Twitter Thread by Robinhood Customer Relations

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THREAD: COUNTERFEIT STOCKS

There are four major players in the industry: Hedge funds, prime brokers, the DTCC, and the SEC.

Hedge funds and the SEC you know of, but the DTCC and prime brokers are important.

Prime brokers are relatively simple - they're brokers that can clear their own transactions by way of moving actual shares between their clients.

The big prime brokers are ones you've heard of - Goldman Sachs, Morgan Stanley, Bear Stearns, Citigroup, etc. - big, big companies.

These prime brokers in turn collectively own the Depository Trust Clearing Corp - DTCC.

The DTCC is an almost impenetrable, behemoth corporation that clears near a billion shares a day and accounts for a vast majority of the clearing house activity in the US market. This is the corporation that ACTUALLY holds physical shares - all your "shares" are on their books

The DTCC is (this will be important later) nearly impossible to get information out of, and it takes an act of Congress or a subpoena to get them to talk on anything.

So onto the big ticket - naked shorting. Hedge funds REALLY like shorting stocks. So much so that they, by way of bad market structure, can create "new" shares through the "float" - the gap between when they sell you a share and they actually deliver on it.

Anyone in the market legally has three days to deliver on a sale of a stock, else it gets marked as a "Fail to Deliver". In the case of a short, this means that a hedge fund has to borrow a share to then sell and deliver to the buyer.

Problem is, for big players, you don’t have to actually borrow the share before you sell it. This is called a “naked” short - you sell the stock, then find someone to borrow a share from within the three day settlement period.

So within those three days, you’re basically playing with the house’s money.

And the hedge funds *really* like playing with the house’s money.

So how do you get more?

You extend the period.

The thing is, nobody ever checks up on Failures to Deliver. A hedge fund can have an FTD, but the sale goes through as normal and the buyer is treated as having an actual share - without the fund having sold one.

Now the SEC doesn’t like stocks having too many FTDs, so funds go a step further.

Stocks owned in margin accounts are not only immediately loaned out, but are also treated like complete, whole shares as soon as the sale goes through. So watch this:

Hedge fund naked shorts a stock.
Buyer in margin account buys said sale.
Stock lands in margin account, is put into loan pool.

Hedge fund borrows back the “share” they just sold to the account, and the books are balanced.

Congrats. You’ve made a share appear out of thin air. However, you can only do this so many times - there are so many margin accounts.

Well, hedge funds pay massive fees to brokers, and as part of that deal, brokers change normal accounts into margin accounts all the time.

What else can you do?

Well, funds also like to have a massive position in naked shorts that they, before the timer is up, sell to an offshore account - resetting the timer.

And they can chain this through dozens of accounts, taking advantage of massive amounts of float.

Basically, by way of naked shorting and creative misuse of the T+3 SEC rule, big hedge funds can make short positions in stocks appear out of nowhere, with no starting capital and no physical shares in hand.

This puts massive downward pressure on targeted stock prices, and if a large amount of funds get in on it together, they can drive a company into bankruptcy for a pittance and pocket MASSIVE amounts of money.

This is why Robinhood’s been having liquidity issues - there literally aren’t any more “real” shares of $GME out on the market

IF YOU DO NOT OWN THE CERTIFICATE IT IS NOT YOUR STOCK

Even better comparison: This is like check kiting, with the entire economy.