

[Securities Regulation Daily Wrap Up, TOP STORY—S.D.N.Y.: Robinhood faces Congressional ire, shareholder suit as ‘Reddit trolls’ squeeze hedge funds over GameStop shorts, \(Jan. 28, 2021\)](#)

Securities Regulation Daily Wrap Up

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As the SEC blandly stated it was "actively monitoring" the situation, Democratic members of Congress called for an investigation into Robinhood's stoppage of purchases of GameStop shares to allegedly benefit Wall Street.

Several members of Congress have called for an investigation and possible regulatory action in the wake of an online "Reddit revolution" that has spurred a wave of purchases of shares of GameStop Corporation by retail investors hoping to profit from the shares' rise while also punishing hedge funds for selling the stock short. Senator Elizabeth Warren (D-Mass) and Reps. Alexandria Ocasio-Cortez (D-NY) and Rashida Tlaib (D-Mich) each made reference to hedge funds using the stock market as a "casino," while Ocasio-Cortez and Tlaib sharply criticized Robinhood Financial for halting new purchases of GameStop stock, suggesting that the pioneering no-fee brokerage was acting to protect the interests of Wall Street at the expense of small investors. Meanwhile, Robinhood was hit with a class action complaint in the Southern District of New York for allegedly using the GameStop trading halt to manipulate the market on behalf of hedge funds ([Nelson. v. Robinhood Financial LLC](#), January 28, 2021).

Shares of GameStop had risen dramatically from a close of \$18.84 on December 31 to a high of \$482.85 on January 27, fueled by calls on Reddit's "Wall Street Bets" online forum for retail traders to squeeze hedge fund Melvin Capital for taking an allegedly 100 percent short position in GameStop stock. In a carefully worded, one-sentence [public statement](#), the SEC said that it was "actively monitoring the on-going market volatility in the options and equities markets" and "working with our fellow regulators to assess the situation and review the activities of regulated entities, financial intermediaries, and other market participants."

Wall Street as "personal casino." Senator Warren was far less measured in her response, blasting hedge funds and other institutional players for gambling profitably in the equity markets to the detriment of Main Street. "With stocks soaring while millions are out of work and struggling to pay bills, it's not news that the stock market doesn't reflect our actual economy," Warren said in a [news release](#). "For years, the same hedge funds, private equity firms, and wealthy investors dismayed by the GameStop trades have treated the stock market like their own personal casino while everyone else pays the price. It's long past time for the SEC and other financial regulators to wake up and do their jobs - and with a new administration and Democrats running Congress, I intend to make sure they do."

On Twitter, Tlaib lambasted Robinhood for instituting the trading halt in the name of protecting investors, saying that the House Financial Services Committee needs to look into the matter. "This is beyond absurd," she [tweeted](#). "@FSCDems need to have a hearing on Robinhood's market manipulation. They're blocking the ability to trade to protect Wall St. hedge funds, stealing millions of dollars from their users to protect people who've used the stock market as a casino for decades."

Ocasio-Cortez echoed Tlaib's criticisms [tweeting](#) that she would support a hearing by the Financial Services Committee, if necessary. She [added](#) that "[i]nquiries into freezes should not be limited solely to Robinhood" and that "Committee investigators should examine any retail services freezing stock purchases in the course of potential investigations - especially those allowing sales, but freezing purchases." to which Tesla founder and CEO Elon Musk, whose firm was reportedly a previous target of Melvin Capital's short-selling strategy, replied "[Absolutely](#)."

Ocasio-Cortez's comments also appeared to reflect some of the popular discontent expressed online against members of the securities industry who had spoken publicly in the media and online against the Redditors' trading crusade on behalf of GameStop. "Gotta admit it's really something to see Wall Streeters with a long history of treating our economy as a casino complain about a message board of posters also treating the market as a casino," she [tweeted](#).

Robinhood had attempted to explain the halt on GameStop purchases in a [blog post](#) titled "Keeping Customers Informed Through Market Volatility." Claiming that "Our mission at Robinhood is to democratize finance for all," the firm stated that it was "restricting transactions for certain securities to position closing only." The named securities included not only shares of GameStop but also AMC Entertainment Holdings Inc. and BlackBerry Ltd., among others. The shares of the latter two firms have also been suspected of being heavy targets of short selling by hedge funds.

The chief of the Massachusetts Securities Division, Secretary of the Commonwealth William Galvin, had publicly supported a 30-day trading ban on GameStop shares. In an [interview on CNBC](#) on January 27, Galvin stated that current trading activity in GameStop shares represented a risk to "unsophisticated investors." Galvin suggested that the coronavirus pandemic has resulted in many individuals getting into day trading who "really have no idea exactly what they're doing." In addition, Galvin believes that the current situation represents a risk to the broader market, reflecting a systemic structural issue in the equity markets that results when there is excess short interest in a stock beyond the issuance of shares. "That has to be addressed immediately," Galvin said.

Robinhood suit. In a putative class action complaint filed in federal court in Manhattan, a Robinhood shareholder claims that the broker-dealer has, among other things, breached its customer agreements and its fiduciary duties by unlawfully depriving shareholders of earnings opportunities in GameStop stock. The complaint alleges that despite having a mantra of "Let the people trade," Robinhood has pulled the securities of GameStop and other companies from its app for no legitimate reason, preventing retail investors from buying or even searching for the stocks on Robinhood's platform. According to the complaint, "Robinhood is pulling securities like GME [GameStop] from its platform in order to slow growth and help benefit individuals and institutions who are not Robinhood customers but are Robinhood large institutional investors or potential investors." The complaint also alleges that Robinhood has breached its best execution obligations under FINRA Rule 5310 by outright blocking customers from trading a security, causing substantial losses to customers due to Robinhood's own negligence and failure to maintain adequate infrastructure.

The case is [No. 21-cv-777](#).

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Companies: Robinhood Financial LLC; Robinhood Securities, LLC; Robinhood Markets, Inc.

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