From: [redacted]@aima.org>
Sent: 17 July 2015 15:21
To: [redacted]
Cc:
Subject: RE: Letter from AIMA on Greek short-selling actions

Thanks, [redacted] We are not making a representation on behalf of any individual firms who have been subject to enforcement action, but would welcome work from ESMA to:

1. Ensure that there is clarity as to when the SSR is applicable (particularly in the context of rights issues), noting our key contention that it is not applicable in situations where an entity sells a share that it already owns. It would be helpful to consider whether the approach of individual NCAs is compatible with their domestic securities ownership law and whether there are any differences between NCAs that should be highlighted (or corrected if necessary).

2. There is a secondary issue concerning the application of Article 12 in the context of rights issues, to the extent that an entity sells shares that it does not yet own. It would be helpful if ESMA could consider whether there is a common view across NCAs regarding the agreements/arrangements referred to under Article 12, i.e. what would evidence a reasonable expectation that settlement can be effected when due.

We appreciate that these are potentially significant questions and that it will take some time for ESMA to consider them properly.

We will also follow up with any information regarding securities ownership under the Greek legal framework.

Many thanks

[redacted]

The Alternative Investment Management Association Limited (AIMA)
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Tel: +44 (0)20 7822 8380
[redacted]
www.aima.org

From: [redacted]esma.europa.eu]
Sent: 17 July 2015 10:35
To: [redacted]
Cc: [redacted]
Subject: RE: Letter from AIMA on Greek short-selling actions

Dear [redacted]

Thanks for your letter. I understand you are asking for ESMA public guidance on the convergent application of SSR to the particular case of sales of shares "covered" by rights issues and that you are not complaining about a particular enforcement case of a National Competent Authority. Please confirm.

If so, it will take us some time to deal with this request, since it involves legal analysis from our side but also interaction with competent authorities, in order to arrive, if possible, to a convergent understanding. Given the dates we are in and the other deliveries that the committees in charge of these matters have, it may take us 2-3 months to produce a result on this. Just wanted to manage your expectations. I don't think a meeting will be necessary at this stage, since the case is clearly spelled out.

By the way, any information you can expand on the reference to "Greek legal commentators" with respect to when ownership occurs according to Greek law will be useful (court sentences, publications, etc.) , even if it is written in Greek (we are multilingual !).

Best regards.

[redacted]

From: [redacted]@aima.org]
Sent: 16 July 2015 10:52
To: [redacted]
Cc: [redacted]
Subject: Letter from AIMA on Greek short-selling actions

Dear [redacted]

Please find attached a letter from [redacted] setting out AIMA's concerns about the way in which the HCMC has applied the short selling regulation.

Once you have had a chance to digest this, we would very much welcome a call or meeting with you and/colleagues so that some of the managers involved can provide further colour on their activities and the actions of the HCMC. Please let me know if that would be possible.

Many thanks,

[redacted]
Director, Global Head of Markets Regulation

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Alternative Investment Management Association

[redacted]
European Securities and Markets Authority
CS 60747
103 rue de Grenelle
75345 Paris Cedex 07
France

By email: [redacted]

16 July 2015

Dear [redacted]

Application of the short-selling regulation to rights issues: need for guidance

The Alternative Investment Management Association[1] (AIMA; we) would like to take this opportunity to bring to the attention of the European Securities and Markets Authority (ESMA) our concerns regarding the interpretation by the Hellenic Capital Market Commission (HCMC) of Regulation (EU) No. 236/2012 on short selling and certain aspects of credit default swaps (the short-selling regulation; SSR), particularly in respect of the sale of long positions gained in the course of a rights issue.

AIMA has been an active participant in the policy debate regarding the design and implementation of the SSR and recognises the value inherent in a framework that helps to prevent the potential risk of settlement failure and volatility in European equity and sovereign debt markets.

We have, however, also stressed the need for consistency in national implementation of the SSR, illustrating the difficulties that have arisen as a consequence of the divergent approaches of individual national competent authorities (NCAs) when it comes to reporting requirements and temporary short-selling restrictions.[2] These inconsistencies are particularly challenging for firms who operate in multiple European markets, creating additional operational cost and legal uncertainty.

We write now to highlight a particular interpretative problem that has seen the SSR applied in situations where its provisions **are not applicable**, specifically where a participant sells a long position gained via a rights issue.

According to the SSR, restrictions on uncovered short-selling apply to the sale of a share or debt instrument, *"which the seller **does not own** at the time of entering into the agreement to sell"* (SSR Article 2(1)(b)). In the cases described in this letter, the entities in question sold shares that they owned following participation in a rights issue and yet were found by the HCMC to have breached the SSR due to outstanding procedural steps required on the part of the stock exchange to approve the admission to trading of the shares in question. These steps did not, however, have any bearing on the ownership of the shares, which had already been confirmed.

We do not believe that it was appropriate to apply the SSR in this context given that the sellers owned the shares and also highlight that the HCMC's approach is at odds with that of other NCAs. Among the many funds impacted were long-only UCITS funds that cannot undertake short-selling of

[1] Founded in 1990, the Alternative Investment Management Association (AIMA) is the global representative of the hedge fund industry. Our membership is corporate and comprises over 1,500 firms (with over 9,000 individual contacts) in more than 50 countries. Members include hedge fund managers, fund of hedge funds managers, prime brokers, legal and accounting firms, investors, fund administrators and independent fund directors. AIMA's manager members collectively manage more than $1.5 trillion in assets.

[2] See http://www.esma.europa.eu/system/files/aima-mfa_joint_response_to_esma_ssr_call_for_evidence_-_15_march_2013.pdf

any kind - underlining the fact that this seems to be a fundamental misapplication of the SSR. We also highlight shortcomings relating to how enforcement decisions were notified, which have further compounded the uncertainty faced by market participants.

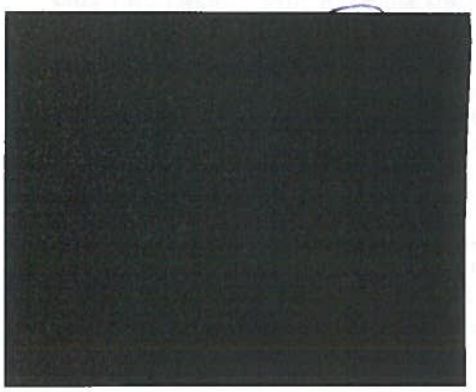
This letter therefore sets out to explain our view that the SSR should not have been applied in this context; we call on ESMA to offer a view on the analysis presented to ensure that the SSR is applied appropriately and to provide market participants with legal certainty regarding its application across the EU.

We also note that legal certainty has a direct bearing on the willingness of market participants to participate in rights issues. The latter provide a vital means for European issuers, including those experiencing financial difficulty, to raise new capital. In the absence of a clear understanding about the application of the SSR in such situations, it may in future be harder for European issuers to raise capital in this manner.

Annex 1 provides a full explanation of our concerns.

If you have questions on our submission, please don't hesitate to get in touch.

Yours sincerely,



Annex 1: Detailed comments

Interpretation of the SSR by the Hellenic Capital Markets Commission (HCMC)

In the period of March 2014 - May 2014, a number of Greek banks with listings on the Athens Stock Exchange (ATHEX) launched capital raising measures in the form of rights issues with a view to strengthening their financial soundness. Several AIMA members subscribed to these rights issues, receiving an allocation of shares. In the fund management context, this would typically involve an investment manager subscribing on behalf of one or more of the funds it manages. Having received formal confirmation from their brokers that they had received an allocation in the rights issue, a number of managers placed sell orders into the market for all or part of their allocations for settlement on the first day of trading.[3]

The HCMC subsequently argued that at the time the sell orders were placed the shares had not been officially admitted to trading and that, therefore, the managers could not be sure that settlement would occur (given that the exchange had yet to formally approve the admission to trading of the shares). It was the view of the HCMC that these sell orders constituted uncovered short sales and subsequently a number of market participants were fined by the HCMC for alleged breaches of the provisions of the SSR.

It is not our intention to comment on the individual cases in question. However, given the number of entities affected - we understand that some 150 trades by multiple fund managers were impacted - it appears to us that the actions taken by HCMC are not consistent with the SSR, or at least, with the SSR as it has been interpreted and applied in other Member States. Indeed, it is worth emphasising that some of the funds impacted were long-only UCITS funds which cannot undertake short-selling of any kind. Below we analyse the relevant provisions of the SSR with a view of contributing to an agreed understanding of the regulation.

Sales of positions allocated via a rights issue are not short sales

Article 12 of the SSR specifies the conditions under which an entity may enter into a short sale of a share admitted to trading on a trading venue. We note that the conditions apply only to sales classified under the SSR as 'short sales', not to all sales generally. The relevant definition of a 'short sale' is contained in Article 2(1)(b) of the SSR as follows: '*"short sale" in relation to a share or debt instrument means any sale of the share or debt instrument which the seller does not own at the time of entering into the agreement to sell...*'. The crucial distinction between a 'short sale' and a regular sale is whether the seller owns the shares at the time of entering the agreement to sell.

In the view of Greek legal commentators, a shareholder who has subscribed for (listed) shares and fully paid the relevant price and further has been allocated the respective amount of shares is the owner of these shares - as, in Greece, ownership of listed shares vests upon subscription, not registration in the Dematerialized Security System of the Athens Exchange ('DSS'). This is based on the understanding that registration in the DSS of listed shares issued by an already publicly traded company (e.g. following a share capital increase) is merely a formality.

[3] As a general observation, managers who subscribe to a rights issue may subsequently wish to sell shares shortly thereafter in order to:

- rebalance their positions in line with internal risk limits (noting that they might have received a larger allocation than they had anticipated) or to free up resources to pursue other trading opportunities;
- transfer positions between funds that they manage to ensure that the funds' exposures to the stock appropriately reflect the funds' strategies;
- to realise a profit associated with the stock's performance if the share price has reached the target level or to provide a stop-loss and limit the potential for losses arising from ongoing exposure to the stock; or
- to account for changes in a fund's target composition between the dates of subscription and allocation.

As regards the acquisition of shares through subscription in a share capital increase, the registration of the new shares to the DSS has the purpose of confirming rather than establishing the legal relationship. Pursuant to the provisions of the Greek limited companies law (2190/1920), rights arising from the new shares are acquired by the new shareholder at the time of fulfillment of the obligations undertaken via the subscription agreement (i.e. with the payment of the price of the new shares) provided that the issuer's resolution for the capital increase has been duly recorded with the company registry. The timing of rights is not related to when the new shares are credited to the DSS account of the investor.

Accordingly, our members firmly believe that sales of positions allocated via a rights issue in Greece do not constitute a 'short sale' for the purposes of Article 2 of the SSR, and thus the requirements of Article 12 of the SSR should not apply to the transaction.

This conclusion is further supported by the fact that the SSR was developed to "*...lay down a common regulatory framework with regard to the requirements and powers relating to short selling and credit default swaps...*" (Recital 2 of the SSR) in response to previous situations in which European financial regulators had "*acted due to concerns that at a time of considerable financial instability, short selling could aggravate the* ***downward spiral in the prices*** *of shares, notably in financial institutions, in a way which could ultimately threaten their viability and create systemic risks*" (Recital 1 of the SSR).

Selling an allocation received via a rights issue is not consistent with this notion of a transaction that explicitly seeks financial advantage from downward share price movement. Any profit which could be made from selling shares allocated in a rights issue would be reliant upon the market price of the relevant shares increasing and becoming greater than the subscription price in the period between the date of allocation and the sell order. Persons selling shares received in a rights issue could not profit from any "*downward spiral in the prices*" of those shares.

Settlement discipline

Clearly, it would not be appropriate for a shareholder, having subscribed to a rights issue, to sell their shares at any time, without considering if and when their shares would be available for settlement. However, we would suggest that settlement discipline relating to non short-sales is **not** addressed by the SSR. In relation to trades other than 'short' ones, any potential problems should be dealt with by the clearing and settlement rules of the particular regulated market and the Regulation (EU) No 909/2014 on improving securities settlement in the EU and on central securities depositories (the CSDR), once implemented.[4] Indeed, the ATHEX Clearing and Settlement Regulation includes a range of rules, tools and techniques for dealing with a potential failure/non-availability of the appropriate assets on settlement of trades,[5] with broad powers for the HCMC to impose fines.

Notwithstanding, if, hypothetically, the sell transaction in a rights issue were to be considered to be a 'short sale', Article 12 of the regulation would be relevant, addressing the conditions that demonstrate that settlement can be effected when it is due.

Article 12

Restrictions on uncovered short sales in shares

1. *A natural or legal person may enter into a short sale of a share admitted to trading on a trading venue only where one of the following conditions is fulfilled:*

   (a) the natural or legal person has borrowed the share or has made alternative provisions resulting in a similar legal effect;

[4] Available here: http://eur-lex.europa.eu/legal-content/EN/TXT/?qid=1410876555408&uri=CELEX:32014R0909
[5] See Section IV of the ATHEX Clearing and Settlement Regulation.

(b) the natural or legal person has entered into an agreement to borrow the share or has another absolutely enforceable claim under contract or property law to be transferred ownership of a corresponding number of securities of the same class so that settlement can be effected when it is due;

(c) the natural or legal person has an arrangement with a third party under which that third party has confirmed that the share has been located and has taken measures vis-à-vis third parties necessary for the natural or legal person to have a reasonable expectation that settlement can be effected when it is due.

The effect of Article 12(1)(b) is that a person may enter into a short sale of a share admitted to trading on a trading venue where that person "*has entered into an agreement to borrow the share or has an another absolutely enforceable claim under contract or property law to be transferred ownership of a corresponding number of securities of the same class so that settlement can be effected when it is due*".

Article 5(1) of EU Regulation 827/2012 (the "Short Selling Implementation Regulation") specifies the forms of agreement that may be regarded as an agreement to borrow or other enforceable claim for the purposes of Article 12(1)(b) of the SSR. Article 5(1)(d) of the Short Selling Implementation Regulation provides that an "*agreement or facility which is entered into prior to or at the same time as the short sale, of a predefined amount of specifically identified shares [...] which for the duration of the short sale, covers at least the number of shares [...] sold short by the natural or legal person and specifies a delivery or execution date that ensures settlement of the short sale can be effected when due*" will be an agreement or enforceable claim for the purpose of Article 12(1)(b) of the SSR.

Article 5(1)(f) of the Short Selling Implementation Regulation provides that "*agreements or claims which cover at least the number of shares [...] proposed to be sold short by the natural or legal person, entered into prior to or at the same time as the short sale, and specifying a delivery or an execution date that ensures settlement can be effected when due*" will be an agreement or enforceable claim for the purpose of Article 12(1)(b) of the Short Selling Regulation.

We further note that Article 5(1)(e) of the Short Selling Implementation Regulation provides that where a person "*is in possession of rights to subscribe for new shares of the same issuer and of the same class and covering at least the number of shares proposed to be sold short provided that the natural or legal person is entitled to receive the shares on or before settlement of the short sale*" he will be regarded as having an enforceable claim for the purposes of Article 12(1)(b) of the Short Selling Regulation.

It therefore appears to us that (if you accept that the sale of a share allocated in a rights issue may constitute a short sale, which we do not) the agreement between the broker and the manager relating to that allocation is likely to constitute either an agreement within Articles 5(1)(d) and 5(1)(f) of the Short Selling Regulation or, alternatively, an enforceable right within Article 5(1)(e).

We would also suggest that Article 12(1)(c) of the SSR provides additional support for this view. In the ordinary course of a rights issue, the issuer and brokers will make representations to managers which give rise "*to a reasonable expectation that settlement could be effected when due*". During the rights issue process, the issuer and brokers will typically publish indicative timetables and will subsequently provide further information about the timetable for the issue when providing confirmation of allocations to market participants. It is at least a market convention, if not a contractual requirement, that the issuer and brokers will inform persons to whom shares have been allocated if there is a possibility that the timetable will change.

Procedural aspects of notification of breaches

An additional observation that we would like to make in the context of the SSR is that the process for notifying market participants of alleged breaches of the regulation should ensure:

- That market participants are properly notified of supervisory decisions ahead of those decisions being publicised.
- That the method of notification is sufficiently reliable that notifications will be received by market participants ahead of publication of decisions.
- That the basis for appeal against decisions is properly set out.

Some of the actions taken by the HCMC - including making public statements about fines without having notified the impacted parties - were not in line with this.

Conclusion

According to the SSR, restrictions on uncovered short-selling apply to the sale of a share or debt instrument, "which the seller does not own at the time of entering into the agreement to sell" (SSR Article 2(1)(b)). In the cases described in this letter, the entities in question sold shares that they owned following participation in a rights issue and yet were found by the HCMC to have breached by the SSR due to outstanding procedural steps required to approve the admission to trading of the shares in question. We do not believe that it was appropriate to apply the SSR in this context and also highlight that the HCMC's approach is at odds with that of other NCAs. We call on ESMA to offer a view on the analysis presented to ensure that the SSR is applied appropriately and to provide market participants with legal certainty regarding its application across the EU.