

Summary: Intervention & Options

Department /Agency: HM Treasury	Title: Impact Assessment of Financial Instrument Order 2008	
Stage: Implementation	Version: 1	Date: 3 November 2008
Related Publications: HMT consultation on implementation of the Transparency Directive, March 2005; FSA consultation on disclosure of Contracts for Difference, November 2007.		

Available to view or download at:

<http://www>.

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What is the problem under consideration? Why is government intervention necessary?

The UK is no longer giving full effect to its obligations under the Market Abuse Directive as it has been modified by Markets in Financial Instruments Directive, or to its obligations under Commission Directive 2007/14/EC.

Furthermore the rule-making powers of the FSA, granted when implementing the Transparency Directive, need to be clarified so that disclosure obligations cannot be avoided through the use of certain derivative instruments.

What are the policy objectives and the intended effects?

To ensure that the UK continues to give full effect to its obligations under the Directives listed above.

To clarify that the FSA's rule-making powers in relation to disclosure of major shareholdings cover derivative instruments, such as Contracts for Difference (CfD). Although not giving a legal entitlement to acquire shares there are instances where CfDs are being used in ways the regulatory regime is designed to catch - specifically holders seeking to influence votes and build up stakes in companies on an undisclosed basis.

What policy options have been considered? Please justify any preferred option.

1. Do nothing.
2. Make an Order to update the UK's position in relation to the Directive listed above and clarify the rule-making powers of the FSA in regard to disclosure of CfDs.

The second option is preferred to ensure that the UK remains fully compliant with EU directives and clarifies the FSA's rule-making powers.

When will the policy be reviewed to establish the actual costs and benefits and the achievement of the desired effects?

The FSA have published their revised cost benefit analysis. The FSA will be responsible for monitoring ongoing compliance with their disclosure regime.

Ministerial Sign-off For final proposal/implementation stage Impact Assessments:

I have read the Impact Assessment and I am satisfied that, given the available evidence, it represents a reasonable view of the likely costs, benefits and impact of the leading options.

Signed by the responsible Minister:

..... Date:

Summary: Analysis & Evidence

Policy Option: 2	Description: Make an Order to update the UK's position in relation to the Market Abuse Directive and the Commission Directive.
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COSTS	ANNUAL COSTS	Description and scale of key monetised costs by 'main affected groups' These costs relate to the FSA implementing a general disclosure regime for CfDs, coupled with aggregation of CfDs and shareholdings and an exemption for authorised firms writing financial instruments in a client serving capacity			
	One-off (Transition) Yrs		£ £5.8m - £16.8m		
	Average Annual Cost (excluding one-off)		£ £1.5m - £3.1m	Total Cost (PV)	£
	Other key non-monetised costs by 'main affected groups'				

BENEFITS	ANNUAL BENEFITS	Description and scale of key monetised benefits by 'main affected groups' Ensuring the UK remains fully compliant with EU directives. Also a disclosure regime will help increase market certainty on the levels of ownership, influence and voting practices.			
	One-off Yrs		£ N/A		
	Average Annual Benefit (excluding one-off)		£ N/A	Total Benefit (PV)	£
	Other key non-monetised benefits by 'main affected groups'				

Key Assumptions/Sensitivities/Risks

The FSA's costs in relation to a disclosure regime are based on research carried out for them, dialogues with market participants and data from their own system.

Price Base Year	Time Period Years	Net Benefit Range (NPV) £ N/A	NET BENEFIT (NPV Best estimate) £ N/A
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What is the geographic coverage of the policy/option?	UK wide				
On what date will the policy be implemented?	FSA rules in Sep 2009				
Which organisation(s) will enforce the policy?	FSA				
What is the total annual cost of enforcement for these organisations?	£ 25-50k p.a.				
Does enforcement comply with Hampton principles?	Yes				
Will implementation go beyond minimum EU requirements?	Yes				
What is the value of the proposed offsetting measure per year?	£ N/A				
What is the value of changes in greenhouse gas emissions?	£ N/A				
Will the proposal have a significant impact on competition?	No				
Annual cost (£-£) per organisation (excluding one-off)	<table style="width: 100%; border: none;"> <tr> <td style="width: 25%; text-align: center;">Micro</td> <td style="width: 25%; text-align: center;">Small</td> <td style="width: 25%; text-align: center;">Medium</td> <td style="width: 25%; text-align: center;">Large</td> </tr> </table>	Micro	Small	Medium	Large
Micro	Small	Medium	Large		
Are any of these organisations exempt?	<table style="width: 100%; border: none;"> <tr> <td style="width: 25%; text-align: center;">No</td> <td style="width: 25%; text-align: center;">No</td> <td style="width: 25%; text-align: center;">N/A</td> <td style="width: 25%; text-align: center;">N/A</td> </tr> </table>	No	No	N/A	N/A
No	No	N/A	N/A		

Impact on Admin Burdens Baseline (2005 Prices)		(Increase - Decrease)
Increase of	£ N/A	Net Impact
Decrease of	£ N/A	£ N/A

Key: Annual costs and benefits: Constant Prices (Net) Present Value

[Use this space (with a recommended maximum of 30 pages) to set out the evidence, analysis and detailed narrative from which you have generated your policy options or proposal. Ensure that the information is organised in such a way as to explain clearly the summary information on the preceding pages of this form.]

PURPOSE

This Order is being made to give further implementation to Directive 2003/6/EC of the European Parliament and of the Council of 28 January 2003 on insider dealing and market manipulation (the Market Abuse Directive), as that Directive has now been modified by Directive 2004/39/EC on markets in financial instruments (MiFID), and to Commission Directive 2007/14/EC of 8 March 2007 (the Commission Directive). Amendments are being made to the Financial Services and Markets Act 2000 and the Financial Services and Markets Act 2000 (Prescribed Markets and Qualifying Instruments) Order 2001.

Collectively these changes ensure the UK remains compliant with the EU Directives and gives the FSA the legislative power to implement its disclosure regime in relation to derivative instruments such as Contracts for Difference (CfD), which currently fall outside the disclosure and transparency rules put in place in respect of obligations under the Transparency Directive.

COSTS AND BENEFITS

The initial intention in implementing the Transparency Directive was that the FSA would have the power to ensure that parties wishing to acquire control over shares could not avoid their disclosure obligations by acquiring derivative instruments such as CfDs. This can be seen in the explanatory notes to the Companies Act 2006, which states:

1610. Subsection (3)(b) enables the Authority to make rules about disclosure in relation to certain comparable instruments in respect of voting shares. These are instruments that give the holder a level of economic, as opposed to legal, control over votes attached to shares. An example of the type of instrument that the rules could extend to cover is a contract for difference, known as a "CFD".

In extending the FSA's rule making powers, these Regulations correct an unintended shortcoming in the FSA's powers. The FSA has published its response to its November 2007 consultation on putting in place a disclosure regime for CfDs and is now engaging in a consultation period on the technical aspects of those rules. In response to the feedback received the FSA has changed their recommendation from a targeted disclosure regime to a general disclosure regime. This regime would require the disclosure of institution's gross long positions (i.e. the aggregation of shareholdings and CfD holdings), coupled with an exemption for authorised firms writing financial instruments in a client serving capacity (e.g. where a CfD writer writes a short CfD for a client, it effectively takes a long CfD position itself.)

COSTS

The FSA have concluded that their general disclosure regime will lead to the following costs being incurred: one-off costs of £5.8m - £16.8m and on-going costs of £1.5m - £3.1m per annum.

Compliance costs to firms and issuers are the most significant aspect of the figures derived at. The compliance costs fall into two broad categories: up front costs involved in setting up or updating systems; and, the costs of processing additional disclosures and notifications.

Following feedback on their consultation paper the FSA is introducing an exemption for investment firms and credit institutions that write CfDs. This means that smaller system changes will be needed compared to their original proposals, and the upfront costs have been reduced. The proposed exemption will also reduce the number of disclosures and therefore the level of ongoing costs.

BENEFITS

Benefits of this nature are hard to quantify, however, benefits accrue from increased market transparency; the transparency of control of major shareholdings being important to the efficient functioning of equity markets. Disclosure may therefore help allay market rumour and speculation and promote market confidence.

There is support for the FSA creating a disclosure regime and the thrust of the discussion has been on getting the right regime in place.

There is a further benefit in that making the Order ensures that the UK remains fully compliant with its obligations under the Market Abuse Directive and the Commission Directive; however, this is a qualitative rather than a quantitative benefit.

SMALL FIRMS IMPACT TEST

Smaller firms are not expected to suffer a disproportionate impact from the requirements. It was determined that the original major shareholding disclosure requirements would tend to fall on larger companies; this is expected to remain the case in relation to the disclosure requirements in respect of CfDs.

COMPETITION ASSESSMENT

The Order is not expected to diminish or distort competition in the market or to have a disproportionate impact on particular groups.

ENFORCEMENTS, SANCTIONS AND MONITORING

The FSA will be responsible for monitoring compliance.

IMPLEMENTATION AND DELIVERY PLAN

This Order is being made under the negative resolution procedure.

The FSA has published a response to consultation paper setting out its policy in relation to a general disclosure regime for CfDs. It is now engaging in a technical consultation period on how to implement the rules. They propose to finalise and make the rules in February 2009 with them coming into force in September 2009, subject to being granted the necessary statutory powers.

Specific Impact Tests: Checklist

Use the table below to demonstrate how broadly you have considered the potential impacts of your policy options.

Ensure that the results of any tests that impact on the cost-benefit analysis are contained within the main evidence base; other results may be annexed.

Type of testing undertaken	<i>Results in Evidence Base?</i>	<i>Results annexed?</i>
Competition Assessment	Yes	No
Small Firms Impact Test	Yes	No
Legal Aid	No	No
Sustainable Development	No	No
Carbon Assessment	No	No
Other Environment	No	No
Health Impact Assessment	No	No
Race Equality	No	No
Disability Equality	No	No
Gender Equality	No	No
Human Rights	No	No
Rural Proofing	No	No

Annexes

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