

“naked short selling” in these thinly-capitalized securities trading over-the-counter. The proposed locate and delivery requirements would address some of these concerns. There may be costs associated with implementing these borrowing requirements for OTCBB and Pink Sheets securities. The Commission requests comment on the costs of implementing these requirements, as well as costs associated with ongoing compliance and surveillance associated with this proposal. The Commission is also concerned with the impact this proposal may have on small issuers. Please provide data to quantify the costs to small issuers and potential investors in these small issuers, including whether reduced short selling opportunities may make the securities in these markets more susceptible to having overvalued stock prices. In addition, we request comment on the extent to which the recommended proposals may affect the ability of small issuers to secure financing through the issuance of convertible debentures. Please describe and analyze any other costs associated with this proposal.

The Commission also recognizes that there may be costs to market participants in implementing and complying with the proposed additional delivery requirements targeted at securities with substantial settlement failures. The Commission seeks estimates and views regarding these costs for particular types of market participants, as well as any other costs or benefits that may result from adoption of the proposal.

The Commission is not proposing any exception from the proposed additional delivery requirements for shorts sales in connection with bona-fide market making because we believe that extended fails to deliver appear characteristic of an investment or trading strategy, rather than one related to market making. The Commission believes that there may be costs to market makers that have open extended fail positions. We have requested comment on the need for market makers engaging in bona-fide market making to maintain extended fail positions. Please provide information detailing any costs that may be associated with not providing a market maker exception to the proposed additional delivery requirements. In particular, we request comment on any lost trading or business opportunity costs to market makers, any potential impact on investors, and a detailed description of any such costs.

In general, the Commission acknowledges that the proposed additional delivery requirements may

bring about new costs for market participants. The Commission requests data to quantify the costs identified. Broker-dealers, market makers, SROs, and clearance and settlement firms may incur costs in making initial system changes necessary to implement these new requirements, as well as maintain ongoing compliance and surveillance mechanisms. We request specific comment on the system changes to computer hardware and software, or surveillance costs necessary to implement this rule. If this rule requires additional labor, please indicate what type of jobs are affected, how many additional hours are required and the approximate costs of these additional hours.

C. Proposed Rule 202(T): Temporary Short Sale Rule Suspension

1. Benefits

The proposed pilot program would suspend the operation of the proposed bid test provision for selected stocks that the Commission believes are less susceptible to manipulation because they are more liquid and have a high market capitalization. The proposed pilot program is intended to provide the Commission with empirical data to assess whether the proposed bid test should be removed for liquid securities. The empirical data collected would enable the Commission to study the effects of deregulated short selling on, among other things, market volatility, price efficiency, and liquidity. The proposed pilot program would assist the Commission in determining if, and to what extent, a price test inhibits the markets. The data would also be used to study the extent to which the proposed bid test achieves the stated objectives of the short sale rule by comparing trading activity in liquid securities that are subject to a price test with liquid securities that are not subject to a price test. The markets would benefit in the long run from the possibility of removing a rule that may weaken markets or, alternatively, by retaining a rule that may strengthen markets.

In addition, the Commission recognizes that, in the presence of short sale restrictions in equity securities, the absence of short sale regulation for securities futures may make trading security futures an attractive hedging alternative to equities. The pilot is designed to remedy potentially unfair competition caused by disparate regulation between equities and security futures products. We believe that the proposed pilot program would give the Commission an opportunity to determine whether suspension of the

proposed bid test would enhance competition among equities and securities futures in the most liquid securities. The Commission requests data to quantify the costs and the value of the benefits relating to security futures products and this proposal.

The Commission anticipates that broker-dealers, including market makers, may be able to provide greater liquidity in securities included in the proposed pilot program, because the absence of the proposed bid test would make it easier to fill buy orders. The Commission believes that this could benefit investors, however, the Commission seeks comment on how to assess the potential benefits of short selling without a bid test restriction in these selected securities. In addition, the Commission seeks comment on the benefits of acquiring the potential empirical data gathered from the proposed pilot program. Would the proposed pilot program effectively allow the Commission to better understand short sales and short sale restrictions? Please provide estimates and views on these potential benefits.

2. Costs

The Commission anticipates that the proposed pilot program may cause additional costs to brokers, dealers, SROs, and potentially issuers and investors. While we anticipate that SROs and broker-dealers would need to make system changes in order to exclude the selected securities from the proposed bid test, we do not know what these changes would cost. The Commission seeks detailed comment on the extent of required system changes and costs associated with implementation of the pilot program, and on any potential cost to investors due to the absence of a price test applied to these securities. In particular, the Commission seeks comment on whether the pricing of such securities is going to be more or less efficient, and whether manipulation of market prices (either upward or downward) is apt to be more or less prevalent.

The Commission believes issuers may incur some costs associated with inclusion in the pilot program and seeks estimates and views on potential costs to those issuers selected for the pilot program.

D. Proposed Rule 200: Definition of a Short Sale

1. Unconditional Contracts

a. Benefits

Proposed Rule 200 requires that unconditional contracts provide for present delivery, and specify the price