



Regulation of short selling by CESR members

The ABI's Response to CESR 08/1010

The ABI is the voice of the insurance and investment industry. Its members constitute over 90 per cent of the insurance market in the UK and 20 per cent across the EU. They control assets equivalent to a quarter of the UK's capital. They are the risk managers of the UK's economy and society. Through the ABI their voice is heard in Government and in public debate on insurance, savings, and investment matters. The ABI prides itself on thinking for tomorrow, providing solutions to policy challenges based on the industry's analysis and understanding of the risks we all face.

Thank you for the opportunity to respond to this call for evidence. ABI members are affected by short selling proposals in two ways. Those that hold short positions themselves will bear direct costs of any regulatory changes. Others will be impacted only indirectly, as users of the market, as they do not short themselves.

Because of the very tight timescale, we have not had the opportunity to consult our membership in full. We intend to do so when the UK FSA publishes its consultation in due course. We expect their paper to contain a more detailed discussion of various approaches to short selling and a general overview of the use of short selling in the market – which our members believe is long overdue. Both the proponents and the detractors of the practice have in recent months made claims about its costs and benefits but it has been hard to ascertain which of these, if any, are based on evidence.

In the meantime, we would like to make some more general points about the recent developments in short selling that CESR might find helpful.

First, we are pleased that CESR is coordinating member states' changes to short selling regulation at the European level. However, this needs to go further than merely collating and updating and extend to facilitating an EU-wide response.

For our members, the disparity of approaches taken not just in the EU but globally has represented a significant cost. For example, one large firm, which operates in several jurisdictions, reports that the annual legal and consultancy fees paid merely for identifying and tracking changes run to tens of thousands of pounds. As disclosures made under the UK short selling regime showed, this is a global problem and ideally the solutions should be global too.

Second, in terms of approaches taken by member states last year, we have been supportive of the temporary ban on short selling introduced by several competent authorities. Although we do not see this as a long-term solution and generally believe that short selling is a legitimate investment technique and not abusive in itself, there is no doubt that the market conditions that preceded the ban were exceptional and therefore warranted drastic action by the regulators.

In the UK questions have been raised about the efficacy of the ban, and we are certainly interested in seeing a full assessment of this. But at the time, the introduction of the ban did serve to restore market confidence to a certain extent. Now the background has changed, we have supported the lifting of the UK ban last week.

Our members have also supported the limited disclosure regime. In fact, in terms of future policy options, we have been sympathetic to a general disclosure regime of short positions. This would apply to all stocks, rather than just the financial sector, and to all market participants that hold short positions.

Many ABI members believe a symmetrical approach to disclosing short and long positions would reflect the realities of the market. Their view is that disclosure of economic positions is no longer just about access to voting rights but about market efficiency more generally, and that there is therefore no reason why holders of short positions, whoever they are, should be shielded from disclosure.

The forthcoming review of the Transparency Directive seems to us to be an opportunity to have a full discussion about both the purpose and the structure of the EU disclosure regime.

A further discussion needs to be had on the appropriate disclosure thresholds. The higher the threshold, the smaller the number of disclosures is likely to be. This could alleviate some concerns about the amount of 'noise' disclosure of short positions would produce. In any case, the EU regulators would have to ensure that the percentages chosen, both for initial and for ongoing disclosures, are not arbitrary.

For some investment managers, this option would not be cost-free. Those that short sell would have to bear direct costs of system changes to enable them to identify and report positions to the market. But more generally, they do not believe that public disclosure would constrain their short selling activity.

We can also see some merit in regulators providing to the market an aggregated figure representing the total short interest in a security. This would mean that all market participants would have to disclose their short sales to competent authorities, who would aggregate and publish them.

It may be that the most appropriate policy option is a combination of individual and aggregate disclosure. It is certainly something our members would be interested in exploring further.

We would be happy to share with CESR our views on this subject following a full consultation by the FSA. In the meantime, please do not hesitate to contact me if you have any questions.

Yours sincerely,

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