March 13, 2019

Mr. Christopher J. Kirkpatrick
Secretary
Commodity Futures Trading Commission
1155 21st Street NW
Washington, DC 20581

Re: Industry Filing IF 19-001
Requesting Public Comment on a Rule Amendment Certification Filing by ICE Futures U.S.

Dear Mr. Kirkpatrick:

The FIA Principal Traders Group ("FIA PTG") appreciates the opportunity to comment on the Commodity Futures Trading Commission's ("Commission") "Request for Public Comment on a Rule Amendment Certification Filing (the "Rule Change") by ICE Futures U.S. (the "Exchange" or "IFUS"). FIA PTG is an association of firms that use their own capital to trade in a wide variety of asset classes, including equities, fixed income, foreign exchange and commodities. FIA PTG members are an important source of liquidity in these markets, enabling investors, including commercial end-users, to manage their business risks and to enter and exit markets efficiently. We support transparent, competitive, and well-regulated markets and regulatory measures that support these goals.

1. Introduction

FIA PTG became aware of the Exchange's plans to implement Passive Order Protection functionality (the "Speed Bump") in mid-November through an API Notification[1] distributed to technical staff at some of our member firms. We were surprised by this as, to our knowledge, this was to be the first artificial latency mechanism introduced in the well-functioning U.S. futures markets. FIA PTG has consistently raised concerns with various artificial latency mechanisms that have been proposed, and in some cases adopted, in the U.S. equity markets, but notes that the proposed Speed Bump goes far beyond anything that has been approved in the equity markets given its asymmetrical and discriminatory application to different order types, and by extension, different market participants and trading strategies. Introducing any speed bumps - let alone asymmetric ones - into our futures markets is not only novel, but raises significant concerns.

---

[1] ICE Futures, U.S. API Notification dated November 15, 2018.

We believe that introducing speed bumps to a futures market, as the Exchange is proposing, will:

1. harm market quality, including execution quality, price discovery, and liquidity;
2. increase market fragility during volatile market conditions and contribute to market disruptions;
3. give a misleading impression of what firm quotes are available in the market and create fleeting or potential illusory liquidity;
4. allow bad actors to display quotes that they do not intend to execute and facilitate market manipulation schemes, including spoofing, by creating mechanisms to easily pull quotes out of the way of incoming orders;
5. add unnecessary complexity to the market;
6. present discrimination issues between different types of market participants; and
7. create an unlevel competitive playing field.

We have not been presented with any evidence to the contrary or seen a compelling explanation from the Exchange as to problems that exist in our futures markets, how their proposal would address any such problems, or the grounds upon which they might ascertain whether their experiment has been (in)effective.

To learn more about the Exchange's plans, FIA PTG staff had discussions with various Exchange personnel who offered to conduct an open call with our membership in mid-December. From those discussions, we learned that the proposed Speed Bump was purportedly only an experiment designed to foster liquidity in two otherwise illiquid metals contracts. We were assured that the proposed Speed Bump would only be applied to two products and that the Exchange had no plans to apply this functionality to other products. We took some comfort in this informal assurance, so were surprised and dismayed to learn that the Rule Change submission lacked any limitations with respect to either the contracts to be covered or the duration (and consistency) of the artificial latency mechanisms to be introduced. Per the proposed rule text, the Speed Bump may be applied by the Exchange to any products it chooses and for any amount of time it desires:

> (c) Passive Order Protection may be activated for those Exchange Futures Contracts and contract months as determined by the Exchange from time to time in its discretion. Passive Order Protection delays for a period of time specified by the Exchange (the "Delay Period") the execution of a trade when an order entered into the ETS would match with an order resting in the ETS. During the Delay Period a resting order can be cancelled or modified. Passive Order Protection does not affect priority of execution for orders entered or resting in the system.

Under the terms of this filing, the proposed Speed Bump may be activated at any time, on any product that the Exchange determines in its sole discretion. The length of the artificial delay is also determined at the sole discretion of the Exchange and can vary by product. To be clear, applying the proposed Speed Bump to any product for any duration is a scope and scale with no known corollary. Accordingly, we believe the rule amendment, as proposed, is far more than a small

experiment - it is a broad, precedent-setting change that would have significant adverse impacts on the US futures markets.

2. The Proposed Speed Bump Would Harm Market Quality, including Price Discovery and Liquidity

As active liquidity providers, our members are concerned about the potential impact that artificial latency mechanisms, including asymmetric speed bumps, would have on market quality, including execution quality, price discovery, and liquidity. We believe the proposed Speed Bump would weaken price discovery. It is designed to allow certain IFUS market participants to benefit from the price discovery process on other Designated Contract Markets ("DCMs") by allowing them to cancel or widen their quotes in response to price discovery on other DCMs and thus avoid undesirable executions when prices are moving. The Rule Filing alleges that "[t]his short delay helps level the playing field by giving all traders who have placed a resting order additional time to react to price changes in related markets." However, despite the Exchange's claims, we are concerned that allowing the Speed Bump would harm the price discovery process by diverting some order flow (both passive and active[2]) from other DCMs while discouraging order flow that is more likely to result in a price change (and hence is more informative to price discovery) from trading on IFUS. This cherry-picking would harm overall price discovery as liquidity providers would be discouraged from displaying orders on other DCMs since they would be able to display on IFUS with the ability to cancel in the event of a price move. This would lead to wider effective bid-ask spreads, less truly accessible liquidity and greater volatility.

The proposed Speed Bump is explicitly designed to create an economic advantage for certain market participants that primarily post resting quotes, under the guise that this is the only form of making markets. FIA PTG believes it is a misconception to view market making as an activity that exclusively involves the posting of passive or resting orders. Both active orders and passive orders are used extensively by most market makers. The two are inextricably linked. Market makers, including FIA PTG members, execute active orders in the normal course of business to manage their inventory and to responsibly hedge market risk. To the extent they can do this reliably and competitively, their liquidity provision activities improve (in size and width). Penalizing active orders versus resting orders (equally, rewarding the other) would be damaging to the overall quality of the market. We are also concerned that the potential reduction of market making firms trading with resting orders could have the trickledown effect of harming the quality of fills received by end users resting orders.

In markets where the futures contract is a reference price, the addition of a speed bump - let alone an asymmetric speed bump - would slow the price discovery process. Futures markets are liquid,

---

[2] To be clear, we are generally using the term "active" to refer to orders that are intended to cross a bid-ask spread and be immediately executed. These orders are sometimes referred to as "marketable" or "spread-crossing" and the Exchange uses the term "aggressive" for these orders in its rule proposal. We and the Exchange are generally using the term "passive" to refer to orders that are not intended to immediately execute, but rather to be entered into an order book. These orders are sometimes referred to as "resting" orders or, more generally, as "quotes".

in part, because they are predictable and have firm, executable, and immediately-accessible quotes. In other words, "what you see is what you get." As a result, new strategies (read as "potential new liquidity") are possible because participants can rely on the markets they see and develop and test new trading strategies. We are concerned that the introduction of the Speed Bump, as proposed, would reduce the reliability data on market quoting and trading activity, and in turn the ability of new market making strategies to be developed and deployed. Less development and deployment of market making strategies equals less liquidity. In addition, it would discourage market participants from incorporating information into prices as their active orders would suffer lower fill rates, which would make prices less informed overall as some information would either not be incorporated at all or would be incorporated less quickly. Any market that uses the futures market as a reference price would use the delayed/stale IFUS price, potentially impacting pricing across a broad range of products. While the Exchange purports to only be initially focused on contracts in which the volume is *de minimis*, this Rule Filing would permit IFUS to implement the Speed Bump in any futures contract which could broadly harm market quality. Further, approval of the Rule Filing would open the flood gates to other DCMs introducing countless variations of such speed bumps that would further increase the complexity and fragility of our futures markets.

Allowing market participants that post resting quotes in the marketplace to pull their quotes allows certain participants to display quotes that they do not intend to execute; while also fostering a misleading impression of liquidity in the product. To quote IFUS, "The functionality essentially gives market participants engaged in arbitrage a very short window to modify their Exchange orders where there is a price change in a related market." In effect, this operates like a "last look" in which market makers have a chance to selectively move their quotes out of the way when it is in their interest to do so, but to remain firm for their quotes when they already know that is to their advantage (and generally to their delayed counterparties disadvantage).

3. **The Proposed Speed Bump Would Harm Market Resiliency**

Artificial latency mechanisms - particularly like the proposed asymmetric Speed Bump would contribute to increased intraday volatility and exacerbate market disruptions like "flash crashes." The proposed asymmetric Speed Bump would make it more difficult to execute marketable orders during periods of volatility. During these periods, however, the prices on the Exchange in markets using the Speed Bump would appear better than prices on other DCMs, attracting more active orders to be routed to the Exchange at the exact time that those orders would be less likely to be filled (given the ability of posters of resting orders to rapidly cancel those orders before they can be accessed). The combination of additional orders coming in at the same time that liquidity is allowed to "fade" could lead to unnatural and rapid price dislocations.

4. **The Proposed Speed Bump Could Facilitate Market Manipulation Schemes**

Further, asymmetric speed bumps essentially create a synthetic unactionable order type. Presently, U.S. futures markets are comprised of predominately immediately actionable orders. The addition of the proposed functionality could facilitate various market manipulation schemes. Although the Speed Bump would not encourage spoofing *per se*, it would provide a unique opportunity for bad

actors to engage in nefarious quoting activity in markets in a way that is far harder to define and detect - not to mention with a much lower risk of actual execution. For example, an actor intent on "spoofing" the market could display quotes in the marketplace that he/she did not intend to execute in order to create a false impression of supply and demand with the added protection of extra time to pull the quotes.

5. **The Proposed Speed Bump Would Improperly Discriminate Between Different Kinds of Traders**

The Speed Bump would improperly discriminate between different types of traders. The proposal is designed to impact competition between firms with different business models, advantaging some while disadvantaging others. The proposal clearly favors those firms that predominantly trade with resting orders at the expense of firms that predominantly trade with marketable orders (and inappropriately alter the competitive dynamics for every firm in between). Some contend that the Exchange is not discriminating because market participants can choose whether to post passive or marketable orders. This logic is flawed since if all orders were passive, resting orders - there would be no trades. Moreover, different firms have different trading styles and requirements and are often not easily able to change between execution approaches.

6. **The Proposed Speed Bump Would Result in Unfair Competition**

Approval of the proposed Speed Bump would also result in unfair competition. IFUS seeks an unfair competitive advantage relative to other DCMs by allowing IFUS market participants time to react to price changes happening on other DCMs. The Rule Filing seeks to permit IFUS market participants using passive orders to free-ride off price discovery happening on other DCMs, while avoiding adverse executions during price transitions by fading their quotes when the efficient price discovery process on other DCMs results in a change in price levels. Other DCMs might be forced to adopt similar mechanisms for competitive reasons, compounding the risks and complexities that would be caused by the current proposal alone.

While we are supportive of competition in the futures market, the Commodity Exchange Act ("CEA") requires that the competition is fair. The proposed speed bump does not appear to meet this standard.

7. **Introduction of the Speed Bump Raises Implementation Concerns**

FIA PTG has numerous additional concerns which could be addressed by the Exchange but which we are unable to confirm based on the information currently available. The first centers around whether the first-in-first-out ("FIFO") order matching priority would be maintained post implementation. The Exchange has stated that "In order to maintain FIFO priority, the Exchange will apply the same latency for all incoming requests to enter, change, or cancel/replace orders during the latency period for any order(s) on the *same* [emphasis added] side of the market as the aggressor order." Although activity on the same side of the market would be FIFO, it is unclear how orders that enter the market as "aggressive", are delayed by the Speed Bump, and become

"passive" as a result of resting passive orders being canceled, are introduced into the order book relative orders submitted afterwards that are never delayed due to not being identified as "aggressive". Depending on the implementation of this logic, which is certain to be complex, it is possible that the order book lacks any real semblance of FIFO.

Similarly, the proposed Speed Bump allows for passive orders to be canceled at any time, whereas active orders cannot be controlled during the three-millisecond delay. This scenario sets up a couple of concerning situations, the first being where a market participant may have an active order "stuck" in the IFUS delay when the market moves in his favor at another DCM. Rather than canceling his order in response to the price change, the market participant may be filled at IFUS despite a better price being available at another DCM. The second, and more troubling situation being that due to ongoing market activity while the active order is "stuck" in the IFUS delay, the status of the order may change to "passive" and depending on how it is introduced into the order book may become immediately actionable before the market participant can cancel or change it. For a market maker, not having control of your orders, even for three-milliseconds, introduces unnecessary market exposure and risk.

8. **The Process for Introducing Changes to Trade Matching Algorithms Requires Data Gathering and Quantitative Analysis**

In addition to our many concerns about artificial latency introducing mechanisms, FIA PTG questions whether the Exchange has met the Section 40 requirement to "provide a concise explanation and analysis of the operation, purpose and effect of the proposed rule or rule amendment and its compliance with applicable provisions of the Act, including core principles, and the Commission's regulations thereunder."

In our discussions with the Exchange we were unable to garner many details as to how they developed the idea to introduce the first speed bump in a futures market, let alone an asymmetric speed bump of unprescribed and variable length. The Exchange did not provide any details regarding the metrics it used to predict the impact of the delay, the metrics used to determine the length of the delay itself, or even whether the Exchange planned to use any metrics to evaluate the success or failure of the Speed Bump post implementation. In addition, the Exchange has not explained how the Speed Bump is consistent with the Commodity Exchange Act and Commission regulations, including:

- Core principle 2 and §38.151, which require the DCM to provide market participants with impartial access to its markets and services;
- Core principle 9, which requires the DCM to provide a competitive, open, and efficient market, and to protect the price discovery process of trading in the centralized market of the board of trade;
- Core principle 12, which requires the DCM to promote fair and equitable trading; and
- Core principles 3 and 4, which require the DCM to only list contracts that are not readily susceptible to manipulation and to prevent manipulation and price distortion on its markets.

FIA PTG believes that when introducing a change to a futures market matching engine which may have the wide-ranging and negative impacts described herein, there should be a certain amount of analysis done before self-certification and implementation; and there should be a post implementation plan to gather and share the data necessary for the Exchange, market participants and the Commission to review and evaluate the impact of the functionality.

9. Conclusion

Although FIA PTG supports innovation and where warranted, responsible experimentation, we believe that speed bumps present a tremendous threat to the function, fairness and stability of markets. While this functionality may be purportedly planned for only a couple of products, if allowed, we fear the Commission is opening the door for the Exchange, or other exchanges, to broaden its applicability across all products and for other DCMs to pursue similar functionalities without any constraints or checks and balances. Because of these concerns and the proposal's inconsistency with the Commodity Exchange Act and Commission regulations, we ask that the Commission reject the proposed Rule Change.

If you have any questions about these comments or if we can provide further information, please do not hesitate to contact Joanna Mallers (jmallers@fia.org).

Respectfully,

FIA Principal Traders Group

Joanna Mallers
Secretary

cc: Chairman J. Christopher Giancarlo
        Commissioner Brian Quintenz
        Commissioner Rostin Behnam
        Commissioner Dan Berkovitz
        Dan Bucsa, Chief of Staff & Senior Policy Advisor to Commissioner Stump