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Committee of European Securities Regulators (CESR)
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Paris
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AFG RESPONSE TO CESR'S PROPOSAL TO EXTEND MAJOR SHAREHOLDING NOTIFICATIONS TO INSTRUMENTS OF SIMILAR ECONOMIC EFFECT TO HOLDING SHARES AND ENTITLEMENTS TO ACQUIRE SHARES

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Dear Mr Comporti,

The Association Française de la Gestion financière (AFG)[1] welcomes the opportunity given to express its members' point of view on CESR's proposal to extend major shareholding notifications to instruments of similar economic effect to holding shares and entitlements to acquire shares.

We have carefully gone throughout the document and globally, it appears to us that the subject absolutely needs further study. We are clearly in favour of a consultation on the matter, but we would have greatly appreciated a more backed-up context, with a detailed

1 The Association Française de la Gestion financière (AFG) represents the France-based investment management industry, both for collective and discretionary individual portfolio managements.
Our members include 409 management companies. They are entrepreneurial or belong to French or foreign banking or insurance groups.
AFG members are managing 2400 billion euros in the field of investment management, making in particular the French industry *the leader in Europe in terms of financial management location* for collective investments (with nearly 1400 billion euros managed from France, i.e. 21% of all EU investment funds assets under management), wherever the funds are domiciled in the EU, *and second at worldwide level after the US*. In the field of collective investment, our industry includes – beside UCITS – the employee savings schemes and products such as regulated hedge funds/funds of hedge funds as well as a significant part of private equity funds and real estate funds. AFG is of course an active member of the European Fund and Asset Management Association (EFAMA) and of the European Federation for Retirement Provision (EFRP). AFG is also an active member of the International Investment Funds Association (IIFA).

inventory coupled with analysis of the current state throughout Europe, with extensive discussion of pros and cons and with alternative options proposed. The paper gives the impression not to depict the global picture in full, displaying a somewhat biased view. Therefore, without the complementary elements issued from the necessary further studies, the parties wishing to express an opinion are indeed placed in front of an uneasy exercise.

1. Stated scope of the extended regime

We learn in the consultation paper that the intention would be that **all** instruments that can be used to create an **economic** long position be disclosed **as part of** major shareholding notifications. From the start, these are the terms that set up the framework of CESR's proposition.

However, it seems to us that this perspective is already an outcome of a debate that misses in the paper. We defend the idea that some more time is needed to further assess and back-up the subject so as to present different point of views and ensure that all meaningful options are fully laid down in the proposition's framework.

2. Summary of AFG's position[2]

AFG is globally in favour of reviewing the notifications regime in the light of recent developments in the market within the objective of achieving pan-European harmonisation; however we definitely cannot support the idea of (1) *including* (2) *all* instruments of similar effect to holding shares and entitlements to acquire shares *as part of* the disclosures of major shareholding notifications, disregarding their "proximity" to ever giving voting rights to the investor.

(1) If cash settled derivative positions are to be reported, AFG agrees to the ESME's proposition[3] that they should be part of a **separate reporting obligation** from the present arrangements for positions in normal shares. Also, for the concrete measure to be meaningful (to the regulator and to the market), workable (for the regulator and the market) and cost-efficient (for both regulators and the industry) we strongly support the idea that only **significant positions** should be targeted by the regime.

(2) AFG truly believes that the measure should leave aside as much as possible **instruments** that are in no way and at any time meant to give **voting rights** to the holder. Indeed, the objective is to achieve a meaningful transparency and avoid the overload of information that may easily become misleading. To say nothing of the fact that in the same time it would certainly imply a significantly larger number of disclosures for the asset managers, the latter being forced to put in place additional organisational means.

As discouraging the use of synthetic instruments in the normal course of business is not the target here, let's be careful about unintended effects and focus on steady, meaningful and harmonised reporting obligations. AFG strongly supports an extended reporting regime to all instruments that bear the possibility to **give access** to voting rights at one moment in time (plain vanilla options, cash settled derivatives with physical settlement options…). In our view, this is the only extended measure that may help giving **consistently** to the markets a

2 We have reached our position by replacing the proposed measures into the broader context of market efficiency that the Transparency Directive would like to ensure but also by taking root on the extensive discussions that took place in France and that resulted in the new regime set up last year.

3 AFG was very surprised to see no reference in CESR's consultation paper to the work done by ESME in its November 2009 paper *"Views on the issue of transparency of holdings of cash settled derivatives"*.

true picture of the transactions regarding major holdings.

Let us remind that these derivative instruments are mostly being used for risk management purposes and they help to improve the liquidity in the markets. In their vast majority, there is no intention to hide ownership or to induce an "empty voting". It should be noted that one intrinsic characteristic that makes much of their value is precisely their ability to split off the economic interest from the legal interest. The commingling of positions in derivatives with positions in straight shares may distort at a certain extent their use and bring out confusion in a globally up to now well-functioning market.

This brings us to question the adequacy of the regulatory response in preparation (this paper's proposition) with the nature of the "problem" it is supposed to fix. We would have liked the paper to bring a deeper analysis and discussion of the common characteristics of the 5 cases brought forward and that justify to a great extent the current consultation. At this point, we fail to see clearly the links that put together this limited number (and of different types) of recent cases with the necessity to implement such a broad measure falling on all market participants. Again, we would like to stress the need to fully identify the "problem" through extensive analysis and to clearly envisage different options with their pros and cons in order to achieve a cost-effective measure. The resulting information to the market should be as much as possible **accurate**, **comprehensible, consistent**, **and useful**.

Also, the mere gathering of as much as possible information is not acceptable by market participants, as we believe that supervisory authorities should be able to upgrade in parallel their monitoring, processing and detection capabilities as part of the solution. Unless only significant positions are reported and instruments with high proximity to acquiring shares with voting rights are targeted, we fail to see how this huge amount of information gathered in a context with numerous situations of double counting could be useful and not misleading. Being a bit modest by limiting the scope of the measure may increase the chances to capture a useful and workable flow of information and lead to a more efficient pricing as well as help enhancing market confidence.

Lastly, AFG is **in favour of a pan-European harmonisation** as this will simplify the reporting obligations of the asset managers and create a consistent basis for European issuers. However, different countries throughout Europe have already implemented different systems after having spent a significant time and efforts to disentangle the issue. Those systems should be fully analysed and plainly disclosed so as to try to come to a steady common solution that benefits from all these experiences. In the current proposition, one can assume the model is pretty close to the one implemented in a single European state without mentioning and discussing the other model alternatives. With the objective of harmonization, there is a clear and fundamental need to have the big picture in full. Pan-European harmonization should also bear in mind to a certain extent the non-European regimes (namely US) as a too stringent regime may encourage shifting the trades out of Europe.

Please see below AFG's responses to the specific questions of the consultation.

Q1. Do you agree with CESR's analysis of the issues raised by the use of instruments of similar economic effect to shares and entitlements to acquire shares?

We consider that the instruments that create a similar effect to holding shares and entitlements to acquire shares might lead, although in a limited number of specific cases, to some of the issues raised by the cases mentioned in the paper. However, the issues mentioned are mainly linked to the possibility for the buyer of the long position to exercise an influence over an issuer or to build an undisclosed position by using the shares acquired by the counterparty for hedging (ie in an indirect and somewhat unnatural way). We remind that in the vast majority of cases, the buyers of such positions are not at all intended to exercise an influence on the issuer.

We consider that the cases mentioned above cannot conclude that an economic position is necessarily a holding of shares on behalf and leads to an exercise of a hidden influence on an issuer. As stated previously, we would have appreciated a deeper analysis of the issues raised by the use of these instruments.

Q2. Do you agree that the scope of the Transparency Directive needs to be broadened to address these issues?

AFG is globally in favour of reviewing the notifications regime within the objective of achieving pan-European harmonisation. However, the proposition is far too broad in its scope to allow for a concrete meaningful amendment of the current disclosure regime.

As the implementation and the application of the TD is already complex, we do insist on the need to carefully identify the "issues" based on extensive inventory and analysis of recent cases.

Q3. Do you agree that disclosure should be based on a broad definition of financial instruments of similar economic effect to holding shares and entitlements to acquire shares without giving direct access to voting rights?

No, we do not think that the disclosure should be based on a broad definition of financial instruments of similar economic effect to holding shares and entitlements to acquire shares without giving direct access to voting rights since in major cases those instruments are entered into to give an economic exposure without wishing to gain access to voting rights. As a consequence, using a broad definition of those instruments will lead to broadcast unusable and misleading information to the market. It will certainly give rise to a significant number of practical problems of implementation and processing (numerous situations of double counting...).

AFG supports an extended reporting regime **only to instruments that bear the possibility to give access to voting rights at one moment in time** (plain vanilla options, cash settled derivatives with physical settlement options…). For us, this is the only extended measure that may help giving **consistently** to the markets a true picture of the transactions regarding major holdings.

Q4. With regard to the legal definition of the scope (paragraphs 50-52 above), what kind of issues you anticipate arising from either of the two options? Please give examples on transactions or agreements that should in your view be excluded from the first option and/or on instruments that in your view are not adequately caught by the MiFID definition of financial instrument.

Again, the scope is too broad to allow for a meaningful processing. We do not support the proposition of including all instruments irrespective of their "proximity" to ever giving voting rights to the investor.

Q5. Do you think that the share equivalence should be calculated on a nominal or delta-adjusted basis?

A delta-adjusted basis seems more accurate; however a nominal basis may be a more stable basis for the specific purpose of thresholds reporting. For this reason, we prefer that the share equivalence be calculated on a nominal basis.

Q6. How should the share equivalence be calculated in instruments where the exact number of reference shares is not determined?

If the number of shares is not determined, it should not be included under the scope of the proposed rules in order to prevent from broadcasting uncertain information to the market.

Q7. Should there be a general disclosure of these instruments when referenced to shares, or should disclosure be limited to instruments that contractually do not preclude the possibility of giving access to voting rights (the 'safe harbour' approach)?

We consider that the disclosure should be limited to instruments that contractually do not preclude the possibility of giving access to voting rights since in major cases investors only build economic exposures. Disclosing all the instruments that can be used to create an economic long position will make this information unusable and confusing.

Q8. Do you consider there is a need to apply existing TD exemptions to instruments of similar economic effect to holding shares and entitlements to acquire shares?

Q9. Do you consider there is need for additional exemptions, such as those mentioned above or others?

Since the vast majority of these instruments are not used with the intention of exercising a direct influence over the issuers, we recommend to limit the scope to those instruments that are supposed to give access to voting rights at one moment in time to their holder. Pure economic exposures that will never come close to an influential position, especially when it concerns non significant positions, are clearly to be excluded.

Q10. Which kinds of costs and benefits do you associate with CESR's proposed approach?

The implementation of the proposed amendments may not improve the transparency of the market. As CESR proposed approach is broad, notably regarding the definition of the legal scope, the measures would not allow the market participants to identify the effective exercise of influence over listed issuers.

The proposed approach will instead certainly lead to increase the number of notifications and the amount of the holdings disclosed. The asset managers will be forced to put in place additional organisational means to deal with a more complex and voluminous disclosure regime. Some market participants may be discouraged in their use of these instruments which was on its substance purely economic and had nothing to do with the fact of gaining control of the issuer.

Q11. How high do you expect these costs and benefits to be?

Overloading the reporting burden whereas these instruments are used to gain mere economic exposure in the vast majority of cases with no interest in the control of underlying shares will potentially lead to unusable and confusing information.

Asset managers will incur organisational costs of the type of a one-time information system investment but also in their day-to-day business, especially those with a huge number of daily transactions. Smaller-sized participants with a less frequent use of these instruments may feel discouraged to enter the market.

Q12. If you have proposed any exemptions or have presented other options, kindly also

provide an estimate of the associated costs and benefits.

As previously stated AFG supports an extended reporting regime only to instruments that bear the possibility to give access to voting rights at one moment in time and is in favour of separate reporting obligations between straight ownership and indirect exposures. Only sufficiently size-meaningful positions should be targeted (at least 5 or 10%).

A fully harmonized and regulated disclosure measure at the European level based on our proposition above may, in our view, bear fewer costs than the consultation paper' provisions while potentially sending a more consistent and comprehensible message to the issuers and the market as a whole.

We remain available for any further questions. Please do not hesitate to contact myself at +33.1.44.94.94.29 (p.bollon@afg.asso.fr) or Eric Pagniez, at +33.1.44.94.94.06 (e.pagniez@afg.asso.fr) or Adina Gurau Audibert, at +33.1.44.94.94.31 (a.gurau.audibert@afg.asso.fr).

Sincerely Yours,

Pierre Bollon