



**Report of the Secretary General**  
**on the**  
**Resolution on Principles for the Oversight of**  
**Screen-Based Trading Systems for**  
**Derivative Products**

September 1991

## **Resolution on Principles for the Oversight of Screen-Based Trading Systems for Derivative Products**

At its Santiago, Chile November 12-15, 1990 meeting the Presidents Committee approved a Resolution on Principles for the Oversight of Screen-Based Trading Systems for Derivative Products which is presented in Appendix. This resolution recommended that the members adopt the principles included in the Resolution which identify areas of common regulatory concern. In that regard, it was understood that individual jurisdictions would take account of differences in national legal standards, regulatory policies, and market custom or practice in addressing these concerns.

On January 17, 1991, the General Secretariat sent to all the members of IOSCO a letter inquiring on the action taken with respect to the above mentioned Resolution. Replies have, as of the date of this report, been provided by 22 members. A summary of the replies follows:

**1. Australian Stock Exchange Limited - Australia (affiliate member)**

Has not yet adopted the Principles but can see no barrier to their acceptance and is comfortable with their general nature. Formal adoption of the Principles would however require full exposure to and input from a range of advisory groups and market participants.

**2. Sydney Futures Exchange Limited - Australia (affiliate member)**

Indicates its acceptance and adoption of the Principles in so far as they concern its role as a systems sponsor and a self-regulatory organization. Indicates that the Principles are being applied in relation to its SYCOM screen-based trading systems.

**3. Vienna Stock Exchange - Austria (regular member)**

An option or future exchange does not presently exist in Austria. The Principles are however being evaluated as there is a project to launch an option future exchange sometime during 1991.

**4. Commission bancaire et financière - Belgium (regular member)**

The principles are being considered as the CBF is currently in the process of reflecting on the establishment of a regulatory framework for derivative products.

**5. Investment Dealers Association of Canada (affiliate member)**

Indicates that the IDA currently has no responsibility for the oversight of any screen-based trading systems for derivative products but does not disagree with any of the Principles.

**6. Superintendencia de Valores y Seguros of Chile (regular member)**

Screen-based trading systems for derivative products do not presently exist in Chile. If such systems are eventually set up the Superintendencia indicates that it will adopt the Principles. Similar principles for other currently operational screen-based trading systems have already been adopted.

**7. Commissione Nazionale per le Società e la Borsa - Italy (regular member)**

Screen-based trading systems for derivative products do not presently exist in Italy. The CONSOB is however authorized by law to issue regulation concerning the operation of such systems. The Principles could therefore be implemented through the adoption of corresponding regulation. Indicates that it will inform the General Secretariat if and when it does so.

**8. Securities and Exchange Commission of Korea (regular member)**

Screen-based trading systems for derivative products do not presently exist in Korea. Indicates that if such systems are eventually set up and if SEC obtains jurisdiction over their operations, it will examine the Principles with a view of possibly adopting them.



9. **Kredit Tilsynet - Norway** (regular member)

Existing screen-based system does not have a trading function but only an information function. Indicates that the Principles have not been adopted as such but are implemented, as much as they relate to the existing system, through the present body of regulation and practices.

10. **Securities and Exchange Commission of the Philippines** (regular member)

Screen-based trading systems for derivative products do not presently exist in the Republic of the Philippines. Indicates that it will implement the Principles when the setting-up of such systems is considered.

11. **Commission des valeurs mobilières du Québec** (regular member)

The CVMQ indicates that the eventual adoption of the Principles as such is in the interest of all market participants. Meanwhile the Commission indicates that the Principles are in fact implemented through the existing regulation.

12. **Monetary Authority of Singapore** (regular member)

Screen-based trading systems for derivative products do not presently exist in Singapore. The Principles are presently the object of a detailed evaluation although MAS expresses general support for them.

13. **Association of Swiss Exchanges - Switzerland** (regular member)

Under the present Swiss legislation, standardized derivative products are traded at SOFFEX (Swiss Options and Financial Futures Exchange), which is not submitted to any federal or cantonal law. SOFFEX is a privately organized and exclusively self-regulated exchange having rules and regulations which however compare favourably with markets in governmentally regulated jurisdictions. Given the above mentioned regulatory situation and the fact that in Switzerland "system sponsor" and "relevant regulatory authority" are identical, the Principles are fully met, where applicable, by SOFFEX.

- 14. Securities and Investments Board of the United Kingdom** (regular member)

Has endorsed the Principles and has publicly issued them in the form of a Guidance Release (Release No. 2/91 issued in April 1991).
- 15. International Stock Exchange of the United Kingdom and the Republic of Ireland Limited** (affiliate member)

Resolution on the Principles for the Oversight of Screen-Based Trading Systems for Derivative Products is under consideration.
- 16. Investment Management Regulatory Organization Limited - United Kingdom** (affiliate member)

Indicates that it is not responsible for the regulation of trading systems.
- 17. The Securities and Futures Authority - United Kingdom** (affiliate member)

Resolution on the Principles for the Oversight of Screen-Based Trading Systems for Derivative Products is under consideration.
- 18. Commodity Futures Trading Commission of the United States of America** (associate member)

On November 15, 1990, the Commission adopted as a statement of regulatory policy the ten Principles for the Oversight of Screen-Based Trading Systems for Derivative Products formulated by Working Party No. 7 on Futures. The Commission adopted the Screen-Based Principles to serve as general policy goals that will guide the Commission in resolving regulatory issues arising from screen-based trading systems.
- 19. National Association of Securities Dealers, Inc. - United States of America** (affiliate member)

Indicates that at the present time, the NASD provides no system for the trading of standardized options or other categories of derivatives. Similarly, the proposed NASDAQ International Service is designed solely to support trading of equity securities by participating broker dealers. Given these circumstances, indicates that it would not be meaningful for the NASD to adopt the Principles

at the moment even though it supports their intent. If the NASD later determines to develop a screen-based system for derivatives, it would consider adoption of the Principles at that point. Indicates that it would welcome the opportunity to provide input on the formulation of suitable principles for the oversight of screen-based systems that support equities trading on a cross-border basis.

**20. North American Securities Administrators Association Inc. - United States of America** (associate member)

Has adopted at its April 20, 1991 annual meeting a resolution endorsing all the Principles.

**21. Commission of the European Communities** (affiliate member)

Has not yet contemplated developing legislation with respect to the oversight of screen-based trading systems for derivative products.

**22. Organization for Economic Co-Operation and Development** (affiliate member)

Will discuss the Principles within its Financial Markets Committee.





## **Appendix**





PRINCIPLES FOR THE OVERSIGHT OF  
SCREEN-BASED TRADING SYSTEMS

INTERNATIONAL ORGANIZATION  
OF  
SECURITIES COMMISSIONS  
REPORT OF THE TECHNICAL COMMITTEE

JUNE 1990



PRINCIPLES FOR THE OVERSIGHT  
OF SCREEN-BASED TRADING SYSTEMS  
FOR DERIVATIVE PRODUCTS

The regulatory authorities responsible for oversight of screen-based trading systems for derivative products <sup>1/</sup>, whether governmental, quasi-governmental, or private ("relevant regulatory authorities"), should articulate the jurisdictional interest and supervisory principles applicable to the organizations responsible for the system such as an exchange ("system sponsor"), the organization or organizations which provides or provide the hardware, software, and/or the communications network and related services ("system providers"), the persons authorized to execute transactions on the system such as a broker-dealer ("system users"), and persons with financial exposure to the system ("system customers"). These principles should reflect the shared objectives of ensuring that, among jurisdictions, the levels of investor protection and regulation are adequate. <sup>2/</sup>

To that end, it is suggested that jurisdictions adopt the following ten non-exclusive, general principles for the oversight of screen-based trading systems for derivative products which identify areas of common regulatory concern. It is understood that individual jurisdictions will take account of differences in national legal standards, regulatory policies, and market custom or practice in addressing these concerns.

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<sup>1/</sup> For purposes of these Principles, the term "derivative products" refers to those products in which the exchange or market ("market") itself is the issuer, which are subject to the rules of the issuing market, and for which a clearing organization is used to settle profits and losses, make deliveries, and guarantee cleared trades.

<sup>2/</sup> The Principles set out in broad terms regulatory considerations arising from cross-border screen-based trading, and not the specific concerns of some members in respect of the particular laws applying to their jurisdiction (e.g., those dealing with anticompetitive rules and practices, margin levels, or capital requirements).



1. The system sponsor should be able to demonstrate to the relevant regulatory authorities that the system meets and continues to meet applicable legal standards, regulatory policies, and/or market custom or practice where relevant.
2. The system should be designed to ensure the equitable availability of accurate and timely trade and quotation information to all system participants and the system sponsor should be able to describe to the relevant regulatory authorities the processing, prioritization, and display of quotations within the system.
3. The system sponsor should be able to describe to the relevant regulatory authorities the order execution algorithm used by the system, i.e., the set of rules governing the processing, including prioritization, and execution of orders.
4. From a technical perspective, the system should be designed to operate in a manner which is equitable to all market participants and any differences in treatment among classes of participants should be identified.
5. Before implementation, and on a periodic basis thereafter, the system and system interfaces should be subject to an objective risk assessment to identify vulnerabilities (e.g., the risk of unauthorized access, internal failures, human errors, attacks, and natural catastrophes) which may exist in the system design, development, or implementation.
6. Procedures should be established to ensure the competence, integrity, and authority of system users, to ensure that system users are adequately supervised, and that access to the system is not arbitrarily or discriminatorily denied.
7. The relevant regulatory authorities and the system sponsor should consider any additional risk management exposures pertinent to the system, including those arising from interaction with related financial systems.
8. Mechanisms should be in place to ensure that the information necessary to conduct adequate surveillance of the system for supervisory and enforcement purposes is available to the system sponsor and the relevant regulatory authorities on a timely basis.
9. The relevant regulatory authorities and/or the system sponsor should ensure that system users and system customers are adequately informed of the significant risks particular to trading through the system. The liability of the system sponsor, and/or the system providers to system users and system customers should be described, especially any agreements that seek to vary the allocation of losses that otherwise would result by operation of law.
10. Procedures should be developed to ensure that the system sponsor, system providers, and system users are aware of and will be responsive to the directives and concerns of relevant regulatory authorities.