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VERBAND DEUTSCHER PFANDBRIEFBANKEN E.V. BERLIN

Mr Carlo Comporti
Committee of European
Securities Regulators (CESR)
11 – 13 Avenue de Friedland
75008 Paris
FRANCE

10785 Berlin, 30 September 2009
Schellingstraße 4
Tel.: + 49 (0) 30/20 21 – 1610
Fax: + 49 (0) 30/20 21 – 19 1600
Dr. La / sk

Response to the CESR Proposal for a Pan-European Short Selling Disclosure Regime

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AZ BVR: EG-INV-RE

Dear Mr Comporti,

We are grateful for the opportunity to comment on CESR Proposal for a Pan-European Short selling Disclosure Regime. Please find enclosed our comments to the consultation paper. Please feel free to contact Mr Diedrich Lange in case of any queries.

Yours sincerely,

on behalf of the Zentraler Kreditausschuss
Bundesverband der Deutschen
Volksbanken und Raiffeisenbanken e.V. BVR
National Association of German Cooperative Banks



Gerhard Hofmann



by proxy

Dr. Diedrich Lange

Enclosure

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Response to the **CESR Proposal for a Pan-European Short Selling Disclosure Regime**

September 2009

* The ZKA is the joint committee operated by the central associations of the German banking industry. These associations are the *Bundesverband der Deutschen Volksbanken und Raiffeisenbanken (BVR)*, for the cooperative banks, the *Bundesverband deutscher Banken (BdB)*, for the private commercial banks, the *Bundesverband Öffentlicher Banken Deutschlands (VÖB)*, for the public-sector banks, the *Deutscher Sparkassen- und Giroverband (DSGV)*, for the savings banks financial group, and the *Verband deutscher Pfandbriefbanken (VdP)*, for the mortgage banks. Collectively, they represent more than 2,200 banks.

General

We appreciate the opportunity to comment on CESR's Consultation Paper. We support CESR's endeavours aimed at achieving a European harmonisation of the short selling regimes in the various Member States. In view of its positive effect on liquidity, pricing and risk management, short selling is a vital factor for financial markets. Hence, a general ban on short selling would be absolutely unacceptable. However, we also feel that the present impact assessment is only to a limited extent capable of fully gauging the macroeconomic impact of the current, extremely far reaching proposal. In order to assess their potential implications, several aspects of the envisaged transparency regime require a closer analysis. Particularly the disclosure of short selling positions is likely to lead to a strong liquidity deterioration of the affected equity markets. This is due to the fact that many market participants are not going to be willing to run the risk that their short positions will be identifiable for the opposite market side in a form that is not anonymised. Such an obligation which is tantamount to a soft short selling ban is just as unacceptable as a general ban on short selling.

Please find our more detailed comments on the Consultation Paper's questions below:

Q1 Do you agree that enhanced transparency of short selling should be pursued?

Basically, the request for enhanced transparency of short selling is principally understandable. However, it remains doubtful whether it will indeed engender the expected positive impact. The differentiation between divulgence of confidential information to the competent authority and a short selling disclosure obligation *vis à vis* the market is, however, important in any case. We strictly oppose the latter obligation. If and when a transparency regime is to be introduced then this would at least have to be harmonised at the European level (preferably at a global level) lest this would lead to competitive distortion.

Q2 Do you agree with CESR's analysis of the pros and cons of flagging short sales versus short position reporting?

We share CESR's reservations over strong disadvantages inherent in the flagging regime.

Q3 Do you agree that, on balance, transparency is better achieved through a short position disclosure regime rather than through a 'flagging' requirement?

We agree that transparency is best achieved by position reporting. Preferably, disclosure should have to take place only on the basis of positions that are being held and not on the basis of orders that have been given or executed.

Q4 Do you have any comments on CESR's proposals as regards the scope of the disclosure regime?

The scope of the disclosure regime should be reviewed. If and when it refers to shares of EEA issuers admitted to trading on a regulated market or on an MTF or to shares of non-EEA issuers that are predominantly traded on such a platform then, *per se*, this is not a cause for concern. However, it becomes a cause for concern if and when the scope of the disclosure regime also includes open positions pertaining to derivatives (c.f. below).

Q5 Do you agree with the two tier disclosure model CESR is proposing? If you do not support this model, please explain why you do not and what alternative(s) you would suggest. For example, should regulators be required to make some form of anonymised public disclosure based on the information they receive as a result of the first trigger threshold (these disclosures would be in addition to public disclosures of individual short positions at the higher threshold)?

We object to a public disclosure of short selling positions by the position holder (the "short seller"). As a result of the divulgence of the non-anonymised open positions it might lead to a *de facto* ban on short selling as of a certain threshold with all the implications of reduced liquidity for markets. This is at odds with CESR's statement that, essentially, short selling plays an important role when it comes to enhancing the markets' efficiency and liquidity. The fact that in those States where such a disclosure obligation exists, short squeeze problems were not an issue seems curious. One potential explanation might be that there may have been hardly any instances of short selling either due to the disclosure obligation which, *de facto*, worked like a ban or due to the poor market situation. The proposed exemption for market-makers, too, indicates that CESR is indeed aware of the fact that short squeezes may become a problem. During normal market phases where short selling is more frequent, the risks of short selling disclosures could indeed materialise: Short squeeze problems, overreactions as well as "herding" behaviour. At this point, market participants may not only turn against the short seller, but they may also follow them thereby further exacerbating volatility. The effect would be exactly the opposite of what should be achieved: This would result in an exacerbation of the negative effects on the financial markets.

At most, there might be an anonymised disclosure in an aggregated form made by the competent authority but even this will allow conclusions to be drawn by market participants about individual positions what should be avoided in any case.

Q6 Do you agree that uniform pan-European disclosure thresholds should be set for both public and private disclosure? If not, what alternatives would you suggest and why?

In view of cross-border markets, we feel that there is a need for uniform European disclosure thresholds.

Q7 Do you agree with the thresholds for public and private disclosure proposed by CESR? If not, what alternatives would you suggest and why?

Cf. our answer under question number 5 on the issue of public disclosure. As far as private disclosure is concerned, we feel that the proposed thresholds are too low.

These thresholds could be reached fairly quickly particularly by smaller companies. Therefore, we first of all perceive a need for a field test. The proposed disclosure thresholds constitute a novel concept. Hence, they would first of all merit a statistical test. On this basis, it would then be possible to determine the frequency and distribution of short selling volumes which could then serve for an extrapolation of the respective thresholds. This helps to further disclosure efficiency. After all, an excessively low threshold will, more likely than not, only increase reporting errors. In addition to this, the lower the threshold value, the less informational benefit will be provided by the disclosure. Besides, the large number of reporting thresholds is in need of a further review.

Q8 Do you agree that more stringent public disclosure requirements should be applied in cases where companies are undertaking significant capital raisings through share issues?

Whilst we understand that a company's capacity to raise capital may be impaired by instances of short selling on the part of other market participants in the context of a rights issue, we still object to a public disclosure obligation for the short seller even during these constellations. This is due to the fact that - also during said phases - the latter can have an adverse impact on the company.

Q9 If so, do you agree that the trigger threshold for public disclosures in such circumstances should be 0.25%?

No, we do not.

Q10 Do you believe that there are other circumstances in which more stringent standards should apply and, if so, what standards and in what other circumstances?

No, we are not aware of any other circumstances which would warrant exceptions.

Q11 Do you have any comments on CESR's proposals concerning how short positions should be calculated? Should CESR consider any alternative method of calculation?

Both, the inclusion of derivative positions but also the calculation at the level of the legal entity would be extremely onerous for the reporting persons. The inclusion of derivative positions goes beyond what is to date commonly understood in Germany under the term short selling. Also during the calculation, such an inclusion of derivatives results extremely difficult. First and foremost, it is necessary to create systems which juxtapose short and long positions from cash and derivative positions in the respective shares across the entire credit institute. This is already an extremely onerous task. At present, it is not possible to assess the forthcoming costs associated with this. Furthermore, derivatives are compounded by specific complexities: For instance, there are derivative forms where different computational models lead to different results; furthermore, there are partly complex products which consist of a range of components where it is difficult to assess whether they constitute genuine short positions or whether they merely constitute short positions for accounting purposes. Also the calculation of the short positions at the level of the legal entity should be reviewed in favour of a more flexible solution where the reporting persons have the right to customise the disclosure system to meet their respective internal workflows.

At this juncture, we would like to emphasise once more that for the sake of a solution that is fit for purpose as far as supervisory authorities are concerned, it is of paramount importance that there be Europe-wide, uniform methods for the calculation and disclosure of short selling positions.

Q12 Do you have any comments on CESR's proposals for the mechanics of the private and public disclosure?

We would like to explicitly endorse CESR's proposal that the disclosure of the short selling positions be made by the short seller.

Q13 Do you consider that the content of the disclosures should include more details? If yes, please indicate what details (e.g. a breakdown between the physical and synthetic elements of a position).

No, it should not contain any further details. Furthermore, not only the methodology but also the requirements with regard to the form and content of the disclosure ought to be identical across the entire European Economic Area.

Q14 Do you have any comments on CESR's proposals concerning the timeframe for disclosures?

Regardless of the duration of the time period within which the disclosure has to be made, it needs to be safeguarded that the event triggering said deadline – i.e. t in $t+1$, is defined in a precise manner and that there is a common understanding thereof across the whole of Europe.

Q15 Do you agree, as a matter of principle, that market makers should be exempt from disclosure obligations in respect of their market making activities?

We share CESR's view that market makers should be exempt from public disclosure obligations. An exemption from the public disclosure obligation for market makers on the grounds of the liquidity provision for the market shows that also CESR has acknowledged that the envisaged public disclosure obligation might have potentially detrimental consequences for the market which are supposed to be mitigated by exempting particularly active market participants like market makers. Hence, the question arises whether the same should also apply to other market participants, i.e. whether market participants who equally make a considerable contribution to market liquidity should similarly be exempt from the public disclosure obligation. In practice, it will not be possible to draw a line to arrive at the requisite clear cut differentiation and level playing field in this regard. This means that it would be judicious to drop the public disclosure obligation altogether.

Q16 If so, should they be exempt from disclosure to the regulator?

No.

Q17 Should CESR consider any other exemptions?

Cf. our answer under question 15.

Q18 Do you agree that EEA securities regulators should be given explicit, stand-alone powers to require disclosure in respect of short selling? If so, do you agree that these powers should stem from European legislation, in the form of a new Directive or Regulation?

If EEA securities regulators were to be given the authority to impose a private disclosure obligation (let alone public disclosure obligation) upon short sellers then this would obviously require a uniform European legal mandate. However, it is also worth bearing in mind that exemptions for individual Member States incur the danger of an erosion of a uniform, harmonised regime.