

PS12/19

Financial Services Authority

Short selling regulation

Handbook changes – Feedback to CP12/21

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This Policy Statement reports on the main issues arising from Consultation Paper 12/21 *Short Selling Regulation – Handbook changes* and publishes final rules.

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Copies of this Policy Statement are available to download from our website – www.fsa.gov.uk. Alternatively, paper copies can be obtained by calling the FSA order line: 0845 608 2372.

Abbreviations used in this paper

PS	Policy Statement
SSR	Short Selling Regulation
FINMAR	Financial Stability and Market Confidence Sourcebook
MAR	Market Conduct Sourcebook
CP	Consultation Paper

1

Overview

Introduction

- 1.1 In this Policy Statement (PS), we summarise the responses to our consultation on the proposed changes to the Handbook we need to make to comply with the EU Short Selling Regulation¹ (SSR) from 1 November 2012 as well as our policies regarding the exercise of the discretions the SSR gives us. We also set out the changes to the Handbook that we are making in light of our consultation and the feedback that we received. Overall, the instrument does not differ significantly from the consultation draft. We received six responses to the CP and are grateful to those who responded, especially given the short timescale in which we were seeking comments on our proposals.

Background

- 1.2 The SSR, which provides a common framework for regulating short selling across Europe, will apply from 1 November 2012. As a European Regulation it has direct applicability as law in the UK and so does not require specific implementation in domestic legislation and FSA rules. There are, however, some areas in the SSR where Member States have discretion about how to exercise their powers or where the SSR requires matters to be dealt with in accordance with the domestic law. In CP12/21, *Short Selling Regulation – Handbook changes*, we consulted on our overall approach on our policies regarding these discretions, as well as the amendments to the FSA Handbook, which are necessary to ensure our practices conform with the SSR by its application date.

Who should read this paper?

- 1.3 This PS is relevant to market participants.

1 Regulation (EU) No236/2012

Next steps

- 1.4 Our Handbook changes will come into effect on 1 November 2012.

2

Summary of responses to CP12/21

2.1 In CP12/21, we asked the following questions:

Q1: Do you agree with the proposed approach of repealing the existing short selling provisions in FINMAR 2?

Q2: Do you agree with the proposed amendment to SUP?

Q3: Do you have any comments on the proposed framework?

Q4: Do you have any comments on the proposed policy?

Q5: Do you agree with our approach of using our existing policy?

Q6: Do you agree with our approach of using the current penalty policy for breaches under the SSR?

Q7: Do you agree with the method proposed for calculating the exchange rate?

Q8: Do you agree with these proposals?

Q9: Do you agree with our approach to the cost benefit analysis?

- 2.2 Respondents were generally content with our proposals, so we are making the changes to the FSA Handbook we proposed. However, respondents did raise the following detailed issues.

Proposed framework for use of temporary suspension powers

- 2.3 We proposed that violent movements in the price of a financial instrument would be one factor we would take into account when assessing the powers of intervention provided to us by the Regulation. One respondent suggested that we should quantify what we would regard as ‘violent movements’. We also proposed that the existence of unsubstantiated rumours concerning an issuer or financial instrument was another factor to be taken into account. This respondent also observed that it may be difficult to quickly determine whether rumours are substantiated or not. They asked whether the proposed text for FINMAR 2.5.2 G(2), which refers to the price of a financial instrument being set at a ‘level that would be considered abnormal’, should be read in the same way as ‘abnormal or artificial level’ in MAR 1.6.

Our response

We do not think it would be helpful to quantify what we would regard as violent movements, as the powers of suspension apply to a very wide range of financial instruments and it would be difficult to set meaningful quantitative thresholds. While we recognise it may be difficult to determine whether rumours are substantiated or not, we are able to check with issuers or their advisers whether there is any truth in a story. There also needs to be some scope for regulatory discretion in these cases. Lastly, we can confirm that it is our intention to read ‘a level that would be considered abnormal’ taking into account the factors we set out in MAR 1.6.10E.

Market maker and authorised primary dealer exemption prohibition procedure

- 2.4 One respondent was concerned that the time period for the review of a decision to prohibit use of the market maker or authorised primary dealer exemption (within three months) was too long, given the importance of the exemption to those parties wishing to use it.

Our response

We emphasise that the three-month limit is the maximum time period within which the review could take place. Our intention is to carry out any reviews requested as soon as possible.

Method for calculating the exchange rate

- 2.5 Respondents welcomed our intention to fix a sterling equivalent of the 50 eurocents figure, which determines a particular category of share for the purposes of the temporary suspension powers. They also agreed that we should provide for this figure to be adjusted if currency fluctuations went beyond a certain limit. But they suggested that we be more precise about the circumstances in which we will adjust the figure within the 12-month period.

Our response

We agree and have amended our approach. We will be using the Sterling-Euro spot rate set by the Bank of England at the end of the first business day in October 2012. The Sterling amount will then remain fixed until the following year. However, we will make an in-year adjustment where there has been a fluctuation in the exchange rate of more than 10% above or below this level for 20 consecutive business days.

Cost benefit analysis

- 2.6 One respondent questioned our cost benefit analysis on the grounds that it failed to take into account the costs to market participants arising from the Regulation concerning buy-in procedures. However, the costs of this provision arise directly from the Regulation itself, not from any of the changes we are making to our Handbook and so therefore this is not relevant under our cost benefit analysis.

Annex 1

List of non-confidential respondents

Alternative Investment Management Association

APCIMS

Association of British Insurers

Investment Management Association

Société Générale

Appendix 1

Made rules (legal instrument)

SHORT SELLING REGULATION INSTRUMENT 2012

Powers exercised

- A. The Financial Services Authority makes this instrument in the exercise of the following powers and related provisions in the Financial Services and Markets Act 2000 (the Act):
- (1) section 138 (1) (General rule-making power); and
 - (2) section 157(1) (Guidance).
- B. The rule-making powers listed above are specified for the purpose of section 153(2) (Rule-making instruments) of the Act.

Commencement

- C. This instrument comes into force on 1 November 2012

Amendments to the Handbook

- D. The modules of the FSA's Handbook of rules and guidance listed in column (1) below are amended in accordance with the Annexes to this instrument listed in column (2).

(1)	(2)
Glossary of definitions	Annex A
Financial Stability and Market Confidence sourcebook (FINMAR)	Annex B
General Provisions (GEN)	Annex C
Supervision manual (SUP)	Annex D
Decision Procedure and Penalties manual (DEPP)	Annex E

Amendments to material outside the Handbook

- E. The Enforcement Guide (EG) is amended in accordance with Annex F to this instrument. The general guidance in EG does not form part of the Handbook.

Notes

- F. In Annex B to this instrument, the "notes" (indicated by "**Note:**") are included for the convenience of readers but do not form part of the legislative text.

Citation

- G. This instrument may be cited as Short Selling Regulation Instrument 2012.

By order of the Board
31 October 2012

Annex A

Amendments to the Glossary of definitions

In this Annex, underlining indicates new text and striking through indicates deleted text, unless otherwise stated.

Insert the following new definitions in the appropriate alphabetical order. The text is not underlined.

<i>authorised primary dealer</i>	(as defined in article 2(1)(n) of the <i>short selling regulation</i>) a natural or legal person who has signed an agreement with a <i>sovereign issuer</i> or who has been formally recognised as a primary dealer by or on behalf of a <i>sovereign issuer</i> and who, in accordance with that agreement or recognition, has committed to dealing as principal in connection with primary and secondary market operations relating to debt issued by that <i>sovereign issuer</i> .
<i>authorised primary dealer exemption</i>	an exemption from articles 7, 13 and 14 of the <i>short selling regulation</i> for the activities of an <i>authorised primary dealer</i> pursuant to article 17 of the <i>short selling regulation</i> .
<i>market maker exemption</i>	an exemption from articles 5, 6, 7, 12, 13 and 14 of the <i>short selling regulation</i> for transactions performed due to <i>market making activities</i> pursuant to article 17 of the <i>short selling regulation</i> .
<i>market making activities</i>	(as defined in article 2(1)(k) of the <i>short selling regulation</i>) the activities of an <i>investment firm</i> , a <i>credit institution</i> , a third-country entity, or a firm as referred to in point (1) of article 2(1) of <i>MIFID</i> , which is a member of a <i>trading venue</i> or of a market in a third country, the legal and supervisory framework of which has been declared equivalent by the European Commission pursuant to article 17(2) of the <i>short selling regulation</i> where it deals as principal in a <i>financial instrument</i> , whether traded on or outside a <i>trading venue</i> , in any of the following capacities: <ul style="list-style-type: none"> (a) by posting firm, simultaneous two-way quotes of comparable size and at competitive prices, with the result of providing liquidity on a regular and ongoing basis to the market; or (b) as part of its usual business, by fulfilling orders initiated by clients or in response to clients' requests to trade; or (c) by hedging positions arising from the fulfilment of tasks under points (a) and (b).
<i>short selling regulation</i>	regulation (EU) No 236/2012 of the European Parliament and of the Council of 14 March 2012 on short selling and certain aspects of credit default swaps.
<i>sovereign issuer</i>	(as defined in article 2(1)(d) of the <i>short selling regulation</i>) any of the

following that issues debt instruments:

- (a) the *EU*; or
- (b) a Member State including a government department, an agency, or a special purpose vehicle of the Member State; or
- (c) in the case of a federal Member State, a member of the federation; or
- (d) a special purpose vehicle for several Member States; or
- (e) an international financial institution established by two or more Member States which has the purpose of mobilising funding and provide financial assistance to the benefit of its members that are experiencing or threatened by severe financing problems; or
- (f) the European Investment Bank.

Amend the following as shown.

<i>breach</i>	<p>in <i>DEPP</i>:</p> <p>...</p> <p>(6) a contravention in respect of which the <i>FSA</i> is empowered to take action pursuant to section 131G (Breach of short selling rules etc <u>short selling regulation</u>: Power to impose penalty or issue censure) of the <i>Act</i>.</p>
<i>competent authority</i>	<p>...</p> <p>[Note: article 1(7) of the <i>Market Abuse Directive</i>.]</p> <p>(7) <u>the authority designated by each <i>EEA State</i> in accordance with article 32 of the <i>short selling regulation</i>.</u></p>
<i>disclosable short position</i>	<p>a net short position which represents an economic interest of one quarter of 1% or more of the issued capital of a <i>company</i>, excluding any interest held in the capacity of a <i>market maker</i>.</p>
<i>disclosure</i>	<p>disclosure of a <i>disclosable short position</i> which:</p> <ul style="list-style-type: none"> (a) is made on a <i>RIS</i> by no later than 3.30pm on the <i>business day</i> following the day on which the position reaches or exceeds a <i>disclosable short position</i> of 0.25% of the issued capital of a <i>company</i>; and (b) includes the name of the <i>person</i> who has the <i>disclosable short position</i>, the amount of the <i>disclosable short position</i> and the name

	of the company in relation to which the person has that position.
<i>discretionary investment manager</i>	(in COBS, FINMAR and (in relation to <i>firm type</i>) in SUP 16.10 (Confirmation of standing data)) a <i>person</i> who, acting only on behalf of a <i>client</i> , manages <i>designated investments</i> in an account or portfolio on a discretionary basis under the terms of a discretionary management agreement.
<i>EEA regulator</i>	<p>(1) a <i>competent authority</i> for the purposes of any of the <i>Single Market Directives</i> or the <i>auction regulation</i>.</p> <p>(2) <u>(in DEPP 7) (as defined in section 131FA of the Act) the competent authority of an EEA State other than the United Kingdom for the purposes of the short selling regulation.</u></p>
<i>market maker</i>	<p>(1) (except in COBS and FINMAR) (in relation to an <i>investment</i>) a <i>person</i> who (otherwise than in his capacity as the <i>operator</i> of a <i>regulated collective investment scheme</i>) holds himself out as able and willing to enter into transactions of sale and purchase in <i>investments</i> of that description at prices determined by him generally and continuously rather than in respect of each particular transaction.</p> <p>...</p> <p>(3) (in FINMAR) a person who, ordinarily as part of his business, deals as principal in financial instruments (whether OTC or exchange traded):</p> <p style="padding-left: 40px;">(a) to fulfil orders received from another person in response to that person's request to trade or to hedge positions arising out of those dealings; or</p> <p style="padding-left: 40px;">(b) in a way that ordinarily has the effect of providing liquidity on a regular basis to the financial markets on both bid and offer sides of the market in comparable size. [deleted]</p>
<i>net short position</i>	<p>(1) (except in IPRU(INV) 13 and FINMAR) a net short position which gives rise to an economic exposure to the issued <i>share</i> capital of a company. Any calculation of whether a <i>person</i> has a short position must take account of any form of economic interest in the <i>shares</i> of the company.</p> <p>...</p> <p>(3) (in FINMAR) a position which gives rise to an economic exposure to the issued capital of a company, calculated in accordance with FINMAR 2. [deleted]</p>
<i>non-discretionary investment</i>	(in FINMAR and in relation to <i>firm type</i> in SUP 16.10 (Confirmation of standing data)) a person who, acting only on behalf of a client, manages

<i>manager</i>	<i>designated investments</i> in an account or portfolio on a non-discretionary basis under the terms of a non-discretionary management agreement.
<i>ongoing disclosure</i>	<p>disclosure of a <i>disclosable short position</i> which:</p> <p>(a) is made on a <i>RIS</i> by no later than 3.30pm on the <i>business day</i> following the day on which the position reaches, exceeds or falls below a <i>net short position</i> of 0.25%, 0.35%, 0.45% and 0.55% of the issued capital of a <i>company</i> and each 0.1% threshold thereafter; and</p> <p>(b) includes the name of the <i>person</i> who has the <i>disclosable short position</i>, the amount of the <i>disclosable short position</i> and the name of the <i>company</i> in relation to which the <i>person</i> has that position.</p>
<i>relevant financial instrument</i>	<p>(in accordance with sections 131C(4) and 131C(5) of the <i>Act</i>) a <i>financial instrument</i> that:</p> <p>(a) is admitted to trading on a <i>regulated market</i> or any other <i>prescribed market</i> in an <i>EEA State</i>; or</p> <p>(b) has such other connection with a market in an <i>EEA State</i> as may be specified by the <i>short selling rules</i>.</p>
<i>rights issue</i>	(in <i>LR</i>, <i>FINMAR</i> and <i>DTR</i> 5) an offer to existing <i>security</i> holders to subscribe or purchase further <i>securities</i> in proportion to their holdings made by means of the issue of a renounceable letter (or other negotiable document) which may be traded (as “nil paid” rights) for a period before payment for the <i>securities</i> is due.
<i>rights issue period</i>	the period that commences on the date a <i>company</i> announces a <i>rights issue</i> and which ends on the date that the <i>securities</i> issued under the <i>rights issue</i> are admitted to trading on a <i>prescribed market</i>.
<i>short selling rules</i>	(in accordance with section 131B(8) of the <i>Act</i>) rules concerning the prohibition or disclosure of short selling in relation to <i>relevant financial instruments</i>.
<i>trading day</i>	<p>(1) (in <i>MAR</i> 7 (Disclosure of information on certain trades undertaken outside a regulated market or MTF) and <i>SUP</i> 17 (Transaction reporting)) in relation to post-trade information to be made public about a share under <i>MAR</i> 7.2.10EU, any day of normal trading in a share on a <i>trading venue</i> in the <i>relevant liquid market</i> for this share. [Note: article 4(2) of the <i>MiFID Regulation</i>]</p> <p>(2) other than in (1) or (3), a day included in the calendar of trading days published by <i>FSA</i> at www.fsa.gov.uk.</p> <p>(3) <u>(in <i>FINMAR</i>) as defined in article 2(1)(p) of the <i>short selling regulation</i>, a trading day as referred to in article 4 of Regulation</u></p>

(EC) No 1287/2006.

trading venue

(1) *(except in FINMAR) a regulated market, MTF or systematic internaliser acting in its capacity as such, and, where appropriate, a system outside the EU with similar functions to a regulated market or MTF.*

[**Note:** article 2(8) of the *MIFID Regulation*]

(2) *(in FINMAR) (as defined in article 2(1)(1) of the short selling regulation) a regulated market or an MTF.*

Annex B

Amendments to the Financial Stability and Market Confidence sourcebook (FINMAR)

In this Annex, underlining indicates new text and striking through indicates deleted text, unless otherwise stated.

2.1 Application and purpose

Application

- 2.1.1 R ~~This chapter applies to all persons who:~~
- (1) ~~engage, or are intending to engage, in short selling in relation to *relevant financial instruments*; or~~
 - (2) ~~have engaged in short selling in relation to *relevant financial instruments* where the resulting short position is still open. [deleted]~~

- 2.1.1A G This chapter is relevant to all natural and legal persons to whom the *short selling regulation* applies, whether or not they are regulated by the *FSA*.

Purpose

- 2.1.2 G The purpose of this chapter is to ~~set out rules and~~ provide *guidance* in relation to ~~short selling in order to promote the *FSA's* statutory objectives of: the *FSA's* functions under the *short selling regulation*.~~
- (1) ~~maintaining confidence in the *UK financial system*; and~~
 - (2) ~~contributing to the protection and enhancement of the stability of the *UK financial system*.~~

Note: Other parts of the *Handbook* that may also be relevant to natural and legal persons to whom the *short selling regulation* applies include:

Chapter 2 of *SUP* (the Supervision manual) and *DEPP* (the Decision Procedure and Penalties manual).

The following Regulatory Guides are also relevant:

1. the Enforcement Guide (*EG*)

FINMAR 2.2 (Disclosure of disclosable short positions) is deleted in its entirety. The text of the section is not shown.

FINMAR 2.3 (Calculation of net short position) is deleted in its entirety. The text of the section is not shown.

FINMAR 2.4 (Responsibility for disclosure) is deleted in its entirety. The text of the section is not shown.

After FINMAR 2.4 [deleted] insert the following new sections. The text is not underlined.

2.5 Measures to prohibit, restrict or limit transactions in short selling

Approach to imposing measures

2.5.1 G The *FSA* is required by article 23 of the *short selling regulation* to consider whether to impose measures to prohibit or restrict short selling or otherwise limit transactions in a *financial instrument* on a *trading venue* where the price of that *financial instrument* on that *trading venue* has fallen significantly during a single *trading day* in relation to the closing price on that venue on the previous *trading day*. In fulfilling this obligation, the *FSA* will assess:

- (1) whether the price fall is or may become disorderly; and, if so in either case,
- (2) whether the imposition of measures to prohibit, restrict or limit transactions will prevent a further disorderly decline in the price of the *financial instrument*.

2.5.2 G The *FSA* will assess whether the price fall in a *financial instrument* on a *trading venue* is or may become disorderly having regard to at least the following factors:

- (1) whether there have been violent movements in the price of the particular *financial instrument* on a particular *trading venue*, including any sudden or significant movements in price of a *financial instrument* during the *trading day*;
- (2) whether there is evidence of unusual or improper trading in the *financial instrument* on a particular *trading venue* which could indicate that there was pressure to set the price of the *financial instrument* at a level that would be considered abnormal for that *financial instrument*; and
- (3) whether there are unsubstantiated rumours or dissemination of false or misleading information regarding the *financial instrument*.

The list above is not exhaustive and the *FSA* will consider such other factors as it considers appropriate.

2.5.3 G The *FSA* may consider that the price fall in a *financial instrument* is not disorderly, for example, if the *FSA* considers that there is legitimate cause for a price fall in trading, such as the announcement of poor financial results.

2.5.4 G The *FSA* will consider at least the following factors when assessing whether measures to prohibit or restrict short selling or otherwise limit transactions are necessary or likely to prevent a further disorderly decline in the price of the *financial instrument*:

- (1) the volume of trading in that *financial instrument* on the *trading venue* as compared with the total trading volume in the *financial instrument* over at least that *trading day*; and
- (2) whether the price of the *financial instrument* has stabilised after the significant fall in price.

The list above is not exhaustive and the *FSA* will consider such other factors as it considers appropriate.

- 2.5.5 G Where the *FSA* imposes measures under article 23 of the *short selling regulation* it will normally specify that the measures will not apply to natural or legal persons who have satisfied the criteria to use the *market maker exemption* or the *authorised primary dealer exemption* and who are included on the list maintained and published by *ESMA* pursuant to article 17(13) of the *short selling regulation*.

Exchange rate calculations

- 2.5.6 G
- (1) For the purposes of article 23(1)(b) of Commission Delegated Regulation (EU) No 918/2012 the *FSA* will convert the figure of EUR 0.50 into pounds sterling using the daily spot foreign exchange rate of Sterling to Euro of the Bank of England applicable at the end of the first *business day* of October 2012 rounded up to the nearest £0.01. The *FSA* will state this figure (the ‘sterling figure’) on its public website.
 - (2) The rate will be calculated on the same basis at the end of the first *business day* of October every subsequent year, unless the situation in (3) occurs in the intervening period, in which case the *FSA* will recalculate the sterling figure.
 - (3) The situation referred to in (2) is if the daily spot foreign exchange rate of the Bank of England of Sterling to Euro fluctuates for a period of 20 consecutive *business days* by more than 10% from the rate last used to calculate the sterling figure.
 - (4) If the situation in (3) occurs more than once in a year, the *FSA* will convert the figure of EUR 0.50 into pounds sterling using the daily spot foreign exchange rate of Sterling to Euro of the Bank of England applicable at the end of the 20th *business day* of the period referred to in (3).
- 2.5.7 G The *FSA* will treat the FTSE 100 index as the main national equity index of the Member State for the purposes of article 6(4) of Commission Implementing Regulation (EU) No 827/2012 and article 4 of Commission Delegated Regulation (EU) No 826/2012 and article 23(1) of Commission Delegated Regulation (EU) No 918/2012.

2.6 Procedures relating to the market maker exemption and the authorised primary

dealer exemption

Decision on use of the market maker exemption or the authorised primary dealer exemption

[**Note:** The *FSA* has powers under the *short selling regulation* to prohibit a natural or legal person from using the *market maker exemption* and the *authorised primary dealer exemption* if the *FSA* considers that that person does not satisfy the conditions of the exemption that that person has notified the *FSA* it intends to use.]

- 2.6.1 G Pursuant to the Financial Services and Markets Act 2000 (Short Selling) Regulations 2012 (SI 2012/2554), the *FSA* will direct how notifications to use the *market maker exemption* or the *authorised primary dealer exemption* shall be made. Such directions will be published on the *FSA* website and listed in *FINMAR 2 Annex 1G*.
- 2.6.2 G (1) If the *FSA* considers that a natural or legal person ('P') who has notified the *FSA* of his intention to use either the *market maker exemption* or the *authorised primary dealer exemption* does not satisfy the criteria to use the *market maker exemption* or the *authorised primary dealer exemption*, the *FSA* will send a letter to P setting out the reasons why it is minded to prohibit P from using the *market maker exemption* or the *authorised primary dealer exemption*.
- (2) P will be given the opportunity to make written representations to the *FSA* concerning P's use of the *market maker exemption* or the *authorised primary dealer exemption*.
- (3) The *FSA* will decide whether to prohibit P's use of either the *market maker exemption* or the *authorised primary dealer exemption* having regard to P's notification and any written representations made by P. The decision whether or not to prohibit the use by P of either the *market maker exemption* or the *authorised primary dealer exemption* will be made by senior staff members of the *FSA* who were not involved in the initial consideration of P's notification.

Review of a decision to prohibit the market maker exemption or the authorised primary dealer exemption

- 2.6.3 G If P is not satisfied with the *FSA*'s decision to prohibit P's use of the *market maker exemption* or the *authorised primary dealer exemption*, P may seek a review of the decision. This will be conducted by a group of at least three senior *FSA* staff. None of the group conducting the review will have been connected with the earlier decision taken in respect of P's use of the *market maker exemption* or the *authorised primary dealer exemption*. The review may take place after the expiry of the 30 day period in which the notification should be made under the *short selling regulation*, but within 3 months of the decision referred to in *FINMAR 2.6.2G(3)*.

After FINMAR 2.6 insert the following new Annex.

2 Annex 1G List of directions on how notifications to use the market maker exemption or authorised primary dealer exemption should be made

This table belongs to *FINMAR* 2.6.1G

[to follow]

Amend the following as shown.

Schedule 4 Powers Exercised

Sch 4.1G

The following powers and related provisions in or under the <i>Act</i> have been exercised by the <i>FSA</i> to make the <i>rules</i> , statements of policy and guidance in <i>FINMAR</i> :	
	Section 131B (Short selling rules)
	...

Annex C

Amendments to the General Provisions (GEN)

In this Annex, underlining indicates new text and striking through indicates deleted text.

Schedule 4 Powers exercised

...

Sch 4.2G

The following powers and related provisions in or under the <i>Act</i> have been exercised by the <i>FSA</i> to make the <i>rules</i> in <i>GEN</i> :	
	...
	<u>Section 131B (Short selling rules)</u>
	...

Annex D

Amendments to the Supervision manual (SUP)

In this Annex, underlining indicates new text.

2.3 Information gathering by the FSA on its own initiative: cooperation by firms

...

Access to premises

- 2.3.5 R (1) A *firm* must permit representatives of the *FSA*, or *persons* appointed for the purpose by the *FSA*, to have access, with or without notice, during reasonable business hours to any of its business premises in relation to the discharge of the *FSA*'s functions under the *Act* or its obligations under the *short selling regulation*.

...

Annex E

Amendments to the Decision Procedure and Penalties manual (DEPP)

In this Annex, underlining indicates new text and striking through indicates deleted text.

1.1 Application and Purpose

Application

- 1.1.1 G This manual (*DEPP*) is relevant to *firms, approved persons* and other *persons*, whether or not they are regulated by the *FSA*. It sets out:

...

- (3) the *FSA*'s policy with respect to the conduct of interviews by investigators appointed in response to a request from an ~~overseas regulator~~ overseas regulator or an EEA regulator (*DEPP* 7).

Purpose

- 1.1.2 G The purpose of *DEPP* is to satisfy the requirements of sections 63C(1), 69(1), 93(1), 124(1), 131FA, 131J(1), 169(9), 210(1) and 395 of the *Act* that the *FSA* publish the statements of procedure or policy referred to in *DEPP* 1.1.1G.

...

7 **Statement of policy on ~~section 169(7)~~ interviews conducted on behalf of overseas and EEA regulators**

...

Application

- 7.1.1 G *DEPP* 7 applies when the *FSA*:
- (1) has appointed an investigator at the request of an *overseas regulator*, under section 169(1)(b) (Assistance to overseas regulators) or of an EEA regulator under section 131FA of the *Act*; and
 - (2) has directed, or is considering directing, the investigator, under section 169(7) or section 131FA of the *Act*, to permit a representative of the *overseas regulator* or of the EEA regulator to attend, and take part in, any interview conducted for the purposes of the investigation.
- 7.1.2 G In *DEPP* 7, a "~~section 169(7) requested~~ requested interview" means any interview conducted for the purposes of an investigation under section 169(1)(b) or section 131FA of the *Act* in relation to which the *FSA* has given a direction under section 169(7) or section 131FA of the *Act*.

Purpose

- 7.1.3 G The purpose of *DEPP 7* is to set out the *FSA*'s statement of policy on the conduct of interviews to which a direction under section 169(7) or section 131FA has been given or the *FSA* is considering giving. The *FSA* is required to prepare and publish this statement of policy by section 169(9) and (11) and section 131FA of the *Act*. As required by section 169(10) and section 131FA of the *Act*, the Treasury has approved the statement of policy.
- 7.1.4 G The *FSA* is keen to promote co-operation with *overseas regulators* and EEA regulators. It views provision of assistance to *overseas regulators* and EEA regulators as an essential part of the principles set out in section 2(3)(e) of the *Act* to which it must have regard in discharging its general functions.

...

Appointment of investigation and confidentiality of information

- 7.2.1 G Under section 169(1)(b) and section 131FA of the *Act*, the *FSA* may appoint an investigator to investigate any matter at the request of an *overseas regulator* or EEA regulator. The powers of the investigator appointed by the *FSA* (referred to here as the '*FSA*'s investigator') include the power to require *persons* to attend at a specified time and place and answer questions (the compulsory interview power).
- 7.2.2 G Where the *FSA* appoints an investigator in response to a request from an *overseas regulator* or EEA regulator it may, under section 169(7) or section 131FA of the *Act*, direct him to permit a representative of that regulator to attend and take part in any interviews conducted for the purposes of the investigation. The *FSA* may only give a direction under section 169(7) or section 131FA if it is satisfied that any information obtained by an *overseas regulator* or EEA regulator as a result of the interview will be subject to the safeguards equivalent to those contained in Part XXIII (Public Record, Disclosure of Information and Cooperation) of the *Act*.

...

Policy on use of investigative powers

- 7.2.4 G The *FSA*'s policy on how it will use its investigative powers, including its power to appoint investigators, in support of *overseas regulators* and EEA regulators, is set out in the *FSA*'s Enforcement Guide (*EG*).

Use of direction powers

- 7.2.5 G The *FSA* may need to consider whether to use its direction power at two stages of an investigation:
- (1) at the same time that it considers the request from the *overseas regulator* or EEA regulator to appoint investigators;

- (2) after it has appointed investigators, either at the request of the *overseas regulator* or *EEA regulator* or on the recommendation of the investigators.

- 7.2.6 G Before making a direction under section 169(7) or section 131FA the *FSA* will discuss and determine with the *overseas regulator* or *EEA regulator* how this statement of policy will apply to the conduct of the interview, taking into account all the circumstances of the case. Amongst other matters, the *FSA* will at this stage determine the extent to which the representative of the *overseas regulator* or *EEA regulator* will be able to participate in the interview. The *overseas regulator* or *EEA regulator* will be notified of this determination on the issuing of the direction.
- 7.2.7 G The direction will contain the identity of the representative of the *overseas regulator* or *EEA regulator* that is permitted to attend any interview and the role that he will play in the interview. If the *FSA* envisages that there will be more than one interview in the course of the investigation, the direction may also specify which interview(s) the ~~overseas~~ representative is allowed to attend.

Conduct of interview

...

- 7.2.9 G The *FSA's* investigator will act on behalf of the *FSA* and under its control. He may be instructed to permit the representative of the *overseas regulator* or *EEA regulator* to assist in the preparation of the interview. Where the *FSA* considers it appropriate, it may permit the representative to attend and ask questions of the interviewee in the course of the interview. The interview will be conducted according to the terms of the direction and the notification referred to in *DEPP* 7.2.6G
- 7.2.10 G If the direction does permit the representative of an *overseas regulator* or *EEA regulator* to attend the interview and ask the interviewee questions, the *FSA's* investigator will retain control of the interview throughout. Control of the interview means the following will apply:
- (1) The *FSA's* investigator instigates and concludes the interview, introduces everyone present and explains the procedure of the interview. He warns the interviewee of the possible consequences of refusing to answer questions and the uses to which any answers that are given can and cannot be put. The *FSA's* investigator will always ask preliminary questions, such as those establishing the identity of the interviewee.
 - (2) The *FSA's* investigator determines the duration of the interview and when, if at all, there should be any breaks in the course of it.
 - (3) The *FSA's* investigator has responsibility for making a record of the interview. The record should note the times and duration of any breaks in the interview and any periods when the representative of the *overseas regulator* or *EEA regulator* was either present or not present.

- (4) Where the *FSA*'s investigator considers it appropriate, he may either suspend the interview, ask the overseas representative to leave the interview, or terminate the interview and reschedule it for another occasion. In making that decision he will bear in mind the terms of the direction, any agreement made with the *overseas regulator* or *EEA regulator* as to the conduct of the interview and the contents of this statement of policy.
- 7.2.11 G The *FSA* will in general provide written notice of the appointment of an investigator to the *person* under investigation pursuant to the request of an *overseas regulator* or *EEA regulator*. Whether or not the interviewee is the *person* under investigation, the *FSA*'s investigator will inform the interviewee of the provisions under which he has been appointed, the identity of the requesting authority and general nature of the matter under investigation. The interviewee will also normally be informed if a representative of the *overseas regulator* or *EEA regulator* is to attend and take part in the interview. Notification of any of these matters may not be provided in advance of the interview if the *FSA* believes that the circumstances are such that notification would be likely to result in the investigation being frustrated.
- 7.2.12 G The interviewee will normally be given a copy of the direction issued under section 169(7) or section 131FA in advance of the interview unless to do so would be likely to result in the investigation being frustrated. The interviewee will also be provided with a copy of this statement of policy.
- ...
- 7.2.14 G When the *FSA*'s investigator has exercised the compulsory interview power, at the outset of the interview the interviewee will be given an appropriate warning. The warning, amongst other things, must state that the interviewee is obliged to answer all questions put to them during the interview, including any put by the representative of the *overseas regulator* or *EEA regulator*. It will also state that in criminal proceedings or proceedings for *market abuse* the *FSA* will not use as evidence against the interviewee any information obtained under compulsion during the interview.
- 7.2.15 G The *FSA*'s investigator may decide which *documents* or other information may be put to the interviewee, and whether it is appropriate to give the interviewee sight of the documents before the interview takes place. Where the *overseas regulator* or *EEA regulator* wishes to ask questions about *documents* during the interview and the *FSA*'s investigator wishes to inspect those *documents* before the interview, he will be given the opportunity to do so. If the *FSA*'s investigator wishes to inspect them and has not been able to do so before the interview, he may suspend the interview until he has had an opportunity to inspect them.
- 7.2.16 G When the *FSA*'s investigator has exercised the compulsory interview power, the *FSA*'s investigator will require the *person* attending the interview to answer questions. Where appropriate, questions may also be posed by the representative of the *overseas regulator* or *EEA regulator*. The interviewee

will also be required to answer these questions. The *FSA*'s investigator may intervene at any stage during questioning by the representative of the *overseas regulator* or *EEA regulator*.

Language

- 7.2.17 G Interviews will, in general, be conducted in English. Where the interviewee's first language is not English, at the request of the interviewee arrangements will be made for the questions to be translated into the interviewee's first language and for his answers to be translated back into English. If a translator is employed at the request of the representative of the *overseas regulator* or *EEA regulator* then the translation costs will normally be met by the *overseas regulator* or *EEA regulator*. Where interviews are being conducted in pursuance of an *EU* law obligation these costs will be met by the *FSA*. In any event, the meeting of costs in relation to translators and, where applicable, the translation of documents will always be agreed in advance with the *overseas regulator* or *EEA regulator*.

Tape-recording

- 7.2.18 G All compulsory interviews will be tape-recorded. The method of recording will be decided on and arranged by the *FSA*'s investigator. Costs will be addressed similarly to that set out in the preceding paragraph. The *FSA* will not provide the *overseas regulator* or *EEA regulator* with transcripts of the tapes of interviews unless specifically agreed to, but copies of the tapes will normally be provided where requested. The interviewee will be provided with a copy of tapes of the interview but will only be provided with transcripts of the tapes or translations of any transcripts if he agrees to meet the cost of producing them.

Representation

- 7.2.19 G The interviewee may be accompanied at the interview by a legal adviser or a non-legally qualified observer of his choice. The costs of any representation will not be met by the *FSA*. The presence at the interview of a representative of the *overseas regulator* or *EEA regulator* may mean that the interviewee wishes to be represented or accompanied by a *person* either from or familiar with that regulator's jurisdiction. As far as practical the arrangements for the interview should accommodate this wish. However, the *FSA* reserves the right to proceed with the interview if it is not possible to find such a *person* within a reasonable time or no such *person* is able to attend at a suitable venue.
- 7.2.20 G In relation to the publication of investigations by *overseas regulators* or *EEA regulators*, the *FSA* will pursue a policy similar to the policy that relates to its own investigations.

...

Sch 3.2G

The <i>FSA</i> 's power to impose financial penalties is contained in:
--

	<u>section 131G (Power to impose penalty or issue censure) of the <i>Act</i></u>
	section 206 (Financial penalties) of the <i>Act</i>
	...

Sch 4.1 G

The following powers and related provisions in or under the <i>Act</i> have been exercised by the <i>FSA</i> to make the statements of policy in <i>DEPP</i> :	
	...
	Section 131J (<u>Impositions of penalties under section 131G: Statement statement of policy</u>)
	...

...

Annex F

Amendments to the Enforcement Guide (EG)

In this Annex, underlining indicates new text and striking through indicates deleted text.

1 Introduction

...

1.2 In the areas set out below, the *Act* expressly requires the FSA to prepare and publish statements of policy or procedure on the exercise of its enforcement and investigation powers and in relation to the giving of *statutory notices*.

...

(3) ...

(3-A) section 131FA requires the FSA to publish a statement of its policy on the conduct of certain interviews in response to requests from *EEA regulators*; and

(3A) ...

...

...

Assisting overseas regulators

2.16 The FSA views co-operation with its overseas counterparts as an essential part of its regulatory functions. Section 354 of the *Act* imposes a duty on the FSA to take such steps as it considers appropriate to co-operate with others who exercise functions similar to its own. This duty extends to authorities in the UK and overseas. In fulfilling this duty the FSA may share information which it is not prevented from disclosing, including information obtained in the course of the FSA's own investigations, or exercise certain of its powers under Part XI of the *Act*. Further details of the FSA's powers to assist overseas regulators are provided at *EG* 3.12 – 3.15 (Investigations to assist overseas authorities), *EG* 3.15A – D (Information requests and investigations to assist *EEA regulators* in relation to short selling), *EG* 4.8 (Use of statutory powers to require the production of documents, the provision of information or the answering of questions), *EG* 4.25 – 4.27 (Interviews in response to a request from an overseas regulator or *EEA regulator*), and *EG* 8.18 – 8.25 (Exercising the power under section 47 to vary or cancel a firm's part IV permission in support of an overseas regulator). The FSA's statement of policy in relation to interviews which representatives of overseas regulators or *EEA regulators* attend and participate in is set out in *DEPP* 7.

...

Use of information gathering and investigation powers

- 3.1 The FSA has various powers under sections 97, 131E, 131FA, 165 to 169 and 284 of the *Act* to gather information and appoint investigators, and to require the production of a report by a *skilled person*. In any particular case, the FSA will decide which powers, or combination of powers, are most appropriate to use having regard to all the circumstances. Further comments on the use of these powers are set out below.

...

Information requests and investigations to assist EEA regulators in relation to short selling

- 3.15A The FSA may use its section 131E power to require information and documents from natural or legal persons to support both its monitoring and its enforcement functions.
- 3.15B An officer with authorisation from the FSA may exercise the section 131E power to require information and documents from natural or legal persons. This includes an FSA employee or an agent of the FSA.
- 3.15C The FSA's power to conduct investigations to assist *EEA regulators* in respect of the *short selling regulation* is contained in section 131FA of the *Act*. The section provides that at the request of an *EEA regulator* or ESMA, the FSA may either use its power under section 131E to require the production of information, or appoint a person to investigate any matter.
- 3.15D Section 131FA states that the FSA must, in deciding whether or not to exercise its investigative power, consider whether the exercise of that power is necessary to comply with an obligation under the *short selling regulation*.

...

Use of statutory powers to require the production of documents, the provision of information or the answering of questions

- 4.8 The FSA's standard practice is generally to use statutory powers to require the production of documents, the provision of information or the answering of questions in interview. This is for reasons of fairness, transparency and efficiency. It will sometimes be appropriate to depart from this standard practice, for example:

...

- (3) In some cases, the FSA is asked by *overseas regulators* or *EEA regulators* to obtain documents or conduct interviews on their behalf. In these cases, the FSA will not necessarily adopt its standard approach as it will consider with the *overseas regulator* or *EEA regulator* the most appropriate method for obtaining evidence for use in their country.

...

Interviews in response to a request from an overseas regulator or EEA regulator

4.25 Where the FSA has appointed an investigator in response to a request from an *overseas regulator* or *EEA regulator*, it may, under ~~section~~ sections 169(7) or 131FA of the *Act* respectively, direct the investigator to allow a representative of that regulator to attend, and take part in, any interview conducted for the purposes of the investigation. However, the FSA may only use this power if it is satisfied that any information obtained by an *overseas regulator* or *EEA regulator* as a result of the interview will be subject to safeguards equivalent to those in Part XXIII of the *Act* (~~section~~ sections 169(8) and 131FA respectively).

...

4.27 Under ~~section~~ sections 169(9) and 131FA respectively, the FSA is required to prepare a statement of policy with the approval of the Treasury on the conduct of interviews attended by representatives of *overseas regulators* or *EEA regulators*. The statement is set out in *DEPP 7*.

...

7.2 The FSA has the following powers to impose a financial penalty and to publish a *public censure*.

(1) It may publish a statement:

...

(ea) if a ~~person~~ natural or legal person has contravened any provision of the short selling rules regulation, or any requirement imposed on ~~the person~~ that person under section 131E or 131F, under section 131G of the *Act*; and

...

(2) It may impose a financial penalty:

...

(ca) on a ~~person~~ natural or legal person who has contravened any provision of the short selling rules regulation, or any requirement imposed on ~~the person~~ that person under section 131E or 131F, or any ~~person~~ natural or legal person who was knowingly concerned in the contravention, under section 131G of the *Act*; and

...

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