



London
Stock Exchange

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

N07/12

STOCK EXCHANGE NOTICE

Consultation on proposed rule amendments - Obligations of member firms to market makers in quote-driven securities

Introduction

1. The London Stock Exchange (“the Exchange”) proposes to amend the obligations of member firms trading on Exchange in quote-driven securities as set out in the Rules of the London Stock Exchange (“the rules”). The proposed amendment seeks to introduce new rules (and guidance) which specify that a member firm shall not execute a trade on Exchange in a quote-driven security which is on terms that are less favourable than the firm quotes in that security on the SETSqx and SEAQ trading services (“quote-driven”).

Background

2. The proposed rule change is intended to ensure an efficient price formation process in quote-driven securities whereby trades executed off order book that are subsequently trade reported to the Exchange are done so with reference to the displayed firm quotes. The proposals for quote-driven securities are consistent with the principle of the existing negotiated trade waiver arrangements which require member firms to ensure that when bringing an off order book trade in an EU regulated market security on Exchange, the terms of that trade are no worse than those which could have been achieved on the relevant Exchange trading service.
3. Currently, when challenged by a member firm in a quote-driven security, other than another market maker in that security, a market maker is obliged under the rules to deal at its displayed price and in any size up to that displayed in its firm quote. As there is no explicit requirement to refer to the displayed price on SETSqx and SEAQ, this could potentially result in trades being reported to the Exchange that are on worse terms than those that could have been obtained from another market maker registered in that quote-driven security.

Proposed changes to the rules

4. The Exchange proposes to amend the rules to remove any inconsistencies on the pricing of an on Exchange trade executed on the quote-driven trading services. Irrespective of whether the member firm concerned is a market maker, or whether the security concerned is an EU regulated market security, when conducting an off order book trade in a quote driven security, all member firms will be required to consider the firm quotes displayed by each registered market maker before concluding and reporting that trade to the Exchange. A member firm should not execute a trade on Exchange which is on terms that are worse than any of the individual firm quotes available on the relevant quote-driven trading service. This obligation will extend across all securities available on the SETSqx and SEAQ trading services. The new rule does not apply to member firms trading on order driven services such as SETS as market makers are not obliged to trade off order book at their displayed price and size.
5. A new exception is being created to relieve market makers in quote-driven securities of the obligation to actively offer to buy or sell at their displayed price and in any size up to that displayed in their quote where to do so would cause a breach of the proposed rule.
6. Where the Exchange becomes aware of trades conducted outside of the best quoted bid and offer available on the SETSqx and SEAQ trading services, it will reserve the right to contact either counterparty to obtain confirmation that the trade has been executed in accordance with the proposed rule. This proposed amendment will have no impact on trades reported using OTC trade types which are identified as being off Exchange and therefore not subject to the rules.

Rules consultation

7. The Exchange is consulting on the rules changes set out in Attachment 1 for a period of four weeks. Interested parties are therefore asked to provide any comments or feedback on this consultation and any other aspects of the current market maker quote-driven securities rules that they believe are relevant by 4 April 2012.
8. Any comments or queries regarding the content of the proposed rule amendments should be addressed to Nisha Patel, UK Regulation, telephone +44 (0)20 7797 3130 (STX 33130) or email: npatel@londonstockexchange.com
9. Any comments or queries regarding market making should be addressed to Ian-Patrick Lauder, telephone +44 (0)20 7797 4355 (STX 34355) or email: ilauder@londonstockexchange.com

Denzil Jenkins

Head of Compliance and Regulation

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