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ESMA consultation paper on ESMA's draft technical advice on possible delegated acts concerning the regulation on short selling and certain aspects of credit default swaps (ESMA/2012/98)

The City of London Law Society ("CLLS") represents approximately 14,000 City lawyers through individual and corporate membership including some of the largest international law firms in the world. These law firms advise a variety of clients from multinational companies and financial institutions to Government departments, often in relation to complex, multi jurisdictional legal issues.

The CLLS responds to a variety of consultations on issues of importance to its members through its 17 specialist committees and in this case the response has been prepared by a working party of the CLLS Company Law Committee comprising senior and specialist corporate lawyers.

We welcome the opportunity to respond to ESMA consultation paper ESMA/2012/98. The timescales for the consultation have not allowed us to take industry soundings, so we therefore have focused on equity reporting rather than sovereign debt. We understand some of the industry groups will be responding on the latter, having liaised more with market participants.

Question 1

We agree with the proposal concerning article 2(1)(r) save for that "legal or" in line 1 should be deleted as the definition is really looking at beneficial ownership, not legal ownership (for example a nominee should not be included).

In relation to the question of ownership, we think that this should be related to the law by which the securities themselves are governed rather than the law of the jurisdiction where the short sale takes place as otherwise those taking short positions could deliberately enter into the short sale in a jurisdiction whose law they think will be favourable to them.

Question 2

We are not aware of any other cases which need to be excluded from the definition of short sale.

Question 3

We are not aware of any other definitions which need further clarification.

Question 4

We agree with the proposal on "holding" for the purposes of determining a long position save that instead of the wording "without having ownership, having a legally enforceable claim to be transferred ownership…" we suggest "without having ownership, having an entitlement to acquire, on his own initiative alone, under a formal agreement…". The reason for this change is so as to make it clear that a call option would be covered – a legally enforceable claim is not entirely clear because until service of the option exercise notice, it is not legally enforceable. (The alternative wording we have suggested comes from article 13(1) of the Transparency Directive).

Question 5

No, we do not have any suggestions on possible further criteria to describe the holding of a share/sovereign debt.

Question 6

We agree with the proposal for calculating long positions and short positions save as follows:

1. in relation to "long positions", there is a sub-heading "complex derivatives". We think that all derivatives should be covered and therefore suggest that "CFDs" is substituted for "complex derivatives". There is no reason why simple derivatives should not also be covered; the word "complex" implies that simple derivatives would not amount to a long position.

2. under "long positions", it is stated that "instruments that give rise to a claim to shares not in issue 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…". An equivalent statement should be made in relation to short positions. It would be illogical to exclude subscription rights and convertible bonds (or similar rights over unissued shares) from long positions, but not to exclude them from short positions.

Questions 7-11

These relate to sovereign debt and we are not commenting on these questions.

Question 12

We agree that it is appropriate that the "delta-adjusted method" be used for calculation.

Question 13

We make no comment on the calculation, save that we consider that there should be some *de minimis* level below which financial advantage achieved through baskets need not be calculated. We think the UK Disclosure and Transparency Rules provide a good template for this (DTR 5.3.3(2)(c)).

Question 14

We make no comment on additional methods of calculation.

Question 15 and 16

These relate to sovereign debt and we are not commenting on these questions.

Question 17

We are not commenting on the provisions relating to fund management. In relation to the provisions relating to groups, we consider them to be extremely complicated in implementation and, once published, interpretation. We question whether the requirement to categorise by Decision Makers and by Investment Strategies is workable in practice. We recognise that ESMA welcomes the views of market participants before it makes a final determination, and we would urge it to explore this position more fully. We believe a much simpler structure, where all legal entities in a group have to aggregate and only one disclosure is made for the entire group, is preferable (subject to the potential for disaggregation where merited and practicable).

In paragraph 3 (b) of the draft advice, ESMA states that funds should be aggregate where the "same investment strategy" is pursued. We query how you would determine whether funds have the "same" strategy. How small a difference would stop them being the "same"?

Question 18

We think that most groups would find it easier to stick to the article 2(1)(f) of the Transparency Directive definition (i.e. alternative 2) since that will already be used for reporting purposes.

Alternative 1 is too vague in that an entity that is equity accounting for an investment would "incorporate in its balance sheet the gains and losses of one or more single entities that belong to it". To make alternative 1 clearer if it was preferred, one would need to incorporate the concept of full consolidation i.e. exclude entities that are subject to proportional consolidation or equity accounting. Under alternative 1 as amended therefore one would refer to an undertaking "and all other undertakings whose results are fully consolidated".

Question 19

No comment.

We do not have any comments on the remaining questions.

Date: 13 March 2012