

## Client Alert

# Financial Markets Developments

### SEC Approves Technical Amendments to Short Sales Reporting Order and Financial Institutions Order

On September 21, 2008, the US Securities and Exchange Commission (the "SEC") issued technical amendments to the following two orders that it issued last week:

- Its emergency order issued on September 18, 2008, temporarily requiring institutional money managers with more than US\$100 million under management as of June 30, 2008 to report short sales in publicly traded securities on a new Form SH (the "Short Sales Reporting Order")<sup>1</sup> and
- Its emergency order issued on September 18, 2008, temporarily prohibiting short sales of securities of certain financial institutions (the "Financial Institutions Order").<sup>2</sup>

We have summarized below the key elements of the technical amendments.

#### Overview of Recent SEC Emergency Orders

The technical amendments bring to a total of six the number of orders and amendments issued by the SEC within the last week. In addition to the Short Sales Reporting Order and the Financial Institutions Order, the SEC previously issued an emergency order on September 17, 2008 temporarily prohibiting "naked" short sales of securities of any public company (the "Naked Short Sales Order")<sup>3</sup> and an emergency order on September 18, 2008 temporarily relaxing restrictions on issuer repurchases of securities pursuant to Rule 10b-18 under the Securities Exchange Act of 1934, as amended (the "Issuer Repurchase Restrictions Order").<sup>4</sup> For details, please see our previous memorandum dated September 19, 2008 at [http://www.whitecase.com/alert\\_cmsecurities\\_shortsell\\_091908/](http://www.whitecase.com/alert_cmsecurities_shortsell_091908/).

For ease of reference, we have summarized in *Appendix A* to this memorandum the emergency orders and related amendments issued to date by the SEC.

#### Amendments to the Short Sales Reporting Order

The SEC's technical amendments<sup>5</sup> to the Short Sales Reporting Order make the following changes and clarifications to the original order:

- While the SEC still requires institutional money managers to file a Form SH on EDGAR, the filing will initially be non-public and the SEC will make each Form SH publicly available two weeks after the due date for the form. The filer must label each page of the Form SH report "NON-PUBLIC" in bold and capital letters at the top and bottom of each page. The due date for Form SH is before 5:30 p.m. ET on the first business day of the calendar week following a week in which a short sale was effected, and the first Form SH is required to be filed on September 29, 2008. As a result, the first Form SH will be publicly available on October 13, 2008. This provides limited relief to money managers concerned about premature disclosure of their short positions. The only way to avoid disclosure (prior to the expiration of the Short Sales Reporting



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Order, assuming it is not extended or replaced) is to stay within the SEC's de minimis threshold of US\$1 million or 0.25 percent of the issuer's outstanding securities.

- Form SH is only required to be filed to report short sales effected on or after September 22, 2008. Investment managers are not required to disclose pre-existing short positions.
- Gross short positions should be reported on Form SH (i.e., it is not permitted to net long and short positions).

#### Amendments to the Financial Institutions Order

The SEC's technical amendments<sup>6</sup> to the Financial Institutions Order amend the original order in the following ways:

- The Financial Institutions Order applied to the publicly traded securities of 799 financial firms identified in an appendix to the original order. The amendments modify this list by providing that the Financial Institutions Order applies to the publicly traded equity securities of issuers identified as those of a financial institution by national securities exchanges listing such securities ("Covered Securities"). The SEC expects each national securities exchange to identify financial institutions covered by the Financial Institutions Order and publish a list of these companies on its website.<sup>7</sup> The lists will include banks, savings associations, broker-dealers, investment advisers and insurance companies and will include domestic and foreign companies and their owners.
- The amendments allow financial institutions to opt out of the Financial Institutions Order's prohibition on short sales by notifying the exchange, which will then not include that financial institution in the published list.
- The SEC also modified an exception included in the Financial Institutions Order for bona fide market making and hedging activity in derivatives based on Covered Securities. This exception, which was to expire at 11:59 p.m. ET on September 19, 2008, was extended for the duration of the order and the SEC has clarified that it applies to all market makers, including in the over-the-counter market. The SEC has, however, limited this exception by prohibiting short sales by a market maker if a customer or counterparty position in a derivative is established on or after 12:01 a.m. ET on September 22, 2008, where the market maker knows that the transaction will result in, or increase, an economic net short position by the customer or counterparty in the issued share capital of a covered firm. A market maker relying on this exception is required to publish a notice to that effect on its website.
- The amendments allow short sales resulting from the expiration of futures contracts held prior to the effectiveness of the Financial Institutions Order. The order originally included only an exception for short sales occurring due to automatic exercise or assignment of equity options held prior to effectiveness of the order, upon the expiration of the option.
- The amendments allow short sales by a writer of a call option that effects a short sale occurring as a result of assignments following exercise by the holder.
- The amendments clarify that the prohibition on short sales does not apply to the sales of Covered Securities pursuant to Rule 144 of the Securities Act of 1933.

## Appendix A

### Summary of SEC Recent Regulatory Actions to Address Market Disruptions

The following chart summarizes the SEC's recent regulatory actions designed to address recent market disruptions:

Emergency Order	Summary of Purpose	Issuance Date	Effective Date	Expiration Date
Naked Short Sales Order	Prohibition on "naked" short sales in <i>any</i> security and adoption of new "naked" short selling antifraud rule.	September 17, 2008.	September 18, 2008 at 12:01 a.m. ET.	October 1, 2008 at 11:59 p.m. ET (although extension or additional rulemaking is likely).
Financial Institutions Order (as subsequently amended)	Prohibition on short sales in securities of financial institutions.	September 18, 2008 (amended September 21, 2008).	September 18, 2008.	October 2, 2008 at 11:59 p.m. ET.
Short Sales Reporting Order (as subsequently amended)	Requires institutional money managers with more than US\$100 million under management as of June 30, 2008 to file a Form SH with the SEC on a weekly basis reporting short sales.	September 18, 2008 (amended September 21, 2008).	September 22, 2008 at 12:01 am ET; first Form SH required to be filed on September 29, 2008; first Form SH to be made publicly available by the SEC on October 13, 2008.	October 2, 2008 at 11:59 p.m. ET.
Issuer Repurchase Restrictions Order	Elimination of the "time of purchase" requirement and relaxation of the "volume limitation" requirement under Rule 10b-18.	September 18, 2008.	September 19, 2008 at 12:01 a.m. ET.	October 2, 2008 at 11:59 p.m. ET.

1. See Emergency Order Pursuant to Section 12(k)(2) of the Securities Exchange Act of 1934 Taking Temporary Action to Respond to Market Developments, Release No. 34-58591, dated September 18, 2008, at <http://www.sec.gov/rules/other/2008/34-58591.pdf>.
2. See Emergency Order Pursuant to Section 12(k)(2) of the Securities Exchange Act of 1934 Taking Temporary Action to Respond to Market Developments, Release No. 34-58592, dated September 18, 2008, at <http://www.sec.gov/rules/other/2008/34-58592.pdf>.
3. See Emergency Order Pursuant to Section 12(k)(2) of the Securities Exchange Act of 1934 Taking Temporary Action to Respond to Market Developments, Release No. 34-58572, dated September 17, 2008, at <http://www.sec.gov/rules/other/2008/34-58572.pdf>.
4. See Emergency Order Pursuant to Section 12(k)(2) of the Securities Exchange Act of 1934 Taking Temporary Action to Respond to Market Developments, Release No. 34-58588, dated September 18, 2008, at <http://www.sec.gov/rules/other/2008/34-58588.pdf>.
5. See Emergency Order Pursuant to Section 12(k)(2) of the Securities Exchange Act of 1934 Taking Temporary Action to Respond to Market Developments, Release No. 34-58591A, dated September 21, 2008, at <http://www.sec.gov/rules/other/2008/34-58591a.pdf>.
6. See Emergency Order Pursuant to Section 12(k)(2) of the Securities Exchange Act of 1934 Taking Temporary Action to Respond to Market Developments, Release No. 34-58611, dated September 21, 2008, at <http://www.sec.gov/rules/other/2008/34-58611.pdf>.
7. See [http://www.nasdaqtrader.com/Micro.aspx?id=options\\_sec\\_shortsalelist](http://www.nasdaqtrader.com/Micro.aspx?id=options_sec_shortsalelist) for the NASDAQ list of covered securities, and <http://www.nyse.com/attachment/NYSE%20SS%20ORDERUPDATED.xls> for the NYSE list.

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