SEC Issues New Rules to Protect Investors Against Naked Short Selling Abuses

FOR IMMEDIATE RELEASE
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Washington, D.C., Sept. 17, 2008 — The Securities and Exchange Commission today took several coordinated actions to strengthen investor protections against "naked" short selling. The Commission's actions will apply to the securities of all public companies, including all companies in the financial sector. The actions are effective at 12:01 a.m. ET on Thursday, Sept. 18, 2008.

"These several actions today make it crystal clear that the SEC has zero tolerance for abusive naked short selling," said SEC Chairman Christopher Cox. "The Enforcement Division, the Office of Compliance Inspections and Examinations, and the Division of Trading and Markets will now have these weapons in their arsenal in their continuing battle to stop unlawful manipulation."

In an ordinary short sale, the short seller borrows a stock and sells it, with the understanding that the loan must be repaid by buying the stock in the market (hopefully at a lower price). But in an abusive naked short transaction, the seller doesn't actually borrow the stock, and fails to deliver it to the buyer. For this reason, naked shorting can allow manipulators to force prices down far lower than would be possible in legitimate short-selling conditions.

Today's Commission actions, which are the result of rulemaking under the Administrative Procedure Act, go beyond its previously issued emergency order, which was limited to the securities of financial firms with access to the Federal Reserve's Primary Dealer Credit Facility. Because the agency's exercise of its emergency authority is limited to 30 days, the previous order under Section 12(k)(2) of the Securities Exchange Act of 1934 expired on Aug. 12, 2008.

The Commission's actions were as follows:

Hard T+3 Close-Out Requirement; Penalties for Violation Include Prohibition of Further Short Sales, Mandatory Pre-Borrow

The Commission adopted, on an interim final basis, a new rule requiring that short sellers and their broker-dealers deliver securities by the close of business on the settlement date (three days after the sale transaction date, or T+3) and imposing penalties for failure to do so.

If a short sale violates this close-out requirement, then any broker-dealer acting on the short seller's behalf will be prohibited from further short sales in the same security unless the shares are not only located but also pre-borrowed. The prohibition on the broker-dealer's activity applies not only to short sales for the particular naked short seller, but to all short sales for any customer.

Although the rule will be effective immediately, the Commission is seeking comment during a period of 30 days on all aspects of the rule. The Commission expects to follow further rulemaking procedures at the expiration of the comment period.

Exception for Options Market Makers from Short Selling Close-Out Provisions in Reg SHO Repealed

The Commission approved a final rule to eliminate the options market maker exception from the close-out requirement of Rule 203(b)(3) in Regulation SHO. This rule change also becomes effective at 12:01 a.m. ET on Thursday, Sept. 18, 2008.

As a result, options market makers will be treated in the same way as all other market participants, and required to abide by the hard T+3 closeout requirements that effectively ban naked short selling.

Rule 10b-21 Short Selling Anti-Fraud Rule

The Commission adopted Rule 10b-21, which expressly targets fraudulent short selling transactions. The new rule covers short sellers who deceive broker-dealers or any other market participants. Specifically, the new rule makes clear that those who lie about their intention or ability to deliver securities in time for settlement are violating the law when they fail to deliver. This rule also becomes effective at 12:01 a.m. ET on Thursday.

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http://www.sec.gov/news/press/2008/2008-204.htm
