COMMITTEE OF EUROPEAN SECURITIES REGULATORS

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REPORT

Model for a Pan-European Short Selling Disclosure Regime

Table of contents

Executive summary 3
1. Background 3
2. Why CESR wants enhanced transparency of short selling 5
3. Model for the disclosure of significant short positions 7
4. Impact assessment 12

Executive summary

This report contains CESR's proposal to the European Institutions for a pan-European short selling disclosure regime. It is based on a two-tier model for disclosure of significant individual net short positions in all shares that are admitted to trading on an EEA regulated market and/or an EEA MTF. However, the regime would not apply to shares admitted to trading on an EEA regulated market or an EEA MTF if their primary market is located outside the EEA. At the lower threshold of 0.2%, positions would be disclosed to the relevant regulator, at the higher threshold of 0.5% positions would be disclosed, in addition to the regulator, also to the market as a whole. All changes of position would be reported at increments of 0.1%, first to the regulator (from 0.3% until 0.4%) and then to the regulator and the market.

In calculating whether a disclosure was required, market participants would need to take account of any transaction which provided an economic exposure to a particular share. Hence transactions in exchange-traded and OTC derivatives would be covered as well as short positions in the cash markets. Disclosure calculations and reports would be done on a net basis with any positions involving long economic exposures to a share subtracted from the short positions. Disclosure reports of short positions – whether to the regulator or the market – would be made on the trading day following that on which the relevant trigger threshold had been crossed. There would be exemptions from the disclosure requirements for short positions resulting from market making activities.

In parallel to making this proposal to the European Institutions, those CESR members that already have powers to introduce a permanent disclosure regime, will begin the process of implementing the regime, the others will aim at implementing such a regime on a best efforts basis.

1. Background

1. In the light of very turbulent market conditions and concerns in the second half of 2008 about the threat to financial stability and the associated risks of disorderly markets and market abuse, a significant number of CESR members took emergency measures to restrict and/or impose conditions on short selling. These measures took various forms – some imposed restrictions on all short selling of specified shares or specified categories of shares (i.e. financial sector), some restricted naked short selling and some also introduced disclosure obligations of different kinds. Many of these measures still remain in place, having been extended or renewed in modified form.

2. As a result of all the activity on short selling regulation, CESR considered that it was appropriate to launch a review of policy on short selling with a view to formulating pan-European standards in this area. This initiative also reflected the concerns of market participants who have made clear their views about the burdens of having to comply with a number of different sets of national requirements.

3. CESR therefore launched work to examine what permanent regime would be appropriate for short selling within the EEA. Without prejudice to the right of the individual CESR members to take or maintain additional measures on short selling (such as temporary emergency measures or measures that do not relate to disclosure), CESR decided that it was important to achieve a harmonised approach to this issue.

4. While CESR continues to consider whether further measures for the regulation of short selling, beyond disclosure, are required, CESR members have agreed already that a harmonised pan-European regime for enhanced transparency of short selling should be implemented on a permanent basis.

5. CESR's proposal has benefited from a public consultation, where CESR published in July 2009 a consultation paper (CP), CESR Proposal for a Pan-European Short Selling Disclosure Regime (Ref. CESR/09-581).

6. A Feedback Statement (Ref. CESR/10-089) the FS), summarising the responses that CESR received to the CP and highlighting CESR's feedback on those responses and any changes to its proposals in the light of them, is published alongside and should be read in conjunction with this Report.

7. This Report sets out CESR's finalised model for a pan-European short selling disclosure regime. It has been prepared by the CESR-Pol Standing Committee, chaired by Anastassios Gabrielides, the Chairman of the Capital Market Commission of Greece, and by its Short Selling Task Force.

2. Why CESR wants enhanced transparency of short selling

8. This chapter provides a brief description of short selling and the benefits and potential problems the practice brings with it. It then sets out why CESR has prioritised development of a pan-European regime for enhanced transparency of short selling via short position disclosure.

Short selling

9. Short selling is generally understood to be the sale of a financial instrument the seller does not own. The seller can undertake a 'covered' short sale by borrowing, before or at the time of submitting the sale order, the instruments he is due to deliver to the purchaser or a 'naked' short sale in which the previous condition is not satisfied. In both cases the seller will at some point need to purchase an equivalent amount of the financial instruments so that he can fulfil his obligations (to the lender or directly to the purchaser).

10. It is important to note that short positions can be obtained through derivatives (whether exchange-traded or over the counter products) as well as by selling in the cash market.

11. Legitimate short selling plays an important role in financial markets and is undertaken by a variety of market participants. It contributes to efficient price discovery, increases market liquidity, facilitates hedging and other risk management activities and can possibly help mitigate market bubbles. However, there are some concerns that it can be used in an abusive fashion to drive down the price of financial instruments to a distorted level, can contribute to disorderly markets and, especially in extreme market conditions, can otherwise have an adverse impact on financial stability. In addition, enhanced transparency of short selling has informational benefits for the market.

12. CESR's objective in developing this model is to reduce or mitigate the negative consequences and risks which short selling can have without having an undue adverse impact on the benefits which the practice brings to markets.

CESR's prioritisation

13. Although the design of a common disclosure regime has been prioritised so far, CESR continues to consider whether further harmonised measures for the regulation of short selling, beyond disclosure, are required and feasible.

14. In addition, it is recognised that individual CESR members may need to impose temporary emergency measures, such as bans or partial bans or the imposition of special conditions on short selling. CESR continues to examine whether all its members have the necessary powers to introduce such emergency measures and, if not, what steps may be required to remedy any deficiencies.

15. CESR also respects the right of individual members to maintain their own particular measures, beyond enhancing transparency, on short selling in the light of their judgements of what is appropriate in the specific circumstances of their markets. For example, some CESR members have had long-standing prohibitions on naked short selling.

Enhanced transparency of short selling

16. CESR considers that improving the transparency of short selling would have distinct benefits which would outweigh the associated costs. It would help deter and constrain particularly aggressive large-scale short selling which may threaten the maintenance of orderly markets or pose the risk of market abuse and provide early warning signs of a build up of large short positions, thereby alerting regulators to potentially abusive behaviour and enabling them to monitor

and take action more effectively. Facilitating ready access to information on short selling would provide informational benefits to the market, improving insight into market dynamics and making available important information to assist price discovery.

17. As to what form the enhanced transparency might take, there are two basic approaches (although it is possible to use the two in combination). The first involves the 'flagging' of short sales or short sale orders – requiring a marker to be put on each individual short sale or short sale order that a broker sends to a regulated market or multilateral trading facility for execution. Aggregated information about the level of short interest in each security may then be published to the market. CESR understands that information about the aggregate short position in a single share could help the market judge the extent to which short selling is driving down the price of that share and also the extent of the overhang of prospective buy orders when short sellers decide to close out their positions. Flagging also has the potential to give the regulatory authorities real-time data on short selling, including intra-day activity, and is more suitable for micro-supervision of transactions.

18. Naturally, there are inherent imperfections in the data which arise from the mechanics of aggregation, but in jurisdictions where other data, such as stock lending data, is not available, such information would seem to add value. It should be noted, however, that flagging of short sales does not provide regulators with information about outstanding short positions in the market or necessarily enable them to identify any large short positions. The fact that individual positions remain anonymous would mean it is less effective as a constraint on aggressive short selling.

19. In addition, no CESR member other than the Greek HCMC currently has a marking requirement or the infrastructure necessary to operate such a system. Therefore, it is likely that introducing a short sale flagging regime would be both operationally difficult and expensive for both brokers and trading platforms.

20. The second approach involves a requirement to report individual significant short positions to the regulator and/or the market. What constitutes a 'significant' position would be determined by pre-set thresholds embedded in the disclosure requirement.

21. Requiring the reporting of significant short positions would better enable regulators to identify which parties are taking the lead in short selling and as necessary pursue enquiries with those participants. Requiring those positions to be reported publicly to the market as a whole provides a more effective potential constraint on aggressive large-scale short selling.

22. Obviously there are some downsides to a position reporting regime. First, there are costs to those market participants that have to comply with such a regime. The bulk of these would appear to be incurred in calculating participants' positions in order to determine whether there is a disclosure obligation. However, on the basis of the information available so far, it appears that the compliance costs are considerably lower than for a flagging regime. It is, of course, also relevant to note that the temporary disclosure regimes introduced by the various CESR members since 2008 have been based on the disclosure of significant short positions, so market participants already have some experience and familiarity with this type of regime. Secondly, a position reporting regime cannot aspire to capture real-time data. As discussed below, it is, in effect, a 'snapshot' of a person's position taken at a pre-determined time. As a result, intra-day positions will not be captured. Finally, even when position data is aggregated, it cannot provide a complete picture of the overall levels of shorting in particular stocks because it relies on threshold triggers for disclosure and, by definition, will not include those positions held beneath the disclosure thresholds. Nevertheless, on balance, CESR considers that the second approach is preferable.

23. Accordingly, whilst CESR recognises that both approaches (flagging and position reporting) have advantages and disadvantages, it has decided, at this time, to proceed on the basis that transparency of short selling should be enhanced on a pan-European basis through the reporting of significant short positions.

3. Model for the disclosure of significant short positions

Introduction

24. This chapter sets out CESR's pan-European model for permanent harmonised short position disclosure obligations. The intention is to provide a uniform approach to assist market participants who operate on a cross-border basis in a number of CESR jurisdictions and allow them to utilise their resources in as efficient a manner as possible. A harmonised regime would need to cover a variety of different markets involving different sizes of company, liquidity and market practice.

Scope

25. In most cases where a temporary disclosure regime has been introduced it has been limited to particular, named securities, or particular sectors (e.g. banking and insurance companies). CESR considers that the scope of the permanent disclosure regime should therefore not be limited by sector or by the nature of the security (e.g. its liquidity or systemic importance or market capitalisation). There are a number of reasons for this.

26. First and foremost, the risks posed by short selling are not confined to the financial sector and it is not possible to predict with any certainty how the next crisis might develop or which sector might become vulnerable to abusive short selling or disorderly markets. Second, applying the disclosure obligations to only particular categories of security risks 'displacement' of the problems to other areas of the market. Finally, if it is accepted that disclosure of significant short positions is beneficial, it is not logical to restrict those benefits only to one sector or group of issuers as they apply equally to all.

27. However, CESR considers that there should be two limitations to the scope of the regime proposed in this report. First, only short positions creating an economic exposure to shares admitted to trading on an EEA regulated market and/or an EEA MTF should be included. This regime is not justified for the shares of other issuers nor appropriate for other types of security such as bonds or medium term notes where short selling does not pose the same type of issues as for equities. Second, the regime should only apply to EEA issuers and those issuers whose shares are admitted to trading on an EEA regulated market and/oran EEA MTF. However, the regime should not apply to shares admitted to trading on an EEA regulated market or an EEA MTF if their primary market is located outside the EEA. Shares of many other non-EEA issuers have been admitted to trading on an EEA regulated market and/or an EEA MTF but it would not be appropriate for the regime to include them within its scope if their primary market is located outside the EEA.

A two-tier disclosure system

28. CESR favours a two-tier system involving a mixture of private and public disclosures and based on the net short position (howsoever obtained) expressed as a percentage of the company's issued share capital. Once a net short position has reached a specified first trigger threshold it would need to be disclosed to the relevant regulator. If the short position then reaches a second, higher threshold, an obligation to make a public disclosure to the market, in addition to the regulator, as a whole would be triggered.

29. The public disclosure requirement is supplemented by an obligation to make disclosures to the regulator at a lower threshold because CESR recognises that some short sellers may not wish to trigger a public disclosure of their positions and therefore keep them just below the relevant threshold. To track what is happening in particular shares, regulators would benefit from knowing which market participants have positions which, while not large enough to warrant public disclosure, are still nevertheless significant. In the absence of such disclosures, it can be very time and resource consuming to identify such parties from transaction reporting data – and only

a partial picture may be obtained. The benefits of enabling regulators to monitor growing short positions before they are made public are clear.

30. In addition, a two-tier disclosure regime affords a degree of flexibility that enables harmonisation amongst CESR members of the precise disclosure thresholds, which is an issue that CESR knows is of great importance to the market.

31. CESR considers that short positions of a given size do warrant public disclosure and that private disclosure to the regulator alone would not achieve the same benefits. A short selling disclosure regime should aim to achieve a measure of behavioural change and, for that reason, CESR holds the view that public individual position disclosure should be a central plank of the regime. In addition to the substantial informational benefits it provides to the market, this option will help to constrain particularly aggressive large-scale short selling which may involve unacceptable risks of abuse or disorderly markets. CESR considers that when short positions reach certain, relatively high levels, short sellers should be required to consider whether they wish to be identified to the market before they choose to continue with their strategy. Whilst this may have some effect on absolute levels of short selling, CESR does not think that this will put a halt to short selling or be such as to reduce market quality materially.

32. CESR is aware of certain grounds for opposing public individual position disclosure – namely, the perceived risk of 'herding' behaviour when the identities of big-name short sellers are revealed, forced disclosure of companies' intellectual property, the risk of short 'squeezes' by competitors, concerns about the impact on the relationship between issuers and short sellers (investors). It has been argued that as a result of all of these factors, public disclosure of significant short positions will deter short selling and damage market quality. However, those CESR members who operate such disclosure regimes and who have undertaken empirical analysis of the impact of those regimes have not seen these concerns crystallise. This, together with the benefits highlighted above, justifies the public disclosure of significant short positions. In addition, CESR notes that there are precedents for the public disclosure of private information in other contexts (for significant long positions under the Transparency Directive and managers' transactions in the shares of the company they work for under the Market Abuse Directive).

33. In addition, CESR recognises the potential informational benefits of publishing aggregated data on short positions and would note that, in addition to the disclosure model as previously proposed, members may choose to publish aggregated data that they receive as a result of private disclosures. CESR regards this to be an optional rather than a mandatory element of the regime for members to implement at their discretion. CESR believes that this is appropriate because to do so does not affect the nature of the requirements that will fall on market participants and, therefore, the fundamental harmonising objective of the regime is not undermined.

Disclosure thresholds

34. CESR recognises that the efficacy of a position disclosure regime and the extent of the compliance burden it imposes will, to a large degree, depend on the levels at which thresholds are set. Selecting disclosure thresholds that would generate meaningful information and a proportionate compliance burden is crucial. If the thresholds are set too high, then disclosures may be rarely triggered so that regulators may not receive sufficient advance warning of possible market abuse or impending disorderly markets and the market may not receive enough information to help it make informed investment decisions. If the thresholds are set too low, then the 'warnings' sounded to regulators may be of little value and the compliance costs for market participants may be high and not justifiable. In addition, large numbers of disclosures of positions that are not considered by the market to be meaningful are of questionable value. In particular, the initial public disclosure threshold needs to be set at a level which provides to the market meaningful information about the size of positions and the identities of short sellers, whilst minimising the degree to which trading strategies which may not risk creating disorderly markets are deterred.

35. CESR considers that the benefits of having harmonised uniform thresholds across the EEA outweigh the disadvantages and, accordingly, considers that there should be one set of disclosure thresholds applicable to all EEA jurisdictions.

36. As regards the threshold for public disclosure of short positions, CESR's view is that the public disclosure threshold should be higher than that introduced by many CESR members in 2008 in relation to financial sector shares. The reasons for this are that, firstly, this model should apply to positions held in all shares instead of only financial sector shares. Secondly, given that CESR considers that there should be a lower, private disclosure trigger, regulators would already have had advance notice of building short positions in the issued share capital of a particular issuer and would already have had the opportunity to consider their response.

37. CESR continues to believe that a figure of 0.5% would strike the right balance and concludes that this should be the level for the public disclosure threshold.

38. In response to the feedback from the consultation, CESR however decided to raise the initial threshold for private disclosure to the regulator to 0.2%, which should significantly reduce the reporting burden but would still facilitate proper market monitoring by competent authorities. The decision taken by CESR was supported by the results of an informal survey conducted by one member on the likely number of disclosures to be received at the lower threshold.

39. In addition, for the private and public disclosure regimes steps of 0.1% should be used as incremental threshold bands to trigger further disclosure obligations on change of a short position (either up or down), after the initial disclosure obligation has been incurred. Thus further notifications to the regulator would be required at 0.3% and 0.4%. Further notifications to the public and to the regulator would be required at 0.6%, 0.7% etc. Disclosures would also be required at the point at which the short position fell back below any of the trigger thresholds, including the initial trigger thresholds.

40. These thresholds should apply irrespective of whether a company is engaged in a rights issue.

41. Finally, CESR agrees with IOSCO[1] that "reporting of short positions is a "greenfield" area" and that "reporting threshold or trigger levels … may need to be fine-tuned as more experience is gained." Thus CESR recommends that there should be a review of the suitability of the chosen thresholds after sufficient experience had been gained in their operation.

The basis for calculating short positions

42. Calculation of short positions can be done on either a gross basis or a net basis. CESR considers that using a net basis would mean that a more accurate picture of the actual short position would be disclosed. This information would be more useful to both regulators and market participants and the costs for calculating these positions would fall on the short seller. Accordingly, short positions for the purposes of this model should be calculated on a net basis, meaning that long positions could be off-set against short positions in order to determine whether or not an investor was subject to a disclosure obligation.

43. As regards precisely how the net position is calculated, this should be done by taking into account transactions in all financial instruments that create an economic exposure to the issued share capital of the issuer. Calculating the net short position should not be limited to that taken in the cash equity markets, but should also extend to positions in linked derivative contracts (whether exchange-traded or OTC), indices, baskets and exchange traded funds (ETFs). Without such coverage, it would be easy for investors to circumvent the disclosure requirements.

[1] IOSCO Regulation of Short selling - Final Report, paragraph 3.23.6 p. 14.

44. The 'economic exposure to the issued share capital of the issuer' should be calculated taking into account all classes of shares admitted to trading on an EEA regulated market and/or an EEA MTF except if their primary market is located outside the EEA.

45. CESR continues to develop its thinking on the calculation of short positions and anticipates that it is likely to publish its position on them as and when it is able to do so.

The mechanics of disclosure

46. Given that the market impact of short positions is generally most significant on the most relevant market in terms of liquidity (as per Article 25(3) of MiFID), CESR's view is that the regulator of this market should receive timely and adequate information on the short positions held.

47. CESR continues to develop its thinking on the mechanics of disclosure and anticipates that it is likely to publish its position on them as and when it is able to do so.

48. Information about short selling should be disclosed as soon as possible so that users of it, whether regulators (acting on both private or public information) or market participants (acting on public information), can make informed decisions on whether any action on their part is warranted. Delaying disclosures unnecessarily will lessen the value of the information but, equally, requiring disclosures to be made too quickly may unnecessarily burden the short sellers who are making the disclosures. Experience from the temporary disclosure obligations introduced since autumn 2008 has shown that investors' systems can cope with calculating (and then disclosing) short positions within a day of the trading taking place.

49. Accordingly, disclosures should be made at a specified time before the end of the trading day following the day on which the disclosure obligation is triggered (i.e. T+1). CESR recognises that intra-day positions that breach a disclosure threshold, but which return below that same threshold before the end of the trading day, will not be captured.

The content of disclosures

50. CESR understands the need for a uniform format and content for the disclosure across its members and considers that there should be maximum harmonisation in this regard. Accordingly, disclosures should contain the identity of the short position holder, the identity of the issuer, the size of the position held and the date on which the position was created or was no longer held. At this point, CESR does not believe that any further information is required However, CESR notes that this issue may need to be re-visited in order to take into account future policy developments in other, related areas, such as in relation to the Transparency Directive.

Exemptions to disclosure obligations

51. CESR's view is that market makers should be exempted from any general disclosure regime based on individual short positions. This exemption is included because market makers play an important role in the financial markets through the provision of liquidity by offering two-way prices on an ongoing basis. This activity is vital to the efficient and effective running of the markets. As part of their market making function, the firms in question regularly have to take short positions (generally temporary ones) and may be at risk of unjustified commercial prejudice if those positions are known to the market. In allowing this exemption, CESR's principal objective is to ensure that liquidity provision is not unduly hampered by this disclosure regime.

52. CESR believes that there should be a clear definition of 'market maker' for these purposes and continues to develop its thinking on the precise terms of that definition. CESR anticipates that it is likely to publish a definition as and when it is able to do so.

53. The exemption would only cover market makers when, in the particular circumstances of each transaction, they are genuinely acting in the capacity of a market maker. They are afforded a certain level of flexibility in anticipating sales as long as this activity is genuine market making in line with their existing general levels of business. Consequently, CESR would not expect market makers to hold significant short positions, other than for brief periods. Proprietary trading, where a firm is acting more as an investor or trader rather than liquidity provider, would not fall within the scope of market-making and would not be exempt.

54. CESR's view is that this exemption should be an absolute one (i.e. in relation to both private and public disclosure). However, in order to assist competent authorities monitor appropriate reliance on this exemption and to ensure that it is not abused, it would be open to CESR members to require those financial institutions intending to rely on this exemption to notify the relevant regulator of this intention before making use of the exemption.

The legal basis for a permanent disclosure regime

55. One of the critical requirements of a permanent disclosure regime for short selling is that it should apply to the unregulated as well as the regulated community. There is clearly no point requiring regulated entities to disclose their short positions if, for example, hedge funds operating outside the EEA do not have to do so. This was a significant factor for many CESR members when they opted for the market abuse regime as the mechanism for implementing their temporary measures.

56. However, CESR considers that EEA securities regulators should be given explicit, stand-alone powers to require disclosure in respect of short selling. This would provide confidence in the clarity and legal soundness of such requirements, allow for flexibility and minimise the scope for legal challenge to the use of such powers.

57. CESR's view is that there should be new European legislation in this area, either via the enactment of a separate directive or regulation or through amendments to the Transparency Directive. Given that CESR envisages a number of areas of divergence from the long position disclosure regime, it believes that proceeding via a new directive or regulation, rather than through an amendment to the Transparency Directive, would be more suitable. At this stage CESR does not have a view as to whether a Directive or a Regulation is preferable.

58. In parallel to making this proposal to the European Institutions, those CESR members that already have powers to introduce a permanent disclosure regime, will begin the process of implementing the regime, the others will aim at implementing such a regime on a best efforts basis.

4. Impact assessment

59. This Impact Assessment describes the economic costs and benefits of the proposed two-tier short selling disclosure regime of significant individual short positions.

Benefits

60. As discussed earlier in this FR, the proposed disclosure regime can help to address potential market abuse and disorderly markets through acting as a constraining factor on particularly aggressive, large-scale short selling which might involve such risks. In addition, it can provide informational benefits to the market by improving transparency of short positions.

61. *Market abuse* – The first element of the disclosure regime, private disclosure of short positions to the regulator at a low threshold 0.2% provides regulators with early warning signs of a build up of large short positions. This allows regulators to monitor the situation and can alert them to potentially abusive behaviour. They might therefore be able to take action more effectively. Without a disclosure regime, identification of significant short positions would be resource-intensive for regulators. CESR recognises the limits to these benefits, as short sellers might operate below the disclosure threshold. This issue is mitigated by proposing a relatively low threshold for private disclosure to the regulator. However, it should be noted that short sellers might also fail to comply with the disclosure obligation.

62. *Disorderly markets* – Disclosures of short positions to the regulator at a relatively early stage may help to identify unusual short selling activity. This helps regulators to identify whether short selling activity potentially leads to price amplification effects (if markets 'over-react' to the negative price signal inherent in short selling) at an early stage and to determine whether intervention is required.

63. *Transparency* – The second element of the disclosure regime, public disclosure of individual short positions above a second and higher threshold (i.e. 0.5%) generates information for market participants on the size of significant short positions above this second disclosure threshold. It also provides information about the identity of significant short sellers in the relevant shares. If this information is interpreted correctly by the market, this provides insight into short sellers' price movement expectations and can improve pricing efficiency.

64. Providing appropriate information to the market as well as minimising the potential negative side effects of making individual short positions public depends on the level at which the public disclosure threshold is set. When setting the threshold, a balance needs to be struck between providing too much information which is not meaningful (if the threshold is set too low) and not capturing potentially important information (if the threshold is set too high).

Costs

65. Disclosures of individual short positions would impose compliance costs on market participants engaging in short selling. These costs are related to monitoring short positions, making appropriate disclosures to the regulator and the market and, in some cases, seeking legal advice on the nature of the disclosure obligation.

66. It is likely that the major part of these costs is generated by monitoring short positions as firms may need to incur one-off costs to adjust their existing internal systems or install the necessary monitoring functionality. The size of the costs due to the implementation of a permanent disclosure regime across the EEA depends on the complexity of the business of a short seller and on the systems for monitoring short positions that are already in place. Market participants will also have ongoing costs to monitor their short positions.

CESR

67. Making the appropriate disclosures to the regulator and the market will lead to further ongoing costs. CESR has not yet finalised the mechanics for disclosure to the market so, at this stage, it is more difficult to assess the costs of public disclosures. CESR however believes that the costs of making these disclosures are relatively small.

68. CESR does not expect that the levels at which the disclosure thresholds are set will have major impacts on compliance costs to firms. This is for two reasons. Firstly, these levels are unlikely to have major impacts on one-off costs to update internal systems necessary for complying with the disclosure obligations. Secondly, although the levels of the thresholds will affect the number of disclosures that need to be made, CESR does not expect the costs of making disclosures to the regulator and to the market to be great.

69. When considering compliance costs, it is also worth noting that the operation of different disclosure regimes could add to firms' compliance costs as this is adding complexity. A harmonised disclosure regime that employs uniform thresholds that apply across all EEA jurisdictions is likely to lead to lower compliance costs for market participants operating across borders.

70. Public disclosures of short positions might also lead to indirect costs for short sellers. Short sellers might have competitive disadvantages if others follow their short selling strategy. They might also face a short squeeze, i.e. increased costs of closing their short positions if other market participants are alerted to their need to do so. While, overall, public disclosure obligations might reduce firms' willingness to hold disclosable short positions, the extent to which this might happen is unclear. If this does happen in practice, then it will reduce liquidity in the market with all the associated indirect costs that that brings. However, as noted already in this FR and in the FS, CESR jurisdictions that have operated public disclosure regimes have not, so far, identified compelling evidence that these concerns have crystallised.

71. The actual level of the public disclosure threshold is relevant to the size of this potential cost, with a higher threshold associated with lower indirect costs.

72. Another indirect cost of public disclosure of short positions concerns potential over-reactions to the information disclosed by market participants. This risk is likely to be higher in times of severe market turbulence. This may lead to an increase of short selling due to herd-like behaviour, resulting in excessive sales of shares and price declines following disclosures of short positions to the market, although again there has yet to be clear evidence of this occurring in the context of the temporary disclosure regimes which various Member States have been operating since Autumn 2008.

73. Regulators would also incur costs as compliance with the private and public disclosure requirements needs to be monitored and, if necessary, enforced.