

BAHRAIN BOURSE B.S.C. (c)

**Uncovered “Technical” Short Selling
Guidelines in Bahrain Bourse**

July 2024

1 Introduction

1.1 PURPOSE

These guidelines supplement Bahrain Bourse's Market Rules hereafter the "Market Rules". These guidelines do not supersede the Market Rules and should be construed in conjunction with related provisions of the Market Rules. A Member shall operate within the regulatory framework as envisaged and laid out in the Market Rules and these guidelines.

1.2 GLOSSARY

The following terms and expressions used in this document shall have the same meanings as assigned to them below unless the context requires otherwise:

"BHB"	Bahrain Bourse B.S.C (c)
"BHC"	Bahrain Clear B.S.C (c)
"CBB"	The Central Bank of Bahrain
"Eligible Securities"	Securities which have been approved by Bahrain Bourse for Short Selling Activities. In consideration of the following criteria, BHB shall define the securities eligible for short selling and shall review them every 6 months: 1- Securities turnover ratio. 2- The presence of a market maker. 3- A contract signed with a liquidity provider.
"External Trading Member"	An eligible foreign institution (remote member) who is a member of a licensed exchange and authorized by the CBB but who conducts their regulated activity (including trading on behalf of their clients) exclusively outside the Jurisdiction of the Kingdom of Bahrain.
"External Market Maker"	An External Trading Member approved by the CBB to undertake market making activities and registered with BHB in accordance with BHB Market Rules and relevant Guidelines to provide bid and ask quotes as a principal through the initiation and administration of a type of Fund
"Fund"	A sum of money utilized by the Market Maker to undertake its market making activity for the purpose of liquidity enhancement
"Issuer"	A company or other legal person or undertaking some or all of whose securities have been admitted to listing
"Institutional Investor"	An institutional investor is a company, high net worth individual or organization that invests money on behalf of clients or themselves. Hedge funds, mutual funds, and endowments are examples of institutional investors.

“Local Market Maker”	A Member registered with BHB in accordance with BHB Market Rules to provide bid and ask quotes as a principal through the initiation and administration of a type of Fund.
“Market Maker”	A Local Market Marker and/or an External Market Maker.
“Market Making Agreement”	A written agreement concluded between BHB and the Market Maker prior to commencement of market making activities.
“Market Rules”	The BHB Rules governing membership, trading, supervision and arbitration on BHB’s market. These Rules are applicable only to those institutions accepted as members or who are otherwise authorized to conduct transactions on BHB.
“Member”	An entity that has been approved as a Member of BHB in accordance with BHB Market Rules i.e. brokers, Market Makers.
“OMS”	Order Management System
“Securities”	As specified in the CBB Volume 6 and the BHB Market Rules

2 Short Selling

2.1 DEFINITION

- 2.1.1 Short selling is the sale of Eligible Securities that the seller does not own at the time of the sale. These guidelines are set to regulate “uncovered” short selling only.
- 2.1.2 In ‘uncovered’ short selling (also referred to as ‘naked’ short selling or technical short selling), the seller is not in possession of the Eligible Securities at the time of the sale or has not made borrowing arrangements before the short sale is made.

2.2 ELIGIBILITY CRITERIA

- 2.2.1 Members interested in engaging in short selling activities must satisfy the following requirements:
- (a) Must be authorized by BHB to conduct Market Making activities;
 - (b) Have the necessary financial solvency and capital adequacy to conduct short-selling activities whether in principal or on behalf of its clients in accordance with the relevant standards issued by BHB
 - (c) Must have in place an agreement with a guarantor that has a sound financial standing and credibility. The guarantor shall provide assurance for the Member's ability to cover any short trades which the Member fails to cover by the settlement date. The guarantor accordingly must have the ability and commitment to satisfy the delivery of the Eligible Securities to be short sold on the settlement date.
 - (d) Have in place adequate supervisory measures and a system of internal control to ensure the following:
 - (1) *An adequate undertaking of risk management;*
 - (2) *An adequate management of conflict of interest; and*
 - (3) *Compliance with the Market Rules and these guidelines*
 - (e) Attain one of the following licenses or authorizations;
 - (1) Broker Dealer
 - (2) External Trading Member
 - (f) Must possess the technical and administrative capabilities along with the competence required to undertake the processes pertaining to the adequate management of the concerned accounts authorized for short selling and their short selling activities; and
 - (g) An OMS capable of distinguishing short-sell orders from other orders, and send a message to the client of the content of the issued order.
 - (h) Ensure that the account interested in participating in Short Selling activities in the BHB Market through the member, satisfy the following requirements:
 - (1) *Shall have adequate liquid capital to cover any defaults;*

- (2) *Shall have the ability to satisfy the delivery of the Eligible Securities to be short sold on the settlement date;*
- (3) *Shall be an Institutional Investor; or*
- (4) *Shall be a Fund managed solely by the authorized short selling member; and*
- (5) *Shall be required to attain prior approval from BHB for each account whether it be a principal account of the Member itself in its capacity as a Market Maker or a client account before commencing any short-selling activities on behalf of the respective account; and*
- (6) *Any other rules as set by BHB from time to time*

2.2.2 BHB and/or BHC may from time to time define the clients or accounts who will not be eligible to engage in short-selling activities.

2.3 APPLICABILITY OF SHORT SELLING

2.3.1 Short selling only applies to the following securities listed in the BHB market:

- (1) Equities
- (2) Any other securities approved by BHB from time to time

3 Requirements and Obligations

3.1 REQUIREMENTS

3.1.1 To be approved by BHB to conduct short selling activities a Member must submit an application to BHB as per the form designated for this purpose, together with the information, details and supporting documents, particularly the following:

- (1) Business Overview: Brief description of the Member's set up for undertaking short selling trading activities, including:
 - a. business structure and set up of the short selling activity;
 - b. description of the operations of the front office and back office for short selling activity;
 - c. description of the background, experience, role and responsibilities of key personnel to be involved in short selling activity;
- (2) Detailed financial information including evidence of the controls and procedures in place to ensure compliance with the financial requirements of BHB; and the Controls and procedures in place to meet settlement obligations related to short-selling.
- (3) Risk Management Framework: The framework of the Member's risk management policy and procedures including but not limited to;
 - a. Trading strategy, trading and position limits, and risk monitoring;

- b. Controls and procedures in ensuring the implementation of the risk management policy and procedures.
- c. A report describing the technical system used to manage accounts authorized for short selling.
- d. A technical report, audited and signed by the Member's executive management (mainly the CEO or Managing Director), the internal auditor, and the IT officer, showing that the Member's OMS meets BHB requirements.
- e. System and Control: A description of the computer system to be used and internal security procedure, including;
 - I. software to be used for pricing, risk monitoring and back office processing
 - II. source of the software and applicant's experience in the software
 - III. history of major failures of the software, if any; and
 - IV. The internal security procedure in place.
- f. A report demonstrating the member's system of record keeping related to short selling orders and transactions.
- g. A process document showcasing the internal controls in place to monitor short-selling activities.
- h. BHB may request other clarifications, information, or documents as deemed necessary.

(4) A copy of the agreement governing the arrangement with a guarantor in line with 2.2.1 (c).

- 3.1.2 The applicant should receive BHB's approval within 30 business days, provided that all relevant documents are submitted and all terms and conditions are met.
- 3.1.3 BHB may reject an application provided such an applicant fails to meet the applicable qualification criteria set forth in these Guidelines or the Market Rules or it is in BHB's prudent view that such an applicant is unfit to engage in short-selling.
- 3.1.4 If an application is rejected by BHB, no new application by the same applicant, within a period of ninety (90) calendar days after the date of refusal, shall be considered by BHB.
- 3.1.5 A member approved for short-selling must submit the client agreement form when requesting for BHB's approval for client accounts. The client agreement should encompass the following;

(1) The client's express written acknowledgement and acceptance of:

- a. The right of the Member to secure the proceeds of the short-sale and use it for settlement in case the client fails to provide the short-sold Securities for settlement.

- b. The right of the Member to use the deposited collateral, to cover the shortage of the buying value in case a client fails to provide the shorted Securities for settlement.
 - c. The right of the Member to use the collateral in case the client fails, when the value of his contribution decreases, to respond within the specified period and increase its contribution accordingly.
- (2) Indication of the potential risks that might result from engaging in short-selling activities.
 - (3) The client's declared affirmation that they recognize and acknowledge the implications of the procedures, their responsibilities, and the risks involved.
- 3.1.6 BHB reserves the right to reject the approval request for any client account if BHB believes it is not in the market's interest to allow such an account to engage in short-selling activities.
- 3.1.7 A Member must have an existing agreement with BHC

3.2 OBLIGATIONS

3.2.1 The Member Firm shall:

- (1) *Maintain at all times an adequate level of financial solvency or capital adequacy according to the standards issued by BHB*
- (2) *Make sure that its client is financially solvent before executing a short-sell order on behalf of the respective client.*
- (3) *Limit the Short Selling transactions to Eligible Securities in accordance with the provisions of these Guidelines.*
- (4) *Enter into a short-selling agreement with the client wishing to engage in short-selling activities. This client agreement form must be submitted to BHB*
- (5) *Follow and comply with the policies and procedures of BHC.*
- (6) *Maintain a separate short-selling account for the client engaging in short-selling activities from any other accounts the client might have with the member.*
- (7) *Receiving an initial collateral from the client, or maintaining an initial collateral in case of a Market Maker acting as principal, with a value of no less than 50% of the market value of the Short Selling order (calculated by multiplying the last closing/reference price of the security to be short sold with the quantity to be short sold), and further retaining the sale proceeds of the short sale until the client's, or the Market Maker's financial position is closed through repurchasing the securities short sold. Thus, the Member is obligated to retain "Total Collateral = Initial collateral plus the sale proceeds of the short sale".*
- (8) *Evaluate the securities short sold at the market closing price by the end of each working day, and inform the client immediately if his contribution falls below 25% (Maintenance Margin ratio), by applying the following formula: (value of the total Collateral minus the market*

value of the securities short sold) + (the proceeds of the securities short sold) divided by the market value of the securities short sold, in order for the client to cover the shortage by increasing his contribution to more than the Maintenance Margin ratio, no later than the next working day at the agreed time between Member and the client from the date of being notified of the same.

- (9) *Allow the client to withdraw the excess funds of their contribution that exceeds 50% of their initial collateral.*
- (10) *Settle all short selling transactions, without changing the specified settlement cap during the specified settlement date in the market (T+2)*
- (11) *Buy the same quantity of the securities short-sold (considering corporate action adjustments) and close the client's financial position, if the client fails to cover the shortfall (by the settlement date). Only excess amounts of securities can be transferred to other accounts of the client.*
- (12) *Provide the client with a detailed monthly statement showing the movements in the Short Selling account, including changes in the Collateral value.*
- (13) *Have a mechanism to ensure adequate availability of cash;*
- (14) *Be responsible for the continuous monitoring of cash and securities balance held in its account and its clients' accounts;*
- (15) *Manage inventory risk related to short-selling activities*
- (16) *Comply with and adhere to all provisions of the Market Rules and other guidelines, regulations, requirements and directives issued by BHB*
- (17) *Comply with and adhere to the CBB Law, Rules and Regulations, CBB Rulebook Volume 6 and other directives issued by the CBB.*

3.3 REPORTING & RECORD KEEPING

- 3.3.1 A BHB Member who has entered into a short-selling transaction as an agent or principal must report complete and accurate details of such transactions to BHB as prescribed by BHB from time to time
- 3.3.2 A BHB Member who has entered into a short-selling transaction as an agent or principal must record and retain sufficient information about its short-selling activities to demonstrate compliance with the CBB and BHB Rules
- 3.3.3 Records required to be maintained by these Guidelines must be retained for a period of at least ten years from the date of the short-selling transaction
- 3.3.4 In the event such records relate to any litigation or claim (including any potential litigation) or any on-going investigations, the Member must retain such records until the conclusion of that litigation, claim or on-going investigation
- 3.3.5 All necessary records should be made available to BHB or the CBB as and when requested.

3.4 SETTLEMENT

- 3.4.1 Settlement must be conducted as per the BHC's applicable policies and procedures for short selling activities.

3.5 DISCLOSURE

- 3.5.1 BHB shall disclose to the market on a daily basis and after the end of the trading session the following:
- (1) Information in respect of short selling transactions and the related positions per Eligible Security
 - (2) Any other information deemed necessary by BHB

4 Trading Mechanism and Provisions

4.1 SHORT SELL ORDER REQUIRMENTS

- 4.1.1 No orders are allowed during the pre-open period
- 4.1.2 Only limit orders are allowed
- 4.1.3 Only Day orders are allowed
- 4.1.4 For the purposes of short selling the following order fill terms are allowed
- (1) *Regular Orders*
 - (2) *All or None Orders*
 - (3) *Minimum Fill Orders*

4.2 UPTICK RULE

- 4.2.1 The Short Selling order price must be at least one tick size above the last traded price or the previous day's closing price, whichever is applicable.

4.3 SHORT SELLING SUSPENSION, HALTS & RESTRICTIONS

- 4.3.1 Short selling in an Eligible Security shall be halted if one or more of the below conditions are met:
- (1) *If the price of an Eligible Security declines by a minimum of 5% from the previous day's Closing Price, short selling on the security shall be halted on the same trading day and continue to be halted throughout the next trading day.*
 - (2) *If the Short Selling trades equate to 10% of the security's total issued and fully-paid shares, Short selling will be halted for the trading remainder of the trading session*
 - (3) *Any other conditions as determined by BHB from time to time.*

4.3.2 Short-selling on an Eligible Security shall be restricted during the following periods;

- (1) *During the 5 trading days preceding the issuer's Annual General Meeting (AGM)*
- (2) *During the 5 trading days preceding the day the register is closed for the purpose of cash dividends, bonus shares and rights issue*
- (3) *During the trading period of an issuer's rights issue*
- (4) *During any other period as stipulated by BHB from time to time*

4.3.3 BHB may suspend or restrict the short selling activities of any approved Member if the approved Member is in breach of any of its obligations or upon the occurrence of all or any of the events stipulated in Section 3 of the Market Rules.

4.3.4 BHB may prohibit or suspend short selling transactions in respect of a specific security, or may prohibit or suspend all short selling transactions in the Market, at any time and as it deems fit, including but not limited to the following circumstances:

- (1) *There are adverse events or developments which constitute a serious threat to the financial stability of the market or to the market confidence;*
- (2) *For the protection of the investors;*
- (3) *For the maintenance of an orderly market; or*
- (4) *Where the aggregate sum of short positions in an eligible listed security across the market has reached a level where BHB considers it necessary to exercise such powers.*

4.4 REVOCATION OF APPROVAL

4.4.1 BHB reserves the right to revoke the approval for short selling if BHB reasonably believes that the Member or its client is in breach of any of the rules stipulated in any of the CBB's Rules or BHB's Market Rules.

5 Liability

5.1 BHB LIABILITY

5.1.1 Without prejudice to the provisions of the CBB Rulebook and the Market Rules, subject to exercising the due care necessary. BHB shall not be held liable for any losses or damages incurred by any participant referred to in these guidelines, their clients or any other person that have engaged in trading activities or otherwise in respect of these guidelines.

6 Disciplinary Actions

- 6.1.1 A Member who contravenes any of the provisions of the CBB Law, Rules and Regulations, CBB Rulebook Volume 6, BHB Market Rules and these Guidelines shall be liable for penalties and/or disciplinary actions as stipulated by the applicable rules.

7 Powers of BHB

- 7.1.1 BHB may waive any requirement in these guidelines either based on a request from the relevant person or on its own accord after obtaining CBB's approval.
- 7.1.2 BHB may add any further regulations, requirements or conditions as it deems fit from time to time.