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February 28, 2007

Via E-mail (rule-comments@sec.gov)

Nancy M. Morris, Secretary,
Securities and Exchange Commission,
100 F Street, N.E.,
Washington, D.C. 20549-1090.

Re: Proposal to Amend Rule 105 of Regulation M – File No. S7-20-06

Dear Ms. Morris:

We are pleased to submit this letter in response to the Commission's request for comments on its proposal to amend Rule 105 of Regulation M (the "Proposals") as contained in Release No. 34-54888 (Dec. 6, 2006) (the "Release").

In general, we appreciate the Commission's reasons for the Proposals, namely, to eliminate the possibility that those who sell short in advance of an offering might employ schemes to evade the prohibition under Rule 105 forbidding the use of purchased securities to cover their short positions by instead flatly prohibiting them from purchasing securities in the offering, even if they do not intend to use the purchased securities to cover their short positions. However, we are concerned that this outright prohibition could have serious, unintended consequences in one relatively discrete area, that of shelf offerings, and we urge the Commission to modify the Proposals as they would apply in that particular context. We believe that our suggested modification is necessary to prevent Rule 105 from hurting liquidity in the market for shelf offerings, yet will still enable the Commission to achieve its stated goals. We also set forth a few comments of a more technical nature.

To Avoid Adversely Affecting Liquidity in a Shelf Offering, Start the Restricted Period No Earlier Than at Public Announcement of the Offering

As explained in the Release, in an effort to stop short sellers from using a "progression of schemes and structures engineered to camouflage" prohibited short covering, and to avoid the difficulty of having to establish whether such "schemes" in fact involve a prohibited covering transaction, the Commission has proposed to change the focus of

Rule 105 and simplify the way it operates. Rather than prohibiting the use of offering securities to cover a restricted period short sale, Rule 105, as amended, would simply provide that any person who establishes a short position during a Regulation M restricted period may not "purchase, including enter into a contract of sale for, the security" in the offering, without regard to how the restricted period short sale is covered.

As is currently the case, the restricted period would begin five business days prior to the pricing of the offered security or, if shorter, the date of the initial filing of the registration statement with the Commission. This would be the case without regard to the type of offering. Thus, in the case of a shelf offering, where the registration statement will often have been filed well in advance of the pricing, the restricted period would typically be the five business days prior to the pricing.

Although this is the same restricted period that applies under current Rule 105, the Proposals would prohibit purchases in the offering altogether, rather than prohibiting only the covering of short sales with securities purchased in the offering. We believe that the restricted period as proposed will unnecessarily exclude potential purchasers in the offering who did not have a manipulative intent in establishing their short position. This will make the process of raising capital less efficient for, and thus more costly to, issuers, and is unnecessary to achieve the Commission's purposes.

As the Commission is aware, shelf offerings are often launched and priced in less than five business days, sometimes even on an "overnight" basis, with very little advance notice to investors or the public. Thus, investors who wish to participate in a shelf offering may be unaware that one is being launched until shortly before – or in some cases even after – the pricing. As a result, these purchasers often may not know when the restricted period begins until after it has already begun, and often may not be able to avoid short selling during the restricted period. Thus, these investors may not be able to participate in the offering unless they avoid short selling altogether.

Requiring investors who might wish to participate in a shelf offering to refrain from short selling generally, in order to preserve the ability to participate in a shelf offering that is launched and priced quickly, simply is not practical. Many of these investors may engage in short sales for legitimate reasons having nothing to do with a potential offering. For example, an investor may hold a significant investment in an issuer's stock and have an ongoing hedging program that involves the establishment of a short position in that stock followed by periodic adjustments to increase or decrease the position. Or, an investor may engage in program trading across a broad range of stocks that involves frequent buying and selling, including short selling, of one or more of these stocks, including the issuer's stock. In addition, dealers may sell an issuer's stock short in response to customer orders to purchase the stock, in furtherance of their customary market-making or other customer-facilitation roles, or may manage accounts for clients pursuant to which they need to buy, sell or sell short the issuer's stock. Investors that engage in multiple trading activities of these kinds may be among the most likely to participate in a shelf offering conducted on short notice, particularly an offering conducted as a large block trade in which the success of the offering depends on the ability to sell large positions to a small number of large, sophisticated institutions.

Investors that are active market participants are an important source of liquidity for issuers that wish to go to market quickly. Yet it is precisely this segment of the market that may be foreclosed from purchasing in the offering if the Proposals are adopted in their current form. Ironically, while Rule 105 was intended to protect issuers from practices that might unfairly reduce the proceeds of the offering, the Proposals could make it even harder for issuers to go to market, at least by means of a shelf offering on short notice.

We do not see any reason to exclude potential purchasers from an offering just because they may have engaged in short sales within the five business days prior to pricing but without notice that the offering was coming, as long as they do not in fact use the offering securities to close out their short positions. The potential for abusive short sales that Rule 105 is intended to address should not be present when the short sales are made in ignorance of the offering. We respectfully suggest that the Commission modify its Proposals so that the restricted period for purposes of Rule 105 begins five business days prior to pricing or, if shorter, upon the later of the initial filing of the registration statement or the initial public announcement of the offering, and in each case ending at the pricing of the offering. This modification would enable investors that engage in legitimate short selling – *i.e.*, without knowledge that an offering is coming – to participate in the offering, thereby preserving an important source of liquidity for shelf issuers without sacrificing the important goals of the Proposals. Those who sell short during the five business days before an offering with knowledge that the offering is coming would be prohibited from buying in the offering.

We recognize there is a risk that an investor could learn about a potential shelf offering before it is publicly announced and, under the modification of the Proposals that we suggest, would be permitted to sell short even with the knowledge that an offering is coming. However, the antifraud provisions of the federal securities laws already address this issue. Rule 10b-5, for example, would prohibit trading, including short selling, on the basis of material, non-public information. In light of these antifraud provisions, we believe that modifying the Proposals as we have suggested should not create a significant risk of abusive short selling in advance of an offering.

Exception to Allow Purchases by Persons Who Close Out Short Sales with Market Purchases

In the Release, the Commission specifically requested comment as to whether Rule 105 should permit purchases in an offering if a restricted period short sale is closed out before pricing. We believe that the risk of abusive short sales would be greatly reduced if the short sellers are required to close out their positions before they may participate in the offering; therefore, we support a modification of the Proposals that would permit this. However, we do not believe that such a modification is sufficient to address the more critical issue discussed above – namely, permitting short sellers who sell short before the offering is announced to participate in the offering. Legitimate short sellers may not be in a position to close out their short positions where the short sales are effected in response to market or other factors that are unrelated to the offering. For example, an investor that has hedged a significant investment in an issuer's stock may not be able to close out a short position established for hedging purposes without exposure to significant loss. In these situations,

requiring that the short position be closed as a condition to participating in the offering will not solve the problem; the investor may have no practical choice but to stay out of the offering, which in turn could hurt the success of the offering. In short, adding such an exception to the Proposals, while desirable, would not address the most serious issue raised by the Proposals and would not eliminate the need to modify the restricted period as we have suggested.

Confirm that Investors May Rely on Internal Information Barriers

If the Commission adopts the Proposals in any form, we respectfully request that it make clear, either in Rule 105 or in the adopting release, that institutional investors who maintain internal information barriers sufficient to permit them to treat the trading activities of their different affiliates or other units as separate for other purposes of Regulation M (*e.g.*, the proviso in clause (3) of the definition of "affiliated purchaser" in Rule 100) are permitted to rely on those barriers for purposes of Rule 105 as well. Thus, if an affiliate or separately identifiable department of a firm need not be treated as an affiliated purchaser of the firm for purposes of Rule 101 or 102, were either rule to apply to the firm, then the affiliate or department should not be prohibited by Rule 105 from purchasing in an offering as long as it did not itself conduct short sales during the restricted period, even if the firm did so. In that event, only the firm, which made the short sales, and not the affiliate or department, which made no short sales, should be subject to the prohibition of Rule 105. In our view, this interpretation is consistent with the premise of the "affiliated purchaser" exception in Rule 100, and we see no reason why it should not apply with regard to Rule 105 as well as Rules 101 and 102.

Meaning of "Enter Into a Contract of Sale"

As mentioned above, Rule 105, as amended, would provide that any person who establishes a short position during the restricted period may not "purchase, including enter into a contract of sale for, the security" in the offering, but the meaning of the phrase "enter into a contract of sale" is not clearly explained in the Proposals or the Release. In light of the discussion in the Release of schemes of evasion and concealment, we interpret this phrase to mean that the prohibition on purchasing offering securities applies even if the purchase is accompanied by a contemporaneous or other sale of the securities, and *not* to mean that a contract of sale, in its own right or by itself, is prohibited. We respectfully request that the Commission clarify the meaning of this confusing phrase in the adopting release or the rule text itself, or eliminate it altogether.

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We appreciate the opportunity to comment on the Proposals, and would be pleased to discuss any questions that the Commission may have with respect to this letter. Any such questions may be directed to David B. Harms (212-558-3882) in our New York office or to Eric J. Kadel, Jr. (202-956-7640) in our Washington, D.C. office.

Very truly yours,

SULLIVAN & CROMWELL LLP

cc: Erik R. Sirri, Director, Division of Market Regulation
James A. Brigagliano, Associate Director for Trading Practices and Processing, Division of Market Regulation