The Security Traders Association of New York, Inc.

Members of the Security Traders Association
39 Broadway, Suite 1840 New York, NY 10006 ● (212) 344-0410 ● Fax (212) 943-8478
e-mail - stany@stany.org website - www.stany.org

September 30, 2008

The Honorable Christopher Cox
Chairman
The Securities and Exchange Commission
100 F. Street, NE
Washington, DC 20549

RE: SEC Release No. 34-58592

EMERGENCY ORDER PURSUANT TO SECTION 12(k)(2) OF THE SECURITIES EXCHANGE ACT OF 1934 TAKING TEMPORARY ACTION TO RESPOND TO MARKET DEVELOPMENTS

AMENDMENT TO EMERGENCY ORDER PURSUANT TO SECTION 12(k)(2) OF THE SECURITIES EXCHANGE ACT OF 1934 TAKING TEMPORARY ACTION TO RESPOND TO MARKET DEVELOPMENTS

Dear Chairman Cox:

The Security Traders Association of New York (STANY)[1] understands and appreciates that the Commission, along with the Federal Reserve, the Treasury Department, and the Federal Government believe there is a need for extraordinary actions to bring a measure of stability to the markets. We are living through difficult times that may require unprecedented actions on many fronts.[2]

STANY, however, is extremely concerned that the current prohibitions on short sales are in fact not helping the markets as intended by the Commission. Rather than reducing market turbulence, the Emergency Orders have heightened volatility, decreased liquidity, hampered price discovery and disrupted the functioning of fair and orderly markets. We respectfully urge the Commission to allow the Emergency Orders to expire this week and restore the forces that drive the free market pricing of securities.

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[1] The Security Traders Association of New York is the voice of the trader in the New York metropolitan area. STANY represents approximately 1,000 members, all engaged in the buying, selling and trading of securities and is the largest affiliate of The Security Traders Association (STA). The STA is a worldwide professional trade organization that works to improve the ethics, business standards and working environment for our members. STA and STANY provide a forum for our traders, representing institutions, broker-dealers, ECNs, and floor brokers to share their unique perspectives on issues facing the securities markets. They work together to promote their shared interest in efficient liquid markets, as well as in investor protection

[2] To be clear, STANY supports the SEC's emergency order adopting new Rule 10b-21 which clarifies that deception regarding the intention or ability to deliver securities in time for settlement and failure to deliver those securities amounts to a manipulative or deceptive device or contrivance. STANY opposes market manipulation in any form and is pleased to see a hard-line being taken against those who intentionally engage in action to manipulate stock prices. Likewise, we appreciate the Amendments to the Emergency Order which reinstate the market maker exemption and allow for a two week lag in public reporting of short positions on EDGAR by investment managers.

While STANY fully supports enforcement of rules that prevent and punish manipulative short selling, we believe that these practices can be curtailed and policed without eliminating this critical order type. We believe that Reg. SHO if properly enforced is adequate to prevent abusive naked short selling. Rather than banning short selling, or creating a new set of rules, the markets would be best served by enforcement of already available anti-fraud provisions.

Moreover, we do not believe that current market prices are the result of either the inadequacy of regulation of short sales, or manipulative short selling, but rather the result of a changing economic climate which affects the underlying fundamentals of a broad array of exchange traded companies. It is misplaced to blame short sellers of the stock of financial institutions for causing, or even contributing to, the current financial crisis. The United States is undergoing a credit crisis caused by loan defaults and exotic securities such as credit default swaps. Despite the ban on short selling, the stock prices of financial companies continue to fall and in some cases have gone to near zero. The ban on short sales has not helped Wachovia, Washington Mutual or AIG, all of which have seen significant declines in the price of their shares since the ban on short selling. Credit practices not short selling are the problem. Yet, so far there has been neither a ban on credit default swaps nor prohibition of lending to suspect creditors.

The ban on short selling has not materially benefited the financial institutions it was aimed to protect. It appears that the ban has in fact made it more difficult and costly for investors to trade. Decreased liquidity, larger spreads and higher costs have served to further erode investor confidence.

It is important to recognize the distinction between market manipulation and the legitimate use of short sales as an investment strategy that contributes to price discovery. Short selling is an important part of the investing, hedging and outright policing of corporate governance by the investment community. As the Commission has recognized in the past, short selling is a valuable component of risk management. Chairman Cox noted in a CNBC interview on July 16, 2008 “if we are talking about legitimate short selling…that’s *vital* to the functioning of our markets.” (Emphasis added.) We view a ban on short selling as akin to “throwing out the baby with the bathwater.”

Short sellers are important to the proper functioning of markets because they reflect the expectations of some market participants that a company’s prospects are diminished. Normally sellers, both those who hold shares and those who sell short, provide the liquidity necessary to buyers. By removing short sellers, this equilibrium is disturbed. While the stock might temporarily be forced to a higher price, this higher price comes with greater instability and volatility. It may seem that elevated stock prices are a good thing, but that is not necessarily the case. Investors may be purchasing artificially pumped up stocks. It is the balance of buyers and sellers, optimists and pessimists, which sets the “correct” stock price.

In addition to providing price discovery, short selling is vital to risk management. When an options market maker facilitates a customer trade, it may be necessary for the options market maker to hedge its risk by selling short the underlying stock. These trades are neither manipulative nor intended to destabilize the price of the security. Rather they are related directly to a transaction in the overlying option. The exemption has permitted option market makers to provide liquidity and depth to the market for listed options. Without the ability to hedge their risk, liquidity in the options market will be significantly impaired.

Likewise, international traders are having an extremely difficult time with the current proscriptions. They often short the ADR and go long the ordinary. Rather than paying the fee to convert the ordinary into an ADR, they will hold the matched position. The new rules preclude this strategy, thereby increasing the cost of providing a useful arbitrage activity that effectively lines up the two markets.

ADRs and Global Shares of foreign equities that trade in US markets during common trading hours with their respective home markets derive their value from three primary components, excluding transaction costs and taxes: 1) The price of the stock in the home market, 2) The exchange rate between the home country currency and the US dollar, and 3) The conversion ratio of the ADR into the common stock. Utilizing these three inputs, a 'fair value' of the ADR/Global Share can be determined. Arbitrage strategies that capitalize on pricing deviations between the two markets are critical to ensuring that the value of the US shares are as consistent as possible with the fair value calculation. The arbitrage strategy cannot be affected without the ability to short the US security, resulting in a mispricing of the ADR/Global Share. The mispricing creates significant costs to investors as well as to issuers.

In addition to the disruptions to these markets, the ban on short selling, and specifically the buy-in requirements, have created burdensome and expensive systems adjustments and resulted in massive back office confusion. The Emergency Orders were issued without warning, leaving brokers with hours to implement systems changes and no time for systems testing. Although the Commission has recognized that not all failures to deliver stem from naked shorts and provided leeway for inadvertent fails, determining the cause of delivery failures is in many cases difficult under a T+4 deadline.

It is our view that emergency orders, being less well considered than rules developed through notice and public comment, tend to have unintended, adverse consequences. As with the previous Emergency Order, we believe that the current measures should be temporary. It is not the SEC's job to promote bull markets or stem bear markets, but to maintain fair and orderly markets. It may have seemed necessary to institute rules to curtail short sales and generate repurchases and buy-ins, decreasing downward pressure and increasing upward momentum in the short term. However, the continued slide in financials despite the short sale ban indicates there are real fundamental and economic reasons for these stocks to continue to decline. The short sale ban has not stemmed the overall selling in these issues. Making short sales either more difficult or, in the case of financial industry stocks, prohibiting them altogether has increased market inefficiency, reduced liquidity, and inhibited the price discovery process.

While we appreciate the tremendous pressure under which the Commission has been operating, we caution against regulation for regulation's sake and urge the Commission to eliminate the limitations on short sales in the Emergency Orders.

Respectfully submitted,

Kimberly Unger
Executive Director

cc:
Commissioner Luis A. Aguilar
Commissioner Kathleen L. Casey
Commissioner Troy A. Paredes
Commissioner Elisse B. Walter
Dr. Eric Sirri, Director of Trading and Markets
Ms. Florence E. Harmon, Acting Secretary