

Title: Share counterfeiting, DRS, and where we may be heading

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Disclaimer and overarching notes

* I'm not a financial advisor or analyst, everything here is my opinion and not an investment/financial advice. There is no claim of veracity for any statement here

* Unless otherwise stated all data is as-of Oct 06, 2021 and sourced from Yahoo Finance

* Cash collateral for *forever borrow* is estimated to be average price for the day (not considering haircut and other fees or discounts)

* All figures and date are approximate. Emphasis is on directional numbers, not accuracy

Recommended background read

[Short

post](https://www.reddit.com/r/DDintoGME/comments/psonag/followup_elaboration_to_dd_why_direct)

[DD - longer post](https://www.reddit.com/r/DDintoGME/comments/prscya/why_direct_ownership_of_gme_at_computershare_is/)

Terminologies

* Acronyms: **MM** – Market Maker; **BD** – Broker Dealer; **DTCC** – [Casino Operator](<https://www.dtcc.com/about>); **SHFs** – [Short Hedge Funds and their BFFs](<https://www.investopedia.com/terms/h/hedgefund.asp>)

* **Shorting** = selling by borrowing from someone else's `inventory` by paying interest

* **Short sale** = selling by MM, where inventory is to be `located` *later* (sell now, locate later)

* MMs have multiple settlement dates to locate share. Such shares in limbo are referred to as fail-to-deliver (FTD)

* When MMs fail to locate eventually (T+X days), they are forced to close out FTD [sauce: Regsho](<https://www.sec.gov/investor/pubs/regsho.htm>)

* But thanks to continuous net settlement (CNS) and supporting services designed by DTCC/NSCC, there are tricks to kick the FTD can using `forever borrowing` called [SFT

service](<https://dtcclearing.com/products-and-services/equities-clearing/sft-clearing.html#tab-about>) and `forever hiding` called [obligation

warehouse](<https://www.dtcc.com/clearing-services/equities-clearing-services/ow>)

* **Short interest (SI)** = total shares that are legitimately shorted i.e. sold with `requirement` to be bought back when lender asks

* **Naked shorting** *aka* **Counterfeit share** = selling by market maker with no intention of locating (*aka* strategic fails)

* **Synthetic shares** are created by MMs for hedging when trading Options. Technically synthetics should go *poof* after options expiry date. Shares that continue to exist beyond expiration date are counterfeit

Difference between shorting and counterfeiting (naked shorting)

* It's important to note that ***legitimate shorting*** involves borrowing from whoever has inventory, by paying interest rate and posting a % of share value as margin cover

- * For e.g. when you *short* on broker platform, they may demand 30%, 100%, or 120% margin to lend shares based on volatility risk. In many instances `hard to borrow (HTB)` stocks are not even lent out for borrowing
- * ***Counterfeiting*** involves DTCC market participants (broker dealers, hedge funds, prime brokers) ***forever borrowing*** from ***inventory pools*** that gets shuffled around to obfuscate transparency and accountability
- * Counterfeiting costs the full price of share plus additional fees, so it is an expensive way to (illegally) shortsell
- * Melvin Capital lost control in Jan because they were legitimately shorting, and were shuffling FTDs using synthetic shares created via [Options](https://www.investopedia.com/options-basics-tutorial-4583012)
- * When Point72 and Shitadel injected billions of dollars to Melvin and "took control" of the situation, they resorted to the more expensive ***counterfeiting*** solution to dilute shares
- * This exploded the shares available to trade (share dilution) and depressed price
- * However, counterfeiting shares brings its own problems when a decisive victory is not achieved (i.e. majority paperhanding), as explored below

Shares available for trading (the float)

- * Total float (GME^(DTC) shares available to trade) is 61.8M
- * Of which 30.5M are held by institutions and funds
- * Remaining 31.3M are available for retail traders

[Sauce: Yahoo Finance](https://preview.redd.it/u2x0r8t3b7r71.jpg?width=1109&format=jpg&auto=webp&s=20f2cff5c0e397a6c4b15f013c1b76616955e773)

- * Estimated counterfeit shares are 142.8M
- * This puts the real float for trading GME^(DTC) at 204.6M
- * MMs injected heavy liquidity (63.9M net short sales) in Feb/Mar to "stabilize" prices
- * From April onwards avg. of 3.7M shares were being "added" (read counterfeited) monthly to "stabilize" (read suppress) the price

[SI as of JAN, 2 – Net Short Sales FEB thru SEP](https://preview.redd.it/2uw3za21b7r71.jpg?width=1479&format=jpg&auto=webp&s=266786007cdf3f327534b3b30333dcb9839f3319)

Sauces: [1 Forbes Article](https://www.forbes.com/sites/georgecalhoun/2021/03/19/gamestop-were-the-short-sellers-routed-does-it-matter-beware-the-gamma/), [2 FINRA Short Volume Data](https://www.finra.org/finra-data/browse-catalog/short-sale-volume-data)

- * This does not account for BDs/MMs maliciously marking short sales as long – for which some have been caught and fined in the past. Some violations are listed in this [Naked Short Selling article](https://oilprice.com/Energy/Energy-General/Naked-Short-Selling-The-Truth-Is-Much-Worse-Than-You-Have-Been-Told.html)

Impact of share dilution on borrow collateral and real float size

- * The initial float size issued by DTCC GME^(DTC) is the same as GME^(GME) held under Cede & Co.'s name at Computershare
- * Counterfeiting adds to this float, however it comes at a cost. Every share ***borrowed forever*** (counterfeited) [locks-up cash collateral](https://dtcclearing.com/products-and-services/settlement/settlement-services/collateral-loans.html) roughly equal to the current share price
- * This borrow collateral is repriced daily (marked-to-market) as share price goes up/down
- * Based on ~143M counterfeits, real float is approximately 3.5x official float (~200M)
- * There are various methods and efforts put into calculating the real float, but we'll go with 3.5x for this post as it aligns with Jan SI and short volume data from FINRA. This *multiple* has several implications:

- * ~\$26B capital is likely locked-up as collateral for ***forever borrowing*** using \$170 average price
- * This is mostly financed by prime brokers (big banks), and not all ponied up by SHFs
- * As of Oct 6th, every \$1 share price move results in \$155M change to collateral need
- * In other words, \$6.5 price increase in GME price, necessitates \$1B additional collateral; On the flip side a \$6.5 price decrease reduces collateral need by \$1B

[3.5x float multiple in red is probable based on Jan SIVFINRA short sale volume](<https://preview.redd.it/60282k16b7r71.jpg?width=1090&format=pjpg&auto=webp&s=e558995ab450b1cfd945dc6c332f60362b90c15e>)

- * As real float increases, not only does it increase the risk of seller having to buy back at a potentially higher price, but also the collateral multiples
- * For e.g. when MMs add 3.7M shares to real float in a month, a \$5 price increase forces \$18.5M additional collateral to be locked-up

Forever (re)borrow creates chain of fakes based on original

- * Since the net short position of SHFs/MMs are multiple times the float, we can safely assume that almost every lend-able share has been be lent
- * When GME^(DTC) is sold short, the buyer gets GME^(DTC-fake1); when this share is lent again it becomes GME^(DTC-fake2); and so on
- * The buyer has no idea that it's fake because they **bought it** by paying real money, so they are entitled to sell as they wish, which creates the next fake share
- * So, this results in a chain of fake shares starting from the original GME^(DTC) share. Only DTCC and perhaps BDs have visibility to this
- * Per [SEC 15c3-3 Customer protection rules](<https://www.law.cornell.edu/cfr/text/17/240.15c3-3>), BDs are prevented from lending shares from Customer cash accounts. However, DTCC has [CNS gimmick](<https://www.dtcc.com/clearing-services/equities-clearing-services/the-fully-paid-for-account>) to temporarily change sub-account type* and borrow from BD inventory, including customer assets, to satisfy `fully-paid-for location services` when asked by institutional investors. From [DTCC site](<https://www.dtcc.com/clearing-services/equities-clearing-services/the-fully-paid-for-account>)

>Members instruct NSCC to move their expected long allocations from the general CNS "A" subaccount into a fully-paid-for location (the "E" subaccount) and are then permitted to use customer fully-paid-for positions to complete institutional deliveries in DTC.

Impact of DRS on share borrow and collateral

- * When a GME^(GME) share is transferred from DTCC to Computershare, DTCC has to retire the original GME^(DTC) and move the full chain of fake shares created based on it
- * GME^(DTC-fake1), GME^(DTC-fake2), GME^(DTC-fake3) now have to be attached to another chain of fake shares tied to real GME^(DTC)
- * I'm using the words chain and attached figuratively. Not sure how DTCC technically handles it, but one can imagine it being convoluted set of transactions and accounting

[When GME^(GME) is moved from DTCC to CS, GME^(DTC) has to be retired](<https://preview.redd.it/5b4f7zhbb7r71.png?width=1166&format=png&auto=webp&s=ffa0b177accc0bdf8ea66673f30ea820261733e5>)

So, moving shares from DTCC to Computershare **does not** reduce collateral burden because collaterals are only posted for counterfeit shares that are never transferred

- * It may however increase the collateral, because the first *forever borrowed* GME^(DTC-fake1) \- have

used lower margin (legitimate short), but it now requires full collateral (naked short)

Impact of counterfeiting, and DRS on price

- * SHFs/MMs have the tiger by its tail

- * ****If they stop counterfeiting shares****, then bid-ask spread widens and bid depth plummets pushing price up – in turn forcing MM's to hedge calls, which in turn increases price – a classic ****gamma squeeze like in Jan****

- * ****If they continue counterfeiting shares****, they'll need to ****post more collateral to the tune of ~\$600M/month**** (assuming 3.6M new counterfeits/month to suppress price @ \$170)

- * There's only so much collateral they can raise, so they'll resort to further price suppression by more counterfeiting (\$1 price drop saves ~\$155M collateral / month)

- * Every \$1 price drop requires selling ****X**** counterfeit shares, which in turn requires more collateral ... till they ****spiral down**** to a point where they can't keep up with collateral requirement

- * The amount of counterfeit shares required to drop price by \$1 is hard to estimate as it depends on market conditions. It's easier to drop price on red days than green (ETF buy/sell pressure, institutional money flow, etc.)

- * ****Ongoing collateral**** for this `tightrope walking act` is exactly the ****reason they need PFOF, freedom to pump-and-dump OTC pink sheets**** and crypto

- * Every share DRS-ed ***may*** be putting additional collateral pressure, but is hard to guess without knowing historical borrow rates

- * A ****BIG unknown**** with DRS-ing is ****if DTCC/NSCC at some point conclude that the chain of fake shares is too long and too risky**** and needs more collateral to mitigate risk – this is a real issue they have to address sooner than later

Concluding thoughts

- * ****DRS/direct buy from Computershare, is still and perhaps the only way to expose share counterfeiting****

- * Keeping shares in the DTCC casino under street name, gives them free hand to create new rules/tricks to depress price and satisfy regulatory reporting. This is because some of the big gamblers actually own the casino

- * As buying pressure stays, and Gamestop works toward pivoting the company, ****SHFs default on ongoing collateral requirement will be the choke point****

- * There is also the possibility that largest group of retail share *****hodlers***** can demand share recall directly or through Gamestop to protect unrestricted share price dilution by SHFs/DTCC

- * ****Till then, there will be a constant fight to keep the price low****, especially as real float gets bigger – tasty discounts

- * There will be a lot of PR/misdirection/media FUD to once again have majority of Apes paperhand because something else is better, and/or Gamestop hype is over

- * The ****best reaction a long term investor can have is to ignore sensational news/provocations and keep most of their shares directly registered in their name**** at Computershare, and some in brokerage to sell

****EDIT****: Some concerns on amount to DRS. Without being specific and without giving advice, more the better, especially for larger positions. Every share counts. But also remember selling from brokerage during squeeze gives less ammo for SHFs.