Public Statements & Remarks

Statement of Support by Commissioner Brian D. Quintenz Regarding Final Rule on Electronic Trading Risk Principles

December 08, 2020

I support today's final rule requiring designated contract markets (DCMs) to adopt rules that are reasonably designed to prevent, detect, and mitigate market disruptions or system anomalies associated with electronic trading. It also requires DCMs to subject all electronic orders to pre-trade risk controls that are reasonably designed to prevent, detect and mitigate market disruptions having a "material" effect on its participants and to provide prompt notice to the Commission in the event the platform experiences any material market disruptions that meet a higher threshold of being "significant".

I believe all DCMs have already adopted regulations and pre-trade risk controls designed to address the risks posed by electronic trading. As I have noted previously, many—if not all—of the risks posed by electronic trading are already being effectively addressed through the market's incentive structure, including exchanges' and firms' own self-interest: DCMs through their interest in operating markets with integrity, and firms through their interest in not exposing their or their customers' funds to huge losses in a matter of minutes through algorithmic operational error. Both exchanges and firms have been leaders in implementing best practices around electronic trading risk controls. Therefore, today's final rule merely codifies principles underlying existing market practice of DCMs to have reasonable controls in place to mitigate electronic trading risks.

Significantly, the final rule puts forth a principles-based approach, allowing DCM trading and risk management controls to continue to evolve with the trading technology itself. As we have witnessed over the past decade, risk controls are constantly being updated and improved to respond to market developments. In my view, these continuous enhancements are made possible because exchanges and firms have the flexibility and incentives to evolve and hold themselves to an ever-higher set of standards, rather than being held to a set of prescriptive regulatory requirements which can quickly become obsolete. By adopting a principles-based approach, the final rule provides exchanges and market participants with the flexibility they need to innovate and evolve with technological developments. DCMs are well-positioned to determine and implement the rules and risk controls most effective for their markets. Under the rule, DCMs are required to adopt and implement rules and risk controls that are objectively reasonable. The Commission would monitor DCMs for compliance and take action if it determines that the DCM's rules and risk controls are objectively unreasonable. Importantly, the Appendix to the final rule points out that a DCM will be held to a standard of reasonableness and not to how other DCMs implement the rule. Any horizontal review across DCMs of rules or risk controls would only inform objectively unreasonable determinations, not create a baseline set of specific risk controls that become de-facto regulatory requirements.

The Technology Advisory Committee (TAC), which I am honored to sponsor, has explored the risks posed by electronic trading at length. In each of those discussions, it has become obvious that both DCMs and market participants take the risks of electronic trading seriously and have expended enormous effort and resources to address those risks.

For example, at one TAC meeting, we heard how the CME Group has implemented trading and volatility controls that complement, and in some cases exceed, eight recommendations published by the International Organization of Securities Commissions (IOSCO) regarding practices to manage volatility and preserve orderly trading.[1] At another TAC meeting, the Futures Industry Association (FIA) presented on current best practices for electronic trading risk controls.[2] FIA reported that through its surveys of exchanges, clearing firms, and trading firms, it has found widespread adoption of market integrity controls since 2010, including price banding and exchange market halts. FIA also previewed some of the next generation controls and best practices currently being developed by exchanges and firms to further refine and improve electronic trading systems. The Intercontinental Exchange (ICE) also presented on the risk controls ICE currently implements across all of its exchanges, noting how its implementation of controls was fully consistent with FIA's best practices.[3] These presentations emphasize how critical it is for the Commission to adopt a principles-based approach that enables best practices to evolve over time.

I believe the final rule issued today adopts such an approach and provides DCMs with the flexibility to continually improve their risk controls in response to technological and market advancements. Because this rule allows for flexible implementation and effectively places that burden on the market participants with the most aligned and motivated interests, I believe this rule will stand the test of time and serve as a paradigm of the CFTC's mission statement: sound regulation that promotes the integrity, resilience, and vibrancy of the U.S. derivatives market.

---

[1] Meeting of the TAC on March 27, 2019, **Automated and Modern Trading Markets Subcommittee Presentation, transcript and webcast available at,** https://www.cftc.gov/PressRoom/Events/opaeventtac032719

[2] Meeting of the TAC on Oct. 3, 2019, **Automated and Modern Trading Markets Subcommittee Presentation, transcript and webcast available at,** https://www.cftc.gov/PressRoom/Events/opaeventtac100319

[3] Id.

-CFTC-