NSCP
NATIONAL SOCIETY OF COMPLIANCE PROFESSIONALS INC.

June 19, 2009

VIA E-MAIL RULE-COMMENTS@SEC.GOV

Elizabeth M. Murphy
Secretary
Securities and Exchange Commission
100 F. Street, NE., Washing, DC 20549-1090

Re: Proposed Amendments to Regulation SHO;
File No.: S7-08-09

Dear Ms Murphy:

I write this letter on behalf of the National Society of Compliance Professionals ("NSCP"). NSCP is the largest nonprofit membership organization dedicated to serving and supporting compliance officials in the securities industry, with a membership of more than 1,700. NSCP's members consist of professionals from broker-dealers, investment advisers, banks, insurance companies, hedge funds and law firms. NSCP's mission is to serve compliance professionals exclusively, including through education, certification (CSCP), publications, consultation forums, and regulatory advocacy.

NSCP appreciates the opportunity to comment on the Securities and Exchange Commission's (the "SEC" or the "Commission") proposed amendments to Regulation SHO (the "Proposed Amendments") as set forth in Release No. 34-59748 (April 10, 2009) (the "Proposing Release"), which set forth two separate approaches, and several variations thereto, to restricting short sales consisting of (i) a short sale price test and (ii) a so-called circuit breaker approach.

I would like to begin by placing the comments that NSCP is about to provide in perspective. The diversity of NSCP's membership as well as NSCP's mission of assisting compliance professionals within the securities industry to achieve high professional standards means that NSCP does not comment for the purpose of furthering an economic or business interest. Although NSCP's members are not economically interested, they are, of course, interested in the health and quality of the U.S. equity markets, including their depth, breadth and liquidity and their ability to efficiently facilitate price discovery. Moreover, because NSCP's membership consists overwhelmingly of compliance professionals, they understand the need for a robust regulatory scheme that is designed to protect investors as well as the soundness of our financial system and

markets. As compliance professionals, however, they are also vitally interested in encouraging the adoption of regulations that are carefully considered, narrowly focused, and accompanied by clear direction and guidance. In short, NSCP's comments are intended to offer constructive observations from the perspective of the compliance professionals that make up our membership.

Our comments are organized under the following three headings:

- A Prudent Approach
- Cost Effective Compliance
- Comment and Implementation Concerns

A Prudent Approach

Given the importance of the Proposed Amendments to the U.S. equity markets and, therefore, to the economy of the United States and of the world, NSCP commends the Commission for the careful approach that it has, so far, exhibited with respect to the Proposed Amendments, as well as previously when it eliminated former Rule 10a-1 and added Rule 201 to Regulation SHO, which prohibited the imposition by an SRO of a short sale price test. NSCP urges the Commission to continue to adhere to this careful and deliberate approach based upon objective, empirical evidence. NSCP believes that a focus on investor education and enforcement is likely to be both more efficient and effective than the Proposed Amendments.

The Need for Empirical Evidence

NSCP believes that it would not be prudent of the Commission to adopt any of the complex, costly and potentially far reaching regulatory alternatives set out in the Proposing Release for the purpose of restoring "investor confidence" in the equity markets[1] unless and until the Commission is able to point to some underlying inefficiency or failure in the equity markets that is both responsible for the deterioration of investor confidence in the first place and that would be remedied by the Proposed Amendments.[2]

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[1] *See* the Proposing Release at text following FN 7.

[2] By way of contrast, after the collapse of Enron and other business failures in the early part of this decade, the Commission championed a set of reforms that was designed to specifically address the failure of issuer disclosure to be timely and informative, which was perceived to be at the heart of the Enron debacle and directly related to the deterioration in the investing public's confidence that was then being experienced. *See, e.g.*, Harvey L. Pitt, then Chairman, SEC, Written Testimony Concerning Account and Investor Protection Issues Raised by Enron and Other Public Companies, Before the Committee on Banking, Housing and Urban Affairs, United States Senate (March 21, 2002) (available on the Commission's web site at: http://www.sec.gov/news/testimony/032102tshlp.htm).

NSCP is particularly concerned that any reversal by the Commission of its recent action to eliminate Rule 10a-1, by, for example, approval of any of the Proposed Amendments that incorporate a price test where such approval is not grounded upon empirical data or findings, could expose the Commission to charges that it is acting merely from political expediency rather than seeking to ensure that markets are fair, efficient and transparent.[3] This concern is made all the more real by the contrast between the Commission's exceptionally careful, thoughtful, and exhaustive data driven approach that supported its earlier action to eliminate Rule 10a-1 as compared to its current approach in the Proposing Release, which appears to rest entirely on the amorphous concept of "investor confidence" and is lacking in supporting data or empirical evidence. Put simply, even accepting for the sake of argument the Commission's belief that investor confidence is actually in need of restoration,[4] the Commission's stated goal of restoring investor confidence is, in the absence of empirical support, too thin a reed to support such a complex and expensive endeavor.

NSCP believes that a loss of confidence in the Commission as a fair and impartial regulator could, in the long run, do far more to damage the confidence of investors than any supposed harm that the Proposed Amendments might address. To avoid this concern, we urge the Commission to follow in its own footsteps and ground its actions in this matter on an objective, data-driven examinations of the market, just as it did when it repealed former Rule 10a-1.[5] To the extent solid studies are lacking to help guide the Commission's actions, NSCP

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[3] *See* footnote 55 of the Proposing Release (listing numerous letters from members of Congress requesting the reimposition of a short sale price test restriction). *See* also Mary L. Schapiro, Chairman, SEC, "Improving the Role of the Securities Regulators in a Changing Global Financial System" (June 11, 2009) (referencing "ensuring markets are fair, efficient and transparent" as one of three "core principles" that must animate "all who oversee securities markets") available on the Commission's web site at http://www.sec.gov/news/speech/2009/spch061109mls.htm

[4] Indeed, in light of the recent rise in the S&P 500 of approximately 40% in just under three months, NSCP believes that it could be argued that investor confidence is in fact dangerously high and most definitely not in need of further restoration. *See, e.g.*, the Up & Down Wall Street Column in Barrons (June 8, 2009). In light of such uncertainty, NSCP believes that it would be prudent for the Commission to consider that excess investor confidence, also known as "irrational exuberance," has frequently been a much greater source of harm to the market, and the economy, than its absence.

[5] We are unaware of any studies that have suggested that further restrictions on short sales would, in any way, improve the market for investors or issuers. By contrast, we are aware of several studies with respect to the actions taken by the Commission last September to restrict short sales of securities of financial companies, *see* SEC Release 34-58592 (September 18, 2008), which found that such actions did not improve the market for such securities or the confidence of investors with respect thereto. *See, e.g.*, the Investment Industry Regulatory Organization of Canada ("IIROC", which is the Canadian equivalent to FINRA) "Report on the Impact of the Prohibition on the Short Sale of Inter-listed Financial Sector Issuers," which was undertaken at the request of the Canadian Securities Administrators to examine the impact of the Ontario Securities Commission Order prohibiting short sales of certain financial sector issuers ("Restricted Financials") on trading activity. The Order, issued on September 19, 2008, prohibited

suggests that the Commission may want to consider a pilot program before imposing such a far reaching proposal on the equity marketplace.

A Suggested Alternative

Alternatively, NSCP posits that it might be both more efficient and effective to focus on investor education and enforcement rather than to impose any of the Proposed Amendments. With respect to education, similar to the approach the Commission took with respect to client commission practices,[6] NSCP recommends that the Commission issue guidance to investors that describes (i) the beneficial role in the marketplace played by short selling, including market liquidity and pricing efficiency;[7] (ii) the very real differences between abusive and legitimate short selling; and (iii) the important and commendable steps the Commission has recently taken to combat abusive short selling, including most importantly the Commission's recent implementation of Rule 204T of Regulation SHO, which imposes a "hard" buy-in requirement with respect to equity securities, thereby dramatically reducing fails and naked short sales.[8] Of course, NSCP also believes that vigorous enforcement by the Commission of existing short sale regulations, including Rule 204T of Regulation SHO, would also go a long way to instilling confidence in the investing public.

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short sales of Restricted Financials listed on the Toronto Stock Exchange that were also inter-listed with exchanges in the United States.

The IIROC study found that the Order appeared to have a significant impact on market quality, including an increase in both volatility and the "spread", which is the difference between the highest price bid to purchase the security and the lowest price offered to sell the security. There was also no appreciable difference between changes in prices of Restricted Financials and those financial issuers for which short selling was permitted. The IIROC study is available at:

http://docs.iiroc.ca/DisplayDocument.aspx?DocumentID=1BB3A789F8A04628A1C1D2CE68FEDEB4&Language=en.

See, also, Prohibitions versus Constraints: The 2008 Short Sales Regulations by Adam C. Kolasinksi, University of Washington, Adam V. Reed, University of North Carolina, Jacob R. Thornock, University of North Carolina (March 2009) (finding that the short sales regulations issued during the financial crisis of 2008 resulted in significant reductions in market quality. This study is available at: http://www.quadriserv.com/pdfs/Prohibitions%20vs.%20Constraints%20Reed%20Working%20Paper.pdf

[6] *See* SEC Release 34-54165 (July 18, 2006).

[7] *See* the Proposing Release at text at FN 15.

[8] *See* SEC Release 34-58572 (September 17, 2008). *See* also SEC Release 34-58785 (October 15, 2008) (imposing weekly reporting requirements on institutional investment managers with respect to short positions); and SEC Release No. 34-58774 (October 14, 2008) (implementing Rule 10b-21 which makes it a violation of the general antifraud provisions of the federal securities law to deceive others about one's intention or ability to deliver securities in time for settlement)

Cost Effective Compliance

To the extent the Commission determines to implement a short sale price test or to adopt a so-called circuit breaker approach, NSCP urges the Commission to consider the potential costs of such an approach and adopt an approach that is designed to both minimize those costs, since such costs will ultimately be borne by the investors whose confidence the Commission is seeking to restore, while at the same time not imposing costs that make it prohibitive for small broker-dealers, on an order by order basis, to offer certain levels of services to their customers.

Over Reliance on the Cost Savings Benefit of Regulation NMS

NSCP believes that the Commission has over estimated the ability of firms to rely on the systems that they put in place to comply with Regulation NMS as a means of holding down the cost of the Proposed Amendments. While systems put in place in response to Regulation NMS are likely to be useful in addressing the Proposed Amendments, NSCP believes that utilizing such systems in the context of any of the Proposed Amendments will require extensive systems mapping and alterations to multiple systems and, therefore, significant technology and operational costs. Of course, such costs will be in addition to costs associated with preparation of procedures, creation and implementation of training, and ongoing surveillance and review as well as ongoing costs of administration.

By way of example, all front end systems will need to be adjusted to provide for the new "short exempt" marking requirement. Many firms, however, have multiple front end systems, each of which will need to be adjusted. These expenditures will be multiplied for firms with correspondent clearing operations who clear for correspondent firms, each with their own front-end systems. Back-end systems will also need to be re-worked to identify where the market for a particular security is trading at any one instant and, significantly, to coordinate with front-end systems to insure proper marking of transactions. Firm's blue sheet, OATS and OTS reporting systems will need to be examined and adjusted. Market participants will need to insure that proper feeds to market centers are established and maintained and that those feeds are incorporated into their systems. There will also be substantial system development costs in connection with the data retention requirements.

Compliance personnel will be required to revise procedures and supervisory procedures manuals. Surveillance routines will need to be amended and implemented on an ongoing basis and supervisors will need to receive training in connection with their new responsibilities. Similarly, non-supervisory personnel (*e.g.* sales, trading, compliance and back office) will also need to receive training in connection with the new requirements and system changes. Moreover, we anticipate an increase in inquiries from regulators with respect to any new restriction that is adopted. Indeed, one of our members estimates that at least one additional, full-time compliance professional will need to be added to staff to help manage the increase in work-flow attendant to the new restrictions.

All of these costs will put tremendous economic stain on market participants already struggling financially. They will increase trading costs, which will be passed along to investors, the same group on whose behalf the Commission seeks to restore confidence. We urge the Commission to carefully consider the financial burdens these proposed amendments would impose on market participants, and seek to adopt the most cost effective model.

Cost Associated with the "Broker-Dealer" Provision

NSCP also believes that any rule, such as the "broker-dealer" provision of the modified uptick rule of proposed Rule 201(c)(1), that would require that broker-dealers maintain so-called "snapshots" of the market is likely to also impose significant costs, including technology, data storage, and, of importance to NSCP's membership, costs associated with surveillance and review. This is particularly true in light of the changes to the market resulting from the adoption of Regulation NMS. Indeed, the Commission itself estimates these costs at over $100,000 per broker-dealer for an aggregate annualized cost for all broker-dealers in excess of over half a billion dollars. The Commission's cost estimates seem to underestimate the cost to large, full service broker-dealers, since the volume of orders handled by these firms are likely to lead to significantly greater technology and storage costs alone as well as more frequent reviews.

Disproportionate Impact on Smaller Firms

Moreover, NSCP believes that it would be useful to also consider costs from a "trade ticket" perspective, which are likely to unduly impact smaller firms. NSCP is concerned that smaller firms may not have a sufficient number of trades to justify the added expense of gearing up for compliance with the Proposed Amendments and, as a result, these firms may decide to entirely forego the benefits of the "broker-dealer provision" since the "costs" on a per-trade basis are likely to be prohibitive for them.

Accordingly, NSCP urges the Commission to consider not only costs associated with the Proposed Amendments but how those costs are likely to be borne across various types of broker-dealers and whether those costs may adversely affect the ability of smaller broker-dealers to compete or the level of service that they can provide to their customers.

Comment and Implementation Concerns

Ability to Evaluate and Comment

NSCP notes that the Commission's decision to propose multiple variations on multiple approaches to a highly complex proposal makes it very difficult, time intensive, and, ultimately, expensive, for commenters to undertake the review necessary to provide meaningful and comprehensive comments on each of the proposed variations and the exceptions thereto. NSCP believes that this is particularly true with respect to smaller broker-dealers and, therefore, that the concerns of smaller broker-dealers are likely to be under represented in the comments received

by the Commission, notwithstanding that the greatest burden of the Proposed Amendments is likely to fall on them.

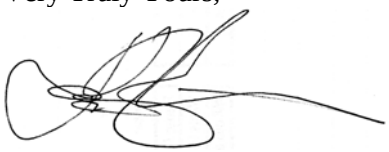
Accordingly, to the extent the Commission decides to proceed with any one of the Proposed Amendments, NSCP urges the Commission to allow an additional round of comments on the chosen approach so as to give firms an opportunity to focus their attention more narrowly on the Commission's chosen approach.

Proposed Implementation Period

As evident from the section above entitled "Cost Effective Compliance," NSCP believes that the proposed three month implementation period will not be a sufficient amount of time for market participants to implement any of the proposed short sale price restrictions and, indeed, that such period is woefully deficient and fails to take into account the complexity of the proposals, the need to identify systems and operating procedures that would be affected as well as the time necessary to (i) revise and test those systems and operating procedures; (ii) modify existing compliance and supervisory procedures; and (iii) train staff on the foregoing revisions. Given the complexity of any likely Proposed Amendment and its reliance on technology, NSCP believes that a minimum of one year would be a more reasonable implementation period.

Thank you for your attention to these comments. Questions regarding the foregoing should be directed to the undersigned at 860.672.0843.

Very Truly Yours,



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