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CORPORATE GOVERNANCE FORUM

European Securities and Markets Authority (ESMA)
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Subject: Eumedion's response to the consultation paper of ESMA on the evaluation of certain elements of the Short Selling Regulation (ESMA70/145/127)

The Hague, 1 September 2017

Dear members of ESMA,

Eumedion welcomes the opportunity to respond to your consultation paper on the evaluation of certain elements of the Short Selling Regulation (hereafter: consultation paper). By way of background, Eumedion is the Dutch based corporate governance and sustainability forum for institutional investors. Our 65 Dutch and non-Dutch participants represent more than € 5 trillion assets under management. Participants include a wide range of institutional investors; pension funds, mutual funds, asset managers and insurance companies. Some of the topics raised in the consultation paper fall outside the scope of Eumedion. Therefore, we have confined our response to the topics that are the most relevant for Eumedion and its participants; 1) short term restrictions on short selling in case of a significant decline in prices and 2) transparency of net short positions and reporting requirements. Below you will find the answers to the questions raised in the consultation paper with respect to the aforementioned topics.

1. Short term restrictions on short selling in case of a significant decline in prices

Q10: What are your views on the proposal to change the procedure to adopt short term bans under Article 23 of the SSR? Please elaborate.
Before answering this question we would like to make a more general remark. The consultation paper (p. 34) states that an alternative to the proposal to modify the current regime with respect to the

adoption of short term bans on short selling might be the elimination of that power. We believe that ESMA should seriously consider that. Especially, since there is no sufficient supportive evidence for regulatory interference in this area. According to the consultation paper (p. 30) there is little if not any evidence of the effectiveness of those short term bans. At the same time such bans can seriously harm market liquidity and investor's confidence in EU markets. If it is decided that the current regime under article 23 of the Short Selling Regulation needs to be preserved instead of eliminated, we would like to make the following remarks.

Currently, the competent authority of the trading venue where a fall in price of a financial instrument has taken place can adopt a short term ban on short selling that applies to that jurisdiction only. In turn, other competent authorities may decide to adopt similar restrictions in their own jurisdiction, take no action in their own jurisdiction or oppose the measure. As a consequence, short term bans on short selling may differ per Member State. For investors with cross-border investments, it is costly and time-consuming to get familiar with and meet the different short term bans on short selling. Against this background, we support the proposal of ESMA to change the procedure of article 23 of the Short Selling Regulation in order to provide that only the competent national authority of the financial instruments concerned can adopt a short term ban with respect to that instrument that is effective in all Member States. However, that competent authority should be reluctant to use this power and should in our view not use it if there is a reason which justifies the drop in the prices (e.g. unexpected bad financial results). ESMA is also considering whether to propose that other competent national authorities should have any power to oppose a short term ban on short selling (p. 32 of the consultation paper). Given the short duration of the ban, we agree with the vast majority of competent national authorities that such a power should not be introduced.

According to the consultation paper (p. 33) ESMA is contemplating proposing the possibility for competent national authorities to also adopt a short term ban where the trading of the share is halted on a trading venue and the share's indicative/theoretical price calculated by the trading venue shows a significant fall in relation to the closing price on that venue on the previous trading day. We can understand that the proposed measure might contribute to the prevention of disorderly declines in the prices of shares by competent national authorities. Therefore we would not object to the introduction of such a possibility for competent national authorities.

Q11: What are your views on the proposal to change the scope of short term bans under Article 23 of the SSR? Please elaborate.

As already mentioned in our answer to question 10, we believe that ESMA should seriously consider to eliminate the power to adopt short term bans on short selling. If it is decided that the current regime under article 23 of the Short Selling Regulation needs to be preserved instead of eliminated, we would like to make the following remarks. The consultation paper (p. 34) contains several proposals with respect to the scope of short term bans. ESMA mentions on p. 34 of the consultation paper that in order to avoid the circumvention of the ban the scope could be changed from a ban on short selling into a ban on taking or increasing net short positions. It follows from the consultation paper that the extended scope includes short selling and short positons obtained through derivatives,

but excludes index trading. We are not in favour of the proposal to change the scope of the short term bans under article 23 of the Short Selling Regulation into a ban on taking or increasing net short positions. In practice many market participants holding short positions use specific entities for hedging the exposures of other entities within their group. As a result short positons are often covered at the level of the group instead of the level of an individual legal entity and are not resulting in impermissible uncovered short positions.[1] A ban on taking or increasing net short positions instead of a ban on short selling would have profound practical implications for the aforementioned market participants. It would involve significant complexity in terms of calculation and would result in additional investments in IT systems. Besides that we believe that a ban on taking or increasing net short positions would be at odds with the objectives of the Short Selling Regulation. Recital 28 of that Regulation reads as follows "*As this Regulation addresses only restrictions on short selling and credit default swaps to prevent a disorderly decline in the price of a financial instrument, the need for other types of restrictions such as position limits or restrictions on products, which may give rise to serious investor protection concerns, are more appropriately considered in the context of the Commission's revision of Directive 2004/39/EC*". Against this background we believe that the current scope of article 23 of the Short Selling Regulation should be preserved.

Furthermore, ESMA is of the view that the current thresholds set to identify a significant drop in the price falls for shares traded on a trading venue should be kept. We agree with that. With respect to short term bans on other financial instruments, ESMA is considering (among other things) to remove the relevant current thresholds. We have no objections against that.

2. Transparency of net short positions and reporting requirements

Q12: Do you see any reasons to change the current levels of the thresholds regarding the notification to competent authorities and the public disclosure of significant net short positions in shares? Please elaborate.

Yes. As already mentioned in our response to the ESMA's Call for evidence on the evaluation of the Regulation on short selling and certain aspects of credit default swaps (2013) Eumedion generally supports the current levels of the initial thresholds for net short positions in shares. However, we still doubt whether the requirement to report all changes (upwards and downwards) of net short positions at increments of 0.1% is appropriate and results in meaningful information for both market participants and regulators. Against this background and in order to avoid disproportionate compliance costs for notifying market participants, we advise ESMA to consider removing the uneven incremental thresholds. This would result in wider reporting bands and as a consequence in notifications and disclosures which reflect a more meaningful change in the size of a net short position.

[1] See also: ESMA's technical advice on the evaluation of the Regulation (EU) 236/2012 of the European Parliament and of the Council on short selling and certain aspects of credit default swaps (ESMA/2013/614), nr. 116: "*Third, ESMA considers that it is reasonable to conduct calculations as to whether a sovereign CDS position is a covered one at the level of a group rather than at individual legal entity level only when a dedicated entity within that group is tasked with the hedging the exposures of other entities within the group. The principle that a sovereign CDS transaction should not be uncovered would still be respected but this change would cater for circumstances where groups chose to specialise certain activities within particular entities* ".

Q13: Do you see benefits in the introduction of a new requirement to publish anonymised aggregated net short positions by issuer on a regular basis? Can you provide a quantification of the benefit of such new requirement to your activity? Please elaborate.

Just like ESMA, we see benefits in the introduction of a new requirement for competent national authorities to publish anonymised aggregated net short positions in the shares of issuers on a regular basis. Those aggregated positons could be based on the public and non-public notifications received by the competent national authorities. As a result, investors would have better information on the extent to which short selling in the shares of a specific issuer is used and could use that information to base their investment decisions on. The consultation paper (p. 42) correctly states that the introduction of this new requirement would increase costs for competent national authorities. Nevertheless, we believe that the benefits of enhanced transparency could outweigh the costs of implementing this new requirement.

Q14: Do you agree that the notification time should be kept at no later than 15:30 on the following trading day? If not, please explain.

We are not aware of any practical issues with respect to the current notification time.

Q15: Do you agree that the publication time should be changed at no later than 17:30 on the following trading day? Please elaborate.

Currently, the 15:30 deadline applies to both the notification and the disclosure. ESMA is now considering proposing that the timeframe needed for the publication should be of two hours after the notification is received. The reason for that proposal is that approximately half of the competent national authorities are not able to conduct basic checks on the notifications received around the deadline (p. 43 of the consultation paper). In order to avoid the provision of erroneous information to the financial markets, we support ESMA's view that the publication time of the notifications received should be after the notification time. In this respect we would like to note that such an approach is also more in line with the current procedures for the notification and disclosure of major holdings in the Transparency Directive[2].

Q16: What are your views on a centralised notification and publication system at Union level? Can you provide a quantification of the benefit of such centralised notification to your activity? What are your views on levying a fee on position holders to have access to and report through such a centralised system? Please elaborate.

Currently, the process for registration and for submitting notifications is not harmonised across the Union. For institutional investors with net short positions in different Member States, it is costly and time-consuming to meet all these different requirements. Therefore we are in favour of a pan-European notification and publication system. Such a system would save institutional investors a lot of time and money and can contribute to achieving the overall aim of the Short Selling Regulation: uniform application throughout the European Union of the obligations stemming from that regulation[3].

[2] Art. 12 (7) of that directive reads as follows: "*A home Member State may exempt issuers from the requirement in paragraph 6 if the information contained in the notification is made public by its competent authority, under the conditions laid down in Article 21, upon receipt of the notification, but no later than three trading days thereafter.*"

[3] See recital 3 of the Short Selling Regulation *"It is appropriate and necessary for those rules to take the legislative form of a regulation in order to ensure that provisions directly imposing obligations on private parties to notify and disclose net short*

At this stage, it is rather difficult to quantify the benefits of such a system precisely since the details of the new regulation are not clear yet. Our answer is therefore limited to some high level comments.

According to the consultation paper (p. 44) the new set-up and operational costs of a pan-European notification and publication system could be partially balanced by setting up a fee for position holders to have access to and report through such a system. We are not in favour of the introduction of such a fee. A pan-European notification and publication system will help to achieve the underlying objectives of the Short Selling Regulation: uniform disclosure of net short positions throughout the Union.[4] The consultation paper (p. 44) correctly states that such a system would lead to a more harmonised reporting mechanism and would reduce the administrative burden and costs that position holders currently incur when submitting notifications to multiple reporting systems. In other words, such a system would promote supervisory convergence and would solve the existing cross-border problems that are mentioned above. Eumedion regards it as a task of the national competent authorities to facilitate this while keeping the administrative burden for investors as low a possible. Against this background we are of the opinion that the new set-up and operational costs of a pan-European notification and publication system should be completely borne by the national competent authorities and not be partially balanced by a fee for position holders.

Q17: Which other amendments, if any, would you suggest to make the notification less burdensome?
As already mentioned in our response to ESMA's Call for evidence on the evaluation of the Regulation on short selling and certain aspects of credit default swaps (2013), some of our participants consider it a very burdensome task to constantly monitor and calculate (using publicly available information) net positions regarding a share, where it is one of many in an index, basket or exchange traded fund (ETF). Therefore we are still of the opinion that the Short Selling Regulation should be amended in such a way that indices, baskets and ETFs are only included in the calculation of net positions insofar as a set threshold is crossed. For more details we refer to our previous response.

Q18: Do you agree that the identification code of the position holder should be the LEI and that such code should be mandatory for legal entities? Please elaborate.
In ESMA's view, the Legal Entity Identifier (LEI) is an internationally established code for financial markets that should replace the Bank Identifier Code (BIC) code currently in place (p. 45 of the consultation paper). Against this background, we have no reservations regarding the use of the LEI for legal entities.

Q19: What are your views on the method that should be favoured, the nominal method or the duration-adjusted method as described above? In the latter case, do you think that the thresholds should be changed? Please elaborate.
We prefer option a (the "nominal method") since this is the least complex method.

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positions relating to certain instruments and regarding uncovered short selling are applied in a uniform manner throughout the Union".
[4] See recital 3 of the Short Selling Regulation.

If you would like to discuss our views in further detail, please do not hesitate to contact us. Our contact person is Diana van Kleef (diana.vankleef@eumedion.nl, tel. 070 2040 302).

Yours sincerely,

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