

SEC Proposes “Naked” Short Selling Anti-Fraud Rule

March 18, 2008

On March 17, the U.S. Securities and Exchange Commission (SEC) issued its formal proposal to adopt an anti-fraud rule under the Securities Exchange Act of 1934 (Exchange Act). The rule would address failures to deliver securities that have been associated with “naked” short selling. The SEC stated that the proposed rule is intended to highlight the liability of persons that deceive certain specified persons about their intention or ability to deliver securities in time for settlement, including persons that deceive their broker-dealer about their locate source or ownership of shares, and that fail to deliver securities by settlement date. Comments will be due to the SEC 60 days after the proposal is published in the Federal Register, which should occur by March 25.

If adopted, the SEC-proposed Rule 10b-21 under the Exchange Act would specify that it is unlawful for any person to submit an order to sell a security if such person deceives a broker-dealer, a participant of a registered clearing agency, or a purchaser regarding the person’s intention or ability to deliver the security on the date delivery is due, and such person does in fact fail to deliver the security on or before the date delivery is due. The SEC stated that scienter would be a necessary element to establish a violation of the proposed rule. The SEC also stated that, because one of the principal goals of proposed Rule 10b-21 is to reduce fails to deliver, violation of the proposed rule would occur only if a fail to deliver results from the relevant transaction.

To view the SEC’s Proposing Release, please visit: <http://www.sec.gov/rules/proposed/2008/34-57511.pdf>.

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