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The "Uptick Rule" and Other Measures to
Address Abuses in the CDS Market Are Urgently Needed

As we head into a new year, the worldwide securities and credit markets continue to experience unprecedented meltdowns and turmoil. Financial firms have been particularly hard hit. The SEC with a new chair expected to be confirmed by the Senate shortly needs to take a leadership role in addressing abusive practices affecting the markets and in restoring investor confidence in the markets.

For over six months, we have called on the SEC to reinstate the "Uptick Rule" which helps limit downward spirals by allowing a stock to be sold short only after a rise from its immediately prior price. Despite widespread market participants' calls to do so, the SEC has to date failed to act. We again urge the SEC to reinstate the "Uptick Rule" immediately to address the short selling, bear raids, and the spreading of false rumors that continue to threaten the markets (see our memos of July 1, August 14, September 17, 2008 and November 20, 2008). As we have previously stated, the abolition of the "Uptick Rule" in July 2007 was a major policy error.

A related issue to abusive short selling is speculative and manipulative trades in the CDS market which are adversely affecting the ability of companies to raise and/or refinance debt. As we have previously noted in our memo dated September 22, 2008, the CDS market is being used by speculative traders to purchase CDS protection relating to the debt of an issuer even though they have no risk of loss in connection with a credit default by such issuer. Due to the limited transparency and other factors in the CDS market, speculators can affect the CDS market by quickly purchasing small amounts of CDS protection to drive up the spreads of such CDSs, thereby sending a misleading signal to the marketplace that the credit default risk of an issuer has increased. At the same time, the traders either have or establish a short position on the common stock of the issuer. These trading activities may drive down the prices of the securities of that issuer and adversely affect the ability of that issuer to issue new debt or refinance. The SEC needs to issue a public report of the extent of these speculative trades and abusive tactics and to take action to stop such practices.

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