

## **NAPF Response to the FSA's Discussion Paper 09/1: Short Selling**

### **1 About NAPF**

The NAPF is the leading voice of workplace pensions in the UK. We speak for 1,200 pension schemes with some 15 million members and assets of around £800 billion. NAPF members also include over 400 businesses providing essential services to the pensions sector. As major investors accounting for approximately one fifth of investment in the UK stock market, our members have a strong interest in the integrity and efficient functioning of the capital markets. We are grateful for the opportunity to reply to your Discussion Paper 09/1 on short selling.

### **2 General Considerations**

**2.1** Short selling plays an important role in the efficient functioning of the UK equity market, assisting the process of price discovery. We would oppose any blanket ban on short selling or other constraints on short selling to slow the process of price discovery (for example tick rules and circuit breakers). Furthermore, investment strategies like Absolute Return that seek to reduce market risk depend on the ability to go short. We recognise that short selling has on occasion been seen as undermining a company's share price, but the market impact of selling and the information that this provides to the market are in essence no different from that of buying. Well targeted disclosures will do much to limit the scope for abuse. It is essential that such disclosures should be well targeted and proportionate to the costs involved. In drawing up specific requirements the FSA will need to have concern for the availability of the data on which they are based and the requirements' practicability and ease of enforcement. We feel that the disclosure threshold should not be any lower than the 0.5 per cent proposed in the Discussion Paper.

**2.2** We would also encourage the FSA to work closely with overseas securities regulators, for example through IOSCO, towards securing a common approach to short selling internationally.

### **3 Answers to the specific questions in the Discussion Paper**

Our answers to the specific questions posed by the Discussion Paper are as follows:

*Q1 What are your views on the costs and benefits of a blanket short selling ban? Where possible please quantify.*

We agree with the conclusion reached at the end of Section 3 of the Discussion Paper, that short selling can generally be expected to increase market efficiency but can also have negative impacts (paragraph 3.20). A blanket ban on short selling would not be desirable; we believe that the negative impacts can generally be avoided by appropriate disclosure requirements.

*Q2 Do you agree that there should not be a ban on all forms of short selling?*

We agree.

*Q3 Do you think any further measures are necessary to deal with naked short selling. If so, what is required and why?*

We agree with the FSA's conclusion that no special restrictions are required on naked short selling. We also agree with the FSA that to the extent that non-delivery of stock remains an issue, this should be addressed through a tightening of the settlement rules.

*Q4 Should short selling of financial sector stocks be banned permanently?*

No.

*Q5 Do you agree that, subject to having a satisfactory disclosure regime, we should not ban short selling of the stocks of companies engaging in rights issues?*

We agree.

*Q6 Do you agree that we should not ban short selling by underwriters of rights issues (of the shares they are underwriting for the duration of the underwriting process)?*

We agree.

*Q7 Should we intervene to ban short selling on an emergency basis where necessary e.g. to combat market abuse and/or to maintain orderly markets?*

Evidence that the FSA's recent ban on selling financial sector stocks short had any positive effects is hard to find, even on the basis of the FSA's own analysis, and we believe that the FSA should only consider an emergency ban once it is clear that the extensive powers that it has to combat market abuse are not working.

*Q8 Do you agree that no additional circuit-breakers should be introduced?*

We agree.

*Q9 Do you agree that we should not introduce a tick rule?*

We agree.

*Q10 Are there any other direct constraints on short selling that you think ought to be considered? If so, please provide information regarding their costs and benefits.*

We cannot think of any direct constraints that the FSA should consider.

*Q11 Do you agree, in principle, that the benefits of transparency around short selling outweigh the costs?*

Depending upon the exact form of the requirements, we agree that the benefits of disclosure outweigh the costs. We would support appropriate, well targeted disclosures.

*Q12 If disclosure obligations are introduced, do you agree that those obligations should apply to all equities and their related instruments rather than be limited to certain sectors or companies?*

We agree, subject to the need for the FSA to specify more precisely what it means by 'related instruments'. In answering this question and the following ones we are assuming that they refer to derivative

instruments and other securities (like convertible bonds) whose price is likely to be correlated with the share price.

*Q13 Do you agree that the disclosure obligations should be limited to the stocks and related instruments of UK issuers?*

We would prefer uniform reporting requirements for all UK listed companies, whether or not the company is incorporated in the UK.

*Q14 Do you agree that the costs of introducing a regime based on disclosure of aggregate short positions would outweigh the benefits?*

Although we have no reason to doubt the accuracy of the cost benefit analysis in Annex 3, we remain concerned about the opportunities for abuse that can arise from the public disclosure of individual investors' short positions (for example, for trading against these positions). We also feel that disclosure of the positions of traders with a record of success could disrupt markets by providing opportunities for other traders to mimic their positions.

*Q15 Do you agree that benefits of public disclosure of significant short positions outweigh the costs?*

Depending upon the exact form of the requirements and subject to the concerns we express in our answer to Question 14 about opportunities for abuse, we agree that the benefits of public disclosure (as opposed to disclosure only to the regulator) outweigh the costs.

*Q16 Do you agree that an individual significant short position disclosure regime should be on a net basis?*

We agree.

*Q17 Do you agree that 0.50% would be an appropriate threshold for triggering disclosures under a net short position regime? If not, what alternative would you propose and what are your reasons for this figure?*

We feel that the threshold should not be any lower than the 0.50% proposed in the Discussion Paper.

*Q18 Do you agree that a banded approach to disclosure should apply in conjunction with a minimum threshold? If so, do you agree that such a banded approach should be based on bands of 0.10% of a company's issued share capital?*

We agree on the banded approach. Our initial assessment is that the proposed bands are appropriate.

*Q19 If long-term disclosure obligations are introduced, do you agree that market makers should be exempt from those obligations when they are acting in the capacity of a market maker? Do you also agree that this should be an absolute exemption?*

We agree that market makers should be exempt when acting in that capacity, and that this should be an absolute exemption. We also agree with the definition of market maker set out in paragraph 4.58.

*Q20 Do you agree that maintaining the current disclosure obligation of 0.25% of a company's issued share capital for rights issue situations is appropriate?*

We agree.

*Q21 Do you agree that the ongoing disclosure obligations should be the same as the general regime?*

We agree.

*Q22 Do you consider that any further measures are necessary in respect of CDS?*

No, we do not consider that further measures are necessary in respect of Credit Default Swaps.