HMRC - STSM117060 - Trading Of A Futures Contract

Like traded options, the majority of equity futures contracts are listed and traded via an electronic order-book system operated by a derivative investment exchange such as Euronext.LIFFE.

An electronic order-book allows members of the system to place an order to buy or sell a futures contract at a published price but without revealing their identity (commonly called pre-trade transparency). When the electronic system is able to match a transaction between an anonymous selling member with an anonymous buying member, the transaction is reported to both parties as well as to a clearing house which acts as a central counterparty to both selling and buying parties.

The role of a clearing house is to ensure that the transaction takes place or is ‘cleared’ with the underlying asset moving (if relevant) on the specified settlement date from the ultimate seller to the ultimate buyer and cash for the asset is received by the seller, if one of the parties defaults on the transaction.

When a transaction is matched in the electronic system, the contractual arrangements are such that the clearing house effectively becomes the purchaser of the asset acquired from an ultimate seller and the seller of the asset to the ultimate buyer.

Previous page

Next page