

industry, these commenters believe, has achieved success in significantly reducing risk in the trading markets and in enhancing processing efficiencies within the securities infrastructure supporting book-entry clearance and settlement. In their view, much of the success can be attributed to immobilizing stock certificates and mandating book-entry settlement among financial institutions and their financial intermediaries. Accordingly, many of the commenters claimed that a move to certificated securities is a step backwards in the development of the modern securities processing system and will hinder the industry's efforts to reduce risk, cost, and inefficiencies for all parties involved in securities transactions.²⁹

Fourteen commenters specifically raised concerns that an increase in the use of certificates will raise costs and cause significant inconveniences for investors.³⁰ They believe that increased costs associated with transfers, lost certificates, custody, and trading delays will ultimately be borne by investors. One commenter stated that the withdrawal from DTC might require customer securities to be held in the broker's vault in order to meet the customers' needs and will increase costs associated with transactions, including transfer costs, which are currently ranging from \$50.00 to \$100.00 per certificate.³¹ This commenter claims that these costs are hard to justify to

shareholders when the shareholder did not request a certificate.

Ten commenters contended that operating outside the DTC environment would undermine the ability of broker-dealers to effectively complete transactions on behalf of their customers.³² Forced withdrawals of customer positions held in street name would prevent shareholders from fully participating in services provided by their broker, such as margin accounts, automated dividend payments or reinvestments, asset management, proxy services, account transfers, and prompt processing of corporate actions (particularly where old securities need to be exchanged for new securities as required, for example, in mergers and tender offers). Seven of the ten commenters also indicated that such an action would result in an increase in trading delays and trade failures, which would increase risk in the system.³³

Three commenters believe that the final decision regarding custody and registration should reside with the beneficial owners or their appointed agents and not with the issuers of such securities.³⁴ These commenters objected to imposing registration restrictions on beneficial owners, because such registration restrictions would be disruptive to market practices, would impose costs on investors, and would cause inefficiencies in the market. Further, nine commenters noted that the direct registration system ("DRS")³⁵ was specifically designed by the industry to give shareholders an alternative to either holding a certificate or holding in street name registration.³⁶ Several commenters pointed to AT&T's decision to dematerialize its securities as further support of the industry's initiatives to dematerialize.³⁷

Four commenters stated they believe DTC's proposed rule change complies with its obligation under section 17A of the Act to promote the prompt and accurate settlement of securities transactions.³⁸ In fact, one of these commenters stated that honoring issuers' request to withdraw from DTC was inconsistent with section 17A.³⁹ One commenter expressed surprise that DTC's filing on this issue was necessary because of the ability of an owner of a negotiable security to register the securities in whatever name it wished has existed for a long time under the Uniform Commercial Code and therefore should not be restricted by the issuer.⁴⁰

With regard to the naked short selling issue, one commenter indicated that the withdrawal of securities from DTC would not have any material or effective impact on the short selling concerns of issuers.⁴¹ Another contended that short selling is vital to ensuring the asset price reflects the underlying fundamentals of the asset and thereby facilitates a more efficient market.⁴² This commenter noted that as a result of the additional costs and trade delays associated with certificate-only securities, some brokers are refusing to conduct trades in issues that have been withdrawn from DTC, which has resulted in an illiquid market for those securities.

C. DTC's Response Letter to Opposing Comment Letters

DTC emphasizes in its response letter that the proposed rule change does not constitute a departure from DTC's existing rules and procedures approved by the Commission. Those rules, DTC contends, govern requests to make shares eligible and enable participants to withdraw shares on behalf of themselves or their customers from the DTC system through DTC's withdrawal-by-transfer mechanism.⁴³

Further, DTC states that issuers do not have continuing ownership rights in shares they have sold into the marketplace and therefore cannot control the disposition of shares already registered in DTC's nominee name by directing that those shares be surrendered to the transfer agent or by restricting their eligibility for book-entry

block" to achieving STP or shorter settlement cycles.

²⁹ Letters from A.G. Edwards & Sons, Inc., Ameritrade, Inc., Banc of America Securities LLC, Bank Depository User Group, BNY Clearing, Cashiers' Association of Wall Street, Inc., Citibank North America, Inc., Edward Jones, Ingalls & Snyder LLC, ING Financial Markets LLC, JP Morgan Securities, Inc., Merrill Lynch, Mizuho Trust & Banking Co. (USA), Morgan Stanley, National City Bank, National Financial Services LLC, National Investor Services Corp., Pershing LLC, Prudential Securities Incorporated, John Rideout, Salomon Smith Barney, Securities Industry Association, Securities Industry Association Customer Account Transfer Division, Spear, Leeds & Kellogg, State Street Corporation, Stearns Securities Corp., Sterne, Agee & Leach, Inc., Union Planters Trust & Investment Group, and USB Warburg LLC.

³⁰ Letters from Ameritrade, Inc., Mark Cashion, Citibank North America, Inc., First Clearing Corporation, Merrill Lynch, Mizuho Trust & Banking Co. (USA), National Investor Services Corp., Pershing LLC, RBC Dain Rauscher, John Rideout, Salomon Smith Barney, Securities Industry Association Customer Account Transfer Division, Stearns Securities Corp., and Union Planters Trust & Investment Group.

³¹ Letter from Raymond James and Associates. According to this comment letter, Raymond James recently initiated a client certificate transfer fee as a disincentive to requesting a certificate. This fee, the commenter claims, has reduced certificate requests by 67% over the past two years.

³² Letters from Ameritrade, Inc., BNY Clearing, Mark Cashion, First Clearing Corporation, Mizuho Trust & Banking Co. (USA), National City Bank, National Investor Services Corp., RBC Dain Rauscher, John Rideout, and Union Planters Trust & Investment Group.

³³ Letters from Ameritrade, Inc., BNY Clearing, Mizuho Trust & Banking Co. (USA), National City Bank, First Clearing Corporation, RBC Dain Rauscher, and Union Planters Trust & Investment Group.

³⁴ Letters from First Clearing Corporation, Mizuho Trust & Banking Co. (USA), and John Rideout.

³⁵ DRS allows a shareholder to hold a book-entry position in his or her own name on the books of the issuer. As a result, shareholders can enjoy the benefits of both holding their securities in a book-entry system and being a "named" shareholder on the issuer's record.

³⁶ Letters from Banc of America Securities LLC, Edward Jones, Merrill Lynch, Pershing LLC, Prudential Securities Incorporated, RBC Dain Rauscher, Securities Industry Association Customer Account Transfer Division, Stearns Securities Corp., and Sterne, Agee & Leach, Inc.

³⁷ Letters from Edward Jones, Pershing LLC, RBC Dain Rauscher, and Stearns Securities Corp.

³⁸ Letters from A.G. Edwards & Sons, Inc., Banc of America Securities LLC, Prudential Securities Incorporated, and Securities Industry Association Customer Account Transfer Division.

³⁹ Letter from Prudential Securities Incorporated.

⁴⁰ Letter from A.G. Edwards & Sons, Inc.

⁴¹ Letter from Citibank North America, Inc.

⁴² Letter from John Rideout.

⁴³ See e.g. Rules 2, 6, and 9 of DTC's Rules.