



Principal Traders Group

February 4, 2013

John Ramsay, Acting Director
Division of Trading & Markets
Securities & Exchange Commission
100 F Street, N.E.
Washington, D.C. 20549

Dear Mr. Ramsay:

The Futures Industry Association Principal Traders Group (FIA PTG)¹ appreciated the opportunity for representatives of a number of its member firms to meet with your staff on November 14, 2012. During the course of that meeting, we addressed several topics related to risk management and market integrity. In particular, your staff inquired as to the availability and use of "Drop Copies" as a risk management mechanism. To follow-up on that discussion, we are providing in this letter a more detailed description of Drop Copies and their use by FIA PTG members.

The FIA PTG believes that well-regulated markets provide stability, promote competition, and create efficiencies – all of which contribute to investor confidence. Moreover, as major providers of liquidity to the regulated markets and as counterparties to a large percentage of trades, our members have a vested interest in facilitating and maintaining the integrity of the markets. For those reasons, and

¹ The FIA PTG was founded in January 2010 and is comprised of over 30 trading firms, which trade only their own capital. The purpose of the organization is to provide a forum for firms trading their own capital to identify and discuss issues confronting the PTG community; define common positions on public policy issues and advance the group's collective interests through the FIA; improve public understanding of the constructive role played by the wide variety of individual trading groups in the exchange-traded derivatives markets; and promote cost-effective, transparent access to U.S. and non-U.S. markets. While FIA PTG members do not all trade in the same manner, many of them rely on automated trading technology with direct connections to exchanges, and they play an important role in maintaining liquidity in these markets.

as discussed in greater detail below, the FIA PTG believes that Drop Copies, when available in a timely and meaningful manner, are a valuable risk management tool.

Background: Description of Drop Copies

Drop Copies are a service provided by exchanges and other trading venues that allows members and participants to receive real-time or near real-time copies of trade reports and, in some cases, messages related to orders. Drop Copies are generally sent via a dedicated communication session that is separate from the communication session over which production trading occurs.

The contents of a Drop Copy feed vary by trading venue. At a minimum, a Drop Copy feed reports each trade executed by the member or participant. Other data points that may be reported within a Drop Copy feed include: New Order Requests, New Order Acknowledgement, New Order Rejects, Modify Order Requests, Modify Order Acknowledgement, Modify Order Rejects, Cancel Order Requests, Cancel Order Acknowledgement, Cancel Order Rejects, and Trade Bust/Adjustment Reports².

Valuable Risk Management Tool

Trading firms, such as FIA PTG members, typically use Drop Copies for live trade reconciliation and risk management. When processed in real-time, information provided by a Drop Copy can be compared to a trade notification received over production trading sessions. This comparison allows a trading firm to confirm the accuracy of the information its trading systems are receiving from the trading venue. Discrepancies in information received via production trading sessions and Drop Copies can be one of the first indications of a potential issue. For example, a trading firm could maintain a system that compares, in real-time, their filled orders reported via a Drop Copy to those reported through production trading sessions. If there is ever a persistent disparity between the two trade reports an alert may be raised with the responsible parties so the necessary action may be taken. To satisfy their unique needs, some trading firms also use Drop Copy as a way to consolidate the reporting of their trading activity on a trading venue into a single data feed. This consolidated data feed can then be used by those responsible for managing the firm's risk.

² There are a variety of fields available for inclusion within the data points reported by Drop Copy. They include product symbol, whether the recipient is a buyer or seller, price, quantity, Order ID, transaction time, clearing account, trader ID, execution ID, client order ID, session ID, time in force, and a free form text field.

There are several features of a Drop Copy that make it a valuable risk management tool—the redundancy of information it provides, its timeliness, and its richness of information. In order to fully appreciate the value of Drop Copies, it is important to understand the functionality associated with these features.

Drop Copies increase a trading firm’s ability to manage its risk by providing a redundant source of information. In order to maximize the redundancy provided by Drop Copies, some trading venues offer the service via an infrastructure that is independent of the production trading infrastructure. In doing so, an outage in the production trading environment is less likely to affect receipt by a firm of Drop Copies and, consequently, the firm’s ability to manage its risk.

The timeliness of data dissemination to risk management systems is crucial to any trading operation. The sooner a firm is able to identify discrepancies between trades reported by the production trading session and Drop Copies the better positioned it will be to address those discrepancies. Trading venues that disseminate trade reports over production trading and dedicated Drop Copy sessions simultaneously help to minimize the amount of time that a discrepancy may go unnoticed by market participants that consume both data feeds.

A risk system’s ability to identify potential issues is correlated to the amount of information to which it has access. As was described above, there are a number of data points that can be included in Drop Copies beyond trade reports. When Drop Copy and production trading sessions provide precisely the same information, trading firms may maintain a mirror image of its production order book and audit trail independent of their system used to submit, modify and cancel orders.

Due to the variability in organizational structures among trading firms there may be a need to aggregate risk exposure at a variety of different levels. Trading venues that allow members or participants to configure the aggregation level of the information reported in the Drop Copy provide greater flexibility and a finer level of control to risk managers.

Conclusion

The FIA PTG appreciates contributing to the ongoing industry dialogue focused on identifying means to facilitate greater market stability and resiliency. Our review of this and related risk management mechanisms is continuous and ongoing. To further our discussion, the FIA PTG is in the initial stages of preparing a document designed to identify best practices pertaining to the availability and use of drop copies. We anticipate publishing such a paper in the near future. Thank you again

for the opportunity to meet with your staff; we are happy to provide any additional information as needed.

Sincerely,

A handwritten signature in black ink, appearing to read 'Donald R. Wilson, Jr.', with a long horizontal flourish extending to the right.

Donald R. Wilson, Jr.
Chairman
FIA Principal Traders Group

cc: Office of Analytics and Research,
Gregg E. Berman, Associate Director

Division of Trading and Markets,
James R. Burns, Deputy Director