

## Comment on proposed rule 10b-21



# NIPC

## National Investor Protection Coalition

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*“Advocates for the Protection of Equity Securities Investors and Issuers”*

March 31, 2008

RE: File Number S7-08-08, Proposed Rule 10b-21

Nancy M. Morris  
Secretary, Securities and Exchange Commission  
100 F Street, NE, Washington, DC 20549-1090

Dear Secretary:

NIPC members are very concerned with naked short selling and delivery failures that the SEC is authorizing market participants to effect in equity securities past T+3. More than anything, proposed rule 10b-21 reinforces the SEC's authorization to effect delivery failures past T+3 on the part of broker-dealers, market makers, clearing agencies and other market participants, while adding nothing to stop the practice. The proposed rule is nothing more than a wolf in sheep's clothing, because all it accomplishes is to establish a protection clause from section 10b for those market participants that do not make a representation about their intent or ability to deliver securities within the settlement cycle.

Creating an exemption from section 10b for market participants is exactly the wrong thing to do if the SEC really wants to reign in naked short selling. This proposal is seen by us as merely an attempt by the SEC to further protect market participants and give them preferential treatment, despite what section 6 (b)(5) of the Securities Act mandates. The protection for market participants from section 10b that the proposed rule creates will make it even harder than it already is to hold naked short sellers accountable for effecting deliver failures past T+3. The proposed rule adds absolutely nothing to stop or prohibit naked short selling and overlaps with already existing laws in this regard. However, it does create an exemption from 10b, so long as market participants make no representation about their intent or ability to deliver by settlement

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date. Delivery failures thus created can then be passed along down the chain by other market participants into customer accounts, without fear of violating rule 10b, if 10b-21 is adopted as proposed. We can only conclude that creating carve out exemptions from 10b for market participants is the primary reason for this proposed rule.

This makes the concern the SEC has voiced regarding naked short selling very hollow. The proposed rule will merely encourage market participants to continue naked short selling, since they would enjoy more protections if 10b-21 is adopted as the SEC has proposed.

The intent of the SEC has remain consistent over a long period of time in that it authorizes effecting delivery failures past T+3 in an informal way, without passing a formal rule. The rule as proposed is consistent with the position that the SEC actually authorizes naked short selling and delivery failures past T+3. If seen in context of Federal securities laws and state jurisdiction issues, effecting delivery failures and crediting “securities entitlements” to customer account past T+3 is prohibited. Yet the SEC has stated itself that it authorizes this activity, without adopting a formal rule to this effect. Instead it relies on the state adopted UCC:

***“...a securities broker-dealer may credit a customer’s account with a security even though that security has not yet been delivered to the broker-dealer’s account by NSCC. In that event, the customer receives what is defined under the Uniform Commercial Code as a “securities entitlement,” (Emphasis added)***

Rules, like the proposed 10b-21, that remove market participants even further from anti fraud rules, shows that the SEC is not serious about stopping naked short selling at all, despite the public comments. Rather, the SEC is actually ensuring that market participants can continue to effect delivery failures past T+3 by creating escaping clauses from the anti fraud rules in place.

We propose that rule 10b-21 be simplified by striking the “escape clause” for market participants from rule 10b, and adopt an amended version as follows:

**“It shall constitute a “manipulative or deceptive device or contrivance” as used in section 10(b) of this Act for any person to submit an order to sell a security if ~~such person deceives a broker or dealer, a participant of a registered clearing agency, or a purchaser about its intention or ability to deliver the security on the date delivery is due, and~~ such person fails to deliver the security on or before the date delivery is due..”**

If the proposed rule is adopted as the SEC has proposed, it would do more harm than good by making it safer for market participants to effect delivery failures. There for, we urge the SEC to either amend the text of the rule as we have proposed or to not adopt it at all.

Sincerely submitted,

Thomas Vallarino  
President - NIPC