

Comments

on the European Securities and Markets Authority (ESMA) consultation paper on the evaluation of certain elements of the Short Selling Regulation (Regulation (EU) 236/2012)

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Comments on the Consultation Paper of the ESMA the evaluation of certain elements of the Short Selling Regulation

A. General comments

We, the German Banking Industry Committee (GBIC), representing more than 1,700 banks in Germany, would like to take the opportunity to bring to your attention our remarks regarding the ESMA consultation paper on the evaluation of certain elements of the Short Selling Regulation (Regulation (EU) 236/2012).

As a general remark, we would like to point out that we intend to address only a few of the most significant aspects of the consultation paper. However, we would also like to stress that the non-response to or omission of certain aspects of the consultation paper in our official comments should not be considered as approval or disapproval regarding those aspects.

B. Comments on individual questions

Question 2: Considering the new regulatory framework under the MiFID II/MiFIR, how do you suggest addressing the issue of the membership requirement in relation to those instruments that will remain pure OTC instruments despite the MiFID II/MiFIR framework? Should the membership requirement not apply to those pure OTC instruments? Please provide justifications.

We expect that despite the MiFID II/ MiFIR framework certain financial instruments will remain pure OTC instruments, e. g. certain credit default swaps. Hence, they will not be eligible for the market making exemption. We strongly agree, that "Market making activities play a crucial role in providing liquidity to markets within the Union and market makers need to take short positions to perform that role. Imposing requirements on such activities could severely inhibit their ability to provide liquidity and have a significant adverse impact on the efficiency of the Union markets. [...] It is therefore appropriate to exempt natural or legal persons involved in such activities from requirements which could impair their ability to perform such a function and therefore adversely affect the Union markets [...]"¹. Moreover, by trading derivative instruments the liquidity of those instruments as well as the underlying financial instruments will be affected positively. Additionally, market making activities also improve the quality of market pricing in those instruments and in the underlying financial instruments respectively. We also consider that, a short position can be taken irrespective of the (OTC) market the financial instrument has been traded on. Trades, which are comparable in their economic substance, should have the same legal consequences. Furthermore, the ability of NCAs to restrict short selling in exceptional circumstances will not interfere with the non-application of the membership-requirement. We also strongly agree with the German competent authority (BaFin) when it says that: "If market makers in OTC-instruments are not able to qualify for the exemption they are subject to all the requirements of the Short Selling Regulation, in particular the requirements to cover short sales by locate arrangements, other enforceable claims etc., they will face extra barriers and costs to conducting their market making activities. This will adversely affect market liquidity and efficiency to the detriment of end users of those markets."² Therefore, and in light of the importance of market making activities and a well-functioning financial market, it is appropriate to abrogate the membership-requirement.

¹ Recital 26 of Regulation (EU) 236/2012.

² ESMA, ESMA/2013/765, p. 5.

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Q6: Do you think it would be appropriate to enlarge the set of financial instruments eligible for the exemption for market making activities? If so, which financial instrument(s) would you suggest? Please provide justifications.

Shares and sovereign debt are used for hedging products other than equity and sovereign debt derivatives. It is a common strategy for market makers in corporate bonds to hedge their market making risks via trades in the relevant sovereign debt. Without a clear exemption, the corporate bond market maker would face additional costs and problems in doing so. Similar arguments apply to market making in convertible bonds and subscription rights. Denying the exemption can inhibit market makers' ability to provide liquidity in those financial instruments³. Therefore, we suggest enlarging the set of financial instruments eligible for the exemption for market making activities to corporate bonds, convertible bonds and subscription rights.

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³ ESMA, ESMA/2013/765, p. 6.