

# Consob extends ban on short selling in financial sector companies

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In light of the current financial turmoil, by resolution No. 18298 of 27 July 2012 (“**Resolution 18298**”), CONSOB (the Italian financial and securities regulator) extended the applicability of the exceptional measures banning short selling in financial sector companies (“**Ban**”) lastly introduced by resolution No. 18283 of 23 July 2012 (“**Resolution 18283**”)¹. On 27 July 2012 CONSOB also updated the frequently asked questions (“**FAQ**”) on short selling.

## 1. Background

Resolution 18298 and the updated version of the FAQ confirm the applicability of the Ban and better clarify the conditions to be met by market makers and other liquidity providers in order to fall outside of the Ban.

Moreover, the updated version of the FAQ introduces further exemptions available to market participants exercising conversion rights, pre-emption rights, and other similar powers and faculties (as the case may be), in order to be able to comply with the settlement obligations under the sale transactions previously entered into.

## 2. Scope

Resolution 18298 confirms the scope of the Ban previously introduced by the Resolution 18283, which requires any market participant, when giving an order to sell (irrespective of the trading venue where the sale is to be executed), to have both the ownership and the availability of the shares being sold. For the purposes thereof, shares borrowed under any type of stock lending agreements are not taken into account.

Consequently, the restrictions on short selling apply to any person and relate to the shares² of any categories – e.g. ordinary shares (*azioni ordinarie*), preferred shares (*azioni privilegiate*) and preference shares (*azioni risparmio*) – issued by banks and insurance companies as identified in the Resolution 18283. Notably, for the purposes of the Ban, no netting is allowed between shares of different categories (e.g. the sale of ordinary shares accompanied by the purchase of preference shares falls within the Ban).

## 3. Exemptions

### 3.1 Market-making exemption

The updated version of the FAQ specifies the requirements for the applicability of the exemptions available to market makers and other liquidity providers (“**Market-Making Exemption**”) originally introduced by the Resolution 18283.

¹ Please see our previous briefing on the Resolution 18283 [[link](#)].

² Short transactions relating to other instruments (e.g. derivatives, covered warrants, ETFs, etc.) fall outside of the scope of the Ban.

In particular, for the purposes above, market makers must:

- (a) be a member of an Italian regulated market;
- (b) either (i) hold themselves out on the financial markets on a continuous basis as being willing to deal on own account by irrevocably buying and selling financial instruments against their proprietary capital at competitive prices (so-called two-way-quotes) or (ii) in their ordinary course of business, execute clients' orders or reply to the requests to trade (so-called client facilitation); and
- (c) notify CONSOB about the intention to benefit from such exemptions and/or any relevant amendment thereto, by delivering a duly completed notice ("**Notice**", form of which is provided by the Regulator).

Moreover, the updated version of the FAQ specifies that:

- (a) market-making activities may be carried out either on Italian regulated markets or on other trading venues;
- (b) following the delivery of the Notice, no prior authorization is required from CONSOB;
- (c) any exempted activity must be carried out in relation to the shares caught by the Ban or on other linked financial instruments (e.g. derivatives or ETFs having such shares as underlying);
- (d) market makers are not allowed to carry out exempted activities on an issuer's shares while simultaneously short selling shares of another issuer included in the Ban;
- (e) with reference to shares being part of the FTSEMIB index, market making transactions carried out on regulated markets and/or MTFs cannot benefit from the Market-Making Exemption, which only applies to (i) transactions carried out on other trading venue (e.g. systematic internalizers) and/or (ii) transactions on financial instruments linked to such shares;
- (f) specialists (as defined in the rules on the regulated markets managed and organized by Borsa Italiana S.p.A.), in the exercise of their own functions on regulated markets and other intermediaries acting pursuant to a liquidity agreement entered into with the relevant issuer can benefit from the Market-Making Exemption.

### 3.2 Other exemptions

In addition to the exemptions already set forth by the Resolution 18283, the updated version of the FAQ clarifies that the Ban does not apply also to the sale of shares carried out:

- (a) by investors who have exercised their pre-emption rights relating to the same shares in the context of a share capital increase;
- (b) by investors who have recalled from the relevant borrower the shares previously lent under a stock lending agreement;
- (c) by holders of convertible bonds who have exercised the conversion right under such bonds;
- (d) by holders of American Depositary Receipt or other type of share certificates who have required the delivery of the underlying shares;

provided that, in any case, such shares must be delivered prior to the settlement date of the relevant sale transaction.

Notably, the updated version of the FAQ expressly exempts from the scope of the Ban, the sales of shares carried out for dynamic hedging purposes by an investor holding one or more long positions on the relevant shares and/or indexes comprising such shares under one or more derivatives<sup>3</sup>, provided that such sales were entered into, before 1.30 p.m. (Italian time) of 23 July 2012.

<sup>3</sup> By way of example, reference can be made to the sale of shares carried out by a bank holding long positions under a call option and a put option in a standard collar structure.

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Conversely, following the coming into effect of the new rules and, in particular, of the provisions providing for the irrelevance of the shares borrowed under stock lending agreements, dynamic delta hedging transactions, carried out without having previously secured the ownership of the shares being sold, will fall within the scope of the Ban. As a result, the costs to be borne by banks and other financial intermediaries for the purposes of hedging their exposure under derivative transactions are likely to increase.

#### 4. Timing and other CONSOB provisions on short selling

The Ban will remain in effect until 6.00 p.m. (Italian time) on 14 September 2012, although the Ban may be extended, amended or revoked according to market conditions.

For the avoidance of doubt, CONSOB clarifies that the resolution No. 17993 of 11 November 2011 introducing a general ban on naked short selling (i) continues to apply to the issuers not covered by the Resolution 18283 and (ii) will re-apply to such financial sector companies once the Ban expires.

In conclusion, the measures adopted by CONSOB, by resolution No. 17682 of 10 July 2011 on disclosure obligations of net short positions on shares, remain in force.

#### INFORMATION PURSUANT TO ARTICLE 13 OF LEGISLATIVE DECREE NO. 196/2003 (Data Protection Code)

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