



March 15, 2019

Via Electronic Delivery

Mr. Christopher J. Kirkpatrick
Secretary of the Commission
Office of the Secretariat
Commodity Futures Trading Commission
Three Lafayette Centre
1155 21st Street NW
Washington, DC 20581

Re: ICE Futures Rule 4.26 Order Execution (New Passive Order Protection Functionality); Submission No. 19-119

Dear Mr. Kirkpatrick:

Managed Funds Association¹ (“MFA”) appreciates the opportunity to submit comments to the Commodity Futures Trading Commission (“CFTC” or “Commission”) on the filing by ICE Futures U.S., Inc. (“ICE Futures”) to amend its Rule 4.26 on Order Execution (the “Rule amendment”).² The Rule amendment would allow ICE Futures to implement a passive order protection functionality (“POP functionality”), an asymmetric delay or “speed bump”, at a delay speed and on futures contracts of its discretion.³ We are concerned that the Rule amendment, as drafted, is inconsistent with the Commodity Exchange Act (the “Act”) and the Commission’s regulations thereunder. We respectfully urge the Commission to reject the Rule amendment. To the extent the Commission supports ICE Futures experimenting with an asymmetric speed bump in the U.S. futures market, we recommend that ICE Futures amend the Rule Amendment so that the POP functionality only applies to the Gold Daily and Silver Daily futures markets for a pilot period of 12 months. In this way the Commission and market participants can study the impact of the asymmetric speed bump, and balance competing considerations of allowing for responsible innovation while protecting investors, market integrity, and market liquidity.

¹ Managed Funds Association (MFA) represents the global alternative investment industry and its investors by advocating for sound industry practices and public policies that foster efficient, transparent, and fair capital markets. MFA, based in Washington, DC, is an advocacy, education, and communications organization established to enable hedge fund and managed futures firms in the alternative investment industry to participate in public policy discourse, share best practices and learn from peers, and communicate the industry’s contributions to the global economy. MFA members help pension plans, university endowments, charitable organizations, qualified individuals and other institutional investors to diversify their investments, manage risk, and generate attractive returns. MFA has cultivated a global membership and actively engages with regulators and policy makers in Asia, Europe, North and South America, and many other regions where MFA members are market participants.

² See CFTC Requests Public Comment on a Rule Amendment Certification Filing by ICE Futures U.S., February 13, 2019, available at: <https://cftc.gov/PressRoom/PressReleases/7870-19>; and ICE Futures Submission No. 19-119, Amendments to Rule 4.26 Order Execution (hereinafter “ICE Futures Submission”), available at: <https://www.cftc.gov/sites/default/files/2019-02/ICEFuturesPassiveOrder020119.pdf>.

³ *Id.*

Comments

A. The Rule amendment is inconsistent with the Act and CFTC regulation.

MFA is concerned that the Rule amendment is inconsistent with Section 3 of the Act on findings and purpose,⁴ the requirement under designated contract market (“DCM”) Core Principle 2 to provide impartial access,⁵ and the requirement under DCM Core Principle 9 to provide a competitive, open and efficient market.⁶ Section 3 of the Act, among other things, finds that it is in the public interest to have “liquid, fair and financially secure trading facilities” and to foster such interest the purpose of the Act is “to promote responsible innovation and fair competition among boards of trade, other markets and market participants.”⁷ Core Principle 2 requires that an exchange provide members and persons with trading privileges impartial, transparent and non-discriminatory access to its markets and services.⁸ Core Principle 9 requires that an exchange “provide a competitive, open and efficient market and mechanism for executing transactions that protects the price discovery process of trading in the centralized market” of the exchange.⁹ We are concerned that the Rule amendment, by implementing an asymmetric speed bump creates an unfair market and unfair competition among markets and market participants by providing certain market participants with trading advantages over others, and violates the impartial access requirements by applying a trading delay only to incoming orders and not to resting orders.

Certain securities exchanges have implemented speed bumps.¹⁰ However, these speed bumps have been implemented symmetrically, applying equally to all inbound (incoming orders, and requests to cancel or modify resting orders) and outbound (execution report) communications; thus, not providing a speed advantage to incoming or resting orders.¹¹ A speed bump that only applies to incoming orders and not to

⁴ See 7 U.S.C. § 5 (describing the purpose of the Act as promoting responsible innovation and fair competition).

⁵ 17 C.F.R. § 38.151.

⁶ 17 C.F.R. § 38.500.

⁷ 7 U.S.C. § 5.

⁸ 17 C.F.R. § 38.151

⁹ 17 C.F.R. § 38.500.

¹⁰ See, e.g., IEX Rule 11.510 available at: <https://iextrading.com/docs/Investors%20Exchange%20Rule%20Book.pdf>; and NYSE Rule 7.29E available at: http://wallstreet.cch.com/AmericanTools/PlatformViewer.asp?SelectedNode=chp_1_5&manual=/american/rules/american-rules/.

¹¹ See, e.g., Order Setting Aside the Order by Delegated Authority Approving SR-CHX-2017-04, Securities and Exchange Commission Release No. 34-84337, Oct. 2, 2018, available at: <https://www.sec.gov/rules/sro/chx/2018/34-84337.pdf>. The Chicago Stock Exchange filed with the Securities and Exchange Commission (“SEC”) a proposed rule change to implement an intentional access delay for all new incoming orders, cancel, and cancel/replace messages, except for orders that would provide liquidity by designated market makers and cancel messages from designated market makers (“**CHX proposed rule**”). The CHX proposed rule was highly controversial. Even the SEC Office of the Investor Advocate submitted comments raising concerns that the CHX proposed rule change was “unfairly discriminatory and inconsistent with investor protection and the public interest. See Memorandum from Rick A. Fleming to SEC, Recommendation of the SEC Investor Advocate, Feb. 27, 2018, available at: <https://www.sec.gov/comments/sr-chx-2017-04/chx201704-3169295-161957.pdf>. The Chicago Stock Exchange amended its proposed rule as a 24-month pilot program and agreed to collect and publicly disclose certain pilot program statistics before ultimately withdrawing its proposed rule. See also Intercontinental Exchange Finalizes Acquisition of Chicago Stock Exchange, July 18, 2018, available at: <https://ir.theice.com/press/press-releases/all-categories/2018/07-18-2018-133237540>.

resting orders is discriminatory in its nature by providing market participants with unequal access to markets; and unfair because it creates and provides an informational advantage to certain market participants.

The Rule amendment would provide market participants with speed advantages (*i.e.*, fast traders) the ability (during the proposed 3 millisecond delay) to observe traders' actions on other venues and use such information leakage to cancel a resting order ahead of executing against a *delayed* incoming order. We disagree with ICE Futures' characterization of the POP functionality as helping "level the playing field by giving all traders who have placed a resting order additional time to react to price changes in related markets."¹² Instead, our view is that the Rule amendment creates an unlevel playing field by institutionalizing a short delay, which allows fast traders to benefit from information leakage from other venues to the disadvantage of other market participants. This is inconsistent with the Act's purpose of promoting fair competition among markets and market participants,¹³ and regulatory requirements for exchanges to provide market participants access to competitive, open and efficient markets in a non-discriminatory manner.¹⁴

A study of the Canadian exchange TSX Alpha's asymmetric speed bump (the "**TSX Alpha study**") found that "advance knowledge – even for a millisecond—of institutional investors' trading intentions (in a probabilistic sense) is valuable . . . [and] can enable substantial (costly) information leakage across venues."¹⁵ The TSX Alpha study found that TSX Alpha's asymmetric speed bump increased total transaction costs and reduced the resiliency of the order book.¹⁶ Further, the TSX Alpha study found that TSX Alpha's asymmetric speed bump had a negative impact on other trading venues.¹⁷ The TSX Alpha study findings are very concerning as they indicate that asymmetric speed bumps promote unfair competition among markets and market participants, do not provide traders with equal or impartial access to markets, and violate the regulatory mandate for exchanges to provide competitive and efficient markets and mechanisms for executing transactions that protect the price discovery process.

Finally, we are concerned that the asymmetric speed bump feature of the Rule amendment may frustrate market participants seeking to execute against posted liquidity that disappears—creating a "phantom liquidity" phenomenon. The Rule amendment may also exacerbate incidents of spoofing by allowing traders to more easily cancel resting orders with less risk of order execution due to the speed bump.¹⁸ Simultaneously, the Rule amendment could make it more challenging for the Commission and ICE Futures to bring enforcement cases against market participants for violating Section 4c(a)(5)(C) of the

¹² ICE Futures Submission, *supra* n. 2.

¹³ 7 U.S.C. § 5.

¹⁴ 17 C.F.R. §§ 38.151, 38.500.

¹⁵ Haoming Chen et. al., *The Value of a Millisecond: Harnessing Information in Fast, Fragmented Markets*, Nov. 18, 2017, at p. 3, available at: https://papers.ssrn.com/sol3/papers.cfm?abstract_id=2860359. While TSX Alpha's asymmetric speed bump differs from the Rule amendment in that TSX Alpha provided the option for market participants to pay a higher fee to enter and cancel limit orders without experiencing a delay, we believe the findings of the TSX Alpha study continue to be relevant and are concerned with the implications of an asymmetric speed bump for institutional investors.

¹⁶ *Id.*

¹⁷ *Id.* at 3 (finding that realized spreads on other venues fell as a result of TSX Alpha's asymmetric speed bump).

¹⁸ *See* 7 U.S.C. § 6c(a)(5)(C).

Act as the Rule amendment may make it more difficult for regulators to make the case that a trader was spoofing rather than simply canceling its resting order.

For the reasons discussed, MFA respectfully urges the Commission to reject the Rule amendment as inconsistent with the Act and CFTC regulations.

B. In the alternative, ICE Futures should conduct a narrowly tailored pilot.

To the extent the Commission supports ICE Futures experimenting with an asymmetric speed bump in the U.S. futures market, MFA believes that given the novel and complex issues that it raises ICE Futures should amend the Rule amendment and the CFTC should only approve a narrowly tailored rule amendment that specifically implements the POP functionality for Gold Daily and Silver Daily futures markets for a pilot period of 12 months. Contrary to the Rule amendment's stated objectives to encourage additional market participants to participate in trading Gold Daily and Silver Daily futures markets by initiating a three-millisecond delay period, the Rule amendment is significantly broader in scope. The Rule amendment would allow ICE Futures to implement the POP functionality for "Exchange Futures Contracts and contract months as determined by the Exchange from time to time in its discretion."¹⁹ Consistent with the purpose of the Act, in promoting responsible innovation,²⁰ the CFTC should take a cautious and deliberate approach in approving novel and complex trading functionalities, similar to the approach the CFTC has taken with respect to novel products.²¹ In addition, it will be important for ICE Futures to collect and publish data on the impact of its passive order protection functionality. In this way, the Commission, ICE Futures, and market participants can review the impact of an asymmetric speed bump on markets and market participants before the Commission determines whether such a feature should be expanded to or applied to other markets.

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¹⁹ ICE Futures Submission No. 19-119, *supra* n. 2.

²⁰ *See* 7 U.S.C. § 5.

²¹ *See, e.g.*, CFTC Statement on Self-Certification of Bitcoin Products by CME, CFE and Cantor Exchange, CFTC Release No. 7654-17, December 1, 2017, available at: <https://cftc.gov/PressRoom/PressReleases/pr7654-17>.

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MFA greatly appreciates the Commission's consideration of the issues raised in this letter. If the Commission or the staff have questions or comments, please do not hesitate to contact Jennifer Han, Associate General Counsel, at (202) 730-2600.

Respectfully submitted,

/s/ Jennifer W. Han
Jennifer W. Han
Associate General Counsel

CC: The Hon. J. Christopher Giancarlo, Chairman
The Hon. Brian D. Quintenz, Commissioner
The Hon. Rostin Behnam, Commissioner
The Hon. Dawn DeBerry Stump, Commissioner
The Hon. Dan M. Berkovitz, Commissioner
Mr. Mike Gill, Chief of Staff to the Chairman
Mr. Amir Zaidi, Director, Division of Market Oversight