

Policy rule in relation to the definition and the calculation of a short position as defined in the Wft



The Netherlands Authority for the Financial Markets

The AFM promotes fairness and transparency within financial markets. We are the independent supervisory authority for the savings, lending, investment and insurance markets. The AFM promotes the conscientious provision of financial services to consumers and supervises the honest and efficient operation of the capital markets. Our aim is to improve consumers' and the business sector's confidence in the financial markets, both in the Netherlands and abroad. In performing this task the AFM contributes to the prosperity and economic reputation of the Netherlands.

Policy Rule

Policy rule of the Netherlands Authority for the Financial Markets in relation to the definition and the calculation of a short position as defined in the Wft

After public consultation, the Netherlands Authority for the Financial Markets (AFM) has decided on the following with reference to Section 5:38 subsection (3) and Section 5:39 subsection (2) of the Financial Supervision Act [Wet op het financieel toezicht, or Wft] and Section 5 of the Disclosure of Major Holdings and Capital Interests in Securities-Issuing Institutions Decree pursuant to the Wft [Besluit melding zeggenschap en kapitaalbelang in uitgevende instellingen Wft]:

Statutory framework

Section 5:38 subsection (3) Wft states that a party that obtains or loses the disposal of financial instruments representing a short position in relation to the shares which it knows or should know will make the percentage of the capital at its disposal reach, exceed or fall below a threshold, shall notify the AFM accordingly without delay.

Regulations may be established by or pursuant to order in council in relation to the determination of a short position as referred to in this subsection.

A subsection will be added to Section 5:39 to include the requirement to notify a short position that reaches, exceeds or falls below a threshold due to a passive change as a result of a change to the capital.

This is a Policy Rule as referred to in Article 1:3 (4) of the General Administrative Law Act [Algemene wet bestuursrecht, or Awb]. The AFM's authority to establish this Policy Rule is based on Section 4:81 subsection (1) Awb.

Policy Rule

I. The definition of terms used in Section 5.3 Wft and the provisions pursuant thereto are as follows:

short position: a position in the issued capital of an issuing institution that arises from one of the following cases:

- a) A short transaction in a share issued by or with the cooperation of an issuing institution¹;
- b) Entering into a transaction that creates a financial instrument other than that referred to in item a) or that is linked thereto whereby the result or one of the results thereof is that the party entering into the transaction receives a financial gain in the event that the price or the value of the share falls.

II. The calculation of a short position as referred to in Section 5.3 Wft must be based on the following:

- i) A short transaction in a share via a short transaction in the index or the basket of shares will not qualify, unless the share in the index or basket represents 1% or more of the total number of issued shares of the same type, or the share represents 20% or more of the value of the securities in the index or basket, or both;
- ii) A position in a financial instrument, including those listed in Annex I Part I of the Commission Delegated Regulation², will qualify if this position confers a financial advantage in the event of a decrease in the price or value of the share (Article 6 paragraph (2) of the Commission Delegated Regulation);
- iii) It is irrelevant whether a cash settlement or physical delivery of the underlying assets has been agreed (Article 7 (a) of the Commission Delegated Regulation);

¹ 'Share' as defined in Section 5:33 subsection (1) at (b) items (1) and (2) Wft.

² Commission Delegated Regulation (EU) no. 918/2012 of the European Commission of 5 July 2012.

- iv) Short positions in financial instruments that give rise to a claim to unissued shares and subscription rights, convertible bonds and other comparable instruments shall not be considered as short positions when calculating a short position (Article 7 (b) of the Commission Delegated Regulation);
- v) The short position must be calculated using the delta-adjusted model described in Annex II Part 1 of the Commission Delegated Regulation (Article 10 (1) of the Commission Delegated Regulation);
- vi) Account must be taken of transactions in all financial instruments, whether on or outside a trading venue, that confer a financial advantage in the event of a decline in the price or value of the share (Article 10 (3) of the Commission Delegated Regulation);
- vii) Allocation is made on the basis of Articles 12 and 13 of the Commission Delegated Regulation;
- viii) No set-off is permitted between a long position and a short position, however purchase and sale transactions in the same financial instrument relating to the same issuing institution during the trading day may be set off (netted), whereby at the end of the day the total of the gross short position in the issuing institution in question must be notified (if this reaches, exceeds or falls below a threshold).

Final provisions

The announcement of this Policy Rule shall be by publication in the Government Gazette.

The policy rule takes effect on 1 July 2013. This policy rule is designated as:

Policy rule in relation to the definition and the calculation of a short position as defined in the Wft

Amsterdam, 20 June 2013

The Netherlands Authority for the Financial Markets

Director
Th. F. Kockelkoren, MBA

Director
G.J. Everts RA

EXPLANATORY NOTE

I.

A number of elements are important for the definition of a short position in the sense of the Wft:

- 1) Financial instrument
- 2) Short position
- 3) Short transaction

1) the definition of a financial instrument must correspond to the current definition of a financial instrument as given in Section 1:1 Wft.

2) the definition of a short position is given in the Regulation and the Commission Delegated Regulation and this definition will be used.

A position arising from one of the following will qualify as a short position in the capital of an issuing institution:

- a) A short transaction in a share issued by or with the cooperation of an issuing institution³;
- b) Entering into a transaction that creates a financial instrument other than that referred to in item a) or that is linked thereto whereby the result or one of the results thereof is that the party entering into the transaction receives a financial gain in the event that the price or the value of the share falls.

3) the term 'short transaction' is defined in Article 2 (1)(b) of the Regulation.

II.

II. i) The Policy Rule will follow the method for the calculation of shares to which financial instruments relate and the notification requirement for cash settled instruments with respect to the notification requirement for indices and baskets.

The position held by the party in question via or by means of an index or basket of shares must be calculated using publicly available information on the composition of the index or basket concerned.

³ 'Share' as defined in Section 5:33 subsection (1) at (b) items (1) and (2) Wft.

Parties are assumed to have made their best efforts to obtain the most recent information with regard to the composition.

II. vii) Article 12 of the Commission Delegated Regulation applies, however the investment strategy described in Article 12 (2)(a) can only refer to short positions.

The management entity as described in paragraph 3 will of course only aggregate the short positions held in the funds and portfolios under its management for which the strategy is focused on short positions in relation to a particular issuing institution.

Article 13 of the Commission Delegated Regulation applies, however only the short positions of all the legal entities constituting a group will be aggregated and may not be set off. The notification thresholds as stated in Section 5:38 subsection (4) and Section 5:39 subsection (3) Wft shall of course apply. Notification of the short position to the AFM shall be made taking account of Section 5.3 Wft and the Disclosure of Major Holdings and Capital Interests in Securities-Issuing Institutions Decree pursuant to the Wft.

II. viii) It is a statutory requirement that gross short positions are notified in the event that a threshold is reached, exceeded or fallen below. This may therefore not be set off against the long position.

After discussion with various participations in the consultation regarding the draft policy rule, the policy rule has been amended to correspond more closely to actual practice while the relevant information in the register will continue to be available to investors.

The policy rule is now formulated so that purchase and sale transactions in the same financial instrument relating to the same issuing institution during the trading day may be set off (netted), whereby at the end of the day the total of the gross short position in the issuing institution in question must be notified (if this reaches, exceeds or falls below a threshold). This therefore applies to shares, but also to derivative instruments if these have the same features. This is in line with the system that already applies regarding the requirement to notify long positions that reach, exceed or fall below a threshold.

For example: the sale of option "C XYZ Jun 8" on trading day 1 may be netted off against a purchase of the same option "C XYZ Jun 8" on trading day 1. This sale of option "C XYZ Jun 8" may not be netted off against the purchase of an option "C XYZ Oct 8", or against the purchase of a future in the same underlying share. The sale may also not be netted off against a purchase of shares. In addition, the total gross short position at the end of the trading day in question may be calculated by counting all the short positions there are at product level to arrive at a total gross short position in an underlying share.

An example as an illustration:

The issuing institution's total issued capital is 1000.

Assuming a position of 0 at the start of the trading day in question, the following transactions in a single issuing institution are initiated during the trading day:

Purchase or sale	Product	Instrument	Number
Purchase	Share	XYZ	5
Sale	Share	XYZ	-20
Purchase	Share	XYZ	25
Purchase	Share	XYZ	15
Purchase	Option	C XYZ Jun 8	25
Sale	Option	C XYZ Jun 8	-10
Purchase	Option	P XYZ Jun 8	5
Sale	Option	P XYZ Jun 8	-5
Sale	Option	C XYZ Oct 8	-20
Sale	Future	XYZ futures Jun 13	-5
Sale	Future	XYZ futures Jun 13	-5

The above transactions lead to the following positions at the end of the day (netted off by the same instrument, but not by underlying share).

Product	Position	Percentage
Share	25	2.50%
Option C XYZ Jun 8	15	1.50%
Option P XYZ Jun 8	0	0.00%
Option C XYZ Oct 8	-20	-2.00%
XYZ futures Jun 13	-10	-1.00%

This results in the total long and short positions shown below. The individual long positions per instrument are thus counted to generate one long position and the individual short positions to one gross short position.

Long/short	Position	Percentage
Long	40	4.00%
Gross short	-30	-3.00%

Based on the notification threshold of 3%, this leads to notification of a substantial interest (long position) of 4% and a short position of 3% to the AFM.

This policy rule does not change the fact that parties must comply with the requirements pursuant to the Regulation on short selling and certain aspects of credit default swaps and the Commission Delegated Regulation⁴.

For the record, it is noted that the Policy Rule regarding the method for the calculation of shares to which financial instruments relate and the notification requirement for cash settled instruments with respect to the notification requirement for indices and baskets will continue to apply in full.

⁴ Regulation (EU) no. 236/2012 of the European Parliament and of the Council of 14 March 2012 and the Commission Delegated Regulation (EU) no. 918/2012 of the Commission of 5 July 2012.

The Netherlands Authority for the Financial Markets

T + 020 797 2000 | F +020 797 3800

Postbus 11723 | 1001 GS Amsterdam

www.afm.nl

