AUTORITÉ DES MARCHÉS FINANCIERS

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Ban on short selling: who was supposed to apply it and to which securities?

In light of the Covid-19 epidemic and its impact on financial markets, the AMF decided in mid-March to impose a temporary ban on short selling[1] and, more generally, on strategies aiming to profit from the fall in the price of an equity. Although this exceptional measure was suspended on 18 May,[2] investors are still likely to send me requests relating to events arising during the course of those two months. It therefore seems useful to address this issue through the following case that was referred to be during this period.

The facts

Ms. T. informed me that on 2 April 2020, she had acquired 5,000 Turbo Put[3] certificates on her account with her bank, with the DAX[4] index as the underlying asset, representing a total amount of almost €30,000.

She explained that a few days later, on 7 April 2020, the certificates were deactivated as they exceeded the barrier level: she had therefore lost the whole amount she had invested.

However, Ms. T. was requesting that the transaction should be cancelled, as she had subsequently learned that transactions on derivatives having the effect of creating or increasing a net short position had been formally prohibited by the AMF over the period from 18 March to 18 May 2020.

As she considered that it was the responsibility of the issuer of the Turbos to prohibit access to these market products, Ms. T. asked me to intervene to obtain the cancellation of a purchase that she considered illegal.

Investigation

On analysing the request from Ms. T., I immediately saw that this was the result not of a malfunction attributable to the issuer, but of a misunderstanding of the decision made by the AMF on two points:

1) On the scope of the ban

We should begin by a reminder that short selling consists in selling a security we do not hold (and that we must therefore borrow in order to be able to sell it) and that we then buy back later because we suppose that its price is going to fall. It is therefore a strategy that anticipates a fall in prices to make a profit corresponding to the difference between the sale price and purchase price, after factoring in the cost of borrowing the securities that were sold.

Without engaging in short selling, it is also possible to profit from the fall in a price via a transaction in certain derivative instruments that have that security as an underlying asset. A position on certain derivative instruments can give the holder a financial advantage in the event of a fall in the price of the underlying asset. In this case, it is also said that the investor holds a “short position”.

In light of the great volatility on financial markets on account of the Covid-19 epidemic, this practice was prohibited temporarily by the AMF[5] when it concerned equities traded mainly on French markets.

In this case, after in-depth analysis, I informed Ms. T. that the temporary ban on net short positions decided on by the AMF applied only **to equities traded on French markets and, indirectly, to instruments allowing a position to be taken on these equities**, which was not the case of the Turbo in question. In the case at hand, the DAX index that was the underlying asset of the disputed Turbo is made up of Germany’s 30 largest listed companies in terms of market capitalisation, and these securities were not featured in the list of securities ~~URL = [https://www.amf-france.org/sites/default/files/2020-03/20200326_liste-actions-concerneesssban_fr.pdf]~~ concerned at that time by the ban on net short positions, as published on the AMF website.

2) On checking compliance with the ban on short selling

I also reminded Ms. T., who was claiming that a breach had been committed by the issuer of the Turbos she had bought, that it was **the personal responsibility of the investor**, and not that of their financial intermediary or of the issuer of the securities, to ensure that they were compliant with these provisions before making their investment.

In this respect, I pointed out to her that the AMF had published a series of Frequently-Asked Questions URL = [https://www.amf-france.org/fr/actualites-publications/actualites/interdiction-temporaire-des-positions-courtes-y-compris-ventes-decouvert-quelles-consequences-pour#Quels_sont_les_titres_concernes_?] that addressed this specific point, among others:

— What does an investor need to check before entering into a transaction?

Before selling any of the securities concerned, **the investor must make sure that the quantity of securities sold does not create or increase a net short position.**

The same applies to buying or selling a derivative where the underlying is one of the equities concerned by this ban (entirely or partly).

— Can your financial intermediary prohibit you from carrying out certain transactions further to the decision by the AMF?

An intermediary is under no obligation to prohibit transactions that are likely to create or increase a net short position on an equity subject to the ban. The intermediary is not necessarily aware of your whole portfolio, insofar as you may have several accounts opened with different intermediaries; consequently, they are not necessarily aware of any net short positions you might hold on each equity. **It is therefore your responsibility to make sure that you comply with this ban.** Your intermediary may, however, draw your attention to this point.

Finally, I pointed out to Ms. T. that I had consulted the website of the issuer of the Turbos in question and had been able to ascertain that a warning to this effect did indeed feature on the website homepage.

Recommendation

On the basis of all this evidence, I informed Ms. T. that I did not have any grounds on which to hold a breach against the issuer and that I was therefore unable to issue an opinion acceding to her request.

Lessons to be learned

For further information about the grounds and arrangements for this ban, I invite investors to consult the publications on this subject available on the AMF website, and in particular the very complete FAQ on this specific point.

For any questions pertaining to this issue, you can also contact Epargne Info Service and, of course, in the event of any dispute you can refer it to me via the online form URL = [https://www.amf-france.org/fr/le-mediateur-de-lamf/votre-dossier-de-mediation/vous-voulez-deposer-une-demande-de-mediation].

[1] A strategy consisting in betting on a future fall in the price of a security by selling equities without holding them, with a view to buying them back later at a lower price.

[2] The AMF suspends the ban on the creation or increase of net short positions

[3] Turbo: a leveraged product that amplifies variations in the price of the underlying asset and has a deactivating barrier (if the underlying asset reaches or exceeds the barrier level, the product is deactivated and immediately loses all value).

[4] DAX: Germany’s main stock market index, comparable to the CAC 40 in France

[5] Decision of 17 March 2020 regarding the extension of the ban on net short positions

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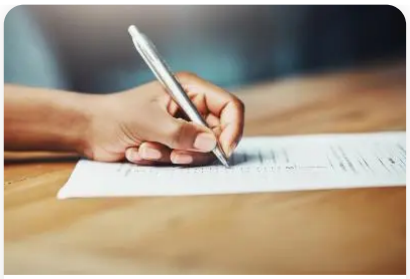

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