

SECURITIES AND EXCHANGE COMMISSION

17 CFR Parts 240 and 242

[Release No. 34-48709; File No. S7-23-03]

RIN 3235-AJ00

Short Sales

AGENCY: Securities and Exchange Commission.

ACTION: Proposed rule.

SUMMARY: The Securities and Exchange Commission (Commission) is publishing for public comment new Regulation SHO, under the Securities Exchange Act of 1934 (Exchange Act), which would replace Rules 3b-3, 10a-1, and 10a-2. The Commission is also proposing amendments to Rule 105 of Regulation M. Proposed Regulation SHO would, among other things, require short sellers in all equity securities to locate securities to borrow before selling, and would also impose strict delivery requirements on securities where many sellers have failed to deliver the securities. In part, this action is designed to address the problem of “naked” short selling. Proposed Regulation SHO would also institute a new uniform bid test allowing short sales to be effected at a price one cent above the consolidated best bid. This test would apply to all exchange-listed securities and Nasdaq National Market System Securities (NMS Securities), wherever traded.

We are also seeking comment on a temporary rule that would suspend the operation of the proposed bid test for specified liquid securities during a two-year pilot period. The temporary suspension would allow the Commission to study the effects of relatively unrestricted short selling on market volatility, price efficiency, and liquidity.

DATES: Comments must be received on or before January 5, 2004.

ADDRESSES: To help us process and review your comments more efficiently, comments should be sent by hard copy or e-mail, but not by both methods. Comments sent by hard copy should be submitted in triplicate to Jonathan G. Katz, Secretary, Securities and Exchange Commission, 450 Fifth Street, NW., Washington, DC 20549-0609. Comments also may be submitted electronically at the following E-mail address: rule-comments@sec.gov. All comment letters should refer to File No. S7-23-03. Comments submitted by E-mail should include this file number in the subject line. Comment letters received will be available for public

inspection and copying in the Commission's Public Reference Room, 450 Fifth Street, NW., Washington, DC 20549. Electronically submitted comment letters will be posted on the Commission's Internet Web site (<http://www.sec.gov>).¹

FOR FURTHER INFORMATION CONTACT: Any of the following attorneys in the Office of Trading Practices, Division of Market Regulation, Securities and Exchange Commission, 450 Fifth Street, NW., Washington, DC 20549-1001, at (202) 942-0772: James Brigagliano, Assistant Director, or Gregory Dumark, Kevin Campion, Lillian Hagen, Elizabeth Sandoe and Marla Chidsey, Special Counsels.

SUPPLEMENTARY INFORMATION: The Commission is publishing for comment proposed Regulation SHO and a proposed temporary rule, Rule 202², and proposed amendments to Regulation M, Rule 105³ under the Exchange Act.

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¹ Personal identifying information, such as names or e-mail addresses, will not be edited from electronic submission. Submit only information that you wish to make publicly available.

² 17 CFR 242.202.

³ 17 CFR 242.105.

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I. Introduction

Congress, in 1934, directed the Commission to “purge the market” of short selling abuses, and in response, the Commission adopted restrictions that have remained essentially unchanged for over 60 years. Originally adopted in 1938, the Commission's short sale rule, Rule 10a-1, is designed to restrict short sellers from effecting short sales in an exchange-traded security when the price of that security is declining.⁴

Since its adoption, the Commission has engaged in studies, investigations, and reviews of the efficacy of the Rule.⁵

⁴ 17 CFR 240.10a-1.

⁵ See 2 Securities and Exchange Commission, Report of Special Study of Securities Markets, H.R. Doc. No. 95, 88th Cong., 1st Sess. 247 (1963) (study to determine the relationships between changes in short positions and subsequent price trends); see also Short-Selling Activity in the Stock Market: Market Effects and the Need for Regulation (Part I)(House Report), H.R., Rep. No. 102-414 (1991), reprinted in CCH Federal Securities Law Reports Number 1483 Part II (1992).