

## Attachment 2 to Stock Exchange Notice N13/11

### Member firm services

#### Gilt inter dealer brokers and wholesale dealer brokers [1120-1128]

##### List of users

1124	A <b>member firm</b> which operates a service that is available to users other than <b><u>gilt-edged market makers</u></b> must maintain an up to date list of all users of that service and supply such a list to any <b><u>gilt-edged market maker</u></b> using that service on request. Any subsequent changes to a list already supplied shall be sent immediately to each such <b><u>gilt-edged market maker</u></b> .
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### Systems and trading

#### Member firm system problems [1500]

G 1500	Where a <b>member firm</b> identifies a system problem it shall inform the <b>Exchange</b> in accordance with notification rule 1050 and follow any subsequent instructions from the <b>Exchange</b> . An authorised employee of a <b>member firm</b> may request the deletion of orders or <b>quotes</b> .
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##### *Guidance to Rule:*

*For the purposes of this rule, a system problem would include, but not be restricted to, one preventing:*

- a **member firm** accessing its orders on the **trading system**;
- a **member firm** submitting a **trade report**;
- a **market maker** maintaining, amending or deleting its **quotes**; or
- a **market maker** from answering its telephone lines.

##### *Dealing during a systems failure:*

*While a **member firm** is experiencing a system failure it is not precluded from dealing in the relevant securities. However, the **member firm** must ensure that any **on Exchange** trades are reported to the **Exchange** in compliance with the rules.*

##### *Orders and quotes:*

***Member firms** are reminded that, while orders remain on the **trading system** they are firm and available for execution. Accordingly, it is essential that a **member firm** contact the **Exchange** as soon as possible when it experiences a system failure, especially if it wishes to have its orders deleted from the book.*

*Once the systems problem is rectified, the **member firm** should contact the Market Supervision department to notify them of this fact. The **member firm** can recommence order input to the **trading system** as soon as the systems problem is rectified.*

*If a **member firm** wishes to reverse an automatically executed trade in accordance with rule 2110 while it is experiencing a systems problem, it should seek guidance from the Market Supervision department on (0044) 20 7797 3666, (STX 33666) - option 2, to determine whether a **contra** submission should be made immediately or after the system problem is resolved.*

##### *Order and quote deletion:*

***Member firms** have primary responsibility for deleting their own orders. Where this is not possible, the **Exchange** will aim to provide a back-up service to delete orders.*

*The **Exchange** will maintain a list of **employees** authorised by each **member firm** to request the deletion of orders and **quotes**. A person authorised by a **member firm** must be "a director, partner or principal or person employed in or about the firm's business as a **member firm**, whether under a contract of service or for services (including a training contract) and*

any person seconded to work in or about that business".

If a **member firm** requests the **Exchange** to delete its orders or **quotes**, the **Exchange** will only action this request if it comes from a person named on the **member firm's** authorised person list. The **Exchange** will refuse to provide details of the names on a **member firm's** authorised list to anyone not themselves on the list and a request received from someone not on the authorised list will be declined. In this event the **Exchange** will contact the **member firm's** compliance department for clarification in respect of the request.

**Member firms** that choose to segregate their business by multiple **Trader Groups** will need to provide a list of individuals authorised to delete orders on behalf of each **Trader Group**. **Member firms** are advised to ensure that the list is broad enough to provide sufficient coverage in cases of staff absence. For example, it may be more practical to have a number of nominated people in compliance who are authorised to request deletions for all **Trader Groups**.

**Member firms** should register authorised **employees** or changes in their status with the **Exchange** using the form supplied for the purpose.

Recognition of new authorised **employees** will be effective on the business day after the notification is received by the **Exchange**.

When contacting the **Exchange** to request the deletion of an order or **quote**, the authorised person must provide the following information:

- the name of the **member firm**;
- the **member firm's member ID**;
- the **member firm's trader group**; or
- the **member firm's Comp ID**;
- the identity of the caller and a contact number; and
- the reason for the request (e.g. system problems, building evacuation).

For single order deletions (up to a maximum of five), the **member firm** must also provide the Order ID. If this is not available, the **member firm** should provide:

- the name of the security;
- whether it is a buy or a sell;
- the price and size; and
- the time the order was entered.

If a **member firm** requests the deletion of more than one order in a single security, each of the orders will count towards the maximum allowed number of five order deletions. The Market Supervision department will normally delete all orders within a particular segment. However, upon application, the Market Supervision department will consider the deletion of individual orders providing the total of individual orders does not exceed five.

For mass order deletions, the **member firm** must provide the following information:

- whether it wants all orders and / or **quotes** deleted; and
- the specific segments to which the deletions should apply.

**Member firms** should be aware that all parked orders will be deleted during a mass order deletion performed by the **Exchange**.

The Market Supervision department will attempt to delete orders as soon as possible after receipt of a valid request to do so. However, if an order is executed during the period between a **member firm** requesting deletion of its orders and the Market Supervision department effecting the deletions the **member firm** will be obliged to honour the trade.

Trade reporting:

Where a **member firm** has a system problem that prevents it from submitting a **trade report** (where it has the responsibility to do so), the **member firm** must immediately upon execution of the trade inform the **Exchange**.

The **Exchange** will determine what trade details it requires until such time as the problem is

resolved. This will normally be any trade in a size that is in excess of six times the **Exchange market size** for the security (or the equivalent average daily turnover) or a consideration in excess of £1,000,000. The same procedure will apply to the correction of a trade report during a system problem. Such trades must not then be re-reported by the **member firm** once the system problem has been resolved.

If any trades are re-reported, they should be cancelled as soon as the **member firm** becomes aware of the error. If a **member firm** is unable to effect a cancellation it should contact the **Exchange** immediately.

If the **Exchange** is not informed of a **member firm's** trade reporting difficulties, it will treat resultant late trade reports as breaches of rule 3020.

#### Market maker systems:

In the event of a **market maker** system problem, including a problem arising from an act or omission beyond the **market maker's** control, ~~the **Exchange** will issue a market status message explaining that the **market maker** should notify the **Exchange** that it is unable to update its **quotes** on the **trading system**.~~ If system problems persist on subsequent business days, the **market maker** is required to notify the Market Supervision department on (0044) 20 7797 3666, (STX 33666) prior to the start of the **mandatory period** of each subsequent day ~~so that market status messages can be issued.~~

If a **market maker** cannot update or delete its own **quotes**, it may ask the **Exchange** to close its prices in a sector or segment until the fault has been repaired. Where a reported fault affects a dealer terminal only, that **market maker** in a **quote-driven security** is expected to continue to quote firm prices over the telephone.

If a **market maker** in a **quote-driven security** reports has problems with any telephone lines associated with its dealing desk, the **market maker** should notify the **Exchange** as soon as possible. ~~a market status messages can be issued to advise users of an alternative number, where available.~~

A **market maker** should contact their market access provider at the same time as it notifies the **Exchange**.

The **market maker** should re-enter its **quotes** as soon as it is able to do so, notifying the **Exchange** beforehand. In all cases a **market maker** shall ensure that the Market Supervision department is kept appropriately informed.

## **ORDER BOOK TRADING RULES**

### **Order entry**

(Rules 2000 – 2101 unchanged)

#### **Access to the trading system and the responsibility of member firms**

G	2103	A <b>member firm</b> may allow a <b>customer</b> to submit orders to the <b>trading system</b> under the <b>member firm's</b> trading codes, either by way of <b>direct market access</b> or by providing <b>sponsored access</b> , subject to the <b>member firm</b> having in place adequate systems and controls.
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Guidance to Rule:

#### **Direct market access and sponsored access**

Submission of **customer** orders may be facilitated by either **direct market access** or via a **sponsored access** to the **trading system**.

**Direct market access** is a service through which a **member firm** allows a **customer** to submit orders to the **trading system** under the **member firm's** trading codes and via the **member firm's** usual order management systems, but without manual intervention by the **member firm**. These order management systems may be housed within the **member firm's** facilities or hosted within the **Exchange's** Primary Data Centre but, importantly, are the same

systems through which the **member firm** submits at least some of its own order flow to the **trading system**.

**Sponsored access** is a direct technical connection provided so that a **customer** is able to access the **trading system** under a **member firm's** trading codes. As the connection is direct, orders submitted by the **customer** to the **trading system** do not pass through the usual order management systems of the **member firm**.

**Exchange** level controls are provided within the **trading system** to assist **member firms** with **sponsored access** order flow validation. All orders submitted via **sponsored access** will pass through the **Exchange** level controls before reaching the **order book**.

Responsibility for **customers'** order flow (whether submitted to the **Exchange** via **direct market access** or **sponsored access**)

**Member firms** providing **customers** with **direct market access** or **sponsored access** to the **trading system** are responsible for all obligations and liabilities arising from the entry, deletion and execution of all orders submitted by that **customer**.

The **Exchange** is aware that **member firms** may have contractual arrangements with their **customers** that mean the **customer** bears the financial risks of entering erroneous orders. However, under the **Exchange's** Rules the responsibility for such orders rests wholly with the **member firm** under whose trading codes the order is entered.

The **Exchange** requires a **member firm** providing **direct market access** to be able to delete a **customer's** orders from the **trading system**. ~~or, if necessary, restrict the **customer's** ability to enter orders, without having the express consent of the **customer**. Such action by the **member firm** may be instigated unilaterally by the **member firm** because of its own concerns regarding the **customer's** behaviour or at the specific instruction of the **Exchange**.~~

**Member firms** providing **sponsored access** may contact the Market Supervision department to delete a **customer's** orders from the **trading system** following the guidance set out under rule 1500. Where the number of individual order deletions exceeds five, a mass order deletion is required. As the Market Supervision department actions such requests using reasonable endeavours, **member firms** should consider utilising the proactive kill switch to delete orders immediately where a mass order deletion is necessary.

**Member firms** must be able to restrict a **customer's** ability to submit orders to the **trading system**.

**Member firms** must have the ability to delete a **customer's** orders or restrict their ability to submit orders to the **trading system** without having the express consent of the **customer**. These actions may be instigated unilaterally by the **member firm** because of its own concerns regarding the **customer's** behaviour or at the specific instruction of the **Exchange**.

The **member firm** is expected to adopt a regime where sufficient consideration is given to assess matters such as:

- the training that has been given to the individuals entering orders;
- the access controls over order entry that the **customer** applies;
- security controls over any network link between the **customer** and the **member firm**. These should be sufficient such that the **member firm** can be sure that an order purporting to come from a **customer** actually has done so (e.g. by use of authentication codes in a similar manner to the secure interactive interface linking the **member firm** to the **Exchange**); and
- clear allocation of responsibility for dealing with actions and errors (e.g. it should be clear how, when and by whom orders on the book would be deleted).

All of these matters should be dealt with in formal agreements between the **member firm** providing **direct market access** or **sponsored access** and its **customer**. (**Member firms** may provide **sponsored access** to non **member firms** only.)

### **Direct market access**

Whilst ongoing education, training and guidance for a **member firm's customers** that submit orders through the **member firm** to the **trading system** are to be encouraged, these cannot entirely replace the safeguards that internal system controls and alerting functionality can provide.

In order to prevent the submission of erroneous orders by a **customer**, a **member firm** may wish to consider the following controls and system alerts:

- prevention of submission of an order if the **customer** has overridden alerts and/or notification to the **member firm** that the **customer** has attempted to over-ride the alert;
- the segregation of this order flow by the use of the Trader Group facility within the **trading system**;
- appropriate training, education and guidance provided to those **customers** entering orders;
- the need for order acknowledgements from the **customer**;
- controls over maximum order sizes that can be submitted by different **customers**;
- controls over prices of orders and having system parameters that would generate an alert if the order would execute at a price with which the **member firm** would not be satisfied; and
- monitoring and controls over the total exposure of the **member firm** to orders submitted for a particular **customer**.

### **Sponsored access**

The **Exchange** does not require **sponsored access** order flow to pass through the **member firm's own system controls** but mandates that all orders submitted via **sponsored access** will pass through **Exchange** level controls, ~~however, before reaching the order book.~~ **Member firms** should also assess whether any additional controls are necessary to appropriately manage **customer** order flow, taking into consideration the nature and complexity of its **customer's** business.

**Member firms** are responsible for determining the limits of the configurable **Exchange** level controls within the parameters provided by the **Exchange** and ensuring that they are appropriate for each individual **sponsored access customer**, based on the scope and scale of its business.

A **member firm** that provides this facility for a **customer** must:

- complete a **sponsored access** application form for each of its **sponsored access customers** and inform the **Exchange** if it becomes aware that the information provided on the form has changed;
- ensure that relevant staff at the **customer** are conversant with the Rules and, in particular, those relating to **order book** trading. Relevant staff include the Head of Trading, the Head of Compliance and person(s) who signs off trading algorithms at the **customer**;
- segregate each **customer's** order flow from the **member firm's** order flow using the Trader Group facility within the **trading system**. This is necessary to assist the **Exchange** in maintaining fair and orderly markets;
- provide the **Exchange** with the name, ~~head~~ registered office address and country of incorporation of the **member firm's customer** for regulatory purposes. This information will be treated as confidential and will not be subject to commercial use;
- have systems in place which will allow the **member firm** to accept and review drop

copy feeds, on a real-time basis from ~~its customer~~ the **Exchange** and monitor all **sponsored access** order and post-trade flow;

- proactively utilise the **Exchange's** proactive kill switch facility to disconnect a **customer** which it has reason to believe is behaving inappropriately; and
- inform the **Exchange** and take appropriate action if it loses either its connectivity with the **Exchange** or its connection to ~~its customer(s)~~ the drop copy feed from the Exchange where that connection allows the **member firm** to monitor the **customer(s)** order and post-trade flow. The **Exchange** mandates the use of its cancel on disconnect facility. Where a connection is dropped by either the **member firm** or its **sponsored access customer**, all of the sponsored access customer's orders will be deleted from the **order book**.

G 2104

A **member firm** must undertake due diligence on any **customer** to which it provides or intends to provide **sponsored access**, in order to assess the suitability of any such **customer** to have a **sponsored access** connection. The **member firm** must confirm to the **Exchange** that such due diligence has been undertaken.

*Guidance to Rule:*

A **member firm** must have undertaken due diligence to confirm that any **customer** to which it provides **sponsored access**:

- is considered fit and proper to have a direct technical connection to the **trading system**;
- has appropriate financial resources;
- has sufficient staff with adequate knowledge, experience, training and competence for the activities the **customer** undertakes on the **Exchange's order books**. **Member firms** may wish to consider whether training should be provided to the Head of Trading, the Head of Compliance and person(s) who signs off trading algorithms at the **customer**; and
- has adequate internal procedures and controls for these activities notwithstanding the **Exchange** level controls provided for all sponsored order flow.

This assessment may fit within the **member firm's** existing due diligence framework or, if considered necessary, involve new due diligence processes that are specific to the provision of **sponsored access**. It is for **member firms** to judge what due diligence is necessary given the business, trading strategies and order flow of the **customer** or prospective **customer** to which the **member firm** wishes to provide **sponsored access**.

**Member firms** are required to confirm when submitting an application form that they have undertaken appropriate due diligence to be satisfied on each of the above points. ~~A template letter is provided on the Exchange's website.~~ The **Exchange** will exercise its right under rule 2105 to refuse **sponsored access** if it believes that the **member firm's** due diligence is inadequate.

Furthermore, **member firms** are required to satisfy themselves and, when requested, the **Exchange** that the **customers** to which they have provided **sponsored access** continue to meet these requirements. For instance, if a **customer** to which a **member firm** has provided **sponsored access** has a significant change in trading volumes or its trading model, the **member firm** may consider it appropriate to refresh its due diligence and/or the limits at which the **Exchange** level controls have been set for that **customer** to ensure that its systems, controls, training and staffing are adequate for its changed business. Otherwise, due diligence should be periodically reviewed according to the **member firm's** normal timetable, and the **Exchange** may require the **member firm** to share this reviewed due diligence with it. A **member firm** that becomes aware that a **customer** no longer meets the requirements must notify the **Exchange** immediately and cooperate with the **Exchange** to halt the **customer's** **sponsored access**.

# OFF ORDER BOOK TRADING RULES

## Trades

### On Exchange trades [3000]

G P	3000	A trade is <b>on Exchange</b> if one or both of the parties to the trade is a <b>member firm</b> (whether as <b>agent</b> or as <b>principal</b> ) and the trade is effected:
	3000.1	in a <b>MiFID transparent security</b> (as detailed in <b>parameters</b> ) and the <b>member firm</b> and its <b>customer</b> or <b>counterparty</b> agree at or prior to the time of effecting the trade that it shall be subject to the rules of the <b>Exchange</b> ;
	3000.2	in an <b>AIM security</b> (as detailed in <b>parameters</b> ) unless the <b>member firm</b> and its <b>customer</b> or <b>counterparty</b> agree at or prior to the time of effecting the trade that it shall be subject to the rules of an <b>AIM primary market registered organisation</b> or an <b>AIM secondary market registered organisation</b> and reports the trade to it in accordance with that organisation's rules; or
	3000.3	in any security admitted to trading on the <b>Exchange's</b> markets not covered by 3000.1 & 3000.2 above (as detailed in <b>parameters</b> ) unless the <b>member firm</b> and its <b>customer</b> or <b>counterparty</b> agree at or prior to the time of effecting the trade that it shall be reported to a venue that has equivalent or greater post-trade transparency than the <b>Exchange's</b> regime for that security.

*Guidance to Rule:*

#### 3000.2

##### AIM primary market registered organisation

**Member firms** may only treat a transaction dealt on an **AIM primary market registered organisation** as being off **Exchange** if (i) the issuer whose security is being traded is regulated by that **AIM primary market registered organisation** in accordance with the considerations outlined in the paragraph below and (ii) they are a member of that **AIM primary market registered organisation** and are reporting the trade to it.

*In determining whether a trading venue qualifies as an **AIM primary market registered organisation**, the **Exchange** will consider whether the trading venue has rules that place a continuing obligation on the **AIM** issuer for the timely disclosure of corporate information; whether those rules also oblige the issuer to provide all necessary information to the trading venue to maintain a proper market in the **AIM securities**; and whether the trading venue has the discretion to refuse to admit to trading, to suspend from trading and to cancel from admission to trading the securities of **AIM** issuers.*

*It is expected that most **AIM primary market registered organisations** will be overseas venues on which **AIM** issuers have chosen to list their securities in addition to being admitted to trading on **AIM**.*

##### AIM secondary market registered organisation

**Member firms** may only treat a transaction dealt on an **AIM secondary market registered organisation** as being off **Exchange** if they are a member of that **AIM secondary market registered organisation** and are reporting the trade to it.

*The regime for **AIM secondary market registered organisations** is designed to provide **member firms** with the ability to trade **AIM securities** on other venues in a manner that will allow the **Exchange** to retain adequate oversight of the **AIM** market and to ensure the maintenance of high regulatory standards. In particular, the regime will allow the **Exchange** to maintain a proper market in **AIM securities**. The requirement to operate a proper market is set out in the Recognition Requirements Regulations and associated FSA Handbook ("REC").*

Where no primary market relationship exists between the applicant venue and the issuer, the **Exchange** will apply the following criteria to establish the suitability of an applicant to be an **AIM secondary market registered organisation**. The criteria that follow represent the minimum standards which the **Exchange** will apply for the purpose of deciding whether an applicant venue may qualify for recognition as an **AIM secondary market registered organisation** in accordance with Rule 3000.2.

1. The **AIM secondary market registered organisation** must have the ability and have appropriate gateways to communicate freely with the **Exchange** on regulatory matters generally, without regard to matters such as client confidentiality or commercial secrecy;
2. The **AIM secondary market registered organisation** must provide at least equivalent pre- and post-trade transparency as that provided by the **Exchange** on **AIM**;
3. The **AIM secondary market registered organisation** must implement practical operational mechanisms (to be approved by the **Exchange**) to provide real time trading information to the **Exchange** on a continuous basis, in respect of transactions in **AIM securities** admitted to the **AIM secondary market registered organisation**. These arrangements may vary from case to case, but must include information that will enable the **Exchange**, in relation to trading in **AIM securities**, to:
  - see all executed trades immediately, including any unpublished trades;
  - identify both counterparties to the trades; and
  - identify through its surveillance system whether any anomalous trades or unusual trading is taking place on the **AIM secondary market registered organisation**.

The above information is required in order that the **Exchange** can ensure a proper market in **AIM securities**. Any material failure to meet these criteria by a venue will result in the **Exchange** withdrawing **AIM secondary market registered organisation** status with immediate effect.

The **Exchange** will maintain a list of the approved **AIM secondary market registered organisations** on its website.

#### 3000.2 & 3000.3

In relation to rules 3000.2 and 3000.3, where a **member firm** is interposed between two principal trades entered at the same time and price and one trade has been reported for publication, there is no obligation to report the second leg to the **Exchange**. **Member firms** should note that if they wish the second leg to be regarded as an **on Exchange** trade then they will have to submit a separate, non publishing **trade report** using the "NM" trade type. This will ensure the **Exchange** has a satisfactory audit trail of the second principal trade.

#### General Exclusions

The following trades would not be considered to be **on Exchange**:

- ~~The equity legs of stock and option contingent strategies.~~
- Trades executed and published under the rules of a Multilateral Trading Facility not operated by the **Exchange**.
- The creation and redemption of **Exchange Traded Funds** (unless bringing **on Exchange** for stamp relief reasons in which case such trades can be reported as non publishing trade reports).

In addition a contract to place, offer or underwrite securities that are the subject of an application to be **admitted to trading**, or admitted to trading on a venue where the contract is made before the application is accepted.

Primary allocations subject to listing are off **Exchange**.

An exception to this is the exercise of an over-allotment option ("green shoe") which is

commonly agreed by a sponsoring **member firm** as part of the stabilisation and underwriting arrangements for an introduction to **admission to trading**, as well as for further new issues of shares. Whether the option is ever exercised, and the extent to which it is utilised, will depend on the take up of the issue, the underlying share price in the market and the stabilisation transactions undertaken. Such trades can be brought **on Exchange** under the following circumstances:

- the terms of the green shoe option must be agreed and included in the circular, prospectus or an **AIM** admission document, where such documentation is required by law or is voluntarily published, prior to sign-off, including confirmation that the option writer holds sufficient shares to meet any obligation under the option;
- that at the point of exercise the shares to be delivered are admitted to trading; and
- a regulatory news announcement has disclosed that exercise has taken place.

Once the shares have been **admitted to trading**, and if all the above points have been met, the exercise of the green shoe option may be trade reported to the Exchange immediately after the agreement to exercise. This will typically be at the same time as the disclosure announcement is made that the exercise has taken place. **Member firms** who wish to report such arrangements to the **Exchange** should contact the Market Supervision department on +44 (0) 20 7797 3666 (STX 33666). The **Exchange's** guidance on reporting the exercise of a green shoe does not override a **member firm's** obligations under UKLA rules.