

Violation of the duty to trade on order book (point 4.8, para 2 GC and Directive 3)

Summary

During trading hours, the participants of SWX Swiss Exchange are in principle obliged to trade on order book. Exceptions to this duty to trade on order book exist for example in the case of portfolio trades. A portfolio trade is understood to be the purchase or sale, in a single transaction, of a basket containing a minimum of 10 different securities traded at SWX Swiss Exchange with a total market value of at least CHF 1,000,000.

The Sanction Commission issued a reprimand to a participant because he violated the duty to trade on order book by trading off order book during trading hours although the conditions for portfolio trades that he asserted were not fulfilled. Thus the participant has violated point 4.8, para 2, of the General Conditions and Directive 3 of SWX Swiss Exchange several times.

Decision

The Sanction commission has rendered a decision, that the participant X AG has violated point 4.8, para 2, of the General Conditions and Directive 3 of SWX Swiss Exchange in breaching the duty to trade on order book. A reprimand is issued to X AG. The costs of the procedure of CHF 10'000.- are imposed to the participant.

Considerations

1. The Surveillance & Enforcement Office (SVE) of SWX Swiss Exchange (SWX) recommended that the Commission orders a reprimand against X AG for multiple breach of the duty to trade on order book of SWX.
2. In 2006, SVE conducted a review to ascertain information on possible breaches of the duty to trade on order book. The investigation of the present case focused on portfolio transactions during September 2005 and showed that not all of the portfolio trades fulfilled the criteria of Directive 3 of SWX defining the exemption of portfolio trades from the duty to trade on the exchange. According to this rule, a "portfolio trade is understood to be the purchase or sale, in a single transaction, of a basket containing a minimum of 10 different securities with a total market value of at least CHF 1,000,000". Some of the transactions of X AG in September 2005 failed to reach the total market value of at least CHF 1 million, or the basket contained less than 10 securities traded on SWX.
3. X AG agreed with the findings, but stated that the definition of the portfolio trade in directive 3 is not clear as it does not specify that the securities mentioned in the directive must be traded on the SWX. X AG believed that the definition of a portfolio trade in directive 3 includes securities which are not traded on the SWX and stated that the rule has to be interpreted with regard to rules of other exchanges. In X AG's interpretation, a portfolio that consists of more than 10 securities and CHF 1 million is a portfolio according to directive 3 even if the number of SWX-traded securities and their notional value in the basket is under these limits. X AG made this interpretation considering the approach of other exchanges such as virt-x and the London Stock Exchange.

4. It must be noted at the outset that even if X AG's interpretations were to be followed, which is not the case for the reasons stated below, some of the transactions did not reach the total market value of CHF 1 million. They therefore did not fulfil both criteria of directive 3. Hence, in any case, even according to its own interpretation, X AG should have traded these portfolios on order book.
5. Further there is no reasonable doubt that rules or regulations of SWX only relate to trading in securities traded on SWX. The exchange system is open for SWX-traded securities exclusively. The provisions of the General Conditions of SWX explicitly govern trading on SWX (see title 4 of General Conditions) and one of the basic rules stated therein is the duty of participants to trade on order book (point 4.8 General Conditions). It is evident that this rule concerns securities traded on SWX. A directive exempting portfolio trades from this duty to trade on the exchange can not be interpreted as introducing rules for other – non trades – securities. The directive was enacted in 2000 and no similar interpretation has been registered.
6. Other exchanges might well have other rules concerning the requirements to trade on exchange or for the definitions of portfolio or basket trades. This is the case – as X AG mentioned itself – for the London Stock Exchange or for virt-x. However, if a participant is of the opinion that a rule of SWX is not clear, it has the obligation to ask the SWX for clarification, but cannot simply refer to definitions or approaches of other exchanges.
7. If a participant violates the rules and regulations, the SWX imposes a sanction taking into account the gravity of the offence and the degree of fault (point 1.26 General Conditions). X AG cooperated fully with SVE and we assume that it will henceforth ensure compliance with the rules and regulations. As the violation as such was not severe, the Commission shall issue the most lenient of the disciplinary measures, a reprimand. There is no need to disclose this sanction. Nevertheless, in order to give guidance to the participants, SWX might publish sanctions in a completely anonymous form on the SWX website.
8. According to the Rules of procedures of the Commission, the costs of the procedure of CHF 10'000.- (CHF 5'000.- for SVE, CHF 5'000.- for the Commission) are imposed to X AG.

(Decision of 09.02.2007)