

16 August 2010

CESR's consultation on Transaction reporting on OTC derivatives and extension of the scope of transaction reporting obligations

Reply of NASDAQ OMX

The NASDAQ OMX Group, Inc. delivers trading, exchange technology, listings and other public company services and post-trading services across six continents. It lists approximately 3,700 companies from 50 countries and from all industry sectors. NASDAQ OMX offers various capital raising and trading solutions to companies around the globe, including its U.S. listings market, NASDAQ OMX Nordic, NASDAQ OMX Baltic, First North, U.S. 144A, NordPool and N2EX. NASDAQ OMX Nordic and Baltic include exchanges in Stockholm, Helsinki, Copenhagen, Iceland, Tallinn, Riga and Vilnius. NASDAQ OMX offers trading across multiple asset classes including equities, derivatives, debt, commodities, structured products and ETFs. NASDAQ OMX also offers post-trading services in the form of central counterparty derivatives clearing. NASDAQ OMX Group technology supports the operations of about 70 exchanges, clearing organizations and central securities depositories in more than 50 countries.

NASDAQ OMX is pleased to have the opportunity to comment on issues relating to the future organisation of transaction and position reporting on OTC derivatives as this is an important step in creating more stable, fair and orderly financial markets.

Executive summary

NASDAQ OMX is of the opinion that the MiFID regime should apply to reporting obligations for the purpose of reporting OTC derivative transactions. These obligations could be dealt with by transaction repositories for the account of investment firms but there should be no exclusivity of transaction repositories in this respect.

Moreover, it is crucial to ensure that the scope of the reporting obligations expands to all OTC transactions on derivative instruments that can directly or indirectly influence the price of an underlying financial instrument admitted to trading on a regulated market or MTF. In this perspective, it is not certain that linking the transaction reporting regime to the scope of another instrument, like EMIR, would be appropriate.

It is also crucial that the same regime applies to all transactions on a given derivative instrument or any equivalent instrument, be they on exchange or negotiated on other trading venues or bilaterally, cleared or non-cleared.

We agree with CESR that it is also essential for this regime to cover all transactions that could potentially constitute market abuse and that the exact scope of the instruments should not be exhaustively set out in the Level 1 text but could be expanded through Level 2 measures or ESMA technical standards.

Detailed replies

1. Possible ways to organise transaction and position reporting on OTC derivatives

Question 1: Do you agree with the solution proposed by CESR for the organisation of transaction and position reporting on OTC derivatives?

Question 2: Do you have any other views on the possible ways to organise transaction and position reporting on OTC derivatives?

We are in favor of option 2 i.e. the MiFID regime would apply to reporting obligations for the purpose of reporting OTC derivative transactions but these obligations could be dealt with by Transaction Repositories for the account of investment firms.

We also want to underline that CCPs already offer the services of trade repositories for the transactions that they clear and there should be no exclusivity of Trade Repositories in providing transaction reports and assisting firms to comply with their reporting obligations. Exclusivity of trade repositories would indeed create duplication and additional costs for the industry without obvious benefits. In addition, the whole regime would be significantly affected depending upon whether there would be one or several Trade Repositories which is unclear currently.

We also wish to underline that in order to achieve the objectives set by the G20 to create more stable financial markets and in particular ensure knowledge of the OTC transactions and where systemic risk is building up, it is crucial to ensure that the scope of the reporting obligations expands to all OTC transactions on derivative instruments that can directly or indirectly influence the price of an underlying financial instrument admitted to trading on a regulated market or MTF or any instruments that can be negotiated in lieu of such underlying instrument (e.g. indices)

In this perspective, it is not certain that linking the transaction reporting regime to the scope of another instrument, like EMIR, would be appropriate. Especially, in view of the fact that the exact scope of EMIR is at present unclear. In order for regulators to ensure a proper monitoring of markets, the transaction reporting regime to be built may have to apply to instruments that will not be included in the scope of EMIR, especially if such scope would only cover instruments for which a central clearing obligation is imposed.

Furthermore, for the sake of efficient monitoring of markets and in order to avoid regulatory arbitrage between venues, it is also crucial that the same regime applies to all transactions on a given derivative instrument or any equivalent instrument (e.g. CFDs), be they on exchange or negotiated on other trading venues or bilaterally, cleared or non-cleared. Also, transactions on such instruments should be reported whether they are carried out by investment firms or non-authorised firms.

2. Extension of the scope of transaction reporting obligations

Question 3: Do you agree with the extension of the scope of transaction reporting obligations to the identified instruments?

We agree with CESR that the MiFID transaction reporting regime is an important supervisory tool to detect and counter market abuse, and that it is therefore essential for this regime to cover all

transactions that could potentially constitute market abuse, including the ones on instruments admitted to trading only on MTFs and not only shares, but also other financial instruments like bonds and derivatives.

We also wish to underline that the suspicious transactions reporting obligations have also to have such broad scope in order to be effective.

We agree with CESR that the exact scope of the instruments should not be exhaustively set out in the Level 1 text but could be expanded through Level 2 measures or ESMA technical standards. This is indeed necessary in order to ensure that the scope of the reporting obligation can be more easily adjusted to respond to innovation in the market.

NASDAQ OMX has replied to other recent consultations of the European Commission on short selling and market abuse as well as the CESR consultation on transaction reporting under MIFID (replies are attached). Specific responses made to such consultations dealing with transaction reports and position reporting should be taken into account in the context of the reporting obligation for OTC derivative transactions.

In particular, information on individual positions may open up for wider abusive behaviour, such as front running and squeezes. Such behaviours have serious impact on price formation and the necessary measures should be taken to make sure that position reporting arrangements minimise risks in this respect.

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July 2010

European Commission

Public Consultation on

A revision of the market abuse directive (MAD)

Reply from NASDAQ OMX

The NASDAQ OMX Group, Inc. delivers trading, exchange technology, listings and other public company services and post-trading services across six continents. It lists approximately 3,700 companies from 50 countries and from all industry sectors. NASDAQ OMX offers various capital raising and trading solutions to companies around the globe, including its U.S. listings market, NASDAQ OMX Nordic, NASDAQ OMX Baltic, First North, U.S. 144A, NordPool and N2EX. NASDAQ OMX Nordic and Baltic include exchanges in Helsinki, Copenhagen, Stockholm, Iceland, Tallinn, Riga and Vilnius. NASDAQ OMX offers trading across multiple asset classes including equities, derivatives, debt, commodities, structured products and ETFs. NASDAQ OMX also offers post-trading services in the form of central counterparty derivatives clearing. NASDAQ OMX Group technology supports the operations of about 70 exchanges, clearing organizations and central securities depositories in more than 50 countries.

NASDAQ OMX appreciates the opportunity to provide comments in the process of the review of the MAD. MAD is one of the fundamental pieces of legislation for maintaining integrity of securities markets. It is important that MAD is appropriately calibrated and it is equally important that the rules are enforced in an efficient and harmonized manner across Europe. Please find below our comments to the specific questions in the consultation document.

A. EXTENSION OF THE SCOPE OF THE DIRECTIVE

(1) Should the definition of inside information for commodity derivatives be expanded in order to be aligned with the general definition of inside information and thus better protect investors?

NASDAQ OMX Commodities provides access to the world's largest power derivatives exchange and one of Europe's largest carbon markets. NASDAQ OMX acquired Nord Pool ASA end of May 2010. All commodities trading is cleared through NASDAQ OMX clearing house. In partnership with Nord Pool Spot, NASDAQ OMX Commodities also offers a cleared physical UK power market, N2EX. The ambition is to launch power derivatives in the UK in the fall of 2010. NASDAQ OMX Commodities, including the subsidiary Nord Pool ASA, has more than 390 members from 22 countries across a wide range of energy producers and consumers, as well as financial institutions.

We answer this question 1 from the perspective of the above described business that we operate within the business area NASDAQ OMX Commodities.

As a general comment, we believe it is necessary for the Commission to recognize that although commodities markets may sometimes be categorized in one group, commodity markets and commodity types are different. The proposed definition may not be suitable for all types of commodities markets, depending on their characteristics and may explain why one definition may *not* suit all commodities markets. From our experience, we believe that a market abuse regime in combination with a transparency regime clearly contribute to the well functioning of our markets. For our markets, we believe that information disclosure is natural for the market participants and does

not pose specific concerns or difficulties. For this reason we do support moving forward with both market abuse regimes and transparency regimes for the gas and electricity markets and we strongly encourage a coordinated approach by authorities responsible for different aspects of these markets.

Yes, we are in favor of changing the definition. It is relevant to insert a notion of effect on prices as this will provide a better link between information disclosure obligations and insider trading/market manipulation. It will be more appropriate to have a regime where the enforcement of abusive and manipulative behavior is related to if there was an impact on prices. Nevertheless, the definition may still need some tailoring in order to take account of the fact that many participants in commodity derivatives markets are also participants in the underlying market, and they have knowledge of their own plans and strategies for trading in the underlying market. The terms "issuer" and "price sensitive information" have to be clarified. This may however be an issue that is most appropriately addressed at the level of enforcement and it may be appropriate for ESMA/ERGEG to produce guidance in order to clarify the application of MAD related to commodities.

Also from the perspectives of power and carbon markets, it is necessary to couple a market abuse regime with a transparency regime. We believe the ongoing initiatives within European Commission DG Energy need to address this issue. The current open consultation on measures to ensure transparency and integrity of wholesale markets in electricity and gas does not include a transparency regime, which is unfortunate. It is however understood that ERGEG and ENTSO-E are assigned to prepare a comitology guideline on fundamental data transparency. Such work is of utmost importance and we look forward to the involvement of the industry in such work, and that a public consultation takes place before it is finalized.

One comment on the proposed wording of the definition of inside information for commodities: It seems to us that the wording suggests a distinction between the price effect on a derivative compared to the underlying, in that the price effect needs to be significant only for derivatives. It is unclear to us whether this is an intended differentiation or not? The part of the definition in MAD that is not specific to commodities seems to not make a distinction. We do not see a reason to differentiate for commodities markets. If there are such reasons they should be explained.

(2) Should MAD be extended to cover attempts to manipulate the market? If so why? Is the definition proposed in this consultation document based on efficient criteria to cover all cases of possible abuses that today are not covered by MAD?

Yes. Well functioning financial markets are dependent on the participants in the market trusting that the price formation process and the trading takes place in an efficient and fair manner. Any behavior with the effect of manipulating the market should be sanctioned and for this reason it also seems logical that attempts to distort markets by manipulation are not tolerated, irrespective of whether the actual attempt was successful in a specific case or not. The definition seems efficient.

When the scope of the MAD is extended to attempts to market manipulation, supervision and enforcement also need to be extended. Supervisors need to be equipped with sufficient resources and tools to enable efficient enforcement of the MAD. It is important that any attempts to abuse or manipulate the market are not tolerated and are sanctioned.

(3) Should the prohibition of market manipulation be expanded to cover manipulative actions committed through derivatives?

Yes. A full enforcement of market manipulation requires that also derivatives come within the scope. MAD should be extended to also cover manipulation committed through any derivative when such behavior can have an impact on the value of an instrument admitted to trading on a regulated market or an MTF.

(4) To what extent should MAD apply to financial instruments admitted to trading on MTFs?

The parts of MAD that include the „criminal“ rules on trading activities should apply to financial instruments admitted to trading on MTFs. This would support the well functioning of and the trust in those markets.

However, most of the parts of MAD that are targeted at the issuers should not be extended to apply to the issuers admitted to trading only on MTFs. A disclosure regime is a basic requirement for operating a well functioning market. That is why all MTFs have basic rules on disclosure requirements for the issuers, be it in the national law and/or in the private rule book set up by the market operator. This is the case for NASDAQ OMX MTF First North in the Nordics. However, as the MTFs provide a listing venue that is an alternative to the regulated markets, the further disclosure rules are, and should be, lighter than on the regulated market. Otherwise the MTFs will not serve the function as a market where smaller issuers may access finance on the securities markets and grow under conditions and rules that are tailored for their needs. For instance, on First North there are several segments specifically adapted to the needs of the different types of issuers. The First North special segment „Premier“ can be mentioned. The Premier segment rule book is tailored for issuers aiming to switch to the main market, the regulated market, so the rules are close to the main market rule book. Issuers that select the Premier segment for instance comply with IFRS. Issuers can select the Premier segment as a preparatory step before switching to the main market. If all the MAD rules targeted at issuers would be extended to MTFs, the MTFs would lose their function as a market place where smaller issuers can access finance. If one aims at facilitating the access to finance for SMEs, it seems counterproductive to extend all the rules for issuers listed on regulated markets also to issuers listed on MTFs. This will introduce an additional obstacle for smaller issuers to even list on the alternative MTFs.

The MAD provisions that seem appropriate to extend to MTFs seem to be Articles 2-5, 6.1-3 sections 1 and 2, 6.6, 6.7, 6.9 and 8. Article 9 should also apply in relation to the provisions that are extended to MTFs.

Parts that should not be extended to MTFs include the obligations to report managers' transactions and to maintain an insiders list (Article 6.3 section 3, 6.4, 6.5 and 6.8). The benefits of these provisions do not match the compliance costs for smaller issuers. Especially when it comes to insiders lists it should be considered sufficient that the competent authorities have the power to ask for the information as needed.

(5) In particular should the obligation to disclose inside information not apply to issuers who only have instruments admitted to trading on an MTF? If so why?

Obligation to disclose inside information is a basic feature of any well functioning market. All MTF markets already have disclosure rules. They are nevertheless not harmonized, so to extend the MAD requirements on disclosure of inside information would have the benefit of improving the level playing field. See also the reply to Q 4 above.

(6) Is there a need for an adapted regime for SMEs admitted to trading on regulated markets and/or MTFs? To what extent should the adapted regime apply to SMEs or to "companies with reduced market capitalisation" as defined in Prospectus Directive? To what extent can the criteria to be fulfilled by SMEs as proposed for such an adapted regime be further specified through delegated acts?

No. It is more relevant to distinguish between issuers listed on MTFs and RMs respectively, rather than to distinguish between issuers of different sizes. The business model of the so called „junior“ MTFs is already adapted to support the specific needs of smaller issuers. When these MTFs are subject to an appropriately level of regulation they can continue to cater for these issuers.

Furthermore we believe that introducing a specific layer of rules on the regulated markets pose the risk of deteriorating market quality on those markets. Those issuers that decide to list on the regulated market, be it directly or moving up from an alternative MTF venue, have made the choice to join the highest quality market. The MTF market is the already existing choice for other companies, irrespective of size.

In addition, it has several times been questioned whether the issuers listed on a regulated market would in fact experience that a few reductions in the regulatory burden would make a significant

difference. It seems that other aspects of access to finance are higher on the wish-list of issuers, such as better opportunities for investment funds to invest in smaller issuers, less strict language regimes enabling smaller issuers on regulated markets to avoid translation costs by using only English for disclosures and better corporate governance responding to demands from investors.

Should nevertheless the Commission believe that a specific regulatory segment on the regulated market is a good option and choose to progress with such a regime, the most important thing is to apply one single definition of SMEs across Europe. There should be one threshold, thus placing all issuers of the same size on the same footing. This definition should be the same in all relevant legal acts (such as the Transparency and Prospectus Directives). It has been proposed that the „small“ companies should be singled out in relation to the size of their home market.¹ However, this option would not provide all smaller issuers of the same size with the same opportunities. Investors that wish to know what regime a specific issuer complies with cannot rely on the size of the company but also needs to check with this issuer's home market. It will create a fragmented and confusing situation that does not support smaller companies. For aspects related to smaller issuers we strongly encourage the Commission to coordinate sufficiently with especially the ongoing review of the Transparency Directive.

1 <http://www.mazars.com/content/download/37683/867875/version/2/file/SBA-smiles-english.pdf>

See also the reply to Q 4 above.

B. ENFORCEMENT POWERS AND SANCTIONS

(7) How can the powers of competent authorities to investigate market abuse be enhanced? Do you consider that the scope of suspicious transactions reports should be extended to suspicious orders and suspicious OTC transactions? Why?

The scope of STRs obligations should be extended to suspicious orders and suspicious OTC transactions. With this, market abuse cases will more easily be detected. It will also facilitate the detection of attempted market manipulation, as proposed in the consultation paper. On OTC, it is important to recognize that these transactions should definitely be within the scope. Otherwise there is a gap where market abuse can take place outside the regulated trading venues. Generally, competent authorities should continue to develop methodology for cross-border cooperation and they need to be equipped with sufficient resources in order to maintain the efficient enforcement of market abuse that is crucial for the trust in the markets.

In addition, we wish to underline the importance of ensuring strict and proper enforcement of STR obligations and to allocate sufficient resources to investigate the suspicious transactions that are reported to authorities. We note that already today article 6.9 of MAD requires reports on suspicious transactions in financial instruments.

(8) How can sanctions be made more deterrent? To what extent need the sanction regimes be harmonised at the EU level in order to prevent market abuse? Do you agree with the suggestions made on the scope of appropriate administrative measures and sanctions, on the amounts of fines and on the disclosure of measures and sanctions? Why?

Sanction regimes need to be sufficiently harmonized in order to prevent driving criminal activities to markets where sanctions are not as strict as in other markets. Ensuring a uniform application of the sanctions is important. ESMA should have an important role to play to achieve this.

As far as legal certainty allows, administrative sanctions should be available to authorities, as it provides better opportunities for quicker handling than criminal sanctions. Also, where possible, linking fines to the benefit gained provides a good basis for a harmonized sanction regime. In our view, publishing the measures or sanctions and who they relate to, is useful.

Regarding sanctions, in addition, we propose that ESMA is empowered with the possibility to act on behalf of a national authority, when this authority does not take action and carry out investigations as needed. To maintain the integrity of European markets, an appropriate regulatory system is a prerequisite, and so is prompt and adequate enforcement of the rules in place. It must not be tolerated that ESMA can passively observe suspicious behavior in the market continuing without a power to act. Such a possibility to substitute the national authority should be coupled with a power to address the insufficiently active national authorities (see Q 9 below).

(9) Do you agree with the narrowing of the reasons why a competent authority may refuse to cooperate with another one as described above? Why? What coordination role should ESMA play in the relations among EU competent authorities for enforcement purposes? Should ESMA be informed of every case of cooperation between competent authorities? Should ESMA act as a binding mediator when competent authorities disagree on the scope of information that the requested authority must communicate to the requesting authority?

With both market fragmentation within Europe and with internationalization of markets increasing, it is absolutely necessary to ensure that authorities can and do cooperate efficiently. ESMA should be given a strong role in as far as possibly facilitating and encouraging more and better cooperation. ESMA should have a role to facilitate multilateral cooperation. For bilateral cooperation it could bring added value if ESMA was informed and thus could detect links between ongoing investigations that would otherwise not be detected.

We believe there should be rules to address the, hopefully extremely rare, situations when national authorities do not cooperate as needed. ESMA could either be empowered to issue sanctions or at least to make public the non-cooperative behavior. The well functioning of financial markets and increased internationalization require that authorities develop their cross-border cooperation, just like the industry does. This is a natural evolution and the ultimate goal of the single market.

(10) How can the system of cooperation among national and third country competent authorities be enhanced? What should the role of ESMA be?

ESMA has a very important role as regards cooperation with third country competent authorities. ESMA can both be a single point of contact when this is relevant and also be a facilitator for bilateral contacts between competent authorities of third countries and EU countries. ESMA's role is especially illustrated in cases where investigations involve several EU countries, which is more likely in the fragmented trading environment. ESMA needs to be the natural authority to ensure there is sufficient cross-border cooperation within the EU as well as with third countries, otherwise there is a significant risk that market abuse and manipulation will take place undetected.

C. SINGLE RULE BOOK

(11) Do you consider that a competent authority should be granted the power to decide the delay of disclosure of inside information in the case where an issuer needs an emergency lending assistance under the conditions described above? Why?

Competent authorities should not in general be given the role of deciding whether the disclosure of information can be delayed. It would place an administrative burden on both the issuers and the competent authority and it would not add benefit.

It may nevertheless be appropriate that emergency cases are treated differently. However, it then seems necessary to further elaborate what constitutes a systemically important entity. Recently, both various types of financial institutions have suffered, but also for instance car companies. It cannot be ruled out that in the future other industry sectors may come into grave conditions and this may have systemic impact in various Member States. Thus, in order to in fact provide further clarity about delays, as aimed for in the consultation paper, the conditions for the application of the rules need to be further developed.

(12) Should there be greater coordination between regulators on accepted market practices?

Accepted market practices have so far been decided nationally and are often considered to address the special conditions of local markets. However, it seems natural that when one market is considering accepting a certain market practice, others Member States should be consulted in order to detect possible similarities between markets that would in fact justify the same response also as regards accepted market practices. Accepted market practices should therefore be consulted on within the framework of ESMA before a decision is taken. Also, especially, as is recognized in the consultation paper, as shares may be traded on more than one market, it is necessary to address cross-border effects. As a minimum, an accepted market practice should provide a safe harbor for anyone engaging in trading activities on that market, irrespective of whether the market participant is licensed in that Member State or not.

(13) Do you consider that it is necessary to modify the threshold for the notification to regulators of transactions by managers of issuers? Do you consider that the threshold of Euro 20,000 is appropriate? If so why?

The proposed threshold seems appropriate, on the condition that the regime contains an aggregation mechanism.

The threshold itself is not however the major issue. What is more important is that the threshold is harmonized across Europe, i.e. it should not be optional for Member States to apply a threshold, or to opt for a lower threshold. Harmonisation would facilitate for those managers that are in businesses across borders and would thus improve the functioning of the internal market.

(14) Do you consider that there are other areas where it is necessary to progress towards a single rulebook? Which ones?

Much progress towards a single rule book in fact lies at the implementation and application level. It is necessary to implement the proposals in the de Larosière report in order for CESR/ESMA to be given a stronger role as regards supporting the uniform implementation and application of the MAD.

An area where further harmonization may be needed is the interpretation and practical application of the rules regarding reporting of managers' transactions.

We also believe that the national rules and practices regarding delayed disclosure can be further harmonized. This concerns the interpretation of when delayed disclosure is allowed and also if anyone, and who, needs to be informed about a delay.

(15) Do you consider that it is necessary to clarify the obligations of market operators to better prevent and detect market abuse? Why? Is the suggested approach sufficient?

It is crucial that all trading venues offering the same execution service also provide the same level of surveillance. Otherwise there is no level playing field between those market operators and also importantly there is a risk that market abuse and market manipulation can go on undetected on those venues where surveillance is not sufficiently rigid. CESR/ESMA seems well placed to contribute to that there is equally sufficient surveillance across all trading venues in order to maintain market integrity.

Competent authorities need to regain the trust from the market in taking the overall view of the trading. The fact that trading is more fragmented post-MiFID has put new challenges for market surveillance. For competent authorities, the TREM system has been set up for the exchange of transaction reports so that one authority shall have the opportunity to have the overall view of each instrument. We believe the practical functioning and the efficiency of this setup is crucial for the integrity of markets. Currently however, there seems to be a lack of trust from market participants in the way competent authorities take the overall view. This trust needs to be regained.

There is room for improvement when it comes to trading venues' overall surveillance of fragmented markets post-MiFID. Even pre-MiFID, when there was no market fragmentation, competent authorities were dependent on the exchanges' own surveillance function to detect suspicious

transactions and inform the competent authorities. Back then, the exchange had the overall picture of the trading of each instrument as well as the information disclosure by each issuer. The exchanges' market surveillance function could provide the competent authorities with information on suspicious trading, based on analyses of this overall picture. The obligation for the trading venues to report to competent authorities on suspicious transaction remains post-MiFID. What is missing however are the exchanges' analyses based on the overall picture. There is no exchange of information on the level of the trading venues, similar to what the TREM is intended to provide for the competent authorities, and there is no trading venue that has the overall picture or responsibility for each instrument. As a consequence, the competent authorities are not provided with reports on suspicious transactions from trading venues based on an overall picture. It needs to be underlined that regulated markets are in a position to do such analyses, should they get access to information on trading on other venues. Regulated markets maintain such functionalities for analyses. In addition, regulated markets are closer to the picture of information disclosure from issuers, as there is always one primary market from which the issuer disseminates its information in accordance with the Transparency Directive. This combination of a picture of the trading in combination with the analyses tools, make regulated markets well placed to fill the gap of the overall analyses at the level of the trading venues' of market surveillance.

Based on the above, we urge the Commission to look into possible measures that could be useful to improve the situation. It can be mentioned that at a roundtable discussion that took place on 18 May 2010, organized by CESR and engaging a broad representation of regulated markets and MTFs in Europe, there was a unanimous call for better opportunities for cooperation between trading venues. An „information gateway“ was called for. Today, trading venues are not allowed to share information due to confidentiality. It should be looked into how such provisions can be modified to allow the surveillance functions of the trading venues to exchange information as necessary. Possibly there also needs to be rules obliging trading venues to cooperate. This would improve the conditions for detecting market abuse and market manipulation, thus supporting the trust in the markets. In addition, it should be considered placing the overall responsibility for market surveillance with the primary market of each instrument admitted to trading. As elaborated on above, exchanges are well placed to undertake such a task.

One specific example of a gap due to fragmentation of trading is the trading halts. When trading in one instrument is halted on one venue, trading in the same instrument should not continue on another venue. However, a system for sufficiently sharing information to ensure that trading is duly suspended seems to not be in place. This is obviously unacceptable. A stable system for sharing information on trading halts not only between the trading venue and the competent authority, but indeed between trading venues, must be ensured.

July 2010

European Commission Public Consultation on Short Selling

Reply from NASDAQ OMX

The NASDAQ OMX Group, Inc. delivers trading, exchange technology, listings and other public company services and post-trading services across six continents. It lists approximately 3,700 companies from 50 countries and from all industry sectors. NASDAQ OMX offers various capital raising and trading solutions to companies around the globe, including its U.S. listings market, NASDAQ OMX Nordic, NASDAQ OMX Baltic, First North, U.S. 144A, NordPool and N2EX. NASDAQ OMX Nordic and Baltic include exchanges in Helsinki, Copenhagen, Stockholm, Iceland, Tallinn, Riga and Vilnius. NASDAQ OMX offers trading across multiple asset classes including equities, derivatives, debt, commodities, structured products and ETFs. NASDAQ OMX also offers post-trading services in the form of central counterparty derivatives clearing. NASDAQ OMX Group technology supports the operations of about 70 exchanges, clearing organizations and central securities depositories in more than 50 countries.

Initially, we wish to highlight some general points in relation to the proposal for measures related to short selling.

As the Commission rightly points out, short selling plays an important role in financial markets, in a positive sense. We are not convinced of the conclusion that short selling is to a significant extent used in an abusive fashion to drive down prices and contributes to disorderly markets. Nor that short selling can amplify price falls and have adverse effect on financial stability. On the contrary, during the most turbulent times when short selling increased on our markets, there were also other special conditions clearly impacting prices, and we did not necessarily observe significantly larger price movements in those stocks in which short selling increased compared to other stocks. We believe there is simply not enough established evidence that short selling needs such regulatory measures as proposed in the consultation paper. The measures proposed in the consultation paper risk reducing the positive role short selling plays in financial markets, they risk not having any positive effects and they are disproportionate. It would instead be appropriate for the Commission to back the proposals in the consultation paper with academic findings.

If one believes that short selling may have such negative effects as described in the consultation paper and referred to above, one has to recognize that the same effects of short positions may be achieved by the use of derivatives positions. By introducing a regulatory regime on short selling, the aims will not be reached. Other market practices will continue unregulated. This also puts the proposals in question.

Also, to have the intended effect, the proposed measures need to apply to positions taken outside regulated trading venues. The possibly speculative actions that have recently triggered local restrictions on short selling, have primarily been conducted using instruments that were not admitted to trading on regulated markets but that were traded OTC. Not only will the intended effects not be realized if the OTC market is outside the scope of the short selling regime, but leaving the OTC space unregulated would also incentivize a move of trading activities to unregulated venues. The

measures would run counter to the intentions expressed by G20, EU institutions as well as globally to increase transparency and reduce the opacity of markets. Furthermore, if measures are introduced that place a burden on those that make use of regulated venues, this affects the level playing field vis-à-vis OTC markets. It seems most relevant to focus measures on OTC markets rather than on practices taking place on regulated venues, where the level of transparency is already high.

In order for measures on short selling to have effect, one also needs to underline that markets are global, and measures introduced only in EU will only have limited effects, and may possibly move business outside the EU.

In addition, we wish to underline the importance of ensuring that the measures are linked to the intended effects. For instance, regarding disclosure, the measures need to be adapted to the intentions – is disclosure meant for information to the market and/or for regulators to be able to investigate abusive behavior, to take emergency measures or to do analyses at macro level?

It is our opinion that the measures proposed in the consultation are not justified and indeed not proportionate. They are not detailed enough for respondents to sufficiently analyse and understand the proposals, or to provide as useful comments as would have been preferred. We urge the Commission to reconsider its proposals. Before the proposals could be moved forward, it would be needed to provide justification, to elaborate on the details and to provide sufficient time for consultation.

Should nevertheless the Commission decide to move forward, please find below a summary of the responses from NASDAQ OMX, and the answers to the questions that we were able to provide within the limited consultation period.

We welcome the harmonization of powers and tools available to authorities. This will support a smoother operation of any regime adopted.

NASDAQ OMX also reiterates that public disclosure of short selling positions should be made by the regulator on aggregated level, not by individual participants.

Naked short selling should not be banned or subject to conditions. Any measures should instead be focused on settlement failures and encouraging central clearing.

Emergency powers need to be well-defined in order for the application of such rules to be as foreseeable and as harmonized as possible and they also need to be as limited in time as possible. This is necessary to support the well-functioning of the financial markets. Emergency situations should be detailed and an open consultation should be carried out.

A. SCOPE

Q 1. Which financial instruments give rise to risks of short selling and what is the evidence of those risks?

We do not specifically see the risks of short selling, nor as such, neither related to specific instruments. Possible risks seem to be concentrated to OTC markets rather than to activities taking place on regulated venues.

Q 2. What is your preferred option regarding the scope of instruments to which measures should be applied?

If measures are to be introduced at all, we prefer an option closer to B than to A.

It should be carefully considered which instruments need to be covered by the measures proposed by the Commission. It needs to be recognized that a scope covering all instruments admitted to trading on regulated markets, and only those, will have restrictive impacts on the trading taking place on transparent venues, while leaving OTC markets unaffected. This seems ill balanced, as much of the debate on possible speculative activities seem to concern CDSs traded OTC, rather than trading activities on regulated venues.

However, the details of the scope of option B would need to be outlined in more detail before a detailed answer can be provided.

Q 3. In what circumstances should measures apply to transactions carried on outside the European Union?

Any measure imposed in relation to an instrument admitted to trading on a regulated market within the EU needs to apply to this instrument irrespective of where a transaction is carried out. Otherwise there is a risk for regulatory arbitrage and loopholes, and the EU measures will not have the intended effect. Also, measures limited to regulated venues may incentivize OTC trading, thus favoring the more opaque trading venues over the transparent venues.

B. TRANSPARENCY

General comment

If a transparency regime is introduced and for it to be as efficient as possible, NASDAQ OMX strongly agrees that calculations of net short positions should also include such positions created by trading both on regulated venues and OTC and also positions created by the use of derivatives.

It is also necessary to keep in mind the purposes of a transparency regime – is it for public disclosure to the market, or for private use by the regulators? It seems appropriate that regulators may need more information than the market.

Q 4. What is your preferred option in relation to the scope of financial instruments to which the transparency requirements should apply?

The consultation paper lacks an explanation for why all or some types of instruments would need to be covered by a transparency regime. A regime should not be adopted unless there is a need for information disclosure.

For shares admitted to trading on a regulated market, we have already in our response to CESR's consultation on a pan-European transparency regime, welcomed a harmonized approach to transparency. The benefits would be that reporting regimes would be harmonized across Europe and cross-border business would be facilitated as market participants would not need to comply with a multitude of different reporting rules. ESMA should be given an important role in supporting a harmonized implementation and application of the regime.

For other instruments, especially as regards CDSs, where the OTC market plays a large role, it seems less appropriate to determine a scope related to what instruments are admitted to trading on regulated markets. This would place a burden on the trading taking place on regulated markets, but not achieve much. We also question whether specifically targeting sovereign bonds would provide regulators with more than a fragment of the overall picture.

Q 5. Under option A, is it proportionate to apply transparency requirements to all types of instruments that can be subject to short selling?

Even if a regime applied to all instruments admitted to trading on a regulated market, it would anyway not capture all relevant information, as it does not cover OTC markets, especially for CDSs.

Q 6. Under option B, do you agree with the proposals for notification to regulators and the markets of significant net short positions in EU shares?

For notification to the regulator, the 0,2% threshold seems high. If regulators are to make effective use of the information, the threshold may need to be lower.

However, the proposal for public disclosure needs to be significantly adjusted. As already underlined in our response to CESR's consultation in relation to a pan-European short selling disclosure regime, disclosure to the markets should be done on aggregated level by the regulator. The purpose of public disclosure as described by CESR is to provide informational benefits to the market, improve insight into market dynamics and make available important information to assist price discovery. These purposes would be achieved by aggregated disclosure by the supervisor, which would give a comprehensive picture of the status of short selling activities per instrument. Such a system would reduce the risk of the information being very fragmented and more complicated to analyse for the market. Also, the short seller may have a legitimate interest in not disclosing his/her positions, especially at the low levels as suggested by CESR (0,5%). Indeed, there are important risks in publishing such information to the market. Information on individual positions may open up for wider abusive behavior, such as front running and squeezes. Such behavior has serious impact on price formation. The threshold at which aggregated information should be disclosed could be significantly higher than that for the market participants' reports to the supervisor, possibly around 5%.

It may be added that NASDAQ OMX regularly publishes aggregated data on securities lending, for which we see a high demand.

Q 7. In relation to option B, do you agree with the proposals for notification to regulators of net short positions in EU sovereign debt (including through the use of CDS)? In addition to the notification to regulators, should there be public disclosure of significant short positions?

A disclosure regime only aimed at sovereign debt would not be efficient. It seems that either all types of debt instruments should be included, also instruments traded OTC, otherwise regulators will not have a full picture, or instead the regulators could be empowered to ask for information when needed.

For public disclosure, we also see that there could be a value for the market if the information gathered by regulators were published in aggregated form.

Q 8. Do you agree with the methods of notification and disclosure suggested?

The TRS system and the OAMs could provide a good structure to build on.

Q 9. If transparency is required for short positions relating to sovereign bonds, should there be an exemption for primary market activities or market making activities?

No. If there is a regime in place it should apply equally to all participants. Otherwise there is a risk that activities are driven outside the transparent space. If the market maker position is never reported, anyone can trade any instrument (future, swap, repo, CFD, etc.) against the market maker instead of in the market, thus deteriorating transparency. We would prefer that market makers are required to report their positions to the supervisor and that this information is included in the statistics to be

made available to the market on an aggregated level. The market maker positions would then be part of the general statistics, but not disclosed in their names.

If an exemption is to be granted, it would be important to find a very narrow definition of market maker. Considering the wide variety of practices that may today be considered as market making activities, we question whether it is feasible to find a narrow definition. This again is an argument against allowing an exemption.

Q 10. What is the likely cost and impact on different options on the functioning of financial markets?

Costs are very difficult to estimate. A regime that misses the goal will add cost and administration without achieving a benefit. Inefficiencies are costly.

C. UNCOVERED SHORT SALES

General comment

It is important to reiterate that short selling is a useful feature in financial markets. Disproportionate restrictions will curb liquidity, which will cause the costs for legitimate activities to increase.

It is also important to point out that even if a position may be naked at the point of selling, it is not a given that there will be a settlement failure. By introducing restrictions applicable at the point of selling, also perfectly legitimate transactions will be unduly restricted. This seems ill justified and disproportionate.

As most instruments subject to naked short selling is not traded on regulated exchanges (i.e. CDSs), the proposed rules seem somewhat misdirected.

It is also worth pointing out that for transactions that go through a central clearing house, there are already default regimes in place via the CCP. Instead of regulating naked short selling, it would be more appropriate to concentrate on encouraging CCP clearing.

Q 11. What are the risks of uncovered short selling and what is the evidence of those risks?

We do not see evidence of risks. In or markets we have not seen significant problems with settlement failures.

Q 12. Is there evidence of risks of uncovered short sales for financial instruments other than shares (e.g. bonds or sovereign bonds), which would justify extending the requirements to these instruments?

No.

Q 13. Do you agree with the proposed rule setting out conditions for uncovered short selling? Do you consider that more stringent conditions should be put in place? If so, please indicate which ones? Do you agree that the arrangements other than formal agreements to borrow should be permitted if they ensure that shares are available for borrowing settlement? If so, why?

No. From our experience, delivery may very well take place even though the seller may not own/borrow the instrument at the point of sale. Setting conditions risks having an unintended damaging effect on legitimate and useful short selling. If the purpose is to reduce price volatility, conditions for short selling will not have any effect. There should be no conditions. It is better to find a well working regime for actual settlement failures and to encourage CCP clearing as mentioned above.

Q 14. Do you consider that the risks of uncovered short selling are such that they should be subject to an upfront ban/permanent restrictions? If so, why?

No. We are not convinced that restrictions on short selling will have any positive effects. On the contrary, there may be more negative effects.

~~**Q 15. Do you agree with the proposal requiring buy in procedures for settlement failures due to short sales? If so, what is an appropriate base period that could be specified before buy in procedures are triggered (e.g. T+4)?**~~

Buy in procedures are best placed at settlement level. As already mentioned, CCP clearing regimes take care of delivery failures for transactions put to central clearing. For other transactions, a buy in regime should be placed at settlement level. For it to be efficient, it is also crucial that it is sufficiently supervised and enforced, and that sanctions are appropriately discouraging.

Q 16. Do you consider that there should be permanent limitations or a ban on entering into naked credit default swaps relating to EU sovereign issuers? If so, please explain why, including if possible any evidence relating to the use of naked CDS.

No. See above in this section C.

Q 17. Do you consider that in addition to the measures described above there should be marking of orders for shares that short sales?

No.

Q 18. What is the likely costs and impact of the different options on the functioning of financial markets?

Difficult to estimate. If measures are imposed that have adverse effects on financial markets, on liquidity, on inefficiency, which cost.

D. EXEMPTIONS

Q 19. Do you agree with the proposed exemption for market making activities? Which requirements should it apply to?

The fact that market making activities could be exempt, in our view is recognition of the usefulness of short selling, even uncovered short selling. This again raises question marks as to why restrictions on uncovered short selling would be justified broadly.

In case uncovered short selling will anyway be subject to any type of requirements or restrictions, the same rules should apply to all, market making activities included. As already stated above under Q 9, we believe market makers should not be exempt from the transparency requirements, and they should comply with the same rules on uncovered short selling as the rest of the market. Otherwise, it could create incentives for OTC trading vis-à-vis trading on more transparent trading venues. Should market makers anyway be exempt from transparency requirements, it is necessary to apply a very narrow definition of market maker and ensure that the exemption only applies to proprietary trading carried out in relation to market making.

Q 20. Do we need any exemptions where the principal market for a share is outside the European Union? Are there any other special rules needed with regard to operators or markets outside the European Union?

It is important that the same short selling regime applies to a share, irrespective of where the share is traded. Either a short selling regime applies to all markets where the share is traded, or no regime applies. Otherwise, there will be room for arbitrage and loopholes. EU should ensure that sufficient cooperation arrangements are in place

between the EU and those countries where shares admitted to trading on a regulated market in EU is also traded on markets outside the EU.

Q 21. What would be the effects on the functioning of markets of applying or not applying the above exemptions?

As regards market makers, see the answer to Q 19 above.

~~As regards non-EU countries, see the answer to Q 20 above.~~

E. EMERGENCY POWERS OF COMPETENT AUTHORITIES

Q 22. Should the conditions for use of emergency powers be further defined?

Yes. The market suffers from uncertainty. The conditions for invoking emergency powers should be as detailed as possible and a new consultation should be carried out for this. The consultation paper does not provide sufficient details. See also the answer to Q 23 below.

Q 23. Are the emergency powers given to Competent Authorities and the procedures for their use appropriate?

Before restrictions are imposed, it is important that Competent Authorities carefully weigh the pros and cons of restrictions. For instance, restricting short sale will have the effect of destroying totally legitimate strategies, in which short selling is but one leg.

Since we are not convinced about the benefits of the proposed emergency powers, we also have difficulties finding a role for ESMA. It is important that the imposition of emergency measures is limited to the Member State that deems that there is an emergency situation. Other Member States should not be forced to apply the emergency measures imposed in another Member State. For this reason it seems important to underline that the powers to impose of emergency measures should remain nationally, and not be transferred to ESMA. It must be the task of those Competent Authorities considering the imposition of emergency measures to explain the reasons for it and for the other Competent Authorities to maintain their sovereignty in deciding what is appropriate for their home markets. ESMA should however maintain a coordinating role, facilitating the exchange of views between Competent Authorities.

As the powers of one Competent Authority should not extend beyond its jurisdiction, more details are needed on how such emergency measures could be effective, as the same financial instruments can be traded in several Member States. It seems that emergency restrictions will not provide solutions.

In addition, in order to possibly support swift handling by ESMA and Competent Authorities and to provide the market with as much certainty as possible, the conditions for use of emergency powers should be further detailed. The proposed 24 hour time period allowed for ESMA and other Competent Authorities to analyse and provide views on the action proposed is indeed very short. It can be questioned whether this procedure will in practice allow for appropriate coordination to be effectuated. It is true that emergency situations by nature require quick responses. Nevertheless, coordination and harmonized actions are essential in order to avoid other negative effects on the functioning of the markets, so a longer time period seems necessary.

Q 24. Should the restrictions be limited in time as suggested above?

Yes, in order to intrude as little as possible on the normal functioning of the markets restrictions need to be strictly limited to short time periods.

Q 25. Are there any further measures that could ensure greater coordination between competent authorities in emergency situations?

See answer to Q 23 above.

Q 26. Should competent authorities be given further powers to impose very short term restrictions on short selling of a specific share if there is a significant price fall in that share (e.g. 10%)?

Something similar to circuit breakers, which are in use on US markets, could be considered also for European markets.

F. POWERS OF COMPETENT AUTHORITIES

General comments

It should be ensured that all competent authorities have the same powers to seek further information regarding any supervisory purposes. It seems that the suggestion in the consultation paper to give powers to competent authorities on the purposes of anyone entering into a CDS transaction, is related to the general aim to ensure financial stability. If so, the powers for competent authorities should be looked at more broadly than only in relation to the purpose of entering into a CDS transaction.

Q 27. Should the power to prohibit or impose conditions on short-selling be limited to emergency situations (as set out in the previous section)?

We are still lacking support for the view that restrictions on short selling is an appropriate measure. For this reason, we object to introducing powers to impose such restrictive measures.

Should nevertheless such powers be introduced, they should be limited to emergency cases only. However, before this is introduced, a consultation on what may constitute such emergency cases should be carried out.

Q 28. Are there any special provisions that are necessary to facilitate enforcement of future legislation in this area?

Competent authorities need to have the powers to enforce any rules applying to financial market participants, be these rules stated in EU law, in national regulations or imposed in the form of emergency measures. This is crucial in order to ensure that the rules are complied with uniformly.

Q 29. What co-operation powers should be foreseen by ESMA on an ongoing basis?

In relation to short selling, coordination powers should be strong in order to ensure harmonized regulatory solutions across the EU. The current coordination by CESR in relation to short selling has not achieved a harmonized solution.

G. GLOSSARY OF DEFINITIONS

Q 30. Do the definitions serve their intended purpose?

"Principal market" probably needs to be defined with more detail, or at least the process of finding the principal market should be described or referred to.

"Short sale"

- "the time of the sale" may need to be specified, possibly "the time of the entering into the agreement" is better.

- In relation to derivatives a separate definition may be needed. It does not seem to be relevant to demand that the underlying security be held from the time of entering into a derivatives contract until delivery.

CESR Technical Advice to the European Commission in the context of the MiFID Review – Transaction Reporting

Reply of NASDAQ OMX

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NASDAQ OMX appreciates the possibility to comment on the transaction reporting regime and has focused its reply on the issue of transaction reporting by market members not authorised as investment firms.

Transaction reporting by market members not authorised as investment firms

Question 15:

CESR suggests amending MiFID by introducing a transaction reporting obligation according to Article 25(3) to those persons that are members of a regulated market or MTF currently falling under the Article 2(1)(d) exemption or, alternatively, by introducing a similar obligation on regulated markets or MTFs that admit these undertakings as members.

Do you agree with CESR's proposal on the extension of reporting obligations? If so, which of the two alternatives would you prefer?

We believe that the obligation to report transactions carried out by market members not authorised as investment firms should be imposed on the entities concerned and not the trading venues. There is no reason to depart from the general rule imposed on investment firms. Moreover, execution venues will not necessarily have exhaustive information and will in any case need to go back to the entity in question.

For market members not authorised as investment firms, the control of the implementation of the reporting obligation should be carried out by the securities regulator of the first connection.