in absolute return strategies. MFA is headquartered in Washington, D.C., with an office in New York.

[2] Office of Economic Analysis Memorandum from Daniel Aromi and Cecilia Caglio through James Overdahl to Chairman Christopher Cox, dated December 16, 2008, on the analysis of short selling activity during the first weeks of September 2008 (hereinafter "OEA Dec. 16 Memo to Chairman").

- Third, we believe, based on a wide body of empirical data, that a price test will harm markets and investors by causing liquidity to decline and bid-ask spreads to widen, and costs to increase.

- Fourth, we believe that the Commission has taken significant steps through its adoption of several important rules and short selling measures, including Rule 10b-21 (a naked short selling antifraud), Rule 204 (mandating close-out of fails on T+4), and daily publication of aggregate short sale volume in each individual equity security, that have addressed key concerns regarding illegitimate activity. We believe as preliminary data shows that these measures are proving highly effective and that a price test is not needed, nor would it be effective.

- Finally, *if the Commission determines that it must act*, we believe any price test should be triggered by a circuit breaker. By using a circuit breaker, a price test restriction would continue to provide investors the benefits from short selling in all but extreme market conditions. Additionally, we believe a bid test must be used rather than a tick test because the bid represents current market interest and is operationally more sound (given the delay between trades and trade reports). Further, we believe that market centers should implement such price test with a policies and procedures approach (rather than a prohibition) to enforce compliance at the point of execution.

The Alternative Uptick Rule

MFA opposes a price test that would allow short selling only at a price above the current national best bid (the "alternative uptick rule"). In short, we believe that such a test would operate as a near ban on short selling even in non-declining (neutral) markets, and further, that it would lead to unintended consequences and possible gaming, as such a price test has never been utilized in our markets.

First, as discussed in our Initial Comment, the majority of investors that use short selling use it as a risk management or hedging tool. The alternative uptick rule would constrain or limit the applicability of many trading strategies that are market neutral or rely on hedging, including long short equity strategies, convertible securities investors, and the growing number of traditional asset managers deploying hedged strategies such as the 130/30 portfolios. Limiting the ability of market participants that engage in market neutral or hedged strategies to sell securities short would limit their ability to engage in long trades. As such, we are strongly concerned that, initially, the alternative uptick rule would have a massive destabilizing effect on markets as it would cause many market participants to liquidate long positions in order to maintain and balance their market-neutral or hedged portfolios. This would likely have a severe impact on price.

Second, we are concerned the alternative uptick rule would harm investors as we believe it would impose an unreasonable constraint on normal market activity and have a negative impact on market liquidity, bid-ask spreads, stock prices and costs. Take for example, the following situations:

- In stocks with a penny spread, short sellers would be forced to execute at the offer. The alternative uptick rule would thereby impose both an improper surtax on trading to be borne by the short seller and greater delay or no execution for the

buyer. We believe this would deteriorate market efficiency, which would in turn attract fewer orders to such markets.

- Under the alternative uptick rule, market participants selling short would be required to place limit orders as they would be unable to execute marketable short sale orders. The presence of such (short) limit orders could be perceived by buyers as a negative view of a security; as a result, buyers may react by withdrawing their buying interest, thereby exacerbating a downward spiral in price.

Third, we understand that those advocating for the alternative uptick rule have argued that it would be easier and cheaper to implement, operate and enforce. However, ease of implementation is not a sufficient reason or standard in our securities laws for imposing such a dramatic rule change. We note that under Section 3(f) of the Securities Exchange Act of 1934, in considering or determining whether an action is necessary or appropriate in the public interest, the Commission must consider, in addition to the protection of investors, whether the action will promote efficiency, competition, and capital formation. While we do not support a price test, if the Commission determines to adopt a price test, we believe that compliance costs could be minimized through the use of a circuit breaker to trigger a price test, which would limit application of a price test to periods of extreme market conditions. In addition, we believe that implementation concerns would be minimized if executing market centers (or any broker using an intermarket sweep order) surveil for compliance as they could leverage existing architecture developed to comply with the order protection rule in Reg NMS (Rule 611). We note, however, that programming for Reg NMS specifically contemplated the removal of all short sale price tests, and thus, would likely take considerably longer than 2 months to develop. We believe the Commission would need to allow a minimum of 9-12 months for implementation, and the subsequent programming and testing of systems.

Finally, we refer the Commission to our discussion in the Initial Comment regarding a short sale ban that we fear will be analogous to the alternative uptick rule. We have strong concerns with a proposal that is akin to a ban on short selling and believe it would exacerbate market conditions and eliminate key hedging and risk management activities at potentially a very difficult time. Studies on the SEC emergency order prohibiting short selling in financial securities show that the prohibition significantly decreased trading volume and market liquidity, increased bid-ask spreads, increased volatility, decreased market efficiency and led to an estimated $4.9 billion wealth transfer from buyers to sellers. Accordingly, we urge the Commission to not adopt the alternative uptick rule.

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We would be pleased to meet with the Commission or its staff to further discuss our comments. If the staff has questions or comments, please do not hesitate to call Jennifer Han or the undersigned at (202) 367-1140.

Respectfully submitted,

/s/ Stuart J. Kaswell

Stuart J. Kaswell
Executive Vice President, Managing Director
& General Counsel

CC: The Hon. Mary Schapiro, Chairman
The Hon. Kathleen L. Casey, Commissioner
The Hon. Elisse B. Walter, Commissioner
The Hon. Luis A. Aguilar, Commissioner
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