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Stock market orders: a financial institution may reject an order that it deems to be "aberrant"

Alongside Euronext's authority to cancel certain transactions that have already been executed, especially when the price of the order is considered to be "aberrant", account-keeping institutions may also reject a client's order when the limit set by the client is too far from the last known price. However, in order to avoid misunderstandings or even disputes, the client must be made aware of this, as illustrated by the case I am presenting to you this month.

The Facts

In September 2021, Mr H held 2,986 shares in V, a highly volatile biotech stock.

When Mr H checked the V share price before the opening of the trading session, he noticed that his account keeper's website had quoted a theoretical opening price of €10, although the last known price for the stock was €21.

Mr H therefore anticipated a significant fall in the price of V during the day, comparing the theoretical opening price with the last known price. Stating that he wished to keep his losses to a minimum, he tried to enter a limit sell order online at €10, which was however rejected by the institution.



After several unsuccessful attempts to place a €10 limit order, which was persistently blocked by the online trading platform, Mr H finally entered a €16 stop loss order, which was taken into account and executed on the same day at €11.02.

As the price of his shares did not fall below €10 on this occasion, contrary to what the theoretical opening price had suggested, Mr. H decided - surprisingly - that if his initial order at the limit price of €10 had been taken into account correctly from the outset, his shares would never have been sold.

Believing that he had suffered from a malfunction of his account keeper's trading platform, which had not allowed him to place an order at the €10 limit price, Mr H contacted me to obtain compensation for the difference between the highest price of the day and the price at which his order was executed.

The Investigation

As part of the investigation of this case, I contacted the institution in question, which provided me with its observations.

The institution told me that the €10 limit order placed by Mr H had been rejected automatically because of its policy to block "aberrant" orders. (View Ombudsman online diary, October 2017:

[The case of a stockmarket order executed at an unrepresentative price – Euronext can cancel transactions in special circumstances](https://www.amf-france.org/en/amf-ombudsman/ombudsman-online-diary/latest/case-stockmarket-order-executed-unrepresentative-price-euronext-can-cancel-transactions-in-special-circumstances)

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The institution explained to me that this was an internal mechanism, designed to reject "aberrant" orders. These are orders with prices that are too far from the last known price, particularly in the pre-opening phase. The mechanism was established in response to losses suffered by clients who had made major errors when entering orders.

In this case, I was told that the order placed by Mr H had been considered aberrant because it was 50% lower than the last known price.

The institution also acknowledged that it was unfortunate that the person who had spoken to Mr H by telephone in the context of this dispute had not been able to explain to Mr H the reasons for blocking his order when he called to express his concern.



The institution informed me that it could only note Mr H's intention to place a limit order of €10 (as evidenced by the telephone conversation) in the pre-opening period. Thus, according to the institution, had this order been placed under optimal conditions, his shares could have been sold - at best - at €11.55 (opening price).

Consequently, the institution finally agreed to compensate Mr H for an amount of €1,582.58 corresponding to the difference between the sale price obtained and the sale price he would have obtained if his order had been placed as he wished (i.e. a difference of 53 centimes per share).

Recommendation

Regarding the characteristics of the different order types:

First of all, I observed that the investor had not properly understood the characteristics of the different types of order (limit price/stop loss).

When he placed his first limit order at €10, Mr H had set a minimum selling price and was therefore not protecting himself against a possible drop in price.

If this €10 pre-opening order had not been considered too far from the last known price, and had been effectively taken into account, it would have been executed in any event, since €10 was a minimum price and the opening price of the V share was higher than the limit set (€11.55). Thus, assuming that the investor had wanted to limit his losses and protect himself against a possible market reversal, he should have set a price below which his order should have been automatically executed. To do this, Mr H should have placed a stop loss order at €10, and not a limit order. In this case, an order placed in this manner and at this price would not have been executed, since the lowest price observed during the session in question was €11.

The "stop loss" sell order makes it possible to set a price at which the sale will be made at or below that price (which is the opposite of a limit order), and therefore makes it possible to set a limit below which the order is in principle executed.

Regarding the rejection of the order by the account keeper:

With respect to the rejection of the order placed by Mr H, I noted that the general terms and conditions of this institution indicated the possibility of rejecting orders that seemed to be clearly incompatible with market conditions or with the holder's particular situation.



However, I asked the institution again for more information on its policy for blocking "aberrant" orders and, in particular, on the information provided to investors in this regard.

The institution admitted that it did not communicate much about this policy, and that information on this matter simply consisted in a pop-up window stating that the order was too far from the price, without any further details when an investor tried to place an "aberrant" order.

In this particular case, there was no doubt that the €10 limit order was far from the last known price. Nevertheless, I felt that this institution ought to be more precise in its policy, and make its position more visible and clear when it considers an order to be aberrant because it is too far from the last known price,

Although I find this lack of clarity regrettable, I cannot question a measure aimed at setting a threshold beyond which the order appears aberrant in order to prevent excessive volatility in the prices of securities, as well as input errors that can have serious consequences.^[1]

The institution's proposal of compensation seemed a positive reaction in the circumstances and I encouraged Mr H to accept it, which he did.

Lesson to be Learned

There are two lessons to be learned in this case:

For investors:

Firstly, it seems to me that investors should pay particular attention to the type of order they are choosing (market order, limit order and stop loss order). It is essential that investors regularly ensure that they fully understand the specific characteristics of the orders they choose, particularly in the case of priority orders and orders without price control. (See [Ombudsman's Online Diary - April 2022](https://www.amf-france.org/en/amf-ombudsman/ombudsman-online-diary/latest/stop-loss-order-does-not-give-investors-control-over-execution-price) URL = [https://www.amf-france.org/en/amf-ombudsman/ombudsman-online-diary/latest/stop-loss-order-does-not-give-investors-control-over-execution-price])

With regard to limit orders, they make it possible to buy at a maximum price or sell at a minimum price, provided, of course, that the price limit has been reached.

At the same time, I would like to remind investors that a limit order is first and foremost a means of protecting them against a possible market reversal, by limiting losses or ensuring a



minimum gain, but it does not allow them to control the price.


For professionals:

In view of the lack of understanding described in the case in question, it would be desirable, in my opinion, for institutions to communicate more on their policy regarding the blocking of orders that are too far from the last known price.

For example, when an "aberrant" order is rejected, it would be useful to display a pop-up window that explains this policy more fully.

[1] Commercial Division, Cour de Cassation, 13 December 2011, No. 10-10.103

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