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STOCK EXCHANGE

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**For the attention of the
chairman/senior partner/compliance officer,
all member firms**

N57/07

STOCK EXCHANGE NOTICE

CONSULTATION ON THE DETAILED CHANGES TO THE RULES OF THE LONDON STOCK EXCHANGE IN PREPARATION FOR THE MARKETS IN FINANCIAL INSTRUMENTS DIRECTIVE AND GENERAL RULBOOK REVIEW

Introduction

1. The Exchange issued consultation Notice N08/07 in March 2007 highlighting the proposed changes to the Rulebook as part of its Rulebook Review. These changes were confirmed in a feedback statement issued on 11 June 2007 and made available on the corporate website. There are no changes to these confirmed outline rules.
2. This Notice therefore builds on N08/07 and provides the detailed rules consultation for the proposed changes to the Rules of the London Stock Exchange (“the rules”) to accommodate the Markets in Financial Instruments Directive (“the Directive” or “MiFID”). Member firms are encouraged to read N08/07 and its attachments which provide the background to this consultation.
3. The Exchange’s MiFID product offering has already been confirmed via the MiFID Service and Technical Description issued on 20 June 2007. This provides information on subjects such as trade reporting responsibilities, delayed publication thresholds and trade type indicators, which will not change as a result of this detailed rules consultation.
4. There are 3 attachments to this Notice:
 - a) Attachment 1 - the revised Rules
 - b) Attachment 2 - a cross referencing tracker document
 - c) Attachment 3 - a parameters spreadsheet

Guidance notes to assist in the review of these attachments are provided below.

Key features of the new rules

5. In accordance with the objectives of the Rulebook Review, the following are the key features of the new rules:
 - a) A 50% reduction in the number of rules and definitions.
 - b) The scope of the on Exchange rule amended recognising MiFID.
 - c) Transaction reporting rules removed.
 - d) Order book trading rules reduced to approximately 15 rules, recognising the increased order entry functionality of TradElect™.
 - e) Off order book trading rules consolidated into approximately 60 rules.
 - f) Market making rules consolidated together into one section, including gilt-edged and fixed interest market making.
 - g) Settlement, clearing and benefit rules pulled together into one section.
 - h) Compliance procedures unchanged.
 - i) Default procedures relatively unchanged with one rule amended and 9 rules deleted.

Guidance for reviewers

6. The following methodology has been used for the Rulebook review:
 - a) The rules and guidance which are being kept, but re-located, are shown in black text and retain their existing rule number for ease of cross referencing during the consultation period. All rules will be re-numbered at the point of confirmation.
 - b) Rules that are being deleted have been removed from the new Rulebook but are cross referenced in the tracker document.
 - c) New rules are highlighted in green text and given temporary numbers in a 0000 series.
 - d) The tracker document lists every definition and rule indicating whether they are being kept or deleted. Explanatory notes are provided where applicable to assist in the review.
 - e) Supplementary guidance has been moved to sit with the relevant rule rather than as a section at the back of the rules. Rules with guidance are flagged with the notation "G".
 - f) Rules that are Exchange direction type rules are flagged with a "D" .
 - g) Rules that are supported by information in the Guide to Trading Services are flagged with a "GS".
 - h) Rules that are supported by specific parameters are flagged with a "P". The parameters spreadsheet provides the specific system thresholds that govern member firm interaction with TradElect™. Further information on the parameters is provided below.

Parameters

7. The parameters spreadsheet should be used cross referenced where indicated in any particular rule. At a segment and sector level, the parameters include a breakdown of:
 - regulated market (RM) or multilateral trading facility (MTF)
 - the transparency regime (on-Exchange rule 0010)
 - market maker quote type (firm or EQ) (n.b. minimum quote size 1* EMS for all segments)
 - whether named orders enabled
 - whether iceberg orders enabled (n.b. minimum peak for all segments is 0.4 * EMS)
 - whether dynamic tick enabled
 - minimum order size
 - price monitoring parameters
 - trade types enabled

There are also separate worksheets which provide:

- all tick sizes on TradElect™
- dynamic schedules in place
- list of trade types
- trade report fields for both AC and AD messages
- delayed trade publication schedule

Notable changes to the rules

8. Sections of the Rulebook

The membership (the 1000 series rules), core non-trading (the 2000 series rules) and core trading (the 3000 series rules) sections have been pulled together into one section called Core Rules. The domestic market (the 7000 series rules), international equity market (the 7100 series rules), gilt-edged and fixed interest market (the 7200 series rules) and AIM (the 7300 series rules) sections have been deleted and the relevant rules distributed into the new sections. The traditional options market (the 7400 series rules) has been removed.

9. Deferred publication

The Exchange has removed rules relating to worked principal agreements and protection and modified the block trade rules to accommodate the new MiFID deferred publication regime.

10. Member firm system problems

The various dispersed rules relating to member firm system problems have been consolidated together into one new rule (rule 0005) in the core rules section. The guidance is a compilation of existing rather than any new guidance.

11. Market situations

The concepts of trading halts, indicative markets and fast markets have been replaced with a more general term of market situation used to describe issues that impact the orderliness of trading on the Exchange's markets. Hence the numerous rules relating to indicative and fast markets have been replaced by a single rule for market situations (rule 0006).

12. Market maker rules

The market maker obligation rules have been pulled together into one section and divided between order driven, quote driven, gilt-edged and fixed interest. Obligation and exceptions to obligation rules have been collated into a more logical order. These rules also now reference executable quotes or firm quotes where applicable.

13. The concept of market makers in groups has been modified recognising that member firms can now segregate their business by member ID. Hence market maker obligation rule 4400 has been amended so that a member firm that operates under a member ID which also includes a market maker shall be treated as if it was a market maker.

14. Interaction with market makers

As notified in the June confirmation, member firm order exposure rules have been removed in recognition of the over-arching requirements of best execution. The negotiated trades waiver available under MiFID will ensure that an on Exchange trade that is not subject to pre-trade transparency will be representative of the current market price as detailed in the new defined term for negotiated trade.

15. Lending arrangements

The stamp legislation has been amended to remove the venue requirement, including for lending arrangements. However AIM securities remain an exception and relief will continue to only be available on a venue specific basis. The Exchange has therefore added a new rule (rule 0011) to its off order book trading rules allowing member firms to bring these on Exchange using their existing settlement instruction arrangements.

16. Voice recording

A requirement for voice recording has been maintained within the core rules (rule 4170). Market makers will continue to be subject to this rule and in addition all member firms meeting the specified criteria. The reference to intermediaries is been removed from the rules. The Exchange has not changed the length of time that recordings must be maintained, pending the outcome of the FSA's review of this subject.

17. Member firm as agent for non-member principal

In light of the large expansion of order routing business conducted by member firms, the Exchange is removing the rule permitting a member firm to undertake activities as agent for a non-member principal (rule 3110). This permission is seen as out-dated and not relevant in a post MiFID environment.

18. Settlement and clearing

All the settlement and clearing rules have been grouped together into one section on settlement, clearing and benefit rules. A number of rules have been removed and now appear as guidance instead and the ordering of the remaining rules has been made more logical.

19. Central counterparty

The rules relating to central counterparty contracts for both LCH and Clearnet have been replaced by revised generic rules accommodating both novation and open offer clearing. This has led to a reduction in the number of rules in this area and positions the rules to accommodate other central counterparties that may offer services for the Exchange's markets in the future.

20. Customers and clients

The Exchange currently has one definition for "client" and one for "customer". In order to streamline the rules, only "customer" will be retained. All existing references to client will be replaced by customer.

21. Member firm services

Rules that relate to services offered by member firms, such as inter dealer brokers, settlement agents and model B firms, have been grouped together in the core rules section. The defined terms for equity inter dealer broker and designated fund manager have been removed.

Fragmentation

22. The Exchange highlighted a number of fragmentation issues in N08/07, including dealing in suspended securities, when issued dealing, obligations to settle and contract notes and trade confirmations. Whilst the Exchange has accommodated these in the revised rules, issues such as PTM levy and roll over trading deserve special mention.

23. The Exchange has been considering whether or not it would be appropriate for the PTM levy rule 2220 to remain in place after the introduction of MiFID. The Exchange's view is that it would be content for the rule to remain provided that trades on other venues are also subject to an identical levy. The Exchange is in discussion with the Panel to see what comfort can be obtained in this regard. Further information on this subject can be found in the tracker document under rule 2220.

24. The Exchange has decided to remove the roll over trade rule, primarily because of the multi-venue environment which MiFID introduces. The Exchange is still of the opinion that the rolling of positions can create a misleading impression as to the price or value of a security. Consequently some of the Exchange's existing guidance on roll over trading will be incorporated into general conduct rule 3300.6.

Useful information

25. The following information links are provided to assist member firms in their review of these rules:
- Rulebook Review website page containing confirmation of outline rules
<http://www.londonstockexchange.com/en-gb/products/membershiptrading/rulesreg/rulebookreview2007/>
 - MiFID Service and Technical Description
<http://www.londonstockexchange.com/NR/rdonlyres/EB7E86AF-8236-49B1-9A6C-D703708D469A/0/ServiceandTechnicalDescriptionJuly2007.pdf>

Consultation

26. As already stated, this consultation builds on the high level consultation and confirmation already completed. The Exchange recognises that the lead time to the implementation of MiFID is now quite tight and member firms and software houses need to finalise their systems and procedures in readiness. Reviewers are therefore asked to provide any comment and feedback on this consultation by Monday 10 September 2007. The Exchange would however welcome feedback at the earliest possible opportunity.
27. Subject to any feedback received as part of this consultation, the Exchange proposes to issue a rules confirmation Notice during September, with rules effective date set for 1 November 2007.
28. Any comments or queries on this Notice should be addressed to John Newbury, telephone (0044) 20 7797 1615, STX 31615, email jnewbury@londonstockexchange.com.

Nick Bayley
Head of Trading Services

This Stock Exchange Notice will be available on the website at:
<http://www.londonstockexchange.com/en-gb/products/membershiptrading/rulesreg/stockexnoticesnew/>

Calls to London Stock Exchange plc may be recorded to enable the Exchange to carry out its regulatory responsibilities.