London STOCK EXCHANGE

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

N23/08

STOCK EXCHANGE NOTICE

PROPOSED RULE CHANGES TO ALLOW THE EXCHANGE TO ENFORCE THE CANCELLATION OF AUTOMATED TRADES

Introduction

1. The London Stock Exchange ("the Exchange") proposes to amend the Rules of the London Stock Exchange ("the rules") and provide new guidance under which it will consider, in exceptional circumstances, cancelling automated trades executed on TradElect®. The Exchange invites interested parties to comment on the proposed changes, which are set out in the Attachments.

Background

2. The Exchange periodically receives requests to cancel automated trades and has, very occasionally, used its general decision-making power to do so. The Exchange believes it would be more appropriate to have specific rules to allow for this, in the interests of transparency, consistency and fairness.

3. The Exchange proposes that such cancellations be termed "Exchange enforced cancellations". These cancellations may result from a request from a member firm that is party to the trade in question or be initiated unilaterally by the Exchange. An Exchange enforced cancellation differs from a contra, which is a trade that is equal and opposite to a previous trade in the same security and must be agreed by both parties to the original trade. By contrast, the decision to undertake an Exchange enforced cancellation rests solely with the Exchange.

Significant changes to the rules

4. The Exchange's rules state that all trades undertaken on Exchange are firm. The Exchange does not intend to change that overarching principle. However the rules have been changed to reflect that the Exchange may consider cancelling automated trades in exceptional circumstances.

5. The term “Exchange enforced cancellation” has been added to the Definitions section of the rules and the term “contra” has been amended to distinguish it clearly from an Exchange enforced cancellation. All references to the term “reversal” have been removed and replaced with “Exchange enforced cancellation” or “contra” as appropriate, for ease of understanding.

6. The existing rule relating to reversal of erroneous trades for covered warrants has been widened so it covers cancellations for all instruments that can be executed automatically on TradElect®. As the rule is no longer specific to covered warrants, guidance related to the different security types has been added, as has generic guidance relating to all Exchange enforced cancellations.

7. Member firms will note that there is a significant difference between the financial thresholds at which the Exchange will consider a cancellation for a covered warrant and a cancellation in any other security. The thresholds for covered warrants remain the same as those already in the rules and reflect the fact that a precise theoretical value can be calculated for a covered warrant. As a result, it is easier to identify when an erroneous trade has occurred and a cancellation is warranted.

8. However, precise theoretical values cannot be established for most other securities that can be automatically executed on TradElect®. As a result, for securities other than covered warrants the Exchange proposes to introduce a minimum potential loss threshold of £200,000 for a firm, resulting from a trade or group of related trades, before it will consider a request for cancellation. This threshold will not apply to a cancellation that is initiated unilaterally by the Exchange.

9. The Guidance to the rules gives an explanation of the process for requesting an Exchange enforced cancellation and an indication of some of the situations in which the Exchange will consider cancelling an automated trade. In deciding whether to cancel a trade the Exchange will generally have regard to matters such as the time elapsed since the trade, the overall potential loss to the firm involved, the evidence to prove the erroneous nature of the trade, and the market impact of the proposed cancellation.

10. As noted above, the proposed policy is limited to trades automatically executed on TradElect®. However, the Exchange welcomes feedback on whether the proposed policy could be extended to off book trades and how a process for cancelling off book trades might work in practice.

Rules consultation

11. The Exchange is consulting on the rules changes set out in the Attachment for a period of four weeks. Reviewers are therefore asked to provide any comments or feedback on this consultation by 31 October 2008.

12. Any comments or queries on this Notice should be addressed to Tim Rowe, Trading Services, telephone +44 20 7797 3468 (STX 33468) email:

trowe@londonstockexchange.com.

Nick Bayley
Head of Trading Services

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http://www.londonstockexchange.com/en-gb/products/membershiptrading/rulesreg/stockexnotices/stockexchangenotices2008.htm