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Response to European Commission's Public Consultation on Short Selling

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Introduction

EuropeanIssuers is in favour of European legislation on short selling to prevent the fragmented regulatory approach seen in recent markets and thus to help restore investor confidence in European markets.

We also believe, however, that an additional purpose of the legislation is that it should serve as a means to assist issuers to understand investors' views of their company's performance. If investor relations departments cannot see where their shares are being sold short, and do not know who is doing the selling, it is difficult for them to advise the board and company management on the market's views of their shares and thus to alert them reasonably early to any concerns which may need to be dealt with. This can in turn have an impact on market efficiency.

We agree with the Commission's proposal for emergency powers at EU and national level. In addition, we believe that it is essential that short selling is subject to an effective compliance and enforcement system at EU level. This means that regulators need to make it clear that they will use their existing enforcement powers to prevent market abuse and to co-ordinate more closely with each other.

While we welcome the opportunity to comment, we would, however, like to express our strong disapproval of the recent tendency for the Commission to publish consultations with very short deadlines. This makes it very difficult for associations such as ourselves to obtain views from our members. Where those members are also associations who then have to liaise with their own members, this is even more difficult. While we believe that there are cases where shorter deadlines are necessary, we are not convinced that this is the case in all recent instances.

We would point out that many of the most difficult legislative dossiers and those which have required the most amendment and revision over the past 10 years have been those on which consultation has been inadequate. It is also the case that it is the end users who are least likely to have the capacity to be able to respond to shorter deadlines.

We therefore call on the Commission to revert to its own commitment to best practice in all future consultations in order to ensure that genuine consultation with the widest possible range of European stakeholders is achieved.

A. Scope

EuropeanIssuers supports Option B of the Consultation Document[1] based on the two-tier model proposed by CESR, which would include not only short positions obtained by selling short the instrument itself but also positions obtained through the use of derivatives.

We would like to see the legislation cover all shares (and positions as above) admitted to trading on an EEA regulated market. For the purpose of having a truly efficient regime, short selling activity taking place in EEA listed companies' shares outside the EEA will require better co-ordination with other international authorities.

We have also considered the merits of legislation covering all financial instruments under Option A, but on balance we now consider that the legislation should focus on shares and related positions; thus, we exclude option A. Issuers' corporate treasury departments are concerned that if all financial instruments were covered without prior adequate impact assessment and consideration of all the potential implications for hedging corporate risks, their risk management activities could be seriously damaged.

Given the short consultation deadlines, we are concerned that the probability of rushed drafting and unintended consequences is likely to be too high. Further work is needed and in any event the situation could be kept under review in case of potential loopholes.

B. Transparency

Likewise we support Option B for disclosure of EU shares as above, to the regulator at a lower level and to the market at a higher level.

As above, we have concerns that Option A would lead to problems for companies in hedging risks. If Option A were to be chosen, we consider that further work on impact assessments and further consultation would need to be undertaken to consider how this might work in practice.

In terms of the levels of disclosure and to whom these should be made:

- Disclosure to the regulators is necessary in order to ensure that the regulators have a clear picture of what is happening across the market as a whole in order to enable them to enforce the rules on market abuse.

- We would also like to see disclosure to issuers of any interest in their shares, by which we include short selling. Some of our members would like to see this disclosure take place at the lower threshold, with the individual company having access to the same information as the regulator. Others would support disclosure to the market at a higher level, which would enable companies to see the larger short sales.

[1] European Commission's "*Public Consultation on Short Selling*" of June 2010

- We would also like to see an EU rule enabling companies to identify their shareholders. At the moment, companies' ability to do so varies considerably across the different EU jurisdictions. Without this ability, companies may need to seek additional information on investors' activities affecting them elsewhere.

- In calculating the threshold, it is important that the disclosure regime reflect the economic reality of the investment decisions taken. Issuers want to be able to understand who has an interest in their shares and who has the power to vote those shares. Thus within a fund management firm operating many UCITS funds, issuers would like to be able to understand which individual fund managers are long (and may have voting rights) and which are short (in order to understand why they have taken that position). If investor relations departments cannot see who owns their shares or where those shares are being sold short, and do not know who is doing the selling, it is difficult for them to advise the board and company management on the market's views of their shares and thus to alert them reasonably early to any concerns or lack of confidence in company management which may need to be dealt with. This can in turn have an impact on market efficiency, as failure to deal with these concerns across an entire sector may in some cases lead to disorderly markets. A provision clarifying that the notification is made by the position holder rather than the intermediary would also be helpful.

It is also important to focus on the economic reality of the investment decisions so as to avoid circumvention of and the possibility of creative compliance with the rules by inappropriate aggregation. Regulators must be prepared to enforce the rules against such attempts.

C. <u>Uncovered Short Sales</u>

Issuers wish to avoid the situation where the number of shares on the market exceeds the number actually in issuance.

We therefore support both the Commission's options to strengthen the buy-in procedures applying to shares and bonds and to require compulsory borrowing agreements for short-sales.

All participants should be obliged to settle their purchases in a timely manner. The current rules on delivery and settlement take too long in many markets, which makes the rules too easy to circumvent. We would like to see more effective and consistent enforcement of the rules on failed settlements and on market abuse and a harmonised definition of uncovered short selling as there may be the potential for confusion between different jurisdictions.

We would also like to see the Commission consider better disclosure of stock lending, including more consistent use of definitions. We note, for example, that information on stock lending is made available on a daily basis in Spain and we wonder whether it might not be more consistent with the principle of a single market if similar information could be made available across the EU.

D. Exemptions

We agree in principle with the exemptions. However, we are not sure whether there is a common understanding of market making across the EU and thus we are concerned that there may be the potential for confusion and thus for loopholes. Clarity as to what is intended to be covered will be necessary.

In terms of markets outside the EU, ESMA will need to co-ordinate closely with its international counterparts as it will not itself be able to enforce EU rules elsewhere. An internationally consistent approach whereby ESMA or the national regulators were able to approach other international regulators to request their co-operation in investigations would therefore be desirable.

E. Emergency Powers of Competent Authorities

We agree that regulators will probably need to maintain the power to impose a ban on short selling in disorderly markets. The 10% rule could be a useful alternative in aligning the EU with the US, but case by case consideration is likely to be a better option.

We agree that competent authorities should be required to notify each other of any actions taken and that ESMA should seek to ensure consistency across the EU without overruling decisions by the national regulators.

F. Powers of Competent Authorities

See comments in F above.

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***EuropeanIssuers** was set up to represent the interests of publicly traded companies in Europe, which are subject to complex market regulations. Our members include both national associations and companies from all sectors in 14 European countries, where there are some 9.200 such companies with a combined market value of some € 5.000 billion.*

EuropeanIssuers seeks to achieve well functioning European financial markets which serve the interests of their users, together with good corporate governance and responsible share ownership. More information can be found at www.europeanissuers.eu.

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