



CIRCULAR

CIR/MRD/DP/ 16 /2013

May 21, 2013

To,

All Stock Exchanges.

Dear Sir / Madam,

Subject: Broad guidelines on Algorithmic Trading

Please refer to SEBI Circular No.CIR/MRD/DP/09/2012 dated March 30, 2012 on 'Broad guidelines on Algorithmic Trading'.

2. SEBI has received various suggestions with regard to the requirement of system audit of trading algorithm / software used by stock brokers / trading members. After due examination of the suggestions in consultation with the Technical Advisory Committee, it has been decided to revise the requirement as follows:

2.1. The stock brokers / trading members that provide the facility of algorithmic trading shall subject their algorithmic trading system to a system audit every six months in order to ensure that the requirements prescribed by SEBI / stock exchanges with regard to algorithmic trading are effectively implemented.

2.2. Such system audit of algorithmic trading system shall be undertaken by a system auditor who possess any of the following certifications:

- (a) CISA (Certified Information System Auditors) from ISACA;
- (b) DISA (Post Qualification Certification in Information Systems Audit) from Institute of Chartered Accountants of India (ICAI);
- (c) CISM (Certified Information Securities Manager) from ISACA;
- (d) CISSP (Certified Information Systems Security Professional) from International Information Systems Security Certification Consortium, commonly known as (ISC)².

2.3. Deficiencies or issues identified during the process of system audit of trading algorithm / software shall be reported by the stock broker / trading member to the stock exchange immediately on completion of the system



audit. Further, the stock broker / trading member shall take immediate corrective actions to rectify such deficiencies / issues.

2.4. In case of serious deficiencies / issues or failure of the stock broker / trading member to take satisfactory corrective action, the stock exchange shall not allow the stock broker / trading member to use the trading software till deficiencies / issues with the trading software are rectified and a satisfactory system audit report is submitted to the stock exchange. Stock exchanges may also consider imposing suitable penalties in case of failure of the stock broker / trading member to take satisfactory corrective action to its system within the time-period specified by the stock exchanges.

3. In order to further strengthen the surveillance mechanism related to algorithmic trading and prevent market manipulation, stock exchanges are directed to take necessary steps to ensure effective monitoring and surveillance of orders and trades resulting from trading algorithms. Stock exchanges shall periodically review their surveillance arrangements in order to better detect and investigate market manipulation and market disruptions.

4. As directed vide circular dated March 30, 2012 stock exchanges have implemented a framework of economic disincentives for high daily order-to-trade ratio of orders placed from trading algorithms by prescribing penalties in form of '*charges to be levied per algo orders*' at various levels of daily order-to-trade ratio. The penalty rates specified by the stock exchanges have been reviewed and in order to provide sufficient deterrence, stock exchanges are directed to double the existing rates of '*charges to be levied per algo orders*' specified in their circulars / notices.

5. In order to discourage repetitive instances of high daily order-to-trade ratio, stock exchanges shall impose an additional penalty in form of suspension of proprietary trading right of the stock broker / trading member for the first trading hour on the next trading day in case a stock broker / trading member is penalized for maintaining high daily order-to-trade ratio, provided penalty was imposed on the stock broker / trading member on more than ten occasions in the previous thirty trading days.

6. The circular shall be applicable with effect from May 27, 2013.

7. Stock Exchanges are directed to:

7.1. take necessary steps and put in place necessary systems for implementation of the above.

7.2. make necessary amendments to the relevant bye-laws, rules and regulations for the implementation of the above decision.



भारतीय प्रतिभूति और विनिमय बोर्ड
Securities and Exchange Board of India

7.3. bring the provisions of this circular to the notice of the stock brokers / trading members of the stock exchange and also disseminate the same on their website.

8. This circular is being issued in exercise of powers conferred under Section 11 (1) of the Securities and Exchange Board of India Act, 1992 to protect the interests of investors in securities and to promote the development of, and to regulate the securities market.

Yours faithfully,

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