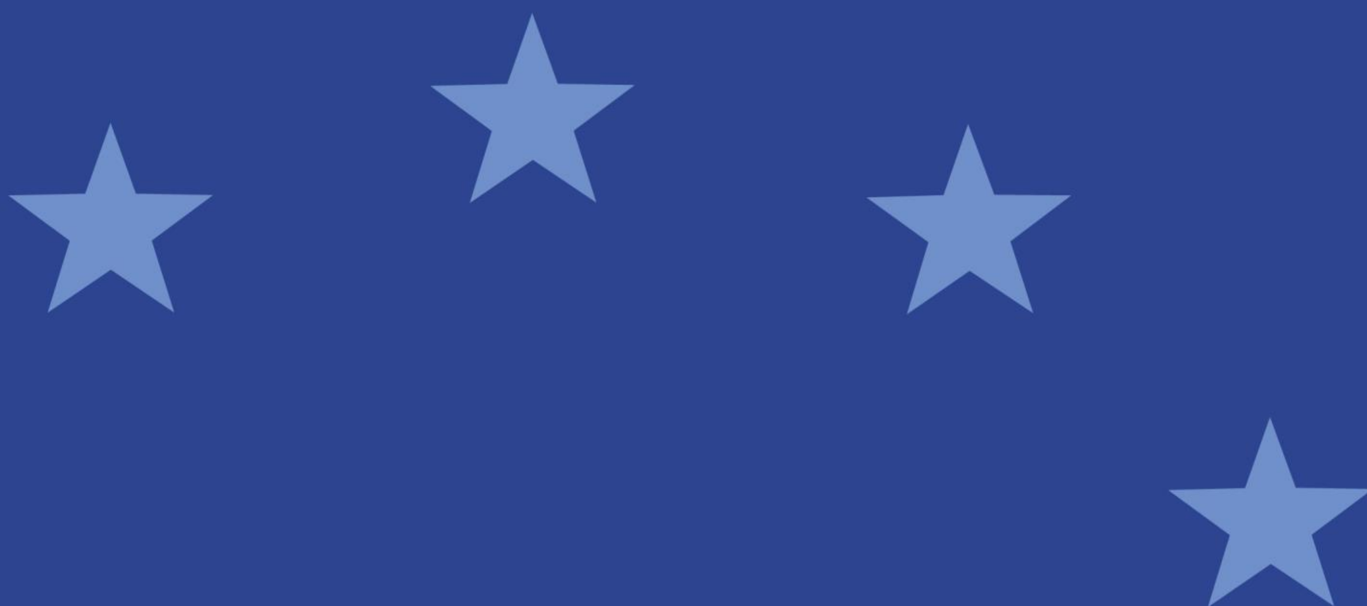
Consultation Paper

On Draft Regulatory Technical Standards on major shareholdings and indicative list of financial instruments subject to notification requirements under the revised Transparency Directive



20 March 2014| ESMA/2014/300

Date: 20 March 2014
ESMA/2014/300

Responding to this paper

ESMA invites comments on all matters in this paper and in particular on the specific questions summarised in Annex I. Comments are most helpful if they:

- indicate the specific question to which the comment relates and respond to the question stated;
- contain a clear rationale, clearly stating the costs and benefits; and
- describe any alternatives ESMA should consider.

ESMA will consider all comments received by **30 May 2014**.

All contributions should be submitted online at www.esma.europa.eu under the heading 'Your input - Consultations'.

Publication of responses

All contributions received will be published following the close of the consultation, unless you request otherwise. Please clearly and prominently indicate in your submission any part you do not wish to be publically disclosed. A standard confidentiality statement in an email message will not be treated as a request for non-disclosure. A confidential response may be requested from us in accordance with ESMA's rules on access to documents. We may consult you if we receive such a request. Any decision we make not to disclose the response is reviewable by ESMA's Board of Appeal and the European Ombudsman.

Data protection

Information on data protection can be found at www.esma.europa.eu under the heading 'Legal Notice'.

Who should read this paper?

This document will be of interest to all stakeholders. It would primarily be of interest to investors in equity, investors in equity derivative markets and their advisors, natural or legal persons which perform investment services or activities, issuers as well as to any market participant who is affected by Directive 2004/109/EC of 15 December 2004 (the Transparency Directive).

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Acronyms and definitions used

CESR	Committee of European Securities Regulators
CfD	Contracts for Differences
Commission	The European Commission
Commission Directive	Commission Directive 2007/14/EC of 8 March 2007 laying down detailed rules for the implementation of certain provisions of Directive 2004/109/EC on the harmonisation of transparency requirements in relation to information about issuers whose securities are admitted to trading on a regulated market
CP	This Consultation Paper
CRD IV	Directive 2013/36/EU of the European Parliament and of the Council of 26 June 2013 on access to the activity of credit institutions and the prudential supervision of credit institutions and investment firms, amending Directive 2002/87/EC and repealing Directives 2006/48/EC and 2006/49/EC
CRR	Regulation (EU) No 575/2013 of the European Parliament and of the Council of 26 June 2013 on prudential requirements for credit institutions and investment firms and amending Regulation (EU) No 648/2012
CWG	Corporate Finance Standing Committee Consultative Working Group
Directive 85/611/EEC	Council Directive 85/611/EEC of 20 December 1985 on the coordination of laws, regulations and administrative provisions relating to undertakings for collective investment in transferable securities (UCITS)
Directive 2013/34/EU	Directive 2013/34/EU of the European Parliament and of the Council of 26 June 2013 on the annual financial statements, consolidated financial statements and related reports of certain types of undertakings, amending Directive 2006/43/EC of the European Parliament and of the Council and repealing Council Directives 78/660/EEC and 83/349/EEC
EC	The European Commission
ESMA	European Securities and Markets Authority

ESMA Regulation	Regulation (EU) No 1095/2010 of the European Parliament and of the Council of 24 November 2010 establishing a European Supervisory Authority (European Securities and Markets Authority), amending Decision No 716/2009/EC and repealing Commission Decision 2009/77/EC
EU	The European Union
MiFID	Directive 2004/39/EC of the European Parliament and of the Council of 21 April 2004 on markets in financial instruments amending Council Directives 85/611/EEC and 93/6/EEC and Directive 2000/12/EC of the European Parliament and of the Council and repealing Council Directive 93/22/EEC
NCA	National Competent Authority
Omnibus Directive	Directive 2010/78/EU of the European Parliament and of the Council of 24 November 2010 amending Directives 98/26/EC, 2002/87/EC, 2003/6/EC, 2003/41/EC, 2003/71/EC, 2004/39/EC, 2004/109/EC, 2005/60/EC, 2006/48/EC, 2006/49/EC and 2009/65/EC
OJ	The Official Journal of the European Union
RTS	Regulatory Technical Standard
SMSG	Securities and Markets Stakeholder Group set up in accordance with article 37 of Regulation 2010/1095 of 24 November 2010
Takeover Bids Directive	Directive 2004/25/EC of the European Parliament and of the Council of 21 April 2004 on takeover bids
TD/Transparency Directive	Directive 2004/109/EC of the European Parliament and of the Council of 15 December 2004 on the harmonisation of transparency requirements in relation to information about issuers whose securities are admitted to trading on a regulated market and amending Directive 2001/34/EC
TFEU	Treaty on the Functioning of the European Union
UCITS	Directive 2009/65/EC of the European Parliament and of the Council of 13 July 2009, on the coordination of laws, regulations and administrative provisions relating to undertakings for collective investment in transferable securities (UCITS)

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I. Executive Summary

Reasons for publication

The revised Transparency Directive 2013/50/EC (TD) was published in the Official Journal of the European Union on 6 November 2013 and entered into force on 27 November 2013. ESMA is required to submit certain draft Regulatory Technical Standards (RTSs) on major shareholdings (for details on each RTS, see the relevant section) to the European Commission (Commission or EC) by 27 November 2014.

According to Articles 10 and 15 of Regulation (EU) No 1095/2010 of the European Parliament and of the Council establishing ESMA (ESMA Regulation), ESMA must conduct a public consultation before submitting draft RTSs to the Commission. This Consultation Paper (CP) therefore seeks stakeholders' views on proposals for such RTSs. The input from stakeholders will help ESMA finalise the draft RTSs. Respondents to this CP are encouraged to consider the costs and benefits that the draft RTSs would imply and provide the relevant data to support their arguments or proposals.

The CP also seeks stakeholders' views on the proposed content of an indicative list of financial instruments referenced to shares and with economic effect similar to holding shares and entitlements to acquire shares.

Contents

This CP covers two main subjects, namely 1) the RTSs on major shareholdings; and 2) the establishment of an indicative list of financial instruments which are subject to the notification requirements laid down in Article 9 of the TD.

RTSs on major shareholdings

The revised TD tasks ESMA with drafting RTSs concerning:

1. The method of calculation of the 5 % threshold for the market maker and trading book exemptions referred to in paragraphs 5 and 6 of Article 9, including in the case of a group of companies, taking into account Article 12(4) and (5).
2. The method of calculating voting rights referred to in the first subparagraph of Article 13(1a) in case of financial instruments of similar economic effect to holding shares and entitlements to acquire shares and which are referenced to a basket of shares or an index.
3. The methods of determination of delta for the purposes of calculation of voting rights relating to financial instruments which provide exclusively for a cash settlement as required by the second subparagraph of Article 13(1a).
4. The cases in which the exemptions mentioned in Article 13(4) apply to financial instruments held by a natural person or a legal entity fulfilling orders received from clients or responding to a client's requests to trade otherwise than on a proprietary basis, or hedging positions arising out of such dealings.

Indicative List

The revised TD furthermore mandates ESMA with establishing an indicative list of financial instruments that are subject to notification requirements according to Article 13(1). The TD tasks ESMA with periodically updating the indicative list, taking into account technical developments on financial markets. The CP sets out the proposed content of this list and outlines the processes for updating it.

Next steps

ESMA will consider all feedback received in relation to this consultation when finalising the draft RTSs to be submitted to the European Commission by 27 November 2014 for endorsement.

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II. Background

1. In January 2010 ESMA's predecessor CESR (Committee of European Securities Regulators) released a Consultation Paper with a proposal to extend major shareholdings notifications to instruments with similar economic effect to holding shares and entitlements to acquire shares[1]. This proposal was inspired, inter alia, by a number of cases where cash-settled derivatives were used to gain economic exposure in a specific issuer without the concurrent assignment or transfer of the right to buy or sell the underlying share. These cases included Fiat and Continental/Schaeffler.

2. In the Fiat case the Agnelli family entered into an equity swap agreement with Merrill Lynch in April 2005 for approximately 8 % of Fiat's share capital. Initially, the contract provided exclusively for cash-settlement of shares, but in September 2005 the agreement was modified to provide for the physical delivery of shares. As Merrill Lynch had acquired a long position to offset the short position written for the client, the shares were available to the Agnelli family and played a crucial role in their maintaining a 30% controlling stake in Fiat.

3. As for the Continental/Schaeffler case, in the summer of 2008 Schaeffler acquired an almost 36 % stake in Continental, thereof 2,97 % in shares, 4,95 % in options with physical settlement and 28 % through a cash-settled total return equity swap entered into with Merrill Lynch as a counterparty. In turn, Merrill Lynch hedged its position executing swap transactions with other dealers in parcels below the minimum threshold for mandatory disclosure. The agreements were never disclosed by the financial intermediaries involved because German law only required disclosure of direct or indirect ownership of more than 3 % of the shares of a publicly listed company or physically cash-settled derivatives on shares exceeding 5 % of capital. Hence, the market only came to know of the transactions by the time Schaeffler launched a takeover bid for 100 % of Continental and made public the position acquired through derivatives.

4. Following the cases above and similar ones, a number of Member States have adopted regulatory initiatives contemporaneous with that of CESR. Outside the EU, Switzerland, Hong Kong and Australia also have regulation addressing the issue in place.

5. At a supra-national level, and according to Article 33 of the Transparency Directive, the Commission was obliged to report on the operation of said Directive to the European Parliament and to the Council by 30 June 2009. On 27 May 2010 the Commission adopted a Report on the operation of the TD[2] which concluded that the effectiveness of the existing transparency regime could be improved, notably with respect to the disclosure of corporate ownership[3].

6. In the Report it was acknowledged that financial innovation has led to the creation of new types of financial instruments that expose investors to an economic risk similar to that experienced when

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1 CESR proposal to extend major shareholdings notifications to instruments of similar economic effect to holding shares and entitlements to acquire shares, CESR/09-1215b, January 2010.

2 COM(2010)243 final, Report from the Commission to the Council, the European Parliament, the European Economic and Social Committee and the Committee of the Regions, Operation of Directive 2004/109/EC on the harmonisation of transparency requirements in relation to information about issuers whose securities are admitted to trading on a regulated market (hereafter 'EC Report').

3 EC Report, p. 3.

holding shares. Additionally, these financial instruments may facilitate the exercise of influence on the issuer by the holder. This could lead to the building of secret stakes in companies, allowing for hidden ownership and creeping control.

7. To address these concerns, one of the overarching principles regarding major shareholdings of the revised TD is that "in order to ensure that issuers and investors have full knowledge of the structure of corporate ownership, the definition of financial instruments in that Directive should cover all instruments with similar economic effect to holding shares and entitlements to acquire shares" (Recital 9). Such disclosure under Article 13(1)(b) shall be made in addition to the disclosure of shareholdings under Articles 9(1) and 10 and the disclosure of entitlements to acquire shares under Article 13(1)(a). This new requirement also promotes harmonisation of the currently divergent disclosure regimes across Member States.

8. The revision process of the TD led to the identification of a number of areas where further harmonisation should be fostered, e.g. ensuring that the same exemptions apply on the same terms in all Member States. The necessity of such harmonisation can be illustrated by the case of the trading book and market maker exemptions, where it is necessary to harmonise the method for calculation of the respective notification thresholds.

9. The draft RTS on the market maker and trading book exemptions takes into consideration Article 10 of Commission Directive 2007/14/EC (Commission Directive) regarding the conditions of independence to be complied with by management companies and investment firms involved in individual portfolio management. ESMA is of the opinion that said Article 10 does not apply directly to the cases regulated in Article 9(5) and (6) of the revised TD as the latter concern holdings held in the capacity of a market maker and holdings held in trading books by credit institutions and investment firms, whereas Article 10 details further the conditions of independence to be complied with by management companies and investment firms regarding portfolio and asset management holdings.

10. Nonetheless, ESMA considers that there is no reason to treat credit institutions and investment firms in relation to holdings held in the trading book or market makers conducting market making activities differently than management companies and investment firms involved in asset management and individual portfolio management, respectively, as exertion of influence over an issuer is not sought in either situation. Therefore, principles of independence similar to the ones set out in Article 10 of the Commission Directive should apply to entities covered by Article 9(5) and (6) of the revised TD.

11. The revised TD has introduced a notification requirement for all financial instruments with similar economic effect to holding shares and entitlements to acquire shares. Therefore, it is necessary to create both a clarified and harmonised regime on how to calculate the number of voting rights in the case of financial instruments referenced to baskets of shares and indices and to specify the method for determining delta for the calculation of voting rights relating to such financial instruments where they provide exclusively for a cash settlement.

12. To collect input to the drafting of the RTS specifying methods for determining delta under Article 13(1a), point (b), ESMA organised an informal round table on 26 September 2013 with represent-

atives of market participants, including issuers, investment management funds and associations, banks, other investment services providers and corporate finance advisors.

13. Participants to the round table provided useful feedback to consider in the approach to this RTS. It was emphasised that market participants prefer having a principle-based approach to delta-adjusted calculation as opposed to a prescriptive approach based on (a) mathematical formula(s) depending on the type of financial instrument. Some participants advised that the prescription of a single method of delta calculation would be problematic due to a lack of availability of market prices (frequent for illiquid shares) and the existence of exotic or non-standard financial instruments such as barrier and knock-out options, where the possibility of agreeing on a common method of calculation would be very limited. Furthermore, a principle based approach permits to address new financial instruments that might be introduced in the future, thus discouraging the use of financial innovation to avoid compliance.

14. We recognised that firms would want clarity and legal certainty, but reality is that this is impossible and if you try to do it you will simply encourage new instruments/combinations that are not on the list.

15. The broad scope of financial instruments subject to notification requirements under the revised TD necessitates an assessment of the regime applicable to client-serving transactions, i.e. the fulfilment of orders received from clients or responding to a client's requests to trade otherwise than on a proprietary basis, or hedging positions arising out of such deals. The revised TD tasks ESMA with clarifying whether existing exemptions under Articles 9 and 12 apply to such transactions.

16. In recognition of the fact that financial markets tend to evolve rapidly, developing new and complex financial instruments with characteristics that are unknown today, the revised TD mandates ESMA with establishing a list of financial instruments which are entitlements to hold shares and financial instruments which are considered economically equivalent to shares. ESMA will be responsible for periodically updating this list, taking into account technical developments on financial markets.

17. In developing the four RTS and the above mentioned list, ESMA has consulted the Consultative Working Group of its Corporate Finance Standing Committee.

III. Definition and scope of the draft regulatory technical standards

III.I. Draft regulatory technical standard on the calculation method of the 5 % threshold referred to in the Article 9(5) and (6) exemptions

Mandate

18. Article 9(6b) of the revised TD states that ESMA shall develop a draft RTS to specify the method of calculation of the 5 % notification threshold applicable to acquisitions or disposals of shares by a market maker in its capacity of a market maker and the 5 % notification threshold applicable to voting rights held by a credit institution or investment firm in its trading book, including in the case of a group of companies, taking into account Article 12(4) and (5).

Scope

19. ESMA's interpretation of the Article 9(6b) mandate is that the draft RTS should firstly clarify whether the different categories of holdings – Article 9, 10 and 13 of the revised TD – are to be aggregated when calculating holdings for the purpose of Article 9(5) and (6). In other words, it must initially be determined whether holdings should be *horizontally* aggregated. Secondly, the draft RTS should clarify whether holdings are calculated at group level or at individual company level within the group; this second element concerns the *vertical* aggregation of shares.

20. ESMA has considered whether the market making and trading book exemptions should be treated in the same manner and thus subjected to the same principles in the draft RTS.

21. The obvious similarity between Article 9(5) and (6) is that a prerequisite to benefit from the exemption is that no type of intervention in the management of the issuer occurs. This facilitates the identification of who actually exercises control over an issuer[4].

22. At the same time, there are some differences between Article 9(5) and (6). A market maker should have a business organisation allowing for identification of activities conducted in relation to the issuer in question and in particular to the shares or financial instruments held for market making purposes. As such, the Commission Directive sets up control mechanisms regarding market makers in Article 6[5]. Different thresholds also apply to the market making and trading book exemption, the latter being capped at 5 %.

23. However, while differences do exist between the two exemptions, we believe that these differences are more of a formal nature than actual differences in content and that they do not provide adequate reason for taking different regulatory approaches to the market maker and trading book exemptions. A credit institution or investment firm intending to avail itself of the trading book exemption will need to have in place similar organisational requirements to the ones required of the market maker in the Commission Directive. In fact, a credit institution or investment firm should be able to identify the shares or financial firms concerned in order to benefit of the trading book exemption. For this reason, ESMA proposes following a common approach for the two exemptions in the draft RTS.

Q1: Do you agree that the trading book and the market maker holdings should be subject to the same regulatory treatment regarding Article 9(6b) RTS?

Q2: If not, please identify reasons and provide quantitative evidence for treating

[4] Cfr. Recital (20) of TD: "In order to avoid unnecessary burdens for certain market participants and to clarify who actually exercises influence over an issuer, there is no need to require notification of major holdings of shares, or other financial instruments as determined by Article 13 that result in an entitlement to acquire shares with regard to market makers or custodians, or of holdings of shares or such financial instruments acquired solely for clearing and settlement purposes, within limits and guarantees to be applied throughout the Community. The home Member State should be allowed to provide limited exemptions as regards holdings of shares in trading books of credit institutions and investment firms."

[5] The control mechanisms comprise the market maker's obligation to: notify the Home Member State that it conducts or intends to conduct market making activities on a particular issuer; be able to identify the shares or financial instruments held for market making purposes; and provide upon request of the relevant competent authority the market-making agreement between the market maker and the stock exchange and/or the issuer when such is mandatory under national law.

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trading book and market making holdings differently?

a. Horizontal aggregation – Aggregation of different categories of holdings (Article 9, 10 and 13 of the revised TD)

24. The fact that the mandate is inserted in Article 9 could mean that the calculation method should only specify the 5 % threshold for shares, because Article 9 specifically addresses notification of shares.

25. However, when considering shares only, the method of calculation of the 5 % threshold in the market making or trading book at company level can be considered to be resolved by Article 9 (1), second subparagraph which states that voting rights shall be calculated on the basis of all the shares to which voting rights are attached even if the exercise thereof is suspended.

26. Therefore, ESMA is of the opinion that the mandate to specify the method of calculation of the 5 % threshold refers not only to the calculation of the threshold for shares but also for a natural person or legal entity's ability to influence voting rights (Article 10) and their acquisition of financial instruments (Article 13(1)).

27. Further indications to this effect are that the TD requires the notification of shares, voting rights <u>and</u> financial instruments in Articles 9(1), 10(1) and 13(1), respectively and that the newly introduced Article 13a creates the rule of aggregation when calculating the thresholds set out in Article 9(1). Additionally, according to Article 13(4) first subparagraph the exemptions laid down in Article 9(5) and (6) shall apply *mutatis mutandis* to the notification requirements under Article 13 which refers to financial instruments. This means that all types of holdings are subject to the same type of requirements but also to the same exemptions.

28. However, the question as to whether aggregation of all financial instruments applies in the case of the market making and trading book exemptions remains unresolved. It is necessary to address this issue as leaving it unresolved is likely to lead to different interpretations across Member States, effectively preventing harmonisation.

29. In analysing whether the same principle of horizontal aggregation of all types of Article 9, 10 and 13 holdings should apply to the market making and trading book exemptions and respective thresholds, ESMA has weighed the TD's call for enhanced transparency against the need to avoid unnecessary burdens for credit institutions and investment firms with positions in shares and financial instruments for resale and/or the intention of benefiting in the short term from actual and/or expected differences between buying and selling prices or from other price or interest rate variations.

30. Taking into account these two fundamental principles of the revised TD, ESMA has considered whether the 5 % threshold should only be used to disclose Article 9 and 10 holdings or if this should also include holdings of Article 13 financial instruments. According to the first alternative, two separate buckets of up to 5 % each would exist; one consisting of Article 9 and 10 shares and another with Article 13 financial instruments. Thus, a credit institution or investment firm could

hold as a market maker or in its trading book a combined position in a share of up to the double of the actual respective threshold. According to the second alternative, all Article 9, 10 and 13 holdings should be aggregated in a single bucket up to the 5 % threshold mentioned in Article 9(5) and (6). In accordance with this alternative a credit institution or investment firm could have up to 10 % and 5 % under Article 9(5) and (6) respectively in a combined position of Article 9, 10 and 13 holdings.

31. The two alternatives are illustrated in the table below:

Table 1: Different approaches to horizontal aggregation

Disaggregation	*First bucket contains*	*Second bucket contains*
	Article 9 and 10 holdings	**Article 13 holdings**
Aggregation	*Single bucket contains*	
	Article 9, 10 and 13 holdings	

32. Article 9(6b) mandates ESMA to specify the method of calculation of the **5 % threshold** which in our opinion provides a clear quantitative limit that should not be crossed. Considering the low threshold of the exemption and the condition that voting rights are not to be exercised, the exemption ensures that intermediaries and investors would not be burdened by unnecessary information requirements.

33. Moreover, the aggregation of all Article 9, 10 and 13 holdings keeps the principle intact that all financial instruments which are considered to be economically equivalent to shares should be treated like shares for the purposes of notification requirements. Finally, the aggregation of all holdings comprising Articles 9, 10 and 13 instruments is the only approach capable of preserving the thresholds mentioned for the trading book and market maker exemptions. Disaggregation of holdings of different types would permit an increase of the 5 % threshold within the trading book if a credit institution or an investment firm held a combined position in a share. Eventually, a credit institution or investment firm could end up with a combined position (shares and Article 13(1) financial instruments) of at least 10 % in the trading book, whereas for the market maker this figure could reach 20 %.

34. It should be noted that in addition to the above mentioned figures, there is also the minimum 5 % threshold generally applicable under Article 9(1) to holdings not covered by any exemption.

35. **In conclusion, ESMA considers that the second alternative, i.e. aggregation of all holdings under Articles 9, 10 and 13, is most compatible with the revised TD as one of the purposes of the revised TD is to take into account holdings of financial instruments considered to be economically equivalent to shares for the purposes of calculating voting rights. Therefore, ESMA proposes the following wording for Article 2 of the draft RTS:**

    "For the purposes of calculation of the 5 % threshold provided for in Article 9(5) and (6), holdings under Article 9, 10 and 13 shall be aggregated."

Q3: Do you agree with the ESMA proposal of aggregating voting rights held directly or indirectly under Articles 9 and 10 with the number of voting rights relating to financial instruments held under Article 13 for the purposes of calculation of the threshold referred to in Article 9(5) and (6)? If not, please state your reasons.

Q4: Can you estimate the marginal cost of changing your general major shareholding disclosure system for the purposes of notification of trading book and market making holdings, i.e., having different buckets for the purposes of the exemptions? Please distinguish between one-off costs and on-going costs.

b. Vertical aggregation – Aggregation of holdings of financial instruments within a group of companies in relation to the trading book and market making exemptions

36. The second part of the mandate concerns the specification of the method of calculation of the 5 % threshold in the case of a group of companies. In ESMA's understanding, this part of the mandate concerns the question of whether positions held in the trading book or by a market maker should be aggregated at group level or disclosed at individual company level when the respective exemptions apply.

37. ESMA considers that the principle of aggregation at group level would be in accordance with the TD spirit. In our opinion this reading is confirmed by taking into account the existing rules on major shareholdings that refer to corporate groups.

38. The TD does not define the concept of "group", nor is the word used elsewhere than in Article 9(6b). However, the concept was already implicit in Article 10(e) and 12 which refer to the "parent undertaking" and the "controlled undertaking". These concepts are further used to assess the conditions of independence between the "parent undertaking" and a "controlled company" in the context of portfolio management holdings under Directive 85/611/EEC. According to the latter, such concepts have the meaning defined in Directive 2013/34/EU[6] whereby a "group" means a parent undertaking and all its subsidiary undertakings, a "parent undertaking" means an undertaking which controls one or more subsidiary undertakings and a "controlled undertaking" means an undertaking controlled by a parent undertaking, including any subsidiary undertaking of an ultimate parent undertaking.

39. On this basis, ESMA considers it unnecessary to further define "group" as the concept is already established in the market and it is comprehensible in the context of the overall corporate regulatory system of the EU.

[6] Directive 2013/34/EU of the European Parliament and of the Council of 26 June 2013 on the annual financial statements, consolidated financial statements and related reports of certain types of undertakings.

40. Putting the above definitions into practice, aggregation at group level means that the group will disclose all holdings owned by the parent undertaking and subsidiary companies when that holding reaches the notification threshold. Aggregation at individual company level, on the other hand, means that companies notify their holdings when they reach the threshold individually, regardless of the relationship between the companies.

41. The TD's main rule of major shareholding disclosure remains Article 10(e) under which the final beneficial owner, e.g. the parent undertaking, has to disclose any voting rights which are held, or may be exercised within the meaning of points (a) to (d) of said Article, by an undertaking controlled by that person or entity. Furthermore, ESMA considers that the reference to Article 12(4) and (5) in the wording of Article 9(6b) already implies that in principle, the different holdings under Article 9, 10 and 13 shall be aggregated on group level in the case of groups.

42. **The rules above indicate that for the purposes of notifying a major shareholding on an issuer, a group should be treated as a single investor because of the existing control relationships which normally restrict the independent use of voting rights by the subsidiary. Accordingly, ESMA is of the opinion that the main rule of aggregation of holdings in the case of a group should be aggregation at group level. Hence, having regard to the TD's existing group rules, ESMA proposes Article 3(1) of the draft RTS to state the following:**

    "For the purposes of calculation of the 5 % threshold provided for in Article 9(5) and (6), holdings shall be aggregated at group level."

Q5: Do you agree that, in the case of a group of companies, notification of market making and trading book holdings should be made at group level, with all holdings of that group being aggregated (Article 3(1))?

43. According to the wording of the Article 9(6b) mandate, ESMA is also required to take into account Article 12(4) and (5). An exception to the general rule of aggregation is provided in these provisions whereby asset management and portfolio management holdings can be disaggregated when the voting rights attached to it are exercised in the best interest of those on whose behalf the holdings are managed. Even in this case, the subsidiary should be able to exercise the voting rights referred to those holdings independently from the parent undertaking. Based on the above, ESMA believes that the reference to Article 12(4) and (5) in Article 9(6b) permits two alternative versions of the RTS:

Option 1

44. The reference can be read in a literal sense, meaning that the reference is limited to only Article 12(4) and (5) and that where an investment firm and/or management firm exists within the group, the exemption from aggregation would apply at group level under the terms laid down in Article 12(4) and (5), i.e. compliance with requirements of independence.

45. According to this option, the reference to Article 12(4) and (5) is made for the sake of clarification only, reassuring the reader that the general rules of disaggregation already in place apply when an entity mentioned in those provisions exists within the group.

46. Consequently, the assessment of independence between the parent undertaking and the subsidiary is needless because trading book or market making holdings will always be aggregated with the group holdings. Only Article 12(4) and (5) portfolio management holdings can be disaggregated, in case the group has a management or investment firm conducting such activity.

47. During the revision process of the TD, CESR proposed that holdings of all instruments (Article 9, 10 and 13) should be aggregated when considering the trading book and market maker exemptions and that the threshold should be calculated at group level where exemptions set out in Articles 12(4) and 12(5) do not apply[7].

48. While option 1 is in line with CESR's line of thinking, it broadly preserves the existing approach and maintains the "status quo".

49. Option 1 enhances transparency because only Article 12(4) and (5) portfolio management holdings are undisclosed and because this option keeps credit institutions and investment firms out of the scope of the exemptions to aggregate trading book and market making holdings at group level. However, the greatest disadvantage of this option seems to be that it does not take into account that positions held as a market maker or in the trading book are not used to exert influence on the issuer, but instead are merely held for resale and/or taken on by the institution with the intention of benefiting in the short term from actual and/or expected differences between buying and selling prices or from other price or interest rate variations. The lack of interest in the corporate control of the issuer is reflected in the short-term nature of such positions.

Option 2

50. An alternative reading is that the reference to the exemption of aggregation at group level provided for in Articles 12(4) and (5) should be understood as a reference to the principle of independence and the conditions laid down in the before mentioned Articles. Hence, the holdings held in the trading book of a credit institution or investment firm or in the capacity of a market maker should not be aggregated with any other holdings of the group, as long as conditions of independence apply.

51. The difference between Option 1 and 2 can be illustrated by the figure below. The dark blue holdings are the ones that can currently be disaggregated under Article 12(4) and (5). The light blue ones are those that under Option 2 could be added to the exemption from aggregation at group level:

[7] CESR's Response to Consultation on the Modernisation of the Transparency Directive (CESR/10-1275b Annex), p. 6.

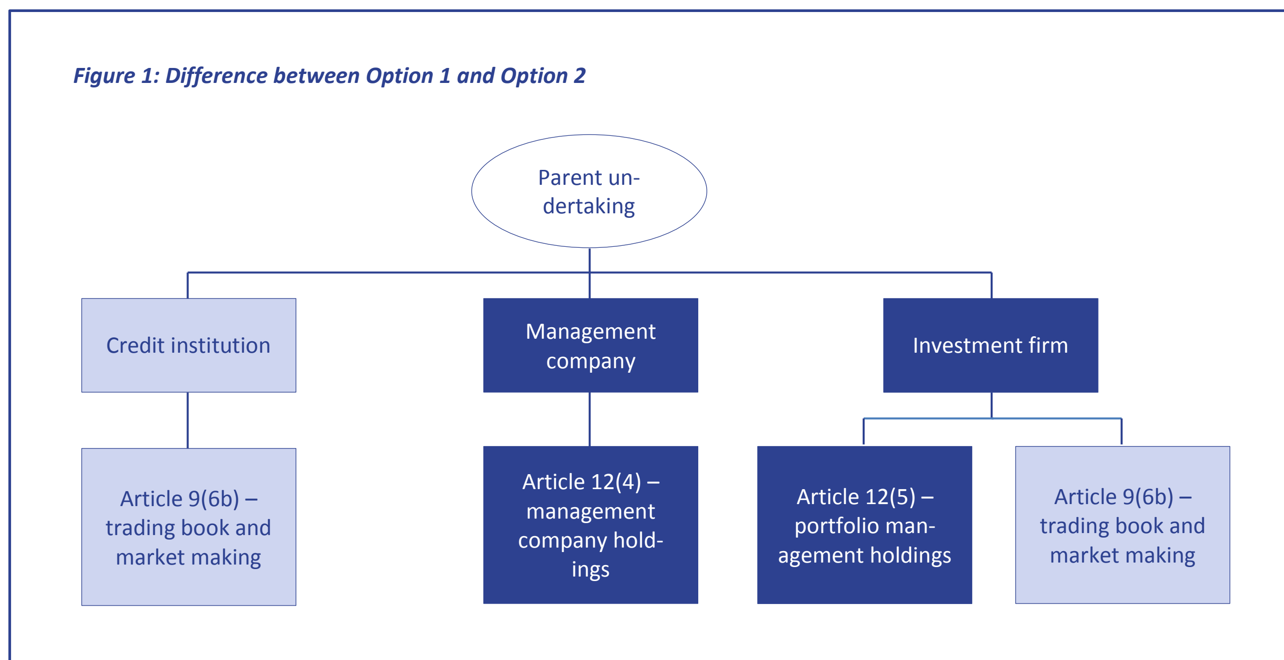

Figure 1: Difference between Option 1 and Option 2

52. ESMA considers that the wording of the mandate allows the wider interpretation of the reference to Article 12(4) and (5) set out under Option 2.

53. This alternative contains two elements for consideration. Firstly, it extends the subjective scope of the exemption from disaggregation provided for in Article 12(4) and (5) to also include credit institutions and investment firms in relation to its trading book and market making holdings. In fact, the market making activity can be exercised both by a credit institution and an investment firm which are authorised to perform such activity under MiFID. Additionally, the trading book exemption benefits credit institutions and investment firms.

54. Regarding this first element for consideration, it should be noted that the trading book and market maker exemptions operate separately, thus a single credit institution or investment firm can exceed the 10 % threshold without any disclosure obligation. In this context, lack of transparency is amplified in the case of a group, under Option 2, even though according to supervisory experience it seems relatively unlikely to find more than one firm within the group acting as a market maker in the same issuer. The vertical disaggregation rule of financial instruments held in the trading book may, however, legitimise a situation of a highly concentrated ownership structure of the issuer enhancing a lack of transparency to this effect (when shares are held in the trading book of more than one undertaking in the same group).

55. The practical consequences of adopting Option 2 can be illustrated by the following figure:

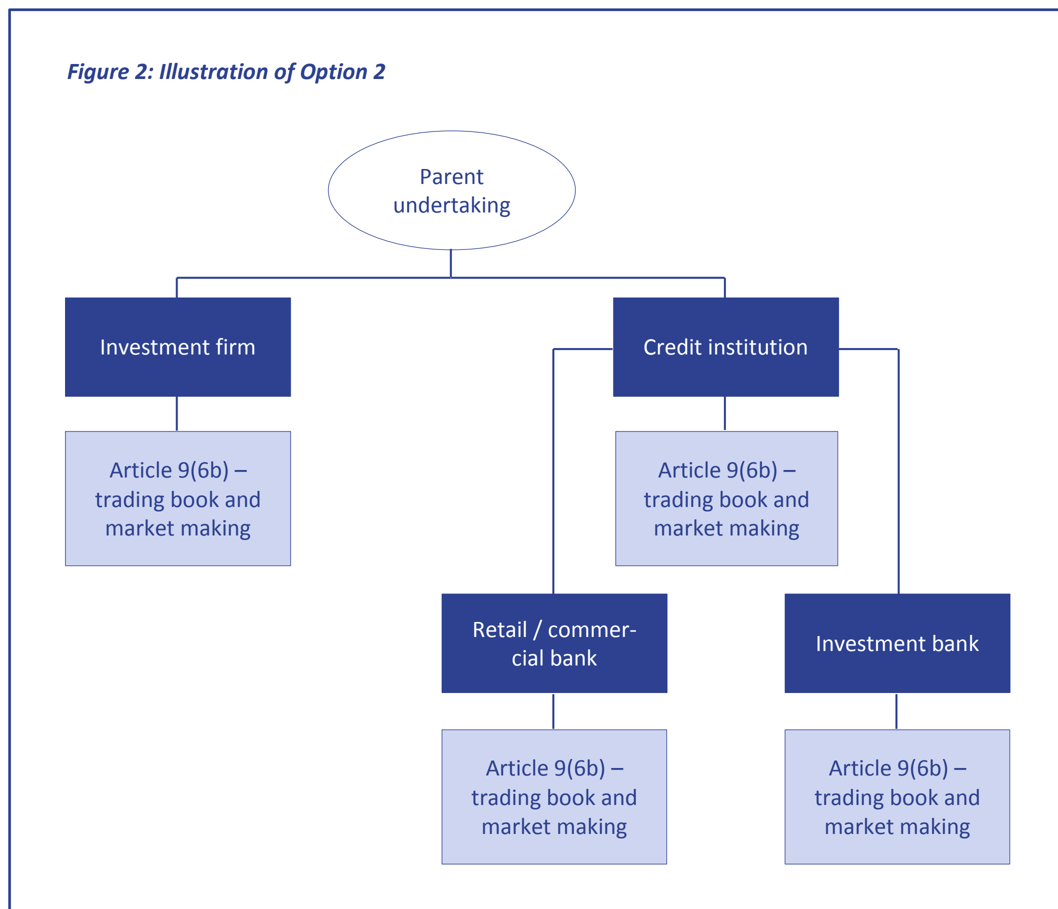

Figure 2: Illustration of Option 2

56. Looking at the figure, it can be concluded that when there are multiple levels of controlled undertakings within a group, it is possible to have as many trading books as the number of entities and thus to expand the room for trading book and market making holdings not subject to notification requirements. Such a situation may create a lack of transparency regarding the actual holdings of a group.

57. The second element for consideration is the assessment of independence between the parent undertaking and the subsidiary undertaking and the question is what should be the content of such an independence assessment. In this connection, it is to be noted that the existing test of independence under Article 12(4) and (5) requires that both the management company and the investment firm exercise voting rights regarding the portfolio management holdings independently from the parent undertaking.

58. An identical concept of independence cannot be used in the context of the market making and trading book exemptions because in order for a credit institution or investment firm to benefit from the existing market and trading book exemptions, voting rights connected to these positions are not to be exercised. Accordingly, having a similar independence requirement for the purpose of disaggregation would be meaningless.

59. In the context of the market maker and trading book exemptions, any assessment of independence should refer to “other” holdings in the same issuer held by the credit institution or investment firm which are unrelated to the trading book or market maker activity. Thus the parent undertaking would be able to use the Article 12(4) and (5) principles to disaggregate trading book and market making holdings provided the subsidiary exercises its voting rights – referred to holdings not held in the trading book or unrelated with the market making activity – independently from the parent undertaking.

60. The criteria of independence relate to the exercise of voting rights; Article 12(4) and (5) to voting rights attached to shares managed by the respective company and Article 9(6b) to voting rights attached to shares held in general.

61. ESMA proposes the conditions of independence to be complied with by the parent undertaking of credit institutions and investment firms intending to benefit of an exemption from aggregation at group level regarding market making activities or the trading book holdings to be based on the ones laid down in Article 10 of the Commission Directive. Using these conditions would prevent a situation where analogous cases (TD Article 9(5) and (6) and Article 12(4) and (5), respectively) are treated differently.

62. We are aware that under the Takeover Bids Directive[8] a parent undertaking and its subsidiary are always presumed to be “acting in concert” and this presumption is un-rebuttable in some Member States. Furthermore, in the national rules of a number of Member States, the same factors will trigger a mandatory takeover bid and the disclosure of voting rights. However, the Commission Directive and the Takeover Bids Directive address intersecting but not totally coincidental issues. Whilst the Takeover Bids Directive focuses on control, the TD’s aim is to provide transparency to the market concerning ownership structure.

63. Accordingly, ESMA proposes that the parent undertaking of a credit institution or investment firm wishing to benefit from the exemption in relation to holdings under Article 9(5) and (6) should ensure that:

    a. the credit institution or investment firm exercises its voting rights unrelated to the shares held in connection with the trading book and market making activities independently from its parent undertaking; and
    b. it sends a declaration as to its status to the competent authority of the issuer of the shares.

a. Credit institution’s/investment firm's independence from its parent

64. The parent undertaking must be able to demonstrate on request that:

    - the organisational structures of the parent undertaking and the credit institution or investment firm are such that voting rights are exercised independently; and
    - the persons deciding how voting rights are to be exercised are not the same for the parent undertaking and the credit institution or investment firm and such persons act autonomously from one another.

[8] Directive 2004/25/EC of the European Parliament and of the Council of 21 April 2004 on takeover bids.

b. Declaration to the competent authority

65. In order for the competent authority to know who wants to make use of the exemption, it is necessary for the parent undertaking to make a declaration to the relevant national authority competent within the TD, i.e. the competent authority of the issuer of the shares.

66. It is, however, important to point out that if other factors are present which run counter to the declaration of independence, such will be taken into account by NCAs. In other words, ESMA is of the opinion that where the parent undertaking has fulfilled the requirements mentioned above in para 63, this does not constitute binding proof in the establishment of independence.

67. Option 2 enables the parent undertaking to disaggregate holdings both of a credit institution and an investment firm under the trading book and market maker exemptions. The following examples illustrate how the provision would work in practice:

Table 2: Illustration of Option 2

	Holdings	*Aggregation and disclosure requirements*
Example 1	Parent undertaking: 3 % Subsidiary A (investment firm, credit institution or market maker, all independent): 3 % Subsidiary B (investment firm, credit institution or market maker, all independent): 3 %	No aggregation required as both subsidiaries are independent. No disclosure required as neither trading book holding exceeds the threshold.
Example 2	Parent undertaking: 3 % Subsidiary A (investment firm, credit institution or market maker, all independent): 3 % Subsidiary B investment firm, credit institution or market maker, all independent): 9 %	No aggregation required as both subsidiaries are independent. Disclosure required of trading book holding of subsidiary B as the holding exceeds the threshold. Disclosure to be performed by subsidiary B.
Example 3	Parent undertaking: 4 % Subsidiary A (investment firm, credit institution or market maker, all non-independent): 3 % Subsidiary B (investment firm, credit institution or market maker, all independent): 3 %	Aggregation required of trading book holdings of parent undertaking and subsidiary A as subsidiary A is not independent. No aggregation required with subsidiary B as subsidiary B is independent. Disclosure required of aggregated trading book holding of parent undertaking and subsidiary A as the aggregated holding exceeds the threshold. Disclosure to be performed by parent undertaking.
Example 4	Parent undertaking: 4,9 % Subsidiary A (investment firm, credit institution or market maker, all independent): 4,9 % plus 9,9 % in the capacity of market maker Subsidiary B (investment firm, credit institution or market maker, all independent): 4,9 %.	No aggregation required as the subsidiaries (A and B) are independent (and conditions provided by articles 9(5) and 9(6) are satisfied).

68. The above table does not address the question of aggregation between subsidiaries when neither subsidiary is controlling the other. This is because the main rule of major shareholding disclosure at group level in the TD is that the controlling person or legal entity has to aggregate its own holdings with holdings of its subsidiaries (Article 10(e)). By logic, this excludes subsidiaries from having to aggregate their individual holdings when there is no control relationship between them.

69. This position is in line with the CESR technical advice on which the Commission Directive was based[9]:

"There are circumstances where neither the controlled undertakings nor the controlled undertaking(s) and the controlling natural person or legal entity have reached a trigger threshold at an individual level, but they may have reached a trigger threshold together. Under these cir-

[9] CESR's Final Technical Advice on Possible Implementing Measures of the Transparency Directive, (CESR/05/407), p. 31-32.

cumstances, the controlled undertakings have no duty to notify (because they do not reach a trigger threshold at an individual level). However, the controlling natural person or legal entity, who is considered to have control over the exercise of the voting rights of the controlled undertaking(s), will have to notify when either the controlled undertakings or the controlled undertakings and the controlling natural person or legal entity have crossed a threshold together. To do so, the controlling natural person or legal entity will need to aggregate the holdings."

70. Currently a parent undertaking can only disaggregate trading book holdings of companies within the group in the cases laid down in Article 12(4) and (5) (subsidiary management companies and investment firms, respectively). Applying the same principle to credit institutions and investment firms with respect to trading book and market making holdings would inflict fewer costs on the group because fewer holdings would have to be disclosed. On the other side, ESMA understands that expanding the exemption could lead the way to a decrease of transparency, potentially enabling a group of companies to veil a relevant stake as illustrated in Case 4 of Table 2 above. While the potential costs for the market arising from such an undisclosed stake could be very high, the probability of this situation occurring is very small.

71. In ESMA's view, evidence provided by the respondents of this CP on the consequences of Option 2 will be crucial in confirming its validity.

72. **On the basis of the above considerations, ESMA proposes for consultation the following wording for Article 3(2) to (7) of the draft RTS:**

"2. By derogation from paragraph 1, the parent undertaking of a credit institution or investment firm shall not be required to aggregate its holdings in the trading book with those held in the trading book of a credit institution or investment firm or in the capacity of a market maker provided such credit institution or investment firm exercises independently its voting rights in respect of shares not held in the trading book and for the purpose of market making activities independently from the parent undertaking.

3. For the purposes of paragraph 2, a parent undertaking of a credit institution or investment firm must not interfere by giving direct or indirect instructions or in any other way in the exercise of the voting rights held by that credit institution or investment firm.

4. A parent undertaking of a credit institution or investment firm who wishes to make use of the exemption shall, without delay, notify the following to the competent authority of the home Member State of issuers whose voting rights are attached to holdings of the investment firm, credit institution or market maker:

- ***(a) a list of the names of such credit institution(s) or investment firm(s), indicating the competent authorities that supervise them or that no competent authority supervises them, but with no reference to the issuers concerned;***
- ***(b) a statement that for each such credit institution or investment firm, the entity in the group complies with the condition laid down in paragraph 3.***

The parent undertaking shall update the list referred to in point (a) on an ongoing basis.

5. Where the parent undertaking intends to benefit from the exemptions only in relation to the financial instruments referred to in Article 13 of Directive 2004/109/EC, it shall notify to the competent authority of the home Member State of the issuer only the list referred to in point (a) of paragraph 4.

6. Without prejudice to the application of Article 24 of Directive 2004/109/EC, a parent undertaking of a credit institution or investment firm shall be able to demonstrate to the competent authority of the home Member State of the issuer on request that:

(a) the organisational structures of the parent undertaking and the credit institution or investment firm are such that the voting rights are exercised independently of the parent undertaking;

(b) the persons who decide how the voting rights are to be exercised act independently.

The requirement in point (a) shall imply as a minimum that the parent undertaking and the credit institution or investment firm must have established written policies and procedures reasonably designed to prevent the distribution of information between the parent undertaking and the credit institution or investment firm in relation to the exercise of voting rights.

7. For the purposes of paragraph 3, 'direct instruction' means any instruction given by the parent undertaking, or another controlled undertaking of the parent undertaking, specifying how the voting rights are to be exercised by the investment firm or credit institution in particular cases.

'Indirect instruction' means any general or particular instruction, regardless of the form, given by the parent undertaking, or another controlled undertaking of the parent undertaking, that limits the discretion of the investment firm or credit institution in relation to the exercise of the voting rights in order to serve specific business interests of the parent undertaking or another controlled undertaking of the parent undertaking."

Q6: Do you agree that an exemption to notify at group level can apply if an entity meets the independence criteria set out under paragraph 72 (Option 2)?

Q7: Please provide an estimate on how many times a year would your group have to report a major disclosure under the current regime in comparison to Option 1. Please include an estimate of the one-off or on-going costs involved.

Q8: Do you think that Option 2 poses any further enforceability issues than Option 1? If yes, what kind of issues can you foresee arising out of it? Can you propose an alternative approach?

III.II. Draft regulatory technical standard on the method of calculating the number of voting rights referred to in Article 13(1a)(a) in the case of financial instruments referenced to a basket of shares or an index

Mandate

73. The mandate given to ESMA in Article 13(1a)(a) of the revised TD is to specify the method for calculating the number of voting rights in the case of financial instruments referenced to a basket of shares or an index.

Scope

74. Financial instruments referenced to a basket of shares or an index are subject to notification requirements under TD Article 13. As such, it is necessary to have a clear and harmonised regime regarding the treatment of baskets of shares and indices.

75. ESMA is of the view that Article 13(1a) already provides part of the method for calculating the voting rights attached to such financial instruments by requiring the use of the full notional amount of shares underlying the financial instrument in the calculation, except where the financial instrument provides exclusively for a cash settlement, in which case the number of voting rights shall be calculated on a delta-adjusted basis.

76. In further specifying this method for calculating the voting rights attached to such financial instruments referenced to a basket of shares or an index, ESMA suggests taking into account the weight of the financial instrument in the basket or index. Furthermore, interpreting the mandate, ESMA considers that an assessment of whether holding such financial instrument represents a sizeable interest in the issuer should determine whether voting rights attached to the financial instrument should be calculated and, ultimately, subject to notification requirements.

77. Our proposal is that a financial instrument referenced to a basket or index will be subject to the notification requirements laid down in Article 13(1) if the underlying financial instruments:

    a. represent 1 % or more of voting rights attached to shares of the specific issuer; or

    b. represent 20 % or more of the value of the securities in the basket/index.

78. The 1 % threshold aims at taking into account only holdings in a single issuer with a certain weight. The threshold represents the point at which a holder of shares should start to aggregate these holdings with others it may have in the same underlying issuer. The threshold has been set at a relatively high level to offer a degree of flexibility and takes into account that where relevant instruments make up only a small part of the basket or index, market manipulation by this method is unlikely to take place as it would not be cost efficient.

79. The 20 % threshold has been set to allow for a degree of portfolio diversification suitable for investment in financial instruments referenced to a basket of shares or an index rather than promoting a focus on single shares. This threshold goes as far as possible without compromising market transparency or creating a serious risk of abuse. Further supporting this figure is the fact that stock market indices run by stock exchanges use a cap so that the maximum weight of an issuer remains under 20 % in order to account for sufficient diversification.

80. Though diversification is more a risk management measure, it does relate to the concern regarding the weight of an issuer in a financial instrument. In addition, it is more straightforward to use than a different mechanism connected with the percentage of voting rights. Quantitative thresholds based on diversification reasoning are also set in other financial market sectors, e.g. for undertakings for collective investment in transferable securities (UCITS). In this regard, Article 53 of the UCITS Directive[10] sets, as a general rule, a cap of 20 % for investment in shares or debt securities issued by the same body when, according to the fund rules or instruments of incorporation, the aim of the UCITS' investment policy is to replicate the composition of a certain stock or debt securities index.

81. Consequently, the proposed combination of the two thresholds would guarantee that only relevant disclosures are required, resulting in a small number of notifications per year and thus minimising compliance costs for investors.

82. The 20 % threshold currently exists in six Member States, of which two Member States also use the 1 % threshold. Based on these numbers and the above reasoning, ESMA believes that selecting these thresholds will facilitate implementation of the RTS and make it less costly, as the thresholds are in line with legislation already in place and market participants are accustomed to such thresholds.

83. **Accordingly, ESMA suggests the following wording for Article 4(1) of the draft RTS:**

"1. Voting rights in the case of a financial instrument subject to notification requirements laid down in Article 13(1) and which is referenced to a basket of shares or an index shall be calculated on the basis of the weight of the share in the basket or index and if at least one of the following conditions apply:

(a) The shares in the basket or index represent 1 % or more of voting rights attached to shares of the specific issuer; or

(b) The shares in the basket or index represent 20 % or more of the value of the securities in the basket or index."

Q9: Do you agree with the proposal that financial instruments referenced to a basket or index will be subject to notification requirements laid down in Article 13(1a)(a) when the relevant securities represent 1 % or more of voting rights in the underlying issuer or 20 % or more of the value of the securities in the basket/index or both of the above?

Q10: Are there any other thresholds we should consider?

Q11: Please estimate the number of disclosures you would have to make per year should the above mentioned thresholds be adopted. Please also provide an estimate of the compliance costs associated with the disclosure (please distinguish between one-off and on-going costs).

[10] Directive 2009/65/EC of the European Parliament and of the Council of 13 July 2009, on the coordination of laws, regulations and administrative provisions relating to undertakings for collective investment in transferable securities (UCITS).

84. **Where a financial instrument is referenced to a series of baskets which are under the thresholds individually but would exceed the thresholds if added and totalled, ESMA would not expect disclosure on an aggregated basis, as it would not be cost-effective to build a stake by obtaining small holdings in different baskets, extracting them from each basket and then aggregating. Therefore, the following wording is proposed for Article 4(2) of the draft RTS:**

"2. By derogation from paragraph 1, financial instruments referencing a series of baskets which are individually under the thresholds mentioned in paragraph 1 but would exceed the thresholds if added and totalled are not subject to notification requirements."

Q12: Do you agree that a financial instrument referenced to a series of baskets which are under the thresholds individually but would exceed the thresholds if added and totalled should not be disclosed on an aggregated basis?

III.III. Draft regulatory technical standard on the methods of determining delta for the purposes of calculating voting rights relating to financial instruments which provide exclusively for a cash settlement

Mandate

85. Article 13(1a)(b) of the revised TD mandates ESMA with specifying the methods for determining delta for the purposes of calculating voting rights relating to financial instruments which provide exclusively for a cash settlement.

Scope

86. Delta is a measure of the sensitivity of a financial instrument's price to the changes in the price of the underlying and estimates the number of shares the investor should hold for each financial instrument in order to minimise risks in the portfolio (i.e. hedging).

87. ESMA considers it important to point out that whereas the definition of delta as one of the sensitivities of a financial instrument is straightforward, the definition of methods for determining delta poses several difficulties. With this in mind, ESMA considers that there are two options in order to fulfil the mandate:

Option 1

88. Following a prescriptive approach and demanding the calculation of voting rights according to one or more precise delta-adjusted methods, potentially specific to the type of financial instrument.

89. However, ESMA sees a number of difficulties connected with applying such an approach. Firstly, a prescriptive approach has limitations due to the existence of non-standard financial instruments and the fast evolution of financial products which would make it difficult to establish a formula (or several formulas, each specific to the type of financial instrument) capable of ade-

quately covering the range of financial instruments referred to shares. Secondly, financial innovation would render it necessary to continuously update formulas established at a given point in time. Thirdly, prescribing a single delta formula would be unlikely to achieve total harmonisation as a difference would remain in the market data and assumptions used in the parameters which are part of the calculation. Fourthly, ESMA considers it unduly burdensome to impose a formula on the market.

90. In light of these considerations, ESMA has decided against proposing a specific formula.

Option 2

91. Following a principle-based approach, allows investors to use generally accepted industry standard pricing models to calculate voting rights in the case of financial instruments which are exclusively cash-settled.

92. ESMA has the following considerations regarding this approach. First of all, a principle-based approach was strongly supported and recommended by representatives of the financial industry during the stakeholder round table conducted by ESMA on 26 September 2013. Second of all, ESMA has looked into other areas of financial regulation where the delta-adjusted method is also being used, particularly the CRD IV[11] and the CRR[12] and its implementing rules which are being prepared at national level in coordination with national competent authorities. In these areas, a principle-based approach is applied. Following a similar approach in the TD area would contribute to minimising the burden on market participants.

93. ESMA expects that calculating delta under a principle-based approach will be very straightforward for many firms as delta is a long established risk measure which is routinely used as part of risk management. This approach also has the benefit of allowing national competent authorities to monitor the method of calculation as the investor would provide its own model.

94. Based on these considerations, ESMA favours a principle-based approach, provided of course that it is in line with Article 13(1a) (e.g., no-netting of short and long positions).

95. In order to specify the methods for determining delta within a principle-based approach, ESMA considers it necessary to identify the methodology to follow and the parameters to use. Ancillary rules about governance and IT systems should also be set.

96. On an introductory note, ESMA wishes to point out that Article 13(1a) provides for the delta-adjusted method for all cash-settled financial instruments. However, we are of the view that the delta-adjusted method is only to be applied where the financial instrument does not have a linear, symmetric pay-off profile in line with the underlying share; that is, where the instrument does not have a 'delta 1' profile.

[11] Directive 2013/36/EU of the European Parliament and of the Council of 26 June 2013 on access to the activity of credit institutions and the prudential supervision of credit institutions and investment firms, amending Directive 2002/87/EC and repealing Directives 2006/48/EC and 2006/49/EC

[12] Regulation (EU) No 575/2013 of the European Parliament and of the Council of 26 June 2013 on prudential requirements for credit institutions and investment firms and amending Regulation (EU) No 648/2012

97. There is no need to calculate delta for instruments with a delta 1 profile as delta for such instruments will be equivalent to the notional amount of the underlying shares. This should be the case for futures. For financial instruments which do not have a linear pay-off profile in line with the underlying share, e.g. options, the concept of generally accepted industry standard pricing models is further specified by the parameters such models should include.

Methodology

98. Turning to methodology, ESMA proposes using generally accepted industry standard pricing models to calculate voting rights in the case of financial instruments which are exclusively cash-settled.

99. Our proposal is based on the fact that most investors will use standard pricing models such as Black-Scholes for calculating delta. Even the calculation of delta for non-standard derivatives will be based on variations of standard pricing models.

100. In addition, ESMA suggests that investors should take the last closing price of the underlying share into account when determining delta. This rule aims to ensure that the price used by all market participants is the same, thus pursuing accuracy in reporting.

101. Furthermore, voting rights, and thereby delta, should be calculated daily. This rule would reinforce accuracy since frequent calculations of delta ensure that the information about the total voting rights accessible to an investor is as up-to-date and as precise as possible.

Parameters

102. The list of parameters to use when determining delta cannot be exhaustive because of the diversity of financial instruments providing exclusively for a cash settlement. The approach suggested by ESMA relies on the assumption that a number of parameters constituting a common core to all generally accepted standard pricing models can be identified.

103. In our view, such parameters consist of the interest rate, dividend payments, time to maturity, volatility and price of the underlying instrument.

Governance

104. According to a principle-based approach delta shall be calculated using an appropriate model. In addition to utilising the parameters set out above, ESMA would consider a model to be appropriate where certain principles are respected.

105. Firstly, there should be proportionality between the level of sophistication of the calculation model and the complexity and risk of each financial instrument. Ideally, where deltas are calculated daily by an exchange, this information should be considered by investors. Where it is possible for an investor to calculate his own delta – e.g. for relatively simple options – and he chooses to do so, the investor would be expected to use generally accepted industry standard pricing models, e.g. Black-Scholes. ESMA is aware that whilst European options[13] will not require highly complex

[13] European and American options differ from one another because European options can be exercised only on the expiration date itself and American options can be exercised at any time up to the expiration date.

models, American and exotic options (e.g. knockout options, barrier options) will require more complex models in order to be accurately calculated.

106. Secondly, investors should consistently use the same method to calculate delta for a particular financial instrument. This rule is intended to provide the market with a number of voting rights which is calculated in a consistent manner over the lifetime of the financial instrument.

IT systems

107. ESMA believes that some investors will possess the means to do delta calculations and will have their own systems to perform such calculations. As long as these systems respect the defined methodology, investors may use their own systems. When using their own IT systems to calculate delta, investors should ensure that computational models used to run the calculation of delta guarantee consistent, accurate and timely reporting of voting rights.

108. By suggesting a principle-based approach and proposing the use of generally accepted industry standard pricing models, ESMA acknowledges that some professional investors possess the means to perform the complex delta calculation and can apply familiar methods already in place for such calculations. This would be the case for credit institutions, investment firms and management firms. Other types of entities or natural persons not necessarily accustomed to such methods would have to seek advice/assistance in order to perform the calculation. Stock exchanges are calculating delta for exchange-traded equity derivatives and data providers are calculating delta both for exchange-traded equity derivatives and OTC derivatives. Such delta calculations – which in the case of some data providers are public – can be used by investors wishing to calculate the number of voting rights relating to a cash-settled financial instrument.

109. **Based on these reflections, ESMA proposes the following wording for Article 5 of the draft RTS:**

"1. The number of voting rights relating to an exclusively cash settled financial instrument with a linear, symmetric pay-off profile with the underlying share shall be calculated on a delta-adjusted basis with cash position being equal to 1.

2. The number of voting rights relating to an exclusively cash settled financial instrument without a linear, symmetric pay-off profile with the underlying share shall be calculated on a delta-adjusted basis, using generally accepted standard pricing models.

3. A generally accepted standard pricing model is one that is widely used in the finance industry and sufficiently robust to consider the elements that are relevant to the valuation of the financial instrument. Those elements that affect the valuation include at least the following:

(a) interest rate;

(b) dividend payments;

(c) time to maturity;

(d) volatility;

(e) price of underlying share.

4. When determining delta the holder of the financial instrument shall ensure that:

(a) the model used covers the complexity and risk of each financial instrument;

(b) the same model is used in a consistent manner for the calculation of the number of voting rights of a given financial instrument.

5. IT systems used to run the calculation of delta shall ensure consistent, accurate and timely reporting of voting rights.

6. The number of voting rights shall be calculated daily, taking into account the last closing price of the underlying share. The holder shall notify the issuer when he reaches, exceeds or falls below the thresholds provided for in Article 9(1).”

Q13: Do you agree that our proposal for the method of determining delta will prevent circumvention of notification rules and excessive disclosure of positions? If not, please explain.

Q14: Do you agree with the proposed concept of “generally accepted standard pricing model”?

III.IV. Draft regulatory technical standard on client-serving transactions

Mandate

110. Article 13(4) of the revised TD mandates ESMA with specifying the cases in which the exemptions referred to in Article 9(4), (5) and (6) and in Article 12(3), (4) and (5) apply to financial instruments held by a natural person or legal entity:

1. fulfilling orders received from clients;
2. responding to a client’s requests to trade otherwise than on a proprietary basis; or
3. hedging positions arising out of such dealings.

111. For the purposes of this CP the above mentioned types of transactions will be referred to as “client-serving transactions” and a natural person or legal entity undertaking such transactions will be referred to as “client-serving entity”.

Scope

112. Since it was first proposed to introduce a notification obligation for cash-settled financial instruments, it has been advocated that authorised financial institutions holding positions in cash-settled instruments only to facilitate a client's position should be exempt from this obligation. It is argued that if such an exemption is not provided, both an excessive amount of notifications and notifications of potential lower value to the market could be the consequence.

113. Transactions undertaken within the three situations listed above will by nature all have a professional as the buyer counterparty. From the point of view of the disclosure obligation and a respective exemption, only long positions in a financial instrument are of interest. Finally, a financial in-

termediary has a long position by means of a transaction which was requested by a client or performed because of a client.

114. ESMA has discussed the possible content for the three types of transactions. Previous analysis performed by CESR[14] indicates the following:

115. Case 1 – Fulfilling orders received from clients: If a financial intermediary holds on behalf of a client a financial instrument considered to be economically equivalent to a share, the holder of the instrument is not the financial intermediary but the client. This situation is no different from any other order fulfilment whereby the client will be the holder of the financial instrument. Therefore, the person obliged to notify in this case is the client, and the financial intermediary will not be under the obligation to disclose.

116. Case 2 – Responding to a client's request to trade otherwise than on a proprietary basis: If a bank takes a long position with a client as a result of the client taking a corresponding short position on an underlying share, the bank itself will have a long position referenced to the issuer. The bank has entered into the transaction not for proprietary purposes, but because the client solicited its counterparty's services. However, without an exemption the bank will also have to notify holding a long position in the issuer while only performing its normal business activities.

117. Case 3 – Hedging positions arising out of such dealings: If a bank is the counterparty of an equity swap for a client with a long position, the bank itself will have a short position in the issuer. Normally, the bank will try to hedge its position, buying the shares in the market or holding the shares given as a pledge by the client. Again in this case, the client will notify being the holder of a long position having shares of the issuer as an underlying. Without an exemption, the bank would also be obliged to notify a major shareholding.

118. The common thread in all three types of transactions is that the long position held by the client-serving entity does not primarily serve its own interest and normally will not be used to exert influence on the issuer. But while in Cases 1 and 3 the financial intermediary's economic interest is neutral, in Case 2 the financial intermediary could hold a positive economic interest. In fact the intermediary in Case 2, unless it hedges its position, will hold a positive economic interest, i.e. its long position is not offset by a symmetric short position. For this reason, ESMA has considered whether this case creates a risk of circumvention if a full exemption was put in place.

119. This could theoretically arise for example if the client went short with a financial intermediary and in consequence the financial intermediary held a long position. Again, this would only happen in those very rare cases where a financial intermediary chose not to hedge its long position, which arose purely from its client's request to trade, with a symmetric short position. In such case, it might be asked whether the client would be able to exert influence covertly through the financial intermediary's long position. Nevertheless ESMA considers that this situation is very unlikely to arise in practice as in this situation the client would have either an unhedged short position – and therefore carry its own economic risk – or if the client would hedge the position it would itself have a long reportable position.

120. Hypothetically, a similar situation could also occur where a financial intermediary acting in collusion with a client builds up an undisclosed stake above the TD thresholds by taking advantage of

[14] CESR/09-1215b, CESR proposal to extend major shareholding notifications to instruments of similar economic effect to holding shares and entitlements to acquire shares, p. 14.

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the client-serving exemption. This could theoretically happen if the financial intermediary agreed with its client that the client would go short, enabling the intermediary to claim that its resulting long position fell within the exemption and to suddenly disclose its stake to the market at a later stage.

121. These cases could be particularly problematic in that the client-serving exemption is intended by the legislator to be a full exemption, not limited to a threshold. However, the risk of circumvention is presumably counteracted by other rules: In the case described in paragraph [120], the client going short would be under the obligation to notify its net short position under the very restrictive thresholds of the Short Selling Regulation[15]. Other Directives, such as Market Abuse Directive[16], could also apply. All in all, it seems highly unlikely that a financial intermediary would enter into such transactions to secure a one-off gain at the cost of facing different and possibly severe consequences.

122. However, despite the above analysis, ESMA does not have any concrete evidence to assess the probability of occurrence of the two examples described in para 119 and 120 or of other possible cases of circumvention. Therefore, ESMA would welcome stakeholder views on both our analysis of the likelihood of such circumvention taking place and on its potential costs, compared to the benefits of avoiding an overload of meaningless notifications. Such views are necessary to enable ESMA to assess whether the risk of circumvention outweighs the market efficiency gains implied in the exemption.

Q15: Are these three types of client serving exemptions all appropriate in terms of avoiding excessive or meaningless disclosures to the market? Please provide quantitative evidence on the additional costs borne by financial intermediaries should any of these exemptions not be adopted.

Q16: Can these three types of client-serving exemption allow for a potential risk of circumvention of major shareholdings' disclosure regime?

123. Based on the above reflections, ESMA considers that two options could fulfil the mandate:

Option 1

124. The first option would be to interpret the wording of the mandate in a literal way and in accordance both with Article 290 of the Treaty on the Functioning of the European Union and with *Meroni* case law and specify the cases for client-serving transactions within the sphere of existing exemptions. By doing so, ESMA would clarify the notification regime applicable to financial instruments held by a professional fulfilling orders received from clients or responding to a client's request to trade otherwise than on a proprietary basis or hedging positions arising out of such dealings.

[15] Regulation (EU) No 236/2012 of the European Parliament and of the Council of 14 March 2012 on short selling and certain aspects of credit default swaps

[16] Directive 2003/6/EC of the European Parliament and of the Council of 28 January 2003 on insider dealing and market manipulation (market abuse)

125. The exercise to be undertaken would require comparing the existing exemptions, for instance market making, and assessing whether Article 9(5) would apply to any or all three types of client-serving transactions. Should the answer be positive after analysing the requirements of the exemption, the RTS would clarify that the exemption could be used to cover one or more specific types of client-serving transactions.

126. Article 13(4), first paragraph states that the existing exemptions shall apply *mutatis mutandis* to the notification requirements under the same Article. This means that such exemptions can apply with the changes required for it to adequately address the cases in Article 13 and that ESMA can specify cases to which the already existing exemptions apply. However, based on this assessment of the wording ESMA does not seem to be able to create a new full exemption.

127. CESR defended the existence of a separate exemption for the client-serving transactions instead of the extension of the current exemptions to such transactions. Nevertheless, given the wording of the mandate, ESMA considers it necessary to perform an analysis in order to establish whether a literal interpretation would be sufficient in achieving the legislator's intention, i.e. avoiding unnecessary disclosures to the market.

128. The first exemption to consider is Article 9(4). This Article exempts from the notification requirements laid down in Article 9(1) the acquisition of shares for the sole purpose of clearing and settling within the usual short settlement date. As illustrated with the cases above, client-serving transactions serve different purposes than the ones covered by the clearing and settlement exemption. Thus, this exemption should not be used for such holdings.

129. Regarding the Article 9(4) exemption covering custodians holding shares in their custodian capacity, ESMA considers that the exemption does not cover any of the three types of client-serving transactions as safekeeping financial instruments is different than acquiring them.

130. According to Article 9(5), notification requirements laid down in paragraph 1 of that Article shall not apply to the acquisition or disposal of a major holding reaching or crossing the 5 % threshold by a market maker acting in its capacity of market maker. A market maker is defined in Article 2(1)(n) of the TD as a person who holds himself out on the financial markets on a continuous basis as being willing to deal on own account by buying and selling financial instruments against his proprietary capital at prices defined by him. The market maker provides a price and continuous offer and demand for a share, thus enhancing liquidity.

131. Analysing the three types of client-serving transactions, we conclude that transactions done for clients (fulfilling orders) or because of clients (responding to a client's requests to trade otherwise than on a proprietary basis) fall out of the scope of the market making exemption. As regards hedging activities, these are intended to avoid the exposure to adverse movements in the price and constitute the reverse of the market making activity. By nature the market maker is not working in an intermediary or client-serving capacity but is rather assuming the risk for the transactions entered into. Therefore, hedging also falls out of the scope of the market making exemption.

132. Article 9(6) exempts from notification requirements voting rights held in the trading book as defined in Article 3(1)(54) of the CRD IV which refers to point (86) of Article 4(1) of CRR. According to this provision "Trading book means all positions in financial instruments and commodities held by an institution either with trading intent, or in order to hedge positions held with trading intent." It is to be noted that the trading book exemption was not covering financial instruments which are considered to be economically equivalent to shares, as the disclosure obligation of this type of financial instrument was introduced by the revised TD. Responding to a client's request to

trade otherwise than on a proprietary basis has a nature similar to the content of the trading book definition and for this reason we believe it can be covered.

133. The same reasoning applies in the case of hedging. The trading book exemption is in principle not designed to cover positions held with the sole purpose of facilitating clients' positions. However, it is possible to place such holdings in the trading book and as such, hedging of financial instruments would be covered by the trading book exemption. The practical consequence of this interpretation is that the quantitative cap of 5 % set out for the trading book exemption would have to be used by a credit institution or investment firm to exempt from notification requirements financial instruments held for the purpose of hedging client-serving transactions.

134. Article 12(3) exempts the subsidiary undertaking from performing the notification required in accordance with Article 12(1) if the notification is made by the parent undertaking. The content of this situation is not specific to financial instruments, but takes into account a group structure, (i.e., parent undertaking and subsidiary). As such, it constitutes a procedural rule potentially applicable to all groups. However, it is possible to clarify that a subsidiary natural person or legal entity holding financial instruments will not be required to make a notification if a notification is made by the parent undertaking. It is to be noted that the cases where a natural person could be involved in a group should be rather limited.

135. Article 12(4) grants the parent undertaking of a management company an exemption from the obligation to aggregate its holdings under TD Articles 9 and 10 with the holdings managed by its management company provided that the management company exercises the voting rights independently from the parent undertaking. Portfolio management is the activity performed by the management company under Annex I, Section A(4) of MiFID and it is a different activity than the ones considered in client-serving transactions. Therefore, portfolio and management holdings, on one side, and client-serving holdings on the other are mutually exclusive.

136. The above analysis of the exemptions mentioned in Article 13(4), first subparagraph shows that some of these exemptions do not address client-serving transactions at all – as is the case for the Article 9(4) exemption for custody, clearing and settlement and the Article 9(5) exemption for the market maker.

137. Other exemptions, namely the trading book exemption, can be applied to client-serving transactions. However, the 5% threshold for the trading book exemption would still be applicable and that would pose a limit to its ability to reduce meaningless notifications.

Q17: Do you agree with our analysis that applying the current exemptions can address certain notification requirements for cash-settled financial instruments introduced by Article 13(1)(b)?

Q18: In your opinion, is the application of current exemptions sufficient to achieve the aim of this provision (i.e. avoiding unmeaningful notifications to the market)?

Based on the reasoning provided for Option 1, ESMA would propose the following wording for the RTS, should this be the chosen option after consultation:

"1. The exemption referred to in Article 9(6) shall apply to financial instruments held by a natural person or legal entity responding to a client's request to trade

otherwise than on a proprietary basis or hedging positions arising out of such dealings.

2. The exemption referred to in Article 12(3) shall apply to financial instruments held by a natural person or legal entity fulfilling orders received from clients, responding to a client's request to trade otherwise than on a proprietary basis or hedging positions arising out of such dealings."

Option 2

138. The second approach to the mandate is from a teleological interpretation to consider that client-serving transactions are an independent subject from existing exemptions and should be treated accordingly. This line of approach seems to correspond to the legislator's intention but may however be subject to legal challenge.

139. As mentioned, the Article 13(4) mandate should be interpreted and exercised in such a way that it does not change the scope of application of the existing exemptions and that the identified specific cases of client-serving transactions fit within the situations to which the first subparagraph of the same provision apply.

140. The above analysis of the Article 9 and 12 exemptions has shown that the trading book exemption could be used to address client-serving transactions. Nonetheless, the trading book exemption and also the market making exemption have a quantitative cap, thus potentially failing the objective of eliminating meaningless notifications to the market. Only a full exemption could completely achieve this goal, thus contributing to market efficiency.

141. CESR defended the creation of a separate exemption for the client-serving transactions instead of the extension of the existing exemptions to such transactions. However, CESR never developed the features that such an exemption would have. Also, the EC's Impact Assessment[17] referred to the creation by ESMA of a client-serving exemption to reduce the amount of unnecessary disclosures of cash-settled financial instruments. For an analysis of the specific nature of the three cases please see paragraphs 113-121.

142. Interpreting the mandate in this way would ensure that the client-serving exemption creates an actual and practical impact. Practically, this interpretation would entail taking the second subparagraph of Article 13(4) to mean Article 13(1)(b) financial instruments and letting the exemption cover cash-settled financial instruments only. Article 13(1)(a) entitlements to hold shares are covered by the trading book and market maker exemptions which are already being appropriately used with meaningful and suitable thresholds.

143. Cash-settled financial instruments represent the core mass of notifications that would be done on the basis of client-serving transactions and based on concerns expressed in the previous paragraphs, imposing the disclosure of cash-settled financial instruments would seem to be a disproportionate burden on the market. Therefore, the subject matter of such an exemption should be cash-settled Article 13(1)(b) financial instruments.

144. To avail itself of this exemption, a natural person or legal entity should be able to certify that it would not intervene in the management of the issuer. Only in such a case should an intermediary

[17] P. 93 2.1.3 of the European Commission's Impact Assessment, SEC(2011) 1279 final/2.

be exempt from disclosing its long position as it would not be using its position to exert influence on the issuer.

145. As is the case for the market making exemption, a natural person or legal entity should be able to demonstrate that it has appropriate systems and controls in order to identify its dealings and interests to avail itself of the exemption for client-serving transactions. The identification of the financial instruments corresponding to such transactions is also necessary, to ensure a clear separation from other financial instruments held for other purposes and allow the relevant competent authority to monitor whether the financial intermediary holds those financial instruments purely for client-serving purposes.

146. The objective behind this requirement is to ensure that the business organisation of the financial intermediary is such that a clear line between client-serving transactions and pure proprietary transactions in relation to the same issuer can be drawn. Thus, the client-serving entity should be capable, upon request from the relevant competent authority, of identifying the activities conducted in relation to the issuer in question and the financial instruments corresponding to the transactions.

147. A natural person or legal entity acting as a counterparty of a client in client-serving transactions will naturally have to be authorised to perform investment services under MiFID. The same entities would be subject to the client-serving exemption. Also, a natural person or legal entity which is not itself authorised under MiFID to perform investment services but is in the same group as an authorised person or entity under MiFID and is authorised by its home regulator to provide investment services should be able to avail itself of the exemption.

148. This will ensure consistent treatment of entities belonging to the same group (provided the group falls appropriately under the scope of MiFID) that may be dealing in the same capacity with the group's clients. Furthermore, it will ensure that – where positions falling within the scope of the client-serving exemption are passed from one group entity to another – the objective of avoiding excessive or meaningless disclosures continues to be achieved.

149. Furthermore, the obligation of disclosure falls upon any shareholder or holder of a share or financial instrument in an issuer, regardless of its geographical localisation. Financial intermediaries acting as investment services providers constitute, however, a special case of "holder" in the sense that they have to be able to demonstrate to the competent authority that they comply with the conditions of the exemption. Additionally, client-serving entities authorised under MiFID are subject to conditions governing the authorisation and operating requirements for financial intermediaries including conduct of business rules which assure market efficiency and provide investors with a high level of protection.

150. The conditions mentioned in the previous paragraph are harmonised at European level under MiFID. For non-European entities, the exemption would only be available where such entities are in the same group as a MiFID authorised entity and are authorised by their non EU home state regulator to perform investment services connected with client-serving transactions.

151. In order to have in place control mechanisms of the entities using the exemption, a natural person or legal entity wishing to use the exemption should have to notify the competent authority of the issuer's home Member State stating that it is either authorised under MiFID or in the same group

as such an authorised person or entity and authorised by its home regulator; that it neither intervenes nor exerts influence on the management of any issuer concerned; and that it is able to demonstrate to the competent authority of the home Member State of the issuer on request that it has appropriate systems and controls in order to identify its dealings in financial instruments and interests which fulfil orders received from clients, respond to a client's request to trade otherwise than on a proprietary basis, or hedge positions arising out of such dealings and its proprietary trading dealing and interests.

152. Regarding the interplay between this exemption and the TD's partial exemptions for market making, trading books and investment management, holders of financial instruments should first consider whether they can use the exemption for natural persons or legal entities fulfilling orders received from clients, responding to a client's requests to trade otherwise than on a proprietary basis or hedging positions arising out of such dealings. If this exemption is not applicable, they have to aggregate their positions across all financial instruments. If the aggregated holding reaches or crosses a relevant threshold, they need to establish whether they are eligible for any of the other exemptions on an aggregated basis.

Q19: Do you agree that the client-serving exemption should cover MiFID authorised entities as well as a natural or legal person who is not itself MIFID authorised but is in the same group as a MiFID authorised entity and is additionally authorised by its home non-EU state regulator to perform investment services related to client-serving transactions? Can you foresee any additional cost in case the exemption does not also cover non-EU entities within the group? If yes, please provide an estimate?

Q20: Do you think that the proposed methods of controlling client-serving activities are effective? Do you envisage other control mechanisms which could be appropriate for financial intermediaries who wish to make use of the exemption?

153. **Based on the above reasoning underlying Option 2, ESMA would propose the following wording for Article 6 and 7 of the draft RTS regarding eligibility criteria for the client-serving exemption:**

"Article 6

Scope

Cash-settled financial instruments referred to in Article 13(1)(b) of Directive 2004/109/EC held by a natural person or legal entity fulfilling orders received from clients, responding to a client's requests to trade otherwise than on a proprietary basis, or hedging positions arising out of such dealings shall not be subject to the notification requirements laid down in Article 9 of such Directive where the natural person or legal entity:

(a) is authorised to perform such investment services according to the relevant provisions of Directive 2004/39/EC or,

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(b) is in the same group as a natural person or legal entity covered by (a) and is authorised by its home state regulator to perform such investment services.

Article 7

Control mechanisms by competent authorities as regards client-serving entities

1. The client-serving entity seeking to benefit from the exemption provided for in Article 13(4) of Directive 2004/109/EC shall notify the competent authority of the home Member State of the use of the exemption, stating that it:

(a) is authorised according to (a) or (b) of Art. 6;

(b) neither intervenes in nor exerts influence on the management of any issuer concerned;

(c) is able to demonstrate to the competent authority of the home Member State of the issuer on request that it has appropriate systems and controls in order to identify its dealings in financial instruments and interests which fulfil orders received from clients, respond to a client's request to trade otherwise than on a proprietary basis, or hedge positions arising out of such dealings and its proprietary trading dealing and interests.

2. Where the client-serving entity ceases to comply with the conditions laid down in paragraph 1, it shall notify the competent authority accordingly."

IV. Definition and scope of the indicative list of financial instruments

Introduction

154. According to Article 13(1b) of the revised TD, "ESMA shall establish and periodically update an indicative list of financial instruments that are subject to notification requirements according to paragraph 1, taking into account technical developments on financial markets."

155. Paragraph 1 of Article 13 states that the notification requirements laid down in Article 9 shall also apply to a natural person or legal entity who holds, directly or indirectly:

    a. financial instruments that, on maturity, give the holder, under a formal agreement, either the unconditional right to acquire or the discretion as to this right to acquire, shares to which voting rights are attached, already issued, of an issuer whose shares are admitted to trading on a regulated market;

    b. financial instruments which are not included in point (a), but which are referenced to shares referred to in that point and with economic effect similar to that of the financial instruments referred to in that point, whether or not they confer a right to a physical settlement.

156. Paragraph (1b) of Article 13 determines that the following types of financial instruments are covered by the notification requirements, provided that these instruments satisfy any of the conditions under Article 13(1)(a) or (b): transferable securities, options, futures, swaps, forward rate agreements, contracts for differences and, as a catch-all clause, any other contract or agreement with similar economic effects which may be settled physically or in cash.

157. On this basis, ESMA believes that in order to establish a list of financial instruments subject to notification requirements and provide guidance to the market, the conditions set out in Article 13(1)(a) and (b) have to be analysed.

Types of financial instruments according to Article 13(1)

158. Article 13 of the TD sets out the prerequisites which a financial instrument has to fulfil in order to trigger a notification requirement under the TD. ESMA believes that it is necessary to distinguish between the characteristics of financial instruments covered by point (a) and point (b), respectively, i.e. to distinguish between entitlements to hold shares and financial instruments considered to be economically equivalent to shares.

a. Entitlements to hold shares

159. Financial instruments covered by Article 13(1)(a) must fulfil the following conditions:

   i) give the holder either the unconditional right to acquire or the discretion as to his right to acquire, already issued shares to which voting rights are attached, of an issuer whose shares are admitted to trading on a regulated market;

   ii) on maturity;

   iii) based on a formal agreement.

160. Regarding the first of these three conditions, ESMA considers that the holder's "unconditional right to acquire" means that the natural person or legal entity has a legal right to acquire which is not subject to conditions of any kind.

161. Furthermore, the holder's "discretion as to his right to acquire" means that the natural person or legal entity has a legal right to acquire the shares on his own initiative, not influenced by any external factors, e.g. the issuer's decision, market conditions regarding price or administrative authorisations.

162. Additionally, as the holder has a right to acquire or the discretion as to his right to acquire shares to which voting rights are attached, financial instruments under Article 13(1)(a) are either exclusively physically settled or optionally physically settled. In no case are the financial instruments exclusively cash-settled as this would take away the holder's right to acquire shares to which voting rights are already attached.

163. The last element of this first condition that must be considered is the concept of "already issued shares to which voting rights are attached". Where an issuer issues a convertible bond depending on a share capital raise, shares attributed to the holder of the bond are not yet issued. Therefore, such bonds do not qualify as a financial instrument under point (a) of Article 13(1).

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164. Regarding the second of the three conditions, ESMA considers that “maturity” refers to the term of the contract of a financial instrument. An instrument where the option to acquire can be exercised at any time should also qualify as an entitlement to hold a share. For example, American and European options differ from one another regarding the time to exercise the option, the first allowing the holder to exercise the option at any time before the option expires and the latter conferring the holder the same right only at expiration of the contract.

165. Regarding the third of the three conditions, we understand the term “formal agreement” to mean an agreement which is legally binding. As in the previous version of Article 13(1), the question of whether an agreement is legally binding is determined by the law governing the contract, i.e. the national law of the relevant Member State.

166. On this basis, mutual expectations of counterparties involved in a derivative contract on the duration of the contract or on the possibility of acquiring the counterparty’s shares at the end of the contract do not constitute a formal agreement. However, where the holder of a financial instrument has the potential of gaining an economic advantage in acquiring or gaining access to the underlying shares, he may be required to file a major shareholding notification under Article 13(1)(b) for holding a financial instrument considered to be economically equivalent to holding a share.

b. Financial instruments which are considered to be economically equivalent to shares or entitlements to hold shares

167. Financial instruments covered by Article 13(1)(b) must fulfil the following conditions:

    i) not be included in point a);

    ii) be referenced to shares;

    iii) have similar economic effect to that of entitlements to acquire shares.

168. The first of these conditions reflects the fact that Article 13(1)(b) works as a second screening when assessing whether a financial instrument is subject to the Article 9 notification requirements. To determine whether a financial instrument is subject to such requirements, one should first analyse whether the instrument fits under point (a), i.e. whether it constitutes an entitlement to acquire a share. Only if the instrument does not fulfil the conditions under point (a) is the financial instrument to be analysed as to its ability to meet the conditions under point (b).

169. Naturally, financial instruments having optionality depending on external factors should be analysed regarding their capability of fitting under point (b), because they are not covered under point (a). This is the case of pre-emption contractual rights where the discretion as to the right to sell and, consequently the ability of the counterparty to buy, normally lies with the owner of the shares and not with the holder of the pre-emption right.

170. Similarly, writing a put option gives the writer potential access to voting rights when the buyer chooses to exercise his option to sell. Nevertheless, writing a put option or benefiting of a pre-emption contractual right does not result in an entitlement to acquire, on the holder’s initiative alone, shares to which voting rights are attached.

171. In the same manner, if a financial instrument does not give the holder the right to acquire or the discretion as to his right to acquire under a formal agreement, it would not be covered by Article 13(1)(a).

172. The following case from 2003, which appears to be the first reported case on the treatment of equity derivatives from the perspective of major shareholding disclosure[18], illustrates the approach: Perry, a US investment adviser to hedge funds, sold its shares in Rubicon Ltd., a New Zealand public company, to two investment banks (Deutsche Bank and UBS Warburg) and simultaneously took a long position in equity swaps on Rubicon shares with the same banks as counterparties. As Rubicon shares were not very liquid the two banks held them as hedge. After the transactions took place the two banks filed major shareholdings notifications and Perry filed a notification reporting that it had ceased to hold Rubicon shares. Later on, Perry exercised the right of early termination of the equity swaps, buying back the shares held by the two banks as hedging.

173. The Wellington Court of Appeal in New Zealand decided that Perry had not violated the major disclosure rules of New Zealand as these aimed at disclosing voting rights rather than economic interests. The Court held that although a reasonably informed market participant would have been aware of Perry's possibility of buying the shares held by the banks as hedge, there was no formal agreement between Perry and the banks to that end.

174. Were such reasoning to be analysed in light of the revised TD, the conclusion would be that although Perry did not have the right to acquire under a formal agreement and was not bound to report an entitlement to acquire a share, it had the same economic exposure of a shareholder and benefited from a special knowledge that the shares held by the banks would most probably be available throughout the contract's duration and on termination. Such contract would have to be reported under Article 13(1)(b).

175. In conclusion, pre-emption contractual rights and put options are not subject to notification requirements under point (a) of Article 13(1). Similar financial instruments whereby no formal agreement has been concluded giving the holder the right or the discretion as to his right to acquire a share are also not subject to notification requirements under point (a). However, all three types of financial instruments can be subject to notification requirements under point (b) of Article 13(1) if they create a similar economic effect to holding shares and entitlements to acquire shares.

176. Regarding the second of the three conditions that has to be fulfilled for an instrument to fall within Article 13(1)(b), ESMA considers that a financial instrument is "referenced to shares" if its [final] terms mention an issuer's shares.

177. It is to be noted that the revised TD's major shareholding disclosure regime still remains limited to instruments referenced to shares to which voting rights are attached, already issued, of an issuer whose shares are admitted to trading on a regulated market. In fact, point (b) of Article 13(1) clearly refers to "shares referred to in that point [(a)]". In this respect, the general principles un-

[18] Ferrarini, Guido, "Equity Derivatives and Transparency: When Should Substance Prevail?", in *Festschrift für Klaus Hopt zum 70. Geburtstag am 24. August 2010, Unternehmen, Markt und Verantwortung*, Band 2, 2010, pp. 1803- 1822.

derlying the prior disclosure regime remain unchanged. On that basis, ESMA understands that under Level 1 legislation, convertible bonds providing an option to choose on maturity between cash and shares to be issued are not supposed to be disclosed at all, neither under point (a) nor under point (b). However, ESMA recognises that treating issued and unissued shares differently can constitute a possible loophole in the regulatory framework.

178. Regarding the third of the three conditions, ESMA considers that a financial instrument has "similar economic effect to that of entitlements to acquire shares", in the case for instance when such an instrument exposes the holder to the benefits of an upward movement and/or the damages of a downward movement of the price of these shares (i.e. the value of the financial instrument is positively correlated with the underlying equity instrument). Such an instrument gives the holder the potential to gain an economic advantage in acquiring, or gaining access to, the underlying shares.

179. For example, such an economic advantage may occur in a case where a financial institution (the writer of the financial instrument or seller) does not want to face the risk that the price of the share increases, having to pay for the difference on the maturity of the contract. It is highly probable that such a financial institution will hedge its position with the underlying share or with an instrument which may provide access to such shares. At the end of the contract, the financial institution will normally sell the shares, and its counterparty (the holder of the long instrument or buyer) will be in a privileged position to buy or in any other way gain access to those shares, either directly by purchasing the shares from the financial institution or indirectly by purchasing the shares that the financial institution is selling in the market.

180. Additionally, given the commercial relationship between the client and the financial intermediary, the latter will seek to preserve the business relationship with its client. As a result, the financial intermediary may have the ability to exercise a significant degree of de facto control over the voting rights attached to the shares held as a hedge[19].

Q21: When does a financial instrument have an "economic effect similar" to that of shares or entitlements to acquire shares? Do you agree with ESMA's description of possible cases?

Content of the list

181. In applying the conditions which a financial instrument has to fulfil in order to qualify as a financial instrument for the purposes of the TD, ESMA considers that the following instruments qualify under Article 13(1):

i. Irrevocable convertible and exchangeable bonds conferring a right to already issued shares

[19] CESR/09-1215b, CESR proposal to extend major shareholding notifications to instruments of similar economic effect to holding shares and entitlements to acquire shares, p. 6.

182. Convertible bonds are bonds issued by an issuer where the holder has the option to exchange the bonds for the issuer's shares at a certain time in the future according to a conversion ratio defining the number of shares obtained in exchange for one bond.

183. Exchangeable bonds follow the same structure as convertible bonds, however, differing from the latter because they give the holder the right to exchange the bond for the shares of a company other than the issuer, normally a subsidiary undertaking of the issuer.

184. ESMA considers that both convertible and exchangeable bonds conferring a right to already issued shares have to be disclosed. This type of hybrid financial instruments should be subject to notification requirements in the cases where they fulfil Article 13(1)(a) criteria regarding maturity and lack of conditionality.

ii. Financial instruments referenced to a basket of shares or indices and which comply with the criteria laid down in Article 4 paragraph 1 of the Commission Regulation

185. ESMA considers that a financial instrument referenced to a basket of shares or to an index and complying with the conditions set forth in the Commission Regulation should be subject to notification requirements.

iii. Warrants

186. Warrants are structurally options which have the specific characteristic of being issued, normally by financial institutions. They can be either put or call warrants, depending whether they give the holder the right or option of selling or buying a share from the issuer at a specific price within a certain time frame. They are similar to call options, differing from such on in that an option is neither issued nor guaranteed by the issuer or a third entity and has normally a longer maturity term.

187. Consequently, ESMA is of the opinion that such financial instruments are subject to notification requirements, if they fulfil the criteria specified either under point (a) or (b) of Article 13(1).

iv. Repurchase agreements

188. A repurchase agreement – also known as a sale and repurchase agreement or a repo in financial jargon – is a sales contract connected to an agreement for the seller to buy the security back at a later point in time. Due to the buy-back agreement, the seller has the right to acquire the securities which are the subject of the first contract.

189. A repurchase agreement should thus be considered a financial instrument falling under the provision of Article 13(1)(a) or (b), depending on the specific contractual terms agreed between the parties.

v. Rights of recall lent securities

190. Under a securities lending contract, the lender lends the borrower securities in exchange of cash, having in principle the right to reacquire, on maturity, the securities lent. The lender is then the holder of a financial instrument giving him the right to acquire a share to which voting rights are attached. In some contracts it is agreed between the parties that lent shares should be returned to the lender for the purposes of voting in the annual general assembly.

191. Rights of retransfer can qualify as financial instruments for the purposes of the TD under Article 13(1)(a).

vi. Contractual buying pre-emption rights

192. A pre-emption right awards the beneficiary a priority right to buy a security, should the seller decide to sell. ESMA considers that pre-emption rights are not covered by Article 13(1)(a), because the holder does not have "the unconditional right to acquire or the discretion as to his right to acquire". In fact, the discretion as to the right to acquire lies with the counterparty, as it is its decision to sell that will give the holder of the pre-emption right the opportunity to acquire the share.

193. Although not knowing exactly when or if he is going to acquire, the holder of the pre-emption right is in an advantageous situation compared to other market participants by having a financial instrument which is economically equivalent to holding shares.

vii. Other conditional contracts or agreements than options and futures

194. Conditional contracts or agreements are the most basic type of financial instruments, of which futures and options are only sub-types, and refer to cases in which the condition for execution of the contract/agreement is either a declaration of one of the parties or reaching a certain date.

195. Besides futures and options, there are numerous variations of contracts/agreements in which execution depends on the occurrence of one or more conditions, for example approval by an authority (e.g. antitrust approval), reaching a certain price of the underlying and conduct of a capital increase by the issuer of the underlying. Depending on whether the acquisition of shares can or cannot be prevented by the counterparty, a third person or an event, on which occurrence the holder of the financial instruments either has or does not have an influence, the financial instrument would qualify under point (a) or (b) of Article 13(1).

viii. Hybrid financial instruments

196. Hybrid financial instruments combine characteristics of equity and debt instruments, of which convertible bonds constitute the most common type. For the qualification as a financial instrument under Article 13(1), the distinction between equity, debt and hybrid instruments is of no consequence; the qualifying factor is whether the instrument enables (economically) the holder to acquire shares.

197. As this is the case for convertible bonds, such qualify in principle under Article 13(1)(a) or (b), depending on the further conditions – as pointed out, a convertible bond depending on a share capital increase by the issuer of that bond does not qualify as a financial instrument as the bond does not refer to "already issued shares to which voting rights are attached".

198. The same rationale applies to other examples of hybrid financial instruments.

ix. Shareholders' agreements

199. Any shareholders' agreement having any of the above mentioned financial instruments as its subject is itself a financial instrument.

x. Combination of financial instruments

200. ESMA considers that a financial instrument with an underlying which refers directly or indirectly to shares should be notified. An underlying refers indirectly to shares when it is referenced to another financial instrument or to a series or combination of financial instruments which in turn refer to shares.

Aim of the list and caveats

201. The aim of the list of financial instruments is to provide further clarity to the market regarding the types of financial instruments which are expected to be disclosed by an investor. Because of the continuous arrival of new financial instruments into the market, the list cannot be exhaustive. Considering the list to be exhaustive would create the risk of circumvention through the creation of new financial instruments not mentioned in the list.

202. Level 1 characterises the list as indicative because the instruments already mentioned in Article 13(1b) of the TD and the ones added by ESMA should not mechanically be disclosed; only when instruments fulfil the conditions of Article 13(1) (a) or (b) are they subject to disclosure requirements. In this sense, ESMA expects holders of instruments mentioned in the list, having obtained appropriate advice if necessary, to come to their own view as to whether they fall within the disclosure requirements of Article 13(1). In other words, the list should be seen as a guide.

203. At the same time, financial instruments not mentioned in the list do not necessarily fall outside of the scope of the notification requirements laid down in Article 13(1). Holders of such instruments should consider whether notification is required by assessing whether they fulfil the conditions in Article 13(1)(a) and (b).

204. Finally, it should be noted that in order to bring further clarity and guidance to the market, the list consists of instruments which according to a wide consensus among Member States will be subject to notification requirements, provided they satisfy the conditions set out in Article 13(1). Member States treat some financial instruments differently due to variations in national legal systems as well as different interpretations on whether an instrument has a similar economic effect. An investor trying to assess whether disclosure of a given financial instruments is required should ultimately consult the national competent authority to be sure to comply with national rules.

205. Any combination of different financial instruments mentioned in the list should be treated as an additional financial instrument subject to notifications requirements.

Update process and disclosure of the list

206. The TD acknowledges that the establishment of an exhaustive list of financial instruments of similar economic effect to holding shares and entitlements to acquire shares may rapidly become outdated, leaving new financial instruments that pose similar concerns out of the disclosure scope.

207. The revised TD entrusts ESMA with establishing and periodically updating the list, taking into account technical developments on financial markets. ESMA is of the opinion that the text of the revised TD does not require an update on a regular basis, but that it requires such update only when necessary due to market developments. Technical developments represent one of the facets of financial innovation. As part of ESMA's continuous monitoring of financial innovation, it will identify new financial instruments which have to be disclosed as they meet Article 13(1) conditions.

208. ESMA will identify further instruments that should be added to the indicative list by using financial models designed to track financial innovation and by engaging in a regular dialogue with relevant market players, including national competent authorities, about their observations on this matter.

209. The list will be published on ESMA's website. For the purpose of allowing the market to feed into the process of updating the list, ESMA is considering creating an e-mail address to which market participants can address suggestions to include additional financial instruments in the list.

Q22: Do you think that any other financial instrument should be added to the list? Please provide the reasoning behind your position.

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ANNEX I – SUMMARY OF QUESTIONS

Q1: Do you agree that the trading book and the market maker holdings should be subject to the same regulatory treatment regarding Article 9(6b) RTS?

Q2: If not, please identify reasons and provide quantitative evidence for treating trading book and market making holdings differently?

Q3: Do you agree with the ESMA proposal of aggregating voting rights held directly or indirectly under Articles 9 and 10 with the number of voting rights relating to financial instruments held under Article 13 for the purposes of calculation of the threshold referred to in Article 9(5) and (6)? If not, please state your reasons.

Q4: Can you estimate the marginal cost of changing your general major shareholding disclosure system for the purposes of notification of trading book and market making holdings, i.e., having different buckets for the purposes of the exemptions? Please distinguish between one-off costs and on-going costs.

Q5: Do you agree that, in the case of a group of companies, notification of market making and trading book holdings should be made at group level, with all holdings of that group being aggregated (Article 3(1))?

Q6: Do you agree that an exemption to notify at group level can apply if an entity meets the independence criteria set out under paragraph 72(Option 2)?

Q7: Please provide an estimate on how many times a year would your group have to report a major disclosure under the current regime in comparison to Option 1. Please include an estimate of the one-off or on-going costs involved.

Q8: Do you think that Option 2 poses any further enforceability issues than Option 1? If yes, what kind of issues can you foresee arising out of it? Can you propose an alternative approach?

Q9: Do you agree with the proposal that financial instruments referenced to a basket or index will be subject to notification requirements laid down in Article 13(1a)(a) when the relevant securities represent 1 % or more of voting rights in the underlying issuer or 20 % or more of the value of the securities in the basket/index or both of the above?

Q10: Are there any other thresholds we should consider?

Q11: Please estimate the number of disclosures you would have to make per year should the above mentioned thresholds be adopted. Please also provide an estimate of the compliance costs associated with the disclosure (please distinguish between one-off and on-going costs).

Q12: Do you agree that a financial instrument referenced to a series of baskets which are under the thresholds individually but would exceed the thresholds if added and totalled should not be disclosed on an aggregated basis?

Q13: Do you agree that our proposal for the method of determining delta will prevent circumvention of notification rules and excessive disclosure of positions? If not, please explain.

Q14: Do you agree with the proposed concept of "generally accepted standard pricing model"?

Q15: Are these three types of client serving exemptions all appropriate in terms of avoiding excessive or meaningless disclosures to the market? Please provide quantitative evidence on the additional costs borne by financial intermediaries should any of these exemptions not be adopted.

Q16: Can these three types of client-serving exemption allow for a potential risk of circumvention of major shareholdings' disclosure regime?

Q17: Do you agree with our analysis that applying the current exemptions can address certain notification requirements for cash-settled financial instruments introduced by Article 13(1)(b)?

Q18: In your opinion, is the application of current exemptions sufficient to achieve the aim of this provision (i.e. avoiding unmeaningful notifications to the market)?

Q19: Do you agree that the client-serving exemption should cover MiFID authorised entities as well as a natural or legal person who is not itself MIFID authorised but is in the same group as a MiFID authorised entity and is additionally authorised by its home non-EU state regulator to perform investment services related to client-serving transactions? Can you foresee any additional cost in case the exemption does not also cover non-EU entities within the group? If yes, please provide an estimate?

Q20: Do you think that the proposed methods of controlling client-serving activities are effective? Do you envisage other control mechanisms which could be appropriate for financial intermediaries who wish to make use of the exemption?

Q21: When does a financial instrument have an "economic effect similar" to that of shares or entitlements to acquire shares? Do you agree with ESMA's description of possible cases?

Q22: Do you think that any other financial instrument should be added to the list? Please provide the reasoning behind your position.

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ANNEX II – LEGISLATIVE MANDATE TO DEVELOP TECHNICAL STANDARDS

Regulation (EU) No 1095/2010 establishing the European Securities and Markets Authority empowers ESMA to develop draft regulatory technical standards where the European Parliament and the Council delegate power to the Commission to adopt regulatory standards by means of delegated acts under Article 290 TFEU.

Directive 2013/50/EC of the European Parliament and of the Council of 22 October 2013 inserted the following paragraphs into Directive 2004/109/EC (the Transparency Directive) conferring powers on ESMA to draft RTS on major shareholdings:

Article 9(6b)

ESMA shall develop draft regulatory technical standards to specify the method of calculation of the 5 % threshold referred to in paragraphs 5 and 6, including in the case of a group of companies, taking into account Article 12(4) and (5).

ESMA shall submit those draft regulatory technical standards to the Commission by 27 November 2014.

Article 13(1a)(a) and (b)

ESMA shall develop draft regulatory technical standards to specify:

(a) the method for calculating the number of voting rights referred to in the first subparagraph in the case of financial instruments referenced to a basket of shares or an index; and

(b) the methods for determining delta for the purposes of calculating voting rights relating to financial instruments which provide exclusively for a cash settlement as required by the first subparagraph.

ESMA shall submit those draft regulatory technical standards to the Commission by 27 November 2014.

Article 13(4), second subparagraph

ESMA shall develop draft regulatory technical standards to specify the cases in which the exemptions referred to in the first subparagraph apply to financial instruments held by a natural person or a legal entity fulfilling orders received from clients or responding to a client's requests to trade otherwise than on a proprietary basis, or hedging positions arising out of such dealings.

ESMA shall submit those draft regulatory technical standards to the Commission by 27 November 2014.

ANNEX III - COST-BENEFIT ANALYSIS

Introduction

1. The revised TD was published on 6 November 2013 and empowers ESMA with the task of preparing certain draft regulatory technical standards (RTS) regarding major shareholdings.

2. According to Article 10 (1) third subparagraph of the ESMA Regulation, the Authority shall analyse the potential related costs and benefits of the RTS, unless such analyses are disproportionate in relation to the scope and impact of the draft RTS concerned or in relation to the particular urgency of the matter.

3. ESMA is also empowered under Article 13(1b) to establish and periodically update an indicative list of financial instruments that are subject to notification requirements according to Article 13(1).

4. This task stems directly from the TD which does not mention a precise legal instrument through which ESMA should fulfil the task. Whereas the conduction of a CBA in this case is not mandatory, ESMA considers it to be a good practice to seek market stakeholders' view in this respect as well.

5. The Cost-Benefit Analysis (CBA) aims to provide the reader with an overview of findings with regard to the problem definition, options identified to remove the problem and their potential impacts.

Contents

Section I explains the background to our proposals.

Section II sets out our proposals on the trading book and market exemption, regarding the method of aggregation, including at a group level. Section III deals with the method of calculation of voting rights in case of financial instruments referenced to a basket or an index. Section IV addresses the methods for determining the delta for the purposes of calculation of voting rights relating to financial instruments which provide exclusively for a cash settlement. Section V tackles the client-serving exemption cases.

Finally, Section VI covers the list of financial instruments subject to notification requirements.

Section 1, a) – Article 9(6b) RTS on the method of calculation of the 5% threshold: Aggregation of financial instruments (horizontal aggregation)

The objective of this RTS is to ensure meaningful notification of holdings across different classes of financial instruments. In principle, there are different technical options. Either all financial instruments could for notification purposes be aggregated in one bucket. Alternatively, different types of financial instruments (holding of shares, entitlements to acquire shares and financial instruments with economic effect similar to the first two) could be separated into different buckets and require a notification when the threshold is crossed in a certain bucket.

ESMA considers the first option to be consistent with the TD revision's primary goal: to enhance transparency regarding major shareholdings. Firstly, the aggregation of all Article 9, 10 and 13 holdings keeps intact the principle that all financial instruments which are considered to be economically equivalent to shares should be treated like shares for the purposes of notification requirements. Secondly, the aggregation of all financial instruments comprising Articles 9, 10 and 13 holdings is the only approach capable of preserving the thresholds mentioned for the trading book and market maker exemptions. Disaggregation of holdings of different types would permit an increase of the 5% threshold within the trading book if a credit institution or an investment firm held a combined position in a share. Eventually, a credit institution or investment firm could end up with a combined position (shares and Article 13(1) financial instruments) of at least 10% in the trading book, whereas for the market maker this figure could reach 20%. On top of this figure, there is also the minimum 5% threshold generally applicable under Article 9(1) to holdings not covered by any exemption.

Option 1	*Aggregate shares and all financial instruments (Article 9, 10 and 13) for notification purposes. The two buckets are added and totalled. Whenever the 5% threshold is crossed, full disclosure has to be made regarding the content of the two buckets.*	
	Qualitative description	Quantitative description
Benefits	*This option provides the highest degree of clarity to the market regarding major shareholdings (see explanation above).* *Compared to the regime in place before the entry into force of the revised TD, ESMA's proposal enhances transparency as a full disclosure of the position of the credit institution or investment firm has to be done from the moment the thresholds mentioned in Article 9(6b) are reached in Article 9 and 10 shares and Article 13 financial instruments.*	
Costs to regulator	*The proposal sets one way of specifying the 5% threshold for the purposes of the trading book exemption and the 10% threshold for the purposes of the market maker exemption.* *Compared to the regime in place before the entry into force of the revised TD, this solution will result in an increase of costs for NCAs who will have to moni-*	*By way of example, the UK FCA introduced a similar notification regime which entered into force on 1 June 2009 and notifications have increased by around 10%, even with the trading book and market maker exemptions in place. Before the regime was introduced, the FCA estimated an increase in regulatory costs of around £25,000-50,000 per*

	tor more notifications due to the fact that the 5% threshold will encompass all holdings in shares whereas until now in some Member States Article 9 and 10 financial instruments were disclosed in one basket and 13(1) (a) financial instruments were disclosed separately.	*year. p. 9 of the FSA CP 07/20 on Disclosure of Contracts for Difference.* *In Germany the trading book exemption currently applies only for shares and physically settled instruments, i.e. cash settled instruments have to be considered in any case. In 2012 the number of notifications for non-physically settled financial instruments was twice the number of notifications for physically settled financial instruments. However, this represented only around one sixth of notifications regarding shares.*
Compliance costs	*Issuers will suffer small incremental costs due the need to make disclosures to the market about the notifications they have received. However, these costs will be minor because the disclosure of holdings of financial instruments with similar economic effect is relatively rare and issuers will use existing systems to make notifications to the market.* *For credit institutions and investment firms the exemption represents an increase in the costs compared to the baseline scenario of the current exemption. The 5% threshold will cover Article 9, 10 and 13 financial instruments which will result in a higher number of notifications being made. However, it is to be noted that the trading book exemption has been rendered mandatory by way of the revised TD. Notification costs will decrease in Member States who prior to the revised TD did not provide for the trading book exemption.* *For market makers the exemption also represents an increase in the costs compared to the baseline scenario of the current exemption. The 10% threshold will cover Article 9, 10 and 13 holdings. The increase in costs is balanced with a higher threshold than the existing one for the trading book. It is also to be noted that the majority of Member States have not adopted the market maker exemption (on the basis of Article 3 (1), 2nd subparagraph) and as a consequence the impact of the change is relatively small at European level*	*The FCA estimated the cost of a notification to range from £12,5 to £50 (p. 4 of Annex I of the FSA CP 07/20 on Disclosure of Contracts for Difference).*

	(Source: Mapping of the Transparency Directive – Options, Discretions and "Gold-plating", ESMA 07 July 2011/194). In Member States that have not adopted the market maker exemption, a market maker will experience a decrease in costs if the market maker exemption is adopted following the RTS.	

Section 1, b) –Article 9(6b) RTS on the method of calculation of the 5% threshold: aggregation of holdings at group level (vertical aggregation)

The main reason for the provision in Article 9(6b) of the TD is the need to harmonise the exemptions provided for in Article 9(5) and (6). Different interpretations of the NCAs regarding the scope of the exemption currently lead to divergent application and to differences in the level of information regarding major shareholdings being provided to the market.

Policy Objective	*The 5% exemption for voting rights held on the trading book or by a market maker should be applied in the same terms in all Member States. Without an RTS setting out how the 5% threshold should be calculated, it is likely that the lack of certainty as to the way the holdings should be aggregated in the case of a group within the market making and trading book exemptions will continue.*
Option 1	*Aggregation of holdings at group level and disaggregation when exemptions set out in Articles 12(4) and 12(5) apply.*
Option 2	*Aggregation of holdings at group level and disaggregation when the credit institution or investment firm exerts its voting rights regarding any non-trading book holdings independently from the parent undertaking applying the general principle of independence present both in Article 12(4) and (5).*
Preferred Option	

Option 1	*Aggregation of holdings at group level and disaggregation when exemptions set out in Articles 12(4) and 12(5) apply.*	
	Qualitative description	Quantitative description
Benefits	*To ensure an accurate picture of voting rights held within a group, holdings should be aggregated at a group level unless subsidiaries are independent in their voting decisions. Option 1 fulfils this criterion, however does not fully capture credit institutions (see Option 2).* *A subsidiary undertaking will normally*	

	exercise its voting rights according to the instructions given by its controlling parent undertaking. Therefore, ESMA is of the opinion that the principle of aggregation of all financial instruments which applies at individual level according to Article 13a should be kept intact in the case of a group. The exemption of disaggregation at group level would continue to be present when the exemptions laid down in Article 12(4) and (5) apply, i.e. whenever the group has a management firm and/or an investment firm which meet the conditions of independence set out in those provisions.	
Costs to regulator	*NCAs may incur some on-going staff costs in order to assess the conditions of independence between the parent undertaking and the subsidiary. However, these are likely to be small as NCAs will be acquainted with the assessment as the conditions to be fulfilled are similar to the exemptions of aggregation laid down in Article 12(4) and (5).*	
Compliance costs	*Implementation of option 1 is not expected to lead to an increase in the number of notifications, given that in general this aggregation rule is already followed. Therefore, the compliance costs are likely to be minimal.* *In some cases there can be small compliance cost decreases, for example for parent companies of investment firms as they do not have to include the holdings of the subsidiary investment firm when conditions of independence exist.* *If the number of notifications increases, issuers may suffer small incremental costs due to the need to make disclosures to the market about the notifications they have received.*	

Option 2	*Aggregation of holdings at group level and disaggregation when the credit institution or investment firm exerts its voting rights regarding any non-trading book holdings independently from the parent undertaking applying the general principle of independence present both in Article 12(4) and (5).*

	Qualitative description	Quantitative description
Benefits	*This proposal has a wider subjective scope than Option 1. Option 1 relies on a more literal approach wherein Article 12(4) and (5) are mentioned for the sake of clarifying that they apply even in the case of the trading book exemption. Option 2 brings credit institutions into the scope of the subsidiary undertakings which can avail themselves of the exemption from aggregating with the parent undertaking in case of the trading book and market maker exemption. As these types of holdings are in general not voted, one can argue that Option 2 makes disclosures of voting rights more accurate, as only holdings where influence on the issuer can be exercised would be disclosed.* *Option 2 is consequently less costly than option 1 due to a lower number of notifications. However, compliance costs both for Options 1 and 2 are small.*	
Costs to regulator	*There could be a potential risk that a relevant stake held by one single group in an issuer remains undisclosed, to the detriment of the market.* *NCAs may incur some on-going staff costs in order to assess the conditions of independence between the parent undertaking and the subsidiary. However, these are likely to be minor as NCAs will be acquainted with the assessment as the conditions to be fulfilled are similar to the exemptions of aggregation laid down in Article 12(4) and (5).*	
Compliance costs	*If parent companies are allowed to disaggregate trading book holdings from credit institutions and investment firms and market making holdings of market makers (assuming independence conditions are met), the number of notifications will decrease, leading to a small decrease in compliance costs arising from notifications.*	

Section 2 – Article 13(1a) (a) RTS on calculation of voting rights in the case of financial instruments referenced to a basket of shares or an index

The revised TD subjects financial instruments referenced to a basket of shares or an index to notification. Systematically requiring the disclosure of such financial instruments would be disproportionate in the cases where the basket or index is well diversified and the individual weight of the share is not significant considering the composition of the basket or index. On the contrary, if the basket includes only a limited number of securities, disclosure should be required. A right balance needs to be found in order both to avoid meaningless notifications and to require the disclosure of a financial instrument referenced to a basket or an index when the position assumed in a share through such financial instrument is relevant.

Option 1	*Basket and index instruments should only be reported if either the relevant securities represent 1% or more of voting rights in the underlying issuer or 20% or more of the value of the securities in the basket/index, or both.*	
	Qualitative description	Quantitative description
Benefits	*The requirement ensures that significant positions in underlying securities acquired through baskets / indices will be disclosed. The absence of such a requirement would mean that the purchase of financial instruments referenced to indices / baskets could be used to build significant positions in the underlying securities without disclosing them.* *As mentioned above, the thresholds need to be set at a level where disclosures are meaningful and thus should ensure that well diversified baskets and indices are normally not disclosed.* *These minimum thresholds exist alone, or in combination, in a number of Member States which already require notification of such instruments. Whereas prior existence does not in itself justify the continued use of these thresholds, it indicates that a minimum consensual threshold exists among investors which they might legitimately expect at European level. Accordingly, a continued application of these thresholds will reduce implementation costs for firms.* *The 1% threshold has been set to offer a degree of flexibility and to reflect that where relevant securities make up only a small part of the basket or index, acquiring securities by this method would not be cost efficient.*	

	The 20% threshold has been set to offer a degree of diversification suitable for investment in financial instruments referenced to a basket of shares or index rather than focus on a single share. This threshold goes as far as possible without compromising market transparency or creating a serious risk of abuse.	
Costs to regulator	*NCAs would incur staff costs in order to supervise the notifications. However, these are likely to be minimal, as the thresholds provided for in the RTS are set at a level of materiality that will lead to a very small number of notifications of voting rights regarding financial instruments referenced to a basket of shares or index.*	
Compliance costs	*Compliance costs for firms are likely to be small for two reasons. Firstly, notification costs will be very small as the number of notifications generated will be very small. Secondly, the proposed thresholds are in line with legislation already in place in the EU which reduces implementation costs.*	*Italy introduced the requirement to disclose baskets in September 2011 and Austria on 1 January 2013. To date the NCAs have not received any notification regarding baskets or indices.*

Section 3 - Article 13(1a) (b) RTS on methods for determining the delta

Article 13 (1a) of the TD requires ESMA to draft RTS to specify the methods of determination of delta for the purposes of calculation of voting rights relating to financial instruments which provide exclusively for a cash settlement.

Information about the total voting rights accessible by the investor should be as accurate as possible to achieve transparency. The lack of specification of methods for determining the delta would cause the calculation of voting rights regarding cash-settled financial instruments to be less accurate and comparable.

Policy Objective	*The calculation of voting rights for cash-settled financial instruments should be comparable and accurate.*
Option 1	Principles based approach
Option 2	Prescription of formula to determine delta
Preferred Option	*Option 1 – Principles based approach.* *Both options will achieve the policy objective. The costs to implement Option 1*

	are however significantly lower than costs to implement Option 2. Option 2 also has a feasibility issue, as firstly a very large number of derivatives with different valuation formulas would need to be covered and secondly valuation formulas for new derivatives would need to be added over time.

Option 1	*Principles based approach*	
	Qualitative description	Quantitative description
Benefits	*A principles based approach provides sufficient accuracy and comparability if supervised on a consistent basis. At the same time it is flexible, as newly developed derivative instruments would be captured by the RTS, which would also minimise the scope for regulatory arbitrage. As explained below, a principles based approach would also lead to minimal compliance costs.*	
Costs to regulator	*NCAs will incur one-off and on-going supervision costs (staff costs) as they will need to gain expertise to have the means to approve and supervise the models.*	
Compliance costs	*CRD IV entities and management firms already have sophisticated models to calculate delta in place. For this reason a system according to which such entities are able to continue using their own models - provided they are compatible with the TD - would entail no further costs.* *For natural persons there are additional costs due to the need of computing the delta. In fact, many natural persons will contract the services of financial advisors to perform such services. However, the decision of adding this cost for this type of investors was already taken at Level 1.*	

Option 2	*Prescription of a formula*	
	Qualitative description	Quantitative description
Benefits	*For instruments covered in the RTS, prescribed formulas lead to accurate and comparable approaches across Member States.* *However, Option 2 has a feasibility is-*	

	sue, as firstly a very large number of derivatives with different valuation formulas would need to be covered and secondly valuation formulas for new derivatives would need to be added over time. The latter would be difficult to achieve with a RTS. Both factors mean that the RTS may be incomplete, which could lead to legal uncertainty.	
Costs to regulator	*NCAs will incur one-off and on-going supervision costs (staff costs) as they will need to gain expertise to ensure compliance with the prescribed valuation methods. These costs will however be lower as costs for Option 1.*	
Compliance costs	*Compliance costs are likely to be significant.* *Where investors need to change their valuation methods from models currently used, one-off compliance costs are likely to be significant due to systems changes. Investors may also have to support two different systems for TD reporting and other purposes on an ongoing basis.* *Entities subject to CRD IV/CRR will also have to comply with the regulatory approach for delta calculation. This will add complexity, potentially leading to some additional compliance costs.*	

Section 4 – RTS for the client-serving exemption

Article 13a of the TD provides for a fully aggregated disclosure regime encompassing shares, entitlements to acquire shares and financial instruments considered to be economically equivalent to shares. This fully aggregated regime could cause an increase of meaningless disclosures where the provider of a client service would have to disclose positions when simply acting as an intermediary and providing liquidity. Therefore, ESMA has been tasked with drafting an RTS to specify application of existing exemptions for financial instruments held by professionals performing client-serving transactions.

Policy Objective	*The objective of the RTS is to clarify the regime applicable to client-serving transactions.*
Option 1	*Literal interpretation of the mandate – client-serving exemptions are located within existing exemptions: Situations covered by the client-serving exemption*

	will be identified within the situations to which the first subparagraph applies.
Option 2	*Practicable interpretation of the mandate – client-serving exemptions are independent of existing exemptions: For a situation to be covered by the client-serving exemptions it must be possible to ascertain that the service provider's position is assumed strictly as part of its intermediation business and in order for it to provide liquidity to the market. Therefore, the service provider should be able to ascertain that it does not intervene in the management of the issuer, that it is able to separate client-serving holdings from holdings held for proprietary business and that it ensures that the client complies with notification obligations arising from the TD.*
Preferred Option	*Option 1 – Literal interpretation of the mandate.* *Only option 1 will fully achieve the policy objective in line with the mandate.*

Option 1	*Literal interpretation of the mandate – client-serving exemptions located within existing exemptions.*	
	Qualitative description	Quantitative description
Benefits	*Applying this option prevents double notifications of positions to the extent that entities can make use of the existing exemptions provided for in Article 9(4) for custodians and in Article 12(3) exemption for the parent undertaking.* *Regarding the trading book exemption provided for in Article 9(6), applying this option ensures that holdings below the 5% threshold are not subject to meaningless notifications by an entity facilitating or hedging the client order.*	
Compliance costs	*The exemption from disclosure of Article 13 financial instruments may lead to some cost reductions where entities can make use of the trading book exemption. However, the cost reduction is smaller than for option 2.* *There may also be one-off and ongoing costs to adapt systems in order to make use of the trading book exemption for cash-settled financial instruments as well as for shares.*	

<table>
<tr><td>Option 2</td><td colspan="2">Practicable interpretation of the mandate – client-serving exemptions independent of existing exemptions

Specification of the cases in which financial instruments held by a natural person or a legal entity fulfilling orders received from clients or responding to a client's request to trade otherwise than on a proprietary basis, or hedging positions arising out of such dealings should be exempt from notification requirements laid out in Article 9 of TD.</td></tr>
<tr><td></td><td>Qualitative description</td><td>Quantitative description</td></tr>
<tr><td>Benefits</td><td>Option 2 ensures that there is no double-counting of securities holdings in the case where a client serving entity is fulfilling orders on behalf of clients. It also avoids meaningless notifications done by client-serving entities when assuming a long position in response to a client's request to trade otherwise than on a proprietary basis or hedging positions arising out of such dealings. Option 2 thus increases clarity in the market regarding the ownership of an issuer.</td><td></td></tr>
<tr><td>Costs to regulator</td><td>NCAs might incur one-off and ongoing supervision costs (staff costs) as they will need to ensure compliance with a new exemption.</td><td></td></tr>
<tr><td>Compliance costs</td><td>The exemption of disclosure of Article 13 cash-settled financial instruments reduces costs for client-serving entities, which will not have to do notifications.</td><td></td></tr>
</table>

Section 5 – List of financial instruments

In the IA[20] of the EC it was already suggested, upon advice from CESR, that ESMA could be required to draft some guidance on a non-exhaustive list of financial instruments considered to be economically equivalent to shares. The TD has broadened the scope of the task by including entitlements to acquire shares in the list.

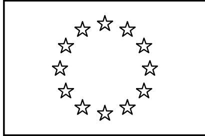
[20] Page 70, 2.1.3 of the European Commission's Impact Assessment, SEC (2011) 1279 final/2.

Article 13(1b) TD provides for a list of financial instruments which are subject to notification requirements provided they satisfy any of the conditions set out in order to be considered entitlements to acquire shares or financial instruments considered to be economically equivalent to a share.

ESMA is required to provide guidance to the market regarding the types of financial instruments that should be the subject of notification, clarifying which financial instruments should currently be disclosed and, in a prospective angle, including at a given point in time, new financial instruments in the list when financial innovation justifies it.

Option		
	Qualitative description	Quantitative description
Benefits	*The decision which specific instruments to include in the list or not does not in itself create benefits or costs. It is a technical consideration whether the specific instrument fulfils the conditions of Art. 13(1a) and 13(1b) of the TD.* *Disclosing a list of financial instruments will provide more legal certainty to the market.*	
Costs to regulator	*Establishing and updating the list will create non-material staff costs to the NCA.* *However, compared to a situation with no list of financial instruments, increased clarity resulting from the list will lead to a lower number of requests which should also be easier to handle.*	
Compliance costs	*The disclosure of a list would bring more clarity to the market, therefore decreasing costs related to financial and legal advice.*	

ANNEX IV – DRAFT REGULATORY TECHNICAL STANDARDS



EUROPEAN COMMISSION

Brussels, [...]
C(20..) yyy final

COMMISSION DELEGATED REGULATION (EU) No .../..

of [ ]

Draft

COMMISSION DELEGATED REGULATION (EU) No …/..
of […]

supplementing Directive 2004/109/EC of the European Parliament and of the Council with regard to certain regulatory technical standards on major shareholdings

(Text with EEA relevance)

THE EUROPEAN COMMISSION,

Having regard to the Treaty on the Functioning of the European Union,

Having regard to Directive 2004/109/EC of the European Parliament and of the Council of 15 December 2004 on the harmonisation of transparency requirements in relation to information about issuers whose securities are admitted to trading on a regulated market and amending Directive 2001/34/EC [1], and in particular Article 9(6b), 13(1a)(a), 13(1a)(b) and 13(4) thereof,

Whereas:

(1) Directive 2004/109/EC harmonises transparency requirements relating to information about issuers whose securities are admitted to trading on a regulated market and also requires development of regulatory technical standards to ensure consistent harmonisation in the regime for notification of major holdings, adequate transparency levels and exemptions to the notification requirements for major holdings of voting rights.

(2) The thresholds for the market making and trading book exemptions should be calculated by aggregating all financial instruments referred to in Articles 9, 10 and 13 of Directive 2004/109/EC in order to ensure consistent application of the principle of aggregation of all financial instruments subject to notification requirements as well as prevent a misleading picture of how many financial instruments related to an issuer are held by an entity benefiting of such exemption.

(3) In the case of a group of companies, the threshold should be calculated at group level and therefore all holdings owned by the parent undertaking of a credit institution or investment firm and subsidiary companies should be disclosed when the total sum of the holdings reaches the notification threshold.

(4) The application of the market maker exemption is subject to requirements on non-intervention in the management of the issuer and the non-exercise of any influence on the issuer. However, a parent undertaking of a credit institution or investment firm may have other holdings with voting rights in the same share or financial instrument. If a subsidiary manages such holdings in an independent manner from the parent undertaking, it is reasonable to exempt its parent undertaking from aggregating its voting rights with those of the subsidiary held for the purpose of market making activities with voting rights in the same share or financial instrument which are unrelated to the market making activity.

(5) The trading book exemption bears a similar requirement of non-intervention in the management of the issuer as well as non-exercise of voting rights attached to shares held in a trading book. It would be consistent that in case of a group of companies, the parent undertaking of a credit institution or investment firm should benefit from an identical

[1] OJ L 390. 31.12.2004, p. 38.

exemption to aggregate the voting rights held in the trading book of a credit institution or investment firm.

(6) For reasons of clarity and consistency, similar requirements to the ones laid down in Article 10 of Commission Directive 2007/14/EC further detailing Article 12(4) and (5) of Directive 2004/109/EC should be taken into consideration when setting out conditions of independence to be complied with by credit institutions, investment firms and market makers regarding trading book and market making exempted holdings, respectively.

(7) The disclosure regime for financial instruments having a similar economic effect to shares should be clear. Exhaustive knowledge of the structure of corporate ownership should be proportionate with the need for adequate transparency in major holdings, the administrative burdens such requirements place on holders of voting rights and the flexibility in the composition of a basket of shares or an index. Financial instruments referenced to a basket of shares or an index should only be calculated for the purposes of notifying voting rights when the holding of a share through such instrument is significant. It would not be cost-efficient for an investor to build a position in an issuer through holding several financial instruments referenced to different baskets. Therefore, where financial instruments referenced to a series of baskets are below the thresholds individually but over them when aggregated, voting rights should not be calculated.

(8) Financial instruments not having a linear, symmetric pay-off profile in line with the underlying share (that is, instruments not having a 'delta 1' profile) should be calculated using delta. To render the notification of voting rights of exclusively cash-settled financial instruments more accurate and comparable, the methods for determining delta should respect certain rules regarding methodology, parameters, governance and IT systems.

(9) In order to render the information about the total voting rights accessible by the investor as accurate as possible, delta should be calculated daily taking into account the last closing price of the underlying share.

(10) The regime applicable to client-serving transactions should be detailed so as to create clarity regarding which exemptions apply to such transactions.

(11) This Regulation is based on the draft regulatory technical standards submitted by the European Securities and Markets Authority (ESMA) to the Commission.

(12) ESMA has conducted open public consultations on the draft regulatory technical standards on which this Regulation is based, analysed the potential related costs and benefits and requested the opinion of the Securities and Markets Stakeholder Group established by Article 37 of Regulation (EU) No 1095/2010.

(13) The application of this Regulation shall be deferred in order to align its date of application with the date prescribed for the transposition of Directive 2013/50/EU of the European Parliament and of the Council of 22 October 2013 in Article 4(1) of said Directive[2].

[2] OJ L 294, 6.11.2013, p. 13.

HAS ADOPTED THIS REGULATION:

Chapter I

GENERAL PROVISIONS

Article 1

Subject matter and scope

This delegated Regulation lays down detailed rules for the implementation of Article 9(6b), 13(1a) and Article 13(4) of Directive 2004/109/EC.

Chapter II

METHOD OF CALCULATION OF THE 5 % THRESHOLD

(Article 9(6b) of Directive 2004/109/EC)

Article 2

Aggregation of holdings

For the purposes of calculation of the 5 % threshold provided for in Article 9(5) and (6), holdings under Article 9, 10 and 13 shall be aggregated.

Article 3

Aggregation of holdings in the case of a group

1. For the purposes of calculation of the 5 % threshold provided for in Article 9(5) and (6), holdings shall be aggregated at group level.

2. By derogation from paragraph 1, the parent undertaking of a credit institution or investment firm shall not be required to aggregate its holdings in the trading book with those held in the trading book of a credit institution or investment firm or in the capacity of a market maker provided such credit institution or investment firm exercises independently its voting rights in respect of shares not held in the trading book and for the purpose of market making activities independently from the parent undertaking.

3. For the purposes of paragraph 2, a parent undertaking of a credit institution or investment firm must not interfere by giving direct or indirect instructions or in any other way in the exercise of the voting rights held by that credit institution or investment firm.

4. A parent undertaking of a credit institution or investment firm who wishes to make use of the exemption shall, without delay, notify the following to the competent authority of the home Member State of issuers whose voting rights are attached to holdings of the investment firm, credit institution or market maker:

(a) a list of the names of such credit institution(s) or investment firm(s), indicating the competent authorities that supervise them or that no competent authority supervises them, but with no reference to the issuers concerned;

(b) a statement that for each such credit institution or investment firm, the entity in the group complies with the condition laid down in paragraph 3.

The parent undertaking shall update the list referred to in point (a) on an ongoing basis.

5. Where the parent undertaking intends to benefit from the exemptions only in relation to the financial instruments referred to in Article 13 of Directive 2004/109/EC, it shall notify to the competent authority of the home Member State of the issuer only the list referred to in point (a) of paragraph 4.

6. Without prejudice to the application of Article 24 of Directive 2004/109/EC, a parent undertaking of a credit institution or investment firm shall be able to demonstrate to the competent authority of the home Member State of the issuer on request that:

(a) the organisational structures of the parent undertaking and the credit institution or investment firm are such that the voting rights are exercised independently of the parent undertaking;

(b) the persons who decide how the voting rights are to be exercised act independently.

The requirement in point (a) shall imply as a minimum that the parent undertaking and the credit institution or investment firm must have established written policies and procedures reasonably designed to prevent the distribution of information between the parent undertaking and the credit institution or investment firm in relation to the exercise of voting rights.

7. For the purposes of paragraph 3, ‘direct instruction’ means any instruction given by the parent undertaking, or another controlled undertaking of the parent undertaking, specifying how the voting rights are to be exercised by the investment firm or credit institution in particular cases.

‘Indirect instruction’ means any general or particular instruction, regardless of the form, given by the parent undertaking, or another controlled undertaking of the parent undertaking, that limits the discretion of the investment firm or credit institution in relation to the exercise of the voting rights in order to serve specific business interests of the parent undertaking or another controlled undertaking of the parent undertaking.

Chapter III

CALCULATION OF VOTING RIGHTS IN THE CASE OF FINANCIAL INSTRUMENTS REFERENCED TO A BASKET OF SHARES OR AN INDEX

(Article 13(1a)(a) of Directive 2004/109/EC)

Article 4

1. Voting rights in the case of a financial instrument subject to notification requirements laid down in Article 13(1) and which is referenced to a basket of shares or an index shall be calculated on the basis of the weight of the share in the basket or index and if at least one of the following conditions apply:

(a) the shares in the basket or index represent 1 % or more of voting rights attached to shares of the specific issuer; or

(b) the shares in the basket or index represent 20 % or more of the value of the securities in the basket or index.

2. By derogation from paragraph 1, financial instruments referencing a series of baskets which are individually under the thresholds mentioned in paragraph 1 but would exceed the thresholds if added and totalled are not subject to notification requirements.

Chapter IV

DETERMINATION OF DELTA FOR THE PURPOSES OF CALCULATION OF VOTING RIGHTS RELATING TO FINANCIAL INSTRUMENTS WHICH PROVIDE EXCLUSIVELY FOR A CASH SETTLEMENT

(Article 13(1a)(b) of Directive 2004/109/EC)

Article 5

1. The number of voting rights relating to an exclusively cash settled financial instrument with a linear, symmetric pay-off profile with the underlying share shall be calculated on a delta-adjusted basis with cash position being equal to 1.

2. The number of voting rights relating to an exclusively cash settled financial instrument without a linear, symmetric pay-off profile with the underlying share shall be calculated on a delta-adjusted basis, using generally accepted standard pricing models.

3. A generally accepted standard pricing model is one that is widely used in the finance industry and sufficiently robust to consider the elements that are relevant to the valuation of the financial instrument. Those elements that affect the valuation include at least the following:

(a) interest rate;

(b) dividend payments;

(c) time to maturity;

(d) volatility;

(e) price of underlying share.

4. When determining delta the holder of the financial instrument shall ensure that:

(a) the model used covers the complexity and risk of each financial instrument;

(b) the same model is used in a consistent manner for the calculation of the number of voting rights of a given financial instrument.

5. IT systems used to run the calculation of delta shall ensure consistent, accurate and timely reporting of voting rights.

6. The number of voting rights shall be calculated daily, taking into account the last closing price of the underlying share. The holder shall notify the issuer when he reaches, exceeds or falls below the thresholds provided for in Article 9(1).

Chapter V

CLIENT-SERVING TRANSACTIONS

(Article 13(4) of Directive 2004/109/EC)

[...]

Chapter VI

TRANSITIONAL AND FINAL PROVISIONS

Article 7

Entry into force and application

This Regulation shall enter into force on the day following that of its publication in the *Official Journal of the European Union*.

It shall apply from [].

This Regulation shall be binding in its entirety and directly applicable in all Member States.

Done at Brussels, [].

[For the Commission
The President]

[For the Commission
On behalf of the President]
[Position]

ANNEX V – INDICATIVE LIST OF FINANCIAL INSTRUMENTS

INDICATIVE LIST OF FINANCIAL INSTRUMENTS THAT ARE SUBJECT TO NOTIFICATION REQUIREMENTS ACCORDING TO ARTICLE 13 (1b) OF THE REVISED TRANSPARENCY DIRECTIVE

1. Article 13(1b) TD already considers the following to be financial instruments, provided they satisfy any of the conditions set out in points (a) or (b) of the first subparagraph of Article 13(1) TD:

(a) transferable securities;

(b) options;

(c) futures;

(d) swaps;

(e) forward rate agreements;

(f) contracts for differences; and

(g) any other contracts or agreements with similar economic effects which may be settled physically or in cash.

2. ESMA further clarifies that "options" should be read as including calls, puts or any combination thereof.

3. Furthermore, taking into account current technical developments on financial markets ESMA considers the following to be financial instruments, provided they satisfy any of the conditions set out in points (a) or (b) of the first subparagraph of Article 13(1) TD:

(a) irrevocable convertible and exchangeable bonds referring to already issued shares;

(b) financial instruments referenced to a basket of shares or an index and which comply with the criteria laid down in Article 4 paragraph 1 of the Commission Directive;

(c) warrants;

(d) repurchase agreements;

(e) rights to recall lent securities

(f) contractual buying pre-emption rights;

(g) other conditional contracts or agreements than options and futures;

(h) hybrid financial instruments;

(i) combinations of financial instruments;

(j) shareholders' agreements having any of the above mentioned financial instruments as an underlying.

4. ESMA acknowledges that, depending on the characteristics and typology of such financial instruments, there are overlaps within the categories referred above. In such cases notification is required, under one of the categories.

ESMA

European Securities and Markets Authority

Paris

XX.YY. 2014