



Journalist Sues SEC to Get Naked Short Selling Files

Lawsuit seeks to tear down SEC's veil of secrecy

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Journalist Mark Mitchell has filed a lawsuit under the Freedom of Information Act against the Securities and Exchange Commission (SEC) to obtain the agency's investigative files relating to more than a dozen aborted investigations and cases involving naked short selling.

In a genuine short sale, the seller borrows stock and delivers it to the buyer. According to a federal court, “‘naked short-selling’ occurs when traders sell shares they do not own or borrow, or ever intend to own, and never deliver the ‘borrowed’ securities that they sell.”¹ The phony short sales introduce phantom or counterfeit stock into the markets, which depresses the price of the genuine stock.

According to the Mitchell complaint, naked short selling has flourished over the past decade because of regulatory loopholes designed by Wall Street and embedded into law by the SEC. The complaint describes the frightening history of naked short selling in the global markets. Although the SEC created a regulation in 2005—Regulation SHO—that was supposed to stop the practice, the SEC’s Enforcement Division rarely enforced the regulation.

Regulators assumed that Reg SHO had contained naked short selling until the financial crisis fully blossomed in 2008. As the stock prices of the nation’s biggest investment banks, such as Lehman Brothers and Morgan Stanley, collapsed, their CEOs claimed that naked short selling—which had flooded the market with counterfeit stock—was to blame. Mitchell's complaint tells how the SEC then frantically issued a half a dozen emergency orders and revisions to Reg SHO in 2008 and 2009 to stop naked short selling.

The SEC has also opened multiple investigations and filed a few administrative cases focusing on naked short selling, but has released little information regarding its findings in those investigations. The few cases which the SEC has filed for naked short selling involve minor market participants or trivial violations by major financial institutions.

The SEC has never made public the results of its investigations of the naked short selling of Bear Stearns, Lehman Brothers, Merrill Lynch, Morgan Stanley or Goldman Sachs, the big banks that collapsed or nearly collapsed during the financial crisis. Mitchell's complaint also points to the massive violations of Reg SHO committed by UBS Securities and Credit Suisse Securities,

¹ *Manning v. Lynch*, 2013 U.S. Dist. LEXIS 38501 (D.N.J. Mar. 18, 2013).

which became public in 2011 when the Financial Industry Regulatory Authority (FINRA) released its settlements with those two banks.

The naked short sales by UBS were “in the tens of millions,” according to FINRA, and had the potential to undermine the integrity of the capital markets. The Credit Suisse violations of Reg SHO were in the same ballpark, with approximately 10 million violations, according to FINRA.

Although the releases of FINRA’s settlements confirmed that hundreds of other market participants were involved in these violations, none were identified. Nor did FINRA identify any of the public companies that were victimized by the naked short selling. Nor did the FINRA identify any executives or employees of the banks that participated in these violations.

The Mitchell complaint seeks the SEC investigative files relating to more than a dozen SEC investigations or filed cases involving naked short selling. This complaint seeks to cut through the veil of secrecy that surrounds naked short selling in US capital markets, and to enable the public to understand just how great a risk this form of market manipulation poses to the US capital markets.

Mitchell is represented by Gary Aguirre, a former Senior Counsel in the SEC’s Enforcement Division. In 2006, Aguirre testified before the Senate Judiciary Committee that naked short selling was one of the types of market abuse plaguing the capital markets that the SEC was ignoring. Mr. Aguirre is being assisted by Hal Wood of Horwood Marcus & Berk Chartered in Chicago.

Mark Mitchell is an investigative journalist who publishes on www.deepcapture.com, a website that has published some of the most in-depth investigative reports on the extent to which naked short selling pervades the US capital markets. The website further documents the SEC's complicity in allowing naked short selling to remain an ongoing threat to the capital markets, through ineffective enforcement of existing rules, through non-prosecution of the worst offenders, and through the basic corruption that results from the “revolving door” that permeates American regulatory circles at the expense of the American public.

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