

Market Integrity Notice

Guidance

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Suggested Routing

- Trading
- Legal and Compliance

SHORT SALE DESIGNATIONS AND RESTRICTIONS

Key Topics

- Short Sales
- Short Exempt
- Designations and Identifiers

Summary

This Market Integrity Notice provides guidance relating to the conduct of short sales and the need to designate such orders on entry on a Canadian marketplace as “short” or “short exempt” for the purposes of the Universal Market Integrity Rules.

UMIR Provisions Referenced

- Rule 1.1 – Definitions – “last sale price” and “short sale”
- Rule 1.2 – Interpretation
- Rule 3.1 – Restrictions on Short Selling
- Rule 6.2 – Designations and Identifiers

Questions / Further Information

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Market Integrity Notices Referenced

- Market Integrity Notice 2004-020 – *Sales of Restricted Securities* (August 13, 2004)
- Market Integrity Notice 2005-025 – *Bundling Orders from a Long and Short Position* – (July 27, 2005)
- Market Integrity Notice 2006-002 – *“When Issued” Trading* (January 30, 2006)
- Market Integrity Notice 2006-006 – *Sale Of Securities Subject To Certain United States Securities Laws* (February 17, 2006)

SHORT SALE DESIGNATIONS AND RESTRICTIONS

Summary

This Market Integrity Notice provides guidance relating to the conduct of short sales and the need to designate such orders on entry on a Canadian marketplace as “short” or “short exempt” for the purposes of the Universal Market Integrity Rules (“UMIR”).

Questions and Answers

The following is a list of frequently asked questions regarding the conduct of “short sales” (including the appropriate order designation and the application of price restrictions in particular circumstances) and the response of Market Regulation Services Inc. (“RS”) to each:

1. *Must a sell order be marked “short” if the security is trading on a marketplace on a “when issued” basis?*

If a person has entered into a contract to purchase a security by subscription to an offering or purchase on a “when issued” basis over-the-counter or on a marketplace or would become the holder of such security as a result of an arrangement, amalgamation or take-over bid, that person may sell such “when issued” securities on a marketplace which has posted a “when issued” market for that security and the order for the sale will be considered to be from a long position and should not be marked “short”.

However, if a marketplace has a “regular” market in units of that security which are issued and outstanding any sell order entered in the “regular” market by that person for the sale of their “when-issued” security, the sale will be considered a “short sale” and must be marked as such in accordance with Rule 6.2 of UMIR.

If a person does not have an entitlement to receive a security when that security is issued, any sale of that security in either the “when issued” or the “regular” market will be considered to be a “short sale”.

For a more detailed discussion of issues related to securities trading on a “when issued” basis, reference should be made to Market Integrity Notice 2006-002 – *Guidance - “When Issued” Trading* (January 30, 2006).

2. *What price restrictions apply to the short sale of a security that has not previously traded on a Canadian marketplace?*

Under Rule 3.1 of UMIR, a short sale may not be made at a price which is less than the “last sale price”. The term “last sale price” is defined in Rule 1.1 of UMIR as the “price of the last sale of at least one standard trading unit of a particular security displayed in a consolidated market display but does not include the price of a sale resulting from an

order that is a Basis Order, Call Market Order or Volume-Weighted Average Price Order.” The consolidated market display includes information on order or trades on an Exchange, QTRS or ATS operating in Canada. Information on trades which have occurred outside of Canada does **not** establish a last sale price for a security.

In accordance with Rule 1.2(4) of UMIR, if a security has not previously traded on a Canadian marketplace the “last sale price” shall be deemed to be the price at which the security has been issued or distributed to the public.

3. *What restrictions apply to the entry of a short sale on a marketplace prior to the marketplace opening for trading?*

In accordance with Part 1 of Policy 3.1 of UMIR, a short sale may not be entered on a marketplace prior to the opening of that marketplace for trading as a market order. In these circumstances, the short sale must be entered as a limit order and have a limit price at or above the last sale price of that security as indicated in a consolidated market display (or at or above the previous day’s close reduced by the amount of a dividend or distribution if the security will commence ex-trading on the opening).

4. *Must an order to sell a security subject to a U.S. resale restriction be marked “short” when the order is entered on a Canadian marketplace?*

If a Participant is asked to facilitate the sale into Canada of a security that is subject to resale restrictions in the United States, for example, by virtue of having been acquired under Rule 144A or Regulation D under the *Securities Act of 1933*, then an order to sell that security entered on a Canadian marketplace will generally be considered to be a “short sale” for the purposes of the definition under Rule 1.1 of UMIR. However, as the restriction will “disappear” upon the execution of a trade in Canada that complies with requirements of securities legislation in the United States, the sell order may be marked as “short exempt” in accordance with Rule 6.2 of UMIR on those marketplaces and facilities that permit that marker (and otherwise marked “short” if the “short exempt” marker is not supported) if the Participant effects the trade for “regular delivery” and the Participant would need to borrow free-trading securities to complete settlement while arranging for the removal of any restrictive legend. If the trade is completed as a Special Terms Order with “delayed delivery” to allow time before settlement for the removal of any restrictive legend, the sale will be considered to have been made from a “long” position and will not be marked as “short”.

For a more detailed discussion of issues related to sales of securities subject to a U.S. resale restriction, reference should be made to Market Integrity Notice 2006-006 – *Guidance - Sale of Securities Subject To Certain United States Securities Laws* (February 17, 2006).

5. *Must an order to sell a security that is subject to a resale restriction under applicable Canadian securities legislation (for example a four-month “private placement” hold period) be marked “short”?*

For the purposes of the UMIR definition of a “short sale”, a person will be considered not to own a security if the security is subject to a restriction on sale imposed by applicable Canadian securities legislation or a Canadian marketplace as a condition of listing or quoting the security.

A holder of a security which is subject to such a sale restriction who enters an order on a Canadian marketplace for the sale of the security before the expiration of the sale restriction must mark the sale order as “short”. This obligation to mark the order as “short” applies even if the sale restriction will expire prior to the settlement date of the trade.

For a more detailed discussion of the trading of restricted securities, reference should be made to Market Integrity Notice 2004-020 – *Sales of Restricted Securities* (August 13, 2004).

6. *A person holds an option and intends to pay the exercise price of the option from the proceeds of the sale of the securities that will be issued on the exercise of the option. Must the sell order be designated as “short”?*

The definition of “short sale” in Rule 1.1 of UMIR states that a seller shall be considered to own a security if the seller “has an option to purchase the security and has exercised the option”. Since the holder of the option has not done everything required to exercise the option (including the payment of the exercise price) at the time of the proposed sale, any sell order for the underlying securities must be designated as “short” and will be subject to the price restrictions under Rule 3.1 of UMIR.

7. *Must an order be marked “short” where it is a bundled order of a “long” and “short” position?*

Generally, sell orders from both a long position and a short position may not be bundled together. However, a sale order from a long position may be bundled with a sale order from a short position if:

- the bundled order is entered on a marketplace for the account or accounts of a single beneficial owner; or
- the bundled order is part of an intentional cross.

These exceptions are **not** available in certain circumstances and a bundled order involving sales from both a long and a short position must **not be entered** on a marketplace:

- prior to the opening of trading on that marketplace as the “short” element of the order might adversely impact the price at which the security opens for trading on that marketplace; or
- during a trading session when all trades in a particular security are executed at a single price.

On entry, an order bundling a “long” and a “short” order together should be marked as “short exempt” if that marker is available on the marketplace on which the order is entered. If the order is entered on a marketplace which does not provide for the inclusion of a “short exempt” marker, the sell order should not be designated as a “short sale”. In executing a bundled order, the long portion of the order will be deemed to have traded first. The short portion of the order will be deemed to comply with the price restriction requirement under Rule 3.1 of UMIR. If the bundled order does not fully execute in a single transaction, the Participant or Access Person must ensure that the short portion of the order does in fact comply with the price restriction requirement under Rule 3.1.

Reference should be made to Market Integrity Notice 2005-025 – *Bundling Orders from a Long and Short Position* (July 27, 2005).

Questions / Further Information

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