



European Securities and
Markets Authority

Final Report

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

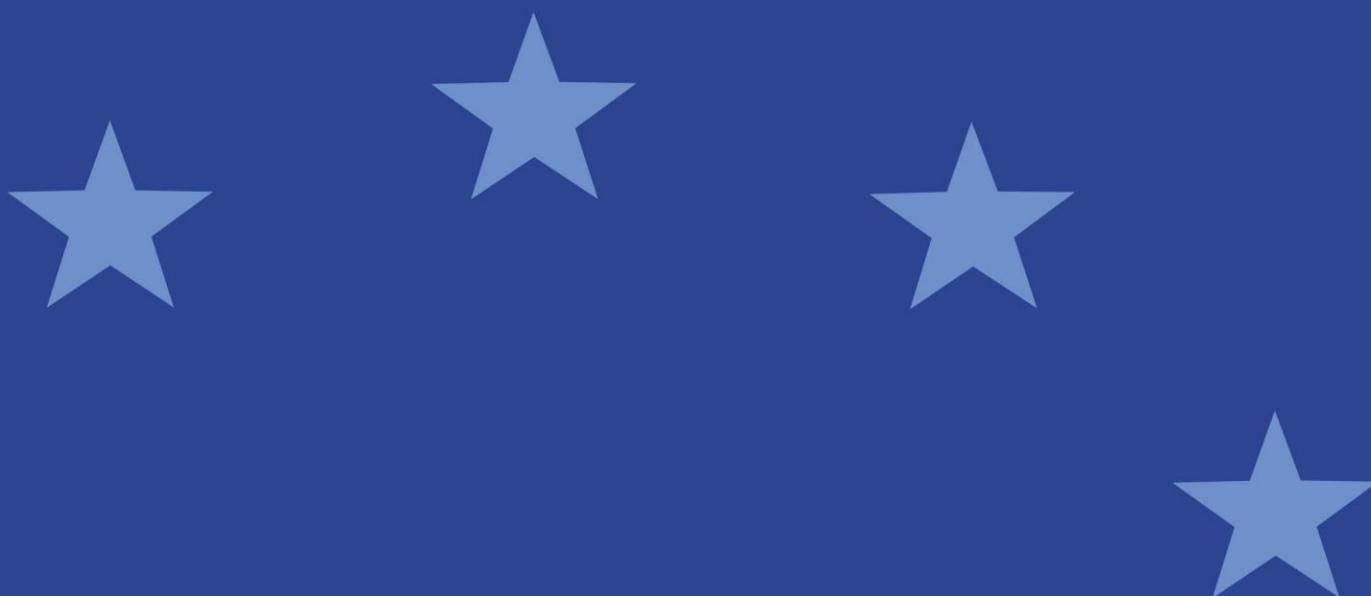


Table of Contents

I. Executive Summary	5
II. Background.....	6
II.I Mandates and consultation process.....	6
II.II Elements of the Final Report	6
III. Summary of the feedback and amendments to the draft RTS	8
III.I Draft RTS on the calculation method of the 5 % threshold referred to in the Article 9(5) and (6) exemptions of the TD.....	8
III.I.a Horizontal aggregation – Aggregation of different categories of holdings (Article 9, 10 and 13 of the revised TD).....	9
III.I.b Vertical aggregation – Aggregation of holdings of financial instruments within a group of companies in relation to the trading book and market making exemptions.....	11
III.II Draft RTS 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	15
III.III Draft RTS on the methods of determining delta for the purposes of calculating voting rights relating to financial instruments which provide exclusively for a cash settlement	19
III.IV Draft RTS on client-serving transactions	23
IV. Definition and scope of the indicative list of financial instruments.....	30
ANNEX I – SUMMARY OF QUESTIONS	35
ANNEX II – LEGISLATIVE MANDATE TO DEVELOP DRAFT RTS	37
ANNEX III – COST-BENEFIT ANALYSIS	38
ANNEX IV – SMSG OPINION	54
ANNEX V – DRAFT REGULATORY TECHNICAL STANDARDS	62
ANNEX VI – INDICATIVE LIST OF FINANCIAL INSTRUMENTS	67



Acronyms and definitions used

Capital Requirements Regulation	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
CESR	Committee of European Securities Regulators
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	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 (ESMA/2014/300)
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
CWG	Consultative Working Group of the Corporate Finance Standing Committee
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
EEA	European Economic Area
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
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
SSR	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
Takeover Bids Directive	Directive 2004/25/EC of the European Parliament and of the Council of 21 April 2004 on takeover bids
TD	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	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)

I. Executive Summary

Reasons for publication

Directive 2004/109/EC of the European Parliament and of the Council of 15 December 2004 amended by Directive 2013/50/EU of the European Parliament and of the Council of 22 October 2013 (hereinafter the “Transparency Directive” or “TD”) requires ESMA to develop draft regulatory technical standards (“RTS”) on major shareholdings.

The TD furthermore mandates ESMA to establish an indicative list of financial instruments that are subject to notification requirements according to Article 13(1) of the TD.

While developing the draft RTS and establishing the above mentioned indicative list of financial instruments, ESMA consulted stakeholders by way of a Consultation Paper (a “CP”) (ESMA/2014/300).

Contents

This Final Report contains a summary of the feedback from the public consultation as well as the changes to the draft RTS and the indicative list which ESMA proposes based on this feedback. To a large extent the structure of the Final Report follows the structure of the Consultation Paper with the first part dealing with each of the four mandates given to ESMA to develop draft RTS and the second part dealing with the indicative list of financial instruments.

The annexes of the Final Report consist of the questions asked in the Consultation Paper (Annex I), the legislative mandates for ESMA to develop draft RTS (Annex II), a revised cost-benefit analysis (Annex III), the advice submitted by the Securities and Markets Stakeholder Group (the “SMSG”) (Annex IV), the revised draft RTS (Annex V) and the indicative list of financial instruments (Annex VI).

Next steps

This Final Report will be submitted to the European Commission (the “Commission”) by 27 November 2014. The Commission has three months to decide whether to endorse ESMA’s draft RTS.

II. Background

II.I Mandates and consultation process

1. The revised Transparency Directive was published in the Official Journal of the European Union on 6 November 2013 and entered into force on 26 November 2013. The Directive undertakes a revision of the regime for notification of major holdings of voting rights, introducing the rule of aggregation of holdings of shares with holdings of financial instruments and harmonising the calculation of notification thresholds and exemptions from the notification requirements.
2. The revised TD thus makes market making, trading book and stabilisation exemptions mandatory for EU Member States. The Directive itself contains certain provisions on the requirements of such exemptions and these provisions are to be complemented by the RTS which ESMA is empowered to draft in the area.
3. Moreover, with the aim to further enhance the transparency of major holdings of voting rights, the revised TD establishes an obligation to disclose holdings of financial instruments considered to be economically equivalent to shares in TD Article 13(1)(b). ESMA is empowered to develop draft RTS to ensure consistent harmonisation in respect of the calculation of notification thresholds applicable to financial instruments referenced to a basket of shares or an index and in the case of cash-settled financial instruments, through the introduction of delta.
4. Regulation (EU) No 1095/2010 establishing the European Securities and Markets Authority (the “ESMA Regulation”) empowers ESMA to develop draft RTS 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.
5. For the purpose of discharging the above mentioned mandates, ESMA published its CP on 21 March 2014 with the purpose of obtaining stakeholders’ views on the proposed draft RTS and list of financial instruments. In addition to the draft RTS and list of financial instruments, the CP included an initial cost-benefit analysis. The consultation closed on 30 May 2014 and ESMA received responses from 24 market participants representing mainly credit institutions, investment firms and asset managers, but also institutional investors, issuers and a stock exchange.
6. In addition, ESMA sought the views of the SMSG, the Consultative Working Group of the Corporate Finance Standing Committee and the national competent authorities (“NCAs”) of Member States to draw on their experiences in this field. These views have been taken into account in the compilation of this Final Report. The Advice submitted by the SMSG is fully reproduced in Annex IV.

II.II Elements of the Final Report

7. The Final Report is structured in the same five main sections as the CP:
 - section III.I covers the draft RTS on a method for calculation of the 5 % threshold referred to in the Article 9(5) and (6) exemptions of the TD;
 - section III.II addresses the draft RTS on a method for calculating the number of voting rights referred to in TD Article 13(1a)(a) in the case of financial instruments referenced to a basket of shares or an index;

- section III.III deals with the draft RTS on a method for determining delta for the purpose of calculating voting rights referred to in TD Article 13(1a)(b) in the case of financial instruments which provide exclusively for a cash settlement;
 - section III.IV addresses the draft RTS on client-serving transactions as referred to in TD Article 13(4); and
 - section IV covers the indicative list of financial instruments subject to notification requirements according to TD Article 13(1).
8. Within each section, ESMA provides a summary of the answers received to the corresponding questions raised in the CP. These summaries are a presentation of the results of the consultation and should be distinguished from ESMA's responses to the views of respondents which are placed at the end of each question or set of questions under the heading "ESMA's response". ESMA's response sets out ESMA's understanding of the answers provided by market participants and explains the rationale for ESMA's decision to either keep or change the RTS/indicative list of financial instruments.
 9. Where the wording of questions allowed, consultation responses were categorised as either "yes" or "no" to facilitate a clear understanding of the trend in the responses to a given question. This categorisation was supplemented with the explanatory comments which the majority of respondents provided to qualify or nuance their answers.
 10. Some interpretation of the responses received was necessary. A number of respondents did not reply to the specific questions raised in the CP but instead provided general statements on the issues covered in the CP. ESMA has interpreted such responses to the best of its abilities in order to allocate the views expressed to the relevant questions.
 11. In some cases, a response was more relevant for another question than the one it was provided under, or the response was also relevant for other questions. In such cases, responses have been taken into account in the analysis of such other questions. Some respondents raised similar or identical issues in their replies to several questions. Where possible, such replies have been grouped under one question in order to facilitate understanding.
 12. When ESMA made its decision regarding how the final draft RTS and indicative list of financial instruments should look, the analysis of the costs and benefits that the proposed measures might entail was an essential element. Annex III of this Final Report contains ESMA's final cost-benefit analysis; the analysis is an amended version of the one included in the CP based on information received in the consultation. Respondents to the CP provided information of a mostly qualitative nature and ESMA's further requests for quantitative information only unearthed limited data. On that basis, ESMA has not been able to perform an in-depth quantitative analysis of the costs and benefits connected with its proposed measures. Notwithstanding this, the cost-benefit analysis does contain quantitative elements where possible and otherwise focuses on qualitative descriptions.

III. Summary of the feedback and amendments to the draft RTS

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

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?

Question 1

13. Nine market participants responded to this question, all agreeing that trading book and market making holdings should be subject to the same treatment for the purposes of TD Article 9(6b).
14. Three respondents made the point that the exemptions for the trading book and the market making holdings have to be treated separately, i.e., a credit institution or investment firm is allowed to use the trading book exemption up to 5 % and the market making exemption up to 10 % and such exemptions act independently of each other.
15. One respondent was not sure whether the “same regulatory treatment” mentioned in Q1 meant that the same organisational requirements would apply for market making and trading book activities. If the “same regulatory treatment” was to consist of the conditions set out in Article 6 of Commission Directive 2007/14/EC (the “Commission Directive”), this respondent would not support an obligation to notify the home Member State about trading book activities on particular issuers.

Question 2

16. No respondents identified a reason to treat trading book and market making holdings differently and consequently, no quantitative evidence was provided on the subject.

ESMA’s response

17. ESMA’s proposal regarding Article 9(6b) of the TD is that the market making and trading book exemptions should be subject to the same principles as concerns the method of calculation of thresholds in respect of the aggregation of shares with financial instruments (horizontal aggregation) and the aggregation of holdings at group or company level (vertical aggregation).
18. In ESMA’s view, market making and trading book activities have similar organisational requirements which allow credit institutions and investment firms to identify holdings in each category. Additionally, it is a common prerequisite to both exemptions that no type of intervention in the management of the issuer occurs.
19. It follows from the answers to Q1 that none of the respondents identified a reason to apply different rules to trading book and market making activities in respect of either horizontal or vertical aggregation. On that basis, ESMA will maintain the equal treatment of both types of exemption in the draft RTS. No additional requirements are proposed in respect of the trading book exemption as that would be beyond the scope of ESMA’s mandate regarding this RTS.
20. As regards the concern of one respondent described in paragraph 15, ESMA notes that Article 6 of the Commission Directive only applies to the market making exemption and the requirements of this article are not to be extrapolated to the trading book exemption. The provision merely illustrates that the industry is already identifying shares or financial instruments held in the trading

book similarly to the requirement already in place for the market making exemption which provides a good argument to treat both exemptions in an analogous manner in what regards the content of the Article 9(6b) draft RTS.

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

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.

Question 3

21. 13 respondents answered Q3 of which 11 were in favour of the proposal and two against.
22. The arguments invoked by respondents in support of ESMA's proposal included 1) consistency with the general disclosure rule under TD Article 13a, 2) consistency with the TD's aim of increasing transparency regarding an investor's potential influence in an issuer, and 3) rapprochement towards the market reality.
23. One respondent in favour of the proposal added, however, that for the purposes of the breakdown to be included in the notification, two categories should be applied – i) voting rights under TD Articles 9 and 10, and ii) financial instruments under TD Article 13(1) – because it can be difficult in practice to distinguish between holdings under TD Article 9 and holdings under TD Article 10. Another respondent suggested that instead of referring to the “calculation of the 5 % threshold” in the proposed Articles 2 and 3 of the draft RTS, it would be more accurate to refer to the “method of calculation of voting rights to ascertain whether the 5 % threshold is met”, given that the calculation referred to relates to assessing whether the number of voting rights exceeds the 5 % threshold rather than calculating the 5 % threshold.
24. One respondent who was against the proposal argued that horizontal aggregation of TD Article 9, 10 and 13(1) holdings leads to 1) a multiplication of meaningless notifications and a consequent decrease of transparency in the market, and 2) unnecessary burdens for market participants. The other respondent against the proposal advocated that the threshold of the trading book and market making exemptions should be kept separate instead of being horizontally aggregated.

Question 4

25. ESMA received ten responses to Q4 and although respondents did not provide quantitative input, it was possible to leverage off the qualitative assessments made. Overall, respondents were of the opinion that changing the current major notification system to accommodate Option 1 (two different buckets for shares and financial instruments) would not be very burdensome. One of the reasons stated was that existing regulatory requirements in certain Member States oblige the separate reporting of holdings in shares and financial instruments. Therefore, firms are already required to have systems in place which are capable of monitoring shares and financial instruments separately. The second reason highlighted was that while changes in such systems can be complex and entail significant one-off costs, on-going costs may be lowered as harmonisation is increased.

26. Respondents also touched upon other topics in their answers to Q4. It was pointed out that credit institutions are already subject to Directive 2013/36/EU (the “Capital Requirements Directive” or “CRD IV”) and are thus required to report their delta positions in the derivatives book and their share positions. Given the observed initial synergies and subject to further analysis of all the details of the draft RTS and its impact, these respondents believed that any financial institution possesses the ability to implement the proposed disclosure system with a marginal cost both from the one-off and the on-going costs perspective.
27. It was also observed that the on-going costs of calculating the market making exemption would be higher than the one-off costs because of the additional administrative exercise required to identify the market making financial instruments and notify the relevant NCA. As regards the impact of the trading book exemption, it was the view that there would be a negligible one-off cost and on-going cost savings. Finally, one respondent expressed concern that regarding costs as well as complexity, the market making exemption does not match the exemption in Regulation (EU) No 236/2012 (the “Short Selling Regulation” or “SSR”). In this respondent’s opinion, there should be a limit or a criterion for the calculation based on what is reasonable in light of the scope of the regulation. Furthermore, to avoid unnecessary costs and administrative burdens the calculation requirements within the TD regime should be harmonised with those in the SSR.

ESMA’s response

28. ESMA observes that a wide consensus exists between different types of market participants regarding the proposal on horizontal aggregation.
29. As regards the suggestion of one respondent that for the purpose of the breakdown to be included in the notification, two categories should be applied, ESMA notes that Article 13a, paragraph 2 of the TD already requires that the notification “shall include a breakdown of the number of voting rights attached to the shares held in accordance with Articles 9 and 10 and voting rights relating to financial instruments within the meaning of Article 13”.
30. ESMA is of the view that the proposed alternative wording (see paragraph 23) would be adequate if voting rights only had to be calculated for the purpose of ascertaining whether the 5 % threshold had been exceeded. However, since the calculation has to be performed also for the purpose of assessing whether voting rights reach or fall below that threshold, the proposed wording does not seem suitable. Furthermore, ESMA considers it important to apply the same terminology in the draft RTS as in the TD in order to aid comprehension and interpretation of the RTS and to avoid ambiguities, contradictions or doubts as to the meaning of a term.
31. Regarding the two respondents who opposed horizontal aggregation, ESMA observes that they seem to have differing reasons for their opposition. One argues that aggregation of Article 9, 10 and 13(1) holdings would overturn TD’s overarching principle of enhanced transparency in the field of major shareholdings as the market would be flooded by meaningless notifications. ESMA considers that the decision to aggregate all holdings was made at Level 1 as the new Article 13a of the TD imposes aggregation of financial instruments economically equivalent to shares, including cash-settled derivatives, with holdings of shares and entitlements to acquire shares which were already subject to disclosure under TD Article 13. Moreover, some market participants have highlighted that it can be considered more burdensome to have two different systems running in parallel, one for the purpose of notification of un-exempted holdings under TD Article 13a and another for the purpose of the calculation of voting rights for exempted holdings, such as the ones under Articles 9(5) and (6) of the TD.

32. The second argument invoked against horizontal aggregation is caused by uncertainty on the part of some respondents regarding the scope of horizontal aggregation. Specifically, some respondents were unsure whether ESMA is proposing a single and common threshold for the market making and trading book exemptions, thus overriding the TD. ESMA clarifies that its proposal is limited to the aggregation of holdings of Articles 9, 10 and 13(1) within each exemption – the market making and the trading book – without thus affecting the general rules established in the TD under which credit institutions and investment firms may benefit of both exemptions. In other words, the proposal does not change the general rules established by the TD.
33. Regarding the comment that two different concepts of market making seem to exist in the TD and the SSR, ESMA acknowledges the presence of differences and the difficulties arising out of such for market participants. However, such dissimilarities must be addressed at Level 1 and cannot be dealt with by means of an RTS. In conclusion, ESMA maintains the proposed wording of the draft RTS.

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

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))?

34. 15 respondents answered this question of which two thirds were favourable to the principle of aggregation at group level.
35. One respondent argued that in one Member State, banks and securities firms would have had to make around 50 disclosures so far this year if aggregation of holdings at group level had been in place (compared to no disclosures with the existing regulations).
36. Additionally, respondents raised two topics, namely 1) ESMA should clarify that the market making and trading book exemptions are not of mandatory use to investors, and 2) the RTS on vertical aggregation should be explicit as to whether the group has to be a European Economic Area (EEA) firm and whether the subsidiaries are limited to the EEA only. It was observed that the trading book exemption should cover all controlled undertakings, including subsidiaries, regardless of whether they are EEA companies. For market making, a non-EEA firm could be supporting the EEA controlled undertakings so the market making should be regarded as applying at group level.
37. Lastly, the SMSG drew attention to two technical issues. Firstly, regarding the fact that according to ESMA's proposal, holdings shall be aggregated at "group level", the SMSG pointed out that, since Directive 2013/34/EU defines a group as "a parent undertaking and all its subsidiary undertakings", Article 3(1) of the draft RTS could be interpreted as meaning that holdings are not only attributed to the parent undertakings but also to subsidiaries in a multilevel group. To avoid such misunderstandings, the SMSG encouraged ESMA to clarify that holdings are solely attributed to the parent undertaking.
38. Secondly, the SMSG questioned how cases in which a parent undertaking is not a credit institution and therefore does not profit from the exemptions provided for market makers and trading books should be handled. By way of example, the SMSG observed that if subsidiary A and subsidiary B in a multilevel group each held a stake of 3 % in their trading books, A and B would be ex-

empt from disclosure requirements according to TD Article 9(6), but the question remains whether A and B's holdings could be attributed to a parent undertaking which is not a credit institution or an investment firm and therefore does not have a trading book.

39. In the view of the SMSG, TD Article 9(6) does not apply to such a parent undertaking and therefore, neither does Article 3 of the draft RTS. The legal basis for the aggregation of A and B's holdings to the parent undertaking can only be Article 10(e) TD, and Article 3 of the draft RTS should not provide a derogation from this article. On that basis, the SMSG observed that the holdings of each subsidiary would have to be aggregated to the parent undertaking, provided that the prerequisites laid down in Article 10(e) TD are fulfilled.

ESMA's response

40. ESMA acknowledges the wide consensus around the suggested draft RTS and clarifies that the market making and trading book exemptions constitute an exception to the rule requiring the notification of major shareholdings. While it is mandatory for Member States to provide for such exemptions, investors are not obliged to make use of the exemptions and whether they do so or not will often depend on the structure and business model of the individual investor.
41. As for the comment concerning whether the group has to be composed of EEA entities, ESMA notes that the market maker and trading book exemptions are defined according to the framework set up in Articles 9(5) and (6) of the TD, respectively. According to these articles, the concept of market maker is linked to the entity in question having obtained an authorisation under Directive 2004/39/EC ("MiFID") whereas the trading book concept is such as defined in Article 11 of Directive 2006/49/EC concerning general prudential requirements applicable to institutions supervised under Directive 2013/36/EU. As such, the conditions for an entity to benefit from the market maker or trading book exemption are set forth in TD Article 9(5) and (6) and are not dealt with in the draft RTS.
42. Regarding the first concern raised by the SMSG, ESMA acknowledges that it should be clarified who is responsible for performing the notification within the group. Article 10(e) of the TD applies to situations where the controlling natural person or legal entity is required to make a notification in respect of its holdings and those of controlled undertakings, regardless of whether or not it holds voting rights itself.
43. On this basis, ESMA clarifies that voting rights can only be attributed in an upward direction, i.e., from subsidiary undertakings to parent company and never the other way around. In other words, if Company A is the ultimate parent company in a chain and controls Company B, which, in turn, controls Company C, Company A must make a notification if a threshold is triggered by the aggregated holdings of A, B and C. At the same time, Company B must apply the same aggregation rule with respect to the aggregated holdings held by itself and its subsidiary, Company C.
44. In situations where a controlled undertaking has made use of the TD Article 12(3) exemption, the notification can be performed by the parent undertaking on behalf of the controlled undertaking, provided that the controlled undertaking holds 5 % or more.
45. Regarding the second point raised by the SMSG, i.e., that the draft RTS would not be applicable to a parent undertaking which is not itself a credit institution or an investment firm, ESMA considers that Article 10(e) of the TD does not prevent a parent company that is not itself a credit institution or investment firm from being entitled to acquiring, disposing of or exercising voting rights of a subsidiary undertaking which is a credit institution or an investment firm. The only requirement is that the parent company is effectively able – because of the existence of a control relationship – to acquire, dispose of or exercise voting rights held by a subsidiary undertaking. TD Article

10 covers situations of indirect holdings whereby there is dissociation between direct ownership and the exercise of voting rights. In this regard, ESMA notes that the proposal put forward in the CP replicates a system which is already in place for individual and collective portfolio management holdings regarding investment firms and management firms, respectively.

46. Consequently, ESMA maintains the proposed wording for the draft RTS as it considers it to be applicable to parent companies which are not themselves credit institutions or investment firms and which are thus not entitled to have trading books or conduct market maker activities.
47. However, to avoid misunderstandings regarding the responsibility for notifications of aggregated holdings, Article 3 of the draft RTS will be amended as follows:

“For the purpose of calculation of the 5 % threshold provided for in Article 9(5) and (6) of Directive 2004/109/EC, holdings shall be aggregated at group level according to the principle laid down in Article 10(e) of said Directive.”

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?

Question 6

48. 15 respondents answered Q6. Nine clearly favoured Option 2 whereas two favoured Option 1 and opposed the exemption suggested by ESMA.
49. The two respondents who were against ESMA’s proposal were not in favour of exempting the parent undertaking from making the required notification concerning market making and trading book holdings of subsidiary companies. The main arguments presented were 1) the TD provides for a general rule of aggregation at group level (cf. TD Article 10(e)), 2) the exemption would lead to a lack of transparency as it would allow for the existence of several layers of trading books within the same group, thereby running counter to the main aim of the revised TD of enhancing transparency regarding major holdings, and 3) the proposed draft RTS is inconsistent with some provisions of Directive 2004/25/EC (the “Takeover Bids Directive”), as under this directive, a parent undertaking and its subsidiaries are always presumed to be “acting in concert”.
50. One respondent thought that the test of independence was not totally convincing as market making and trading book holdings would not be aggregated at group level up to the 10 % and 5 % thresholds, respectively, based on the fact that all other holdings were exercised independently. The respondent considered, however, that all other holdings would still be aggregated at group level following the principle set out in TD Article 10(e) which is based on the general experience that subsidiaries do not exercise votes independently from the parent company. This would result in a different treatment of the same case and thereby create an artificial distinction. Specifically, the respondent observed that holdings held by subsidiaries which are unrelated to trading book and market making activities are always attributed to the controlling parent company under Article 10(e) of the TD. Therefore, considering these holdings to be independent – as proposed with the test of independence – would not preserve the principle underlying TD Article 10(e).

51. Two of the respondents that supported Option 2 rather than Option 1 suggested changes to the proposed draft RTS. Firstly, as regards the declaration to the home NCA of the issuer of the relevant shares, it was suggested that ESMA should adopt an approach in line with the approach to notifications for the market making exemption under the SSR. Under such an approach, a parent undertaking with a home Member State would send the declaration to its own NCA which could then notify ESMA that it had received a notification from the parent undertaking. A third country parent undertaking would send its notification to the NCA of its main trading venue in the EU. ESMA could then publish and maintain on its website a list of all parent undertakings having performed such notifications. According to the respondent, this would be an efficient way of centralising all notifications relating to the same group.

Question 7

52. Six respondents provided answers to Q7 which addresses the costs connected with Option 1. No quantitative data was provided and it is not possible to draw out decisive conclusions from the answers.
53. One respondent stated that Option 1 would generally require more reporting than the current regime since there is currently no requirement to aggregate cash-settled instruments which are economically equivalent to shares, although some Member States have established such rules. However, the respondent stated that costs associated with such an increase in reporting were difficult to quantify at the current stage. At the other extreme, one respondent indicated that due to many European jurisdictions already having implemented a requirement to report on cash-settled instruments and already providing for a disaggregation exemption, disaggregation would have only a minimal impact. A third respondent expected that very few disclosures would have to be made on the basis of the proposal to aggregate at group level. These disclosures would be triggered purely by the trading book or market maker reaching a threshold and it would therefore in general be rare that aggregation with other controlled holdings would significantly increase the number of disclosures for this respondent.

Question 8

54. ESMA received ten responses to this question. Five respondents considered that Option 2 does not pose any further enforceability issues than Option 1 whilst two respondents were of the opinion that Option 2 adds complexity to the major shareholding notification system, thus hindering NCAs' ability to supervise and monitor (one respondent) and increasing administrative costs when compared to Option 1 (other respondent) due to the need to notify NCAs in different Member States. A third respondent argued that NCAs should be equipped to oversee and enforce the disclosure regime.

ESMA's response

55. ESMA has consulted on Option 1 (strict aggregation at group level) and Option 2 (aggregation at group level with possibility of disaggregation of market making and trading book holdings of subsidiary undertakings by the parent undertaking). Option 2 was aimed at providing balance to the principle of aggregation at group level and at following the instruction in the Article 9(6b) mandate to take TD Article 12(4) and (5) into consideration. As such, the intention was to offset the notifications arising from requiring aggregation of all holdings at group level.
56. ESMA acknowledges that supervisory convergence is an important consideration, but the differences in national legislation in the area of control relationships were already highlighted in the CP and have not hampered the utility of TD Article 12(4) and (5) which rely on a somehow similar test of independence. However, respondents have presented the novel argument that the proposed test of independence does not seem to be consistent with the treatment given to all other

holdings under TD Article 10(e). This problem is specific to the market making and trading book exemptions, as it is a pre-condition of the exemptions that the voting rights relating to these holdings are not exercised. For that reason, ESMA designed a different concept of independence addressing other holdings unrelated with market making and trading book activities. However, ESMA acknowledges that the proposed concept of independence is not totally consistent with Article 10(e) of the TD and that it would establish a further unnecessary distinction in group situations.

57. The alternative proposals presented by other respondents do not seem to solve the above mentioned issue. Some respondents suggested taking an approach similar to the one taken in the SSR whereby the notification should be sent to the home NCA which could then notify ESMA of having received such notification from the parent undertaking. It is ESMA's opinion that this proposal is not in line with the empowerment in TD Article 9(6b) according to which ESMA is mandated to consider the solution followed in TD Article 12(4) and (5). These provisions are further complemented by Article 10 of the Commission Directive which provides for a solution similar to the one proposed in the CP. Additionally, the TD itself does not create a competence for ESMA to receive notifications in this area. ESMA therefore considers that following an approach similar to the one taken in the SSR is not within the mandate received.
58. Considering all of the above, ESMA has opted to maintain the principle of aggregation at group level (Option 1) without providing for an exemption of disaggregation of market making and trading book holdings. It has been broadly confirmed by respondents to the consultation that maintaining the aggregation principle is not expected to lead to an increase in the number of notifications, given that in general the aggregation rule is already followed. On that basis, Article 3 of the draft RTS will have the following wording:

“For the purpose of calculation of the 5 % threshold provided for in Article 9(5) and (6) of Directive 2004/109/EC, holdings shall be aggregated at group level according to the principle laid down in Article 10(e) of said Directive.”

III.II Draft RTS 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

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).

Question 9

59. 17 respondents replied to Q9 of which seven were in favour of both thresholds proposed. The ten remaining respondents provided a number of suggestions and comments.
60. Firstly, it was suggested that the thresholds would be costly to monitor, particularly because a number of index providers charge investors for information about constituents and weights of indices and because of costs connected with adapting IT procedures and training staff. Secondly, it

was argued that it would be uneconomical for investors to build a stake in an issuer through financial instruments referenced to a basket of shares or an index. Thirdly, some respondents remarked that since standard indices are calculated based on the full capitalisation of the constituent issuers, financial instruments referenced to such indices would always breach the 1 % threshold. Based on these arguments, it was proposed that:

- One or both of the proposed thresholds should be increased for both baskets and indices (three respondents);
- The 1 % threshold should not apply to financial instruments referenced to indices (three respondents);
- The 1 % threshold should be increased for indices (one respondent); or
- The 1 % threshold should be deleted altogether (three respondents).

61. Lastly, two respondents raised the question whether – in case of financial instruments referenced to indices – the calculation of the 1 % referred to in Article 4(1)(a) of the draft RTS had to be based on 1) each financial instrument separately, 2) an accumulation of all financial instruments referenced to a given index, or 3) an accumulation of all financial instruments referenced to any index containing a given issuer.

62. As regards the application of the thresholds, a number of suggestions were made:

- Financial instruments typically used by asset managers, specifically UCITS, should not be covered by the thresholds because they are not used for stake-building and because Directive 2009/65/EC (the “UCITS Directive”) contains provisions prohibiting significant stake-building (three respondents);
- Aggregation of instruments referenced to a basket of shares or an index with other holdings should only be required when both the 1 % and the 20 % threshold are surpassed (two respondents);
- Aggregation should only be required for financial instruments referenced to actively managed baskets and indices (two respondents);
- Passive breaches of the thresholds or changes determined by a third party should 1) not trigger a requirement to re-calculate (three respondents), or alternatively 2) be calculated on the basis of the latest available public information about index composition as specified in Article 3(3) of the SSR (two respondents).

Question 10

63. There were ten answers to this question but only two respondents provided further thresholds to be considered. One respondent suggested combining a 2 % exemption threshold for cash-settled derivatives with a 10 % notification threshold for long positions while another respondent proposed replacing the 20 % threshold with a 50 % threshold.

Question 11

64. ESMA received answers from nine respondents to this question, two of them estimating they would not have to make additional disclosures if the proposed thresholds were adopted. Respondents to this question provided qualitative rather than quantitative views on costs with a small minority not providing any opinion on costs at all. Generally, the view was that the proposed thresholds would not lead to a significant increase in the number of notifications. However, respondents highlighted that the focus should rather be on the monitoring costs incurred by in-

vestors in order to identify financial instruments referenced to a basket of shares or an index subject to aggregation with other holdings than on the cost of notifications.

ESMA's response

65. In response to the comments presented in paragraph 60, ESMA firstly notes that according to the revised TD, financial instruments referenced to a basket of shares or an index are covered by the TD's notification requirements. While some respondents seem to disagree with this approach, it does not fall within ESMA's mandate to qualify or challenge the Level 1 principle that such instruments must be notified in accordance with the TD.
66. Secondly, and related, ESMA observes that the costs mentioned by respondents do not arise from Article 4 of the draft RTS but rather from Level 1 itself. Following transposition of the TD¹, investors will be obliged to disclose their aggregated holdings in an issuer through shares, entitlements to acquire shares and financial instruments economically equivalent to shares when such holdings reach, exceed or fall below the thresholds set out in TD Article 9(1). To comply with this requirement, investors will need to monitor their exposure to a given issuer through all of the aforementioned holdings, including financial instruments referenced to a basket of shares or an index. On that basis, costs stemming from such monitoring will be incurred due to obligations set out at Level 1.
67. However, upon further analysis of responses, ESMA believes that some respondents might have expected an exemption from the Level 1 notification requirements for financial instruments referenced to a basket of shares or an index. This would explain why some respondents describe costs as stemming from the thresholds proposed in the draft RTS. ESMA wishes to clarify that Article 4 of the draft RTS does not set out an exemption but specifies the method for calculating the number of voting rights for financial instruments referenced to a basket of shares or an index by setting out specific circumstances which should be taken into account in this calculation. Such circumstances aim at decreasing the number of meaningless notifications while recognising that financial instruments referenced to a basket of shares or an index have to be disclosed according to the revised TD. ESMA also highlights that the proposed thresholds do not constitute notification thresholds but thresholds from which one should start aggregating holdings of financial instruments referenced to a basket of shares or an index to other holdings in the same issuer in order to ascertain whether a notification threshold has been reached and a notification is required.
68. On this basis, ESMA is of the view that the two thresholds proposed in the CP should remain unchanged. However, ESMA wishes to address the comment from some respondents that for a number of commonly used indices, the shares of a given issuer in the index represent 100 % of the total amount of shares of that issuer and such indices would thus always surpass the 1 % threshold. ESMA clarifies that the 1 % referred to in Article 4(1)(a) of the draft RTS should be calculated based on the number of voting rights which an investor holds through financial instruments referenced to a basket of shares or an index, not based on the number of voting rights connected to shares contained in the basket or index as a whole. ESMA will amend the wording of Article 4(1)(a) of the draft RTS to reflect this clarification (see paragraph 75).
69. The amendment of draft RTS Article 4(1)(a) also serves a second purpose, namely to address the question raised by two respondents regarding whether – in the case of financial instruments referenced to indices – the calculation of the 1 % referred to in Article 4(1)(a) has to be based on 1) each financial instrument separately, 2) an accumulation of all financial instruments referenced to a given index, or 3) an accumulation of all financial instruments referenced to any index con-

¹ Transposition deadline 26 November 2015.

taining a given issuer. The amended Article 4(1)(a) of the draft RTS makes it clear that when an investor holds more than one financial instrument referring to the same basket/index, such instruments have to be accumulated for the purpose of calculating the 1 % (i.e., option 2 is correct). As it is important that this principle is also clear when reading Article 4(2) of the draft RTS, ESMA has furthermore amended the wording of Article 4(2) to avoid any misunderstanding (see paragraph 78).

70. Furthermore, and as reflected in paragraph 62, respondents have provided suggestions concerning the application of the thresholds. Regarding the argument that derivatives used by asset managers (especially UCITS) should not be covered, ESMA does not share the opinion that provisions in the UCITS Directive prohibit significant stake-building per se. Such provisions establish that a UCITS can have a certain percentage of its assets invested in an issuer. Therefore, the bigger the UCITS, the higher the stake permitted in a given issuer. In any case, ESMA is of the opinion that the existence of Level 1 provisions prohibiting asset managers to build a significant stake is compatible with the proposed content for the RTS.
71. As regards the suggestion that the 1 % and 20 % thresholds should be cumulative instead of alternative, ESMA considers that the two thresholds have different justifications: while the 1 % threshold is an absolute importance threshold – irrespective of the variety of the composition of the basket/index – the 20 % threshold is related to the function of the financial instrument as being one that provides a sufficient diversification of the investment. In conclusion, ESMA considers it important that an investor holding 1 % or more of the voting rights in an issuer through a financial instrument referenced to a basket/index aggregates such voting rights with any others it may have in the issuer in order to ascertain the existence of a major shareholding, even when the shares in the basket or index represent less than 20 % of the value of the securities in the basket/index. Conversely, where the shares in the basket/index represent 20 % or more of the value of the securities in the basket/index, but the investor does not hold 1 % or more of voting rights attached to shares of that issuer, the financial instrument should be aggregated to other positions which the investor holds in the same issuer because the significant weight of the issuer in the composition of the basket/index shows that the holder of the financial instrument has an economic interest in the issuer.
72. As regards the suggestion that the proposed thresholds should apply merely to actively managed baskets/indices and not to the ones which are determined by a third party, as it is the case for most stock indices, ESMA recognises that stake-building is more likely to take place through financial instruments referenced to actively managed baskets and indices. However, the aim of the TD is to enhance transparency regarding voting rights and this cannot be consistently achieved if voting rights pertaining to passively managed baskets and indices are excluded from the scope of the RTS. Therefore, ESMA does not distinguish actively from passively managed baskets/indices.
73. Regarding the argument that passive changes should not trigger a new calculation of voting rights or, alternatively, that passive changes should be calculated on the basis of the latest available public information about basket/index composition as specified in Article 3(3) of the SSR, ESMA considers that it is not within the mandate to address this issue but it may consider addressing it by way of guidance to the market at a later point in time.
74. Lastly, regarding the two alternative thresholds suggested by respondents (see paragraph 63), ESMA notes that the TD expressly calls for the aggregation of shares, entitlements to acquire shares and financial instruments considered to be economically equivalent to shares for the purposes of notification. Therefore, cash-settled derivatives and long positions cannot be exempt from aggregation. As regards replacing the 20 % threshold with a 50 % threshold, ESMA considers that a

threshold of this magnitude would not meet the purpose of creating transparency regarding financial instruments referenced to a basket of shares or an index.

75. Based on the above, Article 4(1)(a) of the draft RTS will be reworded as follows:

“1. Voting rights in the case of a financial instrument subject to notification requirements laid down in Article 13(1) of Directive 2004/109/EC 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 voting rights in a specific issuer held through financial instruments referenced to the basket or index represent 1 % or more of voting rights attached to shares of that 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.”

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?

76. Respondents' views were very convergent on this topic; out of the 17 answers, 16 agreed with ESMA's proposal. Respondents agreed that it would not be cost-efficient to build up a position by obtaining small positions in different baskets before aggregating them which illustrates the lack of suitability of such a strategy to obtain influence or acquire shares in an issuer. Moreover, respondents pointed out that aggregating baskets would add complexity that could compromise firms' ability to monitor effectively without achieving a significant benefit to the market.

77. Three market participants suggested including a reference to indices in Article 4(2) of the proposed draft RTS, as it currently only refers to baskets.

ESMA's response

78. ESMA acknowledges that the same reasons underlying the proposed solution for a financial instrument referenced to a series of baskets of shares apply in the case of a financial instrument referenced to a series of indices. Therefore, in response to the suggestion described in paragraph 77, ESMA has added “indices” to the wording of Article 4(2) of the draft RTS. Furthermore, Article 4(2) has been amended to ensure clarity regarding the comment raised by two respondents in paragraph 61 and addressed by ESMA in paragraph 69. On this basis, the wording of Article 4(2) of the draft RTS is as follows:

“2. When a financial instrument is referenced to a series of baskets of shares or indices, the voting rights held through the individual baskets of shares or indices shall not be accumulated for the purpose of the thresholds set out in paragraph 1.”

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

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”?

Question 13

79. Responses to Q13 showed broad support for ESMA’s proposed method of determining delta (i.e., Option 2). Out of the 18 respondents, 15 fully agreed and one partially agreed that the proposed method will prevent circumvention of notification rules and excessive notifications. No respondents disagreed with the proposed method.
80. The arguments provided in support of Option 2 revolved around two themes; the benefits from the flexibility provided by Option 2 and the disadvantages of Option 1.
81. As regards the benefits of Option 2, one respondent highlighted that a principle-based approach to determining delta would permit regulated entities to utilise the calculation method already agreed with the regulator in the areas of pricing and risk which would prevent confusion and minimise unnecessary costs. A related argument was made by two respondents who observed that a number of market participants (entities regulated by CRD IV, management firms and asset managers) already have models in place for calculating delta which they would be able to continue using under Option 2.
82. Additionally, two respondents remarked that, as opposed to a prescriptive approach, a principle-based approach would avoid the calculation of a ‘fictitious’ delta resulting from a standard formula which would not accurately reflect the economic exposure under a given financial instrument, thereby ensuring more precise calculations and consequently accurate notifications.
83. Lastly, three respondents stated that Option 2 in their view would be able to prevent circumvention of notification rules without requiring excessive disclosures, whereas one respondent did not believe it is possible to wholly prevent circumvention but believed that Option 2 was the best available approach. Another respondent agreed that Option 2 could presumably impede circumvention of notification rules but was unsure as to whether it could prevent unnecessary notifications since the prohibition of ‘netting’ of positions might under certain conditions result in a large number of notifications which would not represent the actual holdings situation. This respondent, however, still preferred Option 2 to Option 1.
84. Concerning the disadvantages of Option 1, it was stressed that a prescriptive approach to determining delta would be unfeasible in practice (one respondent); that it would require continuous updating and as such constantly be lagging behind market developments with the entailed risk of circumvention (two respondents) and that it would oblige some market participants to operate parallel calculation systems, thereby imposing needless costs on them (one respondent).
85. The respondent which partially agreed with the proposed method of delta calculation suggested that paragraph 1 and 2 of Article 5 of the draft RTS be merged which would effectively mean a deletion of the reference to a delta of 1 for cash-settled financial instruments with a linear, symmetric pay-off profile. Furthermore, this respondent proposed that Article 5(5) of the draft RTS should allow for IT systems or procedures for the purpose of running the calculation of delta, given the high implementation costs of IT systems and taking into consideration a principle of proportionality.
86. Other proposed modifications to the draft RTS were that entities should employ the same models for calculation of delta for the purpose of disclosure of voting rights as for the purpose of risk

management (one respondent); that delta calculations and notifications should be performed on a monthly instead of on a daily basis (one respondent) and that in Article 5(5), the word “reporting” should be replaced with “calculation” since IT systems should ensure the adequate calculation of voting rights whereas the reporting of such is the responsibility of market participants (one respondent).

Question 14

87. Responses to Q14 were even more uniform than to Q13: All 18 respondents agreed with the proposed concept of a generally accepted standard pricing model. The following arguments were provided in support of the concept:

- The concept provides flexibility, thereby preventing additional costs/burdens being imposed on market participants (four respondents);
- The approach facilitates current market practice as it allows generally accepted standard pricing models already in use in the market, e.g. under CRD IV and Regulation (EU) No 575/2013 (the “Capital Requirements Regulation”), to be applied (five respondents);
- A more granular approach would limit the models that could be used for calculation of delta as a specific definition would always lag behind market developments (three respondents);
- The five elements mentioned as affecting valuation are correct (three respondents), they will be appropriate even for complex or exotic products (one respondent) and the concept of a delta of 1 for instruments with a linear, symmetric pay-off profile is correct (one respondent); and
- The approach is able to ensure meaningful information to the market and to regulators (one respondent), will enable firms and their clients to report their voting rights in an appropriate manner (one respondent) and will prevent circumvention of notification duties (one respondent).

88. One respondent commented that when new financial instruments are developed, or in the case of exotic and rarely used derivatives, the generally accepted standard pricing model is unlikely to be “widely used” and therefore it might be more appropriate to use the term “best available” or “generally used for that instrument” for the purpose of Article 5(3) of the draft RTS. This respondent further suggested replacing the word “share” with “instrument” in draft RTS Article 5(3)(e) and allowing market participants to change the calculation model for a given instrument when a better model is developed for calculating the delta of said instrument (draft RTS Article 5(4)(b)).

ESMA’s response

89. ESMA acknowledges the wide support received for Option 2 and will accordingly proceed by following a principle-based approach. Some respondents presented wording suggestions regarding which ESMA hereby provides feedback. Concerning the suggestion that paragraph 1 and 2 of Article 5 of the draft RTS be merged and the reference to a delta of 1 for cash-settled financial instruments with a linear, symmetric pay-off profile be deleted, ESMA considers that it is advisable to maintain the current proposal. The two paragraphs propose a method for two different types of cash-settled financial instruments, the ones with a linear, symmetric pay-off profile on the one hand and all the others, on the other hand. Though the first paragraph appears to be simple, it is technically correct and in line with the mandate whereby ESMA should specify the “methods for determining delta for the purposes of calculating voting rights”.

90. Regarding the comment that for the purpose of draft RTS Article 5(3) a generally accepted standard pricing model is unlikely to be “widely used” and therefore it might be more appropriate to use the term “best available” or “generally used for that instrument” in the case of new financial instruments or exotic and rarely used derivatives, ESMA restates that the parameters included are very high level ones and will normally constitute the core part of every new formula. However, ESMA acknowledges that the wording “generally used in the finance industry for that financial instrument” would be better able to take into account the emergence of new financial instruments and has on that basis decided to amend the wording of the proposed Article 5(3) of the draft RTS (see paragraph 96).
91. One respondent further suggested replacing the word “share” with “instrument” in draft RTS Article 5(3)(e) and to allow market participants to change the calculation model for a given instrument when a better model is advanced for developing the delta of said instrument (draft RTS Article 5(4)(b)). ESMA notes that the concept of “generally accepted standard pricing model” is a flexible one, where only some core parameters are required and therefore it will allow for technical developments in accordance with the financial instrument’s specific features.
92. Another proposed alternative wording advanced by a respondent is that Article 5(5) of the draft RTS should allow for IT systems or procedures for the purpose of running the calculation of delta, given the high implementation costs of IT systems and taking into consideration a principle of proportionality. ESMA is of the opinion that a delta calculation made according to a “generally accepted standard pricing model” will normally require the existence of IT systems to run the calculation. In this context, ESMA clarifies that IT systems cover non-manual processes which automate the calculation of delta. The existence of procedures only does not seem to ensure a similar level of reliability of the calculation.
93. It was also suggested that in Article 5(5) of the draft RTS, the word “reporting” should be replaced with “calculation” since IT systems should ensure the adequate calculation of voting rights whereas the reporting of such is the responsibility of market participants. ESMA agrees with the respondent that IT systems run calculations. However, the focus of the rule relies on the investor to whom notification requirements apply and thus “reporting” expresses better that IT systems are ancillary to the performance of the duty of the investor to notify a major holding.
94. One respondent proposed that entities should employ the same models for calculation of delta for the purpose of disclosure of voting rights as for the purpose of risk management. This proposal has the merit of simplicity, but it is not always the case that positions calculated for the purposes of risk management are made on the basis of a delta calculation, whereas the TD requires all voting rights regarding cash-settled financial instruments to be calculated on a delta-adjusted basis. Furthermore, risk management is conducted on a net position basis whereas netting of short and long positions is not allowed when calculating delta-adjusted positions (cf. TD Article 13(1a)). For this reason ESMA has decided not to propose adopting one single calculation model for all purposes.
95. Another suggestion was that delta calculations and notifications should be performed on a monthly instead of on a daily basis. However, this proposal is not in line with the TD, because changes in a position should be reported whenever a threshold is crossed. Therefore, delta calculation should be done daily so that the investor can monitor the necessity of notifying under Article 13(1) of the TD.
96. In view of the above considerations, ESMA has decided to maintain a principle-based approach to calculation of delta. The wording of Article 5 of the draft RTS will remain as presented in the CP, except for Article 5(3) which will have the following wording:

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

- (a) interest rate;***
- (b) dividend payments;***
- (c) time to maturity;***
- (d) volatility; and***
- (e) price of underlying share.”***

III.IV Draft RTS on client-serving transactions

97. It was mentioned in the CP that an interpretation of the mandate allowing for the creation of a stand-alone exemption could be subject to legal challenge (cf. paragraph 138 of the CP).
98. The consultation process is crucial in promoting a mutual understanding of ESMA’s role in the regulatory landscape. In this regard, ESMA has received a number of responses from market participants which acknowledge the lack of clarity of the mandate concerning client-serving transactions and consequently that an RTS might not be the most appropriate regulatory tool to settle a matter involving a policy choice.
99. During the course of the consultation, and, in accordance with Article 10(3) of the ESMA Regulation, ESMA requested the opinion of the SMSG. The SMSG expressed the view that Option 2 would be in line with the purpose of the TD and would be most appropriate to avoid meaningless notifications. However, the SMSG further expressed the view that adopting Option 2 would mean establishing a further exemption from the notification requirements for which ESMA has no mandate. The SMSG concluded that ESMA should restrict itself to the mandate given in the Level 1 text. The problem has to be solved at Level 1 by the Commission, European Parliament and Council and to attempt to do otherwise would upset the inter-institutional balance.
100. From a policy point of view, it is clear to both respondents and to ESMA that Option 2 is the approach which addresses the problem of meaningless notifications arising from the introduction of a notification obligation for cash-settled financial instruments. However, ESMA, supported by some respondents and the SMSG, considers that the empowerment to establish such a stand-alone exemption cannot be extracted from the existing mandate in TD Article 13(4). Based on this, and the fact that a draft RTS should not entail making policy choices, there is a conflict between the policy considerations and legal considerations. ESMA considers itself to be limited by the legal constraints.
101. ESMA notes that it has strongly endeavoured to obtain quantitative data that would evidence the absolute necessity of a separate full exemption for client-serving transactions. However, it was not possible to obtain such data from respondents to the consultation. The discussion of the two options has thus been kept at a qualitative level which prevents a full assessment of the magnitude of the problem and the extent to which the obligation to notify can constitute a burden for market participants or pose a transparency problem for the market, thus affecting market efficiency.
102. Considering the above points, and while acknowledging the potential impact on market participants, ESMA concludes that it has no option other than to proceed according to Option 1 whereby it will assess whether current exemptions can apply to client-serving transactions. Nonetheless,

ESMA wishes to provide comments to the responses received to the consultation as it considers that such comments could provide input, should a Level 1 revision be proposed by the EC at a later stage. The following sections therefore contain feedback regarding the public consultation carried out in respect of client-serving transactions.

103. When considering the content for the RTS according to Option 1, ESMA considers that of the exemptions mentioned in paragraph 1 of TD Article 13(4), only the trading book exemption can address at least some of the concerns posed by client-serving transactions, i.e., avoiding meaningless notifications that would be misleading to the market. Feedback from market participants has confirmed this view, although with the caveat that the trading book exemption might not be sufficient to avoid meaningless notifications.
104. Accordingly, the trading book exemption will have a double function, and should thus be used for the initial purposes it was designed for and also to cover client-serving transactions. Given that this exemption has to cover holdings regarding shares, entitlements to acquire shares and financial instruments considered economically equivalent to shares, there may be some cases where the respective thresholds are exceeded and a notification is required.
105. Market participants furthermore made it clear that, trading book exemption aside, client-serving transactions are an independent topic that cannot be covered by any other exemption provided for in TD Articles 9 and 12. While ESMA restates that it is technically correct that the procedural rule of TD Article 12(3) applies to client-serving transactions, it acknowledges that this rule applies in any case to such transactions and does not need to be dealt with by means of an RTS. For this reason, the draft RTS on client-serving transactions clarifies that the trading book exemption applies to financial instruments held for client-serving purposes whereas the draft RTS does not include a reference to the application of TD Article 12(3).
106. On that basis, the wording of Article 6 of the draft RTS will be based on paragraph 1 of the proposed client-serving article from page 33 of the CP:

“The exemption referred to in Article 9(6) of Directive 2004/109/EC 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.”

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?

Question 15

107. 15 respondents expressed their views on the appropriateness of the three types of client-serving transactions. The vast majority of respondents did not provide views on the costs entailed, should any of these exemptions not be adopted. Some respondents provided qualitative comments about costs without delivering quantitative evidence. The emphasis was put on the misleading picture that such notifications would create in the market.
108. One market participant considered that the three examples for the three types of client-serving transactions are appropriate, but that some clarification is necessary regarding the use of the word "proprietary". Specifically, the phrase "otherwise than on a proprietary basis" should be clarified to mean "otherwise than for the client-serving entity's own investment purposes". Two respondents voiced the concern that the client-serving transactions would extend to other financial instruments than only cash-settled ones, namely TD Article 13(1)(a) entitlements to acquire shares and shares used to hedge positions arising out of client-facilitating transactions.
109. One market participant was not in favour of the introduction of a client-serving exemption for the three types of transactions. This respondent presented the view that the purpose of a client-serving exemption is to avoid double notifications of both the final holder of a share or an economic interest in the share (the client) and the bank providing services to this holder. On that basis, the respondent shared ESMA's analysis of case 1 and case 3, provided that a notification by the client is ensured. At the same time, the respondent was of the opinion that case 2 is different from case 1 and case 3 and that it should therefore not fall under the exemption because any trade in a financial instrument may be regarded as responding to a client's request. In addition, responding to a client's request may be part of a bank's trading and/or market making activities where significant exemptions have already been granted.

Question 16

110. 14 respondents replied to Q16, 12 of these expressing the view that the three types of client-serving transactions do not allow for a potential risk of circumvention of the major shareholdings' disclosure regime. According to these respondents, any potential risk of circumvention would be largely offset by the disincentive of countervailing risks to the investor and/or intermediary, including in particular the economic risk of an unhedged short position (mentioned in paragraph 118 of the CP) and the regime prohibiting market abuse. One respondent could not see a risk of circumvention of the major shareholdings' disclosure regime, because client-serving positions are held "on behalf" of clients and therefore the voting rights will be attributed to the client according to Article 10(g) of the revised TD.
111. Finally, one respondent, declaring to be answering "from an issuer's perspective", believed disclosures should be meaningful and kept to a minimum, however so achieved.

ESMA's response

112. The purpose of these two questions was to benefit from market participants' expertise in order to assess whether the three types of client-serving transactions were adequately described and would be effective in preventing meaningless notifications. Additionally, one of the questions aimed at receiving data from market participants.
113. The responses received confirm the accurateness of the cases described. However, when justifying the reason for avoiding meaningless notifications, respondents have stated that the client would in all cases report its position, rendering avoidable the financial intermediary notification.
114. If avoiding duplication of information constituted the grounds for awarding the client-serving exemption, it should be possible to state that in all three types of transactions – cases 1, 2 and 3 described in paragraphs 115 to 117 of the CP – the financial intermediary ought to be exempt from making a notification because such notification would overlap with that of the final client. Yet, the key rationale behind the client-serving exemption is to avoid meaningless notifications. The situation illustrated by case 2 potentially opens the door to accepting cases where neither the financial intermediary nor the client will notify the market of the transaction. It is thus possible to infer that when responding affirmatively to Q15, respondents have had cases 1 and 3 in mind and have not recognised that case 2 has a different validation logic. On this point, ESMA observes a lack of consistency in respondents' arguments which seem to advise that a full exemption be restricted to cases 1 and 3.
115. Regarding the request for a clarification of the word "proprietary", ESMA notes that the TD does not provide a concept of proprietary trading; however, the concept is widely used in the context of banking regulation where its boundaries are more precisely defined. These circumstances make it difficult to introduce this concept in the RTS without a clear indication in the Level 1 text. Consequently, ESMA has not followed this suggestion.

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)?

Question 17

116. Nine out of the 15 respondents to Q17 agreed with ESMA's analysis that applying the current exemptions can address certain notification requirements for cash-settled financial instruments, given that such exemptions are not restricted to shares and entitlements to acquire shares.
117. One respondent stated that all three types of client-serving transactions constitute market making, although the TD's market making exemption has not been uniformly implemented across Member States and therefore cannot be relied upon in relation to all transactions which are of a client-serving nature. On the other hand, another respondent was of the opinion that only the trading book exemption can cover the three types of transactions but that it is insufficient to obviate meaningless notifications as it is subject to the 5 % cap. Finally, one respondent called for disclosures to be done by the beneficial owner in order to render information to the market more understandable, relevant and clear and to create a more transparent market.

Question 18

118. Of the 15 respondents to Q18, nine were of the opinion that applying the current exemptions will not be sufficient to achieve the aim of avoiding unmeaningful notifications to the market. In general, respondents argued that the 10 % and 5 % thresholds for the market making and trading book exemption, respectively, would be easily exceeded by the inclusion of long positions of financial intermediaries in cash-settled financial instruments for the purpose of client business facilitation. The insufficiency of current exemptions to cover all long positions acquired in the remit of client-serving transactions would ultimately result in lack of transparency by veiling the identity of true stakeholders, thus running counter to the aim of the revised TD. Any cash-settled positions entered into purely for client-serving purposes would, if they were disclosed, mask direct positions entered into for investment purposes and thereby undermine the overriding objective of accurate transparency.
119. Another respondent voiced the opinion that the trading book and market making exemptions are not specifically designed to cover client-serving transactions having cash-settled financial instruments as a subject and therefore will not be effective tools in avoiding meaningless notifications. Additionally, one participant put forward that the effectiveness of the current market making exemption is limited in that the application of the rules can vary substantially across Member States. In certain Member States the application of the rules can be overly cumbersome and to that extent may not be utilised as intended in those Member States.
120. It was furthermore stressed that the inclusion of certain cash-settled financial instruments under TD Article 13(1)(b) has fundamentally changed the objective of the TD from only identifying significant voting interests which can directly influence issuers to also identifying significant economic exposures. The separate addition of this specific component to the TD regime requires that TD Article 13(4) be interpreted as introducing a separate and specific client-serving exemption as opposed to simply overlaying the pre-existing market making and trading book exemptions which are otherwise applicable only to shares or instruments giving a right to acquire shares (Articles 9 and 13(1) of the TD prior to revision).
121. In addition, two respondents believed that the exemption should apply to any financial instrument (including physical shares and physically settled derivatives) that a client-serving entity holds in order to hedge a cash-settled derivative transaction entered into in a client-serving capacity, because just as it would not provide meaningful information to the market if a client-serving entity was to disclose a long derivative position it had entered into at a client's request (case 2, CP paragraph 116), it would also not provide meaningful information to the market if a client-serving entity was to disclose a long position in shares which it held as a hedge to a short cash-settled derivative position it had entered into at a client's request (case 3, CP paragraph 117).

ESMA's response

122. Respondents to this question considered that current exemptions, specifically the market making and the trading book, can cover some types of client-serving transactions. At the same time, respondents relayed that such current exemptions could be insufficient to reach the main objective of avoiding meaningless notifications for quantitative and qualitative reasons. As regards the quantitative reasons, the number of notifications connected with client facilitation can in some cases exceed the 10 % and 5 % thresholds available for the market making and trading book exemptions, respectively. As regards the qualitative reasons, most client-serving transactions would

not be covered by the market making exemption since the market making concept of the TD² is closely related to the activity of a market maker acting as a counterparty in a regulated market, providing both the buy and sell sides on a continuous basis and using its proprietary capital.

123. The purpose of client-serving transactions is different from that of market making under the TD because the principle behind the client-serving transaction is that firms hold a position purely to facilitate a client's position. An example of a client-serving transaction could be that client A of financial intermediary X wants to sell and client B wants to buy shares. The financial intermediary will acquire shares from A and will later sell them to B, bringing both clients together without risking its capital (riskless principal transaction³). Such transactions would not be covered by the market making exemption as currently defined in the TD, because they do not involve the proprietary capital of the financial intermediary. Therefore, ESMA considers that the trading book exemption is the most adequate to cover client-serving transactions.
124. ESMA understands that by introducing a new disclosure obligation for cash-settled financial instruments, the revised TD will lead to an increase in notifications of positions, including the ones connected with client facilitation. The nature of the transactions at the origin of a notification will not always be clear to the market which will necessitate a special care in the explanation provided by the holder of the financial instrument in the notification under Article 11(3) of the Commission Directive.
125. ESMA is of the opinion that the risk of meaningless notifications is well documented whenever the client is obliged to notify. This point has also been widely made by respondents. However, it is more difficult to justify the lack of economic interest of the financial intermediary (i.e., that he is not acting on a proprietary basis for the sole purpose of making a profit for his own account) in the case where the client is not obliged to notify because he does not assume a long position himself and the financial intermediary does not hedge its long position maintaining its financial exposure. In such cases, ESMA considers that notifications correctly reflect the presence of an economic interest and are not meaningless.
126. Finally, some respondents have mentioned that a potential client-serving exemption should apply to all financial instruments and not only to cash-settled ones as the same underlying reasons require the same solutions. When assessing how to specify such cases ESMA considers that the newly introduced obligation to disclose cash-settled financial instruments has to be weighed against market efficiency. TD Article 13(4) mandates ESMA to specify the cases in which current exemptions apply to financial instruments held by financial intermediaries when facilitating clients' business. Shares and entitlements to acquire shares were already subject to notification requirements before the revision of the TD and were equally benefiting of a number of exemptions available in TD Article 9(4), (5) and (6) and in Article 12(3), (4) and (5). Specifically, the market making and the trading book exemption were already being appropriately used with meaningful and suitable thresholds to shares and financial instruments.
127. 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 affect market

² TD Article 2(1)(n) defines market maker 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".

³ Riskless principal transactions involve two clients' orders where the execution of one of these orders is dependent upon the receipt or execution of the other. As a result, the market maker acts as an intermediary but bears no economic risk with the transaction.

efficiency. Therefore, ESMA restates that the subject matter of such an exemption should be cash-settled, TD Article 13(1)(b) financial instruments.

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?

Question 19

128. Q19 was answered by 16 respondents, nine of which were in favour of extending the client-serving exemption to 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. One respondent argued that as the language of TD Article 13(4) refers to “a natural person or a legal entity”, the client-serving exemption should apply to non-MiFID entities, whether EU or non-EU, as long as they are in the same group as a MiFID authorised entity.
129. None of the respondents brought forward an estimate of the costs entailed should the exemption not be extended to non-EU entities.

Question 20

130. ESMA received 12 replies to Q20. In general respondents took the view that no further control mechanisms should be implemented. However, one respondent suggested as an alternative that the proposed notification that client-serving entities would have to make in order to benefit from the exemption should be sent to the NCA of their home Member State rather than to the NCA of the issuer’s home Member State. A third country entity should send the notification to the NCA of the main trading venue in which it trades within the EU rather than to the NCA of the issuer’s home Member State. The NCA receiving such notification should then coordinate with other NCAs of the relevant issuers or ESMA accordingly.
131. Two respondents supported the requirement that the financial intermediary should be authorised under MiFID. Notwithstanding this, they considered that the notification formalities imposed by the proposed text of Article 7 of the draft RTS are unnecessary and do not create any additional comfort that a bank is not abusing the client-serving exemptions. As soon as an investment firm is authorised under MiFID, it should be assumed that it will seek to benefit from the client-serving exemption and, in so doing, has no intention to intervene or exert influence on the management of any issuer. It should thus be sufficient that it maintains appropriate systems and controls to ensure ongoing compliance with this requirement and that the NCA has the possibility to check this at all times.
132. It was also conveyed by a respondent that the exemptions which are available to subsidiaries within the group must similarly be available to the ultimate group parent entity.

ESMA’s response

133. Questions 19 and 20 addressed the subjective scope of a possible client-serving exemption and the control mechanisms to be implemented. While making clear that ESMA already concluded in paragraph 102 that Option 1 is the only approach available for the content of the draft RTS, ESMA is bound to provide feedback to market participants regarding the responses to the consultation.
134. On the first subject, respondents were widely supportive of extending the exemption to non MiFID authorised entities as long as they are in a group where there is a MiFID authorised entity. The respondent that commented that the client-serving exemption should be construed as applying to non-MiFID entities, whether EU or non-EU, as long as they are in the same group as a MiFID-authorised entity further evidenced its point by emphasising that where an exemption under the TD is aimed at MiFID authorised firms, this fact is specifically stated, as in the market making exemption under TD Article 9(5), whereas the custody exemption under TD Article 9(4) does not require MiFID authorisation.
135. ESMA acknowledges this argument and is of the opinion that it is consistent with the TD's wording that a natural person or a legal entity does not necessarily need to be authorised under MiFID. However, it is also true that such natural person or legal entity, in the context of TD Article 13(4), will be a professional holding a position in connection to client activity or for the purpose of hedging its risk as a result of client activity. The exercise of an investment service activity in a Member State is subject to authorisation under MiFID and for this reason it seems consistent with the European regulatory framework to state that such entities have to be authorised under MiFID.
136. As concerns the proposal made by one respondent in paragraph 130, ESMA considers that such proposal is not in line with the control mechanisms provided under the TD's framework, including the Commission Directive, which are built upon a notification being made to the NCA of the home Member State of issuers whose voting rights are attached to holdings (cf. the market making exemption and disaggregation of individual portfolio management holdings).
137. Regarding the control mechanisms to be implemented, ESMA strongly disagrees with the statement that notification formalities are superfluous (paragraph 131). The control mechanisms proposed are similar to the ones in place for market makers (cf. Article 9(5) of TD and Article 6 of the Commission Directive) which have proven to be useful for national regulators and to provide them with the necessary tools to intervene and exercise their supervisory powers when needed, on the one side, and to bestow the necessary flexibility for market participants to conduct their business activities, on the other.

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

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?

138. Of the 22 questions in the CP, Q21 received the greatest number of responses, 21 in total. The majority of respondents did not provide an answer to the first part of the question which pertains to the general concept of “economic effect similar” to that of shares or entitlements to acquire shares. Instead respondents concentrated on the items in the list, providing specific comments relating to certain types of financial instruments.
139. In respect of the first part of the question which enquired about the concept of “economic effect similar” to that of shares or entitlements to acquire shares, six respondents agreed with ESMA’s

proposal that a financial instrument has an economic effect similar to that of shares or entitlements to acquire shares when such financial instrument exposes the holder to the benefits of an upward movement and/or the damages of a downward movement of the price of the underlying shares.

140. Four respondents did not support ESMA's view as they failed to see the reason why cash-settled financial instruments that do not give access to voting rights or enhance the possibility to acquire shares should be disclosed. According to these respondents, this would be contrary to the objective of the revised TD – enhancing transparency regarding the allocation of voting rights – as cash-settled financial instruments are normally not used to acquire voting rights. Consequently, some of these respondents proposed introducing a “safe harbour” clause whereby cash-settled financial instruments would only be disclosed in the presence of trade-specific circumstances – occurring either at the inception or during the term of such instrument – that effectively result in an enhanced possibility for such party to acquire the shares underlying or hedging the trade or to exercise or control any of the voting rights attached thereto.
141. Regarding the second part of the question, the comments focused on the following financial instruments:
- Financial instruments relating to already issued shares: one respondent suggested clarifying that only financial instruments relating to already issued shares should be the subject of disclosure following the TD's indication in respect of convertible and exchangeable bonds. For example, paragraph 3 of the list should only include warrants relating to already issued shares (paragraph 3(c)), conditional contracts or agreements relating to already issued shares (paragraph 3(g)), hybrid financial instruments relating to already issued shares (paragraph 3(h)), and so on;
 - Convertible bonds: one respondent considered that such should either be entirely excluded or included, irrespective of whether they relate to new or already issued shares as any such distinction would be difficult to monitor;
 - Right of recall shares: three respondents asked for the exclusion from the list of routine stock lending or repo agreements whilst one made the point that such rights are already covered by the terms of TD Article 10(b) while still other requested a clarification that the notification is limited to repurchase agreements where the underlying collateral consists of equity securities to which voting rights are attached;
 - “Other conditional contracts or agreements”: one respondent commented that including these contracts irrespective of any derivative element that such contracts or agreements might have would not provide any practical guidance;
 - Instruments which do not have a pay-off profile in line with the underlying share: one respondent observed that such instruments, e.g. options, have not been used for the purpose of stake-building and therefore considering such instruments “economically equivalent to shares or entitlements to acquire shares” and including them in the list would be debatable;
 - Financial instruments having optionality depending on external factors: according to some respondents, such instruments, e.g. pre-emption contractual rights (three respondents), put options (three respondents) and underwriting agreements (one respondent), should be outside the scope of the disclosure obligation;
 - Shareholder's agreements: one respondent called for clarification of the meaning of the expression “having any of the above mentioned financial instruments as an underlying”.

ESMA's response

142. First, ESMA notes that the majority of respondents have not provided contributions regarding a general concept of “economic effect similar” to that of shares or entitlements to acquire shares. ESMA has proposed that a financial instrument should be considered economically equivalent to a share or an entitlement to acquire a share 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.
143. The majority of respondents to this question supported ESMA's view. On this point ESMA notes that Article 13(1) of the TD subjects entitlements to acquire shares and financial instruments considered economically equivalent to shares to the same notification requirements. The task to be performed by ESMA is to establish an indicative list of financial instruments subject to such notification requirements.
144. The characteristics that financial instruments must possess in order to qualify as entitlements to acquire shares were already set in the TD and the Commission Directive before the revision of the TD. The revised TD introduced a different concept; that of financial instruments considered economically equivalent to a share or an entitlement to acquire a share. Therefore, there is a need to further substantiate the characteristics that such financial instruments need to have in order to qualify as TD Article 13(1)(b) financial instruments. Methodologically, ESMA has taken the approach of following the definitions provided for in the TD and further developing the characteristics of the financial instruments, also with recourse to NCAs' past supervisory experience.
145. This said, the arguments presented by respondents who disagree with ESMA mainly address the co-legislators' decision at Level 1 to subject cash-settled financial instruments to the same notification rules which govern shares and entitlements to acquire shares. ESMA clarifies that it is not within its empowerment to follow the suggestion that cash-settled financial instruments should be left off the list because they are not normally used for stake-building, as following this suggestion would completely undermine the TD's objective of subjecting this type of financial instruments to disclosure. Moreover, supervisory experience has shown that although the normal function of these instruments is more closely linked to financing and hedging, there have been certain occasions on which such instruments have been used to acquire a stake in a company. Although such cases account for a small minority in the wide spectrum of notifications, they constitute the main driver of the revised regulatory treatment under the TD.
146. Notwithstanding, it is clear that for the purposes of notification the TD equates economic exposure to the actual or potential exercise of influence on an issuer. Therefore, ESMA considers that the way forward resides in establishing a general concept capable of achieving the objective of meaningful disclosures.
147. Concerning the second part of the question, ESMA will address the comments made by respondents in respect of each of the financial instruments included in the list.

Financial instruments relating to already issued shares

148. ESMA agrees with the respondent who observes that TD Article 13(1)(a) restricts notification requirements to financial instruments that give the holder the right to acquire or the discretion as to his right to acquire shares to which voting rights are attached, already issued. It is stated in TD Article 13(1)(b) that financial instruments with similar economic effect have to be referenced to shares referred to in point (a). Accordingly, all disclosure of financial instruments under TD Article 13(1) should be limited to financial instruments relating to already issued shares.
149. On this basis and for the avoidance of doubt, ESMA clarifies that only financial instruments relating to already issued shares have to be disclosed.

Convertible bonds

150. One respondent considered that monitoring whether convertible or exchangeable bonds refer to already issued shares is difficult to do as terms and conditions are not always publicly or readily available to the investor. This respondent therefore proposed excluding or including entirely this type of instrument from/in the list.
151. ESMA considers that this argument is not easily followed as a public offer of a financial instrument will in most cases be preceded by a prospectus. Even when this is not the case, namely in private offers, investors should be informed of the terms and conditions of the financial instrument being offered. For that reason, and the reason stated in paragraph 148, ESMA reiterates that only convertible bonds relating to already issued shares should be disclosed.

Right of recall shares

152. Respondents' uncertainty regarding regulatory practices in this area supports the inclusion of the right of recall shares in the list of financial instruments subject to notification requirements in order to clarify to investors that irrespective of regulatory practice, the right to recall shares is subject to disclosure. ESMA is of the opinion that TD Article 9 covers in any case the transfer of shares whereas the situations of temporary transfer of voting rights according to Article 10(b) will constitute a minority of cases since company law in most Member States prohibits voting rights from being transferred without the shares to which the voting rights are attached. However, where voting rights have been transferred along with the shares, the transferee would have to notify having an entitlement to acquire a share to which voting rights are attached under TD Article 13(1)(a) .
153. Another comment addressing repurchase agreements only was made by a respondent who was concerned that all repurchase agreements would have to be disclosed irrespective of their underlying. ESMA agrees with the respondent that the aim of the TD is to achieve disclosure of repurchase agreements having shares with voting rights attached as an underlying. For this reason, ESMA will amend paragraph 3 of Annex VI clarifying that only repurchase agreements having shares with voting rights attached as an underlying are subject to notification requirements.

Other conditional contracts or agreements than options and futures

154. Respondents were of the opinion that these financial instruments should be outside the scope of the disclosure obligation as they are not adequate to build a position in an issuer or to exercise influence on the issuer.
155. ESMA notes that this argument would be entirely correct if related only to entitlements to acquire shares as TD Article 13(1)(a) requires the holder to have the unconditional right to acquire or the discretion as to his right to acquire shares.

156. However, TD Article 13(1)(b) does not require the optionality to be controlled by the holder of the financial instrument. Here, the notification requirement is rather triggered by the fact that the financial instrument gives the holder an economic exposure similar to that one has when holding a share or an entitlement to acquire a share. ESMA observes that one Member State experienced a case in which an investor entered into several put options with a bank which enabled the bank to build up a significant stake in an issuer without bearing any economic risk; the investor later offered the bank to purchase the stake paying a surcharge, thus acquiring the stake in one step.
157. In conclusion, it is possible to acquire a stake in an issuer through a financial instrument where the optionality depends on external factors, because – as one respondent confirms – the holder of the financial instrument may be in a more advantageous position compared to other market participants to gain access to the shares, either directly from the counterparty or indirectly, for example in the market following sale by the counterparty.

Shareholders' agreements

158. ESMA understands and shares respondents' view that the definition of shareholders' agreements subject to notification requirements should be as clear as possible. Shareholders' agreements may cover different subjects, not all of them related with a potential exercise of influence on an issuer.
159. For the purpose of clarification, ESMA notes that not all shareholders' agreements have to be disclosed but only the ones which have a TD Article 13(1)(a) or (b) financial instrument as an underlying.

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

160. Nine market participants commented on this question of which none suggested other financial instruments to be included in the list. Instead respondents expressed concerns regarding the procedures for updating the list (regular revision and formal updating every two years), the desirability of having a “white list” identifying financial instruments that should be left outside the disclosure obligation (e.g. any securities held as collateral as long as the default event has not occurred) and the need to justify and document clearly the reasons for including or excluding a financial instrument in/from the list.

ESMA's response

161. ESMA takes note of the fact that for the time being the market does not feel the necessity of extending the proposed list of financial instruments.
162. Regarding the content of the list and the desirability of providing a “white list”, ESMA will continue promoting supervisory convergence using the regulatory tools available to it and thus providing further clarity for investors. The format such clarifications will assume will be determined if and when needed.
163. The TD is silent when it comes to the process for updating the list, and ESMA considers it essential to have some flexibility as to the timing and procedures. In terms of procedure, ESMA is of the opinion that the list has to be public in order to effectively provide guidance. In what refers to timing, ESMA prefers maintaining the flexibility provided for in the Level 1 text, thus being able to engage in a fruitful dialogue with all its stakeholders and providing an update when necessary.

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.



ANNEX II – LEGISLATIVE MANDATE TO DEVELOP DRAFT RTS

Mandate for ESMA to develop draft RTS in general

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.

Mandate for ESMA to develop draft RTS within the Transparency Directive

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

I. Introduction

1. The revised TD was published on 6 November 2013 and empowers ESMA with the task of preparing certain draft RTS regarding major shareholdings. According to Article 10(1), third subparagraph of the ESMA Regulation, ESMA 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.
2. ESMA is also empowered under TD Article 13(1b) to establish and periodically update an indicative list of financial instruments that are subject to notification requirements according to TD Article 13(1). This task stems directly from the TD which does not mention a precise legal instrument through which ESMA must fulfil the task. While a cost-benefit analysis (“CBA”) is not mandatory in this case, ESMA has nonetheless sought the views of stakeholders and carried out such an analysis.
3. Compared to the CBA published with the Consultation Paper, the present version of the CBA is updated in light of responses received to the public consultation.
4. Before finalising the CBA, ESMA consulted with the market and with established working groups within the parameters of the ESMA Regulation in the following ways:
 - Public consultation by publishing a Consultation Paper (ref. ESMA/2014/300) on 21 March 2014 with a consultation period open until 30 May. ESMA received 24 responses from market participants representing credit institutions, investment firms, institutional investors, asset managers, issuers and a stock exchange;
 - Request for an opinion from the Securities and Markets Stakeholder Group (SMSG) which provided its advice on 26 May;
 - Consultation with the Consultative Working Group of the Corporate Finance Standing Committee (“CFSC”) which provided a written response as well as oral feedback at the meeting of the CFSC on 26 February 2014; and
 - Questionnaire sent to 14 banks and insurance companies whose group structure was considered by ESMA as particularly complex and/or which might have had a specific experience in relation to the client-serving exemption. The questionnaire dealt with specific questions regarding TD Article 9(6)(b) and 13(4) and focused on the expected costs and benefits of the proposed draft RTS.

II. Nature of CBA

5. The CBA is mostly qualitative in nature. In order to support ESMA’s choices with precise cost assessments, ESMA endeavoured to obtain quantitative information from market participants responding to the public consultation. This information is not easily available through NCAs, nor is there any readily accessible public dataset that might allow for a systematic analysis of the effects of ESMA intervention. The information gathered through the consultation was, however, almost exclusively qualitative. Many respondents decided not to respond to questions specifically aimed at collecting quantitative evidence. In the very few cases in which quantitative evidence was provided, this was of a very generic nature setting out mostly anecdotal information.
6. In addition to analysing the responses received to the public consultation, the CBA also discloses the four responses ESMA received to the more specific questionnaire it sent to 14 major financial

groups. The additional information collected by ESMA broadly confirms the evaluation of costs and benefits performed on the basis of answers to the public consultation.

III. Contents

7. The CBA is structured as follows:

- Section IV explains the background to the Commission proposals and ESMA intervention;
- Section V sets out ESMA's proposals on the calculation method of the 5 % threshold (horizontal and vertical aggregation);
- Section VI deals with the calculation method of voting rights in case of financial instruments referenced to a basket or an index;
- Section VII addresses the methods for determining the delta for calculation of voting rights relating to financial instruments which are exclusively cash-settled;
- Section VIII covers the client-serving transactions; and
- Section IX covers the list of financial instruments subject to notification requirements.

IV. Problem identification and rationale for the regulatory intervention

8. In order to ensure adequate transparency of major equity holders, the TD imposes a disclosure duty on shares and entitlements to acquire shares above certain thresholds. However, as mentioned in recital 9 of the revised TD, “financial innovation has led to the creation of new types of financial instruments that give investors economic exposure to companies (...). These instruments could be used to secretly acquire stocks in companies which could result in market abuse and give a false and misleading picture of economic ownership of publicly listed companies”. Academic studies and the press have analysed several cases of hidden ownership and undisclosed stake-building that have been facilitated by financial innovation and – in particular – by the easy “decoupling” between economic interest and voting rights.
9. The revision of Article 13(1) of the TD expands the scope of disclosure requirements for major holdings by covering all instruments “with similar economic effect to holding shares and entitlements to acquire shares”. The revised TD thus explicitly addresses the case of cash-settled equity derivatives, the omission of which can be characterised as a main regulatory failure of the previous regime.

V. Article 9(6b) RTS on the method of calculation of the 5 % threshold

V.i Aggregation of financial instruments (horizontal aggregation)

10. The objective of this RTS is to ensure meaningful notification of holdings across different classes of financial instruments. In principle, there could be different technical approaches to fulfilling the empowerment given to ESMA. Either all financial instruments could be aggregated in one bucket for notification purposes. Alternatively, different types of financial instruments (holdings of shares, entitlements to acquire shares and financial instruments with economic effect similar to the first two) could be separated into different buckets, each bucket requiring a notification when the threshold is crossed.
11. ESMA considers the first option to be the only one which is legally consistent with the TD revision's primary goal: to enhance transparency regarding major shareholdings. Firstly, the aggregation of all TD Article 9, 10 and 13 holdings preserves the principle that all financial instruments

which are considered to be economically equivalent to shares should be treated like shares with respect to notification requirements. Secondly, the aggregation of all financial instruments comprising TD Article 9, 10 and 13 holdings is the only approach capable of preserving the thresholds for the trading book and market making exemptions. Disaggregating different types of holdings 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 TD 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 TD Article 9(1) to holdings not covered by any exemption.

Option 1	Aggregate shares and all financial instruments (TD 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.	
	<i>Qualitative description</i>	<i>Quantitative description</i>
<i>Benefits</i>	<p>This option provides the highest degree of clarity to the market regarding major shareholdings (see explanation above).</p> <p>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 combined holding of TD Article 9 and 10 shares and TD Article 13 financial instruments reaches or crosses the thresholds mentioned in TD Article 9(5) and (6).</p> <p>One respondent to the consultation pointed out on-going benefits associated with the trading book exemption, given that control mechanisms similar to the ones applying to the market maker do not apply.</p>	
<i>Costs to regulators (NCAs)</i>	<p>The proposal sets out one way of specifying the 5 % threshold for the purpose of the trading book exemption and the 10 % threshold for the purpose of the market making 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. This is due to the fact that the amount of notifications will increase as the 5 % threshold will encompass all holdings whereas until now TD Article 9 and 10 holdings were disclosed in one basket and TD Article 13(1)(a) financial instru-</p>	<p>By way of example, the UK has a similar notification regime which entered into force on 1 June 2009 following which notifications have increased by around 10 %, even with the trading book and market making exemptions in place. Before the regime was introduced, the UK foresaw an increase in regulatory costs of around £25,000-50,000 per year⁴.</p> <p>In Germany the trading book exemption currently applies only to shares and physically settled instruments, i.e., cash-settled instruments have to be consid-</p>

⁴ FSA CP 07/20 on Disclosure of Contracts for Difference, p. 9.

	<p>ments in another in some Member States.</p>	<p>ered 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.</p>
<p><i>Compliance costs</i></p>	<p>Issuers will suffer small incremental costs due to 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.</p> <p>For credit institutions and investment firms the exemption represents an increase in costs compared to the baseline scenario of the current exemption. The 5 % threshold will cover TD Article 9, 10 and 13 holdings which will result in a higher number of notifications being made. However, it is to be noted that the revised TD has made it mandatory for Member States to offer the trading book exemption. Notification costs will decrease in Member States which did not provide for the trading book exemption prior to the revised TD.</p> <p>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 TD Article 9, 10 and 13 holdings. However, 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 TD Article 3(1), second subparagraph) and as a consequence the impact of the change will be relatively small at European level⁵. In Member States that have not adopted the market maker exemption, a market maker will experience a decrease in costs if the exemption is adopted following the entry into force of the RTS.</p> <p>The responses to the consultation were</p>	<p>The UK estimated the cost of a notification to range from £12,50 to £50⁶.</p> <p>One respondent to the consultation added that the cost of a notification should include the fees that need to be paid to the NCAs (up to 750 €).</p>

⁵ Mapping of the Transparency Directive – Options, Discretions and “Gold-plating”, ESMA 07 July 2011/194.

⁶ FSA CP 07/20 on Disclosure of Contracts for Difference, Annex I, p. 4.

	<p>mixed. On the one hand, one respondent answered that one-off costs are negligible. On the other hand, another respondent stated that the one-off adaptation costs are likely to be relevant for its members while on-going costs (especially in terms of HR) are expected to be low. However, a rationale for this judgement was not provided.</p> <p>One respondent estimated that the on-going costs of calculating the market making exemption are high due to the additional administrative work required to identify the financial instruments and notify the relevant NCA according to Article 6 of the Commission Directive. As regards the trading book, one-off costs were estimated as negligible.</p>	
--	---	--

V.ii Aggregation of holdings at group level (vertical aggregation)

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

Policy objective	The 5 % exemption for voting rights held on the trading book or by a market maker should be applied on the same terms in all Member States. Without an RTS setting out how the 5 % should be calculated, it is likely that the lack of certainty regarding the way 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 TD Articles 12(4) and (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 TD Article 12(4) and (5).
Preferred option	Option 1: 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.

Option 1	Aggregation of holdings at group level and disaggregation when exemptions set out in TD Articles 12(4) and 12(5) apply.	
	<i>Qualitative description</i>	<i>Quantitative description</i>
<i>Benefits</i>	To ensure an accurate picture of voting rights held within a group, holdings should be aggregated at a group level.	

	<p>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 TD 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 TD Article 12(4) and (5) apply, i.e., whenever the group contains a management firm and/or an investment firm which meet the conditions of independence set out in those provisions.</p>	
<p><i>Costs to regulators (NCAs)</i></p>	<p>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 from aggregation laid down in TD Article 12(4) and (5).</p>	
<p><i>Compliance costs</i></p>	<p>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. This has been broadly confirmed by the responses to the consultation.</p> <p>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.</p> <p>Two respondents to the consultation confirmed this view indicating that one-off costs are negligible.</p> <p>The responses to the questionnaire indicated that in a few particularly complex international financial groups, adapting systems (especially IT) to the new rules might imply some one-off cost.</p>	<p>The quantitative responses to ESMA's questionnaire confirmed the qualitative assessment:</p> <ul style="list-style-type: none"> - Two respondents pointed out that under the current regime they do not make use of the trading book and market making exemptions, while two respondents indicated an interval ranging from 20 to 100 notifications per year. - Three respondents indicated that – regardless whether trading book and market making exemptions are applied at company or group level – they would not have to perform additional notifications. One respondent envisaged one additional notification with aggregation at company level and three additional notifications if the trading book and market making exemptions are applied at group level. <p>Respondents to the questionnaire seem to have already incurred relevant costs in the past when establishing systems to monitor whether they were crossing major holdings thresholds in different Member States. Such respondents envisage minor costs from adapting to the new rules and aggregating holdings at group level. In particular, respondents</p>

		<p>to the questionnaire (all large and complex international groups) indicated that:</p> <ul style="list-style-type: none"> - The costs incurred in the past from establishing systems designed to monitor major holdings ranged from 0.3 m€ to 8.1 m€ in terms of one-off costs and from 0 to 6.4 m€ p.a. in on-going costs. - Expected one-off costs to adapt systems to the new rules ranged between 0 and 3.9 m€ and expected on-going costs from 0 to 0.6 m€ p.a.
--	--	--

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 TD Article 12(4) and (5).	
	<i>Qualitative description</i>	<i>Quantitative description</i>
<i>Benefits</i>	<p>This approach has a wider subjective scope than Option 1. Option 1 relies on a more literal approach according to which TD 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 making 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.</p> <p>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.</p>	
<i>Costs to regulators (NCAs)</i>	<p>There is a potential risk that a relevant stake in an issuer held by one single group remains undisclosed to the detriment of the market.</p> <p>NCAs may incur 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</p>	

	in TD Article 12(4) and (5).	
<i>Compliance costs</i>	<p>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 or to a non-increase in compliance costs arising from notifications.</p> <p>Some respondents to the consultation mentioned that there might be on-going costs associated with the conditions of independence to be complied with by the subsidiaries so that the parent company may benefit from the aggregation exemption (namely, the declaration to the NCA of the home Member State of issuers whose voting rights are attached to holdings of the investment firm, credit institution or market maker).</p>	

VI. 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

13. 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 other hand, 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 aggregated with other holdings 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.	
	<i>Qualitative description</i>	<i>Quantitative description</i>
<i>Benefits</i>	<p>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 baskets/indices could be used to build significant positions in the underlying securities without disclosing them.</p> <p>As mentioned above, the thresholds need to be set at a level where well diversified baskets and indices are normally not required to be aggregated with other holdings in the same issuer.</p> <p>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 certain level of consensus exists among investors regarding these thresholds. Accordingly, a continued application of these thresholds will reduce implementation costs for firms.</p> <p>The 1 % threshold has been set to capture holdings in a single issuer with a certain weight. The threshold has been set at a relatively high level to offer a degree of flexibility.</p> <p>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.</p>	
<i>Costs to regulators (NCAs)</i>	<p>NCAs would incur staff costs in order to supervise the new notifications arising from the thresholds. However, these costs 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.</p>	

<p><i>Compliance costs</i></p>	<p>It emerges from the consultation that there are two elements to compliance costs regarding this RTS.</p> <p>Firstly, notification costs which are likely to be very small due to the small number of notifications.</p> <p>Secondly, on-going monitoring costs. Several respondents to the consultation indicated that monitoring activity (namely, systems and staff) will be the main driver of compliance costs and may be particularly high when a look-through approach is applied. Several respondents indicated that asset managers may need to buy additional data on index composition and constituents in case this information is not already available to them.</p> <p>In relation to this second argument, ESMA considers that the costs mentioned by respondents are not caused by the draft RTS but by the Level 1 obligation to monitor whether holdings in an issuer through shares, voting rights and financial instruments economically equivalent to shares reach, exceed or fall below certain thresholds. An additional mitigating factor regarding the size of compliance costs is that the proposed thresholds are in line with legislation already in place in the EU.</p>	<p>Italy introduced 1 % and 20 % thresholds for both baskets and indices in September 2011, while Austria established a 20 % threshold for baskets and indices on 1 January 2013. To date the NCAs have not received any notifications regarding these thresholds.</p>
--------------------------------	--	--

VII. Article 13(1a)(b) RTS on methods for determining the delta

14. 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.
15. Information about the total voting rights accessible to the investor should be as accurate as possible to achieve transparency. If the methods for determining delta were to remain unspecified, this could cause the calculation of voting rights regarding cash-settled financial instruments to be less accurate and comparable.

<p>Policy objective</p>	<p>The calculation of voting rights for cash-settled financial instruments should be comparable and accurate.</p>
<p>Option 1</p>	<p>Principle-based approach</p>
<p>Option 2</p>	<p>Prescription of formula to determine delta</p>
<p>Preferred option</p>	<p>Option 1 – Principle-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</p>

	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	Principle-based approach	
	<i>Qualitative description</i>	<i>Quantitative description</i>
<i>Benefits</i>	A principle-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 principle-based approach would also lead to minimal compliance costs.	
<i>Costs to regulators (NCAs)</i>	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.	
<i>Compliance costs</i>	<p>CRD IV entities and management firms already have sophisticated models in place to calculate delta. For this reason a system under which such entities would be permitted to continue using their own models – provided they are compatible with the TD – would entail no further costs.</p> <p>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 duties. However, the decision of adding this cost for this type of investors was already taken at Level 1.</p>	

Option 2	Prescription of a formula	
	<i>Qualitative description</i>	<i>Quantitative description</i>
<i>Benefits</i>	<p>For instruments covered in the RTS, prescribed formulas lead to accurate and comparable approaches across Member States.</p> <p>However, Option 2 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. The latter would be difficult to achieve with a RTS. Both factors mean that the RTS</p>	

	would risk being incomplete which could lead to legal uncertainty.	
<i>Costs to regulators (NCAs)</i>	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 than costs for Option 1.	
<i>Compliance costs</i>	<p>Compliance costs are likely to be significant.</p> <p>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 on-going basis.</p> <p>Entities subject to CRD IV/the Capital Requirements Regulation will also have to comply with the regulatory approach for delta calculation. This will add complexity, potentially leading to some additional compliance costs.</p>	

VIII. RTS for the client-serving exemption

16. 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 mentioned in TD Article 13(4), first subparagraph.
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 exemption 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 achieve the policy objective in line with the mandate.
------------------	---

Option 1	Literal interpretation of the mandate – client-serving exemptions are located within existing exemptions.	
	<i>Qualitative description</i>	<i>Quantitative description</i>
<i>Benefits</i>	<p>Applying this option prevents double notifications of positions to the extent that entities can make use of the existing exemptions provided for in TD Article 9(4) for custodians and in TD Article 12(3) for the parent undertaking.</p> <p>Regarding the trading book exemption provided for in TD 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.</p>	
<i>Compliance costs</i>	<p>The exemption from disclosure of TD 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.</p> <p>There may also be one-off and on-going costs to adapt systems in order to make use of the trading book exemption for cash-settled financial instruments as well as for shares.</p> <p>One respondent to the consultation confirmed that costs are likely to be very small.</p>	

Option 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 TD Article 9.	
	<i>Qualitative description</i>	<i>Quantitative description</i>
<i>Benefits</i>	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	

	<p>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.</p> <p>One respondent to ESMA's questionnaire indicated that its group does not assume long positions acting as counterparty to a client while another respondent explained that it hedges its positions where there is a necessity to do so, and this decision might depend on business, product offering and prevalent market conditions. Another respondent to the questionnaire added that long client-serving positions are usually hedged, given a certain risk tolerance.</p>	
<i>Costs to regulators (NCAs)</i>	<p>NCAs might incur one-off and on-going supervision costs (staff costs) as they will need to ensure compliance with a new exemption.</p>	
<i>Compliance costs</i>	<p>The exemption of disclosure of TD Article 13 cash-settled financial instruments reduces costs for client-serving entities which will not have to do notifications.</p>	<p>One respondent to the questionnaire indicated that one-off costs connected to the introduction of a notification obligation for cash-settled financial instruments with a specific exemption for client-serving transactions are around 90.000€ while on-going costs are estimated to be around 2.500€ p.a. One respondent added that it incurred minimal costs. Two respondents indicated that they have not used this exemption yet in those countries where it is applicable.</p> <p>Two respondents to the questionnaire envisaged additional costs and minimal one-off costs, respectively, in case the exemption does not also cover non-EU entities within the group. The cost driver would be the adaptation of systems due to the increased number of disclosures: three respondents indicated a range from 6 to 400 third country entities existing in their group structure.</p>

IX. List of financial instruments

17. In the Commission's Impact Assessment⁷ 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.
18. TD Article 13(1b) sets out 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 shares.
19. 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 including, in the future and when financial innovation justifies it, new financial instruments in the list.

	<i>Qualitative description</i>	<i>Quantitative description</i>
<i>Benefits</i>	<p>The decision concerning the specific instruments to include in the list does not in itself create benefits or costs. Whether a given instrument fulfils the conditions of TD Article 13(1a) and 13(1b) is a technical consideration.</p> <p>Disclosing a list of financial instruments will provide more legal certainty to the market.</p>	
<i>Costs to regulators (NCAs)</i>	<p>Establishing and updating the list will create non-material staff costs to NCAs.</p> <p>However, compared to a situation with no list, increased clarity regarding notification requirements resulting from the list will lead to a lower number of information requests to NCAs which should also be easier to handle.</p>	
<i>Compliance costs</i>	<p>The establishment of a list will bring more clarity to the market, thereby decreasing costs related to financial and legal advice.</p> <p>One respondent to the consultation indicated that the adaptation costs coming from an annual review might be relevant and suggested that a two-year review would be more cost efficient.</p>	

⁷ European Commission's Impact Assessment, SEC (2011) 1279 final/2, p. 70, 2.1.3.



ANNEX IV – SMSG OPINION

Advice to ESMA

Response to ESMA’s 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

I. Executive Summary

The objective of this paper is to provide advice to ESMA on the 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.

The SMSG very much welcomes ESMA’s balanced approach between strengthening disclosure of major shareholdings and avoidance of unnecessary costs for market participants.

The key messages the SMSG would like to highlight towards ESMA for consideration in its work going forward regarding finalizing regulatory technical standards and establishing an indicative list of financial instruments subject to disclosure are:

- ESMA’s proposals for dealing with the exemptions from disclosure obligations provided for trading book and market maker holdings is convincing. In particular, the SMSG strongly supports ESMA’s proposal introducing a rule on the aggregation of holdings in a group of companies. The SMSG also agrees with ESMA’s approach exempting a parent undertaking from notification requirements provided that its subsidiaries can be considered as independent. But it will be important that national competent authorities evaluate whether the principles of independence are fulfilled in a consistent way. The SMSG therefore urges ESMA to ensure a consistent application of the exemption in the future.
- The revised Transparency Directive will lead to more disclosure of financial instruments. The SMSG agrees with ESMA’s observation that there will be a risk of a high number of irrelevant notifications. This might explain ESMA’s mandate to specify certain cases in which exemptions laid down in the Transparency Directive apply to financial instruments held by a natural person or legal entity fulfilling orders received from clients. However, the level 1 text is ambiguous. The SMSG is of the opinion that the Transparency Directive does not mandate ESMA to establish a separate exemption for client serving transactions. The problem of potentially excessive and irrelevant disclosure of financial instruments has to be solved on level 1 by the Commission, European Parliament and Council.
- The revised Transparency Directive requires ESMA to establish an indicative list of financial instruments that are subject to notification requirements. Although the list will not be legally binding the SMSG believes that it will be a valuable support for investors in assessing whether financial instruments have to be disclosed or not. The SMSG observes that ESMA has examined in

depth whether financial instruments should be made public under the Transparency Directive. In addition, it would be beneficial for the market to learn if financial instruments are not subject to notification requirements. The SMSG understands that the Transparency Directive does not request ESMA to establish a white list. But it would be helpful if ESMA explained its considerations for including certain instruments in the list and on this occasion explains whether comparable instruments are not covered by the Transparency Directive.

II. Background

1. On 22 October 2013, the European Parliament and the Council adopted Directive 2013/50/EU amending Directive 2004/109/EC on the harmonization of transparency requirements (Transparency Directive – “TD”). One of the main aims of the revised TD is to ensure that issuers and investors have full knowledge of the structure of corporate ownership. Therefore, the revised TD provides a new definition of financial instruments which are subject to disclosure.
2. The revised TD mandates ESMA with the elaboration of draft regulatory technical standards (draft RTS) to specify the conditions for the application of existing exemptions from notification requirements for major holdings of voting rights. In particular, ESMA shall determine cases of exemptions while taking into account their possible misuses to circumvent disclosure obligations.
3. To collect input on some regulatory issues, ESMA organized an informal round table on 26 September 2013 with representatives of market participants, including issuers, investment management funds and associations, banks, other investment service providers and corporate finance advisors.
4. On 21 March 2014, ESMA published its 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” (“CP”). A few days later, ESMA asked the Securities Markets Stakeholder Group (“SMSG”) to respond to the CP.

III. Comments

5. The SMSG very much welcomes ESMA’s excellent CP. ESMA follows a balanced approach between strengthening disclosure of major shareholdings and avoidance of unnecessary costs for market participants. Furthermore, the SMSG recognizes that the CP explains the backgrounds of the proposed RTS in depth and can very well imagine that it will be a reference for future interpretation of the level 2-regime.
6. The SMSG responds to most of the topics ESMA’s CP is dealing with. Its comments focus on fundamental regulatory issues. Additionally, the SMSG addresses several technical points which should be considered by ESMA when submitting the draft RTS to the Commission for endorsement.

Trading Book and Market Maker Exemption

Question 1: 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?

7. According to the revised TD, the notification requirements laid down in the TD are not applicable to voting rights held in the trading book, provided that these rights do not exceed 5 % and are not exercised or otherwise used to intervene in the management of the issuer (cf. Article 9 (5) TD). A

further exemption exists for the acquisition or disposal of a major shareholding reaching or crossing the 5 % threshold by a market maker, provided that it is authorised by its home Member State and it neither intervenes in the management of the issuer concerned nor exerts any influence on the issuer to buy such shares or back the share price (cf. Art. 9 (6) TD).

8. There are some differences between the two exemptions. ESMA however is right to point out that this does not preclude following a common approach for specifying the method of calculation of the 5 % threshold referred to in the two exemptions, since both exemptions are supported by the same regulatory purpose. Firstly, the two exemptions take into account that the disclosure regime intends to clarify who might be interested in exercising influence over an issuer. Secondly, notification requirements can entail unnecessary burdens for a market maker and a credit institution holding voting rights solely with trading intent. Thus, the SMSG agrees that the trading book and the market maker holdings should be subject to the same regulatory treatment regarding Art. 9 (6) TD.

Question 3: 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.

9. The revised TD takes into account that financial innovation has led to the creation of new types of financial instruments which were used to secretly acquire shares in companies. Therefore, it firstly makes sure that instruments with a similar economic effect to holding shares and entitlements to acquire shares have to be disclosed to the market. Secondly, the revised TD requires the aggregation of the holding of shares with holdings of financial instruments. This approach is taken in order to ensure transparency and investor protection (cf. Recital 8 revised TD).

10. In view of the above the SMSG strongly supports ESMA's proposal of aggregating voting rights attached to shares (Article 9 and 10 TD) with voting rights relating to financial instruments (Article 13 TD) for the purposes of calculation of the threshold referred to in the exemptions for market makers and trading books. The SMSG is aware of the fact that ESMA's proposal might lead to more notifications by credit institutions and thus to greater costs for them. However, as stated by the CP, the proposed RTS are in line with the regulatory aim of the revised TD. In addition, not doing so might create a potential loophole as it seems strange that banks would build large derivative positions for the purpose of market making. As to the trading book, large derivative positions might make more sense, but there is an argument for simplification and therefore treating both exemptions in the same way. Finally, the suggested approach is already applied in some Member States who had extended the disclosure regime prior to the revision of the TD, such as Germany (cf. BaFin, Issuer Guideline, 2013, page 132 for the trading book exemption), although others such as France (cf. Art. L. 233-9-II, 3 Commercial Code) have not done so primarily in order to provide more flexibility and reduce costs for their banking sectors.

Question 5: 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))?

11. The TD did not initially provide any rules with regard to a group of companies in the context of the two exemptions. Thus, holdings of a market maker are currently not attributed to the parent undertaking for the purposes of calculation of the threshold provided for in Article 9 (5) and (6) TD. However, according to the revised TD, this will change in the future. ESMA shall draft RTS to specify the method of calculation of the 5 % threshold, including the case of a group of companies.

- 12.** The MSG strongly supports ESMA’s proposal introducing a rule on the aggregation of holdings in a group of companies. It takes into account that a parent undertaking has control over its subsidiaries and may influence its management. Again, ESMA’s proposal might lead to more notifications by credit institutions and thus to greater costs for them. But ESMA also suggests to exempt a parent undertaking from notification requirements if the subsidiary can be considered as independent (see para. 15-17 of this Advice). Thus, ESMA’s proposal principally tackles the problem of a possible increase in costs.
- 13.** Although ESMA’s approach is generally convincing, the MSG raises two technical questions which ESMA should deal with. The first one refers to the wording of Art. 3 (1) draft RTS. According to ESMA’s proposal, holdings shall be aggregated at “group level”. This term is defined in Directive 2013/34/EU as follows: “group’ means a parent undertaking and all its subsidiary undertakings.” Thus, Art. 3 (1) draft RTS could be interpreted in the way that holdings are not only attributed to the parent undertaking but also to subsidiaries in a multilevel group, which can surely not be ESMA’s intention. The MSG therefore requests ESMA to clarify that holdings are solely attributed to the parent undertaking.
- 14.** A second question is how cases are dealt with in which a parent undertaking is not considered a credit institution and therefore does not profit from the exemptions provided for market makers and trading books. For example, subsidiary A and subsidiary B in a multilevel group each hold a stake of 3 % in their trading books. ESMA does not deal with this situation in its CP but it is a practically relevant scenario which should be tackled in line with the level 1-regime. The MSG understands that A and B would be exempt from disclosure requirements according to Art 9 (6) TD. However, are A and B’s holdings attributed to the parent undertaking which is not a credit institution or an investment firm and therefore do not have a trading book? The MSG is of the opinion that Art. 9 (6) TD does not apply to such a parent undertaking and therefore Art. 3 draft RTS neither. The legal basis for the aggregation of A and B’s holdings to the parent undertaking can only be Article 10 (e) TD which should not be derogated by Art. 3 draft RTS. Thus, the holdings of each subsidiary would have to be aggregated to the parent undertaking, provided that the prerequisites laid down in Article 10 (e) TD are fulfilled.

Question 6: 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)?

- 15.** The MSG strongly supports ESMA’s approach exempting a parent undertaking from notification requirements provided that its subsidiaries can be considered as independent. The competence of ESMA to provide an exemption follows from the reference to Article 9 (6b) that TD is making (“taking into account Article 12 (4) and (5)”). The MSG understands that the proposed rule is limited to the two exemptions for market makers and trading books. Thus, it neither applies to the general rule on the attribution of voting rights in a group of companies (Article 10 (e) TD) nor should it be applied analogously.
- 16.** The MSG believes that the proposed independence test is convincing. Specifically, the MSG agrees 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 the credit institution or investment firm exercises voting rights unrelated to the shares held in connection with the trading book and market making activities independently. However, this criterion, also adopted in Article 3 (6) (b) draft RTS in the context of establishing compliance structures, should be put into more concrete terms.

17. In any case, it will be important that NCAs evaluate whether the principles of independence are fulfilled in a consistent way. The MSG therefore urges ESMA to ensure a consistent application of the exemption in the future.

Method of calculation the number of voting rights in case of financial instruments referenced to a basket of shares or an index

Question 9: 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?

18. ESMA's proposal reflects the regulation which is already in place in some Member States. It is identical with the law in the UK [DTR 5.3.3 FCA Handbook – Guidance] and similar to the one in Germany [§ 17 No. 2 WpAIV – rule]. Thus, market participants are already familiar with the prerequisites ESMA is suggesting. The MSG supports that ESMA adopts provisions already satisfactorily developed and applied in the Member States.

Question 10: Are there any other thresholds we should consider?

19. The MSG observes that UK law provides a further rule requiring transparency if the “use of the financial instrument is connected to the avoidance of notification.” It is hardly conceivable that an investor might secretly build an influential position by acquiring financial instruments referenced to a basket or index which are not subject to notification requirements. Furthermore, the rule in the UK is too vague and not specific enough. Thus, the MSG is of the opinion that such a provision or other thresholds should not be implemented by ESMA.

Method of determining delta for the purposes of calculation of voting rights relating to financial instruments which provide exclusively for a cash settlement

Question 13: 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.

20. The notification requirements of the TD also apply to a person who holds certain financial instruments, such as cash settled derivatives. The number of voting rights shall be calculated by reference to the full notional amount of shares underlying the financial instrument 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 by multiplying the notional amount of underlying shares by the delta of the instrument. ESMA shall develop draft RTS to specify the methods for determining delta for the purposes of calculating the voting rights relating to financial instruments which provide exclusively for a cash settlement.

21. The existing national laws do not provide any rules on this question. The reason for this is that most of the Member States require calculation of the number of voting rights on a fixed basis of 1. The UK, requiring the calculation on a delta-adjusted basis, does not regulate the details. The FCA Handbook only gives guidance to the market by stating that holders of long derivative financial instruments not having a linear, symmetric pay-off profile in line with the underlying shares should

monitor delta changes at the end of each trading day in order to determine whether a disclosure is required.

- 22.** Against this background, ESMA had to develop a regime which, on the one hand, does not represent an excessive administrative burden for market participants, and, on the other hand, ensures full transparency of economic ownership of publicly listed companies. The SMSG considers that ESMA has reached this goal.
- 23.** The SMSG acknowledges that a prescriptive approach demanding the calculation of voting rights according to one or more precise delta-adjusted methods is not preferable. It is not possible to require a specific formula which is appropriate for all potential financial instruments. ESMA is therefore right in following a principle based approach. On the one hand, ESMA's draft RTS are flexible since investors may apply general accepted standard pricing models. On the other hand, investors have to take into account that a pricing model has to consider certain elements that are relevant to the valuation of the financial instrument such as interest rate, dividend payments, time to maturity, volatility and price of the underlying share.
- 24.** Art. 5 draft RTS on determining delta is well designed. However, the SMSG raises one technical question which ESMA should deal with before submitting the draft RTS to the Commission for endorsement. According to Article 5 (6)2 draft RTS "the holder shall notify the issuer when he reaches, exceeds or falls below the thresholds provided for in Article 9(1)". The SMSG observes that with this rule ESMA intends to clarify that disclosure can be required due to changes of delta. However, the provision could be misunderstood. Article 5 (6)2 draft RTS could be interpreted as special law requiring a notification if an investor reaches, exceeds or falls below the thresholds "provided for in Article 9(1)", namely 5, 10 % etc. In fact, the disclosure obligation already follows from national law. Member States have transposed Art. 9 (1) and 13 (1a) TD, mostly by providing additional thresholds. This will be the legal basis for disclosure obligations. The SMSG recommends to remove Article 5 (6)2 draft RTS and to indicate in the recitals that a disclosure obligation might arise, depending on the national law.

Client-serving transactions

Question 15: 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.

- 25.** ESMA is requested to "develop draft RTS to specify the cases in which the exemptions [laid down 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 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". This mandate to ESMA can be explained by the extension of the duty to disclose financial instruments, such as cash settled equity swaps. In the above mentioned cases of client-serving transactions there is a risk of a high number of irrelevant notifications. In all types of transactions 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.
- 26.** ESMA is not sure how its mandate in the level 1-text is to be understood and presents two possible interpretations and thus different possible RTS. Option 1 interprets the mandate in a literal way. Thus, ESMA would have to decide whether the trading book, market maker and the other ex-

emptions apply to the three types of client-serving transactions. Option 2 is based on a teleological interpretation of the mandate. As a consequence, ESMA would have to decide whether and under which conditions the three types of client-serving transactions should be exempt from disclosure obligations.

27. The SMSG observes that Option 2 would be in line with the purpose of the TD and most appropriate to avoid meaningless notifications. However, adopting Option 2 would mean that ESMA would establish a further exemption from the notification requirements. The TD does not mandate ESMA in this regard. The SMSG is of the opinion that ESMA should restrict itself to the mandate given in the level 1-text. The problem has to be solved on level 1 by the Commission, European Parliament and Council.

Indicative list of financial instruments

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?

28. The TD differentiates between two categories of financial instruments subject to notification requirements: (i) instruments which give the holder the right to acquire shares or the discretion as to this right to acquire shares (Art. 13 (1) (a) TD); (ii) instruments which are referenced to shares with similar economic effect. Some instruments are listed in the level 1 text, such as transferable securities, options, futures, swaps, forward rate agreements, contracts for difference and any other contracts or agreements with similar economic effects which may be settled physically or in cash (Art. 13 (1) (b) TD). In addition, ESMA shall establish and periodically update an indicative list of financial instruments that are subject to notification requirements, taking into account technical developments on financial markets (cf. Article 13 (1b) TD).
29. ESMA’s indicative list will not be legally binding. It will rather be an instrument of soft law which gives guidance to the market. The SMSG believes that the list will be a valuable support for investors in assessing whether financial instruments have to be disclosed or not. NCA’s should either refer to ESMA’s list on their websites or adopt it into their guidance.
30. The SMSG observes that ESMA has examined in depth whether financial instruments should be made public under the TD. It welcomes ESMA’s efforts to provide a valuable guidance for market participants, not only by listing financial instruments subject to disclosure but also by explaining the reasons for doing so. This is especially important since there are different understandings in the Member States about the characteristics of equity-like financial instruments, such as warrants and stock options. Most of the explanations are clear and comprehensive. But ESMA could clarify that all of the conditions mentioned under para. 159 CP need to be fulfilled.
31. The SMSG recognizes ESMA’s strong commitment to ensure a high level of transparency. However, it is questionable whether any shareholders’ agreements having financial instruments as its subject, should itself be considered a financial instrument (cf. para. 199 CP). For example, it is hardly conceivable that pre-emption rights are used to secretly acquire shares in a company. The SMSG believes that the disclosure of such agreements is not necessary in order to ensure that issuers and investors have full knowledge of the structure of corporate ownership.

32. The SMSG is of the opinion that it would be beneficial for the market to learn if financial instruments *are not* subject to notification requirements. The SMSG understands that the TD does not request ESMA to establish a white list ensuring legal certainty for investors and issuers. But it would be helpful if ESMA explained its considerations for including certain instruments in the list and on this occasion explains whether comparable instruments are not covered by the TD. Market participants might draw valuable conclusions from the explanations. ESMA has already proceeded in this way in the CP, especially with regard to convertible and exchangeable bonds (cf. para. 182-184) and contractual buying pre-emption rights (which shall not fall under Article 13 (1)(a) TD, but should be considered as economically equivalent to holding shares, within the meaning of Article 13 (1) (b) TD). The SMSG encourages ESMA to use the same approach when establishing the indicative list.

Question 22: Do you think that any other financial instrument should be added to the list? Please provide the reasoning behind your position.

33. ESMA has dealt with all relevant financial instruments which might be subject to notification requirements. However, there may be further instruments falling under Art. 13 TD. This can only be evaluated by taking into account the special characteristics and features of national civil and company law. A possible example would be the pledging of shares.

ANNEX V – DRAFT REGULATORY TECHNICAL STANDARDS

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/EC¹, and in particular Article 9(6b), 13(1a)(a), 13(1a)(b) and 13(4) thereof,

Whereas:

- (1) Directive 2004/109/EC establishes transparency requirements relating to information about issuers whose securities are admitted to trading on a regulated market. Said Directive also requires development of regulatory technical standards to ensure consistent application of the regime for notification of major holdings and related exemptions.
- (2) The thresholds for the market making and trading book exemptions should be calculated by aggregating voting rights relating to shares with voting rights related to financial instruments (entitlements to acquire shares and financial instruments considered to be economically equivalent to shares) in order to ensure consistent application of the principle of aggregation of all holdings of financial instruments subject to notification requirements as well as to prevent a misleading picture of how many financial instruments related to an issuer are held by an entity benefiting of these exemptions.
- (3) To provide an adequate level of transparency in the case of a group of companies, the thresholds should be calculated at group level in order to take into account that where a parent undertaking has control over its subsidiaries it may influence their management. Therefore all holdings owned by a 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 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. As a result, financial instruments referenced to a basket of shares or an index should only be aggregated with other holdings in the same issuer when the holding of voting rights through such instruments is significant or the financial instrument is not being used primarily for investment diversification purposes.
- (5) It would not be cost-efficient for an investor to build a position in an issuer through holding a financial instrument referenced to different baskets or indices. Therefore, holdings of voting rights through a financial instrument referenced to a series of baskets of shares or indices

¹ OJ L 390, 31.12.2004, p. 38-57.

which are individually under the established thresholds should not be added between themselves.

- (6) Exclusively cash-settled financial instruments should be accounted for on a delta adjusted-basis, with cash position having delta 1 in the case of financial instruments having a linear, symmetric pay-off profile in line with the underlying share and using a generally accepted standard pricing model in the case of financial instruments which do not have a linear, symmetric pay-off profile in line with the underlying share.
- (7) In order to render information about the total number of voting rights accessible to the investor as accurate as possible, delta should be calculated daily taking into account the last closing price of the underlying share.
- (8) To decrease the number of meaningless notifications to the market, the trading book exemption should 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.
- (9) This Regulation is based on the draft regulatory technical standards submitted by the European Securities and Markets Authority (ESMA) to the Commission.
- (10) 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.
- (11) 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 Directive².

² OJ L 294, 6.11.2013, p. 27.



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), Article 13(1a)(a) and (b) 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 purpose of calculation of the 5 % threshold provided for in Article 9(5) and (6) of Directive 2004/109/EC, holdings under Article 9, 10 and 13 of said Directive shall be aggregated.

Article 3

Aggregation of holdings in the case of a group

For the purpose of calculation of the 5 % threshold provided for in Article 9(5) and (6) of Directive 2004/109/EC, holdings shall be aggregated at group level according to the principle laid down in Article 10(e) of said Directive.

CHAPTER III
METHOD FOR CALCULATING THE NUMBER 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) of Directive 2004/109/EC 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 voting rights in a specific issuer held through financial instruments referenced to the basket or index represent 1 % or more of voting rights attached to shares of that 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. When a financial instrument is referenced to a series of baskets of shares or indices, the voting rights held through the individual baskets of shares or indices shall not be accumulated for the purpose of the thresholds set out in paragraph 1.

CHAPTER IV

METHODS FOR DETERMINING DELTA FOR THE PURPOSES OF CALCULATING 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 a generally accepted standard pricing model.
3. A generally accepted standard pricing model is one that is generally used in the finance industry for that financial instrument and sufficiently robust to consider the elements that are relevant to the valuation of the instrument. Those elements that are relevant to the valuation include at least the following:
 - (a) interest rate;
 - (b) dividend payments;
 - (c) time to maturity;
 - (d) volatility; and
 - (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; and
 - (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) of Directive 2004/109/EC.



CHAPTER V

CLIENT-SERVING TRANSACTIONS (Article 13(4) of Directive 2004/109/EC)

Article 6

The exemption referred to in Article 9(6) of Directive 2004/109/EC 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.

CHAPTER VI

TRANSITIONAL AND FINAL PROVISIONS

Article 7

Entry into force and application

This delegated 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 delegated 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 VI – 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) of Directive 2004/109/EC 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) of said Directive:

- (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. “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) of Directive 2004/109/EC and reference shares to which voting rights are attached:

- (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(1) of Commission Delegated Regulation []³;
- (c) warrants;
- (d) repurchase agreements;
- (e) rights to recall lent shares;
- (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 Directive 2004/109/EC Article 13(1)(a) and (b) financial instruments as an underlying.

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

European Securities and Markets Authority (ESMA)

Paris, [DD.MM.2014]

³ Reference number pending adoption of draft RTS by the Commission.