



Automated Trading Systems

The European Securities and Markets Authority (“ESMA”) recently published its guidelines on systems and controls in an automated trading environment for trading platforms, investment firms and competent authorities (the “Guidelines”).

The Guidelines which are issued under Article 16(3) of the ESMA Regulation No. 1095/2010 set out a comprehensive regime governing the operation of electronic trading systems by a regulated market, a multilateral trading facility (“MTF”) or an investment firm. Competent authorities and financial market participants must make every effort to comply with the Guidelines and their underlying recommendations. ESMA expects all relevant competent authorities and financial market participants to comply with the Guidelines unless otherwise stated.

The underlying objective of the Guidelines is to promote fair and orderly trading, market integrity, financial stability and increase investor protection.

The FSC has issued a Guidance Note on Automated Trading Systems (the “Guidance Note”) which effectively sets out the ESMA’s guidelines. The purpose of this Newsletter is to summarise the contents of the Guidance Note.

The Guidelines are applicable to the following:

- (a) the operation of an electronic trading system by a regulated market or a MTF;
- (b) the use of an electronic trading system, including a trading algorithm, by an investment firm dealing on its own account or for the execution of orders on behalf of clients; and
- (c) the provision of direct market access or sponsored access by an investment firm as part of the service of the execution of orders on behalf of clients.

The Guidelines also apply to firms which are not authorised as market operators or investment firms under the Markets in Financial Instruments Directive (“MiFID”) and firms exempt from MiFID that trade on own account and access trading platforms directly as members, participants or users, or through Direct Market Access (“DMA”) or Sponsored Access (“SA”).

Failure to comply with the Guidelines could result in (a) investors not being consistently protected against, for example, investment firms making errors when executing client orders, (b) investors not being able to interpret trading information properly and therefore not being able to make adequate investment decisions (both of these scenarios can lead to possible financial loss for investors), (c) investors being less able to trade as and when they wish to do so, due to having less robust or resilient systems available, and (d) the prevalence of an increased risk of possible market manipulation.

The Guidance Note sets out the following 8 separate overarching guidelines:

Guideline 1:

Organisational requirements for regulated markets’ and multilateral trading facilities’ electronic trading systems



Guideline 2:

Organisational requirements for investment firms' electronic trading systems (including trading algorithms)

Guideline 3:

Organisational requirements for regulated markets and multilateral trading facilities to promote fair and orderly trading in an automated trading environment

Guideline 4:

Organisational requirements for investment firms to promote fair and orderly trading in an automated trading environment

Guideline 5:

Organisational requirements for regulated markets and multilateral trading facilities to prevent market abuse (in particular market manipulation) in an automated trading environment

Guideline 6:

Organisational requirements for investment firms to prevent market abuse (in particular market manipulation) in an automated trading environment

Guideline 7:

Organisational requirements for regulated markets and multilateral trading facilities whose members/participants and users provide direct market access / sponsored access

Guideline 8:

Organisational requirements for investment firms that provide direct market access and/or sponsored access

The Guidance Note provides a general guideline and then detailed guidance for each of the 8 areas highlighted above, and includes matters such as governance, business continuity, staffing, record keeping, pre- and post-trade controls, reviews, internal audits, training, etc.

Published by:

Financial Services Commission
PO Box 940
Suite 3, Ground Floor
Atlantic Suites
Europort Avenue
Gibraltar

www.fsc.gi

Tel : +350 200 40283

Fax : +350 200 40282

Date Published 1st June 2012