

SUPERVISORY FRAMEWORK FOR MARKETS



OICU-IOSCO

**Report by the Technical Committee
of the
International Organization of Securities Commissions**

May 1999

SUPERVISORY FRAMEWORK FOR MARKETS

I. INTRODUCTION

A. Purpose of the Paper

The Objectives and Principles of Securities Regulation which were adopted by the IOSCO Executive Committee in September 1998 identify the three core objectives of securities regulation as: (1) the protection of investors; (2) ensuring that markets are fair, efficient and transparent; and (3) the reduction of systemic risk.

The Preamble to IOSCO's By-Laws state that securities regulators should co-operate to ensure the better regulation of the markets by exchanging information on their respective experiences and establishing standards that promote the core objectives.

The Technical Committee Working Group on the Regulation of Secondary Markets (WG-2) was given the mandate to survey the methods and scope of members' supervision of regulated markets in order to share information on regulators' experiences. As a result of the survey, WG-2 members decided to prepare a paper that would identify a framework for supervising markets. The framework would provide some guidance to regulators to facilitate the design and execution of oversight and surveillance programs that are appropriate for the structure of the markets in their jurisdiction. The framework is intended to encourage jurisdictions to implement and maintain effective market oversight programs by establishing appropriate mechanisms.

B. Scope

As a result of the combination of technology and innovation, market participants can now develop various types of public and proprietary electronic trading systems which can provide many, if not all, of the bundle of services traditionally provided by organized exchanges, although they may fall short, from a functional or regulatory view, of being recognized as organized markets. Frequently, technology and innovation also allow these trading systems to operate across jurisdictional borders. Therefore, because of the differing types and degree of regulation which jurisdictions apply to such systems, one has to distinguish between traditional, organized markets that are regulated and recognized as such and those electronic trading systems which are regulated either as dealers or in some other way. The framework discussed in this paper focuses on traditionally organized markets, both exchanges and dealer markets.

C. Identifying the Framework Allocation of Regulatory Responsibility and Challenges

This paper will first identify and discuss in Part II a general framework for oversight of traditionally organized markets. Part III will describe how a range of regulatory responsibilities may be allocated among different types of regulatory authorities. Part IV of the paper describes new developments that provide challenges for supervision of traditionally organized markets. A survey of techniques used by various regulators is included in the Appendix as further guidance.

It is important to note that in order to determine whether a particular element of the oversight guidance is appropriate, the regulator should take into consideration the following factors: the nature of the market and its participants, the degree of integration with other markets, growing internationalization, and impact of technology. Generally the regulator will use a variety of techniques. Also, the regulator should periodically review the effectiveness of the techniques it is using and assess whether any changes need to be implemented.

The level of regulation, and application of the framework may also depend upon market characteristics including the structure of the market, users, rights of access, types of products traded, the ability of the market authorities to fulfil their self-regulatory role, and the powers and authority granted by law.

II. A FRAMEWORK FOR MARKET OVERSIGHT

In terms of a general framework, the elements of effective oversight consist of the following:

- A. Identifying the appropriate regulatory objectives.
- B. Establishing mechanisms which will achieve those objectives.
- C. Monitoring whether the objectives are being achieved.
- D. Taking enforcement or other corrective action when there is a violation or lack of compliance with requirements.

A. Identifying Regulatory Objectives

Regulators in all markets acknowledge that investors want fair, honest and orderly markets. Thus, the integrity of the markets is an important matter of public interest and regulators should take actions that promote these objectives of fair and efficient capital markets. The IOSCO Principles expand upon these objectives to develop the following more detailed principles regarding orderly and transparent

markets, prohibition of unfair trading practices, identification and management of risks, and effective clearing and settlement.

(1) Orderly Market

There should be ongoing regulatory supervision of exchanges and trading systems which should aim to ensure that the integrity of trading is maintained through fair and equitable rules that strike an appropriate balance between the demands of different market participants (P# 26)¹. Orderly markets are important because they are the basis of smooth functioning markets and promote confidence in the markets. Markets may not be orderly due to conflicts of interests or the unintended effects of processes implemented by a market. Examples of the elements of an orderly market include, but are not limited to, the following:

1. Trading Rules (Priority, Restriction)
2. Default procedures (trading halts and other disruption), details of procedures for trading halts, other trading limitations in circumstances of potential trading disruption on the system should be provided to the regulator. (13.3)²
 - a. Operator (and systems) competence - regulator should assess the competence of the operator of a trading facility as a secondary market on an ongoing basis (Section 13.3 of the Principles Paper). The assessment of the operator's competence should include a review of the conduct and qualification of the staff of the operator. Third party or independent reviews of technology or other matters may be required.
3. Operator oversight - the operator should be accountable to the regulator and, when assuming principal, settlement, guarantee or performance risk, must comply with prudential and other requirements designed to reduce the risk of non-compliance. (13.3)
4. Review of products to be traded - the regulator should, as a minimum, be informed of the types of securities and products to be traded on the trading system. The proper design of their terms and conditions attaching to a product reduces the susceptibility of the product to market abuses. (13.3)

¹ "P#" refers to the number of the principle as set out in the IOSCO paper.

² Numbers that are not preceded by a "P#" refer to the sections number of the IOSCO paper.

- b. Admission of participants - the regulator should ensure that access to the system or exchange is fair and objective. The regulator should oversee the related admission criteria and procedures. (13.3)

Organized markets should also be subject to regulatory authorization, which will facilitate the process of ongoing supervision (P# 25).

(2) Transparency

Regulation should promote transparency of trading (P# 27), timely access to relevant information regarding specific products (13.3) and access to information regarding the operation of the markets (13.3). All similarly situated market participants should have equitable access to trading information. Information is important for price discovery as well as monitoring prohibited behavior. Examples of how to achieve transparent markets include but are not limited to, the following:

- a. Disclosure about an issuer and securities - listing and continuous disclosure. (P# 14) (10.2, 10.3)
- b. Disclosure of pre-trade information - all similarly situated market participants should have equitable access to trading information (13.3). Pre-trade information concerns the posting of firm bids and offers, in both quote and order-driven markets (13.5), timely information on trading halts, and open interests.
- c. Timely disclosure of post-trade information - information on completed transactions should be provided on the same basis to all participants. Full documentation and an audit trail must be available to the party who is performing the surveillance and monitoring of exchanges and trading systems. (13.3)
- d. Monitoring of derogation from timely disclosure - where a market permits some derogation from the objective of real time (immediate) transparency the conditions need to be clearly defined. (13.5)
- e. Publication of order routing and order execution procedures - the system's order routing and execution procedures must be clearly disclosed to the regulator and to market participants. The order execution rules must be applied fairly. (13.3)

(3) Prohibition of Unfair Trading

Regulation should be designed to detect and deter manipulation and other unfair trading practices (P# 28). Integrity of the markets depends upon fairness and is an important part of investor protection. Examples of conduct that could lead to illicit behavior or that need to be monitored include, but are not limited to, the following:

- a. Unfair or Fraudulent Behavior - identify and prevent such conduct as market manipulation, misleading conduct, insider trading, and other deceptive or fraudulent conduct which may distort the price discovery system, distort prices and unfairly disadvantage investors. (13.6)
- b. Conflicts of Interest^{3*}. (12.5)
- c. Sales conduct*. (12.5)
- d. Criteria for Access*. (12.3, 12.4)
- e. Market Participant Conduct - market intermediaries should conduct themselves in a way that protects the interests of their client and help to preserve the integrity of the market. (12.5)

(4) Proper Identification and Management of Risks

Regulation should aim to ensure the proper management of, default risk and market disruption (P# 29). Identifying and monitoring risks reduces the likelihood of problems occurring and assists in the prompt resolution of problems when they do occur. Examples of matters that should be reviewed to reduce risk include, but are not limited to, the following:

- a. Operator Competence. (13.3)
- b. Financial Condition of Participants \ Prudential Concern - the stability of financial systems are increased by an ongoing supervision of adequate capital standards. Capital adequacy standards foster confidence in the financial markets and should be designed to allow a firm to absorb some losses. (12.4)
- c. Margin - margin requirements should be designed so that sufficient funding is available to cover likely trading exposures. (13. 11.1)
- d. Monitoring and Managing Size and Ownership of Positions - there should be monitoring of large exposures and concentration of risks to permit appropriate assessment of risk.⁴ (13.7)
- e. Publication of Market Default Procedures - relevant information concerning market default procedures should be made available to market participants. (13.7)

³ An asterisk indicates that these issues are more directly related to the regulation of intermediaries, and as such are topics that will not be the primary focus of this review except to the extent that they are the acknowledged responsibility of the exchange or market operator, and the regulator is responsible for oversight of the operator's fulfillment of this responsibility.

⁴ A "large exposure" refers to an open position that is sufficiently large to pose a risk to the market or to a clearing firm.

- f. Cross-market conduct (equity vs. derivatives) - market authorities for related products (cash or derivative) should consult with each other as soon as practicable with a view to minimizing the adverse effects of market disruptions. (13 7)

(5) Effective Clearing and Settlement

Clearing and settlement systems provide the process and data for calculating the obligations of participants in the system and mechanisms for settling those obligations. The system for clearing and settlement of securities transactions should be designed to ensure that it is fair, effective, efficient and that it reduces systemic risk subject to regulatory oversight (P# 30). Effective clearing and settlement processes are also important in establishing confidence in the markets.⁵ Means of achieving effective clearing and settlement include, but are not limited to, the following:

- a. Oversight of an Operator - Review prudential, systems and operational considerations to minimize risk of non-completion of transactions. The stability, financial health and activities of participants of the clearing and settlement systems need to be monitored in order to minimize the risk of failure. (13.11)
- b. Identification and Adequate Management of Risks - should provide for expeditious verification of a trade, information should be available which records the transaction and provides the basis for settlement. There should be procedures to identify and monitor risks on an on-going basis. Margin requirement may be used in combination with other mechanisms to manage risk to market participants, including circuit breakers and risk management systems. (13.9~13.11)

⁵ The mechanisms in Part B are discussed in the context of organized markets. Many of those mechanisms are also applicable to oversight of clearing and settlement systems.

B. Establishing Mechanisms which Achieve Regulatory Objectives Including Monitoring and Enforcement

(1) Licensing / Recognition of Market Participants with Imposition of Appropriate Conditions

Market operators (exchanges and organized dealer markets which hereafter will be referred to as “market authorities”)⁶ as well as market intermediaries should be required to receive authorization from the regulator before engaging in the securities and futures business.⁷ Part of the authorization process should include obtaining evidence that market authorities have proper operational and other competencies (frequently the regulator will not be expert in technical aspects of some operational aspects of markets, such as electronic network integrity. In such cases the regulator should consider requiring the market authority to provide independent expert assessment of those issues). The regulator through the licensing process should impose appropriate conditions.

Appropriate conditions may include the obligations to establish rules, policies and procedures to prevent fraudulent behavior, promote the public interest, treat all members users in a fair and consistent manner, have the capacity to carry out the market authority’s obligations, submit rules for review and / or approval, assure a fair representation of members / users in selection of its directors, require public directors, and avoid rules that impose any unnecessary burden on competition.

Through the authorization process, the regulator retains an important enforcement tool: the ability to prohibit or place restrictions upon operations. Moreover, the risk of revocation of authorization can provide an important incentive for market operators to properly operate their markets. However, since license revocation is such a serious disciplinary action, in many cases market operators will not believe it would ever be used and therefore it may not be an effective deterrent. The regulator should also have the clear power to impose an escalating range of disciplinary actions, such as conditions or restrictions on the market operator. While imposition of these restrictions should be subject to some procedural fairness conditions, the process must not

⁶ In this paper “market authority” refers to organized markets, both exchange and dealer markets. Market authorities often act as regulators, as will be discussed in Part III of this paper, however, the term “regulator” is used in this paper to refer to the government or quasi-government agencies responsible for securities regulation. Market authorities are also often referred to as self-regulatory organizations or “SROs”. However SROs are not limited to markets and the term may also refer to associations regulating intermediaries.

⁷ See P# 25. Exchanges and trading systems should also be subject to regulatory authorization, which will facilitate the process of ongoing supervision.

be so slow or cumbersome as to prevent regulators acting swiftly and effectively when required.

(2) Developing Standards, Requirements or Rules

The regulator and/or, the market authority under the oversight of the regulator, should develop appropriate standards such as standards of business conduct for market intermediaries, high standards of commercial practices, equitable principles for trading, and standards of financial integrity including requirements to identify, monitor and reduce risk (controls such as margin, circuit breakers, trading halts, capital adequacy, risk management systems and guarantee funds).

The regulator may need to establish requirements to facilitate the development of a consistent approach to market issues when numerous market authorities or types of market participants operate within the regulator's jurisdiction.

For example, trigger levels are qualitative or quantitative criteria that are used to identify a large exposure. Regulators should require market authorities to:

1. demonstrate the bases for the trigger levels they have set,
2. explain why those levels are appropriate to their markets,
3. periodically assess (and report on) the adequacy of their trigger levels, and
4. assess (and report on) the adequacy of those trigger levels in periods of market volatility.

(3) Approval of Changes to Operations, Rules, Policies, Bylaws, etc.

The regulator should have a mechanism for reviewing and/or approving changes in the market authority's operation: the market authority's rules, policies and bylaws, consideration of product design for certain types of markets, admission criteria, and procedures to ensure the system is fair and objective. The regulator should consider whether rules and policies are consistent with the securities laws in its jurisdiction and regulatory objectives.

(4) Monitoring of Markets through Reporting, Inspection and Auditing

An effective market oversight program must have a mechanism for monitoring compliance with the securities laws, regulations and market authority's rules, operational competence requirements, and market standards. Monitoring includes collecting and analyzing information.

Essential elements of monitoring compliance include: (1) monitoring the day-to-day trading activity in the markets (through a market surveillance program); (2) monitoring the conduct of market intermediaries (through examinations of business operations); and (3) collecting and annualizing information gathered from these activities.

If the market authority has responsibility for market surveillance and examination programs, the regulator should verify the integrity of the oversight system by reviewing how the market authority is performing its functions and determining if it is effectively carrying out its duties (the reliability of the market's monitoring, surveillance and supervision of trading system and its participants). More over, the regulator should assure itself that the market authority is exercising its authority in the public interest, in a manner, which results in fair and consistent enforcement of applicable requirements.

The regulator should identify the information it requires to verify performance and effectiveness of the market authorities' responsibilities, particularly as they relate to the integrity of the market, to monitor risks, and to be able to respond to such risks. Information can be provided through formal mechanisms such as written reports and inspections, or through informal mechanisms such as regular meetings.

(5) Enforcement

The regulatory system should have an effective and credible inspection, investigation, surveillance and enforcement program. (P# 10)

Where market authorities are responsible for parts of the oversight system, regulators should be able to sanction market authorities that fail to perform their regulatory responsibilities (7.3). In order to sanction a market authority, the regulator must be able to monitor the market authority's performance of its enforcement function. The market authority should report to the regulator on breaches of securities law and breaches of market authority rules, and the market authority's response to those breaches.

Regulators should have the authority to use a combination of or all of the following non-exclusive alternative sanctions on market authorities:

- a. censure (public criticism);
- b. monetary sanctions;
- c. remedial measures, including requirements for independent reviews or monitors;
- d. limitations on activity;
- e. requirement that market authority make special reports;

- f. suspension or revocation of approval of a market to act as a market authority; and
- g. judicial orders.

Investors may be provided with rights of redress to seek compensation for damages suffered as a result of non-compliance with fundamental investor protection provisions. As a supplement to the regulator's enforcement efforts, the regulator may want to encourage the implementation of programs for resolving disputes in a swift and efficient manner (e.g., arbitration mechanisms).

(6) Other Mechanisms

In addition to the more formal mechanisms described above, regulators may use informal mechanism including but not limited to:

1. Information sharing among market authorities, regulators and other approved self-regulatory organizations can be done informally or formally through memorandum of understanding, as well as through regulatory requirements. The regulator or market authority may have information that is not automatically available to other parties. Compiling and providing useful information to the market can be an important role of the regulator or market authority for increasing transparency or better risk management of the market participants. Regulators and market authorities should identify what information under what circumstances should be shared and who should have access to such information.
2. The regulator can provide leadership in addressing emergency situations and establishing informal co-ordination among interested parties.
3. The regulator can evaluate and make recommendations regarding modification of the legal framework and / or the need to change the legal or administrative law requirements.

III. ALLOCATION OF REGULATORY RESPONSIBILITIES AMONG THE REGULATOR, MARKET AUTHORITY AND OTHER SELF REGULATORY ORGANIZATIONS

Different jurisdictions have adopted different regulatory regimes. In some jurisdictions, all regulation of markets, clearing-houses and market participants is conducted by one body. In others, different elements of regulation are allocated to different bodies. Whenever the responsibility for market regulation is shared, the clear allocation of regulatory responsibility is very important. This ensures efficient coverage of all aspects of markets, reduces costs of unnecessary regulatory duplication, and facilitates swift and

sure action by the relevant body in a time of crisis. Part of the regulator's supervision of market authorities is to ensure that the relevant roles and responsibilities are clearly understood and accepted by all parts of the market and regulatory structure.

The allocation of regulatory responsibility can be described as a continuum. At one end is a model where the statutory regulator sets the rules, operates the market, does the monitoring and conducts enforcement. At the other end of the continuum is the model where the market authority sets all of its own rules, monitors the market and conducts enforcement without any statutory supervision, it is a self-regulatory model in the truest sense.

Many exchanges commenced operations when there was no statutory regulator. The exchanges were necessarily therefore the source of regulation on issuer qualification, disclosure requirements, dealer conduct and dealer capitalization.⁸

Principle 6 of the Principles of Regulation states that the regulator should make appropriate use of SROs⁹. In most jurisdictions, the model has shifted from the pure self-regulatory model, so that both the market authority and the regulator perform regulatory responsibilities. However, the extent to which self-regulation is used varies.

One type of model is based on the SRO, subject to oversight by the regulator, acting as the first level of oversight, and having the responsibility for market regulation. The argument for this type of model is that the industry has self-motivation to act responsibly based upon economic and reputational interests.¹⁰ Also this type of model enables the regulator to more efficiently use its resources for oversight of the SRO rather than direct market regulation.

The Principles of Regulation point out the following substantial benefits:

- (1) SROs may require the observance of ethical standards which go beyond government regulations; and

⁸ Mahoney, Paul, "The Exchange as Regulator", 83 *Virginia Law Review* (No. 7), 1453.

⁹ The assumption in this paper is that the market authority does perform self-regulatory functions even if it is not a membership organization.

¹⁰ For example, see The International Federation of Stock Exchanges ("FIBV") guidance for market authorities. The guidance are set forth in "FIBV 1998 Market Principles", which replaces the "1995 FIBV Market Principles". The FIBV states that its principles provide guidance on the minimum level of organization, regulation and supervision a securities market needs to have in order to qualify as an organized market and for applying for membership to the FIBV. The FIBV 1998 Market Principles discusses the following: adequate organizational infrastructures and operational resources, equitable access, listing of and disclosure on traded products, trading, transparency, clearing and settlement, technical infrastructure, risk management, settlement of disputes, surveillance and enforcement, investor protection, and business conduct of intermediaries.

- (2) SROs may offer considerable depth and expertise regarding market operations and practices, and may be able to respond more quickly than the government to changing market conditions. (Section 7.2).

In addition, when market authorities participate in designing the regulation they are more likely to comply with the requirements, and market authorities are highly motivated to develop cost-effective regulation. On the other hand, issues may arise when the SRO acts in a self-interested or discriminatory way. For example, some market authorities have tried to prevent alternative trading systems from operating in their jurisdiction.

It has been suggested that the system of shared oversight responsibility can be pictured as a pyramid. The first level of oversight is conducted by the market intermediaries who should be responsible for training and educating parties about the applicable laws and supervising their activities. At the next level the market authority should be given the responsibility to oversee trading activities, adopting standards to promote orderly markets, reduce systemic risk, and enforce violations. The market authority may only be responsible for the conduct of the market at this second level or may also be responsible for the direct oversight of the intermediaries within its jurisdiction. At the top of the pyramid is the regulator. The regulator must assure itself that the market authority exercises its authority in a manner, which results in fair and consistent rules and enforcement of those rules.

IV. NEW DEVELOPMENTS THAT PROVIDE CHALLENGES FOR SUPERVISION OF TRADITIONALLY ORGANIZED MARKETS

Trends such as globalization, technological change, and consolidation of financial services have an impact on how market services are being provided as well as on market structures themselves. As a result both market authorities as well as regulators will have to consider the impact of these developments on the supervisory techniques that they use in order to adapt to these challenges. This part of the paper will describe some of those challenges and the issues they raise relating to supervisory techniques.

A. Alternative Trading Systems

The number of alternative trading systems (ATs), privately operated computerized systems that match buy and sell orders as well as provide pre-trade and post-trade information, has increased rapidly. One of the effects of multiple ATs trading the same product is to fragment the market in that product. In addition to normal supervision of the market operator of each AT, the existence of multi-markets will often require co-ordination of some regulatory activities such as surveillance and establishing some minimum regulatory requirements that protect the orderliness of the market(s). In such an environment, it may be agreed to be more efficient for the regulator to assume some of

the regulatory responsibilities that are performed by the market authorities in jurisdictions with simpler market structures.

ATS frequently provide different bundles of market services. As mentioned previously, and below, authorization and supervision of ATS and their operators should be based on the bundle of services provided, as well as the other factors such as the nature of participants, the products, and how to minimize any negative effects of fragmentation of the markets.

B. Demutualization of Exchanges


Some traditionally structured exchanges have begun to question the appropriateness of their membership ownership and governance structure. Some are considering restructuring into for-profit organizations where access to trading will be separated from the ownership of the market. Regulators will have to consider what should be the impact of restructuring a membership organization on the regulatory functions of the market authorities, particularly the managing of conflicts of interest. Some market authorities, such as the Amsterdam Stock Exchange and Australian Stock Exchanges, have already restructured their membership organizations. Others, such as the Toronto Stock Exchange and Hong Kong Exchange are in the process of doing so.

C. Deconstruction, Unbundling and Rebundling of Services

One of the consequences of technological developments and globalization is that traditional concepts of how services should be supplied and bundled are being reassessed. In response to new challenges, some traditional integrated financial services businesses (including markets) are unbundling or desagregating the different elements of the services they supply. Using technology, specialized niche players are offering narrowly focussed, low-cost services, such as order routing and matching, in competition with the bundled offerings of traditional dealers and exchanges. A major concern of traditional exchanges in such cases is that these niche competitors, providing only partial services, may shirk their responsibility for the cost of ensuring fair efficient and orderly markets (i.e. they will “ free-ride” on the existing market authority’s regulatory efforts).

Traditional markets have also begun to consider unbundling such services as listing or providing information on quotes. Such unbundling will undoubtedly affect the allocation of regulatory responsibility. Regulators, in considering alterations to exchange or market authority rules, or authorization of niche players, should require this issue to be addressed, in particular, how supervision of the niche players’ activities will be paid for, and how overall supervision of the different elements of the market will be co-ordinated. As for ATS, supervision of niche service providers should be determined by the nature of the services they provide as well as their place in the market system.

V. EXAMPLES OF TECHNIQUES UTILIZED BY REGULATORS IN THE SUPERVISION OF A MARKET AUTHORITY

Attached in Appendix “” is a chart setting out how various regulators currently perform their responsibilities within the context of the framework set out in this paper. The chart is intended to provide some examples. The appropriateness of any approach will depend upon not only the market characteristics but also the authority to act that has been granted to the regulator. Also, as a result of new developments in the market place, regulators are constantly evaluating how to apply the oversight mechanisms discussed in this paper and may change their approach. So the information is accurate as of the date of publication.

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APPENDIX A: MECHANISMS						
Jurisdiction	Licensing/Recognition	Developing Standards/Rule	Approval of Changes	Inspection Audits Monitoring	Enforcement	Other
Ontario Securities Commission (Canada)	<p>Stock Exchange and trade reporting and quotation systems must be recognized pursuant to sections 21 and 21.1 of the Securities Act.</p> <p>As part of the recognition the Commission will consider the following issues: governance structure, capacity, competence, access, and whether any of the exchange policies, rules or by-law are contrary to the public interest. Conditions or requirements may be imposed.</p> <p>Market participants are subject to registration requirements under the Act and must register with the Commission. Dealers who trade on an exchange or belong to an SRO are subject to further SRO registration requirements.</p>	<p>The Securities Act Regulation, and Rule set out specific requirements for intermediaries. Although currently there are no specific standards or rules regarding market behaviour staff is working on a proposal which will set out basic standards regarding manipulation, best execution, transparency and consolidation of markets.</p> <p>The exchange is responsible for establishing rules related to the access to the exchange, operation and governance of the exchange, trading and conduct of members, clearing and settlement and fees.</p> <p>SROs are responsible for rules related to sales and business conduct, capital adequacy and corporate finance.</p>	<p>Recognized markets must submit all rules, policies, by-laws to the Commission for approval. While all by-laws are published in the Commission's weekly publication; by agreement, only by-laws, policies, etc that are identified by the market as public interest require approval. The Commission reviews the Apublic interest by-laws to determine whether they are contrary to the public interest.</p>	<p>The Commission's oversight program evaluates how the market or SRO is performing its functions. The key functions identified by Staff are: listing, trading, rules, surveillance, enforcement, managing risks, and products.</p> <p>Staff intend to implement a program to review the markets automated system.</p> <p>SROs perform annual reviews of compliance with rules of conduct, capital and financial reporting rules and corporate finance activities of members. Stock exchanges and quotation and reporting systems perform periodic reviews of compliance with trading rules.</p> <p>A market surveillance unit is operated by exchanges and quotation and reporting systems and monitors the market on a real-time basis in order to detect non-compliance with trading rules. Historical trading data is collected and analyzed at the exchanges and the Commission.</p> <p>Issuers are subject to regulation directly by the Commission and must comply with Commission standards (including disclosure and financial reporting) as well as listing or quotation requirements of exchanges or quotation and reporting systems.</p>	<p>Activities that are violation of the Securities laws are referred to the Commission.</p> <p>The SROs and exchanges undertake investigation and enforcement of compliance with rules by members and their employees. The SROs and exchanges have the power to impose penalties on members and individuals including fines, suspension or revocation of membership.</p> <p>Investigations and enforcement actions may be referred to the Commission by the SRO, exchange, quotation and reporting system.</p> <p>The Commission has the power to impose fines and suspensions of registration. The Commission may also take civil action against the issuer or market participant, whether or not they belong to an SRO or exchange. The Commission may refer the matter to the police for criminal investigation.</p>	<p>OSC Staff meet quarterly with staff of the market authority to review issues</p>
Commission des Valeurs et des Molulieres de Québec (CVMQ)	<p>The Commission has delegated certain powers to the SRO, including its registration powers for representatives employed by SRO member firms, and its approval powers for senior executives of these firms. To ensure that the SRO properly assumes these responsibilities, the following procedures are in place:</p> <ul style="list-style-type: none"> ! forwarding to the Commission of all representative registration and senior executive approval decisions rendered by the SRO; ! publication of SRO decisions in the Commission's <i>Bulletin</i>; ! on-site inspection of SRO books and records; 		<p>Commission regulations require that any proposed amendments to incorporating documents, by-laws or operating rules of self-regulatory organizations (SRO) must be presented to the Commission for approval. The procedures to be followed are:</p> <ul style="list-style-type: none"> ! request for amendment submitted by the SRO; ! analysis of the request by the personnel; ! recommendation made to the Commission to approve or reject the amendment; ! decision rendered by the Commission; ! forwarding of the decision to the SRO; ! publication of the decision rendered in 	<p>The Commission has entrusted the SRO with the responsibility of processing investor complaints about brokers who are members of an SRO. In order to ensure that complaints from investors are processed properly by the SRO, the following procedures were put in place:</p> <ul style="list-style-type: none"> ! forwarding of investor complaints received by the Commission to the SRO; ! mailing of a letter to investors advising them that their complaints have been transferred to the SRO and informing them of the possibility of requesting a file review to be carried out by the Commission should they not be satisfied with the reply submitted by the 		

APPENDIX A: MECHANISMS						
Jurisdiction	Licensing/Recognition	Developing Standards/Rule	Approval of Changes	Inspection Audits Monitoring	Enforcement	Other
	<ul style="list-style-type: none"> ! analysis of representative registration and senior executive approval files (adherence to registration and approval conditions; time frame for processing the applications; accuracy of information entered in the database shared with the Commission); ! writing of a report related to irregularities found during the inspection; ! inspection report forwarded to the SRO presenting the prescribed corrective measures; ! analysis of proposed measures; ! on-site monitoring of corrective measures 		<p>the Commission=s <i>Bulletin</i>;</p> <ul style="list-style-type: none"> ! prescribed time to process the request for comments. 	<p>SRO;</p> <ul style="list-style-type: none"> ! regular follow-up on the SRO to verify the progress of files; ! receipt of reply letters sent by the SRO to complainants; ! receipt of disciplinary decisions rendered by the SRO; ! on-site inspection of the SRO=s registers; ! analysis of complaint files (quality of information obtained, processing time frame; decision rendered); ! writing of a report on the status of the irregularities found during inspection; ! inspection report forwarded to the SRO presenting the prescribed corrective measures; ! analysis of proposed measures; ! on-site monitoring of corrective measures. 		
<p>Commission des Opérations de Bourse (France)</p>	<p>1) Conseil des Marchés Financiers The Conseil des Marchés Financiers (CMF) is the market professional authority or SRO set up by the 1996 Act. The members of the CMF are appointed by the Minister of Finance after consultation with the professional bodies (6 representatives of the market members, 1 rep. of the commodities markets, 3 rep. of listed issuers, 3 rep. of investors, 1 rep. of the employees of investment firms, exchanges, clearing houses). A representative of a Ministry of Finance sits on its board. The General Regulation of the CMF are approved by the Ministry of Finance after the formal opinion of the COB and the Banque de France have been sought. The CMF has 3 main competencies: a) While the authorization of an investment firm is granted by the CECEI, prior to this authorization or registration, the CMF has to approve the program of operation of the</p>	<p>1) Commission des Opérations de Bourse To carry out its mission, the Commission may issue regulations concerning the functioning of markets under its control or prescribing rules of professional practice that apply to: ! persons or entities making a public offering, ! persons or entities who, by virtue of their professional activities are either involved in transactions concerning securities issued through a public offering or who are involved in the individual or collective management of portfolios. These regulations are issued after the opinion of the CMF, has been sought, when dealing with a regulated market and after approval by the Minister of Finance. The Commission may also adopt instructions with a view to going into more details on the interpretation and implementations of its</p>	<p>1) Conseil des Marchés Financiers Changes in the General Regulation of the CMF are subject to the approval of the Ministry of Finance. After the formal opinions of the COB and the Banque de France have been sought. 2) Regulated Markets The exchange has to inform the CMF, the COB and the Banque de France of the planned changes to its rules, the CMF then decides on the compatibility of the amendments with the recognition as a regulated market notifies the COB and the Banque de France of its decision and refers any incompatibility of such amendments with such recognition to the Minister of Finance. The Commission has to decide whether it agrees or not with the decision taken by the CMF. In case of disagreement with the decision taken by the CMF, the COB and the Banque de France. Banque de France may appeal to the Minister of Finance within 15 days of the</p>	<p>1) Regulated Markets As a first layer, regulated markets operate their own market surveillance in order to monitor compliance with market rules by market members. Violation of market rules may lead to the withdrawal of membership. 2) Conseil des Marchés Financiers Monitoring and market surveillance operated by the CMF aims at ensuring that rules of conduct governing investment firms, market undertakings and clearing houses are fully by and monitoring the compliance of transactions carried out on a regulated market with the exchange rules and the General Regulation of the CMF. The CMF may delegate the monitoring of on-exchange transactions to the exchange on which the transactions are carried out. It may withdraw such delegation at anytime. 3) Commission des Opérations de Bourse Market surveillance and supervision carried</p>	<p>1) Commission des Opérations de Bourse The Chairman of the COB can decide to open an investigation at any moment in connection with a potential violation of securities laws and regulations. Typically, an investigation would be triggered as a result of observations arising out of market surveillance, the follow-up of market activities or as a result of a complaint lodged with the Commission. To carry out these investigations, the Commission has, at its disposal, investigators (staff from the enforcement division) that have been authorised by the the Chairman. COB investigators are entitled : ! to enter all business premises, ! to have made available to them all documents, irrespective of the medium (that would include</p>	

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	<p>investment firm to make sure that it has adequate means, resources and experience to provide the investment services for which the firm requires to be authorized.</p> <p>The General Regulation of the CMF provides for the conditions under which the investment firms may exercise their activities and the rules of conduct to be met by firms when providing investment services. The CMF controls that investment firms comply with these rules of conduct and may take disciplinary sanctions against them.</p>	<p>regulations. These instructions are transmitted to the Ministry of Finance but do not need its formal approval.</p> <p>It can also adopt recommendations on specific points.</p> <p>Finally, the COB can be consulted regarding the interpretation of its regulation by any person contemplating and operation.</p>	notification of such decision.	<p>out by the COB is more broadly designed since it aims at detecting all practices and conducts that may affect investors protection and the proper functioning of the markets, any practice or market manipulation, misleading conduct, insider trading and other fraudulent conduct which may distort prices and unfairly disadvantage investors) or company law (failure to declare the passing of shareholding thresholds, purchase of own shares by an issuer outside the permitted limits).</p>	<p>tapes for instance) and to obtain a copy of those documents.</p> <p>! to summon and interview any person likely to be in a position to provide information. Any person summoned to provide information has the right to legal counsel of her/his choice.</p> <p>! with authorization of a judge, to proceed with search in any place, including domiciliary visits, and any subsequent seizure of documents.</p>	
<p>Commission des Opérations de Bourse (France)</p>	<p>(b) The General Regulation of the CMF also sets out the general principles governing the organization of regulated markets and clearing houses. Exchange rules as well as the clearing houses rules has to be approved by the CMF.</p> <p>(c) The CMF is also in charge of the regulation of tender offers (cash or exchange tender offers).</p> <p>1) <i>Recognition as a regulated market</i> Under the Modernisation of Financial Activities Act of July 2, 1996 (the A1996 Act), the recognition of a futures or a securities market as a regulated market is subject to the approval of the Ministry of Finance, upon proposal of the Conseil des Marchés Financiers (CMF) which acts as the SRO for French regulated markets, and after the formal opinions of the Commission des Opérations de Bourse (COB) and the Banque de France have been sought.</p> <p>Under the 1996 Act, in order to be recognized as a regulated market, a market for financial instruments must provide for regular trading. The rules governing the market, and enacted by the market undertaking ruling the market, must include, inter alia, membership requirements, listing requirements, the organization of which trading in one or more financial instruments may be halted as well as rules for the recording and disclosure of transactions.</p>	<p>2) Conseil des Marchés Financiers The General Regulation of the Conseil des Marchés Financiers sets out the conduct of business rules to be met by investment services providers. It also sets out the general organizational and operating principles that regulated markets must observe and the rules governing, execution, reporting and disclosure of transactions in financial instruments traded on such markets.</p> <p>Guidance relevant to standards required from regulated markets set out in the General Regulation of the CMF relates mainly to rules of conduct to be met by market undertakings, membership, trading, concentration of transactions on a regulated market.</p> <p>The General Regulation of the CMF also provides guidances to be met by clearing houses.</p> <p>3) <i>The market rules</i> Each regulated market has its own set of rules governing the admission of members, the admission of financial instruments to trading, trading, reporting, disclosure, etc.</p>		<p>Although market surveillance is primarily aimed at the supervision of activities or transactions on the market by intermediaries or investors, it can also be a mean of assessing the integrity of the market itself. Any concern on the operation of the market arising from surveillance of activities or transactions on the market may result in a <i>Afor cause</i> investigation in or review of the market.</p> <p>If, in the course or as a result of an investigation, the Commission believe that some aspect of the exchange rules need to be reviewed, and possibly improved, the Chairman of the Commission would raised this points the Chairmen of the regulated exchanges and with the Chairman of the CMF. As a stronger step, the COB may also, where appropriate, take a regulation that would require a change in the rules of the exchange to be complied with. It could also recommend that the recognition as a regulated market be withdrawn by the Ministry of Finance.</p> <p>The Chairman of the COB may refer to the Chairman of the CMF any matter within the competence of the latter, including the supervision of regulated markets. If the CMF proves deficient, measures required by the circumstances are taken in emergency by a decree of the Ministry of Finance.</p>	<p>The judge must verify that the request for the search warrant is justifiably motivated. The request must therefore include all information setting out ground for the request. If access is granted, the judge must then appoint a Police Officer to attend the visit and report to the judge.</p> <p>Upon request of the COB, the President of the TGI (High Court) may order any funds, shares, securities or right that belong to persons under investigation to be seized, regardless of who may be holding them. He may also order a temporary bar from professional activities</p> <p>Upon request of the COB, the President of the TGI (High Court) may order a person under investigation to post bail. The President decides upon the amount to be deposited, its allocation and the duration of the bail.</p> <p>Any person who obstructs the investigation conducted by the COB investigators in compliance with the provisions of the Ordinance may be imprisoned from 15 days to two years and/or fined \$5,000 to \$400,000.</p>	

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Commission des Opérations de Bourse (France)	<p>The General Regulation of the CMF provides that, in order to propose the recognition of a market as a regulated market, the CMF takes into account, in addition to market rules, the following elements :</p> <ul style="list-style-type: none"> ! the by-laws of the market undertaking (including its code of conduct) ; ! the identity of the market undertaking=shareholders; ! the human, technical and financial means of the market undertaking; ! the fitness and integrity of its management ; ! where relevant, the rules of the clearing house (trades on a regulated derivative markets must be cleared by a clearing house). <p>(2) Licensing of investment firms and other market members</p> <p>Under the Act, membership in a regulated market is opened to :</p> <ul style="list-style-type: none"> ! Duly authorized investment service providers (investment firm or bank). In France, investment service providers are authorized by the Comité des Etablissements de Crédit et des Entreprises d'Investissement (CECEI) (Committee for Credit Institutions and Investment Firms) after approval of their business plans by the Conseil des Marchés Financiers. They are subject to the prudential supervision of the Banking Commission. 				<p>The Commission may also conduct investigations at the request of foreign counterparts fulfilling similar duties, subject to reciprocity and confidentiality (conditions considered to be met for EEA countries).</p> <p>Based on the findings of the investigations, the COB may transfer the case to the public prosecutor, impose administrative sanctions (fines), raise the issue with the persons involved or close the case.</p> <p>2) Conseil des Marchés Financiers</p> <p>The CMF may take disciplinary action against an investment firm acting in violation with the exchange rules and/or CMF General Regulation. If, in the course of its surveillance activities, the CMF comes across a misbehaviour that is not only in breach of the CMF General Regulation but may also constitute a potential violation of the COB regulations, the CMF has to inform the Commission of the relevant facts of the Commission of the relevant facts.</p>	
Commission des Opérations de Bourse (France)	<ul style="list-style-type: none"> ! Natural or legal persons authorized by the Conseil des Marchés Financiers based on the General Regulation of the CMF with respect to the information to be included in the application file and to the minimum capital requirements. <p>Remote members from the EEA which are duly authorized as investment service provider in their home jurisdiction may also become members of regulated markets.</p>					

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	<p>Remote members from countries outside the EEA, or remote members from EEA countries that are not authorized as investment service provider in their home country, must be authorized by the CMF prior to applying for remote membership at the exchange. They must be under the control of a competent authority in their home jurisdiction.</p> <p>Once duly authorized, investment firm and natural persons may apply for membership at the exchange according to the rules governing the admission of market participants as set out in the market rules.</p>					
<p>BAWe (Germany)</p>	<p>Admission of an exchange Exchanges need admission by the Exchange Supervisory Authority of the respective federal state (Land). They must have a certain institutional and legal infrastructure, including:</p> <ol style="list-style-type: none"> 1) An Exchange Council is responsible for the adoption of Exchange Rules and Fee Regulations, the appointment and removal of the Board of Management in consultation with the Exchange Supervisory Authority, supervision of the Board of Management and adoption of conditions for transactions on the exchange. The Exchange Council consists of a maximum of 24 persons from the industry with each industry group represented. When a new exchange is approved, the Exchange Supervisory Authority appoints a provisional Exchange Council for a maximum period of one year. 2) A Board of Management of the exchange. 3) Fee Regulations. 4) Disciplinary Committee. <p>Admission of market participants to the exchange Admission to the exchange requires authorization by management of the exchange.</p>	<p>Exchange The exchange is responsible for issuing rules and regulations, the most important of which are:</p> <ol style="list-style-type: none"> 1) Exchange Rules: These include provisions regarding the scope of business of the stock exchange, the organisation of the stock exchange and the publication of prices and official quotations. These Rules may contain provisions ensuring the settlement of stock exchange transactions and provision regarding transactions on the exchange. 2) Rules of procedures for the Exchange Council; 3) Fee Regulations; 4) Rules of procedure for the Board of Management; <p>Federal Securities Supervisory Office (BAWe) Rules of conduct: The BAWe may specify the statutory rules of conduct which apply to investment services provided on behalf of customers by issuing guidelines and ordinances.</p> <p>The BAWe may issue regulations on the reporting requirements applying to market participants which are necessary to monitor the market to detect illegal insider trading.</p>	<p>Exchange The exchange is responsible for changes of its own rules and regulations. For a list of these rules see developing standards/Rules.</p> <p>Exchange Supervisory Authority All changes of rules and regulations require the approval of the Exchange Supervisory Authority.</p> <p>BAWe, BAKred The BAWe and the BAKred are responsible for changes of their guidelines and ordinances.</p>	<p>Exchange Supervisory Unit Each exchange has to set up, in accordance with the Exchange Supervisory Authority, a Supervisory Unit.</p> <p>This unit monitors trading on the exchange and the settlement of exchange transactions. It is responsible for systematically and completely recording and evaluating data regarding exchange trading and the settlement of exchange transactions and for conducting any necessary investigations.</p> <p>BAWe Compliance with the rules of conduct is monitored annually. Independent auditors are commissioned to assess bank and investment service enterprise compliance with the rules of conduct.</p> <p>It may demand information and the submission of documents from the exchange, the enterprises and exchange traders and may conduct inspections. It may require trading participants to disclose the identity of their customers and of persons incurring a liability</p>	<p>Disciplinary Committee of the Exchange The Committee may reprimand, impose a fine up to DEM 50,000 upon or exclude from the exchange for up to thirty trading days any trading participant who intentionally or recklessly violates exchange law, provisions or orders that are intended to ensure the orderly conduct of exchange trading or the settlement of exchange transactions or, breaches established principles of commercial trust or damages the reputation of another trading party.</p> <p>Management of the Exchange Suspension and withdrawal of licences of individual traders. If the conditions for admission are no longer fulfilled, admission may be suspended by the exchange management for a maximum of six months.</p> <p>If there are severe breaches of the rules of the exchange, the management of the exchange may withdraw the admission.</p> <p>Exchange Supervisory Authority May issue order for the exchange or trading participants to prevent</p>	

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				<p>or benefiting from the executed transactions. It monitors the security to be provided by the exchange members to the exchange.</p> <p>The Exchange Supervision Unit reports on a regular basis to the Exchange Supervisory Authority and if necessary on an ad hoc-basis.</p> <p>The BAWe may conduct additional audits if deemed necessary and will inform the BAKred of the results of the audits.</p>	<p>violations of exchange law or eliminate irregularities which could impair orderly conduct of exchange trading, settlement or supervision thereof.</p>	
<p>BAWe (Germany)</p>	<p>Applicants must be licensed by the Federal Banking Supervisory Office (Bundesaufsichtsamt für das Kreditwesen, BAKred) as a bank or an investment services enterprise. Applicants must meet certain capital requirements and demonstrate reliability and suitability (i.e. must be fit and proper).</p> <p>Applicants who are not a bank or an investment services enterprise need to have a minimum capital of DEM 100,000. These firms are not permitted to take positions and are restricted to trading in the name and for the account of a third party.</p> <p>The exchange may stipulate that enterprises which are admitted to trading must provide sufficient security to be able to satisfy at obligations arising out of transactions at any time order to ensure orderly settlement of transactions.</p> <p>Admission of individual traders of market participants to exchange trading</p> <p>Applicants must have an appropriate education, professional qualification and experience.</p> <p>Applicants have to pass an examination/test before the Board of Examiners.</p>	<p>Federal Banking Supervisory Office (BAKred)</p> <p>Capital requirements for banks and investment services enterprises: The BAKred may specify the statutory capital requirements which apply to market participants by issuing guidelines.</p> <p>Risk management: The BAKred may specify the statutory requirements which apply to market participants by issuing guidelines (e.g.: "Minimum requirements for the trading activities of credit institutionsA (= banks)). Equivalent obligations exist for investment services enterprises.</p>		<p>Market participants are obliged to report all on and off-exchange trades to the BAWe. These reports form the basis for the insider surveillance of the BAWe.</p> <p>Listed companies are obliged to publish immediately any new material corporate information.</p> <p>Owners of listed companies are obliged to disclose major changes in their holdings.</p> <p>BAKred</p> <p>As part of its ongoing supervision, the BAKred supervises compliance by banks and investment services enterprises with the regulatory provisions regarding their funds, liquidity and large exposures.</p> <p>For this purpose, the BAKred evaluates the monthly and annual statements of account, the reports on the statutory audits of those statements and specific supervisory returns, which comprehend a broad range of data.</p> <p>Besides the statutory audits of the monthly and annual statements of account, the BAKred may order special audits of the institutions so as to gain better insight into their management and financial situation. Those audits are, for the most part, entrusted to public certified accountants rather than to BAKred staff.</p> <p>The monthly and yearly reports contain detailed data with regard to the risk management of the institutions.</p>	<p>BAWe</p> <p>Statutory power to impose fines on banks or investment services enterprises for failing to keep and retain records.</p> <p>BAKred</p> <p>BAKred has the authority to take actions to prevent insolvency or over indebtedness. In less serious situations, the BAKred may require the replacement of managing directors who do not meet the Afit and proper requirements.</p>	
<p>Hong Kong Securities &</p>	<p>The SFC licenses/ recognises and regulates the securities and futures industries pursuant to the following Ordinances and subsidiary</p>	<p>The Exchanges and Clearing Houses develop their own rules.</p>	<p>The SFC is granted rule-making powers under the relevant Ordinances. The SFC's rule-making powers vary from being</p>	<p><i>Inspection</i></p> <p>The SFC undertakes regular inspections of</p>	<p>The Exchanges and clearing houses are SRO=s and, in the first instance, are required to regulate their own</p>	<p>Listing</p> <p>Under the</p>

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<p>Futures Commission (SFC)</p>	<p>legislation. <i>Stock Exchanges Unification Ordinance [SEUO]</i> Under the SEUO, the Stock Exchange of Hong Kong (SEHK) is granted the exclusive right to establish, operate and maintain a stock market in Hong Kong. The SEUO empowers the SFC to withdraw the recognition of the SEHK under circumstances described therein. <i>Securities Ordinance [SO]</i> The SO provisions include: (i) restrictions on the establishment of stock exchanges (ii) registration requirements for dealers, investment advisers and representatives. <i>Commodities Trading Ordinance [CTO]</i> The CTO covers: (i) the licensing of a commodity exchange and revocation of the license; <i>(Note: there is no monopoly granted to the futures exchange, as there is for Stock Exchange);</i> (ii) registration requirements for traders; The SO and CTO should be read in conjunction with some related ordinances and subsidiary legislation, including the Securities and Futures Commission Ordinance (which comprises, among other things, the Financial Resources Rules applicable to persons registered with the SFC), the Commodity Exchanges (Prohibition) Ordinance which prohibits the establish or operate a commodity exchange.</p>	<p>The SFC develops appropriate business standards for the market. Publications include: ! A Code of Conduct for Persons Registered with or licensed by the Securities and Futures Commission (2/94) ! A Conduct of Business Guidelines for License Holders under the Leveraged Foreign Exchange Trading Ordinance (7/94) ! A Core Operational and Financial Risk Management Controls for OTC Derivatives Activities of Registered Persons (3/95) 1995, (which set forth the guidance provided to securities regulators by IOSCO). The Commission formally adopted the IOSCO guidance as a statement of minimum best practice for registered persons in relation to their management control systems and certain procedures. Other codes and guidelines issued by the SFC are as follows: ! Code on Investment-Linked Assurance Schemes ! Code on Immigration-Linked Investment Schemes ! Code on Pooled Retirement Funds ! Code on Unit Trusts and Mutual Funds (3rd Edition) UTC ! Hong Kong Codes on Takeovers and Mergers and Share Repurchases CTM ! Code of Conduct for Persons Registered with the Securities and Futures Commission</p>	<p>exercised by the SFC alone B to those made after consultation with the Financial Secretary and those by the Chief Executive in Council. All require negative vetting by the Legislative Council. Any amendments or additions to the Rules or by-laws of the Exchanges or Clearing Houses must be approved by the SFC before implementation.</p>	<p>the exchanges, clearing houses and registered persons under the remit of the Securities and Futures Ordinance. <i>Audit</i> The SO and the CTO are enforced by the SFC and require dealers to keep accounting and other records which sufficiently explain the transactions, and reflect the financial position of their business. These records are to be kept in such a manner to enable them to be conveniently and properly audited. Under the SO and CTO, a dealer is required to submit to the Commission within four months of its financial year end a true and fair profit and loss account and balance sheet. Together with these, an auditor's report containing the information as prescribed by the Securities (Accounts and Audit) Rules / Commodities Trading (Accounts and Audit) Rules, must also be provided. <i>Leveraged Foreign Exchange Trading Ordinance [LFETO]</i> The LFETO was enacted in 1994 to regulate (as the name suggests) the trading of leveraged foreign exchange contracts by persons other than authorised institutions under the Banking Ordinance. The Ordinance: (i) defines the ambit of leveraged foreign exchange trading; (ii) provides that only limited companies are eligible to be registered as leveraged foreign exchange traders and specifies registration requirements; (iii) provides full powers of supervision and investigation to the Commission;</p>	<p>activities. They are also the front-line enforcers of compliance by their members with the securities laws. The second line enforcement function is performed by the SFC. The Commission has very specific powers under the SFCO, the Securities Ordinance (SO), the Commodities Trading Ordinance (CTO) and the Leveraged Foreign Exchange Trading Ordinance (LFETO) in relation to offences and misconduct. These powers fall broadly under three categories: 1. Prosecution, 2. Court order, and 3. Revocation/suspension/reprimand. The Commission is endowed with the discretion to prosecute, in its own right, offences that are triable summarily. In the prosecution of summary offences, the Commission may be represented by any of its staff, whether legally qualified or not. Where evidence of offences that are serious enough to be tried on indictment is obtained by the SFC, the SFC may involve the Hong Kong Police, or other appropriate law enforcement agency, in the investigation of the matter. The Department of Justice may cause</p>	<p>Securities and Futures Commission (Transfer of Functions) Order, the SFC confers some of its listing functions to the SEHK. Every 18 months the SFC performs an audit of the SEHK's delegated listing function</p>
<p>Hong Kong Securities & Futures Commission (SFC)</p>	<p><i>The Leveraged Foreign Exchange Trading Ordinance (LFETO)</i> The LFETO contains some additional criteria for corporations applying for licenses as leveraged foreign traders. <i>The Securities and Futures (Clearing House) Ordinance</i></p>	<p>! Fund Manager Code of Conduct FMCC ! Conduct of Business Guidelines, Supplementary note to the Fit and Proper CBG Criteria for applicants applying for licences under the LFETO:</p>		<p><i>Monitoring</i> The SFC regulates both the securities and futures industries, but delegates front-line regulation of members to the exchanges. In addition, the SFC's different divisions also conduct reviews.</p>	<p>charges to be brought in the District Court or the Court of First Instance then advises such of the matter. The Department of Justice may cause charges to be brought in the District Court or the Court of First Instance then advises such investigations.</p>	

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	<p>The SF(CH)O pertains to the authorisation of Clearing Houses.</p> <p>In addition, there are the Dealers, Advisers and Representative=s Rules under the SO, CTO and LFETO that govern minor registration matters.</p>	<p>! Management, Supervision and Internal Control Guidelines for Persons ICG</p> <p>! Registered with or Licensed by the Securities and Futures Commission</p> <p>! Licensing Information Booklet (For Securities and Commodities Trading) Foreign Exchange Trading) LIB(FE)</p> <p>! The Fit and Proper Criteria FPC</p> <p>! Guidelines for the Exemption of Listed Companies from the Securities (Disclosure of Interests) Ordinance</p> <p>! Simplified Outline of the Leveraged Foreign Exchange Trading Subsidiary Rules and Guidelines</p> <p>! Revised Guidance Notes Regarding Money Laundering B Notes to FRR</p> <p>! Client Identity Rule Policy</p> <p>Most recently, the Commission published the AGuidance Note on Internet Regulation=.</p>			<p>In respect of the exchanges and clearing houses, the SFC may order closure of the exchanges in emergencies, and may withdraw the recognition of the exchanges under grounds specified in the respective ordinances.</p> <p>The SFC is granted additional powers under the SFCO to, after consultation with the Financial Secretary and requesting in writing to the exchange or clearing house in question, require that exchange or clearing house, to amend, withdraw or revoke any provision of its rules, regulations or other instruments or take actions relating to the management, conduct or operation of its business. Under the same provision, the SFC can also prohibit that exchange or clearing house doing or causing to be done acts or other things relating to the management, conduct or operation of its business. Under a separate provision, the SFC is empowered to make a Asuspension order= to suspend the functions of the governing body, a committee and/or the chief executive officer of the company.</p>	
<p>Consob B Commissione Nazionale per le Società e la Borsa (Italy)</p>	<ol style="list-style-type: none"> According to the AConsolidated Laws on Financial Intermediation= (Legislative Decree n. 58 of February 28th 1998), the organization and management of regulated markets for financial instruments is an entrepreneurial activity and must be performed by companies (S.P.A), authorized by Consob, and which may also operate on a non-profit basis and are subject to minimum capital requirements. Each company can manage more than one regulated market; each of them, however, must be authorized. Consob is also responsible for 	<ol style="list-style-type: none"> Under Italian law, Consob authorizes regulated markets provided that: <ol style="list-style-type: none"> the market rules are: <ul style="list-style-type: none"> - in conformity with the Community law, - sufficient to ensure the transparency of the market, the orderly conduct of trading and the protection of investors; and the company that operates the market meets capital, organizational and fitness and properness requirements. Currently there are no specific standards for authorization of regulated markets other than those cited above; 	<ol style="list-style-type: none"> All changes in the regulation of regulated markets must be authorized by Consob. All changes in the regulation of organized markets other than regulated markets must be reported to Consob. 	<ol style="list-style-type: none"> Consob is empowered by law to require companies operating regulated markets, the communication of data and information and the transmission of documents and records on a regular basis or upon request. Consob may also carry out inspections on the companies and require the production of documents and adoption of such measures as it deems necessary. Consob may require the companies to amend market rules when it deems it necessary to ensure orderly trading, transparency and investor protection. There is a specific market surveillance unit at Consob, which monitors on a 	<ol style="list-style-type: none"> Compliance with insider trading and manipulation rules is monitored by Consob, which refers to a judiciary authority. Such violations are criminal offence under the Italian law. In the event of serious irregularities in the management of markets or in the administration of the companies and whenever it is necessary for the protection of investors, the Ministry of the Treasury, acting on a recommendation from Consob, shall dissolve the administrative and control bodies of the company or revoke 	<p>Consob Market Division staff has informal daily contacts with the staff of the market and assists them in developing market rules.</p> <p>Consob has regular (monthly) formal meetings with the top management of the company that operates the market.</p>

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	<p>supervision of organized markets other than regulated markets (i.e. ATSS).</p> <p>4. The legislative decree 58/1998 makes the provision of investment services by intermediaries conditional upon authorization by the Consob.</p> <p>5. Consob is responsible for authorizing financial intermediaries and for setting conduct of business rules. The Bank of Italy is responsible for prudential regulation of investment firms.</p> <p>6. Clearing and Settlement Systems, as well as Central Depository, are regulated and supervised by Consob and Bank of Italy.</p>	<p>however the development of some more specific guidelines is under consideration.</p>		<p>daily basis (and on real time) the trading activity in the regulated markets and the conduct of intermediaries when trading in the market (in order to detect anomalous trading patterns, concentration of trades, etc.).</p> <p>5. All trading data are collected and analyzed by the market surveillance unit on a daily basis.</p>	<p>the authorization to manage the market .</p>	
<p>Minister of Finance (Japan)</p>	<p>When any securities company plans to develop a securities dealers association, such securities company shall obtain authorization from the Minister of Finance and the Financial Reconstruction Commission (FRC). Article 68 of Securities and Exchange Law.</p> <p>When any securities company plans to develop a securities exchange, such securities company shall obtain license from the Minister of Finance and FRC. 81.</p> <p>When the Minister of Finance and FRC receives an application for license or authorization, the Minister and FRC shall examine such application to determine whether the provision of its articles of incorporation and regulations conform to laws and are adequate to ensure the fairness and facilitate trading, and to protect the investors. 70 83</p>	<p>Securities Dealers Association and Securities Exchange</p> <p>Each securities dealers association and securities exchange shall state in its articles of incorporation, matters relating to investigations, disciplinary actions, its articles of incorporation, regulations and rules of good-faith trading. 74 88</p> <p>Each securities dealers association (this applies only to the association which establishes the over-the-counter securities market) and securities exchange shall state matters necessary for trading in its regulations. 76 108</p> <p>The Minister of Finance and FRC</p> <p>The Minister of Finance and FRC issue regulations which provide the procedure of the license, authorization, approval and notification.</p>	<p>Securities Dealers Association</p> <p>When any securities dealer association wishes to change its articles of incorporation, it shall obtain authorization of the Minister of Finance and FRC. 74</p> <p>When any securities dealer association wishes to change its regulations (this only applies to regulations relating to the over-the-counter securities market), it shall obtain authorization of the Minister of Finance. 76</p> <p>When any changes have occurred in other regulations, any association shall notify the Minister of Finance to that effect. 74</p> <p>Securities Exchange</p> <p>When any securities exchange wishes to change its articles of incorporation or regulations (this applies only to regulations relating to services ensuring the fairness of trading), it shall obtain the authorization of the Minister of Finance and FRC. 85-2</p> <p>When any securities exchange wishes to change its regulations (excluding regulations relating to services ensuring the fairness of trading) or rules for brokerage agreements, it shall obtain authorization of the Minister of Finance. 85-2</p> <p>When any changes have occurred in other regulations, any securities exchange shall</p>	<p>Securities Dealers Association and Securities Exchange</p> <p>Each securities dealer association and securities exchange investigates under the provisions of its articles of incorporation, compliance with rules and takes disciplinary actions. 74 88</p> <p>Each securities dealer association and securities exchange monitors volume and prices, etc. of securities traded each day. 79-3 79-4 122 123</p> <p>The Minister of Finance and FRC</p> <p>When the Minister of Finance and FRC deem it necessary and appropriate in the public interest or for the protection of investors, the Minister and FRC may order any securities dealer association, securities exchange, or the issuer of securities to submit reports, or inspect such securities dealer association or securities exchange. 79-14 154</p> <p>The Minister of Finance</p> <p>Each securities dealer association and securities exchange shall report to the Minister of Finance, volume and prices, etc. of securities traded each day. 79-4 123</p> <p>Surveillance Commission (SESC)</p> <p>In investigating irregularities, SESC may ask</p>	<p>Securities Dealers Association and Securities Exchange</p> <p>Each securities dealer association and securities exchange, under the provisions of its articles of incorporation, may impose a fine on any member who violates rules, may take other disciplinary action against a member, or expel such member. 79-7 98</p> <p>The Minister of Finance and FRC</p> <p>The Minister of Finance and FRC may,</p> <ol style="list-style-type: none"> 1) order any securities dealer association to make changes to its articles of incorporation that FRC deems necessary and appropriate to ensure the fairness of trading, or to protect investors, 79-12 2) order any securities exchange to make such changes in its articles of incorporation and regulations (this applies only to regulations relating to services ensuring the fairness of trading), 155-2 and 3) order any securities dealer association or securities 	

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			notify the Minister of Finance to that effect. 85-2	any suspects or witnesses to report personally, interrogate witnesses, and inspect their property. 210 In investigating irregularities, SESC may, after obtaining written permission from the court in advance, visit, inspect and search the premises or seize property. 211	exchange to discharge its executives, when such securities dealer association or securities exchange has violated the laws, disciplinary actions taken under the laws, its articles of incorporation or regulations, or when such securities dealer association or securities exchange, notwithstanding the fact that any of its member or the issuer	
Ministry of Finance (Japan)					of securities has violated the law, disciplinary actions taken under the laws, its articles of incorporation or regulations, or has committed an act which is contrary to the rules of good-faith trading, fails to exercise its powers to take necessary actions 79-13 155 The Minister of Finance The Minister of Finance may order any securities exchange to make such changes in its regulations (excluding regulations relating to services ensuring the fairness of trading) and business practices, as the Minister may deem necessary and appropriate to ensure the fairness of trading, or to protect the investors. 155-2	
STE (Securities Board of the Netherlands)	Pursuant to the Act on the Supervision of Securities Trade 1995 (hereinafter referred to as the Securities Act) securities exchanges must be recognized by the Minister of Finance upon the recommendation of the STE. Recognized status will be granted provided that the operator of the securities exchange is established in the Netherlands and the operation of the securities exchange, the rules which are to apply to the said securities exchange, their application, and their enforcement meet the conditions necessary to ensure two objectives, that is: an adequate functioning of the securities markets and the		The operator of a securities exchange must notify the STE in advance of any change in rules or in their enforcement. The STE reviews these changes to determine whether they are in accordance with the two above-mentioned objectives and the relevant European Directives. The STE may issue instructions to the operator of a securities exchange in relation to their rules, application and enforcement.	The supervision of the securities exchange by the STE include the following main areas. <i>Listing</i> The securities exchange is the competent authority for listing. Listing rules and the compliance with these rules are subject to supervision by the STE. The securities exchange can only grant dispensation from its listing regulations after notification to the STE. <i>Trading</i> The securities exchange must notify the STE in advance of any changes in its trading system. Furthermore, trading disruptions	The STE may issue instructions to the operator of a securities exchange in the case of a violation of rules by the exchange. The operator must comply with these instructions within a time limit to be set by the STE. Besides instructions, it is expected that this year the STE will obtain the power to impose administrative fines and penalties on institutions subject to supervision in case of non-compliance with statutory regulations. The Minister of Finance may withdraw recognized status or a	

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	<p>position of the investors in these markets. As part of the recognition the following issues will be considered: fit and properness of the management board of the exchange (including subsidiaries) and the properness of the supervisory board, financial guarantees, adequate clearing and settlement systems and the requirements set for safeguarding adequate compliance with the rules and regulations of the exchange. Restrictions may be imposed on, and conditions attached to, the granting of recognized status in the interest of the above-mentioned two objectives.</p> <p>If the holder of the securities exchange is established outside the Netherlands there are two possibilities:</p> <p>1) the securities exchange is a regulated market as referred to in Article 1(13) of the Investment Services Directive. In that case the securities exchange is exempted from the recognition rule but can be subject to rules set out by the Minister of Finance in the interest of the above mentioned two objectives.</p>			<p>must be reported to the STE as well as significant deviating price and turnover figures. These figures are investigated by the STE in respect of market manipulation and insider dealing.</p> <p><i>Market Participants</i></p> <p>As part of its ongoing supervision, the STE supervises compliance by market participants with respect to fit and properness provisions, financial guarantees, management and information. For this purpose, the STE periodically evaluates the reports of the firms, and can order special reports and conduct on-site examinations.</p> <p><i>Rules</i></p> <p>See paragraph AApproval of Changes</p>	<p>dispensation, should insufficient guarantees be furnished for the operation of the securities exchange in question, in the interest of the proper operation of the securities markets and the position of the investors in these markets, or should the securities exchange not observe (in a satisfactory manner) the rules or regulations, restrictions or instructions issued by or pursuant to the Securities Act.</p>	
<p>STE (Securities Board of the Netherlands)</p>	<p>2) the securities exchange is not a regulated market as referred to in Article 1 (13) of the Investment Services Directive. In that case the securities exchange must obtain a dispensation from the recognition rule.</p> <p>Again, the Minister of Finance can impose restrictions on and attach conditions to a dispensation in the interest of the above mentioned two objectives.</p> <p>Brokers and dealers have to obtain a licence from the STE in order to perform their services in or from the Netherlands. A licence will be granted provided that the applicant meets certain rules with regard to fit and properness, financial guarantees, management and establishment of the head office and information to be supplied to the public. A broker or dealer who wants to perform his services on an exchange, must also meet the requirements of the exchange</p>			<p><i>Clearing and Settlement</i></p> <p>The STE and the Dutch Central Bank developed a supervisory framework with respect to the different clearing systems and operators. This framework is based on minimum standards for cross-border and multi-currency netting and settlement schemes, the so-called ALamfalussy standards. After the initial review, clearing and settlement systems are subject to regular supervision by the STE.</p> <p><i>Automated systems</i></p> <p>The securities exchange must inform the STE regularly on EDP-audit findings regarding relevant systems as well as on its problem, change and configuration management. Issues with regard to these subjects are discussed periodically.</p> <p><i>Enforcement</i></p> <p>The securities exchange must inform the</p>		

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	in question. These requirements concern additional prudential requirements and exchange specific requirements.			STE on breaches of the Securities Act and breaches of exchange rules by issuing companies and market participants and on their response of those breaches. Furthermore, the securities exchange has to report to the STE on investor complaints and the way in which these complaints are resolved.		
Comisión Nacional del Mercado de valores (CNMV). Spain	<p>Approval on an exchange</p> <p>The Government is vested with the authority to approve any official secondary market. In a broad sense, the Government may lay down, upon proposal from CNMV, regulations governing the organisation and operative system of the official regulated market.</p> <p>All requirements of organisational structure, transparency, price formation process, risk management are individually analysed.</p> <p>Criteria for market membership</p> <p>So far, only brokers and broker-dealers can be members of the exchanges. Credit institutions are also allowed in the derivatives market and the private bond market, called AIAF.</p> <p>CNMV is solely responsible for the registration of broker and broker-dealers.</p> <p>To be member of a regulated market, an organisation, personnel and materials means theoretically suited to the nature and volume of its business.</p>	<p>Official secondary markets and clearing houses are responsible for their internal organisation, including: trading rules, tariffs and commissions that the governing body charge for its service, listing requirements for admission.</p> <p>The internal procedures can be overridden by the CNMV if rules are contrary to the SMA and other applicable laws and regulations</p>	Changes can be vetoed by the CNMV if they are contrary to the SMA and other applicable laws and regulations.	Article 13 of the Spanish Securities Market Act (SMA) states that the CNMV shall oversee the transparency of the securities markets, the correct fixing of the prices and the protection of investors. To ensure the fairness and integrity in the market, CNMV monitors and supervises listed companies, secondary securities markets and their participants.	<p>In accordance with the SMA, the CNMV has the responsibility for investigating any possible violation of applicable laws or regulations relating to the securities markets and their participants under the supervision of the CNMV.</p> <p>The CNMV can impose of sanctions for serious and minor infringements. Extremely serious infringements are dealt with by the Minister of Economy and Finance on recommendation by the CNMV.</p>	
FSA (United Kingdom)	<p>The Financial Services Act 1986 sets out the criteria an organized market must meet to become a Recognised Investment Exchange (>RIE=). These criteria, set out in Schedule 4 of the Act, require the exchange (in summary) to:</p> <ul style="list-style-type: none"> ! have adequate financial resources; ! have rules that ensure that business is conducted in an orderly manner so as to provide proper protection to investors; ! admit to trading only investments in which there is a proper market; 	The FS Act provides the FSA with extensive powers to issue guidance in areas of public interest e.g. its interpretation of the recognition criteria. Such guidance is non-binding.	RIEs (and RCHs) are free to make, modify or delete rules provided that, as a result of any changes , they continue to meet the recognition criteria. The one exception relates to changes to default rules. Proposed changes must be notified to the FSA at least 14 days prior to their taking effect. In practice, RIEs (and RCHs) informally consult with the FSA before proposing rule changes publicly. The FSA may comment on proposals either before or during formal consultation with RIEs members.	<p>Each recognised body (whatever exchange or clearing house) is required to have procedures for monitoring compliance with its rules.</p> <p>The FSA conducts its oversight of recognised bodies (>RBs=) in a variety of ways. These include:</p> <ul style="list-style-type: none"> ! initial assessment, and subsequent monitoring of RB=s annual regulatory plans; ! monitoring of information supplied on a regular bases under Notification 	<p>The FSA=s main enforcement responsibility in relation to exchanges is to ensure that they remain in compliance with the recognition criteria.</p> <p>Where the FSA determines that an exchange fails to comply with requirements, it may:</p> <ul style="list-style-type: none"> ! apply to a Court for an order requiring the exchange to comply; or ! derecognise the exchange 	

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	<ul style="list-style-type: none"> ! maintain records of transaction; ! have arrangements (of its own or with a recognised clearing house) to ensure the performance of transactions; ! have procedures to enforce compliance with its rules; ! have arrangements for dealing with complaints; and ! be ready to promote high standards of integrity and fair dealing and to co-operate with other regulatory authorities. <p>The FS Act requires all firms conducting investment business in the UK to be authorized in the UK, unless operating under an EU >passport= or a specific exemption set out in the FS Act.</p> <p>The Financial Services and Markets Bill, currently passing through Parliament will maintain the present process for recognising exchanges but will provide greater flexibility for modifying the recognition criteria.</p>			<p>Regulations;</p> <ul style="list-style-type: none"> ! regular meetings and day-to-day contact with RB staff; and ! occasional in-depth assessments of specific aspects of an RB e.g. procedures for admitting securities to trading, general efficiency of the market. This work may be conducted by FSA staff or external consultants (the latter being hired at an RB=s or the FSA=s expense, depending on circumstances) 	<p>(subject to leave from HM Treasury).</p> <p>The new Financial Services and Market Bill provides for the FSA to be given a >power of direction=, enabling it to order an exchange (or clearing house) to alter its rules.</p> <p>HM Treasury also has a power of direction, enabling it to require an exchange to alter any rule the Director General of Fair Trading considers to be anti-competitive (and which cannot be justified on grounds of investor protection).</p>	
<p>SEC (United States)</p>	<p>SROs must register with the Commission pursuant to Section 6 (national securities exchanges), Section 15A (securities associations), Section 15B (Municipal Securities Rulemaking Board), or Section 17A (clearing agencies) of the Act.</p> <p>The Commission may not grant registration unless findings are made that the SRO will satisfy specific statutory requirements. Among other things, the SROs are required to enforce compliance by their members with the securities laws, to insure fair representation of their members and to allocate reasonable dues, fees, and other charges among their members.</p> <p>Pursuant to Section 19(h) of the Exchange Act, the Commission can suspend or revoke the registration of an SRO, or censure or impose limitations upon the activities of the SRO, if the SRO has violated the Act or its own rules or has failed to enforce compliance by its members with such provisions.</p>		<p>Rule Filings</p> <p>Pursuant to Section 19(b) of the Exchange Act, SROs must file with the Commission each proposed change to their rules.</p> <p>SRO rules include the SROs' constitution, bylaws, rules of practice, policy statements, proposed new products, and any material aspect of the operation of the facilities of the SROs.</p> <p>The Commission must publish notice of such filings and afford interested persons an opportunity to submit written data, views, and arguments concerning the filings. The Commission reviews the rule filings for consistency with the Exchange Act, in particular whether the rule filing has significant competitive implications or raises investor protection concerns. The Commission may approve such filings, or start disapproval proceedings, which would allow for an opportunity for a hearing. Action by the Commission is subject to time</p>	<p>Inspections</p> <p>The Commission conducts routine inspections of SROs to evaluate how the SROs are performing their regulatory responsibilities. The following describes the key areas reviewed by the Commission in connection with a routine inspection of an exchange or the NASD:</p> <p><i>1. Listing Program</i></p> <p>Listing of securities in the United States is a two-step process: Issuers who want to sell their securities in interstate commerce first must file a registration statement with the SEC prior to issuing the securities.</p> <p>After a security is registered with the SEC, the issuer must decide whether and where the securities will be listed (ie Nasdaq or the exchanges) and must comply with the listing standards of that particular market.</p> <p>The exchanges and Nasdaq have listing standards that include, among other things, the registration of the security with the SEC,</p>	<p>Disciplinary Program</p> <p>The SROs are required to enforce compliance by their members with their own rules and with the federal securities laws. Pursuant to Section 19(d) of the Exchange Act, an SRO must file a notice with the SEC if it imposes any disciplinary action on a member, denies membership to any applicant, or prohibits or limits access to services offered by the SRO.</p> <p>Any of these actions is subject to SEC review either upon the SEC's own motion or upon appeal by the aggrieved person.</p>	<p>Principal statute is Securities Exchange Act of 1934.</p>

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	<p>The Commission may review any disciplinary action taken by an SRO.</p> <p>The Commission also may disapprove the admission to SRO membership of a participant having certain statutory disqualifications.</p>		limits under the Exchange Act.	<p>minimum market capitalization, minimum number of shareholders, number of publicly-held shares, minimum net income and size of assets. Exchanges and Nasdaq also have maintenance standards in these areas with which issuers must comply on a continuing basis. In addition, a national securities exchange may extend unlisted trading privileges to any security listed and registered on another national securities exchange.</p> <p>The Commission staff inspects SROs to determine whether they are enforcing their listings and maintenance standards.</p> <p>2. Supervision of Brokers and Dealers</p> <p>The SEC oversees SRO examinations of their member firms. For example, the Commission performs examinations of broker-dealers and compares its report and findings with that of the SRO.</p>		
<p>SEC (United States)</p>	<p>Brokers and dealers must register with the Commission (unless exempt from such registration) if they effect transactions in any security (other than exempted securities such as commercial paper, bankers' acceptances, or commercial bills). In addition, any broker or dealer registered with the Commission also must be a member of a registered securities association unless it effects transactions in securities solely on a national securities exchange of which it is a member. The National Association of Securities Dealers is currently the only registered securities association. To avoid duplicative examinations, a designated examining authority is identified for broker-dealers that are members of more than one SRO.</p>			<p>These oversight examinations are conducted on firms examined by an SRO within the past year to determine if the SRO looked at the most significant risk areas and found all substantive violations that occurred during its period of review.</p> <p>Initial responsibility is on the SROs to assure compliance with the federal securities laws and SRO rules. The Commission does not routinely inspect every broker and dealer. To avoid unnecessary duplication in examinations, the Commission conducts oversight examinations of the same broker-dealers once every three years unless concerns exist about a firm's operations that warrant that an examination be done sooner. This process is an important means of quality control over the SROs' examination programs.</p> <p>3. Surveillance Program</p> <p>SROs use audit trails as surveillance and investigative tools to help detect and investigate conduct that may violate federal securities laws or SRO rules.</p> <p>In addition, SROs monitor real-time trading through their individual computerized</p>		

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				surveillance systems such as stock watch programs. These programs monitor trading on a real-time basis, analyze unusual trading activity to determine its cause, and coordinate inquiries and analysis. For example, on the NYSE, Amex, and Nasdaq, computers model trading characteristics of individual securities and flag aberrant trading information which is referred to surveillance analysts for possible enforcement proceedings.		
SEC (United States)				<p>The Commission in turn reviews the SROs' audit trails and computerized surveillance systems for accuracy and usefulness. In particular, the Commission analyzes the parameters the SROs use in their computerized surveillance systems to assure that the systems provide meaningful results. The Commission also reviews surveillance files to assure that investigations are conducted appropriately and referred for further action as action as necessary.</p> <p>4. Automated Systems</p> <p>The Commission also oversees the SROs' automated systems. The Commission's automation review policy calls for the SROs to establish comprehensive planning, testing, and assessment programs to determine systems capacity and vulnerability. The Commission recommended that the SROs establish current and future capacity estimates conduct capacity stress tests and obtain annual independent assessments of systems to determine whether they can perform adequately.</p> <p>The Commission principally relies on the SRO's audit program and its own work analysis to monitor the status of SRO systems operations; in particular, computer operation such as operations processes and physical security of the data centers and their staffs; telecommunications monitoring; adequacy of data security; methodologies regarding the development and/or maintenance of information systems; capacity planning and testing to ensure continued capability of systems to handle</p>		

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				<p>varying amounts of data in a timely fashion; and contingency planning to resolve and respond to problems dealing with systems failures.</p>		
<p>SEC (United States)</p>				<p>The Commission performs automation reviews using a risk-targeted approach. An examination will be conducted when the risk analysis indicates an area of particular vulnerability, such as, for example, significant turnover in technology or audit staff or prolonged gaps in key technology positions at an SRO, frequent systems problems, a substantial decrease in demand on systems capacity or a changeover or introduction of a substantial new systems at an SRO.</p> <p>At the conclusion of an examination, an exit conference is usually held in which the preliminary results of the inspection are discussed with SRO staff. The Commission then sends an inspection report which contains the staff's findings and recommendations for action to be taken by the SRO to address program deficiencies. Each inspection report requests that the SRO respond and describe any action taken or planned to address the deficiencies cited in the report, including a time frame for the implementation.</p> <p>The Commission staff reviews the SRO response to evaluate the adequacy of any proposed action and will notify the SRO if additional information or action is required. The staff also meets regularly with the SROs to follow up on recommendations of inspection reports.</p> <p>Finally, the staff will confirm that appropriate action has been implemented by the SRO during subsequent inspections of the SRO or by conducting special follow-up inspections where warranted.</p>		