FIA EPTA
EUROPEAN PRINCIPAL TRADERS ASSOCIATION

Date: 3 March 2023

FIA EPTA response to the HM Treasury Call for Evidence on the Short Selling Regulation review

Introduction	The European Principal Traders Association (FIA EPTA) represents Europe's leading Principal Trading Firms. Our members are independent market makers and providers of liquidity and risk-transfer for markets and end-investors across Europe. FIA EPTA works constructively with policy-makers, regulators and other market stakeholders to ensure efficient, resilient and trusted financial markets in Europe. The FIA EPTA welcomes the opportunity to respond to the HM Treasury (HMT) Call for Evidence on the Short Selling Regulation Review.

Chapter 1: Introduction

Box 1A Questions:	**FIA EPTA Response:**
1. Do you agree that the activity of short selling plays an important role in the efficient functioning of financial markets?	FIA EPTA wholeheartedly support HMT's statements regarding the important role short selling plays in the efficient functioning of financial markets. As market makers and liquidity providers our members contribute to efficient, resilient, and high-quality secondary markets that serve the investment and risk management needs of end-investors and companies throughout Europe. FIA EPTA members play a crucial role in financial markets, providing liquidity to end investors and companies on an ongoing basis including during times of

	market stress. Short selling brings liquidity and acts as an important risk management tool, particularly in volatile market conditions.
2. Do you think that the activity of short selling should be regulated in the UK? Please briefly explain why or why not.	FIA EPTA believe that some aspects of the Short Selling Regulation ("SSR") have aided UK financial market stability. In particular, we believe the cover requirements have contributed to settlement efficiencies and have shaped standard market practices around locates. However, there are other aspects of the SSR that FIA EPTA considers warrant significant reform. In particular: • the **obligation to report net short positions to the FCA** is disproportionately burdensome on market participants when compared to the ostensible benefit derived by the FCA from the information disclosed. This regime should be reformed to support automation and only require reporting above a threshold that gives a meaningful indication of directional short selling strategies; • the **Emergency Intervention Powers** contribute to market uncertainty and undermine confidence particularly when markets are volatile, as participants anticipate the possibility short sale bans will be imposed, preventing them from engaging in crucial risk management and liquidity provision activities. FIA EPTA has found short sale bans to cause increased transaction costs and volatility and reduced liquidity and thus support removal of the Emergency Intervention Powers; and • whilst FIA EPTA appreciate recognition of the role market makers play in facilitating stable functioning markets, **the Market Maker Exemption** should be adapted so it is sufficiently flexible and efficient to enable market makers to be responsive to changing markets rather than hampered by an administratively burdensome approval process.
3. Do you think the SSR puts a proportionate regulatory burden on short sellers in the UK market? Please briefly set out why.	FIA EPTA believe certain aspects of the SSR impose a disproportionate burden on market participants. **Position Reporting to the FCA** The obligation to report Net Short Positions (NSPs) to the FCA at 0.1% imposes a significant operational compliance burden on market participants and seems disproportionate when compared to the apparent benefit derived from the reported data. This is because: • There is no single source of information for calculating total issued share capital for determining the denominator when calculating net short positions. Consequently, market participants must conduct manual checks of a number of different sources to determine the

	denominator and to ensure position reporting is accurate and in order to meet the reporting deadline; • There is a lack of certainty over instruments in scope for the reporting obligation, for example because of inconsistent written guidance and the list of exempted shares is not aligned with UK FIRDS; and • The manual entry of NSPs is highly inefficient from a data input perspective in that it requires each single NSP to be made on an individual basis. We provide further detail on these impacts and suggested means of addressing them in our response to question 12, below. **The Market Maker Exemption** Whilst the Market Maker Exemption exempts those relying upon it from certain obligations under the SSR, the instrument-by-instrument approach to the exemption is overly complex and burdensome for market participants. FIA EPTA appreciates the recognition of the important role market makers play in facilitating liquidity provision and risk management implicit in the Market Maker Exemption. However, we believe the way the exemption is framed and administered could be improved to alleviate that burden and make its operation more efficient. In particular, FIA EPTA support adopting a self-certification approach to the market maker exemption replacing the current instrument-by-instrument approval requirement. Please see our response to question 20 for further detail.
4. Are there aspects of the SSR which you consider to be essential for ensuring market stability and confidence in the activity of short selling?	In our view the Market Maker Exemption is critical to ensuring market stability as it enables market makers to engage in liquidity provision and risk management in a manner that supports stable efficient markets. For further detail, please see our response to question 20. We also believe the cover requirements contribute to settlement efficiencies. On the other hand, we consider the Emergency Intervention Powers undermine market confidence and that the imposition of short selling bans is damaging to financial markets. For further detail, please see our response to questions 21 and 22.
5. In your view would it be preferable to modify the existing SSR to reflect the UK	We believe there is a significant opportunity to improve market confidence and efficiency and to alleviate unnecessary operational burden as part of this review of the existing SSR. Whilst some

markets, but keep the core framework unchanged, or do you think there is a case for fundamental reform?	elements of the regulation work well, particularly the cover requirements, others would benefit from material changes, namely the position reporting to the FCA requirements and administration of the Market Maker Exemption. In the case of the FCA's Emergency Intervention Powers, we believe UK markets would benefit from these being removed altogether as short sale bans have been empirically proven to increase transaction costs, cause volatility and reduce liquidity.
6. Are there aspects of other jurisdictions' short selling regulations that you think operate better than the SSR?	No comment

Chapter 2: The Short Selling Regulation

Restrictions on 'uncovered' short selling

Box 2.A Questions:	**FIA EPTA response:**
7. Do you consider that uncovered short selling restrictions under the SSR are appropriate?	Yes, FIA EPTA members believe that the current restrictions on uncovered short sales in shares are appropriate. These clearly set out that a short sale position can only be entered into, in an instrument traded on a UK trading venue, where there is a reasonable expectation that that trade can be settled i.e., that the shares can be sourced by the selling party for the purposes of onward delivery to satisfy the terms of the trade. This can be done either by having borrowed, made an alternative provision to that effect, or there is an agreement to borrow or confirmation that a locate is available to be taken up by the selling party. The uncovered short selling restrictions are well established and integrated into market participants' normal procedures for trading shares. These embedded processes contribute to the timely and efficient settlement of shares.
8. Do you consider that current uncovered short selling restrictions are working effectively to reduce risks to settlement and the orderly functioning of the market, in particular current locate arrangements? What arrangements do you use and why are they effective?	Yes, FIA EPTA consider that the current uncovered short selling restrictions are working effectively to reduce risks to settlement and orderly functioning of the market. The current locate arrangements used by our members are fully integrated, robust automated processes. Daily locate approval files are sent by the individual locate providers early in the morning prior to the start of trading. These locate files are bespoke and based on a request from our members to receive specific information on locate availability for a specific list of securities. The files are automatically loaded into our members' trading systems and taken into account for all trading done through the day, with short selling prohibited above the approved locate level and an alert of such sent to both the impacted trader and the member's stock loan team. Dependent on need, the member's stock

	loan team can then work to potentially source an additional locate/borrow from a different lender if required. On the back of short selling, and in line with the approved locates, orders are then submitted to borrow the individual shares in a timely manner. Separately, our members receive ‘easy to find’ lists (also known as availability lists). Given the robust locates process above, these are now used purely to provide colour. Providers will include all securities they have available in these lists rather than being bespoke and so provide information on depth of availability across the board. FIA EPTA does not believe that it is necessary to introduce any measures to reinforce the third-party’s commitment (as recently proposed by ESMA in their 2021 Consultation on the SSR) as the current rules are fit for purpose. Whilst the settlement fails rate increased between December 2020 and March 2021, there is no evidence to directly link this to uncovered short selling or failure to comply with the locate rule. Settlement delays can occur for a variety of reasons on both long and short sales and, given the unique circumstances during that period with Covid-19 impacting not only market conditions but also restricted movement/lockdowns in place, clearing/settlement processing delays were to be expected. We consider the current regime to have worked smoothly to date and any change along these lines may lead to unintended consequences such as a rise in the cost of borrowing and could impact liquidity provision levels which would result in it having a detrimental effect on end-investors. In FIA EPTA’s opinion, the current ‘locate rule’ is sufficient to protect against ‘short ‘squeezes’ as the third parties, with whom our members interact, are guided by the actual borrow liquidity in the borrow market to confirm locates.
9. Is short selling activity causing settlement failures? Do current UK settlement discipline arrangements need to be changed to reduce the risk of short	FIA EPTA members do not believe that any further regulatory changes are required. The existing restrictions on uncovered short sales in shares, requiring borrows/locates to be sourced in advance of short selling, are sufficient to ensure a high level of settlement efficiency. In certain cases, there may be a delay in the delivery of the borrow resulting from a locate by a securities lender, however, this is no different to the usual potential for a borrow to fail for a short period of

selling causing settlement failures? What changes could be made and why?	time. The commitment of the securities lender is robust and, in our members' experience, transparent for the owners of the securities who are consenting for their securities to be used for short selling activities.

Position reporting to the FCA

Box 2.B Questions:	FIA EPTA response:
10. Should the FCA specifically monitor short selling?	Whilst FIA EPTA members appreciate regulators like to have data from a range of different reporting regimes available in order to monitor and understand market developments and the behaviour of market participants, we question the value of data gathered under the SSR in particular. The current reporting obligation at 0.1% is extremely burdensome and it is not currently evident to members that the information is of such value as to justify the considerable resource allocation required to ensure accurate and timely reporting in line with existing obligations. The manual nature of the current reporting mechanism increases the operational burden of the reporting obligation. We note that with the exception of the EU, no other jurisdictions currently require reporting of immaterial short positions. Members are supportive of increasing the reporting threshold to 0.5% so that fewer and only relatively material short positions are reported thereby reducing the administrative burden on firms whilst helping ensure that only position holders intending to take a material directional short position in shares are required to disclose. We do not believe this would materially diminish the value of the data available to the FCA given positions below this threshold do not represent a directional trading strategy.
11. Does the FCA monitoring of short selling help support market integrity and market confidence?	Further information on how this data is used would be welcomed by our members. As indicated in our response to question 10, it is unclear what the FCA is currently using the net short position data for. In order to understand why such a burdensome reporting regime is in place, additional transparency around the use and application of the data by the FCA would aid market participants in understanding the justification for these requirements. Consistent with the application of cost benefit analysis and assessing policy intervention, FIA EPTA support accountability in establishing

	the utility of the data derived from the reporting obligation. This benefit should be proportionate to the considerable burden imposed on firms in the interests of supporting the competitiveness of UK markets. Further detail on the operational burden of the position reporting requirements is set out in our response to Q12.
12. What are the costs and burdens for your firm for sending position reports to the FCA? Please provide any evidence. Are there specific position reporting requirements or arrangements that could be changed to alleviate the cost and burdens of reporting?	We note a number of operational challenges linked with the position reporting requirements which in combination make the existing regime extremely operationally burdensome for market participants to comply with. These include: **1. <u>Calculating total shares outstanding/ Timeframe for shares in issue update</u>** The UK short selling regime denominator includes treasury shares. However, information about the number of these in issue is not available from UK exchange data or major data vendors and thus it requires a manual process to ensure they are captured in the calculation. We note this differs from the regime applicable to disclosure of substantial shareholdings under DTR5. UK listed issuer are also able to publish updates to their shares in issue the morning after the effective date which entails another manual check to ensure information from these announcements is incorporated in the calculation. As a consequence of these two data issues, it is not possible to fully systematically generate NSP notifications making the reporting process manual and thus increasing the operational burden associated with compliance. We recommend the UK regime provides a "golden data source" for total shares outstanding to resolve these time consuming irregularities and to support accurate reporting. Other potential measures could include: • Aligning the approach to denominator calculation in respect of the substantial shareholding disclosure requirements under DTR5 and the SSR, and amend DTR to require that issuers provide the data in a timeframe that will enable accurate reporting under the SSR; • Pre-populating the submission portal with the denominator (such as is currently done in the Netherlands and Sweden) to eliminate altogether the need for market participants to calculate the denominator themselves; and

	• Providing clear guidance that incorrect filings due to inaccurate reference data provided by a large market provider would not result in a regulatory sanction, as long as it can be demonstrated that such a source is used. **2. <u>Scope of obligations (UK FIRDS/UK Exempt List</u>** There is a large number of instruments / issuers on UK FIRDS that are primarily traded outside the UK that have not been added to the UK list of exempted shares (UK Exempt List). The submission portal and lists are also not in sync – ISINs with an RCA UK and not on the UK Exempt List are sometimes not available on the portal while others are. When an issuer is exempted from the portal it is no longer possible to submit NSPs; however, many firms' reference data systems ingest and rely on the UK Exempt List to exclude issuers from alert generation. With the delay in adding issuers to the UK Exempt List there will be alerts that are generated systematically that then cannot be notified as it's not possible to submit NSPs. It would be helpful if the authorities are able to ensure that the UK Exempt List is updated in a timely manner to close the gap between the list and the FCA portal and reduce the unnecessary and manual burden on market participants making or reviewing NSPs for issuers out of scope of reporting requirements. As an alternative, FIA EPTA propose: • Removal of the UK Exempt List altogether (see also our response to question 24). If the primary trading venue for the instrument is not in the UK, then FCA FIRDS RCA should not be set to UK. If this field is used for other purposes, then we would suggest that a new field be created in FCA FIRDS for Short Reporting RCA and amend that to UK or ex-UK. • If the UK Exempt List is to remain, we recommend that it should be more regularly maintained and updated, and be available via file transfer. Currently the Exempt List has to be downloaded as a spreadsheet which creates further issues regarding manual processing. The submission portal should also use the same source data from the lists to bring it in alignment with the UK Exempt List. **3. <u>Submission process (manual entry of NSPs)</u>** The current portal through which NSPs are submitted requires manual submission of each NSP on an individual basis. This is inefficient and burdensome for reporting entities. The lower 0.1% NSP

	reporting threshold has materially increased the number of filings that are made by market participants compared to when the threshold was at 0.2%. In addition, the registration process for new reporting entities or setting up new staff to make reports is burdensome and inefficient, with a request needing to be raised at each individual and entity level, without the ability for an individual to submit a request for a number of entities at the same time. FIA EPTA believe enabling market participants to file all position reports through an automated process would materially reduce the operational burden associated with this reporting obligation. This could involve using a point-to-point file transfer (via SOAP) which is used by the BaFin for German filings, or a similar mechanism to that used for submitting long shareholding disclosure reports under DTR5, which enables uploading a spreadsheet with data common to a number of different filings (as used for chain of control information for DTR5 notifications).
13. Do you think the current reporting threshold and increments are set at the appropriate level? Do you think there are any benefits or risks associated with amending the current threshold? In particular, would you support reverting the threshold to 0.2%? Is 0.2% still too small?	The current reporting obligation of 0.1% is extremely burdensome and it is not currently evident to members that the information is of such value as to justify the considerable resource allocation required to ensure accurate and timely reporting in line with existing obligations. We would caution against assuming that short sale position disclosures are an accurate reflection of a short sale directional strategy particularly where the disclosure thresholds are set at such low thresholds (i.e. starting at 0.1% or at the previous threshold of 0.2%). There are various reasons for our view: ● Disclosures exclude intraday activity and only reflect a snapshot of positions as at midnight on the previous day; ● Disclosures give a snapshot of positions which are aggregated across multiple product types - for example, including ETFs and index products - such that not all short exposures reported are due to short selling in the shares themselves but will often be mixed with index products (ETFs, Index futures etc). A market participant reporting a short position of 0.1% in a particular share may not be an indication that the market participant is seeking a short delta in the share; and

	• If the FCA is using the data to identify market abuse, we would question whether a participant engaged in abusive behaviors would flag this activity via submitting short disclosures. We would expect this kind of behaviour to be picked up in market surveillances and/or transaction reporting. FIA EPTA members would support a material increase in the disclosure threshold to 0.5% which would alleviate some of the burden associated with the existing reporting regime.
14. Are there other adjustments to the reporting requirements which you would suggest?	The reporting deadline is currently 3.30pm UK time. Unless there is a specific reason for this, we would ask that the deadline is changed to a T+1 basis so that reports need to be submitted before the end of the following day. Often UK entities need to wait for other offices (particularly in the US) to come on stream in order to verify certain position reports. Further, as discussed above, current timeframes do not allow for issuer updates to be incorporated in reference data necessary for calculation of the denominator. Please also refer to our response at Q12, above.

Public disclosure

Box 2.C Questions:	**FIA EPTA response:**
15. Do you support the requirement to publicly disclose net short positions under the SSR? What would be the impact to your firm or the market if public disclosure requirements were to be removed?	Due to opposing views within the membership, FIA EPTA has chosen not to respond to the questions on the public disclosure regime.
16. How do you use public net short position disclosures and how does it support your firm's activity or the market?	Due to opposing views within the membership, FIA EPTA has chosen not to respond to the questions on the public disclosure regime.

17. Do the public disclosure requirements contribute to or create any unnecessary barriers to short selling? If yes, please provide details.	Due to opposing views within the membership, FIA EPTA has chosen not to respond to the questions on the public disclosure regime.
18. Are there public disclosure requirements that could be changed to remove any unnecessary barriers to short selling? For example, do the identities of the position holders needs to be disclosed and what would be the impact on your firm and the market from removing this?	Due to opposing views within the membership, FIA EPTA has chosen not to respond to the questions on the public disclosure regime.
19. Do you consider that public disclosure requirements could be improved to increase transparency to the market? What are your views on publishing a net aggregated positions report to supplement or replace current reporting arrangements?	Due to opposing views within the membership, FIA EPTA has chosen not to respond to the questions on the public disclosure regime.

Market Maker Exemption

Box 2.D Questions:	**FIA EPTA response:**
20. Do you think the current market maker exemption regime in the SSR functions efficiently? Are there aspects of the market maker exemption regime requirements or arrangements that could be changed to reduce burdens and improve its efficiency?	FIA EPTA members are supportive of the Market Maker Exemption and in it the recognition of the crucial role market makers play in providing liquidity during times of market stress. However, we believe the current market maker exemption regime does not operate efficiently and thus does not enable market makers to be responsive to market needs, particularly in times of crisis. By way of illustration, during market volatility of 2020 in the early period of the Covid-19 pandemic, approved market makers were able to step in to provide liquidity when many market participants were withdrawing from markets. This reduced volatility and spreads to the benefit of market participants more broadly.

	Self-certification to replace non-objection period: The current requirement that a market maker provide 30 days prior notice in advance of being able to rely on the exemption is unnecessarily onerous. Whilst the FCA effectively treat the 30 days as a non-objection period, it is not evident why such a lengthy time period is necessary given in many cases, the firms giving notice are already operating under the exemption having obtained FCA approval on at least one UK market. FIA EPTA note that in members' experience, some European regulators typically reply on the same or next day following notification. The 30 day notification period also creates complications in terms of market efficiency and stability. ISINs may change on less than 30 days notice, for example as a consequence of a corporate action. Market makers are forced to stop market making in these instruments until the relevant 30 day notification period has passed, resulting in liquidity disruption and greater volatility. Further, firms are required to submit the same evidential proof for each adjustment to the scope of their market making activities. For example, evidence of membership of the relevant exchange is required every time a firm gives notification of an intention to rely on the market maker exemption in a new ISIN. In addition, there is little value in the requirement to submit a list of ISINs, which is in most cases simply a list of liquid shares with little variation between firms seeking to rely on the exemption. It is not clear why this additional information is needed. **Alternative process:** FIA EPTA recommend that the current non-objection process be done away with and replaced by a more efficient and proportionate self-certification regime. Upon first seeking to rely on the Market Maker Exemption, an applicant would submit documentation evidencing trading venue membership, giving notice of intention to rely on the exemption. In relation to the proposed self-certification process, firms would be obliged to maintain a record of the ISINs in respect of which they rely on the Market Maker Exemption along with appropriate evidence supporting compliance with the requirements of the exemption. Firms would be required to make such records and evidence available to the FCA on request in a manner that facilitates full regulatory visibility of market making activities conducted under the exemption, enabling the FCA to challenge reliance on the exemption where appropriate.

	FIA EPTA believe this simplified approach would be more efficient for markets as there would be no disruption to market making activity, more efficient for firms as they would be able to conduct the relevant activity without delay and more efficient for the FCA as it would not have to process largely unnecessary approvals for incremental changes to the scope of firms' activities. We believe this approach is proportionate given the nature of the risk the existing approval process is seeking to address: that firms engaged in directional short selling strategies will be able to do so under the guise of the market maker exemption, given the established nature of the Market Maker Exemption in UK markets and that it is relatively straightforward to establish whether a firm is a market maker. **Application on group rather than legal entity basis:** Currently only legal entities that have membership to a UK trading venue can benefit from the UK Market Maker Exemption. Many group companies have legal entities that undertake market making or liquidity provision in in-scope instruments but who cannot avail themselves of the Market Maker Exemption due to the fact they are not members of a UK venue (albeit they satisfy the market making requirements of their home state). As a consequence, the current net short position reporting requirements mean that reports will include positions from those entities undertaking market making/liquidity provision activity. This creates a misleading impression of short selling activity and additional work for UK firms in terms of position disclosures on behalf of group entities. FIA EPTA would support extending availability of the Market Maker Exemption to group entities that are recognized market makers in their home state. **Update guidance on market making activity:** FIA EPTA members note that the FCA requires firms to take note of and generally follow the ESMA EU SSR Market Maker Guidelines, Q&A and similar publications when applying the UK SSR. The ESMA Market Maker guidelines set out a very specific definition of EU SSR market making. EPTA members would support moving away from a prescriptive approach to the definition of market making. We would instead suggest a simplified market making definition where firms whose principal business is the provision of liquidity should fall within the exemption, whilst those firms undertaking activity such as taking longer term directional positions or fundamental analysis unrelated to providing liquidity should not. This would better reflect the role of market makers who provide liquidity via a diverse range of strategies but which are all intrinsically linked to their market making function.

Emergency Intervention Powers

Box 2.E Questions:	FIA EPTA response:
21. Do you consider the FCA should have powers to intervene in the market in relation to short selling activity in exceptional circumstances? What would be the impact if short selling bans were to be removed under the UK regime?	FIA EPTA is of the view that short selling bans are harmful to the orderly functioning of markets. We note the unnecessary operational risks that were a consequence of short selling bans implemented inconsistently and with limited lead-time in 2020 in a number of EU member states. Moreover, we have previously observed that the potential for bans, associated with its impact on liquidity and hedging, is likely to reduce the attractiveness of UK financial markets. We would reiterate that the ability of regulated firms to use covered short-selling is an important mechanism to allow markets to ensure transparent and orderly pricing of assets. There is no empirical evidence that banning short-selling reduces market volatility. To the contrary, FIA EPTA believe short selling bans increase transaction costs, exacerbate volatility and negatively impact liquidity. We attach a study conducted by FIA EPTA members demonstrating these effects in the case of the French short selling ban in April 2020 at Appendix 1. FIA EPTA consider that there is no convincing evidence supporting the argument that short selling bans prevent equity price slides. In fact, there is clear evidence pointing to the contrary, suggesting that short selling bans can have detrimental effects on financial markets. Price declines during times of economic downturn are mainly driven by long-only investors selling their holdings. Short selling is often claimed to be depressing prices. Nonetheless, short sellers also need to cover their positions and ultimately close their positions out. In effect, short sellers are often the very few market participants that buy in times of economic downturn. This points to the important role that short selling has in providing market liquidity. From the perspective of market liquidity it is also critical to consider the role of short selling in market-neutral strategies, where short positions in related instruments are taken to hedge long positions that would otherwise not be retained. Again, this points to the unintended consequences of potential short sell bans; an increase in volatility and decrease in liquidity. Furthermore, FIA EPTA believes that long-term bans should only address entering into or increasing existing NSPs. Should all NSPs be included in such bans this would lead to further downward pressure on prices as long positions are unwound as they are no longer able to be effectively hedged.

	If the emergency intervention powers were to be removed from the UK Short Selling Regulation, FIA EPTA believe this would improve market confidence as there would no longer be the element of uncertainty over potential market intervention by the regulator during times of market turmoil. Market participants could thus proceed with efficient risk management practices without having to factor in the potential curtailment of a crucial risk management tool. Whilst FIA EPTA members appreciate the FCA's circumspection in its exercise of these powers to date, given short selling bans are demonstrably damaging to market conditions based on empirical evidence (see attached analysis), it is not clear why such powers are needed at all. To the contrary, the potential uncertainty and associated undermining of market confidence associated with retaining the emergency intervention powers outweighs any perceived potential benefit.
22. Do you think any changes could be made to increase the effectiveness of existing short selling bans?	FIA EPTA members support removing short selling bans altogether as they are disruptive and yield no discernable benefit. However, should such intervention power remain in the UK regime, we are of the view that it should be amended. To this end, any such short selling ban should only extend to increases of or the creation of new net short positions. The amended regime should also exempt from any short selling bans instruments such as indices, baskets and ETFs. FIA EPTA would also welcome publication of a list of instruments in scope for a given ban, to make sure that instruments that are not subject to the ban can continue trading and thereby increase legal certainty. Finally, application of any short selling ban should be subject to a greater uniformity of approach between relevant national competent authorities in order to avoid the creation of chaotic market conditions. Advance warning of any intended short selling ban should be provided to the market, along with empirical evidence establishing why the ban is required and the anticipated market impact. Comprehensive guidance regarding scope, treatment of related products and operation of the Market Maker Exemption should be provided in advance of the ban going into effect to enable firms to put in place appropriate controls in order to comply.

	The SSR currently provides that the Relevant Competent Authority has discretion to apply measures subject to exceptions, including in relation to market making activities[1]. FIA EPTA recommend that in all cases there should be an exception for market making activity, rather than leaving this to the discretion of the FCA. End-investors and companies count on market makers, to provide, on a continuous basis, two-sided quotes across a range of financial instruments. Investors use these products to protect themselves against financial risk and to risk manage their exposures against extreme price movements in fixed income, (sovereign and corporate) bond and equity markets. Short-sale bans make it very difficult, or even impossible, for investors to use such risk management products. Not having access to these products would increase market volatility and expose end-investors to even greater risk which causes financial instability.
23. Are there any alternative arrangements to short selling bans that could be put in place (including arrangements from other jurisdictions)?	FIA EPTA do not consider it necessary to implement a substitute for short selling bans. Market confidence would be better supported by less intervention.

Overseas Shares

Box 2.F Questions:	**FIA EPTA response:**
24. Do you consider that the current requirements and arrangements for overseas shares are effective? What changes could be made to improve the arrangements for overseas shares under the SSR? Could the overseas shares list be changed to a "positive" list of shares that are required to be reported/covered by market participants?	FIA EPTA members are supportive of a "positive" list of in-scope shares being published to facilitate legal certainty and operational efficiency. This would assist with addressing areas where it is not clear whether an instrument is in scope, such as in the cases mentioned in our response to question 12, above. If the UK Exempt List is to remain, we recommend that it should be available via file transfer. Currently the exempt list is not available via an electronic form and has to be downloaded as a spreadsheet. We note the exemptions provided by ESMA for EU Short Reporting only apply for 2 years and at the end of this year a number of instruments will come into scope for UK reporting, we encourage the UK SSR regime to resolve this in advance of expiry of the exemption.

[1] Article 20(3) Regulation (EU) No 236/2012

Other Considerations

Box 2.G Questions:	**FIA EPTA response:**
25. Please provide any further views on the SSR, including views on the arrangements relating to sovereign debt and sovereign credit default swaps.	FIA EPTA supports the inclusion of all instruments giving an economic exposure to in-scope shares being included in the net short positions calculation. Currently instruments giving a right to receive shares that have not yet been issued (mostly commonly in the form of subscription rights or certain convertible bonds) are excluded from the calculation - this leads to misleading short position disclosures by firms holding short positions in an equity whilst holding an offsetting long position in related convertible bonds or subscription rights. The current NSP calculation methodology is based on a 2013 ESMA Q&A which should be updated. Based on this Q&A, the current NSP calculation methodology distinguishes between convertible bonds that convert into existing shares (exchangeable bonds) and those that convert into to be issued shares, or where the conversion could be into either existing or newly issued shares at the discretion of the issuer. From an operational perspective this is extremely challenging to code into disclosure calculation systems and as mentioned above may result in short disclosures being made where there is no economic short position taken and the firm is risk flat, which is misleading to the issuer and market. In addition, such inclusion would also enable market participants to maintain delta neutral hedging between equity and convertible bond holdings in the event of a short sell ban. If these instruments are not included in the calculation of the relevant long position, this results in an increase in the NSP which is no longer permitted when a ban is in place thus precluding market participants from undertaking effective delta neutral hedging with respect to these instruments. Finally, further guidance on what instruments constitute "sovereign debt" would be welcomed, including regarding SPVs and bonds issued by regional/municipal authorities.

26. For firms operating in multiple jurisdictions, please provide views on the potential operational impact of changes to the UK short selling regime (e.g. IT changes).	FIA EPTA would welcome pragmatic meaningful change to the UK Short Selling regime, particularly removal of short selling bans and modification of the net short position disclosure to the FCA regime to alleviate the disproportionate burden associated with compliance. Whilst operational and technology changes may be required, we see this as a minor inconvenience when placed in the context of potentially more efficient and effective regulation supporting the growth, competitiveness and stability of UK financial markets.

Appendix 1
(Ref: Q21)

FIA EPTA

Analysis of the Short Sale Ban in France

23 April 2020

1 Introduction

Due to impact of COVID-19, on 17 March 2020, the AMF announced a short selling ban that covered 92 shares for 1 full day [2]. By the end of the trading day the ban had been widened to cover all shares that fall under the jurisdiction of the AMF and would be in effect until midnight 16 April 2020 [1]. On 15 April 2020 the ban was again extended, this time until midnight 18 May 2020 [3]. The purpose of the report is to assess the influence of this ban on market behaviour.

2 Data

Throughout this report we shall compare the behaviour of 6 different instruments, split into three pairs. Each pair contains a French instrument and a similar German instrument that is under no short sale restriction.

	France	Germany
Index	CAC	DAX
Large Cap Stock	Renault	BMW
Large Cap Stock (highly affected by COVID-19)	Air France	Lufthansa

Figure 1: Instruments for comparison

The instruments were chosen in order to gain a varied view of the market. The indices provide an overall picture, whilst BMW and Renault demonstrate the difference between two large, correlated stocks. Lufthansa and Air France were also added as airlines were particularly badly impacted by COVID-19. We collected daily close prices for each instrument starting from 1 January 2020 and all data is available upon request.

3 Effect on Market

The purpose of the short sell ban was to address the ”serious threat to market confidence and financial stability in France” [4]. We understand this to refer to extreme price movements (high volatility) and low liquidity (wide spreads). We assess the significance of the short selling prohibition on volatility in Section 3.1 and in Section 3.2 we look at the effect on spreads. Finally, in Section 3.3 we consider the impact on volumes.

3.1 Volatility

Volatility is the degree of variation of a trading price series over time. In financial markets, it is usually measured by the standard deviation of logarithmic returns [7, 9]. We use logarithmic returns instead of absolute returns to make comparison between instruments easier and we have chosen to use a 5-day Standard Deviation in order to observe the short-term behaviour better.

It is clear that the volatility of the instruments in each of the three graphs is highly correlated. In Figure 2 we see that Renault is historically slightly more volatile than BMW which is then magnified by the impact of COVID-19. There is no clear evidence that the introduction of the short sell ban has any significant effect on the volatility of Renault when compared to BMW.

In Figure 3 we see that the volatility of the DAX and CAC are almost identical throughout the period shown and the difference between them is unaffected by either COVID-19 or the short selling ban. Finally, in Figure 4 we again see no clear evidence that short sell ban reduced the volatility of Air France when compared with Lufthansa.

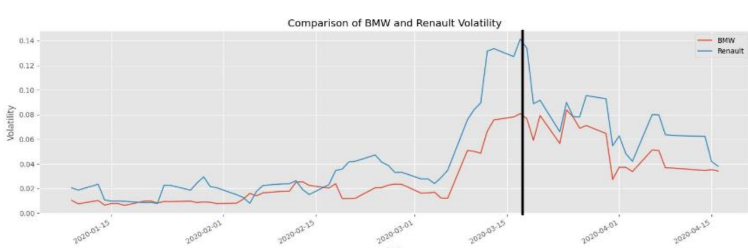

Figure 2: Comparison of the 5-day standard deviation of BMW and Renault logarithmic returns

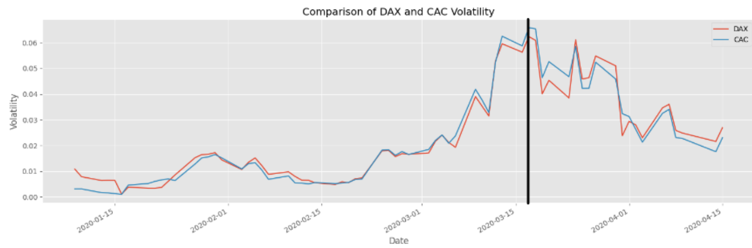

Figure 3: Comparison of the 5-day standard deviation of DAX and CAC logarithmic returns

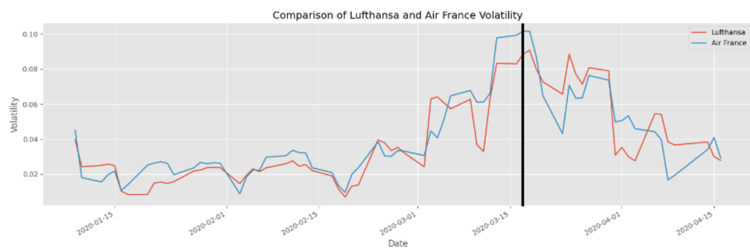

Figure 4: Comparison of the 5-day standard deviation of Lufthansa and Air France logarithmic returns

3.2 Spread

In [5], Gabrielsen, Marzo, and Zagaglia provide a comprehensive overview of methods for modelling and estimating the market liquidity of assets. They suggest that whilst the spread itself represents a measure of transaction costs, in modern markets this translates to a good proxy of liquidity. In order to compare across instruments we have normalized by dividing the spread by the mid-point.

We see similar patterns in both Figure 5 and 6. In both cases, the French stock had historically wider spreads, but only slightly. In the middle of March we see this change dramatically, with the French Stock having much wider spreads than its German equivalent. This suggests than the short selling restriction has reduced liquidity, ultimately resulting in a worse price for investors and higher costs.

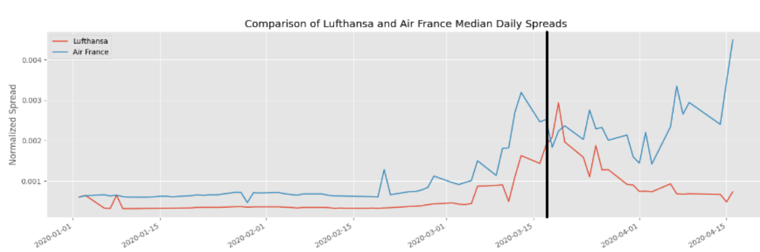

Figure 5: Comparison of Lufthansa and Air France Median Daily Spreads, normalized for price

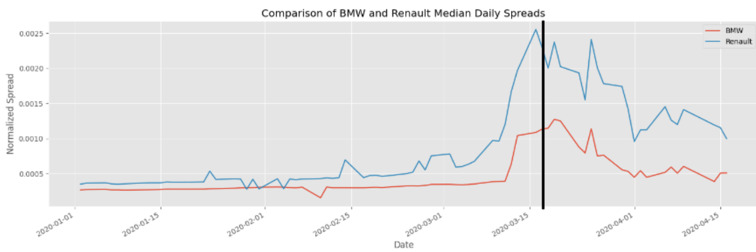

Figure 6: Comparison of BMW and Renault Median Daily Spreads, normalized for price

3.3 Volumes

In 2018, Bektas and Jafari illustrated that higher trading volumes make markets more credible, especially in the developed world [8]. Even in 1999, Johnson and Hart were able to show that theoretical 'low confidence' of traders greatly impacted market volume and price [6].

Figures 7 and 8 compare the daily traded volumes of Lufthansa/Air France and BMW/Renault. In both cases we can see that market volumes greatly reduced after March 20th. For the French instruments, volumes reduced past the stable point from earlier in the year.

Figures 9 and 10 compare the ratio of daily traded volume for Lufthansa/Air France and BMW/Renault. In both cases we see this ratio decrease after March 20th to the lowest levels this year. This suggests that the market confidence dropped more the French instruments than their German counterparts.

4 Conclusion

We looked at the effect of the French short selling ban on volatility, spread and volumes. We found that there was no significant impact on the volatility of French instruments compared to non-restricted German equivalents. When examining the spreads we found that, after the short selling ban, French stocks had much wider spreads than their German equivalent, resulting in higher costs for market participants. When looking at volumes, we found that French stocks dropped more than their German counterparts suggesting lower market confidence and credibility after the ban was introduced. It is our opinion that the short sale ban had no positive impact on the market. Instead, it prevents participants from trading effectively and pricing accurately. We strongly believe that markets are healthier without the introduction of short selling restrictions.

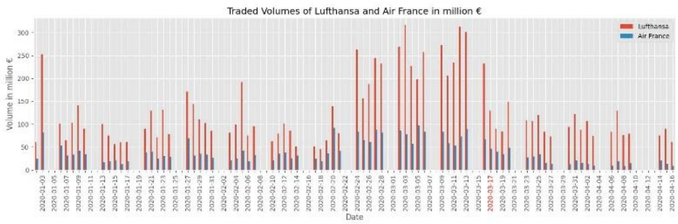

Figure 7: Comparison of Air France and Lufthansa Traded Volume in million €

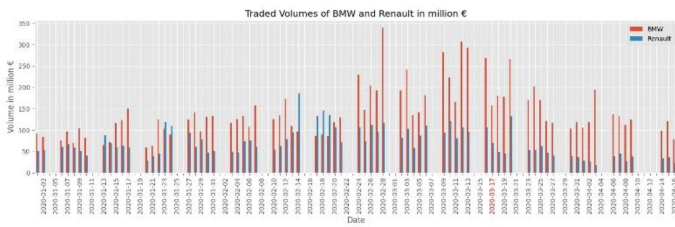

Figure 8: Comparison of Renault and BMW absolute Traded Volume in million €

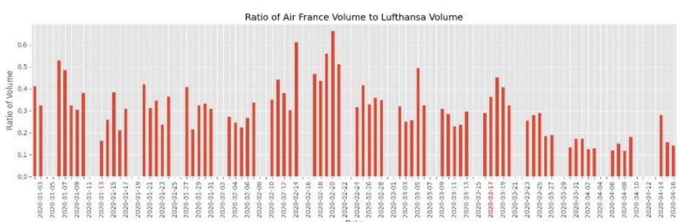

Figure 9: Daily ratio of Air France volume traded to Lufthansa volume traded

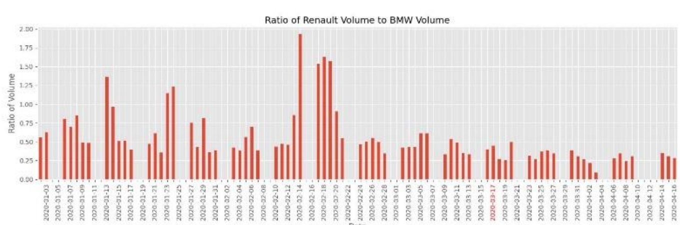

Figure 10: Daily ratio of Renault volume traded to BMW volume traded

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