August 23, 2013
International Bankers Association of Japan

FSA answers to IBA comment on the draft revisions to short selling regulations (published on August 21, 2013)

1. Reporting and publication of short selling positions

	Relevant provisions	IBA comment	FSA answer
1	Overall (perpetuation of the "temporary" framework)	We would hope that the FSA will clarify why the reporting and publication requirements are necessary and to what extent the requirements are likely to be effective. "Prior Assessment of Regulation", conducted for these regulations in November, 2008 and April, 2013, did not sufficiently address these issues. For example, under the current regulations, a short position must be reported by 10:00am, two days after the transaction, and this data is then forwarded to an exchange and published. Thus, the published data are two days old and positions are likely to have changed during these two days. This "time lag" problem would not be resolved even by the introduction of a change report (0.2, 0.3, 0.4%….). It is not clear that this regulation would have any influence on the market other than revealing the names of investors and names of stocks they short.	No answer was provided.
2	Paragraph 1, Article 15-2, Draft Cabinet Office Ordinance on Regulations on	Please enlighten us on the institutional framework in which market participants can specify the "main financial instruments exchange" to which the position information must be provided.	We expect that necessary measures will be taken by relevant parties such as financial instruments exchanges to ensure smooth implementation. (No. 28)

	Relevant provisions	IBA comment	FSA answer
	Transactions in Securities, etc. (the "Draft Cabinet Office Ordinance")		
3	Item 1, Paragraph 1, Article 15-2, Draft Cabinet Office Ordinance	The proposal includes lowering the reporting threshold from 0.25% to 0.2%. Any change would require market participants to change their IT systems, etc. What exactly is the incremental benefit from lowering the threshold by 0.05%? Would any incremental benefit more than offset the additional costs from IT system changes, etc.? The "Prior Assessment of Regulation" published on April 30, 2013 states that "the regulatory framework needs to be reviewed holistically in light of the regulatory trends in various other countries" (4.(1)②), but this explanation does not seem sufficient. Japan has been administering the threshold of 0.25%, since October 2008, while the EU has introduced the threshold of 0.2% only recently in November, 2012). What is the FSA's assessment of the past four years' experience?	The current regulations were introduced as a temporary measure at the time of the Lehman shock. Since then it has been intended that the regulations would be reviewed holistically with the aim of introducing permanent measures in the future, taking into considerations such factors as developments in various other countries. The reporting threshold under these revised regulations is set at 0.2%, taking into account such factors as the regulatory developments in Europe, as you have pointed out. (No. 29)
4	Same as above	We believe the proposal should refer to "exchanges", not "exchange members" - this would sort out reports exceeding the publication threshold, from those below	It is necessary for financial instruments exchanges and regulatory authorities to grasp movements in short selling positions of a certain size. Accordingly, there is significance

	Relevant provisions	IBA comment	FSA answer
		the threshold.	in requiring the reporting of positions smaller than the reporting threshold. (No. 30)
5	Item 2, Paragraph 1, Article 15-2, Draft Cabinet Office Ordinance	Although the "Prior Assessment of Regulation" (published on April 30, 2013) states that "with regard to position reporting and publication, as the introduction of the change report threshold will eliminate the need to report changes within the threshold, costs of reporting by parties such as financial instruments firms will decrease" (6.(1)①a), the introduction of a change report would require changes to IT systems and increased administrative burdens. We would hope that exchanges will continue to be allowed to accept reports from investors and exchange participants who report in accordance with the current regulations but not with the change threshold, to contain their burden of switching to the new reporting system.	It is considered acceptable to report voluntarily even where the position falls short of the reporting threshold. In the event of such reporting, the previous short selling position ratio (to be reported pursuant to Item 8, Paragraph 1, Article 15-3 of the Cabinet Office Ordinance) must be the position information actually reported most recently on a voluntary basis. (No. 31)
6	Same as above	The draft provision stipulates that the position information must be provided ñwhen the ratio of the short selling position changesò. Does this mean that the position information must be provided when the change in the ratio is caused solely by the change in the number of outstanding shares, even where there	Your understanding is correct. (No. 33)

	Relevant provisions	IBA comment	FSA answer
		has been no transaction?	
7	Article 26-5, Draft Cabinet Order for Enforcement of the Financial Instruments and Exchange Act ("Draft Cabinet Order")	Is our understanding correct that the proposed requirement would not include short-positions of derivatives transactions?	Your understanding is correct. (No. 25)
8	Paragraph 2, Article 26-5, etc., Draft Cabinet Order	The public release entitled "A Comprehensive Review of Short Selling Regulations (Draft)" (published on March 7, 2013) explained that an "investor" must report to exchanges "through exchange members". Is our understanding correct that exchange members would have only to forward reports received from investors? In the draft Cabinet Office Ordinance, the deadline for an exchange participant to submit the position information received from the client to the exchange has been tightened from "without delay" to "immediately". Is our understanding correct that this is premised upon the fact that exchange participants are not in a position to verify the accuracy of reports received from investors?	Accurate reporting is required because position reporting is important from the standpoint of fair price formation. But as you point out, it is not intended to require exchange participants to strictly verify the accuracy of the position information. (No. 36)

	Relevant provisions	IBA comment	FSA answer
9	Paragraphs 2 through 6, Article 15-2, Draft Cabinet Office Ordinance	When providing the position information to the exchange, firms must do so "together with the name and address" of the client. Therefore exchanges currently require firms to submit a report on the "name and address" separately from the report on the position information. However, where the client is a legal entity, the name and address are included in the position information as mandatory items. Thus there is a certain degree of administrative burden from having to duplicate the information despite the lack of necessity for it. Therefore, we request that the relevant provisions be amended so that the additional information about "the name and address" will be required for natural persons only.	No answer was provided.
10	Item 8, Paragraph 1, Article 15-3, Draft Cabinet Office Ordinance	We believe the proposal of linking the change report with the previous report (the date and the ratio of the short position reported last time) should also be withdrawn, as the burden on IT system to retrieve and store the data (data for the previous report) and reconcile them for each stock would be significant and the added benefits not worth the costs.	The date and the ratio of the short position reported last time are considered as necessary information for the purpose of grasping the behavior of persons who have short selling positions of a certain size. (No. 40)

	Relevant provisions	IBA comment	FSA answer
11	Paragraph 2, Article 15-3, Draft Cabinet Office Ordinance	Types of transactions excluded from the calculation of the "position amount" are grossly inconsistent among exchange transactions, transactions in OTC registered stocks and transactions through PTSs. This would not just cause confusion but is also undesirable because it would impose inconsistent regulations. Regulations for similar items should be consistent among the three different markets, except where the nature of the particular market requires a different treatment.	Paragraph 1, Article 9-3 of the Cabinet Office Ordinance will apply not only to selling on an exchange market but also to selling in an OTC registered stock market and through PTSs. Item 8 of the said paragraph is included in the calculation in order to require reporting of the whole short selling position and not just a position from short selling on an exchange market. Item 18 of the said paragraph has been included in the calculation prior to the revision. (No. 44)
12	Same as above	For the purpose of calculating the "position amount", it would be difficult to exclude positions from, for example, hedging transactions and arbitrage transactions, from the practicable viewpoints including those of system development. There should be no exemptions for the purpose of calculating the position amount, or otherwise reporting of the aggregate short positions without excluding the exempted transactions should be accepted as compliant.	For the purpose of calculating the "position amount", certain transactions including those which are long sales from the substantive viewpoint are excluded, in order to calculate accurate short selling positions. Accordingly, it is considered necessary to calculate the "position amount" in accordance with the said provision, to the extent practicable. (No. 41)

2. Price restrictions

	Relevant provisions	IBA comment	FSA answer
13	Article 26-4, Draft Cabinet Order	We appreciate the proposed "trigger rule" which aims not to intervene at ordinary times when share prices are stable and to apply only when the share price drops significantly, as the regulation is expected to efficiently deter manipulative sell-offs without excessively reducing market liquidity.	Your precious opinion is noted. (No. 11)
14	Same as above	In the case of a precipitous price fall due to, for example, an erroneous transaction order exchanges (or PTS operators) are required to use their discretion not to trigger price restriction.	In an objectively clear situation in which a price restriction is triggered erroneously even though it cannot be considered as a situation as stipulated in Paragraph 1, Article 26 of the FIEA Enforcement Order, it is considered acceptable if the financial instruments exchange or the PTS operator cancels the price restriction, to the extent practicable. (No. 13)
15	Same as above	On 29th March, 2011, JSDA and TSE have sent notices regarding the exchanges' systematic price-checkers, which stated that "based on the assumption that the price-checking by the TSE trading system functions effectively", firms may consider it compliant with the price restriction (Article 26-4 of the Enforcement Ordinance of the Financial Instruments and Exchange Act) "if an order placement is made by clarifying that the order is subject to short-selling price restrictions". We would like confirmation that under	These revisions are premised on such operation by financial instruments exchanges as you point out. We have the same assumption for PTSs. (No. 15)

	Relevant provisions	IBA comment	FSA answer
		the same conditions, it would also be acceptable to rely on the price-checking function of each PTS for orders being placed to PTSs.	

3. Exempted transactions

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16	Item 17, Paragraph 1, Article 9-3, Draft Cabinet Office Ordinance, etc.	Currently an exemption is available for transactions only in the exchange participant's proprietary account to provide liquidity for foreign ETFs, etc. We would hope that this exemption will be expanded to include a certain range of transactions for a customer account. For example, under the TSE's foreign ETF support member system, a support member or an associate support member designated by the exchange will execute orders to ensure smooth transactions in the market, not just in its proprietary account but also for the account of a third-party market maker (including those overseas) based on a certain contractual relationship. Making those third-party orders ineligible for exemptions from short selling regulations would significantly restrict the functioning of this system for the smooth transactions in the market.	No answer was provided.

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17	Item 12, Paragraph 1, Article 9-3, Draft Cabinet Office Ordinance	We consider it as a good proposal to have a uniform definition of the term "investment trust certificates, etc." and expand the scope of exemptions accordingly, since in this manner transactions which have similar nature will be subject to the same regulations. For example, ETNs which are currently traded on Japanese exchanges have the same economic effects as foreign ETFs. Is our understanding correct that ETNs are within the definition of "investment trust certificates, etc." under Item 12d., Paragraph 1, Article 9-3 of the Draft Cabinet Office Ordinance?	Short selling of ETNs, which are securities defined in Item 5, Paragraph 1, Article 2 of the FIEA, is exempted from the locate requirement (Paragraph 5, Article 26-2-2 of the FIEA Enforcement Order, Item 3(b), Paragraph 1, Article 9-3 of the Cabinet Office Ordinance). (No. 7)
18	Item 6, Paragraph 1, Article 9-3, Draft Cabinet Office Ordinance	The draft provision subjects "securities purchased from a person who consigns short selling on an exchange market, in communication (*tsuujite*) with such person and in lieu of (*kaete*) such consignment" to short selling regulations unless the purchase has been settled. It is our understanding that this is intended to regulate "attempts to circumvent regulations by disguising client short selling orders as long sales in the securities firm's proprietary account" as previously stated in 4.(2)③ of the press release "Regarding a comprehensive review of short selling	"*Tsuujite*" refers to a situation where two or more parties "collude" or "prearrange" with each other to do something, as used in Paragraph 1, Article 94 of the Civil Code. "*Kaete*" means "purchasing" the shares instead of "accepting an order to sell short or agreeing to broker such an order". In all cases, whether these criteria are met should be judged based on specific facts on a case by case basis. (Item 1)

	Relevant provisions	IBA comment	FSA answer
		regulations (draft)". Based on this understanding, what specific content of communication or information sharing is meant by being "in communication with" the person who consigns short selling?	