



# Operational Model and Procedures for Implementation of Regulated Short Selling (RSS)

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## Overview

This document explains:

1. The operational model for implementation of Regulated Short Selling (RSS); and
2. The relevant procedures for implementation of RSS.

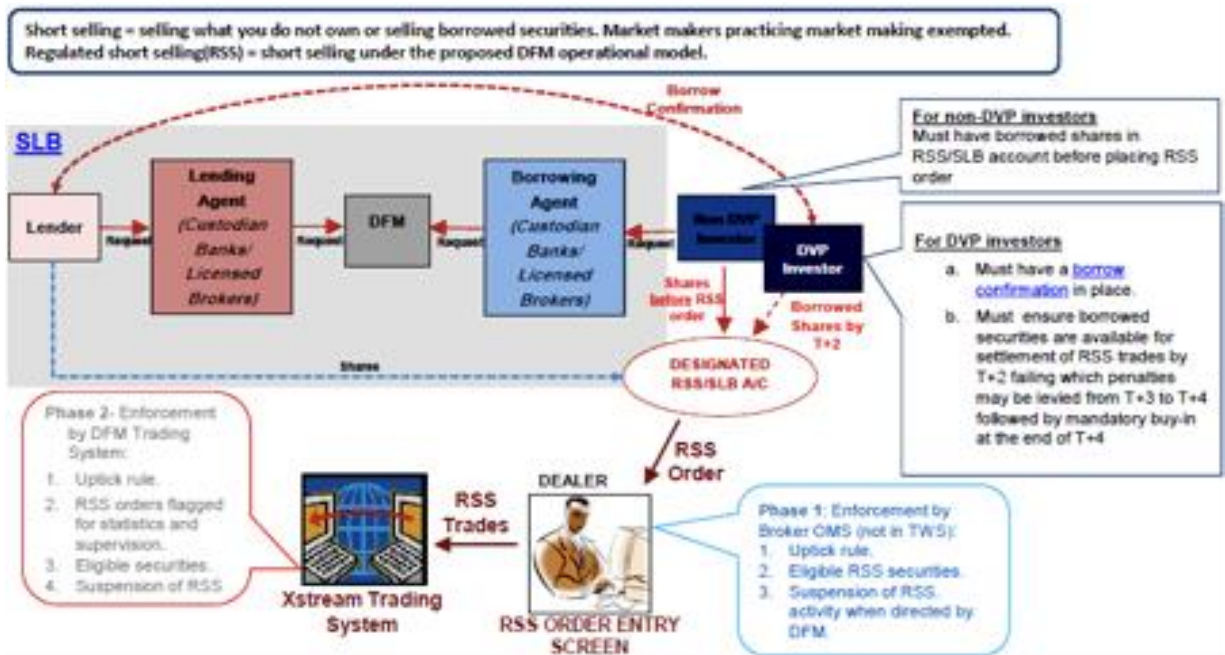
## Terminologies

1. Clearing Member means a member responsible for clearing and settlement operations for the RSS Trading Member.
2. Clearing entity means DFM as a clearing-house.
3. CSD entity means DFM as a depository.
4. DVP investor means an investor client holding an investor number through a DFM custodian and uses a DFM custodian for settlement of trades.
5. Exchange means DFM as a stock exchange.
6. Locate confirmation means a record evidencing that the investor placing the RSS order has obtained confirmation from a lender that the lender has the security available to lend.
7. Non-DVP Investor means an investor holding a direct investor number with DFM and who's trades are settled by the RSS Trading Member as a Clearing Member or via a Clearing Member.
8. OMS means order management system of the RSS Trading Member.
9. RSS means regulated short selling and shall exclude short selling by market makers. RSS is the sale of securities whereby the investor placing the RSS order ("the seller") does not own the related security but has a presently exercisable and unconditional right to vest the security in the buyer by virtue of having a securities lending and borrowing agreement and has either:
  - Obtained a locate confirmation from a lender, who is part of a borrowing/lending agreement, that the lender has the security available to lend to the seller; or
  - Borrowed securities.
10. RSS Trading Member[TM] means a broker licensed to conduct purchase and/or sell of securities and permitted by the Exchange to execute RSS trades.
11. SLB means securities lending and borrowing.
12. Uptick rule means that the RSS order must be at a price greater than the current offer price. There must be a current offer price available before an RSS order may be placed.
13. SD means Settlement Date.
14. Seller means the selling investor providing instructions to the RSS Trading Member.



## Operational Model Obligations of the Brokerage Firm

- The following diagram summarizes the proposed DFM RSS model and interaction of RSS with securities lending and borrowing (SLB):



- Details of the DFM securities lending and borrowing (SLB) model, rules and procedures can be found on the DFM website.
- RSS will be implemented in the following manner:
- Only DFM accredited Trading Members (TMs) can offer RSS to investors. Refer to Section 4 for eligibility requirements to be an accredited RSS TM.
- The RSS TM must open a new RSS/SLB Trading Account for investors intending to do RSS trades.
- This new trading account will be marked as RSS/SLB Account. The rationale for this requirement is to ensure that all sells executed from this RSS/SLB account will be deemed as RSS trades.
- DVP investors may maintain a separate SLB Account with the custodian or use the RSS/SLB account with the RSS TM for holding borrowed securities.
- Borrowed securities shall be delivered only to the designated RSS/SLB Trading Account at the designated RSS TM responsible for executing the RSS trade and not to any other trading accounts.



9. Additional uses of the designated RSS/SLB Account:
  - Purchase securities for returning the borrowed securities of SLB transaction.
  - Purchase securities for the settlement of an RSS transaction if the seller opted not to execute the related SLB transaction. In such a case, the investor takes the risk of settlement failure to settle this purchase, which will lead to the failure of settling the RSS transaction, and, accordingly, will incur all the resulting consequences
  - Transfer of the borrowed securities into the purchaser account on the settlement date of an RSS transaction.
  - Return of borrowed securities shall be through this designated RSS/SLB account only and not from any other trading accounts;
  - Securities from other trading accounts may be transferred into this RSS/SLB Account.
10. Transfers of borrowed securities out of the RSS/SLB Account are prohibited, except for the purpose of settling an RSS transaction or returning the borrowed securities. Failure to ensure compliance will result in a penalty of AED 10,000 per transfer by the CSD entity. The RSS TM may also be terminated from being an RSS TM.
11. RSS transactions through the designated RSS/SLB Accounts will not affect or update the settlement cap of the relevant trading member.
12. Approved RSS trading members must ensure that their MOS are capable to ensure the followings:
  - Compliance to the uptick rule when placing RSS orders.
  - Restricting the RSS orders to the eligible securities designated by DFM.
13. Before executing an RSS order, the RSS Trading Member (RSS TM) must ensure that a DVP investor have a locate confirmation in place while the non-DVP investor must have pre-borrowed securities. Refer to Section 6 on what a locate confirmation is.
14. The RSS TM must keep a record of the locate confirmation.
15. The RSS order must be executed using only the RSS/SLB Account.
16. Once the RSS order is matched, the RSS trade must be settled by the T+2 settlement date through either:
  - A buy trade executed on the same date of the RSS trade (T+0), or
  - The delivery of borrowed securities through the SLB mechanism.
17. The DVP or non-DVP investor may borrow securities either on an OTC basis or through the RSS TM (provided the RSS TM is a Lending Agent) to settle RSS trades due on settlement date. For further details, refer to the DFM SLB rules and procedures on the DFM website.
18. If the investor borrows securities through an RSS TM, the RSS TM must be first permitted by DFM to conduct SLB business to be able to lend securities to the investor for settlement of RSS trades (refer to the DFM SLB rules and procedures on becoming a Lending/Borrowing Agent).
19. An RSS TM cannot offer SLB services to its investor clients to settle RSS trades without first having DFM approval to be a Borrowing/Lending Agent.
20. An RSS TM can execute an RSS trade for investor clients who source their own SLB subject to a locate confirmation (for DVP investors) or pre-borrowed (for non-DVP investors) without the RSS TM being a Borrowing/Lending Agent.
21. The RSS trade is settled on the trade settlement date ie. T+2 but the duration of the SLB transaction is determined by the lender and the borrower subject to the provisions of related Lending/Borrowing Agreement. DFM did not prescribe a fixed duration for SLB transactions.
22. The RSS/SLB account type is restricted to only RSS TMs. The Exchange shall levy a penalty of AED 10,000 for each misuse of the RSS/SLB trading account type.



## Procedures to be a RSS Trading Member

1. Trading Members must submit an application to DFM with a statement confirming compliance with conditions set out in this document.
2. This application is to be signed by the Chief Executive and Head of Compliance of the applicant TM.
3. A sample copy of the RSS/SLB Trading Account agreement to be signed with the investors who ask to perform RSS transactions must be submitted to DFM along with the above mentioned application letter.
4. The applicant Trading Member must also submit a confirmation letter, in which they confirm that they communicate the risks of RSS to their prospective non-DVP investor clients before signing with them the RSS/SLB Trading Account agreement.

## Settlement of RSS Trades

1. RSS Trading Members (RSS TMs) must ensure settlement of RSS trades by the trade settlement date ie. T+2 including for DVP trades.
2. Unless otherwise exempted by the CSD entity, the following penalties may be levied by the CSD entity on the RSS TM or the custodian clearing member if they failed to ensure the settlement of any RSS trades (accepted for settlement) on the settlement date (SD):
  - T+2 (SD): No penalties.
  - T+3 (SD+1): AED 1000 or 0.1% of the unsettled trade value whichever is the higher if a failed sell trade is resolved on SD+1.
  - T+4 (SD+2):
    - AED 5000 or 0.5% of the unsettled RSS trade value whichever is the higher if a failed RSS trade is resolved on SD+2.
    - AED 10,000 or 1% of the unsettled RSS trade value whichever is the higher if a failed sell trade is settled by way of a mandatory buy-in or buyer cash compensation undertaken by DFM, in addition to the buyer cash compensation amount payable.
  - The existing policy of forfeiture of any profit arising from a settlement failure recognized by the RSS TM applies.
  - Penalties will not be levied directly on lenders but on the RSS TM or the custodian clearing member who may pass-on the relevant penalties to their client investors who in turn may claim from lenders where relevant.
3. RSS trades by investors using a custodian for settlement are entitled to be settled on a DVP basis.



## Requirements of a Locate Confirmation Record

1. A locate confirmation record is evidence that the investor, placing an RSS order, has made arrangements with a lender to borrow securities.
2. The locate confirmation record must contain the following details:
  - Date and time of confirmation.
  - Quantity of securities.
  - Name of securities.
  - Name or Identifier Code of Lender.
  - Name or Identifier Code of Borrower.
  - Evidence of lender confirmation to hold the quantity of securities.
3. The SLHK Bloomberg message or similar locate confirmation record is an example of an acceptable locate confirmation record which the RSS TM must maintain as a record for inspection purposes. Such a record can be maintained in whatever media.
4. There is no regulatory requirement for lenders to maintain the locate confirmation given to borrowers.
5. The Exchange shall conduct periodic requests of locate confirmations to support RSS trades. Failure to ensure a locate confirmation record being in place for each RSS trade will result in a penalty of 1% of the trade value or a minimum of AED10,000.00. The Exchange may also suspend or remove the TM from being an RSS TM.

## RSS Restriction Threshold

1. If the price of any designated RSS Security decreases by 10% from the previous day's close price or goes limit down, RSS activity on that security will be suspended immediately for 2 trading days including the day of suspension.
2. RSS will resume on the 2nd trading day from suspension if there is no further 10% decrease in price or limit down event. For example, if RSS is suspended for a security today (T+0), RSS will resume on T+2 provided there is no 10% fall or limit down on T+1.
3. If there is again a 10% fall in price or limit down on T+1, RSS for this security will remain suspended for T+1 and T+2 and will only resume on T+3.
4. RSS will resume only when there is 1 clear trading day where there is no 10% fall in price or limit down of the RSS eligible security.
5. The Exchange may suspend RSS activity:
  - If directed by a regulatory authority; and/or
  - If there is excessive RSS activity creating undue market volatility.



## DFM's Criteria for Selection of Designated RSS Securities

1. A security will be eligible for RSS activities in the following cases:
  - Securities included in any UAE Index issued by a rating agency will be automatically eligible for RSS and shall be removed on the effective date of its exclusion if the rating agency undertakes such an action.
  - Securities which are part of a DFM derivative program will also be automatically be eligible for RSS.
  - All ETFs are automatically eligible for RSS immediately upon listing
  - Securities listed on the market and meet all the following criteria will be eligible for RSS activities:
    - Securities with market capitalization of not less than AED 1 billion and an aggregate turnover during the preceding 12 months to market capitalization ratio of not less than 50%.
    - Securities with value traded not less than AED 100 million throughout the evaluation period.
    - Securities with shares traded not less than 500,000 shares throughout the evaluation period.
    - Securities with number of transactions not less than 150 transactions throughout the evaluation period.
    - Securities traded on 50% of the total trade days throughout the evaluation period.
    - Securities with number of free float shares available for trading not less than 50% of the total number of company's shares listed.
    - Availability of at least 5 percentage points of the ownership limit allowed for foreign investors.
    - Subject to the approval of SCA, the exchange may exempt any security from the requirement of meeting any of the above-mentioned requirements.
2. Right issues and covered warrants are not eligible for short selling.
3. List of eligible securities will be reviewed every 6 calendar months or if there is a review by the rating agency and an updated Eligible Securities list will be published on the last trading day in December and in June unless otherwise necessary or determined by the Exchange.
4. Previously eligible RSS securities will ceased to be eligible for RSS on the next trading day after notification by DFM. SLB transactions for these securities may remain outstanding. However, no new loans for RSS shall be permitted.





## Requirements for RSS Trading Member

1. Uptick rule conditions for RSS orders:
  - Orders using RSS/SLB Trading Account must be entered at a price greater than the current offer price.
  - Market orders are strictly prohibited.
  - RSS orders are strictly prohibited during the pre-opening and pre-closing session.
2. RSS Trading Members (RSS TM) must enhance their OMS to apply the Uptick Rule conditions in 9.1 for orders entered using the RSS/SLB Trading Account.
3. Market Makers are exempted from the criteria of Uptick Rule on the securities on which they are obliged to do market making activity including underlying securities for an ETF.
4. RSS TMs must also ensure that their OMS is capable of ensuring that:
  - RSS orders can only be placed for RSS eligible securities as may be determined by the Exchange from time to time;
  - RSS orders are not entered during the RSS suspension period announced by DFM;
  - The order confirmation must clearly indicate that the order is an RSS order.
5. The Exchange will require an audit confirmation of Parts 9.2 and 9.4 by the OMS vendor of the RSS TM or the RSS TM's Head of Technology and such confirmation countersigned by the RSS Trading Member's Head of Trading and Compliance Officer as part of RSS TM accreditation application procedure.
6. The Exchange will enhance the SMARTS surveillance system to generate Alerts to capture the violations by RSS Trading Members and accordingly penalties will be levied, including but not limited to suspension or removal of RSS Trading Member from further RSS activities.
7. The RSS TM must ensure that they have the necessary expertise to undertake this RSS type of business activity.



### **Publication of RSS Trading Summary by Market**

1. The Exchange will publish the following information on its website for RSS Trades
  - Aggregated Daily RSS Trades summary at security level.
  - Aggregated Monthly RSS Trades summary at security level.

### **Reporting Net Short Positions by RSS Trading Members (RSS TMs)**

1. RSS TMs must report net short positions as mentioned below:
  1. Net short positions of 0.2% of total issued capital and above in Designated RSS Securities must be reported to the Exchange. Every subsequent 0.1% change up or down in Net short position must be reported.
  2. Net short positions of 0.5% of total issued capital and above in Designated RSS Securities will be disclosed as public information by DFM.


### **Submission of Requests**


1. All requests for accreditation of RSS TM are to be sent by email to: [mc@dfm.ae](mailto:mc@dfm.ae)
2. The P.O.Box number to be used for courier delivery purposes is: 9700 Dubai- UAE


**END**

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