

09 / 10

Financial Services Authority

Extension of the short selling disclosure obligation

Feedback to CP09/15

June 2009



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This Policy Statement reports on the main issues arising from Consultation Paper 09/15 (*Extension of the short selling disclosure obligation*). It publishes final text of changes to be made to the Code of Market Conduct.

Please address any comments or enquiries to:

Stephen Sie
Markets Division
Financial Services Authority
25 The North Colonnade
Canary Wharf
London E14 5HS

Telephone: 020 7066 3418
Fax: 020 7066 3419
E-mail: cp09_15@fsa.gov.uk

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1 Overview

Introduction

- 1.1 On 18 September 2008 we introduced short selling measures in relation to stocks in UK financial sector companies on an emergency basis (the Measures). We did this because of concerns about the potential for market abuse resulting from short selling and the consequent destabilising effects in the extreme conditions prevailing. The Measures effectively banned the active creation or increase of net short positions in the stocks of UK financial sector companies (the Ban) and required disclosure to the market of significant short positions in those stocks (the Disclosure Obligation). We introduced the Measures without consultation as we considered there was an urgent need to do so, but we gave them a limited life and they were set to expire on 16 January 2009.
- 1.2 Following a short consultation in January 2009 we allowed the Ban to expire but extended the Disclosure Obligation until 30 June 2009. In February 2009, we published a Discussion Paper (DP09/1)¹ setting out our analysis and conclusions following our comprehensive review of short selling.
- 1.3 On 1 June 2009 we published a Consultation Paper (CP09/15 *Extension of the short selling disclosure obligation*). This set out our proposal to extend the Disclosure Obligation in its current form without time limit. This is because we think that maintaining the Disclosure Obligation will help continue to minimise the potential for market abuse and disorderly markets in UK financial sector stocks. It will also help to enhance transparency in that sector. While we did not propose setting an expiry date for this obligation, we noted that we did not intend it to apply permanently in its current form.
- 1.4 The consultation closed on 12 June 2009 and in this Policy Statement (PS), we summarise and respond to comments received. There were 15 responses, including 6 from trade associations (or trade association coalitions) representing the views of their members. Most of the other responses came from authorised firms. We thank respondents for acting within the shorter than normal consultation period.

1 DP09/1 Short Selling www.fsa.gov.uk/Pages/Library/Policy/DP/2009/09_01.shtml

- 1.5 Chapter 2 provides feedback on the responses to our policy proposals and Chapter 3, provides feedback on the responses to our cost benefit analysis. Appendix 1 lists non-confidential respondents and Appendix 2 contains a copy of our Board instrument, including our final Handbook text.

Policy decision

- 1.6 For the reasons set out in CP09/15 and after taking into account all the comments received (including majority support for the extension), we will extend the Disclosure Obligation without time limit². These changes will become active at 00:00:01 hours on 30 June 2009.
- 1.7 We expect to issue a Feedback Statement summarising the responses received to DP09/1 in the third quarter of 2009 including feedback on alternative methods of increasing transparency. We will also continue to engage in the international dialogue on short selling.

2 Although we note that the power on which the regime is based is itself time limited (s118(8) FSMA).

2 Feedback on policy proposals

- 2.1 This chapter sets out our feedback to the responses received to our proposals set out in Chapter 3 of CP09/15. Generally, our proposals were well received.
- 2.2 We proposed extending the disclosure regime for significant net short positions in UK financial sector stocks. This is because we consider that the disclosure of significant short positions will lessen the potential for the misleading effects of short selling (market abuse, disorderly markets and sub-optimal transparency). We asked:

Q1: Should the Disclosure Obligation be extended?

- 2.3 Nine of the fifteen responders (including four trade associations) supported the extension, recognising the benefits of enhanced transparency. Four responders (one trade association and three authorised firms) opposed it, generally arguing that there was insufficient evidence to justify the extension and/or that measures should not be based on market abuse powers. However, of those objectors, two support the principal of enhanced transparency but advocate alternative regimes. One responder did not object to the proposed extension and another offered no opinion.

Our response: For the reasons set out in CP09/15 and in view of the majority support for our proposals we will extend the Disclosure Obligation.

We will issue additional feedback on views received in response to DP09/1 regarding alternative methods of increasing transparency in this space in the third quarter of 2009.

- 2.4 We also proposed extending the Disclosure Obligation *without time limit*. This is because it is not possible to forecast how long the need for the obligation will continue for and we are currently consulting on proposals for the longer-term regulation of short selling. We therefore considered that setting another defined period would be artificial. We asked:

Q2: Do you agree that the extension should be without time limit?

- 2.5 Seven responders (including three trade associations) supported extending the regime without time limit. Four responses (including two trade associations) opposed the indefinite extension. Two of these thought a one year extension or extension to the

end of 2009 and further review would be more appropriate if, for example, EU policy development did not progress as expected. Three responders expressed no opinion.

Our response: For the reasons set out in CP09/15, and on the basis of the majority support we will extend the disclosure obligation without time limit.

As noted previously, we do not intend this to be a permanent regime. Our expectation is that it would either be superseded in due course by broader permanent disclosure measures – preferably agreed on the widest possible international basis – and/or be revoked. We would of course stand ready to review the regime if there were major changes to EU/international approaches. Additionally, we note that the power on which the disclosure regime is based³ is itself time limited.

3 sll8(8) FSMA

3 Feedback on cost benefit analysis

3.1 This chapter sets out our feedback to the responses received to our cost benefit analysis set out in Chapter 4 of CP09/15. That analysis set out the costs and benefits of our proposal to extend the Disclosure Obligation without time limit. We asked:

Q3: What are your views on the costs and benefits of the proposed extension of the Disclosure Obligation? Where possible please quantify.

3.2 Five respondents (including four trade association responses) have little or no comment on this question. Another five (two trade associations and three authorised firms) think we have underestimated the costs; two of those arguing that we ought to take into account the cost of complying with short selling regimes that are also in existence in other countries. Four respondents were broadly in support of the cost benefit analysis, one reporting that benefits exceeded costs and another that ongoing compliance costs are not material given that compliance systems are already in place to comply with the temporary regime.

Our response: In CP09/1 we set out the full extent of the cost benefit analysis conducted at that time. We still consider these results to be valid. We have received further support from responses to CP09/15. We recognise that conducting CBA in this area is complex. We think it is appropriate to focus the CBA on the UK regime although we have taken into account the impact on the UK's international competitiveness. We will also continue to engage in the international dialogue on short selling.

Appendix 1

List of non-confidential respondents to Consultation Paper 09/15

Association of British Insurers

Alternative Investment Management Association

Association of Corporate Treasurers

British Bankers Association

The Consulting Consortium

Deutsche Bank

IG Markets Ltd and IG Index plc (joint response)

Ignis Asset Management

Investment Management Association

Legal & General Investment Management

London Investment Banking Association, International Securities Lending
Association, Securities Industry and Financial Markets Association, International
Swaps and Derivatives Association (joint response)

Prudential plc and M&G (joint response)

Terence Gale

Short selling instrument, including amendments to the Code of Market Conduct

The instrument does not differ from the consultative draft that appeared in CP09/15.

SHORT SELLING (NO 6) INSTRUMENT 2009

Powers exercised

- A. The Financial Services Authority makes this instrument in the exercise of the following powers and related provisions in the Financial Services and Markets Act 2000 (“the Act”):
- (1) section 119 (The code);
 - (2) section 121 (Codes: procedure);
 - (3) section 149 (Evidential provisions);
 - (4) section 156 (General supplementary powers); and
 - (5) section 157(1) (Guidance).
- B. The rule-making powers listed above are specified for the purpose of section 153(2) (Rule-making instruments) of the Act.

Commencement

- C. This instrument comes into force on 30 June 2009 and applies in relation to any position held on or after that date.

Amendments to the Handbook

- D. The Market Conduct sourcebook (MAR) is amended in accordance with the Annex to this instrument.

Citation

- E. This instrument may be cited as the Short Selling (No 6) Instrument 2009.

By order of the Board
25 June 2009

Annex

Amendments to the Market Conduct sourcebook (MAR)

In this Annex, underlining indicates new text and striking through indicates deleted text.

1.9 Market abuse (misleading behaviour) & market abuse (distortion)

...

Short selling in relation to financial sector companies

1.9.2C E ...

- 1.9.2D E (1) Failure by a person who has a *disclosable short position* in a *UK financial sector company* to provide adequate ongoing disclosure of their position is *behaviour* which, in the opinion of the *FSA*, is *market abuse (misleading behaviour)*.
- (2) In (1), “adequate ongoing disclosure” means disclosure made on a *RIS* by no later than 3.30pm on the *business day* following the day on which the position reaches, exceeds or falls below a *disclosable short position* of 0.25%, 0.35%, 0.45% and 0.55% of the issued share capital of the company and each 0.1% threshold thereafter.
- (a) [deleted]
- (b) [deleted]
- (2A) The disclosure referred to in (1) must include the name of the person who has the position, the amount of the *disclosable short position* and the name of the company in relation to which it has that position.
- (3) For the avoidance of doubt, changes in a *disclosable short position* between the thresholds referred to in (2) do not need to be disclosed under this section. For example, an increase from 0.25% to 0.31% of the issued share capital of the company does not need to be disclosed.
- (4) For the avoidance of doubt, (1) applies during a *rights issue period*.
- (5) ~~This provision ceases to have effect on 30 June 2009.~~ [deleted]

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The Financial Services Authority
25 The North Colonnade Canary Wharf London E14 5HS
Telephone: +44 (0)20 7066 1000 Fax: +44 (0)20 7066 1099
Website: <http://www.fsa.gov.uk>

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