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Circular FSMA\_2012\_12 of 20/06/2012

## ESMA Guidelines on systems and controls in an automated trading environment for trading platforms, investment firms and competent authorities

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### **Scope:**

In Belgium, these guidelines affect the following undertakings:

- market operators governed by Belgian law that operate a regulated market or MTF;
- investment firms governed by Belgian law, including those that operate an MTF in Belgium;
- credit institutions governed by Belgian law, provided they offer investment services;
- branches in Belgium of investment firms governed by the law of States outside the European Economic Area;
- investment firms governed by the law of States outside the European Economic Area and that have expressed their intention to offer investment services in Belgium under the free provision of services;
- branches in Belgium of credit institutions governed by the law of States outside the European Economic Area, provided they offer investment services,

where these undertakings:

- operate an electronic trading system, or
- use an electronic trading system, including a trading algorithm, for dealing on own account or for the execution of orders on behalf of clients, or
- provide direct market access or sponsored access as part of the service of the execution of orders on behalf of clients.

### **Summary/Objective:**

This circular concerns the guidelines issued by ESMA on the systems and controls in an automated trading environment for trading platforms, investment firms and competent authorities.

These guidelines set out ESMA's view of how European Union law should be applied in this area and of appropriate supervisory practices within the European System for Financial Supervision (ESFS). ESMA therefore expects all relevant competent authorities and financial market participants to comply with these guidelines unless otherwise stated.

These guidelines cover:

- a. the operation of an electronic trading system by a regulated market or a multilateral trading facility;
- b. the use of an electronic trading system, including a trading algorithm, by an investment firm for dealing on 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

execution of orders on behalf of clients.

Both trading platforms and investment firms (as well as credit institutions, provided they offer investment services) must, in the internal governance measures they adopt in compliance with these guidelines, take into consideration the nature, scope and complexity of their activities.

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Dear Sir or Madam,

Article 16 of Regulation (EU) No 1095/2010 provides that ESMA shall, with a view to establishing consistent, efficient and effective supervisory practices within the ESFS (European System for Financial Supervision) and to ensuring the common, uniform and consistent application of Union law, issue guidelines addressed to competent authorities or financial market participants. Furthermore, this article stipulates that competent authorities and financial market participants shall make every effort to comply with those guidelines.

In this context, on 22 December 2011, ESMA issued guidelines on the *systems and controls in an automated trading environment for trading platforms, investment firms and competent authorities*.

These guidelines are based on the Markets in Financial Instruments Directive (MiFID, 2004/39/EC) and on the Market Abuse Directive (2003/6/EC) and their respective implementing directives (2006/73/EC and 2004/72/EC). They set out ESMA's view of how European Union law should be applied in the area of automated trading systems, including high-frequency trading (HFT).

The guidelines anticipate the future reviews of MiFID and the Market Abuse Directive. In light of recent events, the members of ESMA, including the FSMA, took the view that we cannot wait for those reviews but that it is desirable to clarify as of now the requirements that market participants are expected to meet in the existing automated trading environment.

### **Scope of the guidelines**

These guidelines cover the following matters in particular:

- the operation of an electronic trading system by a regulated market or a multilateral trading facility (MTF);
- the use of an electronic trading system, including a trading algorithm, by an investment firm for dealing on own account or for the execution of orders on behalf of clients; and
- 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.

Both trading platforms and investment firms (as well as those credit institutions that offer investment services) must, in the internal governance measures they adopt in compliance with these guidelines, take into consideration the nature, scope and complexity of their activities.

References in the guidelines to investment firms relate to investment firms (and credit institutions) where they execute orders on behalf of clients and/or for own account in an automated trading environment. An investment firm or a credit institution that operates a multilateral trading facility falls under the guidelines concerning trading platforms.

ESMA includes within the scope of electronic trading systems used by investment firms (and credit institutions) electronic systems for sending orders to trading platforms (whether or not orders from clients are submitted electronically to the investment firm or credit institution) and electronic systems which automatically generate orders, i.e. trading algorithms. Smart order routers may be part of a firm's systems to send orders to trading platforms. For purposes of these guidelines, ESMA covers smart order routers only from the perspective of the risks involved in order entry and not, for example, in relation to best execution.

The guidelines also have implications for firms that sell electronic trading systems to market operators, investment firms or credit institutions, or act as the outsourced providers of such systems, or provide connectivity services to investment firms or credit institutions for accessing trading platforms. Such firms will be subject to trading platforms' and investment firms' obligations, under these guidelines, relating to their electronic trading systems.

The guidelines also apply to firms exempt from MiFID that trade on own account and access trading platforms directly as members, participants or users, or via direct market access (DMA) or sponsored access (SA).

These guidelines are not limited to trading in shares, but cover trading in any financial instrument (as defined in MiFID) in an automated environment.

### **Structure of the 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

### **Application in Belgium**

In Belgium, these guidelines apply to the following undertakings:

- market operators governed by Belgian law that operate a regulated market or MTF;
- investment firms governed by Belgian law, including those that operate an MTF in Belgium;
- credit institutions governed by Belgian law, provided they offer investment services;
- branches in Belgium of investment firms governed by the law of States outside the European Economic Area;
- investment firms governed by the law of States outside the European Economic Area and that have expressed their intention to offer investment services in Belgium under the free provision of services;
- branches in Belgium of credit institutions governed by the law of States outside the European Economic Area, provided they offer investment services,

where these undertakings:

- operate an electronic trading system, or
- use an electronic trading system, including a trading algorithm, for dealing on own account or for the execution of orders on behalf of clients, or
- provide direct market access or sponsored access as part of the service of the execution of orders on behalf of clients.

These guidelines are intended to ensure the proper operation and integrity of the market. They set out the expectations of the European competent authorities as regards systems and controls in an automated environment in order to guarantee an appropriate, shared, uniform and consistent application of these provisions by the undertakings to which they are addressed.

As part of its competencies in the area of the proper operation and integrity of the markets, the FSMA shall assess the application of these guidelines and invites the undertakings addressed to examine their internal procedures and systems as quickly as possible in the light of these guidelines and, where necessary, to adjust them.

As provided for by the ESMA guidelines on systems and controls in an automated trading environment for trading platforms, investment firms and competent authorities, the FSMA is obliged to integrate these guidelines into its supervisory practices as from 1 month after their publication on its website.

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For questions relating to this circular and the attached guidelines, please contact us at the following e-mail address: [ESMA-guidelines@fsma.be](mailto:ESMA-guidelines@fsma.be). The FSMA's services will do their very best to answer your questions as soon as possible.

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Sincerely yours,

The Chairman,

Jean-Paul SERVAIS

*Annex: [FSMA\\_2012\\_12-1 / ESMA Guidelines on "Systems and controls in an automated trading environment for trading platforms, investment firms and competent authorities" \(ESMA/2012/122-EN\)](#).*