

## COMMENTS ON NOREX JOINT RULE BOOK

The following comments has been made in meetings with members of the securities dealers associations in Denmark, Iceland, Norway and Sweden here for convenience called DINS.

### Norex Member Rules

1. So far Norex has only completed a certain part – that regards trading of equities - of the final Norex Member Rules (NMR) apart from some general provisions regarding equity derivatives, see section 3.2 and 5. Norex has declared that all the present rules and membership agreements for users of the SAXESS and Click trading systems shall be substituted by a one-page agreement accompanied by a confirmation to comply with NMR. DINS believe that it will not be possible to introduce the NMR step by step in the way Norex has planned. The reason is that the current membership agreement and rules will not be entirely substituted as long as NMR is not developed to an extent that it covers all of the present agreements. Conflicts between the present agreements and NMR will be unavoidable if NMR is introduced at the present stage

Thus, DINS recommend that all of the planned NMR be developed in its full extent before any substitution of present membership agreements and rules is undertaken.

If on the contrary NOREX introduces the NMR in several steps, the provisions in each step should be referring only to what is aimed to be covered by that particular step. As an example, in the proposal the concepts of Clearing and Clearing Systems are mentioned even though no specific provisions yet are presented regarding trading of derivatives to which the feature of clearing is connected. All references to “clearing” and “clearingsystems” must therefore be deleted.

In any case NMR should not be operational until all membership agreements and rules connected with the SAXESS system can be substituted completely.

2. In section 3.1.4 in NMR should be stated that the securities dealers associations or the corresponding member organisations should be entitled to call for consultations in respect of any supplement or amendment. (This issue has been addressed in the Norex letter to member organisations 2000-11-22 to which reference is made)

DINS hereby propose a scheme for the handling of any supplement or amendment not only to the NMR but to technical changes of the NOREX systems as well. Thus DINS suggest the following regulation.

Within 14 days from NOREX notifying the securities dealers associations or the corresponding member organisations of any amendments, changes or supplements of the NMR or the technical systems, the organisations should be entitled to call for consultations with NOREX and such consultations should take place, if not otherwise agreed, within 14 days from the call.

Amendments, changes or supplements of the NMR should enter into effect no earlier than 14 days after consultations have been concluded.

Amendments, changes or supplements of the technical systems that are mandatory for the Norex members should be preceded by an adjustment period of at least 6 months including at least 1 month of testing in a stable environment followed by 3 weeks for getting the changes into operation. (The reason is that today most members use third party software providers. From the date Norex announce a mandatory system adjustments by specified protocol amendments, the third party needs 2 months of development and 1 month of testing before they can provide the member the prerequisites for their development and testing, activities that consume another 3 months of development and testing and getting into operation.)

Amendments, changes or supplements of the technical systems that are not mandatory for the Norex members should be notified at least 1 month in advance.

3. In section 3.1.5 it is said that the Norex Exchange(s) “are entitled to assign all rights...”. It is a bit unclear whether this refers to all exchanges as a whole or to what each individual exchange can do, i.e. in connection with cooperation/merger with other exchanges.

In other sections of NMR the wording “The Norex Exchange(s)” is used, but it can sometimes be a bit unclear whether the reference is made to all exchanges or an individual exchange. For instance in section 3.2.7 regarding testing it is said that the Norex Exchange(s) “are entitled ..... to test..” To DINS it is unclear who is going to do the testing. See also similar problems regarding i.e. notifications (section 3.2.7 to 3.2.13, 3.2.16, 3.2.20, 3.2.23, 3.4.6, 4.2.1, 4.4.4 and 4.9.2) In DINS opinion the members obligations relates to the particular exchange at which the member has its membership. This should be made clearer in the NMR.

4. In section 3.2 or adjacent to section 3.8 should be stated the obligations the Norex Exchange takes on to deliver agreed services to its members and what should be the penalty for not doing so. DINS request that NOREX Exchanges takes on specified responsibility at least for the following:

- information with due notice about changes of the prerequisites for trading like trading halts/suspension, restart of the trading after interruption etc
- information with due notice about corporate actions that affect trading e.g. the ex day for dividends and other rights, when an issue is splitted and all other corporate actions undertaken that affect the trading
- guaranty of accessibility according to official trading hours, i.e. commitment for a specified up-time of the system for a certain period (month/year)

- guaranty of response time in Norex internal system and in the network communication to the members premises

The parameters involved in the above mentioned provisions should be comparable with the best international standard and have to be negotiated with securities dealers associations or the corresponding member organisations and set up for a certain time period.

DINS request that the NMR regarding specifications of technical provisions and the exchanges obligations should be at least of the same level as in the present Norwegian membership agreement.

The penalty for any breach by Norex Exchange/s of their obligations should be expressed in monetary terms, e.g. a certain reduction of transaction fees.

5. In section 3.2.2. it is stated that the members have to enter into a network agreement with a third party assigned by Norex. This provision should be altered so that Norex takes full responsibility for the network all the way to the member's premises. If, for reasons dictated by the network provider, the member has to enter into an agreement with the provider it should anyhow be clarified that NOREX takes on responsibility against the members for the monitoring and surveillance of the net-work communication between the exchange and the members router or corresponding access point. Reference is made to OBSE Standard medlemsavtale for borsmedlemmer ved Oslo Bors, Vedlegg IV.

In section 3.2.2 first paragraph it should be stated that changes regarding communication networks, i.e. change of suppliers, are subject to the same consultation-process as mentioned above

DINS also recommend that the NMR under security (section 3.2.15 and 3.2.16) regulates the obligations of the exchanges, see the Norwegian regulation in section 26.1 with annex III.

6. In section 3.3.1 should be indicated certain limits of the Norex entitlement to use the information provided by the member and customer placements in the trading (and clearing, the wording to be deleted see point 1) system for the purpose of its activities. The exchanges rights can not be "exclusive" because each individual member also have a right to use their "own" information. In this connection the Norwegian regulation in section 7.1-3 will be more acceptable. DINS are of the opinion that only trade-related information that is in compliance with national provisions for dissemination of trade information and additional information beyond this restriction not revealing any information referring to a specified member might be used for the purpose of Norex Exchange/s activities.

7. In section 3.3.2-second paragraph, in addition to the internal user categories mentioned in NMR, should also be analysts, corporate finance employees and personnel receiving clients orders in banks local branch offices. See the corresponding Norwegian regulation section 7.2.

It is also stated that the member should keep a log on all internal users of Norex systems. DINS find this is too far reaching and that a log only is needed for those persons that have got an user-id. Other users i.e. users of information from Norex systems only, e.g. employees in a banks local branch office should not be necessarily logged if they are not registering anything into the system.

Pursuant to section 3.3.2 only the member's internal users may use information from the trading and clearing systems. Internal users are generally defined as employees that are directly associated with trading in Instruments.

In addition it should be stated that fees for information from the Norex Exchanges should not be debited for internal users.

8. In section 3.3.3 should be stated that market information older than 15 minutes may be freely disseminated. Furthermore, section 3.3.3 refers to section 3.4.2. which seems to be a mistake. It probably should have been a reference to section 3.3.2 instead.

9. In section 3.3.5 is stated that Norex Exchange or some other entity outside the member may determine from which point of connection to the trading system the member may disseminate information. DINS oppose to this provision but confirm that an agreement may be made for this in which the point of connection may be specified.

10. In section 3.4 several provisions regarding intellectual property rights seems to be more restrictive for the members compared with the Click rules of today (section 1.17.1 –2). DINS suggest the wording in the first sentence of section 3.4.2 ... to any alterations or modifications thereof ... should be deleted and substituted by a clarification on the previous line ... and all other documents *produced from time to time by the Norex Exchange(s)* ...

11. In section 3.4.3 and 3.4.4 are some provisions made that should be clarified according to the following principles:

- members explicit usage of Norex trademarks as signs for own products or services should only be permitted when there is a direct connection with Norex trademarks or intellectual properties. The member should enter into separate agreements with Norex about that usage
- members may freely market products and services not using Norex trademarks as signs for own products or services in spite of the member in its product specification may refer to e.g. an index calculated by a Norex company. In this case the member should not be required to enter into separate agreements with Norex about that usage.

12. In section 3.4.6 the second last sentence should be deleted as this is a far-reaching requirement on the member. The whole section 3.4.6 is quite unclear and should be rewritten for better clarity. This section seems to be a translation of the Norwegian section 33 fourth subsection, but the translation does not seem to be in accordance with the Norwegian text (see especially the two last sentences).

13. In section 3.6.1 the exchange(s) can use certain measures if circumstances occurs that “in the opinion of the Norex Exchange(s), affects the Norex Exchange(s)’ ability to maintain a well-functioning trading and clearing operations”. The word “affects” seems to us to less strict when we look at the different measures that the exchange(s) can implement. The measures mentioned in subsections (v – viii) are relatively radical and it is our opinion that such measures should only be taken when there are serious problems. It is also unclear what is meant by “contracts” in subsection (viii).

14. In section 3.6.3 - 5 the percentages mentioned should refer to a compound figure of both the trading volume and the number of trades in order to capture the various types of member institutes, e.g. banks, securities companies etc, who might have differences in their order structure. Reference is made here to the new rule at OMSE from May 2000.

It should also be declared in NMR that when the new feature of partitioning national markets and submarkets has been put in operation the interruption of trading in one partition should not have any effect on other partitions.

15. Section 3.6.6 should be modified ...to be down when *an essential part* (all) of the Member’s electronic connections ... are down. The reason for the suggested alteration is that it is unrealistic to assume for instance that a bank with a huge flow of small orders should be forced to handle those orders in a manual way through only one work station if that is the only connection left intact.

16. Sections 3.6.10 –12 NMR contains regulation regarding extension of trading in case of interruptions of the trading session. These sections ought to have a provision clearly stipulating a procedure on how the markets will be informed in the case of extension of trading after interruptions that have occurred. Furthermore, it should be explained what a member has to do to fulfil the requirement to notify its customers in respect of “extraordinary measures” as stipulated in section 3.6.11. In addition the wording should be rewritten as follows “Where the Norex Exchange(s) has *either* suspended trading *regardless of duration* or delayed the opening of trading for more than 1 hour...”

17. In section 3.7.4 the words “or anticipated should be deleted, because it is impossible for a member to comply with such requirement

18. In section 3.8.6 is said that the exchanges shall “in no circumstances” be liable for losses that arises as a consequence of the implementation of extraordinary measures, reference to section 3.6. This is too far reaching and not acceptable, see in this connection our comments under section 12 above.

19. In section 3.8.6 further restrictions of the liability for Norex Exchange(s) are made pursuant to section 3.6 Extraordinary measures. DINS are of the opinion that this should not be the case. On the contrary the Norex Exchange(s) should take on the same liability under circumstances where extraordinary measures are called for, as it should under normal conditions. It is stipulated in section 4.2.1 that a member at one Norex exchange may, upon application, become a member of another Norex exchange without further evaluation. DINS are of the

opinion that this provision is of great importance for the success of the NOREX. But there are differences in national legislation as well in membership rules applied by a local exchange regarding specific membership requirements, i.e regarding capital requirements and request for authorisation of investment firms. DINS are of the opinion that no Exchange can apply less strict requirements on members than the other exchanges and therefore the different requirements has to be harmonised.

National comments:

CSE cannot accept a remote member which is a member at another Norex exchange, without further evaluation due to the fact that in accordance with the Danish Act on Security Trading Finanstilsynet has to approve all undertakings who wish to become a remote member of CSE and who is not established in EU/EES.

Sweden can not accept members with capital less than € 1 mill and that a member must be an authorised investment firm.

Provisions in 4.2.5 should be rewritten to the following wording "Other parties than investment firms may not become Member at the Norex Exchange(s) [full stop]."

20. Referring to provision 4.2.7 it should also be stated that each user entitled to enter registrations into the system should have an individual user-ID for the purpose of surveillance. This provision suggested should also be reflected in the list of definitions under User-ID.

21. Referring to provision 4.2.7 the last sentence and 5.1.4.3, DINS are not in favour of any marking of order with characteristics like owner category or whether the order regards purchase of sale of an issuer's own Equities.

One of the reasons for not marking an order with owner category is that it is very difficult to get this marking of orders correctly done. In particular this will be the case when a mixed order i.e. on behalf of a client and for the member's own account is considered. Another reason is that DINS are not in favour of a full disclosure of the purpose of a specific order by any indication of for who's account the order is registered, see section 5.1.4.3. The reason is that the Exchange by this disclosure will get redundant information regarding varying purposes of an order in an unwarranted way.

DINS suggest instead a provision that forbid the member to place orders for the purpose of matching with each other by purpose, see also the provision in section 4.6.2,-second indent. However, if the member enters a pair of buy and a sell orders that are matched in the automatic matching system that match is by definition made coincidentally and therefore can not be questioned.

National comment: Referring to the case where the order regards purchase of sale of an issuer's own Equities, this is currently only regulated by law in Sweden. However the reporting of such transactions may be made after the

transaction has been executed and does not need a special marking of the order when entered.

22. In section 4.4.2 it says that: "The Member's exchange Traders shall be responsible for every entry placed in the trading- and Clearing Systems." In accordance with our principle viewpoint this sentence should be deleted. The responsibility lies with the member and not the individual traders, as it is said in the first sentence.

23. In section 4.4.4 it says that each trader "is assigned a personal user ID and password". Who's doing this? The responsibility for giving ID's and password should lie with the member and not the exchange. This mainly because the member need to have control over all ID's and passwords.

24. Section 4.6.3 in NMR grants the NOREX Exchange(s) a right to cancel orders and trades under certain conditions. First of all DINS suggest a clear separation of the provisions for cancellation of order and cancellation of trades referring to the different implications such cancellations might have. DINS are not in favour of any entitlement to the exchanges to cancel either orders or trades

National comment:

Sweden: The cancellation of an order not in line with the requirements stated in 4.6.1-2 might be undertaken in the way prescribed in section 4.6.3, i.e. without the consent of the member concerned but *only during the opening session*. During continuous trading the cancellation should be done only with the members consent.

When it regards a trade it may only be cancelled by the Norex Exchange(s) on request of a member and without the consent of the counterparty under very severe circumstances

Furthermore In Sweden OMSE and SSSA has discussed to introduce some kind of scale of acceptable spread-with for the judgement of proper order prices (5-15% wider than the prevailing spread on the market). This has been initiated by a request from Finansinspektionen in regard of automatic order routing regulation and is covered by the agreement with clients. If an order is out of the suggested accepted spread it should be reverted by the Norex Exchange(s) to the member for judgement by a broker. He can accept or cancel the order and the client should always be kept informed. See also provisions in section 4.9.10

Such rules might be used as a guideline for the Norex Exchange(s) to decide if a trade is obviously made at a wrong price or if it is not taking the current market conditions for the security concerned.

25. DINS have discussed in accordance with section 4.2.8 that Iceland may keep T+1 as their settlement cycle. This will contravene any arbitrage transactions within Norex markets if Icelandic securities are listed in parallel on other Norex Exchanges. However for the normal trading it should cause no problem that Iceland keep T+1. All the rest of Norex markets may in a few years time have to migrate from T+3 to T+1.

26. The sections 4.7 and 4.8 regulate trading halts and suspension. DINS are of the opinion that the NOREX exchanges should analyse in more detail how these measures are used in practice in each country. In this connection we underline that Norwegian and Swedish brokers are prohibited by law from trading under suspension, while the opposite seems to be the situation in Denmark. DINS are of the opinion that the different measures used should have the same consequences notwithstanding nationality.

DINS also find that the requirements in section 4.7.2 (ii and iii) differs from corresponding provisions in 4.8.5 though these particular provisions ought to be the same in case of trading halts and suspensions of trading.

27. In section 4.8 should be stated that it is the Primary Exchange, see definition, that decides suspension of trading to be followed by all other exchanges with a parallel listing of that security. It is of importance that the Primary Exchange has a confirmation in the agreement with the listed company of its status as Primary Exchange.

28. In section 4.9.2 it says that the use of automatic order routing “may be granted”. It is an open question whether members already using such systems have to make new applications or if they can go on under existing approval.

29. In section 4.9.5 is used the term “Head of Trading” (see also section 3.7.7) This term is not defined and therefore have no exact meaning. Can it be more than one person, and isn't it better to only use the term “contact person” – a term more precise to the actual function.

30. In section 4.9.9, subsection (i) it is stated that the agreement shall contain “the limits of the maximum risk ...” In our opinion it will also be sufficient if the agreements has as a condition that the member shall control the customers VP-accounts and make reservations of securities and money. We think that subsection (i) therefore need some rephrasing.

In subsection (iii) the phrase “which may entail substantial...” is very difficult to handle and it is also unnecessary, and should therefore be deleted. It should be enough to specify “specified conditions” in the agreement and what the member are entitled to do when these conditions occur.

It is stated in section 4.9.9, subsection (iv) that a Member who has the right to use Automatic Order Routing must have an agreement with the clients. The agreement must contain provisions, which gives the Member the right to cancel trades, which fail to meet the requirements concerning quality of pricing of orders and trades in section 4.6 and cancellation pursuant to section 5.1.9. See above under point 24.

National comment: DSDA has discussed whether it's possible from a legal point of view to have a provision that gives the Member a right to cancel a client's order or trade, if the client has not approved of the cancellation. In the opinion of DSDA, the exchanges, which are a part of the NOREX alliance, should evaluate

this problem carefully and involve the security dealer associations in this evaluation. See also above under point 24.

31. In section 4.9.11 are made provisions that might be most cumbersome to comply with for the members. They seem to DINS to be unwarranted as well to the Norex Exchange(s) need for surveillance. For example the provision (i), provision (iii), provision (iv), the last sentence, provision (v) and provision (ix) can not be accepted. National legislation seems to impose different requirements e.g. in number of years of saving information (iii).

32. NMR contains provisions in section 4.10 regulating Program Trading. As far as DINS are informed none of the NOREX Exchanges regulate Program Trading at present time. This means that the regulation of Program Trading is not a harmonisation of regulation but something new for all the members of the stock exchanges who are not remote members. It is not clear to DINS whether there is a need for provision regulating Program Trading. Therefore, it should be analysed whether there exist a need to regulate Program Trading and other countries' regulation regarding Program Trading ought to be analysed before such rules are introduced.

National comment: Program trading is regulated in Norway and also to a certain extent in LEC.

33. National comments on section 4.11.9 to 4.11.12:

Norway: In the preliminary reports to the new stock exchange act (Ot.prp.nr 73 1999/2000 page 110) the Ministry of Finance says that the system with exchange representatives (børsrepresentanter) shall be abolished. As a consequence of this the Kredittilsynet has proposed to abolish § 25-9 in the Norwegian government regulation on stock exchanges (børsforskriften) regarding sanctions towards an individual exchange trader. Nevertheless it is proposed in NMR section 4.11.10 to maintain the present regulation with personal violation fees and daily fines. None of the other exchanges has similar sanctions and it is clearly unacceptable to main this Norwegian regulation. It also stands in contrast to the general principle of the members' sole responsibility towards the exchange(s). The same objection goes for "other employees or officers of a Member".

Further the reference to the act in section 4.11.11 seems to be wrong.

34. In section 5.1.2.4 "non-matching trade reports" has to be clarified?

35. In section 5.1.4.3 the two last line-points raises questions about the exchanges use of such information and also if it is necessary and possible to provide this information when placing the order. The information can be forwarded later and under restrictions on the exchanges' use.

36. In section 5.1.5.1 concerning odd lot orders it is stipulated that "the Order is filed at the market price; the Latest Paid Price". DINS are of the opinion that odd lot orders should be matched *within or on* the spread not just at "the Latest Paid Price". As a result thereof section 5.1.6.4 should be changed.

37. Section 5.1.6.1 regulates “open call auctions”. DINS are of the opinion that NMR should also contain regulation regarding “closing call auction”.

Is there a harmony between section 5.1.6.1 and section 5.1.11.1 (i)? Section 5.1.11.1 (ii) seems to be inconsistent with section 5.1.11.2 (ii) and the same goes for section 5.1.11.1-second paragraph (ii) and 5.1.11.2 last paragraph.

38. National comment:

Denmark: With regard to the reporting of Standard Average Based price in section 5.1.7.11 the reporting should be made in the Pre Trade Session on the following exchange day as in section 5.1.7.12. This has been agreed upon between the CSE and DSDA.

39. In section 5.1.8 are provisions made for automatic matching on exchange for order volumes less than a certain limit. DINS are of the opinion that there should be no mandatory order matching in the system at all. An effective Norex Exchange may offer enough incentive for the placement of orders on exchange for automatic matching instead of an off exchange matching.

40. National comment:

Denmark: Referring to section 5.1.11 it is important for DSDA that there is no publication of market shares concerning the Danish market. This has to do with the fact that the current reporting rules in Denmark does not give the possibility of an actual and genuine picture of the market shares.

41. In section 5.1.12.3 is suggested a firm volume of 250 Round lots. DINS believe that this limit could not be harmonised taking into account the various volumes trade on each Norex Exchange. On the contrary, the limits should be set for each market.

Furthermore the wording should be more precise “...xx Round Lots or less must be *on or* within the Spread...”

42. National comment from Norway:

Regarding the section 5.1.13.1, and also section 5.1.14.1, 5.1.15.1 and 5.1.16.1, we will underline that these sections seems to contravene the present requirements for listing in Norway. See in this connection the definition of financial instruments in the securities trading act § 1-2 and the corresponding use of the term in the new stock exchange act § 5-6 and the existing act § 1-1 and the government regulation §§ 1-1 and 1-3.

43. In section 2. *Definitions and Abbreviations* the following remarks are to be made:

- Continuous Trading The period during the Trading Session where Automatic Order Matching *and Manual Trading Reporting* takes place
- Exchange Notice A notice in the Trading System *or otherwise* containing information to the Members...

- Financial Instruments Securities and other rights or obligations that are *aimed* (suitable) for trading on the securities market – The phrase “financial instruments” may be defined differently in each country and in Norway the definition is much wider than in NMR. Norway thinks that this is unfortunate.
- Institute should be defined
- Listed (inregistrerat) should be defined as well as quoted (noterat), [of importance for Swedish capital tax reasons]
- Officially Listed delete the word Instrument
- Securities Firm ought to be defined (banks and securities companies)
- Spread is erroneous and should read The range between the highest Bid Order and the *lowest* Ask Order
- User-ID should be defined