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Short Selling (No. 5) Instrument 2009 - FAQs Version 1 - Issued 14 January 2009

Further to the changes to our emergency measures on short selling of stocks of UK financial sector companies announced in our Policy Statement published on 14 January 2009, we have set out some indicative answers to what we expect will be frequently asked questions.

As a result of the expiry of the short selling ban and the amendment to the disclosure obligation there are substantial changes made in these FAQs compared to those previously issued on this subject.

We will continue to review this information over time and may further update the FAQs to address any other frequently asked questions that arise. The FAQs are not intended to be exhaustive and persons will need to consider how the instrument applies to their particular circumstances taking into account that the purpose of the measures is to prevent potentially abusive behaviour.

1. At what time do the changes to the short selling provisions come into force?
The ban on short selling in UK financial services companies expires at 00:00:01 on Friday 16 January 2009. The amended provisions governing the short selling disclosure obligation take effect at the same time.
2. When will the amended disclosure obligation end?
It is set to expire on 30 June 2009.
3. Will the FSA extend these measures?
We will keep this under review in the light of market conditions.
4. What is the effect of the new measures?
They are evidential provisions describing behaviour that in the opinion of the FSA constitutes market abuse. Accordingly they have the effect described in MAR 1.1.
5. Have these measures changed the suspicious transaction reporting regime?
The reporting obligations under the suspicious transaction reporting regime remain unchanged, but these evidential provisions describe a behaviour that in the opinion of the FSA constitutes market abuse.
6. Which UK financial sector companies are subject to the disclosure obligation?
The scope of the Short Selling (NO 5) Instrument remains unchanged. We have published a list of UK financial sector companies on our website: http://www.fsa.gov.uk/pubs/other/Shortselling_list.pdf. The list has been prepared on a best endeavours basis.

Please note that at the time of writing, the Irish Financial Services Regulatory Authority (IFSRA) will continue to maintain a ban on short selling certain shares in Irish financial sector companies. Please see the IFSRA website for full details: <http://www.ifsra.ie/>
7. When does the short selling disclosure obligation arise?
A person must disclose any new net short position of 0.25% in a UK financial sector company. Once a disclosure has been made, additional disclosures are only required if the short position reaches , exceeds or falls below disclosure bands placed every 0.1% above the 0.25% threshold, i.e. at 0.35%, 0.45%, 0.55% etc. If a net short position decreases below 0.25% a disclosure will also need to be made.
8. By what time must the disclosure be made?

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A person must make the disclosure by 3:30pm the day after the obligation to disclose arises (see response to question 7).

9. Are there any exemptions to the disclosure obligation?

Market makers continue to be exempt from the disclosure obligation. The term ‘market maker’ is not linked to the definition in the FSA’s Handbook. Our indicative view for the purposes of this instrument on market making is as follows:

A market maker is an entity that, ordinarily as part of their business, deals as principal in equities, options or derivatives (whether OTC or exchange-traded):

- a) **to fulfil orders received from clients, in response to a client's request to trade or to hedge positions arising out of those dealings; and/or**
- b) **in a way that ordinarily has the effect of providing liquidity on a regular basis to the market on both bid and offer sides of the market in comparable size. Trading in circumstances other than genuinely for the provision of liquidity is not exempt.**

This exemption covers market makers only when, in the particular circumstances of each transaction, they are acting in that capacity. Market makers are afforded a certain level of flexibility in anticipating sales as long as this activity is genuine market making in line with its existing general levels of business. Consequently, we would not expect market makers to hold significant short positions, other than for brief periods. Proprietary trading strategies where the main intention is to create a short position are not market makers and are not exempt.

Registration as a “market maker” with an exchange or trading platform is not relevant for the purposes of this definition.

10. What will be the consequences of non-compliance with the new measures?

The potential consequences of non-compliance will be the same as for any other breach of the market abuse regime. We have a range of actions at our disposal. These include enforcement action, which could culminate in a fine or a public censure.

11. To whom does the disclosure responsibility apply (e.g. the UK financial sector company or the holder of the short position in that company)?

The disclosure obligation applies to the holder of the net short position. See also FAQ 12.

12. In the case of investment managers and authorised fund managers who act on behalf of clients, to whom does the disclosure obligation apply?

Non-discretionary

Where an investment manager manages on a non-discretionary basis the disclosure obligation applies to the client. The investment manager may make a net short position disclosure on behalf of its client, but this disclosure must clearly identify that it is the client who holds the disclosable position.

Discretionary

The disclosure obligation applies at the level of both the entity to which the prohibition applies and at the level of the investment manager or authorised fund manager. The investment manager or authorised fund manager may make a net short position disclosure on behalf of its client. In respect of itself, the investment manager or authorised fund

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manager is required to disclose its aggregate net short position across all of the funds it manages on a discretionary basis.

Where a disclosure by an investment manager or authorised fund manager is the same as that being made for its client/fund/sub-fund, it is permitted to make a single disclosure provided that the disclosure makes it clear that it applies to both parties.

13. How does the disclosure obligation apply across different trading desks?
If trading desks within a firm are housed within the same legal entity, the aggregate position of the legal entity (across all desks holding positions in UK financial sector companies) would be expected to apply for these purposes, excluding positions taken under the market maker exemption.
14. When calculating a net short position should financial instruments be accounted for on a notional basis or a delta adjusted basis?
Any financial instruments should be accounted for on a delta adjusted basis.
15. What does “economic exposure in the issued share capital of a company” mean?
It means any instrument (contracts for differences, spread bets, options etc) giving rise to an exposure, whether direct or indirect, to the issued share capital of a company.

The issued share capital of a company would include ordinary shares and preference shares but would exclude debt securities.
16. Should any holdings in a UK financial sector company that are held as part of a basket of shares or a share index be included in any aggregation of a person's economic interest in the company?
Any economic interest held as part of a basket, index or exchange traded fund (‘ETF’) where the basket, index or ETF has economic exposure to UK financial sector companies must be included when calculating the net short position in each relevant stock.
17. Has the FSA imposed any additional restrictions on stock lending activities?
No.
18. Does the disclosure obligation apply to UK financial sector companies on all UK markets?
This instrument applies to all “prescribed markets” under the Code of Market Conduct.
19. How will it apply to listings of UK companies traded on exchanges in other countries?
The UK’s market abuse regime covers not just the shares themselves but also related investments, i.e. something whose price or value depends on the price or value of the share. Common examples might include, CFDs, spread bets, options, futures, depository receipts and dual line stocks.
20. How is the relevant denominator calculated?
The relevant denominator for the calculation of net short positions is the entire issued share capital of the company comprising ordinary shares or preference shares.
21. In what format must the disclosure be made?
The disclosure must be made by means of a Regulatory Information Service (RIS) announcement. Persons making a disclosure may use the TR4 form on the FSA website or may choose a different format. However, all disclosures should include the information required by the TR4 form. The form, or the required information, should be disclosed using the RIS short code SSD.
22. What is the process for making an RIS disclosure?

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To make an RIS disclosure, it is first necessary to register with one or more of the RIS providers. Further information can be found at

<http://www.fsa.gov.uk/Pages/Doing/UKLA/ris/index.shtml>

23. Should the disclosure be made on a gross or net basis?
A holder of economic interests in a UK financial sector company may net its long and short positions in that company. The disclosable position will be any net short position of 0.25% or above.
24. When disclosing the net short position, will the holder of that position be required to include details of both short and long positions (if applicable) in order to provide a breakdown of the net economic interest?
No. Only the aggregate net short position of 0.25% or above will need to be disclosed. There is no requirement to disclose any individual short and long positions underlying the net position.
25. Does an aggregated net short position need to be broken down into its component parts for the purposes of the disclosure obligation (i.e. any positions in cash settled shares, CFDs, other derivative instruments etc)?
No. Only the aggregate net short position requires disclosure.
26. If a person's previously disclosed net short position falls below the 0.25% disclosure threshold, is a further disclosure of this fact required?
Yes. If a person's net short position falls below 0.25%, disclosure of that fact is required.
27. Where a person has a structure that includes more than one legal entity, at what level is a net short position disclosure required?
A disclosure should be made at the level of each legal entity. It is possible for one entity within the group to disclose on behalf of each individual entity that has a disclosable net short position, provided it clearly states which position belongs to which entity.
28. How do the provisions of Short Selling (No. 1) Instrument 2008 (relating to companies in rights issue periods) and the provisions of Short Selling (No. 5) Instrument 2009 (relating to UK financial sector companies) interact in circumstances where a UK financial sector company enters into a rights issue period?
If a UK financial sector company enters into a rights issue period, trading in relation to its securities is subject to provisions under both Short Selling Instruments No. 1 and No. 5. In such circumstances, the provisions of MAR 1.9.2A E and MAR 1.9.2D E will apply.
- When calculating a net short position in such circumstances, a person should only include economic interests in the pre-existing share capital of the company. Economic interests relating to share capital that will be issued in the future must be excluded from the calculation. A person cannot therefore net off a short position in the company's pre-existing share capital with a long position in the nil-paid rights. Similarly, nor can a prospective long position in the new shares arising from an underwriting/sub-underwriting commitment be netted off. This applies in respect of the provisions of MAR 1.9.2A E and MAR 1.9.2D E. The denominator for the calculation of a net short position should be the undiluted share capital.**

Further questions

43. What if I have another questions not covered by the FAQs or wish to make a comment about the new rules?
We may publish additional FAQs or clarify existing ones as further questions arise.

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For technical questions (only) in relation to the disclosure obligation (MAR 1.9.2D) please call on 020 7066 8333, option 4.

For all other queries or comments in relation to the new rules, please write in to:

Markets Division
Financial Services Authority,
25 The North Colonnade
Canary Wharf
United Kingdom
E14 5HS