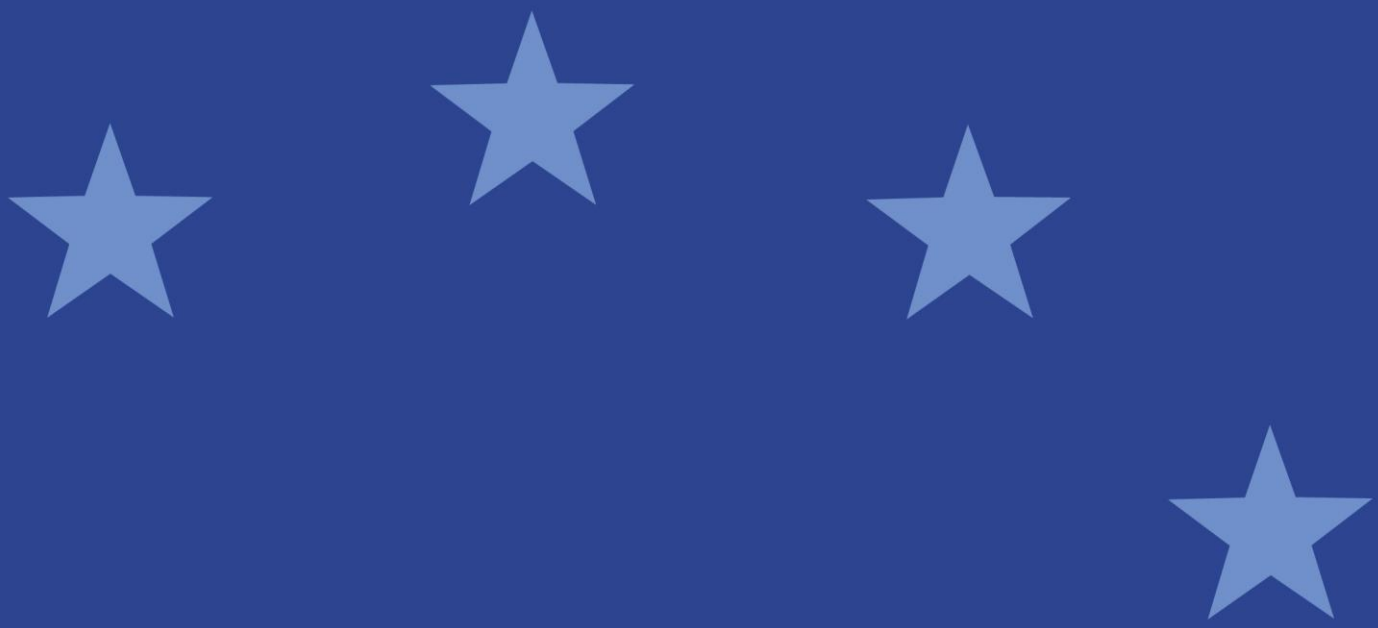
esma European Securities and Markets Authority

Response Form to the Consultation Paper on the review of certain aspects of the Short Selling Regulation



21 September 2021 | ESMA70-156-4948

Responding to this paper

ESMA invites comments on all matters in this consultation paper and in particular on the specific questions. Comments are most helpful if they:

- respond to the question stated;
- indicate the specific question to which the comment relates;
- contain a clear rationale; and
- describe any alternatives ESMA should consider.

ESMA will consider all comments received by **19 November 2021.**

All contributions should be submitted online at www.esma.europa.eu under the heading 'Your input - Consultations'.

Instructions

In order to facilitate analysis of responses to the Consultation Paper, respondents are requested to follow the below steps when preparing and submitting their response:

1. Insert your responses to the questions in the Consultation Paper in the present response form.

2. use this form and send your responses in Word format (**pdf documents will not be considered except for annexes**);

3. Please do not remove tags of the type <ESMA_QUESTION _SSRR_1>. **Your response to each question has to be framed by the two tags corresponding to the question.**

4. If you do not wish to respond to a given question, please do not delete it but simply leave the text "TYPE YOUR TEXT HERE" between the tags.

5. When you have drafted your response, name your response form according to the following convention: ESMA_SSRR_nameofrespondent_RESPONSEFORM. For example, for a respondent named ABCD, the response form would be entitled ESMA_SSRR_ABCD_RESPONSEFORM.

6. Upload the form containing your responses, **in Word format**, to ESMA's website (www.esma.europa.eu under the heading "Your input – Open Consultations" -> Consultation Paper on Review of MAR Guidelines on delay in the disclosure of inside information and interactions with prudential supervision").

Publication of responses

All contributions received will be published following the close of the consultation, unless you request otherwise. Please clearly and prominently indicate in your submission any part you do not wish to be publically disclosed. A standard confidentiality statement in an email message will not be treated as a request for non-disclosure. A confidential response may be requested from us in accordance with ESMA's rules on access to documents. We may consult you if we receive such a request. Any decision we make not to disclose the response is reviewable by ESMA's Board of Appeal and the European Ombudsman.

Data protection

Information on data protection can be found at www.esma.europa.eu under the heading Legal Notice.

Who should read this paper

All interested stakeholders are invited to respond to this consultation paper. This consultation paper is primarily of interest to issuers of financial instruments admitted to trading or traded on a trading venue, investment firms, market makers, primary dealers, persons who engage in short sales or transactions resulting in net short positions. Responses are also sought from any other market participant including trade associations and industry bodies, institutional and retail investors, consultants and academics.

General information about respondent

Name of the company / organisation	Bundesverband der Wertpapierfirmen (bwf)
Activity	Investment Services
Are you representing an association?	☒
Country/Region	Germany

Please make your introductory comments below, if any.

<ESMA_QUESTION_SSRR_0>

The Bundesverband der Wertpapierfirmen e.V. (bwf) is a trade association representing the common professional interests of securities trading firms, market specialists acting as market makers at securities exchanges and/or as systemic internalisers and various other investment firms throughout Germany. In this capacity, we expressly welcome the possibility to comment on ESMA's Consultation Paper - on the review of certain aspects of the Short Selling Regulation.

As an introductory comment, we would like to point ESMA's attention to one aspect which is not expressively addressed in the consultation paper but which we consider to be of paramount importance:

In order to make use of the exemption for market making activities and primary market operations as stipulatesd in Article 17 SSR, the natural or legal person in question has to notify the relevant NCA in writing not less than 30 calender days before the intended use of the exemption. In practice, the notification has to be made on an ISIN by ISIN basis and has to be updated if the ISIN for the instrument in question changes.

This requirement of ex ante notification has resulted in a tremendous administrative burden for market makers and NCAs alike which from our point of view is – with respect to the 30 days ex ante as well as with respect to the ISIN by ISIN requirement – uneccessary and clearly disproportionate. It further leads to frictions in the market, e.g. in the case of IPOs or newly issued instruments (or even in the case of changes in ISINs as already mentioned). These negative effects clearly contradict the legislative intent expressed in recital 26 SSR which states that "imposinging requirements on such activities could severely inhibit their ability to provide liquidity and have a significant adverse impact on the efficiency of the Unions markets".

Another unintended consequence of the ex ante, ISIN by ISIN notification requirement, is that firms engaged in market making activities as defined in Article 2 (k)(ii) SSR ("as part of its usual business, by fulfilling orders initiated by clients or in response to clients' requests to trade") can often not utilise in practice the exemption of Article 17 SSR simply because they do not know in advance for which instruments they receive orders or requests for trade. Consequently, in order to make full use of the market making exemption, notifications would have to be send (and permanently updated) for all instruments a firm is principally willing to trade under Article 2 (k)(ii) SSR, which in fact typically is the full universe of instruments

falling under SSR which are admitted for trading at the trading venues, a market maker is a member of or which he trades OTC. Since this is de facto impractical, the exemption stipulated in Article 17 is often de facto waived in cases of Article 2 (k)(ii) SSR with the effect that the market maker hast to enter into a locate agreement with a third party in order to e able to execute a client order or request for trade in compliance with the wording of SSR. This obvisually adds a significant administrative and economic burden on these firms which should have been avoided by the exemptions stipulated by Article 17.

In this context, it should be noted and remembered that e.g. U.S. Regulation SHO Rule 203(b)(2) provides an exemption from "locate" requirements camparable to Article 17 SSR, given that a firm is able to demonstrate (ex post) that the short sale was executed in direct connection with "bona fide market making activities". While the SEC, to our knowledge, monitors the compliance with the "bona fide market making activities" very closely and intervenes in cases of misconduct, it does – as far as we know – not demand any form of ex ante notification as required under SSR. There is no indication that the absence of an ex ante notification requirement would have effected the integrity and efficiency of the U.S. securities markets in a negative way.

In the light of the arguments presented above, we therefore emphatically urge ESMA to consider to include in its advice a proposal to drop the burdensome and unnecessary (since potential misconduct can always only be detected and sanctioned "ex post") current ISIN by ISIN, 30 days in advance notification requirement. If ESMA should find this proposal unfeasible, it should at least consider the 30 days in advance periode to be significantly shortened and to replace the "ISIN by ISIN" approach by a more practical procedure, e.g. based on certain market segments.

Missing Question on Point 3.4 "Long term bans: scope of ESMA Opinion:

The CP does not contain a dedicated question with respect to the amendments to SSR proposed under Point 3.4.3. To the extent that ESMA proposes that "the relevant Opinion will mainly rely on the factual events and representations outlined by the RCA in its notification and will consider further sources only when available and their assessment is compatible with the short deadline" (paragraph 113), one might ask, which purpose ESMA's Opinion should have if it is more or less just an assessment/second opinion based on the notification presented by the RCA? On the other hand, that ESMA cannot provide an in dept analysis which is – under reasonable expectations – is not compatible with the 24 hours deadline, is just stating the obvious. We would suggest that the 24 hours deadline for an immediate urgent Opinion by ESMA should be supplemented by the option to issue a more comprehensive revised Opinion within a 48 or 72 hours deadline.

<ESMA_QUESTION_SSRR_0>

Q1 Does ESMA's analysis confirm the observation that you made in your perimeter of competency? Please provide data to support your views?

<ESMA_QUESTION_SSRR_1>
We remain of the opinion that any short selling bans, whether short or long term, should be handled extremely carefully and should remain the "ultima ratio" of regulatory intervention. In this context, it must be remembered that (except form obvious cases of market abuse) it is

extremely difficult – if not impossible – for regulators to identify an aledged misspricing caused by short selling. Accordingly, the risk of fundamentally wrong regulatory decisions regarding imposed short selling bans, which might have very severe negative effects – as could be observed e.g. in the case of "Wirecard" – cannot be ruled out.
<ESMA_QUESTION_SSRR_1>

Q2 What are your views on the proposed clarifications?

<ESMA_QUESTION_SSRR_2>
We have no objections with respect to the proposed clarifications.
<ESMA_QUESTION_SSRR_2>

Q3 Do you agree with the proposed clarification?

<ESMA_QUESTION_SSRR_3>
While we do not see a need for clarification in this context, since the wording "or" to our understanding already allows the measures contained in point (a) and (b) of Article 20(2) SSR to be applied either on a single or combined basis, we do not mind, if ESMA seeks further elucidation at this point.
<ESMA_QUESTION_SSRR_3>

Q4 What are your views regarding the exclusion or, alternatively, a percentage–based weighting approach, for indices, baskets and ETFs in the context of long – term bans?

<ESMA_QUESTION_SSRR_4>
We widely agree with ESMA's analysis at this point and support the exclusion of indices, baskets and ETFs from the scope of long term bans. We are not in favour of an alternative percentage based weighting approach because of the disproportionate administrative requirements with respect to calculating and since we fully agree with ESMA's assessment that "those instruments would less likely be used by market partikipants to take an NSP in a single share". In this respect, any weighting based approach for indices, baskets and ETFs would be generally speaking a costly and impractical "solution, is looking for a problem" measure.
<ESMA_QUESTION_SSRR_4>

Q5 Do you agree with the proposed alignment of the conditions to adopt measures under Article 20 and Article 28 of SSR?

<ESMA_QUESTION_SSRR_5>
To our understanding, the intervention powers conferred to ESMA by Article 28 of SSR contain some element of subsidiarity, which is crucial for the understanding of the legislatitive intent and which we think is adequately reflected by the current wording of SSR. Furthermore, the different wording with respect to events which potentially can trigger interventions by RCAs and by ESMA are futher elaborated and explained in Article 24 of Delegated Regulation 918/2012. Overall, we think that the current differentiation is adequate and does not give rise to regulatory concern.
<ESMA_QUESTION_SSRR_5>

Q6 Do you agree with the proposed amendments to Article 24 of Delegated Regulation 918/2012?

<ESMA_QUESTION_SSRR_6>
We are not in favour of the proposed amendmets to Article 24 of Delegated Regulation 918/2012; please see also our answer to question 5.
<ESMA_QUESTION_SSRR_6>

Q7 Do you agree with the proposed amendments to the SSR and, more specifically, the mediation procedure under Article 23 of SSR?

<ESMA_QUESTION_SSRR_7>
The only comment we have in this context is that whenever a single RCA decides to implement a ban which needs to be observed throughout the Union, the decision should be published throughout the Union in an easily accessible way. While currently it is foreseen that ESMA immediately informs the competent authorities of the home Member States of venues which trade the same instrument (Article 23, Paragraph 4), we think it would be worthwhile considering to authorize ESMA to made such information available to the market in a centralised and harmonised way (similar to the proposal discussed in question 17).
<ESMA_QUESTION_SSRR_7>

Q8 What are your views on ESMA's proposal to include subscription rights in the calculation of NSPs in shares?

<ESMA_QUESTION_SSRR_8>
We strongly encourage the future inclusion of subscription rights in the calculation of NSPs in shares by a change to the Level 1 text of the SSR (Article 3(4)) together with an amendment to Article 7(b) of Delegated Regulation 918/2012 as proposed by ESMA (CP Paragraph 167).

Such an inclusion not only seems appropriate with respect to the economic similarities to call options as ESMA rightly states in CP Paragraph 166, but it would most likely foster the trading in subscription rights, e.g. with respect to arbitrage between subscription rights and the referring shares which could contribute to more efficient markets by increasing price quality. We think that not only professional but also retail investors could profit from such a step which ceteris paribus makes trading in subscription rights more attractive and increase the economic value of these instruments.

This would also help to avoid undesirable situations like mass sell-offs of subscription rights, not executed by (often retail) investors (respectively their custodians on their behalf) at the last day of the subscription periode, often resulting in significant oversupply and double digit price reductions compared to the theoretic inner value of those subscription rights. By allowing the inclusion of subscription rights in the calculation of NSPs, among other effects, an arbitrage between the subscription rights and the referring shares would be incouraged, resulting in fairer prices and consequently also better returns also for retail investors which do not want to execute but to sell those subscription rights.

However, since an intended capital increase might fail under certain conditions, an investor who has sold the shares short while covering the short position with subscription rights might find himself unintendedly with a "positive" NSP and unable to deliver the sold shares (which

he expected to receive by executing the subscription rights) in time. Therefore, it should be clarified that such an unintended NSP,resulting from the non-execution of the capital increase, would not be regarded as a breach of the prohibition of naked short sales under SSR.
<ESMA_QUESTION_SSRR_8>

Q9 Do you agree with this proposal to reinforce the third-party's commitment? If not, please elaborate. If yes, would you either (A) keep the three types of locate arrangements, but increase the level of commitment of the third party to a firm commitment for all types of arrangements, or (B) simplify the regime to keep only one type of firm locate arrangement?

<ESMA_QUESTION_SSRR_9>
In this context, we think that different aspects need to be taken into account. On the one hand, we fully agree that locate agreements must not be seen a pure alibi instrument and anecdotal evidence received from bwf members with significant market making business and long years of experience in this field support the impression that certain market participants do not undertake sufficient effort to be able to deliver shares they sold in time. This might also be influenced by the circumstance that non-compliance up to now is associated only with very limited economic and legal risk (e.g. suspicious activities reports usually remain ineffective when any kind of locate agreement can be presented). Therefore, our members which are engaged in market making activities (for a significant number of them, it is still there sole or most important business) are particularly concerned about missing settlement discipline, which might also arise from non enforceable locate agreements, in the light of the upcoming penalty fees for settlement fails under CSDR which are supposed to e introduced next year.Therefore, we agree that the reliability of locate agreements should be increased.

On the other hand, it must be notetd that the concept of "reasonable expectation" (which also can be found in in US Regulation SHO Rule 203 as ESMA expressly mentioned in CP Paragraph 171) was certainly chosen with care and from an educated perspective with respect to the practical limits of any collateral-managagement arrangement in the light of the complexity of securities settlement chains and the resulting high technical requirements of collateral-management techniques such es securities lending in the case of SSR locate provisions. In other words, there is no such thing as an "absolute certainty" with respect to securities settlement. E.g. a "locate agent" might be unable to deliver a certain share which he lended out before and which was not returned in time because of a technical fail.

Therefore, those bwf member firms who either are dependend on the availability of locate agreements at competitive prices (e.g. in the course of executing client orders on own account as described in our introductory remarks) or firms who act as locate agents themselves (which might be custodians or investment firms) have rightfully pointed out that any tightening the requirements for and the enforceability of locate agreements still must contain an element of proportion and a realistic assessment of feasibility. Otherwise, there is a risk that the pricing of locate agreements might become prohibitive for many business models and that the firms which are able and willing to act as locate agents might unintendedly diminish significantly.

In balancing these two aspects, we think that a practical and realistic way forward could be a more detailed clarification of the concept of "reasonable expectation" and a stricter enforceability where noncompliance of the locate agent verifiably results from neglective behaviour and poor business practices. We think that this could be more helpful than

demanding a comprehensive "firm commitment" in all cases, no matter whether it can be realistically achieved or not.

In this context, we are rather indetermined whether the different types of locate arrangements should be kept or merged into a single standard, which would have to be flexible enough to serve for different purposes.
<ESMA_QUESTION_SSRR_9>

Q10 Do you agree with this introducing a five-year-long record-keeping obligation for locate arrangements? If not, please justify your answer.

<ESMA_QUESTION_SSRR_10>
We are rather sceptical about the proposed five-year-long record keeping obligation for locate arrangements, which would create a significant additional administrative burden and just another "data cemetery" without clear benefit. We think it would be more purposeful, if firms would be required to document significant breaches of obligations under a locate arrangement, which give reason to the assumption that they might result from neglect or inappropriate business practices on the side of the locate agent and that firms will be required to change their locate agent in the case of repeated unreliability.
<ESMA_QUESTION_SSRR_10>

Q11 Do you agree with reinforcing and harmonising sanctions for "naked short selling" along the proposed lines? If not, please justify your answer.

<ESMA_QUESTION_SSRR_11>
While we have some understanding for the regulatory attempt to harmonize sanctions and penalties, the practical problem will be the definition of an appropriate calibration. It also should be taken into account that the risk of penalty fees to be paid most likely will be priced into the product "locate agreement" with the potential effect that the economic cost will be shouldered – at least to some extent – by the locate agent's clients. Therefore, we think that the concept of "administrative sanctions/measures" as proposed in CP Paragraph 206 would be more appropriate than relying primarily on pecuniary fines. Another serious problem in the complex field of collateral management is the determination of culpability. As mentioned before "reasonable expectation" does and cannot provide absolute certainty.
<ESMA_QUESTION_SSRR_11>

Q12 Do you consider that shares with only 40% of their turnover traded in a EU trading venue should remain subject to the full set of SSR obligations?

<ESMA_QUESTION_SSRR_12>
We are clearly opposed to the proposal that shares with only 40% of their turnover traded in EU trading venues should become (the wording "remain" in the question seems to be incorrect since the current threshold is 50%) subject to the full set of SSR obligations, not only because a significant number of bwf member firms are market makers in often thousands of third country shares at the various securities exchanges throughout Germany and would be strongly negatively affected by an increased administrative burden (numerous additional applications for new market maker exemptions) and temporary loss of revenue (until the new exemptions are granted) but also because we think that there is not sufficient empirical evidence which would make such a far reaching intervention appear appropriate and

proportionate. Even more since ESMA itself concludes "that the current Article 16 of SSR still permits an adequate monitoring of the relevant shares in question (CP Paragraph 226).

An aproximate estimate conducted by a bwf member firm, which assumes a normal distribution of trading turnover across shares, suggests that lowering the threshold to be included in the list of exempted shares from 50% to 40% of turnover within the EU might result in 20% to 25% more shares being subject to the full set of SSR obligations. The ESMA negative list, which currently contains 23,045 shares, therefore might shrink by an estimate of 4,600 to 5,800 shares in the event of reducing the threshold of trading within the EU to 40% (respectively increasing the "principle venue" requirements for the trading of shares in a third country to 60%).

Accordingly, firms which are currently market makers in the affected shares would have to

a) apply for market making exemptions in the affected shares
b) suspend trading (suspension of trading on the stock exchanges and as systematic internalisers), which would result in a loss of liquidity on the markets, until such exemptions have been granted (confirmation that the notifications are not rejected) by the national competent authority
c) halt short sales for hedging transactions in the affected shares, e.g. for sold own derivative products, which could entail a delta risk.

Aside from the additional costs associated with papering requirements it is again the 30 days ex ante notification requirement (see also our introductory remarks) which would cause significant negative economic effects, not only for market makers but potentially also for – in particular retail – investors, since market maker facilitated trading is the most significant form of trading for the shares in question, since basis market liquidity is usualy too low to enable an orderly trading. Therefore, in the case that ESMA should continue to advocate the proposed changes to the thresholds and shares should be exempt from the negative list in the future, the legislative provision should necessarily contain a waiver of the 30 days ex ante notification requirement for the shares in question during the transition process, in order to – at least in part – mitigate avoidable negative market-structural effects.

However, once again, we emphatically urge ESMA not to take the proposal of a significantly shrinked negative list for third country shares further. In our view, ESMA does not provide sufficient justification for such an intervention. Our members in their capacity as a market maker in numerous third-country shares, have not obtained any concrete evidence which would support the assumption that a reduction of the ESMA negative list would reduce systemic risks, market abusive behaviour or disorderly trading conditions.

Should the intended ESMA measure be related to so-called meme shares, we also do not consider the proposed measure to be fit for purpose. In the contrary, the cases of so-called meme shares such as Gamestop have shown that trading volumes in third-country shares on EU trading venues can increase so abruptly that a sufficiently timely reaction by the competent authorities with the current regulatory toolbox is realistically not possible.

Therefore, the right way forward does not seem to be to remove more shares from the ESMA negative list but to enable ESMA to selectively apply SSR provisions – in particular temporary short selling bans for non market makers (it must remembered that the market

maker shorts the share to provide liquidity to the market and to execute buy orders from the market) – also to shares on the negative list under clearly defined very exceptional market conitions.

Last ut not least, ESMA completely overlooks the additional administrative burden and knock-on effects with respect to the CSDR framework in particular regarding the enhanced settlement discipline regime, which – in full or with ajustments recently proposed by ESMA – will be entering into force by February 2022. In this context, it must be remembered that the SSR ESMA negative list is also the basis for the exemption under Art. 7 (13) CSDR with regard to penalty payments in the case of settlement fails (with the risk of fails – not surprisingly – being significantly higher for shares with their main pool of liquidity outside the Union). This is another reason why we consider proposed reduction of the EDMA negative list to be highly counterproductive.
<ESMA_QUESTION_SSRR_12>

Q13 Do you consider that NCAs should take any other qualitative but specific parameter into account in the identification of the shares subject to the full set of SSR obligations even if they are more heavily traded in a third-country venue? If yes, please elaborate

<ESMA_QUESTION_SSRR_13>
Please see our answer to question 12; we could imagine that under extremely exceptional market conditions SSR measures, in particular temporary short sale bans for non market makers could als be applied to shares on the otherwise "negative" list.

However for the question of inclusion in the negative list, we think that turnover is a practical, easy to understand and measure and sufficiently reliable measure and that the general methodology for in-/exclusion from the list should not be uneccessarily complicated.
<ESMA_QUESTION_SSRR_13>

Q14 Would you modify the threshold for the public disclosure of significant NSPs in shares? If yes, at which level would you set it out? Please justify your answer, if possible, with quantitative data.

<ESMA_QUESTION_SSRR_14>
First of all, we fully agree with the analysis provided in CP Paragraph 233 which convincingly demonstrates that disclosure requirements are a double-edged sword (band-wagon effects, discouragement of information gathering exercises, free-riding options etc.) and that therefore higher disclosur obligations are not necessarily preferable from a regulatory point of view (which might be one reason why there is no obligation to disclose NSPs in the U.S. as ESMA has noted in CP Paragraph 240).

We would also like to point out that one problem which was never addressed lies in the fact that homougenous quantitative publication thresholds, independend from the market capitalisation, might have quite different accentuated effects on small (SME issuers) and large caps (blue-chips).

This said, we agree with ESMA's preliminary conclusion that the current 0,5% threshold "provides a good compromise between transparency to the market and market efficiency" (CP

Paragraph 255) and therefore should remain unchanged (in particular, it should not be lowered).
<ESMA_QUESTION_SSRR_14>

Q15 Would you agree with the publication of anonymised aggregated NSPs by issuer on a regular basis? If yes, which would be the adequate periodicity for that publication?

<ESMA_QUESTION_SSRR_15>
We have no unified consolidated view on the pros and cons of the publication of anonymised aggregated NSPs by issuer on a regular basis. However, what can be said is that if such an information is made public, it shoud be done in a timely manner and it is paramount to carefully verify the accuracy of such data.
<ESMA_QUESTION_SSRR_15>

Q16 Have you detected problems in the identification of the issued share capital to fulfil the SSR notification/publication obligations? If yes, please describe and indicate how would you solve those issues.

<ESMA_QUESTION_SSRR_16>
We are not aware of practical problems related to the issue in question.
<ESMA_QUESTION_SSRR_16>

Q17 Do you agree with the establishment of a centralised notification and publication system for natural and legal persons to communicate their NSPs? In your view, which would be the benefits or shortcomings this system would bring? Please explain.

<ESMA_QUESTION_SSRR_17>
While we are not determined regarding the usefulness of the publication of aggregated NSPs by issuer (see our answer to question 15), we would see merits in a centralized “one stop shopping” solution, in case that a political decision would opt for such a publication.
<ESMA_QUESTION_SSRR_17>