



Summary of the SEC Proposed Rule on Sponsored Access

Proposed SEC Rule on Sponsored Access (Summary)

On January 13, 2010 the SEC voted unanimously to propose a new rule that would effectively **prohibit broker-dealers from providing customers with "unfiltered" or "naked" access to an exchange or alternative trading system (ATS).**

The SEC's proposed rule would require broker-dealers to establish, document and maintain a system of risk management controls reasonably designed to manage risks related to its market access, including:

- **access on behalf of sponsored customers**
- **all flow conducted as part of an agency business**
- **its own internal trade flow including proprietary trading on behalf of the broker**

Broker-dealers would be required to:

- **Prevent the entry of orders** that exceed appropriate **pre-set credit or capital thresholds**, or that appear to be erroneous.
- **Ensure compliance** with all regulatory requirements applicable in connection with market access.
- **Apply risk controls automatically on a pre-trade basis** before orders route to an exchange or ATS.
- Maintain **direct and exclusive control over the risk management function**, without delegation of this critical function to the customer or another third party. **NOTE: The use of FTEN's risk management solutions does not constitute "delegating to a third party" nor does it transfer risk management and compliance responsibilities to FTEN – these responsibilities are retained by and under the exclusive control of FTEN's clients, the Broker Dealers.**
- Employ **market-wide risk management controls-- across venues and asset classes.**
- Establish, document and maintain a system for regularly **reviewing the effectiveness of its risk management controls** and for promptly addressing any issues.
- Establish a supervisory system, including an **annual CEO certification**, to assure the ongoing effectiveness of its controls.

Types of Trading Risk Controls Proposed by the SEC for Compliance

- Compliance Controls (RegSHO and restricted stocks)
- Erroneous "Fat Finger" Orders (Single Order Value, Single Order Quantity)
- Credit and Capital Limits
- Account Level Positions (across venues and asset classes)













Best Practices for Implementing a Broker-Managed Sponsored Access Risk Systems

Based on client experience over the last 8 years, the following list represents best practices in risk management:

- Beginning of Day (BOD) files are needed to accurately track intra-day client positions.
- Pre-trade Order Level risk checks are needed to guard against fat-finger mistakes.
- Real-time Account Level risk checks are needed to protect committed capital and P&L from erroneous exposure.
- Real-time Account Level risk checks are needed to protect capital from erroneous exposure across multiple venues
- The ability to stop erroneous trades by account in real-time is needed to protect capital and maintain uninterrupted service for accounts that are not in breach under the same Member ID.
- The ability to adapt risk checks to accommodate changes in regulations and evolving business needs.

Types of Sponsored Access Risk Systems

Many exchanges that offer Sponsored Access programs provide risk management tools to monitor and protect trading activity that occurs on their own venue at the order level. As trading strategies move across liquidity venues, exchange-neutral, cross-venue risk tools are available to provide cross-market awareness and account level control.

Best Practices	Exchange Risk Tools	Exchange Neutral Risk Tools
Process Beginning of Day Positions		
Pre-Trade Order Level Risk Checks		
Real-time Account Level Risk Checks		
Cross-Venue Awareness		
Stop Trading by Account		
Change Management Capabilities		

KEY:  Not offered  Offered  Not Always Offered