

# virt-x *compliance*

Newsletter from  
virt-x Regulation and Compliance Department

30 March 2006  
Issue 14

We hope you will find this issue of virt-x *compliance* useful. We welcome your comments and suggestions.



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## **MARKET NOTICES**

The numbering of virt-x's Market Notices was changed with effect from 1 January 2006, restarting with 001.

Since the last Compliance Newsletter, Market Notices 761 to 010 inclusive have been issued. The contents of those Market Notices have been included in standing data with exception of Market Notice 003 setting out the virt-x market holidays and Market Notice 004 concerning the trial removal of the closing auction on virt-x for pan-European securities. Both of these topics are detailed below. .

All Market Notices are available at [www.virt-x.com](http://www.virt-x.com) in the Regulation section.

## **UPDATES TO RULES AND DIRECTIVES**

There have been no changes to the virt-x Rules or Directives since Compliance Newsletter 13.

The Rules and Directives are also available at [www.virt-x.com](http://www.virt-x.com) in the Regulation section.

## **VIRT-X MARKET HOLIDAYS**

Market notice 003 advised members that virt-x will be closed for all business on the following days each year, unless there is an announcement to the contrary:

- 1 January
- Good Friday
- Easter Monday
- 25 December
- 26 December.

In addition, virt-x order books will be closed on the following dates but members can report off-order book transactions unless the date falls on a UK Bank Holiday:

- 2 January
- 1 May
- Ascension Day
- Whit Monday
- 1 August.

## **TRIAL REMOVAL OF CLOSING AUCTION FOR PAN-EUROPEAN SECURITIES**

Following a request last year from the Kommission Wertpapiere ("KW") in Zurich that virt-x should consider removing the "auction pre-opening" period in respect of pan-European equities on virt-x, a trial removal will commence on Monday 10 April 2006. The trial has been set for 3 months but this may be extended or curtailed as appropriate during the trial period.

The trial removal will apply to pan-European order books only (not to SMI/Swiss securities or ETFs). During the trial, these securities will close at 17:30 CET unless a Stop trading occurs between 17:25:01 and 17:30:00.

In the event of a Stop trading in that period, the security will close immediately following the 5 minute Stop Trading period and all matchable orders will be executed.

virt-x will monitor for increased risk of attempted market manipulation due to the removal of the two- minute randomised closing period and we will halt or amend the trial at any time if we have concerns on this or any other regulatory implication arising from the trial.

**We are keen to receive members' feedback during the trial. Please send your comments to [regulation@virt-x.com](mailto:regulation@virt-x.com).**

## **TRADE REPORTING FAQ**

Q Which trading capacity code should be used where a member deals with a customer from a proprietary or house account?

A PR, reported from the member's perspective.

## **SWISS TARIFF CONTROLS**

virt-x requires the compliance department of users of the Swiss Tariff to hold on file documentation which shows that it is satisfied that its own firm has adequate internal controls to ensure on an ongoing basis the accurate identification of trade capacity to virt-x.

The absence of adequate documentation will be treated as grounds in its own right for refusing the member the right to the use of the Swiss Tariff. virt-x will ask for copies of this documentation from time to time to confirm the adequacy of these arrangements.

Swiss Tariff users should therefore ensure that they have on file documentation which covers:

- segregation of principal and agent trading
- accuracy of flagging
- general control points

Questions which virt-x expects to be addressed with regard to each of these categories are set out below.

### **Segregation of principal and agent trading**

- The member's definitions of principal and agent and how these reconcile for reporting purposes with virt-x's definitions in Directive 9 (Fees) which states:

Principal trade	A trade where the member is trading for its own account, i.e. the member is taking price risk, and is <b>not</b> acting either in an agency capacity on behalf of its client or as principal for its customer (e.g. a Riskless principal trade)
Agent trade	Any trade which is not a Principal trade

- How does the member segregate client and principal trading?
- How are the member's internal trading codes matched to virt-x's PR, AG, CU codes?

### Accuracy of flagging

For flags which are set automatically by the member's systems:

- Who authorises set-up defaults (trader/trading books)?
- What controls are in place to ensure accuracy?
- Who reviews changes to flagging defaults and who authorises them?
- What checks are made to confirm accuracy and how frequent are these?
- Can flags be overridden (and, if so, by whom)?
- What happens if an error is identified?

For flags which are set manually:

- Who decides what flag to use?
- What controls and procedures exist to ensure flagging is accurate?
- Who reviews this activity and how often?
- What happens if an error is identified?
- Who is authorised to amend flags?
- Who authorises set-up / changes to defaults?
- What other checks are made to confirm accuracy? (by whom and how frequently?)

### General control points

- What happens if a trader changes role?
- What other security measures are in place (eg passwords)?
- Have the controls / procedures been tested by internal or external audit? If yes, please be prepared to provide virt-x with a summary of the results
- If the controls / procedures have not been tested by internal or external audit, what other tests have been carried out and what was the outcome?
- Have the member's controls over its use of the Swiss Tariff been signed off by the firm's head of compliance?

## **SHORT SELLING**

The FSA have recently carried out a review of short selling as a follow-up from the FSA's Discussion Paper on Short Selling in October 2002.

The FSA's view remains that short selling is a legitimate investment activity which plays an important role in supporting efficient markets. The FSA recognise, however, that short selling also may pose risks to the market including contributing to the potential for disorderly trading, increasing the possibility of short term price volatility, being used in manipulative trading strategies and leading to settlement disruption. This may arise particularly in less liquid stocks.

virt-x has agreed to issue a market status message to members when virt-x becomes aware of securities experiencing a significant proportion of settlement failures. The intention of these messages is to notify the market of building settlement problems and thereby reduce the potential risk of a disorderly market.

## **TOPICS FOR FUTURE COMPLIANCE NEWSLETTERS**

We welcome topics for inclusion in future issues of the compliance newsletter. Please contact us with suggestions. Thank you!

**Please address any comments/questions/suggestions to**  
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