

COMMENT LETTER

August 17, 2011

ICI Letter on Regulatory Action on Short Selling in the European Union (pdf)

August 17, 2011 Steven Maijoor Chair European Securities and Markets Authority 103 Rue de Grenelle 75007 Paris France Re: Regulatory Action on Short Selling in the European Union Dear Chairman Maijoor: The Investment Company Institute ("ICI") is writing to respond to the decision by several European regulatory authorities to impose or extend existing short selling bans and restrictions in their respective countries and to the European Securities and Markets Authority's ("ESMA") statement addressing the regulatory action. As discussed further below, while ICI strongly supports regulatory action to address abusive and manipulative short selling, we do not support a ban or substantial restrictions on short selling as the means to address regulators' concerns. ICI is the national association of U.S. investment companies, including mutual funds, closed- end funds, exchange-traded funds ("ETFs"), and unit investment trusts ("UITs").¹ The structure and efficient operation of the global financial markets has a significant impact on ICI members, who are investors of over \$13 trillion of assets on behalf of over 90 million individual shareholders.² U.S. registered investment companies and their shareholders therefore have a strong interest in ensuring that the global financial markets are highly competitive, transparent and efficient, and that the regulatory structure that governs the financial markets encourages, rather than impedes, liquidity, transparency, and price discovery. Consistent with these goals, ICI has supported efforts to address issues relating to

¹ ICI seeks to encourage adherence to high ethical standards, promote public understanding, and otherwise advance the interests of funds, their shareholders, directors, and advisers. ² According to ICI data, as of March 2011, U.S. based long-term mutual funds held \$2.4 trillion in non-U.S. securities, accounting for almost 25 percent of the assets of these funds. For more information on the U.S. registered investment company industry, see 2011 Investment Company Institute Fact Book at www.icifactbook.org. Mr. Steven Maijoor August 17, 2011 Page 2 of 4 short selling that may impact the fair and orderly operation of the financial markets and investor confidence in those markets.³ Short selling is an integral part of an efficient and effective trading environment, playing an important role in providing market liquidity and price discovery, as well as in investment strategies and risk management activities designed to enhance fund performance and maximize returns to investors. For this reason, legitimate and lawful short selling must be allowed to continue. ICI recognizes regulators' concerns about the impact on investor confidence of recent market events. Short selling, as with any other type of trading, should be subject to appropriate controls to minimize the potential risks it could have on the orderly and efficient functioning and stability of the financial markets. At the same time, we do not support a ban or substantial restrictions on short selling as the means to address these risks. As we experienced in the United States in response to the market events in 2008, it is

unclear from available empirical data whether a short selling ban addresses abusive or manipulative behavior, increases investor confidence or alleviates market volatility. In fact, the emergency short sale ban implemented in the United States at that time on the publicly traded securities of certain financial institutions did not improve confidence in the markets or prevent the prices of those particular stocks from declining; studies have shown that the U.S. short sale ban instead reduced liquidity and increased volatility in the markets.⁴ In addition, the unintended consequences of a ban on short selling are uncertain. Specifically, a ban could decrease market efficiency and price discovery, and result in a less efficient allocation of capital. None of these outcomes would benefit investors. Thus, we believe the potential costs

3 See, e.g., Letters from Ari Burstein, Associate Counsel, Investment Company Institute, to Jonathan G. Katz, Secretary, Securities and Exchange Commission, dated January 5, 2004, available at <http://www.ici.org/pdf/16938.pdf>; Paul Schott Stevens, President and CEO, Investment Company Institute, to Christopher Cox, Chairman, Securities and Exchange Commission, dated September 19, 2008, available at http://www.ici.org/pdf/comment_leakage_08.pdf; Ari Burstein, Senior Counsel, Investment Company Institute, to Florence Harmon, Acting Secretary, Securities and Exchange Commission, dated December 16, 2008, available at <http://www.ici.org/pdf/23128.pdf>; Heather Traeger, Assistant Counsel, Investment Company Institute, to Florence Harmon, Acting Secretary, Securities and Exchange Commission, dated December 16, 2008, available at <http://www.ici.org/pdf/23128.pdf>; and Ari Burstein, Senior Counsel, Investment Company Institute, to Greg Tanzer, Secretary General, IOSCO, dated May 18, 2009, available at

http://www.ici.org/pdf/comment_051809_iosco_consult.pdf. See also Industry Statement from ICI (USA), IMA (UK) and IFSA (Australia), dated January 6, 2009, available at http://www.ici.org/policy/current_issues/09_news_short_selling. 4 See, e.g., Shackling Short Sellers: The 2008 Shorting Ban, Boehmer, Jones, and Zhang, September 25, 2009 and The 2008 Short Sale Ban: Liquidity, Dispersion of Opinion, and the Cross-Section of Returns of U.S. Financial Stocks, Autore, Billingsley, and Kovacs, January 19, 2011. Mr. Steven Maijoor August 17, 2011 Page 3 of 4 associated with a short sale ban may outweigh any potential benefits of such a restriction. For these reasons, we believe a ban on short selling is not warranted at this time. To be clear, ICI strongly supports action against abusive and manipulative behavior relating to short selling. We support ESMA emphasizing in its statement the requirements in the Market Abuse Directive prohibiting the dissemination of information which gives, or is likely to give, false or misleading signals as to financial instruments. We believe regulators should continue to examine regulatory tools, such as short selling anti-fraud rules and rules inhibiting abusive “naked” short selling, to address potentially abusive or manipulative behavior. In the United States, we have seen that these types of rules can add necessary protections to the markets and address concerns relating to short selling. Finally, as regulators examine their current, and consider future, initiatives relating to short sales, we strongly support the coordination by regulators to ensure sensible cross-border regulations in this area. Varying regulations in different jurisdictions result in inconsistent rules and uncertainty for investors. Many ICI members operate with interconnected trading desks in several locations around the world. Our increasingly global markets therefore demand cooperation among regulators as funds pursue an increasing cross-border presence in the interest of shareholders. * * * * ICI offers its assistance to ESMA as it continues to examine the issues surrounding short selling and their impact on the financial markets. If you have any questions on our letter, please feel free to contact me directly at (202) 326-5815, or Ari Burstein at (202) 371-5408. Sincerely, /s/ Karrie McMillan Karrie McMillan General Counsel Mr. Steven Maijoor August 17, 2011 Page 4 of 4 Cc: Jean-Pierre Jouyet, Chairman, Autorité des Marchés Financiers François Baroin, Ministre de l'Économie, des Finances et de l'Industrie, Ministère de l'Économie, des Finances et de

I'Industrie Giuseppe Vegas, Chairman, Commissione Nazionale per le Società e la Borsa
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