From: "Patrick J. Healy"
Date: Thu, 2 Apr 2009
To: <redacted>

Subject: Follow up

Good morning to all,

First, my sincere thanks to all for your continuing and invaluable assistance. If the pinheads in the media had any idea how helpful you can be, they would sing a better tune!

We recently sent out two emails with regard to the Uptick Rule. I thought that these might be informative and have cut and pasted them below. We will also be sending out a letter to the SEC with some issuer thoughts in advance of next week's meeting. I will make sure to cc all of you on that.

Again, many thanks to all. See email copies below:

Email sent on March 18:
Good afternoon to all,

Good news. Driven by a number of factors, the markets appear to be turning in a positive direction with the DOW up five of the last six days. You may recall that the genesis of this move upward was chatter early last week about the imminent restoration of the Uptick Rule, perhaps by the end of the month. Barney Frank, et al, seemed quite confident. While we, too, are confident that some form of relief is indeed imminent, our belief is that it is likely to take longer and be quite different than the historic "Uptick Rule" that simply prevented short selling on a minus tick.
The SEC is already scheduled to meet on the Uptick Rule on April 8. Whatever proposal surfaces, it will be subject to public comment, etc. Hence, more time will be required. In the interim however, Senate Bill 605, mandating certain short selling restrictions, has been proposed. In short, the proposed legislation directs the SEC to write regulations within 60 days accomplishing five things to end abusive short selling.

- First, the SEC must reinstate the substance of the uptick rule prohibiting short sales that are not made on an increase in the price of the stock. This is designed to prevent short sellers from piling on a declining stock, driving prices down.
- Second, the SEC must require exchanges and other trading venues to execute the trades of long sellers ahead of short sellers, all other things being equal.
- Third, with the concurrence of Treasury and the Federal Reserve Board, the SEC must prohibit short sales of the securities of any financial institution unless that trade is affected

at a price (in minimum lots specified by the Commission) at least 5 cents higher than the immediately preceding transaction in such securities. Since the financial sector is in such a fragile state, if the Treasury and Fed believe they it needs additional protection, the legislation permits it.

- Fourth, SEC rules must prohibit any person from selling securities short unless that person has at the time of the short sale a demonstrable legally enforceable right to deliver the securities at the required delivery date. Under current law, many short sellers fail to deliver.
- Fifth, the SEC will require that all short sales settle on the same time frame employed for long sales of the same securities.

All that said, here is our take-away:

- The solution will take longer than the pundits project. Our guess, mid-year, at best. Hope we're wrong.
- The solution will involve some kind of "price test" rather than the historic uptick rule(1). There will be a lot of yelling and screaming on this one, with an especially heated debate over a "return to nickels" for shorting financial stocks.
- Faster settlement on short sales (to parity with longs) is a no-brainer.
- While not addressed in the above legislation, we believe that some form of increased disclosure by shorts is imminent. Time to get these guys out in the sunshine!

So, the really good news is that progress is being made and, albeit not as fast as everyone wants, we are going to get there!

While surely less exciting, I would also like to bring to your attention that we petitioned the SEC in a letter last week for some relief to the Penny Stock Rule. In our letter we requested that companies whose stock price is below $4 be permitted to switch markets. Many companies hurt by the current economic situation could benefit from either reduced listing costs or enhanced branding opportunities. Hence, switches in both directions would be permitted.

As always, please shoot an email to me or give me a ring with any comments or questions. We value highly our role as an independent issuer advocate and rely heavily upon your input.
Tks/PJH

(1) Further reasoning on why we believe that some form of "price test" will replace the historic uptick rule, which in our opinion has been rendered outdated. One, with the

inception of Reg NMS, the markets are no longer centralized and no market can claim a majority of the trading in its own stocks. Two, with the proliferation of algorithmic trading, changes in the average trade size and speed have made implementation of the old rule impracticable.

Patrick J. Healy, CEO
[redacted]

Email Sent on March 24:
Good morning to all,

Indeed, it is a good morning for issuers. As forecast in our email to you last week, help on the Uptick Rule appears to be on the way - and pretty darned close to our projected outcome to boot. Clairvoyant? Not really; just some good, old-fashioned common sense combined with our Issuer Advocacy efforts.

In a joint letter to the SEC (copy cut and pasted below), the Exchanges collaborated on a joint recommendation to modify the historical Uptick Rule (we referenced this as a "Price Test") and made it subject to a "circuit breaker". Precisely when this Modified Uptick Rule will be triggered via the circuit breaker still remains to be determined by the SEC.

You will recall that the catalyst for our Market Update last week was proposed Senate Bill 605 calling for multiple measures. Our "takeaways" indicated that a solution that involved a price test and circuit breakers would likely be implemented by midyear. We believe that today's joint letter validates both our recommended form of relief and the timeframe. There is still much work to be done here to include the SEC concurring with the recommendations, defining the stress points that would trigger the circuit breakers, receiving comments, drafting regulations and implementing the solution.

We expect that the SEC will put some kind of proposal out for public comment following the April 8th meeting. You will likely receive one more bite at the apple and we would be happy to submit a collective response to include your thoughts. To this end, I will personally follow up with you.

I must say, we are flattered by these developments and encouraged to see the Exchanges come together on this issue. Congratulations to all of you.

As always, please give me a call or shoot an email to me with any comments or questions.

<u>Copy of Joint Letter:</u>

March 24, 2009

The Honorable Mary Schapiro Chairman U.S. Securities and Exchange Commission 100 F Street NE Washington, DC 20549 Dear Chairman Schapiro: The United States national securities exchanges welcomed the announcement that the Securities and Exchange Commission (the Commission) will consider a proposal to adopt a rule to combat abusive short selling. Abusive short selling harms investors and the companies listed on our exchanges, and destroys the overall confidence in our capital markets. Our challenge is to restrict abusive short selling while still permitting liquidity creating short selling that continues our status as the most efficient capital market in the world. As you know, we worked closely with the Commission to implement new rules and emergency measures to combat abusive short selling during 2008. We also applaud the Commission for pursuing new restrictions while permitting a full opportunity for comment given the complexity of our markets and the technology that currently supports our markets. Continuously attacking abusive short selling and other manipulative activities is critical to restoring public confidence in the US equities markets. First, let us commend the Commission in its efforts to attack an abusive form of short selling; "naked short selling" in combination with failures to deliver. On September 17, 2008, 2008, the Commission adopted interim final Rule 204T under Regulation SHO to restrict and penalize brokers and their customers for failures to deliver securities.1 As a result, the number of securities with significant failures to deliver on the "Threshold" lists has decreased by over 95 percent, from over 400 prior to the adoption of the rule to fewer than 20 today. More recently, there has been a great deal of discussion around reintroducing old rules that were designed to regulate short selling. As operators of the US equities markets that applied the original Short Sale Rule (the "Uptick Rule") in our trading systems and enforced broker-dealer compliance with that rule, we are well-positioned to help the Commission to review possible short selling restrictions. The original Uptick 1 See Exchange Act Release No. 58572 (Sept. 15, 2008); Exchange Act Release No. 58166 (July 15, 2008). Rule, whereby short selling could occur only when the last sale was at or above the previous sale, operated for a long period of time, is understood by the trading community, and is supported by issuers. However, the original Uptick Rule would likely prove difficult to implement and enforce in our current penny increment market structure and would not be as prohibitive in today?s market where transaction prices change multiple times in a single second and message traffic has exploded to billions of messages storming down on our markets every day. As such, we are proposing a slightly altered and modernized version of the previous Uptick Rule, which we will refer to as the "Modified Uptick Rule." The Commission can, we believe, adopt a similar but simple, effective and more prohibitive Short Sale restriction that takes into account how equity trading has changed over the past several years since the original Uptick Rule was eliminated. The exchanges have worked in a coordinated and unified approach to craft a proposal that will deliver appropriate restrictions on abusive short selling practices. Under our Modified Uptick Rule, short selling can only be initiated at a price above the highest prevailing national bid by posting a quote for a short sale order priced above the national bid. As such, the execution of a short sale would occur only at a higher price than the prevailing market at the time of initiation, and only on a passive basis (i.e., short sales cannot hit bids). This restriction would greatly assist the prevention of manipulative short selling, which is so harmful to the markets. This Modified Uptick Rule is superior to the original Uptick Rule in several ways. It is conceptually simple, likely to be more effective in dampening downward price pressure, and easier to program into trading and surveillance systems than the original Uptick Rule. We understand that no solution is perfect but we believe the Modified Uptick Rule that we are proposing is the most effective solution to deal with the faster-moving, post-Regulation NMS trading environment and to reduce downward pressure on stocks created by abusive short selling. In addition, we believe the most practical and effective way to structure adherence to the Modified Uptick Rule would be similar to oversight of the Trade-Through Rule under Regulation NMS. In this vein, the Modified Uptick Rule would be a policies and procedures requirement, and brokers would have responsibility for ensuring compliance with the rule before sending a short sale order into the marketplace. Exchanges could offer order types to assist brokers in performing their compliance duties, but would rely on a broker?s indication that they had performed the required due diligence on the order when so indicated. In combination with the adoption of this Modified Uptick Rule or any short sale price test, we urge the Commission to also adopt a "Circuit Breaker" that would trigger the application of the Modified Uptick Rule only after the price of a stock has experienced a precipitous decline by a certain percentage, perhaps ten percent. Our national markets and many foreign markets have successfully used circuit breakers on both broad indexes and individual securities for many years. A Circuit Breaker permits normal market activity while a stock is trading in a natural range and short selling is more likely to benefit the market (by, for example, increasing price discovery and liquidity). Conversely, a Circuit Breaker will restricts short selling when prices begin to decline substantially and short selling becomes more likely to be abusive and harmful. The Circuit Breaker is particularly efficient in stable and rising markets because it avoids imposing continuous monitoring and compliance costs where there is little or no corresponding risk of abusive short selling. We focus here only on the broad concepts of the Modified Uptick Rule and a Circuit Breaker to highlight their importance. There are, of course, details of the Modified Uptick Rule about which the exchanges can and will comment further. For example, with respect to the Modified Uptick Rule, the exchanges have views regarding the benefits of bona fide market making in both equities and options markets, and on the need for clear and precise guidance on what constitutes bona fide market making and for an exemption for market makers. Additionally, we believe firms need to know what policies and procedures they must adopt to promote compliance with the Rule, and whether exchanges can assume that short sale orders have been checked properly for compliance with the Rule. With respect to the Circuit Breaker, questions exist about the proper reference price for calculating it and about the duration of the Circuit Breaker once triggered. Also, the network processors must determine how to disseminate an indication that a Circuit Breaker has been triggered and, later, lifted. The exchanges, member firms, and network processors must also provide estimates of programming and testing requirements for both the Circuit Breaker and the Modified Uptick Rule. As always, we know the Commission will consider implementing rules in a time-line that carefully balances the risks of the behavior being regulated against the risks of disrupting the very markets that operated efficiently throughout this crisis. We applaud the Commission for tackling this important and difficult issue. Commission leadership and expertise, along with active engagement by investors, issuers, firms, and exchanges, will lead to a positive outcome and help restore investor confidence in the US equities markets. cc: The Hon. Kathleen L. Casey, Commissioner

The Hon. Elisse B. Walter, Commissioner The Hon. Luis A. Aguilar, Commissioner The Hon. Troy A. Paredes, Commissioner

Dr. Erik R. Sirri, Director, Division of Trading and Markets,

Patrick J. Healy, CEO