esma European Securities and Markets Authority

Questions and Answers

Implementation of the Regulation on short selling and certain aspects of credit default swaps (1st UPDATE)

2012 | ESMA/2012/666

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I. Background

1. 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 ("Regulation") has already entered into force and will be fully applicable on 1 November 2012. It is supplemented by delegated regulations adopted by the European Commission specifying certain technical elements of the Regulation, to ensure its consistent application and to facilitate its enforcement. The objectives of this short selling legislative framework are to increase transparency of short positions held by investors in certain EU securities, reduce settlement and other risks linked with uncovered or naked short selling and create a harmonised framework for coordinated action at European level.

2. The short selling framework is made up of the following EU legislation:

    a. Regulation (EU) No 236/2012 of the European Parliament and the Council of 14 March 2012 on short selling and certain aspects of Credit Default Swaps[1] ("Regulation"). It is supplemented by a European delegated regulation as well as regulatory and implementing technical standards.

    b. Commission Delegated Regulation (EU) No 826/2012 of 29 June 2012 supplementing Regulation (EU) No 236/2012 of the European Parliament and of the Council with regard to regulatory technical standards on notification and disclosure requirements with regard to net short positions, the details of the information to be provided to the European Secu-

[1] OJ L 86, 24.3.2012, p. 1.

rities and Markets Authority in relation to net short positions and the method for calculating turnover to determine exempted ("RTS 1") [2].

c. Commission implementing Regulation (EU) No 827/2012 of 29 June 2012 laying down implementing technical standards with regard to the means for public disclosure of net position in shares, the format of the information to be provided to the European Securities and Markets Authority in relation to net short positions, the types of agreements, arrangements and measures to adequately ensure that shares or sovereign debt instruments are available for settlement and the dates and period for the determination of the principal venue for a share according to Regulation (EU) No 236/2012 of the European Parliament and of the Council on short selling and certain aspects of credit default swaps (ITS) [3].

d. Commission Delegated Regulation (EU) No 918/2012 of 5 July 2012 supplementing Regulation (EU) No 236/2012 of the European Parliament and of the Council on short selling and certain aspects of credit default swaps with regard to definitions, the calculation of net short positions, covered sovereign credit default swaps, notification thresholds, liquidity thresholds for suspending restrictions, significant falls in the value of financial instruments and adverse events ("DR") [4].

e. Commission Delegated Regulation (EU) No 919/2012 of 5 July 2012 supplementing Regulation (EU) No 236/2012 of the European Parliament and of the Council on short selling and certain aspects of credit default swaps with regard to regulatory technical standards for the method of calculation of the fall in value for liquid shares and other financial instruments ("RTS 2") [5].

3. Beyond the legislation, ESMA plays an active role in building a common supervisory culture by promoting common supervisory approaches and practices. In this regard, ESMA has adopted this Q&A and will update and expand it as and when appropriate.

II. Purpose

4. The purpose of this document is to promote common supervisory approaches and practices in the application of the European short selling regulatory regime. It provides responses to questions posed by the general public, market participants and competent authorities in relation to the practical application of the short selling framework.

5. The content of this document is aimed at competent authorities under the Regulation to ensure that in their supervisory activities their actions are converging along the lines of the responses adopted by ESMA. It should also help investors and other market participants by providing clarity on the requirements under the short selling framework.

[2] OJ L 251, 18.09.2012, p. 1.
[3] OJ L 251, 18.09.2012, p. 11.
[4] OJ L 274, 06.10.2012, p. 1.
[5] OJ L 274, 06.10.2012, p. 16.

III. Status

6. The Q&A mechanism is a practical convergence tool used to promote common supervisory approaches and practices under Article 29(2) of the ESMA Regulation.[6]

7. Therefore, due to the nature of Q&As, formal consultation on the draft answers is considered unnecessary. However, even if they are not formally consulted on, ESMA may check them with representatives of ESMA's Securities and Markets Stakeholder Group, the relevant Standing Committees' Consultative Working Group or, where specific expertise is needed, with other external parties. In this particular case, considering the date of application of the Regulation, ESMA has not engaged in such consultations.

8. ESMA will review these questions and answers to identify if, in a certain area, there is a need to convert some of the material into ESMA guidelines and recommendations. In such cases, the procedures foreseen under Article 16 of the ESMA Regulation will be followed.

IV. Questions and answers

9. This document is intended to be continually edited and updated as and when new questions are received. The date on which each question was last amended is included after each question for ease of reference.

10. Questions on the practical application of any of the short selling requirements may be sent to the following email address at ESMA: shortselling@esma.europa.eu

[6] 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 Regulation, 15.12.2010, L331/84.

Question 1: Scope

Date last updated: September 2012

Question 1a: Do the provisions of the Regulation also apply outside the EU and to non-EU natural or legal persons?

Answer 1a: Article 1 of the Regulation defines the scope of the Regulation by listing the financial instrument to which the provisions of the Regulation apply. For financial instruments referred to in Article 1(a) of the Regulation, the only decisive criterion is the admission of the instrument in question to trading on a trading venue in the Union (except where the principal trading venue of that instrument is in a third country), including when they are traded outside a trading venue. For debt instruments referred to in Article 1(c) of the Regulation, the main defining element is that these financial instruments are issued by a Member State or the Union. The same applies to sovereign CDS as defined under Article 1(e) of the Regulation. Neither the domicile or establishment of the person entering into transaction on these financial instruments nor the place where these transactions take place, including in third countries, are of any relevance in this regard.

Question 1b: Does the Regulation impact EU sovereign CDS trades booked outside the EU (e.g. Head Office in NY or Tokyo) but executed by traders in the EU (where a single global CDS book is run)?

Answer 1b: Recital 3 of the Regulation states that it is appropriate and necessary for the rules to take the legislative form of a regulation in order to ensure that provisions directly imposing obligations on private parties are applied in a uniform manner throughout the Union. Therefore, the legislative act taking a form of regulation excludes the possibility of any discretion by a national competent authority when applying the rules. Recital 16 of the Regulation specifies that in order to be effective, it is important that the transparency regime applies regardless of where the natural or legal person is located, including in a third country. Where that person has a significant net short position in a company that has shares admitted to trading on a trading venue in the Union or a net short position in sovereign debt issued by a Member State or by the Union, they need to be reported wherever these are executed or booked.

It should be noted that 'regime' is to be understood not as a mere set of rules for submission of a net short position notification, but as a broad concept encompassing as well rules applicable to entering into or acquiring a net short position.

Question 1c: How do the net position requirements impact on third country branches where there is not a distinct legal entity in the EU or no relationship with subsidiaries in other EU jurisdictions except having the same parent?

Answer 1c: Article 10 of the Regulation specifies that the notification and disclosure requirements apply to any legal person irrespective of where that person is domiciled or established. Therefore, there is no distinction to be drawn between a legal entity or a group in the EU or in a third country as to how they have to calculate their net short position in a given issuer and report it when a notification/disclosure threshold is reached or crossed.

Question 1d: Do shares of all companies traded on markets in the Union fall under the net short position notification and disclosure requirements under Articles 5 and 6, and the restriction on uncovered short sales of Article 12 of the regulation?

Answer 1d: When determining whether the shares of an issuer fall under the regime, two cumulative conditions have to be taken into account:

- the shares are admitted to trading/traded on a trading venue (i.e. regulated market or MTF) in the Union;
- the principal trading venue for the share is in the Union (and not in a third country in case of multiple trading).

For instance, shares of a company domiciled in the USA which are admitted to trading on a trading venue in Germany but whose principal trading venue is located in the USA are exempt from the notification/disclosure requirements (Articles 5 and 6 of the Regulation), the restrictions on uncovered short sales (Article 12) and from the buy-in procedures (Article 15 of the Regulation).

Question 1e: What financial instruments are covered by the net short position notification and disclosure requirements, and the restrictions on uncovered short sales? Is there a list available and where can it be found?

Answer 1e: The financial instruments concerned by the net short position notification and disclosure requirements, and the restrictions on uncovered short sales are:

- shares admitted to trading on a European regulated market or MTF, provided that, in case they are also traded on a third country venue (outside the EU/EEA), their principal trading venue is not located in that third country;
- sovereign debt issued by a sovereign issuer as defined by the Regulation;
- CDS on sovereign debt of a sovereign issuer as defined by the Regulation.

With respect to shares, the Regulation on short selling and certain aspects of CDS requires that a list of exempted shares is published by ESMA on its website on the basis of the information provided by national competent authorities. Therefore, any share not mentioned in that list that is admitted to trading on a regulated market in the EEA or traded on a MTF in the EEA is subject to the requirements of the Regulation.

It should be noted that ESMA has already published a list of shares admitted to trading on an EEA regulated market (http://mifiddatabase.esma.europa.eu/) which identifies the relevant competent authority for each share for the purpose of the Regulation.

With respect to sovereign debt and CDS on sovereign debt, ESMA is required to publish on its website the net short position notification thresholds applicable for each sovereign issuer falling under the scope of the transparency requirements set out by the Regulation. This publicly available list will identify the relevant competent authority for each sovereign issuer (http://www.esma.europa.eu/page/Short-selling).

Question 2: Transparency of net short positions – UPDATED

Date last updated: October 2012

Question 2a: When and for which trading day must the first notification and/or publication pursuant to Articles 5 to 10 of the regulation be submitted?

Answer 2a: The Regulation shall apply from 1 November 2012. The first notification or, as the case may be, disclosure relates to all net short positions existing or having arisen on 1 November 2012 unless it is not a trading day in the Member State of the financial instrument concerned.

Therefore, in Member States where 1st of November 2012 is a trading day [7], net short positions should be notified not later than at 15:30h on 2 November 2012 and, to the extent they are subject to a publication requirement, also disclosed within such period.

In Member States where 1st of November 2012 is not a trading day[8], the first net short positions to consider should be the ones held at the end of 2nd November 2012 (5 November for Hungary) and, where relevant, these net short positions should be notified not later than at 15.30 on 5 November 2012 (6 November for Hungary). To the extent they are subject to a publication requirement, they should also be disclosed within the same time period.

Question 2b: Which trading days should be used for the purpose of the timetable for making a notification or disclosure?

Answer 2b: The time specified in Article 9(2) of the Regulation for the notification (i.e. not later than 15:30h of the following trading day) is the one of the Member State of the relevant competent authority (RCA) for the purpose of notification. By analogy, it is assumed that the trading days would be the one of the Member State of the RCA for the purpose of the notification.

Question 2c: In Member States where a national transparency regime was already in place before the Regulation applies, do holders of existing short positions already notified to the concerned competent authority and/or publicly disclosed under that regime have to make new notifications and (if applicable) disclosures according to European regime?

If so, how should the "position date" field in the form be filled in if the threshold has been crossed before the entry into application of the Regulation?

Answer 2c: Yes they do. Notifications, and where relevant, disclosures of net short positions need to comply with the format specified in the Regulatory and Implementing Technical Standards adopted under the new European regime. This applies to existing notifiable or disclosable positions obtained before 1 November 2012 as well as those created on or after that date.

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[7] Belgium, Bulgaria, Cyprus, Czech Republic, Denmark, Estonia, Finland, France, Greece, Iceland, Ireland, Italy, Latvia, Malta, the Netherlands, Portugal, Romania, Spain, Sweden, United Kingdom.

[8] Austria, Germany, Hungary, Lithuania, Luxembourg, Poland, Slovakia and Slovenia

The “position date” field in the form to use for notification or for disclosure should be filled in with either 1st November 2012 or 2nd November 2012, depending on the trading calendar of the Member State for the concerned financial instrument. (See above).

Question 2d: How is a notification and/or disclosure to be submitted?

Answer 2d: Regulatory and implementing technical standards have been published specifying the details of the information on net short positions to be provided to the competent authorities and disclosed to the public.

The reporting channel (e.g. via fax, electronic systems, web-based solutions) will be specified by each competent authority on its website or on a website it supervises. ESMA will publish on its website the links to the relevant web page (http://www.esma.europa.eu/page/Short-selling).

Question 2e: How will competent authorities manage cases of legal or natural persons notifying for the first time a net short position?

Answer 2e: According to the Regulation, competent authorities or the operator of the central website supervised by the competent authority need to implement mechanisms for authenticating the source of notifications to them.

It should be emphasised that a position holder or the notifying entity remains responsible for the information that it reports to the relevant competent authority and, where relevant, that is publicly disclosed.

However, in order to ensure that disclosures are only made in respect of authenticated sources, competent authorities or the operator of the central website supervised by the competent authority can delay, unless it is not technically feasible, the publication of relevant net short positions until the authentication process has been completed.

Competent authorities or the operator of the central website supervised by the competent authority that have already implemented a strong and robust authentication process under their national transparency regime in force prior to the application of the Regulation will be able to rely on it for those legal or natural persons that have already been accepted under this process.

(New – October 2012)

Question 2f: For the purpose of the reporting and disclosure of net short position in shares, what should be the approach to rounding a net short position expressed in percentage?

Answer 2f: The net short position resulting from the calculation to be performed by an investor and expressed in percentage of the issued share capital of a particular issuer should be reported when a relevant notification threshold (e.g. for net short positions in shares: 0.2 %, 0.3 %, 0.4 %, 0.5 %, 0.6 %, etc.) is reached, exceeded or crossed downwards. In such case, the position to report should be rounded to the first two decimal places by truncating the other decimal places.

For instance, if the net short position is 0.3199 %, a notification is required and should indicate the 0.31% position.

However, for a net short position of 0.1987% of the issued share capital, no notification is required.

(New – October 2012)

Question 2g: What to do when a net short position that has already be notified is changing?

Answer 2g: A notification is required where the position reaches, exceeds or falls below a relevant notification threshold that equals 0.2 % of the issued share capital of the issuer concerned and each 0.1 % above that. If there is a change of net short position which remains within the relevant notification threshold, for which a notification has already been made, there is no requirement for a further notification, e.g. if first a notification threshold was reached and then exceeded.

For example, if the first notified net short position is 0.30 % on a rounded basis and then that net position increases but remains below 0.4% (e.g. to 0.312% or 0.3989%), no further notification is required.

Question 3: Calculating the net short position - UPDATED

Date last updated: October 2012

Question 3a: Do shares in funds have to be taken into account when calculating net short positions?

Answer 3a: Shares in funds which are managed on a discretionary basis by a management entity are not required to be taken into account since the calculation takes place at fund or fund manager level.
However, shares in ETFs are within the scope and should be taken into account when calculating net short positions to the extent to which the underlying shares are represented in the ETF.

Question 3b: At what level is the net short position to be calculated in the case of umbrella structures and master feeder structures?

Answer 3b: In the case of umbrella structures, the calculation of the net short position must take place at the level of the respective subfunds. In the case of master-feeder structures, it takes place at the level of the respective master fund.

(New – October 2012)

Question 3c: To what extent are instruments which give claims to shares not yet issued (subscription rights, convertible bonds) taken into account in the calculation of a net short position?

Answer 3c: Instruments that give a claim to shares that are not issued yet should not be taken into account as long positions when calculating a net short position. In particular, subscription rights, convertible bonds and other comparable instruments are not long positions within the meaning of Article 3(2)(b) of the Regulation.

Question 3d: Should dividends in the form of shares that must be returned by a borrower to the lender (as a result of a lending agreement) be taken into account to calculate short positions?

Answer 3d: No. Those shares which the lender is entitled to receive under the terms of a stock lending agreement as a result of a share dividend distribution and that must be reimbursed by the borrower shall not be included by the latter in calculating their net short position. The mere conclusion of a lending agreement does not confer in itself any financial advantage in the event of a decrease in price of the share borrowed.

Question 3e: Do shares received as a consequence of a bonus share issue or share dividend distribution fall to be treated as a long position for the purposes of calculating a net short position?

Answer 3e: Yes, as shareholders receive shares that can be used to offset short positions taken in the same issuer with other financial instruments. This may happen when, for instance, a net short position is constituted by having a long position in cash and a short position in derivatives.

(New – October 2012)

Question 3f: Can a short position in sovereign debt be offset against an interest rate swap trade?

(For example, Sell 10 year German Bund and receive Fixed (pay floating) 10 year interest rate swap denominated in Euro)

Answer 3f: No. An interest rate swap is not per se an instrument related to the concerned sovereign debt in the meaning of Article 8(2) of the Regulation unlike derivative instruments on the sovereign debt itself.

(New – October 2012)

Question 3g: Under Article 3(3) of the Regulation and Annex II Part 1.3 & 2.4 of the DR, firms need only to look-through indices, baskets and ETFs to the extent that doing so is reasonable having regard to publicly available information. How should this condition be understood?

Answer 3g: ESMA understands "publicly available information" on an index, basket of securities or ETF composition as information which is easy to access on the market operator's or issuer's website and which is obtainable free of charge. Such information, notably on indices, is generally available free of charge when provided with a certain delay.

ESMA is aware that the provision of a real time index, basket or ETF's composition is likely to be charged. However, it should be recalled that there is no requirement under the Regulation to obtain information on the composition of the above on a real time basis. ESMA considers that market participants should strive to use the most recent publicly available information for look-through purposes.

ESMA would like to specify that "acting reasonably" relates only to obtaining information about the composition and not to how investors process that information for conducting the calculation of the net short position. The Regulation is straightforward and requires that the index weighting, the composition of the basket of securities and the interests held in ETFs are considered in this calculation.

Question 4: Duration adjustment for calculating net short positions in sovereign debt - ADDED

Date last updated: October 2012

Question 4a: The DR[9] specifies in the Annex II part 2 para. 1 that positions should be calculated in "nominal value duration adjusted". What duration definition should be used in the calculation?

Answer 4a: The duration formula to use is the Modified Duration. Information about the Modified Duration for a specific debt issue by a sovereign issuer is easily available from data providers. Modified Duration can also be computed from other available "duration" or sensitivity indicators such as the Macaulay duration or PV01.

Question 4b: How should an investor calculate the duration-adjusted net short positions on sovereign debt?

Answer 4b:

For a particular sovereign issuer, the method to calculate the net short position is to multiply the duration of each individual issued debt instrument in which the investor has, at the end of the day, a long or short position by the nominal value of each of those positions, with a positive sign for long positions and a negative one for short positions, and add up all the products.

For each short and long position held on sovereign debt instruments (i) and being D= Modified Duration of each instrument held and V=Nominal volume (in €) of each position debt instrument held, the "nominal value duration adjusted" (NVDA) would be:

$$\mathrm{NVDA} = \sum_{i=1}^{n} (D_i \times \pm V_i)$$

For example, an investor with a short position of 10 million € in a bond with Modified Duration 5 and a 1 million € short position in a bond with Modified Duration 3,5 will have a net short position equivalent to -53,5 million € (-10 x 5) +(- 1 x 3,5).

Since only net short positions are to be communicated, the negative sign shall not be included in the official notification.

[9] Commission Delegated Regulation regarding definitions, calculation of net short positions, covered sovereign CDS, notification thresholds, liquidity thresholds for suspending restrictions, significant falls in the value of financial instruments and adverse events (DR), adopted by EU Com on 5 July 2012

Question 4c: How will ESMA calculate the amount of outstanding sovereign debt of sovereign issuers on a duration adjusted basis?

Answer 4c: Every quarter, the relevant national competent authorities will provide ESMA with a duration adjusted figure of the outstanding amount of sovereign debt for their respective Member States or federated states. The figures for all sovereign issuers will be published on the ESMA website together with the notification thresholds applicable.

On each reference date (end of quarter) for calculation, the method to calculate this figure will be to multiply the Modified Duration of each individual debt instrument issued by the concerned sovereign issuer by its outstanding volume (i.e. nominal amount issued and not redeemed) and add up all these individual results.

For each instrument (i) and being D=Modified Duration of each issued instrument and V=Outstanding volume (in €) of each issued debt instrument, the "nominal value duration adjusted" (NVDA) would be:

$$\mathrm{NVDA} = \sum_{i=1}^{n} (D_i \times V_i)$$

Question 4d: If I reach or cross a notification threshold just because the duration of my position increased or decreased, without having taken any investment decision and without changes in the nominal position, should I update my notification to the competent authority?

Answer 4d: Yes. The net short position should be calculated taking into account any change in the duration of the position held, and be notified to the relevant competent authority if it results in this net short position reaching a threshold.

Question 5: Net short positions when different entities in a group[10] have long or short positions or for fund management activities - ADDED

Date last updated: October 2012

Question 5a: Are funds (or portfolios under management) managed by the same management entity expected to report net short positions?

Answer 5a: No. At individual fund (portfolio) level, only the calculation of the net short position for each particular issuer takes place. Only the positions of the funds that are net short in the particular issuer i.e. pursuing the same investment strategy (i.e. being short), should be aggregated to determine the net short position at the management entity level and whether a threshold is reached warranting thus reporting and, where relevant, disclosure of the aggregated net short position in that particular issuer (see Annex 1).

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[10] In this Q&A document, group has the meaning specified in Article 2(a) of the DR adopted by the Commission on 5 July 2012.

For the purposes of the Regulation, an investment strategy is whether the fund (portfolio) is long or short in a particular issuer.

Question 5b: How should net short position calculation and reporting be conducted when the same single legal entity performs both management and non-management activities?

Answer 5b: According to Article 12(5) and 12(6), when a single legal entity performs both management and non-management activities, it should conduct two different and separate calculations, one for each activity.

For the management activities, the net short position of each individual fund or portfolio under management should first be calculated for each issuer in which a position is held. The second step consists in aggregating, for each issuer, only the positions of the funds and/or portfolios that are net short at the level of the entity/division/unit/department that manages these funds and/or portfolios. If this aggregated net short position reaches a notification threshold, then the aggregated net short position should be reported.

For non-management activities, the legal entity should calculate its net short position in each particular issuer, excluding the management activities, and report (or disclose) when a relevant threshold is reached.

Potentially, on the same issuer, a legal entity may report two net short positions, one for the management activities and the other for the non-management activities.

(See Annex 2)

Question 5c: According to Article 12(4) of the DR, the management entity level report specifically excludes from the calculation the positions of funds and portfolios the management of which is delegated to a third party and includes those of funds and portfolios the management of which has been delegated by a third party. Should the same approach apply to the single legal entity level report when that entity is performing both management activities and non-management activities, even though Article 12(5) of DR does not explicitly refer to Article 12(4) on delegation of management?

Anwer5c: Article 12(4) of the DR clarifies the method set out in Article 12(1) to (3). Therefore, ESMA considers that the approach to delegation for calculating the net short position (excluding mandates delegated away and including received mandates) applies to the management activities of a legal entity also performing non-management activities.

Question 5d: Being a global fund manager of funds, I use derivative instruments that may result in net short positions in particular issuers when calculated as described in the DR though the strategies being implemented do not, however, relate to particular issuers but aim at increasing or reducing exposure to markets or sectors. An example of the type of strategies that may be employed is: selling exposure to European bank equity through the EuroStoxx Banks index (SX7E) using futures contracts.

In light of the definition of investment strategy under Article 12(2)(a) of the DR[11] and considering that such strategies are aimed at reducing my exposure to sectors or markets and do not relate to particular issuers are they subject to short position reporting requirements ?

Answer 5d: Yes they are subject to the net short position reporting requirement.

According to the DR, the calculation of the net short position should be performed at each individual fund level. For a particular issuer, it should include not only cash positions but also positions held by the individual fund through indices where that issuer is represented and in accordance with its weight in the index.

The concept of investment strategy is used to determine whether the fund position is net short or net long. In the former, the net short position of that fund should be aggregated at the level of the management entity with the other funds having a net short position in the concerned issuer.

Question 5e: In a group constituted only of legal entities performing exclusively management activities, how should calculation and reporting be conducted? Who should report?

Answer 5e: As described above in Q&A 5a, positions are calculated at fund or portfolio level. The positions of funds (or portfolios) which are net short in a particular issuer are then aggregated at the level of the management entity managing these funds (or portfolios). The management entity or another entity on its behalf should report the net short position when a threshold is reached.

The funds having net long position in this particular issuer should not be considered in the aggregation.

No aggregation and netting of the short and long positions of the several management entities constituting the group is required.

(See annex 3)

Question 5f: In the case of a group, should a legal entity that is a part of this group always report/disclose its position when it reaches a threshold?

Answer 5f: No, not always. Any legal entity within a group that reaches or crosses a threshold would only have to report its net short position in a particular issuer when the aggregated net short position at the group level (aggregating and netting the net positions, long and short, of all the entities within the group, with the exception of the net positions resulting from management activities by one or more of the legal entities) does not simultaneously reach or cross a notification threshold (See Annex 4).

Question 5g: In a group constituted of several legal entities, including management entities, should the short positions of the management entities arising from their 'non-management activities' be aggregated with those of the legal entities not performing management activities as part of the 'group position' for reporting, or should they be reported separately?

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[11] Art 12(2)(a) of DR sates: "Investment strategy" means a strategy that is pursued by a management entity regarding a particular issuer, that aims to have either a net short position or a net long position taken through transactions in various financial instruments issued by or that relate to that issuer.

Answer 5g: According to Articles 12(5) and 12(6), a legal entity within a group that performs both management activities and non-management activities should calculate separately, and report where relevant, the net short position resulting from its management activities in a particular issuer from the net short position resulting from its non-management activities.

The latter should be calculated at the concerned legal entity level. It should be aggregated and netted at group level with the net short and long positions of the other legal entities of the group that do not perform management activities.

Question 5h: In the case of a group,

a) What if the group and the legal entity within the group cross different thresholds, or they cross the same threshold in different directions?
b) If the legal entity within the group exceeds the 0.5% threshold and, at the same time, the group exceeds the 0.2% threshold, would the legal entity within the group still have reporting/disclosing obligation?

Answer 5h: According to the conditions laid down in Article 13(3) of the DR,

a) In both situations, only the position at the group level should be reported.
b) The legal entity within the group does not have to report/disclose its net short position; only the net short position at group level is reported/disclosed.

Question 6: Handling of notification and disclosure of net short positions - MOVED

Date last updated: September 2012

Question 6a: Should competent authorities accept handling late submissions i.e. notification, modification or cancellation submitted days, weeks or months after the date of the crossed threshold?

Answer 6a: Without prejudice to sanctions that could be applied for breaching the Regulation, a competent authority should handle such late submissions relating to net short positions in shares, sovereign debt and sovereign CDS for supervisory purposes including ensuring consistency over time of the information. Where relevant, for proper information of the public, the net short position in shares should also be publicly disclosed. To avoid confusion of the public in such a case, the position date field of the notification form must include the date on which the position was effectively created, changed or ceased to be held, no matter how far back in the past, and not refer to the date when the notification is made.

Question 6b: How will late submissions of disclosable short positions be dealt with by competent authorities? When will publication of such late disclosures take place?

Answer 6b: A person with a disclosable net short position is required to make the disclosure by the officially specified method no later than 15:30h on the trading day following that on which the position

reached or crossed the relevant publication threshold. If the disclosure is made after that time, the competent authority or operator of the central website supervised by the competent authority will aim to publish it as soon as possible after its receipt, provided this is during normal business hours. Depending on the checking process implemented by the competent authority, the disclosure may occur on the following trading day. Disclosures received after normal business hours will normally only be published the following trading day. Late disclosures will constitute breaches of the Regulation and, as such, competent authorities will pursue cases of late disclosures in line with their stated investigation and enforcement policies.

Question 6c: What happens if a person has made a disclosure before 15.30 but, because of regulatory checks or other issues outside the person's control, the disclosure is not published until after that time?

Answer 6c: The person has met its obligation under the Short Selling Regulation by making the disclosure by no later than 15.30h local time even if the notification is published by the competent authority or the operator of the central website supervised by the competent authority at a later point.

Question 7: Uncovered short sales – UPDATED AND MOVED

Date last updated: October 2012

Question 7a: Can a legal person within a group enter into an uncovered short sale provided that another legal entity within the same group has fulfilled one of the conditions set out in Article 12(1) of the Regulation with regards to the same instrument?

Answer 7a: No, short sales cannot be covered with an agreement, pursuant to Article 12(1) of SSR, entered into by another legal entity within the same group. The same entity carrying out the short sale has indeed to cover it with an agreement pursuant to Article 12(1) of SSR, including a locate agreement concluded with another legal entity within the group.

In shares

Question 7b: To what extent are instruments which give claims to as yet unissued shares (subscription rights, convertible bonds) affected by the restriction?

Answer 7b: According to Article 12(1) of the Regulation, the provisions of the restriction on uncovered short sales of shares relate only to shares admitted to trading on a trading venue. That means that transactions in instruments such as subscription rights and convertible bonds e.g. performed as part of a capital increase do not fall within the scope of Article 12(1) of the Regulation.

Question 7c: Can claims to as yet unissued shares (subscription rights, convertible bonds) cover a short sale?

Answer 7c: Claims to as yet unissued shares (subscription rights, convertible bonds) may only cover a short sale if the availability of the new shares for settlement by the arrangement is ensured when settle-

ment is due e.g. the concerned rights or convertible bonds can be converted into shares that would be available in time for ensuring the settlement.

In sovereign debt

Question 7d: Are foreign currency bonds of EU Member States also covered by the restrictions on uncovered short sales in sovereign debts?

Answer 7d: Yes, the prohibition provision covers sovereign debt securities irrespective of the currency in which they are issued.

Question 7e: Could a short sale on sovereign debt be considered covered by a repo contract executed in the days following the short sale but with the same settlement date as the short sale (e.g. a spot next repo for a T+3 cash sale)?

Answer 7e: Yes, it is possible to cover a short sale by entering into a repo contract afterwards provided that:

1/ prior to the short sale, the short seller entered into one of the arrangements with a third party under Article 13(1)(c) of the Regulation and Article 7 of the ITS (e.g. obtained an "easy to purchase sovereign debt confirmation" according to Article 7(5));

2/ the repo contract has an earlier or the same settlement date as the short sale, so that the delivery of the relevant sovereign debt can be effected when it is due.

Question 7f: A market operator who manages a regulated market for sovereign debt can be considered a third party in accordance with Article 8(1)(f) of ITS?

New answer 7f: Yes, a market operator can be considered a third party according to Article 8(1)(f) of ITS if:

- it "*is subject to the authorization or registration requirements in accordance with Union law*" (Article 8 (1)(f));
- it "*participates in the management of borrowing or purchasing of […] the sovereign debt*" (Article 8(2)(a)), for example by managing a repo platform (for borrowing the debt) or a cash platform (for purchasing the sovereign securities);
- it is able to "*provide evidence of such participation*" and, "*on request, to provide evidence of its ability to deliver or process the delivery of […]sovereign debt on the dates it commits to do so to its counterparties including statistical evidence*" (Article 8(2)(b)- (c)) (e.g. with official statistics of market activity)

Such a third party can provide an "Easy to purchase sovereign debt confirmation" according to Article 7(5) of the ITS (pursuant Article 13(1)(c) of the Regulation), confirming that the sovereign debt is liquid on the platform so that there is a reasonable expectation that the securities can be borrowed or purchased in due time to ensure the settlement of the short sale.

(New – October 2012)

Question 7g: When firms are comparing the correlation between two sovereign issuers (under Article 3(5) of the Regulation and Article 8(5) of the DR) should they do this on an issue per issue basis, or by comparing the yield curve of the two issuers?

Answer 7g: Since net short positions are to be calculated on a sovereign issuer basis, ESMA considers that the calculation of correlation should be undertaken on the basis of the issued sovereign debt. So it would be a matter of comparing the yield curves of the two sovereign issuers to determine whether the test of high correlation as defined in the DR was met.

In sovereign CDS

Question 7h: Do the restrictions on uncovered sovereign credit default swaps also apply to the protection seller?

Answer 7h: No, the restriction on uncovered sovereign credit default swaps applies only to the protection buyer of a CDS.

Question 7i: May a sovereign CDS be used to hedge the risk under another CDS referring to the same sovereign debt?

Answer 7i: Yes, it would be legitimate to use a sovereign CDS position to hedge a risk related to another CDS position in so far as the conditions prescribed in Chapter V (in particular Articles 18 and 19) of the DR (Commission Delegated Regulation No 918/2012) are fulfilled.

Question 8: Exemption for market making activities and for primary dealers operations - ADDED

Date last updated: October 2012

Question: In order for any non-EEA entity to be able to use the market making activities exemption as defined in the Regulation, the market in its home jurisdiction should be subject to a legal and supervisory regime which is equivalent to the MiFID, MAD and Transparency directive and should be declared "equivalent". Has such a determination of "equivalence" already taken place? Will non-EEA entities be able to use the exemption for their market making activities under the Regulation in time for 1 November, 2012?

Answer: According to Article 17(2) of the Regulation, the legal and supervisory framework of a third country is considered equivalent when the European Commission has adopted a decision to that effect.

The Commission has not issued any equivalence decision; thus, at this stage, no third country entity can claim the use of the exemption in relation to a third country market.

Question 9: Enforcement - MOVED

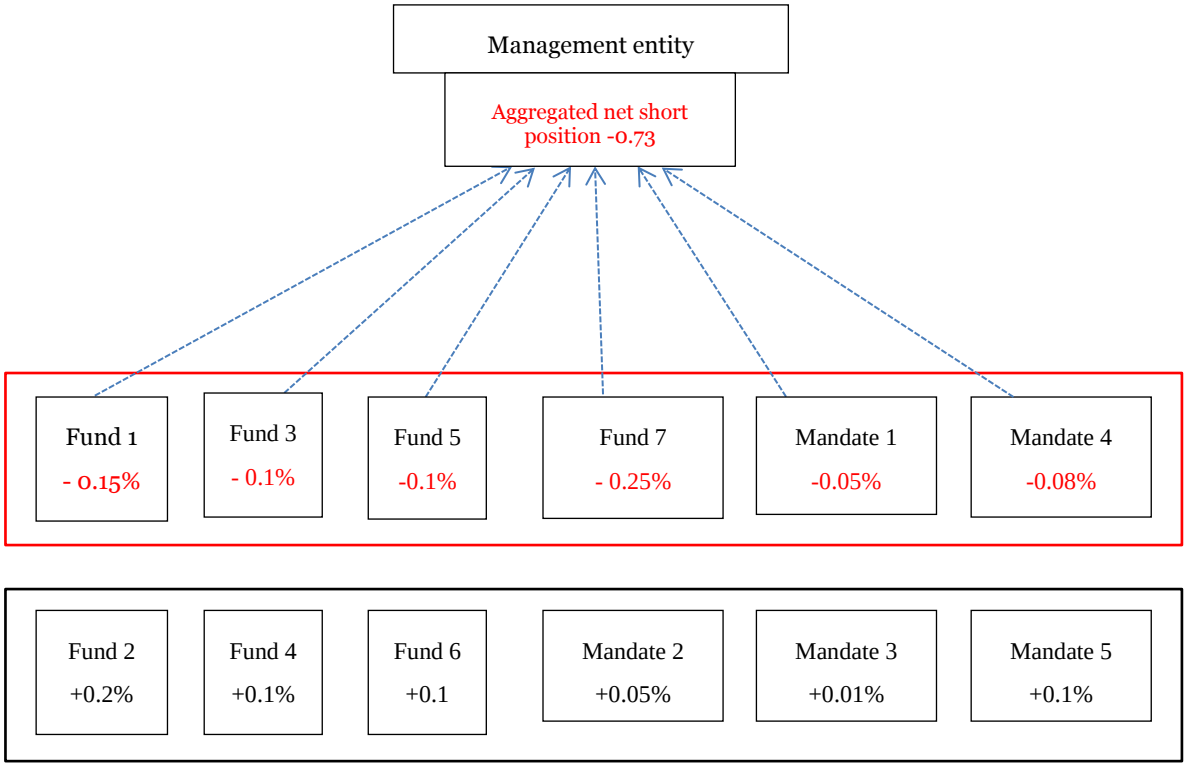
Date last updated: September 2012

Question: How will any violations of the provisions of the Regulation be sanctioned?

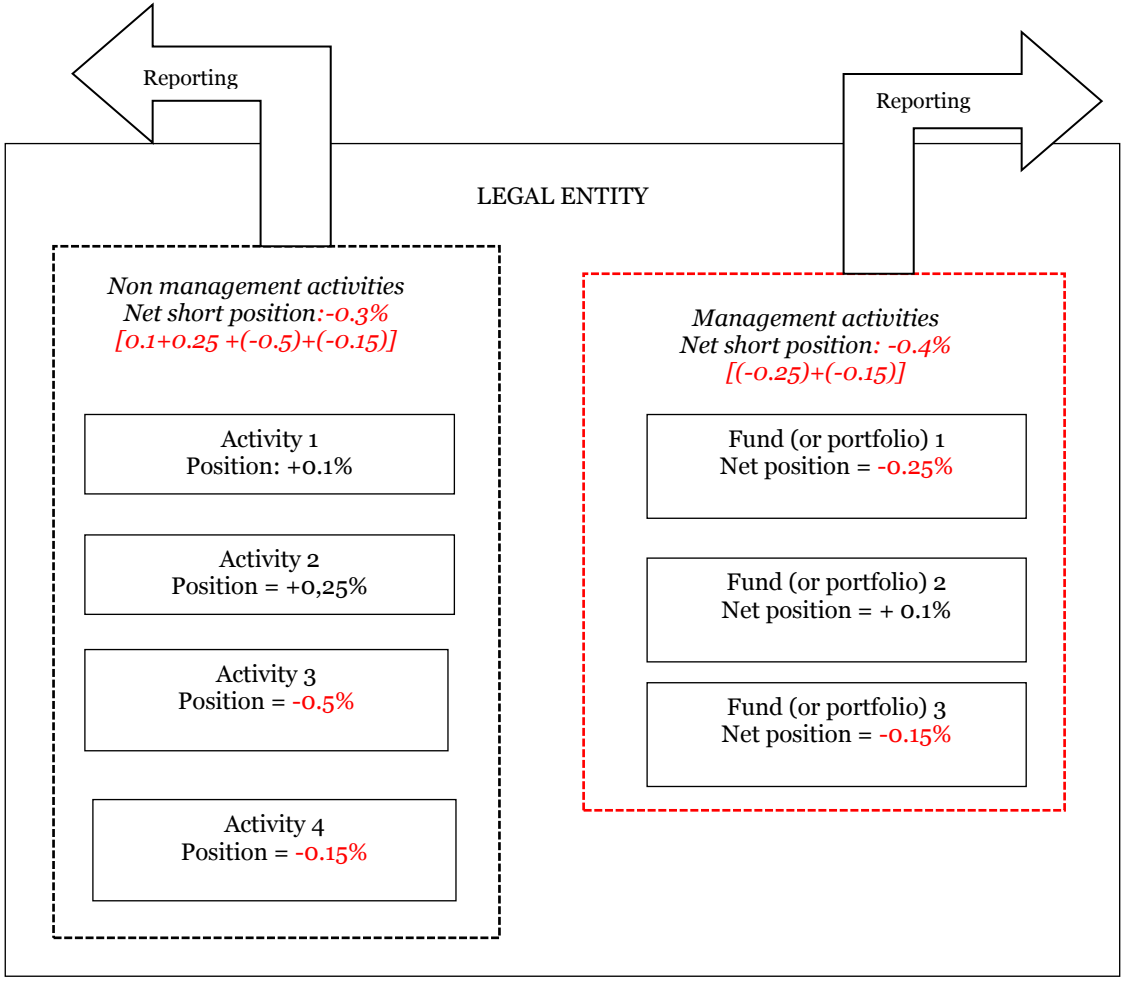
Answer: Pursuant to Article 41 of the Regulation, rules on penalties and administrative measures shall be established by Member States and notified to ESMA.

In addition, ESMA has to publish a list of the existing penalties and administrative measures applicable in Member States on its website (http://www.esma.europa.eu/page/Short-selling).

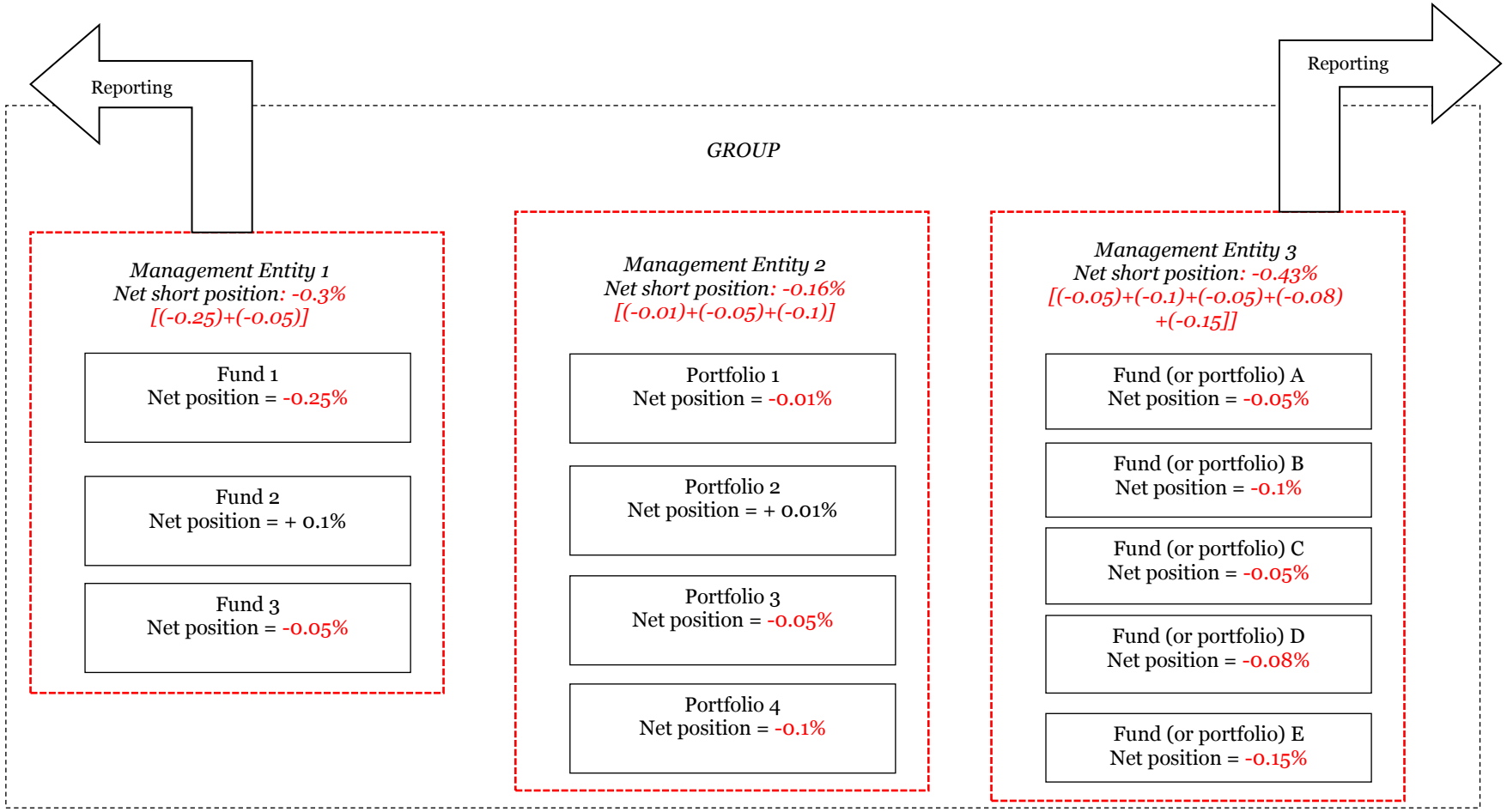
Annex 1: Example of calculation within a management entity



Annex 2 – Example of a single legal entity performing both management and non-management activities

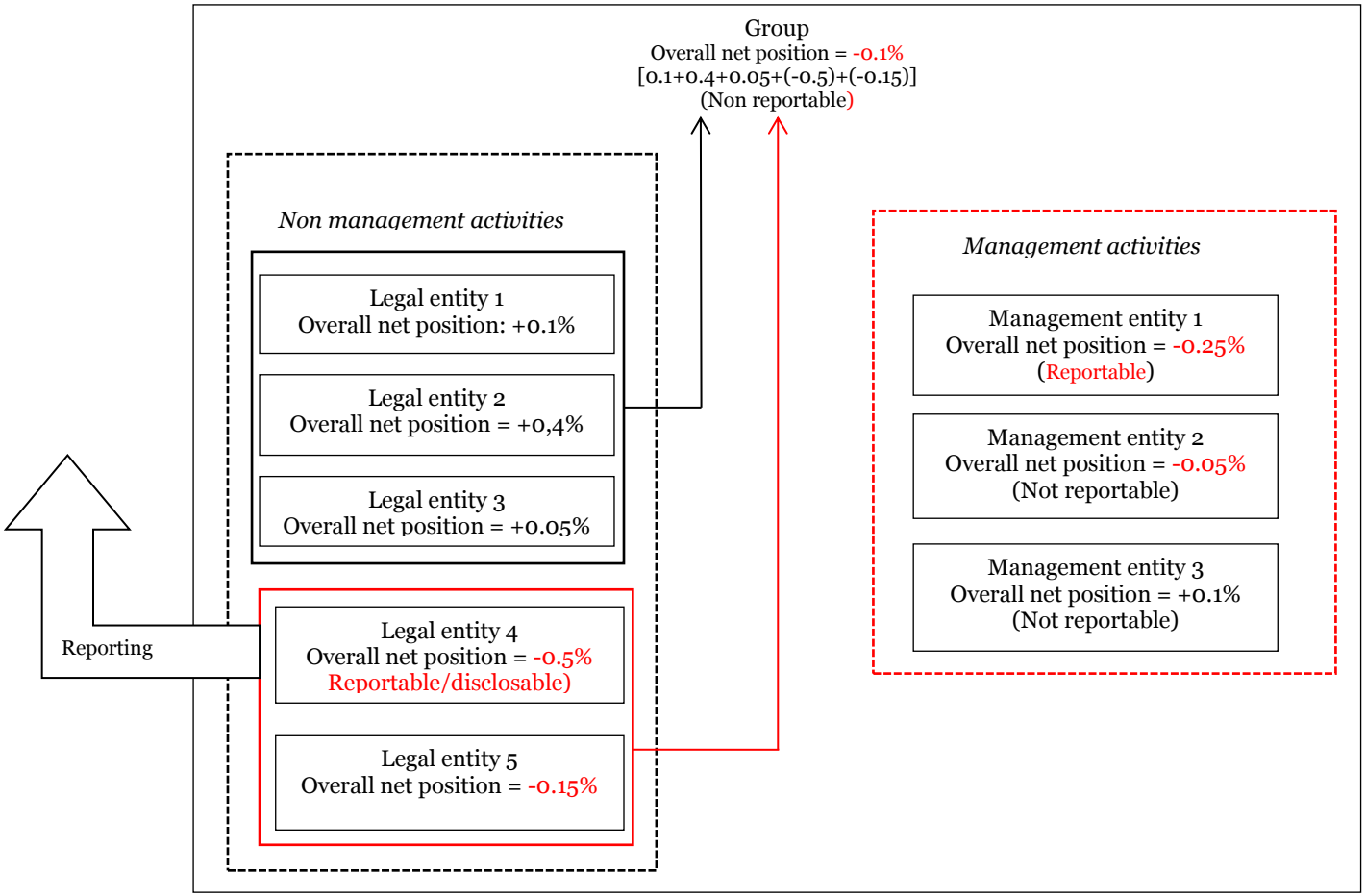


Annex 3 – Example of a group constituted only of management entities performing exclusively management activities



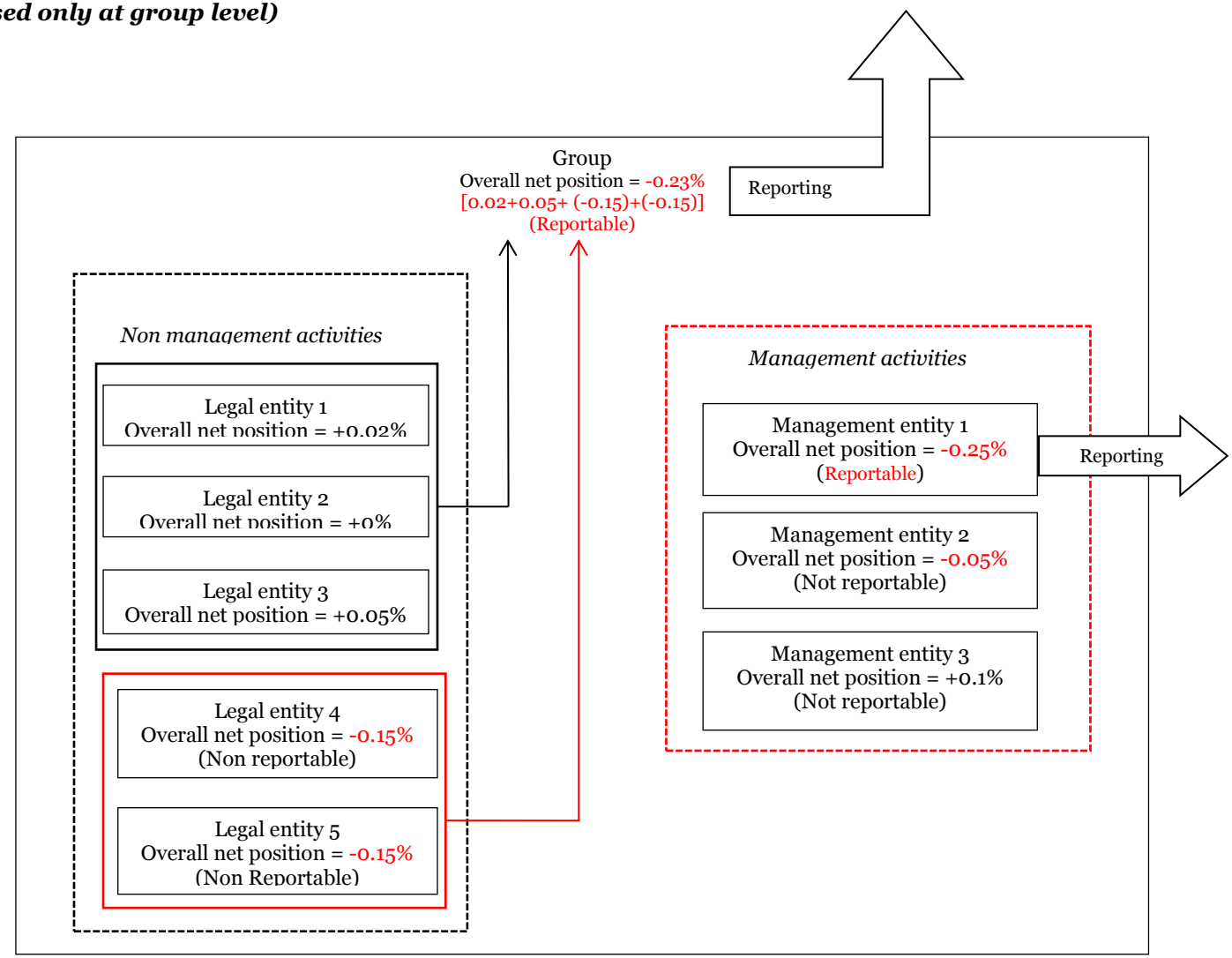
Annex 4 – Examples of calculation within a group

1/ Only the legal entity belonging to the group reports/discloses



2/ Only the net short position at group level is reported/disclosed

Case 1 (threshold crossed only at group level)



Case 2 (simultaneous crossing of thresholds)