

Frequently asked questions (FAQs) relating to the Highfrequency Trading Act

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1) When does the authorisation requirement for highfrequency trading as defined in the High-frequency Trading Act (hereinafter High-frequency Trading) take effect?

The High-frequency Trading Act entered into effect on 15 May 2013. However, with respect to the authorisation requirement, the Act stipulates transitional periods for applying for an authorisation (see section 64p of the Banking Act (*Kreditwesengesetz – KWG*). A transitional period of six months, i.e. until 14 November 2013, for submitting an application for authorisation is stipulated. For enterprises that are not domiciled in Germany and that are not enterprises within the meaning of section 53b (1) sentences 1 and 2 of the KWG, a transitional period of nine months until 14 February 2014 is stipulated.

2) When do the follow-up requirements in accordance with the KWG (i.e. capital requirements, reporting requirements, organisational requirements, etc.) take effect?

With respect to the follow-up requirements, BaFin will not impose any supervisory regime before it has received a complete application for authorisation – nor will it do so retroactively. A transitional period of six or nine months for submitting such an application for authorisation is stipulated in section 64p of the KWG.

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3) When do the follow-up requirements in accordance with the Securities Trading Act (Wertpapierhandelsgesetz – WpHG) take effect?

For enterprises that will additionally be subject to the obligations under the WpHG as a result of the authorisation requirement, BaFin will also not impose any supervisory regime before it has received a complete application for authorisation – nor will it do so retroactively.

4) Are there any transitional provisions for enterprises intending to use the European passport?

Yes. Enterprises that are domiciled in a signatory to the Agreement on the European Economic Area (EEA) and already hold an authorisation there for trading on an own-account basis (cf. No. (3) of Section A of Annex I to the MiFID), but that have yet to use the European passport in Germany (notification procedure) may use the six-month transitional period to obtain authorisation to operate in Germany by way of the prescribed notification procedure.

Enterprises that have not obtained this authorisation after six months (for instance, if the notification procedure was not initiated in due time by their respective home country authorities) may no longer operate such business in Germany without BaFin's approval.

Enterprises that are domiciled in a signatory to the Agreement on the European Economic Area, have been granted authorisation for trading on an own-account basis (cf. No. (3) of Section A of Annex I to the MiFID) in their home country and are already engaged in an activity under the European passport system in Germany may continue their Highfrequency Trading activities without submitting any further application. In such cases, however, the home supervisor is required to have submitted to BaFin a notification in accordance with Article 31 of the MiFID for cross-border activities or a notification in accordance with Article 32 of the MiFID for High-frequency Trading through a branch.

5) Will a trading participant who already engages in Highfrequency Trading in Germany, who will be subject to the authorisation requirement in future and who does not currently have authorisation, be liable to prosecution if that participant continues to engage in Highfrequency Trading in Germany?

No, a trading participant will not initially be liable to prosecution if it continues to engage in High-frequency Trading in Germany. The purpose of the transitional periods is to allow trading participants to adapt to the new legal requirements. For this reason, there are initially no criminal

consequences if a trading participant continues to engage in Highfrequency Trading. However, this is preconditioned on the trading participant's compliance with the time limitations applicable to it under section 64p of the KWG.

6) When do the organisational requirements in accordance with section 33 (1a) of the WpHG (in conjunction with section 9a (1) of the Investment Act (Investmentgesetz – InvG)) take effect for investment services enterprises, asset management companies (Kapitalanlagegesellschaften) and self-managed investment stock corporations (Investmentaktiengesellschaften)?

Article 7 of the High-frequency Trading Act stipulates that these organisational requirements will take effect six months after the promulgation of the High-frequency Trading Act. There is also a transitional period of six months in this respect for investment services enterprises, asset management companies and self-managed investment stock corporations.

7) Can private persons also be subject to the authorisation requirement?

In principle, yes. For example, if, as a direct or indirect participant in a domestic organised market or multilateral trading facility using highfrequency algorithmic trading technology, they purchase or sell on an own-account basis financial instruments commercially or on a scale which requires a commercially organised business undertaking. Persons are deemed to be acting on a commercial basis if the business is established for a certain duration and conducted with the intention of generating profits.

8) Can trading participants who are domiciled in Germany and who have authorisation to engage in proprietary trading and have thus far been engaging in Highfrequency Trading at German trading venues continue doing so without having to submit a further application?

Yes. In future, the authorisation to engage in proprietary trading will also cover High-frequency Trading under the expanded definition of proprietary trading. Institutions that already have unlimited authorisation to engage in proprietary trading under section 1 (1a) sentence 2 no. 4 of the KWG do not need any additional authorisation to engage in Highfrequency Trading.

9) Can trading participants who are domiciled in Germany and who are already providing financial services but who do not have any authorisation to engage in proprietary trading and are at present already engaging in High-frequency Trading at German trading venues continue engaging in High-frequency Trading after the High Frequency Trading Act enters into force?

Yes, on the condition that they have submitted a complete application for authorisation to BaFin by 14 November 2013 (cf. section 64p sentence 1 of the KWG). Then the authorisation to engage in proprietary trading will be deemed provisionally granted until BaFin has reached a decision on the application. Pursuant to section 33 (5) of the KWG, BaFin will notify the applicant within six months from the date on which all the documents required for an application for authorisation under section 32 (1) sentence 2 of the KWG have been submitted as to whether authorisation will be granted or not. Where applicable, applicants should contact BaFin early in the process to clarify any questions about what documents are required for an application for authorisation.

10) Can trading participants who are domiciled in Germany, who have not thus far provided financial services within the meaning of the KWG, but who are already engaging in High-frequency Trading at German trading venues, and who become a financial services institution due to the expansion of the term "proprietary trading", continue engaging in High-frequency Trading after the High Frequency Trading Act enters into force?

Yes, on the condition that they have submitted a complete application for authorisation to BaFin by 14 November 2013 (cf. section 64p sentence 1 of the KWG). Then the authorisation to engage in proprietary trading will be deemed provisionally granted until BaFin has reached a decision on the application. Pursuant to section 33 (5) of the KWG, BaFin will notify the applicant within six months from the date on which all the documents required for an application for authorisation under section 32 (1) sentence 2 of the KWG have been submitted as to whether authorisation will be granted or not. Where applicable, applicants should contact BaFin early in the process to clarify any questions about what documents are required for an application for authorisation.

11) Can foreign trading participants who are domiciled in EEA countries, who have been granted an authorisation to engage in proprietary trading in their home country, are engaged in an activity in Germany under the European pass-

port system, and who already engage in High-frequency Trading at German trading venues, continue their High-frequency Trading without submitting any further application?

Yes. However, the home country supervisor is required to submit to BaFin a notification in accordance with Article 31 of the MiFID for crossborder activities or a notification in accordance with Article 32 of the MiFID for High-frequency Trading through a branch. The notification must relate to the service of proprietary trading (cf. No. (3) of Section A of Annex I of the MiFID) and name the financial instruments to which the proprietary trading relates. As the notification is required to be submitted via the home supervisor, the home country supervisor should be contacted with regard to the relevant process. The information on notifications is standard across the EU and is based on the services, products and ancillary services under Annex I of the MiFID.

12) What steps can be taken by foreign trading participants from the EEA who have been granted an authorisation to engage in proprietary trading in their home country (in accordance with No. (3) of Section A of Annex I of the MiFID), but are not engaged in an activity in Germany under the European passport system and who already engage in High-frequency Trading at German trading venues?

Such enterprises may engage in High-frequency Trading in Germany under the European passport system. However, BaFin must be notified. The prescribed notification procedure must be concluded within six months of the date on which the High-frequency Trading Act entered into force. Otherwise, the enterprise may continue to engage in such activity in Germany only with the consent of BaFin.

13) What steps can be taken by foreign trading participants from the EEA who have not been granted an authorisation to engage in proprietary trading in their home country (in accordance with No. (3) of Section A of Annex I of the MiFID), but who already engage in High-frequency Trading at German trading venues?

Enterprises of this kind must establish a subsidiary or a branch in Germany. In such cases, the transitional period under section 64p sentence 2 of the KWG applies, in other words, provisional authorisation shall be deemed to have been granted if a complete application for authorisation has been submitted by 14 February 2014. In these cases, BaFin will not supervise compliance with follow-up requirements before receiving a

complete application for authorisation, for which a transitional period of nine months is prescribed. Alternatively, enterprises that have been granted an authorisation in their home country but have no authorisation capable of serving as a passport within the meaning of the MiFID may apply for an exemption under section 2 (4) of the KWG. Such enterprises have nine months to clarify whether BaFin will grant them an exemption from the authorisation requirement under section 32 (1) of the KWG in accordance with section 2 (4) of the KWG and the other exemptions set forth in section 2 (4) of the KWG. Before granting an exemption, BaFin will assess whether the applicable supervisory regime to which the applicant is subject in its home country is essentially equivalent, and will clarify co-operative arrangements with the competent home country authorities. For their own benefit, enterprises should submit exemption applications very early. Enterprises that fail to obtain an exemption on time must have submitted a complete application for authorisation after expiry of the nine month period under section 64p sentence 2 of the KWG, or discontinue High-frequency Trading in Germany. Enterprises that intend to apply to the competent supervisory authority in their home country for an authorisation to engage in proprietary trading in order to then use the European passport to engage in Highfrequency Trading in Germany should initiate contact with BaFin early during the authorisation process in their home country in order coordinate any bilateral solutions if required. Otherwise, they must discontinue this activity in Germany after expiry of the six-month period under section 64p sentence 1 of the KWG.

14) Can trading participants who are domiciled in a country outside the EEA who already engage in Highfrequency Trading at German trading venues, but currently have no authorisation to engage in proprietary trading, continue engaging in High-frequency Trading after the High Frequency Trading Act enters into force?

Yes, on the condition that they have submitted a complete application for authorisation by 14 February 2014. In order to obtain an authorisation, such trading participants must establish a subsidiary or branch in Germany. Provided a complete application for authorisation was submitted to BaFin by 14 February 2014, provisional authorisation to engage in proprietary trading shall be deemed granted until such time as BaFin makes a decision on the application. Pursuant to section 33 (5) of the KWG, BaFin will notify the applicant within six months from the date on which all the documents required for an application for authorisation under section 32 (1) sentence 2 of the KWG have been submitted as to whether authorisation will be granted or not. Where applicable, applicants should contact BaFin early in the process to clarify any questions

about what documents are required for an application for authorisation.

15) Can trading participants who are domiciled in a country outside the EEA and who engage in High-frequency Trading in Germany benefit from the European passport?

Yes, provided the trading participant has a subsidiary in an EEA country which is authorised there as a credit or financial services institution, and such authorisation also extends to proprietary trading (trading on an own-account basis within the meaning of No. (3) of Section A of Annex I of the MiFID). If High-frequency Trading is conducted through such a subsidiary, trading participants from non-member countries can also benefit indirectly from the European passport. This is conditional upon the subsidiary domiciled in the EEA country meeting the requirements for business activity in Germany on the basis of the European passport by the time the six-month period under section 64p sentence 1 of the KWG expires. Otherwise, after the expiry of this period, it may no longer commence business activity in Germany without BaFin's consent.

16) Do enterprises from non-member countries that are subsidiaries of enterprises that are eligible to use the MiFID passport to engage in High-frequency Trading in Germany need an authorisation to engage in High-frequency Trading in Germany?

Yes. Any organisation which, as a participant in a domestic organised market or multilateral trading facility, trades on an own-account basis using high-frequency algorithmic trading technology requires an authorisation.

17) If trading participants discontinue High-frequency Trading, when does their authorisation expire?

If trading participants discontinue High-frequency Trading, BaFin may revoke the authorisation pursuant to section 35 (2) no. 1 of the KWG if it has been more than six months since High-frequency Trading was conducted. If after having been granted an authorisation trading participants do not conduct any High-frequency Trading at all, the authorisation will expire pursuant to section 35 (1) no. 1 of the KWG unless they exercise it within one year of the date on which it was granted.

18) At what point will the follow-up requirements in accordance with the KWG cease to apply to trading participants once they have discontinued High-frequency Trading?

The follow-up requirements (i.e. capital requirements, reporting requirements, organisational requirements) apply to credit and financial services institutions within the meaning of the KWG ("Institutions"). Under section 1 (1) sentence 1 or (1a) sentence 1, respectively, Institutions are any enterprises that conduct banking business or provide financial services on behalf of others commercially or on a scale which requires a commercially organised business undertaking. Accordingly, enterprises constitute Institutions if and as long as they conduct such activities. The follow-up requirements cease to apply when an Institution discontinues the activity subject to an authorisation requirement and notifies BaFin in writing of the waiver of such authorisation. Obligations to pay contributions expire at the end of the year following the waiver or revocation of the authorisation. BaFin also requires enterprises to demonstrate that the business subject to an authorisation requirement has been wound-up and to submit audited annual financial statements to serve as a basis for calculating contributions.

19) Who qualifies as an indirect participant in a domestic organised market or multilateral trading facility?

Indirect participants are persons to whom a participant in an organised market grants direct electronic access. Direct electronic access means an agreement by which a participant in a domestic organised market or multilateral trading facility allows a person to use its trading ID to directly and electronically transmit orders in respect of a financial instrument to the trading venue. Indirect participants within the meaning of section 1 (1a) sentence 2 no. 4d of the KWG also include participants who do not gain access directly through an authorised trading participant, but indirectly via other "intermediate" participants (chain of indirect trading participants). However, indirect participants only become subject to the authorisation requirement if, using high-frequency algorithmic trading technology, they purchase or sell on an own-account basis financial instruments commercially or on a scale which requires a commercially organized business undertaking. Persons are deemed to be acting on a commercial basis if the business is established for a certain duration and conducted with the intention of generating profits.

20) What is high-frequency algorithmic trading technique?

Under section 1 (1a) sentence 2 no. 4d of the KWG, high-frequency algorithmic trading technique is characterised by:

- the use of infrastructure intended to minimise latency, particularly co-location, proximity hosting or high-speed direct electronic market access;

- system determination of order initiation, generating, routing or execution without human intervention; and
- high message intra-day rates which constitute orders, quotes or cancellations.

High-frequency algorithmic trading technique shall only be deemed to exist if all three of the above criteria are met (cumulative criteria).

21) What qualifies as infrastructure that aims to minimize latency?

Such infrastructure includes, for example, co-location, proximity hosting and high-speed direct electronic access. Co-location is where market participants place their computer systems directly proximate to a trading venue's computer, which matches "buy" and "sell" orders (matching engine). Proximity hosting is the provision by third parties of computer systems directly proximate to a trading venue's matching engine. High-speed direct electronic access means connections that allow the transmission of messages within fractions of a second, including messages to initiate, amend or cancel orders.

With regard to infrastructure designed to minimise latency, two criteria are crucial based on the latest technology and information available:

- the distance between the trading venue's matching engine and the server on which the algorithms run; and
- the volume of data capable of being transferred via the connection per second (bandwidth).

Based on the latest technology and information available, BaFin therefore presumes the use of infrastructure designed to reduce latency if the server on which the algorithms initiate, generate, route or execute orders are directly proximate to the trading venue's matching engine, and a bandwidth of 10 gigabits per second is used. Where an algorithm runs on a server which is located further away from the matching engine (for example in another city or town), it is presumed based on the latest technology and information available that there is no use of infrastructure that aims to reduce latency.

22) When is there considered to be a system decision on initiating, generating, routing or executing an order, with no human intervention, for individual transactions or orders?

This will depend on whether the system makes independent decisions on initiating, generating, routing or executing orders. A system decision will

also be deemed if the system reacts to algorithms or individual parameters of an algorithm of other systems, and in response initiates, generates, routes or executes orders with no further human intervention.

By contrast, a decision which requires human intervention before orders are initiated, generated, routed or executed does not constitute a system decision. Where algorithms only serve to draw a trader's attention to a particular situation, for example, and the trader must then decide independently whether to initiate, generate, route or execute orders, the use of such algorithms does not trigger any authorisation requirement at this stage. Thus, for example, the use of chart software which is programmed to chime or deliver a pop-up message whenever the price of a certain trading instrument intersects with the rolling average, without then automatically making a decision on issuing, amending or cancelling orders, is not subject to the authorisation requirement

23) What is considered high message intra-day rate?

Based on the latest technology and information available, a large volume of intra-day messages means 75,000 messages or more on average over the year per trading venue according to the ISO 10383 Market Identifier Code per trading day. Message volume must be determined on a rolling basis per trading day based on the previous 12-month period.

24) How is the high message intra-day rate being calculated?

Messages to be counted are each new order or quote, each successful change to an order or quote and each successful deletion of an order or quote. Messages originating from a technical process where the trader was not able to influence their existence, e.g. matches, do not count. The sum of messages is to be calculated for each trading day and the moving average thereof is to be calculated on a daily basis using the last 250 trading days. Days where a particular member/trader did not send messages at all are considered as having zero messages if the respective venue was open for trading on that particular day. In case of the existence of bulk transactions, every single message is to be counted separately. Participants who return the membership of a trading venue will no longer be required to calculate their message rate, as long as they do not continue trading on that venue as indirect participants. The starting point of the calculation of the message rate is 14 November 2013 or 14 February 2014 (end of the transitional periods pursuant to section 64p of the German Banking Act (*Kreditwesengesetz – KWG*)); 14 February 2014 applies to companies that fall under section 64p sentence 2 of the KWG). Starting on 16 July 2013, trading participants are required to store and keep available the data regarding their message rate if they use highfrequency algorithmic trading techniques and do not

hold a licence pursuant to section 32 of the *KWG* or are exempt pursuant to section 2 (4) of the *KWG*.

25) Are trading venues in Germany required to report participants who use a bandwidth of 10 gigabits per second to BaFin?

If BaFin requests such information and has a legal basis to do so, German trading venues must provide the information to BaFin.

26) Are there any exemptions from the high intra-day message rate threshold (75,000 messages per trading day, see above) in the event of market volatility?

No. Since the threshold of 75,000 messages is based on the volume of messages per trading day on average over the year, no exemption for periods of volatility is necessary.

27) When are trading participants required to apply for an authorisation if they exceed the high intra-day message rate threshold of 75,000 messages per trading day for the first time once the transitional periods have expired?

Trading participants must apply for an authorisation without undue delay as soon as they anticipate exceeding the threshold. An application for authorisation must be submitted on or before the date on which the threshold is actually exceeded.

28) Are trading participants required to apply for an authorisation if they exceed the threshold of 75,000 messages per trading day during the relevant assessment period and then decide to discontinue Highfrequency Trading?

No. Trading participants who exceed the threshold during the relevant assessment period and then discontinue High-frequency Trading are not required to apply for an authorisation.

29) Are there any exemptions from the authorisation requirement?

An exemption under section 2 (4) of the *KWG* may be available to enterprises from EEA countries which have been granted an authorisation in their home country, but do not have an authorisation capable of serving as a passport within the meaning of the MiFID.

For details of the requirements for an exemption, see in general the guidance notice entitled "Notes regarding the licensing requirements pursuant to section 32 (1) of the KWG in conjunction with section 1 (1) and (1a) of the KWG for conducting cross-border banking business and/or providing cross-border financial services" dated April 2005: By contrast, no exemption under section 2 (4) of the KWG is available to enterprises from non-member countries.

30) Who is not covered by the authorisation requirement?

Investors in foreign investment funds are not, as investors, subject to the authorisation requirement for High-frequency Trading pursuant to section 1 (1a) sentence 2 no. 4d of the KWG, because they are not themselves already participants in a domestic organised market or multilateral trading facility.

Clients of a broker who concluded agreements with the broker on the provision of principal broking services (*Finanzkommissionsgeschäft*) by the broker on behalf of the client are not subject to the authorisation requirement for High-frequency Trading if they are not themselves participants or indirect participants in a domestic organised market or multilateral trading facility.

31) What applies to investment funds from non-member countries?

Whether investment funds from non-member countries or their managers fall under the German High-frequency Trading Act (*Hochfrequenzhandelsgesetz*) or not can only be assessed on a case-by-case basis and by taking into account how exactly the activity is intended to be performed in the Federal Republic of Germany. In this regard it is essential how the investment fund is legally organised. We recommend contacting BaFin and providing all relevant details including any agreements entered into in order to have such individual cases assessed.

32) When does a trading participant become liable to prosecution for trading without an authorisation?

Any person who conducts banking business or provides financial services without an authorisation under section 32 (1) sentence 1 of the KWG is liable to prosecution under section 54 of the KWG.

Trading participants will be liable to prosecution if they fall under the authorisation requirement but have not submitted a complete application for authorisation by the time the transitional period under section

64p of the KWG expires, yet continue to engage in High-frequency Trading in Germany.

Trading participants who have submitted a complete application for authorisation within the transitional period under section 64p of the KWG and continue to engage in High-frequency Trading in Germany will not be liable to prosecution if a final decision on their application is still outstanding.

However, if their application is ultimately rejected, trading participants may be liable to prosecution if they continue to engage in Highfrequency Trading in Germany without the requisite authorisation.

33) What are the consequences for trading participants who provide indirect participants with access to a domestic organised market or a multilateral trading facility, even though the indirect participants have not been granted the necessary authorisation to engage in proprietary trading?

Under section 37 (1) sentence 3 of the KWG, the trading participant is then deemed involved in the initiation or conclusion of a financial service provided without the required authorisation. In such cases, BaFin may also require the trading participant who granted the access to immediately cease the business operations and promptly settle unlawful business. In some circumstances, trading participants may be held jointly liable for the indirect participant's infringement of section 54 of the KWG.

34) What are the particular points to note with regard to applications for authorisation?

Applications for authorisation are only complete if they meet the statutory authorisation conditions, namely that the resources necessary for business operations are available and the members of governing bodies are reliable and have the requisite professional qualifications and expertise.

In addition, evidence of the applicant's character as an institution at the time the High-frequency Trading Act enters into force (Article 7 (2)) should be attached.

Section 32 (1) sentences 1 and 2 of the KWG in conjunction with the Regulation Concerning Reports and the Submission of Documentation under the Banking Act (Verordnung über die Anzeigen und die Vorlage von Unterlagen nach dem Gesetz über das Kreditwesen – AnzV) dated 20 March 2009 contain details of what is required in order for applications for authorisation to be considered complete.

Further information may be found in the German Bundesbank's guidance "Notice on the granting of authorisation to provide financial services

persuant to section 32 (1) of the German Banking Act".

35) What requirements are applicable to the branches of enterprises from third countries?

The requirements applicable to the branches of enterprises from third countries correspond to the requirements already presented under question above. It should also be noted that the branch requires adequate initial capital for commencing its business operations, which must be provided to the branch for its free disposal by the enterprise maintaining the branch. The branch must also have a manager domiciled in Germany as well as an office in Germany.

Further information may be found in the German Bundesbank's guidance "Notice on the granting of authorisation to provide financial services persuant to section 32 (1) of the German Banking Act".

36) Which algorithms are covered by the term 'algorithmic trading' as defined in section 33 (1a) of the German Securities Trading Act (Wertpapierhandelsgesetz – WpHG)?

This question must be answered by looking at the intended purpose of section 33 (1a) of the WpHG. Investment services enterprises that engage in algorithmic trading should design their trading systems in such a way as to avoid causing disruptions to the market.

Algorithmic trading as defined in section 33 (1a) of the WpHG encompasses:

- algorithms that independently decide on certain aspects of an order (price, volume, time of execution, where applicable deletion, or whether human intervention is required, etc.); and
- algorithms that automatically generate orders and/or decide to execute such orders (the basis for these buy/sell orders is the automatic analysis of market data or news, which is then automatically translated into orders and entered into the trading system).

Where algorithms only serve to draw a trader's attention to a particular situation, for example, and the trader must then decide independently whether to initiate, generate, route or execute orders, the use of such algorithms does not trigger the requirements under section 33 (1a) of the WpHG at this stage. Thus, for example, the use of chart software which is programmed to chime or deliver a pop-up message whenever the price of a certain trading instrument intersects with the rolling average, without then automatically making a decision on issuing, amending or cancelling orders, is not subject to the requirements under section 33

(1a) of the WpHG.

37) If algorithms fulfil the requirements of section 33a of the WpHG (best execution) as systems that can only be used to forward orders to one or more trading venues or to confirm orders, is section 33 (1a) of the WpHG inapplicable?

Yes. If the place of execution is not specified in an order and the algorithm is exclusively used to fulfil the best execution requirement for customer orders within the meaning of section 33a of the WpHG, the algorithm is not subject to section 33 (1a) of the WpHG. Other smart order routing systems which determine the processing of orders beyond the best execution policy mandated by law are definitely covered by section 33 (1a) of the WpHG. For the purposes of risk management, this exception does not apply, which means that follow-up requirements must be fulfilled for such algorithms as set forth in section 25a of the German Banking Act (Kreditwesengesetz – KWG).

38) Does section 33 (1a) of the WpHG provide for an exception for algorithms if an order is processed with limited human intervention after it has been submitted?

No. Besides other factors such as time and price, section 33 (1a) sentence 2 of the WpHG also includes the issue of how the order is processed with human intervention in the definition of the order parameters. This makes it clear that the algorithm is an algorithm as defined by sentence 1 if it uses additional parameters after receipt or automatic generation of an order to decide whether human intervention is required before the order is executed.

39) Are market makers exempt from the requirements of section 33 (1a) of the WpHG?

No. Section 33 (1a) of the WpHG does not provide for any exceptions for market makers.

40) To what degree must an investment services enterprise that permits its customers to carry out algorithmic trading over a direct electronic connection monitor the requirements within the meaning of section 33 (1a) sentences 2-4 of the WpHG?

The term 'carry out trading' in section 33 (1a) of the WpHG is to be construed widely. Besides investment services institutions' proprietary trad-

ing, the term also applies in cases where an investment services enterprise that is, for example, a member/participant or user of a trading platform permits certain customers (including eligible counterparties) to send orders electronically to the institution's internal electronic trading systems so that they can be forwarded automatically to certain trading platforms under the institution's trading ID. If the customer carries out algorithmic trading, the investment services enterprise must ensure in a suitable manner that the customer complies with the statutory requirements pursuant to section 33 (1a) of the WpHG. The term does not apply to retail customers who submit their orders via banks' online systems (in particular, using an online banking service), provided that the orders are simply forwarded to the bank over the Internet without their content being processed.

41) Are investment services enterprises required to retain algorithms?

Under section 33 (1a) sentence 5 of the WpHG, investment services enterprises are required to document any and all modifications made to their trading algorithms. This means that, in the event of an investigation by BaFin, investment services enterprises should be able to demonstrate how a given algorithm functioned at any given point in the past.

42) What information must be retained?

Whatever information is necessary to answer questions as to the functioning of any given algorithm that had been used at any given time in the past. Under section 4 (3a) of the WpHG, BaFin may require that investment services enterprises provide, in particular, a description of the algorithmic trading strategies, the details of the trading parameters and the trading limits to which the system is subject. BaFin may also require that a description be provided of the most important procedures for assessing risks and for complying with the provisions of section 33 as well as details about systems testing.

43) How long does such information have to be retained?

The information must be retained for five years.

44) Do asset management companies and self-managed investment stock corporations fall within the scope of the KWG by virtue of the reference in section 9a (1) of the InvG to section 33 (1a) of the WpHG?

No, the reference should be understood to mean that the organisational

requirements set forth in section 33 (1a) apply mutatis mutandis to asset management companies and self-managed investment stock corporations. These companies are otherwise subject to the applicable provisions of the InvG (now: Investment Code), the Regulation Governing Rules of Conduct and Organisational Rules under the Investment Act (Investment-Verhaltens- und Organisationsverordnung – InvVerOV - now: Regulation on the Rules of Conduct and Organisational Rules Pursuant to the Investment Code (Kapitalanlage-Verhaltens- und Organisationsverordnung – KAVerOV)) and the Minimum Requirements for the Risk Management of Investment Companies (*Mindestanforderungen an das Risikomanagement für Investmentgesellschaften – InvMaRisk*)