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Mr. Carlo Comporti
Secretary General

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Consultation Paper on CESR Proposal for a Pan-European Short Selling Disclosure Regime (CESR/09-581)

Dear Mr. Comporti,

BVI¹ welcomes the opportunity to submit its opinion on CESR's proposal for an EU-wide transparency regime in relation to short selling.

General remarks:

BVI members unanimously endorse CESR's view that the potential for market abuse inherent in short selling activities must be effectively mitigated and in this regard, consider the move towards greater transparency an appropriate measure.

It must be borne in mind, however, that short selling represents a generally acknowledged trading technique which is essential for effective risk management by asset managers and other financial institutions. CESR itself admits that short selling plays an important role in financial markets by

¹ BVI Bundesverband Investment und Asset Management e.V. represents the interest of the German investment fund and asset management industry. Its 88 members manage currently assets in excess of EUR 1.5 trillion both in mutual funds and mandates. For more information, please visit www.bvi.de.

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contributing to efficient price discovery, increasing liquidity and reducing the potential for market bubbles². Moreover, the risk of abusive behaviour or other market disruptions associated with short selling pertains in the first place to uncovered sales of equities (so-called naked short selling) and is to much lesser extent attributable to synthetic short sales through derivatives³.

Therefore, when discussing a prospective pan-European disclosure regime, we call upon CESR to take due account of the following:

- Disclosure duties in relation to short positions must be proportionate to the risk of market abuse or disruption associated with the affected trading activity. In particular, regulated market participants such as fund and asset managers who are bound by legal restrictions on eligible assets and trading techniques must not be subject to overly burdensome disclosure obligations aiming at identifying risks arising outside the scope of their operations⁴.
- The applicable thresholds for disclosure must generate meaningful information which is necessary for the authorities to monitor the risks for functioning and integrity of financial markets and to take any averting measures in that respect. It is essential to avoid a regime which churns out bulks of reports on continuous basis as this would overstrain both market participants in complying with the disclosure duties and market authorities in overseeing the disclosure results.
- In order to keep the implementing burden for market participants at a reasonable level, disclosure regime for short positions should be designed in closest possible alignment with the notification duties for long positions under the Transparency Directive. Even if harmonisation of applicable thresholds appears difficult, convergence should be sought in relation to timing and other formal aspects of disclosure. Moreover, it is essential that the prospective EU regime be recognised as an exclusive approach to supervision of short selling in normal circumstances. Any rights to impose or retain additional restrictions at national level must be clearly limited to

² Cf. paragraph 11 of CESR consultation paper.

³ Cf. paragraph 2.1 and Annex II of IOSCO Final Report on Regulation of Short Selling dated June 2009.

⁴ Under German law, for instance, physical short sales are permitted only for hedge funds which form only a marginal fraction of the German fund market.

temporary emergency situations and subject to justification duty by the intervening authority.

Specific comments:

With regard to the consultation questions raised by CESR, we would like to provide the following replies:

Q1: *Do you agree that enhanced transparency of short selling should be pursued?*

Provided that the above mentioned aspects are sufficiently accounted for, we agree that enhanced transparency might be an appropriate method to strengthen supervisory controls of short selling activities.

In these terms, however, we are of the opinion that disclosure towards regulators should be sufficient in order to achieve the objective of better supervision. Public transparency of short position, if considered desirable, should be organised on the basis of anonymous disclosure of aggregated short positions by the regulators. For details, please refer to our comments on question 5 below.

Q2: *Do you agree with CESR's analysis of the pros and cons of flagging short sales versus short position reporting?*

Q3: *Do you agree that, on balance, transparency is better achieved through a short position disclosure regime rather than through a "flagging" requirement?*

Most BVI members agree that a regime based on short position reporting to regulators is preferable to flagging requirements for short sale orders.

Q4: *Do you have any comments on CESR's proposals as regards the scope of the disclosure regime?*

We assent to CESR's suggestion that the pan-European disclosure regime should apply to positions held in all EEA issuers traded on regulated markets or MTFs and in addition, cover non-EEA issuers solely or primarily admitted to trading on such platforms. Furthermore, the scope of the regime should not be limited by sector or by the nature of the security.

Q5: *Do you agree with the two tier disclosure model CESR is proposing? If you do not support this model, please explain why you do not and what alternative(s) you would suggest. For example, should regulators be required to make some form of anonymised public disclosure based on the information they receive as a result of the first trigger threshold (these disclosures would be in addition to public disclosures of individual short positions at the higher threshold)?*

We have major reservations against the two tier disclosure system proposed by CESR.

We do not object in principle to the private disclosure of short positions towards regulators provided that the applicable thresholds are set at a reasonable level (cf. our response to question 7). Reporting to regulators appears appropriate to facilitate effective supervision of short selling and the associated risks to the functioning and integrity of financial markets.

However, we reject the proposed public disclosure of individual short positions as in our view, it might lead to herding behaviour and disrupt trading activities in the affected shares. The risk of herding appears particularly relevant in cases where influential market participants make significant short positions transparent to the market. Moreover, most BVI members feel that public disclosure on individual basis might be detrimental to the market mechanism of efficient price discovery and impede effective allocation of assets.

CESR argues that public disclosure of short positions might contribute to the discovery of over-valued shares and deter aggressive short sellers. As for the second point, we doubt whether public disclosure would provide a measure of deterrence where disclosure to regulators entailing the risk of being charged for market abuse fails to do so. The first aspect, however, can be equally satisfied by publication of aggregated figures without disclosing the identity of individual investors.

Therefore, should disclosure of significant short positions to the public be deemed appropriate, we strongly favour a system providing transparency on anonymous basis by revealing aggregated short positions in specific shares. Such market information could be provided by the regulators on the basis of individual reports submitted to them or facilitated via a central database established at the level of CESR.

Q6: *Do you agree that uniform pan-European disclosure thresholds should be set for both public and private disclosure? If not, what alternatives would you suggest and why?*

We fully agree with the proposed harmonisation of disclosure thresholds and call for consequent application of the maximum harmonisation approach also with regard to the remaining elements of the transparency regime.

Q7: *Do you agree with the thresholds for public and private disclosure proposed by CESR? If not, what alternatives would you suggest and why?*

The initial threshold of 0.10% proposed by CESR for the purpose of private disclosure is set at an extremely low level. It is very likely that such a low trigger will generate floods of reports requiring frequent updates which could overstrain the resources available to regulators. Also, as the proposed system is meant to effectuate disclosure of significant short positions, it appears disproportionate to demand reporting already from the level of 0.10%. Holdings of that magnitude have only very limited, if any, impact on price formation and hence, should be considered irrelevant for the purpose of detecting market abuse.

In our view, the threshold for private disclosure to regulators cannot be set below the level of 0.25% which has been deemed sufficient by many regulators to ensure transparency of short sales in financial sector during the latest market crisis. Indeed, as this threshold has applied in emergency situations and in respect of a limited number of issuers, we think it appropriate to agree on a higher threshold for permanent disclosure which, in our opinion, should be set at 0.50%. Subsequent notifications should be due no earlier than in case of incremental increase (or decrease) of holdings by further 0.50% (meaning at 1%, 1.5%, etc.).



As regards disclosure of short positions to the public, the majority of BVI members strongly advocates a system facilitating information on aggregated and anonymous terms. If, despite our arguments against it, market disclosure on individual basis were to become mandatory, we urge CESR to reconsider its proposal for the initial trigger threshold and in order to avoid confusion among market participants by frequent reporting, to set it no lower than 1.0%. Further details of a public disclosure regime should be closely aligned with the Transparency Directive in order to facilitate practical implementation by investors.

Q8: *Do you agree that more stringent public disclosure requirements should be applied in cases where companies are undertaking significant capital raisings through share issues?*

Q9: *If so, do you agree that the trigger threshold for public disclosures in such circumstances should be 0.25%?*

We admit that public companies might be more vulnerable to market abuse in capital raising situations. However, information on relevant short sale activities provided under the private disclosure regime should be sufficient to detect potentially abusive investments and to allow for adequate measures to be taken by regulators.

Q10: *Do you believe that there are other circumstances in which more stringent standards should apply and, if so, what standards and in what other circumstances?*

We have no suggestions in this respect.

Q11: *Do you have any comments on CESR's proposals concerning how short positions should be calculated? Should CESR consider any alternative method of calculation?*

In general, BVI members agree with the proposed approach to calculation of short positions. In relation to derivative contracts to be taken into account, however, it is essential that CESR members develop a common understanding of financial instruments which "create an economic exposure to the issued share capital of the issuer". Uncertainties pertaining to the relevance of specific derivatives (e.g. put options or repurchase agreements) must be

sorted out at EU level as they have direct impact on the results of calculation and hence, might impair the quality of information submitted to regulators.

Moreover, in the context of the fund management industry, it is important to clarify the meaning of “legal entity level” in the sense of paragraph 49. In our view, the netting calculation should be conducted at the level of the management company for all funds under management irrespectively of the legal form these vehicles take (contractual or corporate type funds).

Q12: *Do you have any comments of CESR’s proposals for the mechanics of the private and public disclosure?*

Q13: *Do you consider that the content of the disclosures should include more details? If yes, please indicate what details (e.g. a breakdown between the physical and synthetic elements of a position).*

As regards private disclosure to regulators, we are of the opinion that regulated and supervised entities such as fund and asset managers should be generally allowed to report their holdings to the competent authorities of their respective home Member States. Such reports should then be shared between the regulators or filed with a central data repository installed by CESR. From our perspective, creation of a central database represents the best suitable solution as it would simultaneously allow for generation of aggregated public disclosure above the relevant thresholds.

As explained above, we oppose to the suggestion of individual public reporting by market participants. However, should this option be favoured by CESR members, we call upon them not to require identification of the short position holder in order to avoid adverse effects for the functioning of financial markets (for details, cf. our reply to Q5).

Q14: *Do you have any comments on CESR’s proposals concerning the timeframe for disclosures?*

We strongly recommend alignment of short selling reporting modalities with the provisions of the Transparency Directive which requires notification within four trading days after the relevant event⁵. A timeframe of T+4 would accommodate most settlement cycles, thus ensuring that reports are based on legal holdings and not just on entries in trading books.

⁵ Cf. Art. 12 paragraph 2 of the Transparency Directive.

Q15: *Do you agree, as a matter of principle, that market makers should be exempt from disclosure obligations in respect of their market making activities?*

Q16: *If so, should they be exempt from disclosure to the regulator?*

BVI members see no reason to exempt market makers from the scope of reporting obligations. As market makers are major players in the short selling market, such systematic exemption would render disclosure of short positions incomplete and thus, compromise the value of information provided to regulators.

Q17: *Should CESR consider any other exemptions?*

BVI members prefer a disclosure regime which offers little room for exemptions.

Q18: *Do you agree that EEA securities regulators should be given explicit, stand-alone powers to require disclosure in respect of short selling? If so, do you agree that these powers should stem from European legislation, in the form of a new Directive or Regulation?*

We agree with CESR that the new transparency regime for short selling should be construed and consistently implemented at EU level in order to reduce the operational burden hampering cross-border investment activities. To best achieve these objectives, however, the disclosure obligations should be stipulated in detail by binding legal measures which preferably should take the form of an EU Regulation in order to avoid divergences in national implementation between Member States. In this context, the EEA securities regulators should be entitled to exercise powers conferred upon them by EU law, but not be able to inflict additional or deviating requirements upon market participants.

In substantive terms, we would like to reiterate our request for as close as possible alignment with the Transparency Directive as regards timing and other formal aspects of disclosure.



We hope that our remarks will help CESR to adjust and refine its concept of a pan-European disclosure regime for short positions and remain at your disposal for any questions that may arise.

Yours sincerely

BVI Bundesverband Investment und Asset Management e.V.

Signed:
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Signed:
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