



CCBE COMMENTS ON THE PROPOSAL OF A DIRECTIVE MODIFYING THE TRANSPARENCY DIRECTIVE 2004/109/EC

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Note on the inclusion of exclusively cash-settled derivatives for calculating when thresholds are exceeded

The Council of Bars and Law Societies of Europe (CCBE) is the representative organisation of around 1 million European lawyers through its member bars and law societies from 31 full member countries, and 11 further associate and observer countries.

The CCBE has the following comments on the [proposal to amend the Transparency Directive](#):

The European Commission published on 25 October 2011 a proposal for a Directive amending the Transparency Directive. Among the elements covered in this proposal, there is the inclusion of exclusively cash-settled derivatives for calculating when thresholds are exceeded.

It is proposed to amend Article 13 of the Transparency Directive relating to the notification requirement for the acquisition or disposal of major holdings, i.e. statements on threshold being exceeded as follows:

'1. The notification requirements laid down in Article 9 shall also apply to a natural person or legal entity who holds, directly or indirectly:

a) financial instruments that, on maturity, give the holder, under a formal agreement, either the unconditional right to acquire or the discretion as to his right to acquire, shares to which voting rights are attached, already issued, of an issuer whose shares are admitted to trading on a regulated market;

b) financial instruments with economic effects similar to those referred to in point (a), whether they give right to a physical settlement or not.

The notification required shall include the breakdown by type of financial instruments held according to point (a) of the first subparagraph and financial instruments held according to point (b) of that subparagraph.'

In the current state of the Transparency Directive, only operations for the acquisition and disposal of shares are subject to statement requirements for when thresholds are exceeded. If the proposed amendment of Article 13 is adopted, all financial instruments with economic effects which are equivalent to shares will be subject to the same statement requirements.

The amendment aims at exclusively cash-settled derivatives such as *equity swaps* and *CFDs*. While these investments provide economic rights to their holders in companies, they are currently ignored when calculating holdings with respect to reporting thresholds that are exceeded in accordance with the Transparency Directive.

Some Member states have nevertheless already taken the initiative to include these complex derivatives with shares in the calculation of thresholds to be reported. This is the case in Switzerland, in the UK, in Portugal, and in Germany too.

However, as stated in recital 10 of the proposed Directive, the harmonisation of regulations in this area is necessary for the measures implemented by the Transparency Directive to be effective:

'A harmonised regime for notification of major holdings of voting rights, especially regarding aggregation of holdings of shares with holdings of financial instruments, should improve legal certainty, enhance transparency and reduce administrative burden for cross-border investors.'

The interest of statement requirements for thresholds that are exceeded is to provide the market with a true picture of issuers, their capital, and of takeover intentions some third parties may have. This goal is threatened when holding complex derivatives which favour hidden capital increase.

It is also noted in Recital 8 of the proposed Directive:

'Financial innovation has led to the creation of new types of financial instruments that give investors economic exposure to companies, the disclosure of which has not been provided in Directive 2004/109/EC. Those instruments can be used to acquire secret stocks in companies, which could result in market abuse and give a false picture of economic ownership of publicly listed companies. In order to ensure that issuers and investors have full knowledge of the structure of corporate ownership, the definition of financial instruments in that Directive should cover all instruments with similar economic effect to holding shares and entitlements to acquire shares.'

The CCBE has welcomed this proposal as it will better reflect the economic reality of companies and compensate for the lack of legislation, which is now helpless in situations of 'snap' capital increase through the use of derivatives.

This has recently happened in France where the gradual rise of the LVMH stake in the company Hermes by way of equity swaps generated significant litigation. Similar cases were found in Germany (*Porsche v. Volkswagen* and *Continental v. Schaeffler*) or the United Kingdom (*Philip Green v. Marks & Spencer* and *BAE Systems v. Alvis*).

Some CCBE members regretted that the text of the proposal was not more specific about the description of derivatives (the text refers to financial instruments with similar economic effects to shares). However, the use of general terms is relevant because these financial instruments are subject to constant innovation. It is feared that in providing a more precise definition for these instruments, the text will restrain the effectiveness of the Directive: new instruments could indeed be created and used to circumvent the statement requirements for thresholds that are exceeded.

Moreover, it is unfortunate that the draft Directive does not address the relationship between the statement scheme for thresholds that are exceeded and the scheme for the initiation of mandatory takeover bids.

Indeed, Directive 2004/25/EC on takeover bids provides for the mandatory initiation of a takeover bid:

*'1. Where a natural or legal person, as a result of his/her own acquisition or the acquisition by persons acting in concert with him/her, holds securities of a company as referred to in Article 1(1) which, added to any existing holdings of those securities of his/hers and the holdings of those securities of persons acting in concert with him/her, **directly or indirectly give him/her a specified percentage of voting rights in that company, giving him/her control of that company**, Member States shall ensure that such a person is required to make a bid as a means of protecting the minority shareholders of that company.*

As exclusively cash-settled financial instruments do not by definition confer any voting right, they fall outside the scope of securities included when calculating the threshold for initiating a mandatory takeover bid.

Some members felt it would be appropriate to establish an identity for the scope of financial instruments included when calculating thresholds, be it for market information or to initiate a takeover bid. Others believed that such identity is not necessary as derivatives are short-term financial instruments whereas initiating mandatory takeover bids is based on holding long-term financial instruments.

The CCBE nevertheless agrees on the need for a thorough review of the issue, particularly when working on Directive 2004/25/EC.