UNITED STATES OF AMERICA

COMMODITY FUTURES TRADING COMMISSION

STAFF ROUNDTABLE ON DISRUPTIVE TRADING PRACTICES

Washington, D.C.

Thursday, December 2, 2010

PARTICIPANTS:

CFTC Staff:

ROBERT PEASE, Co-Chair

MARK HIGGINS, Co-Chair

ANDREI KIRILENKO

JEREMY CUSIMANO

STEVEN SEITZ

STEPHEN SHERROD

Panel One:

JOHN HYLAND
U.S. Natural Gas Fund

RAJIV FERNANDO
Chopper Trading, LLC

ADAM NUNES
Hudson River Trading Group

CAMERON SMITH
Quantlab Financial, LLC

LIAM CONNELL
Allston Trading, LLC

DON WILSON
DRW Trading Group

JOEL HASBROUCK
New York University

GARY DeWAAL
Newedge USA, LLC

MARK FISHER
MBF Clearing Corp

PARTICIPANTS (CONT'D):

JOHN LOTHIAN
John J. Lothian & Company

Panel Two:

TOM GIRA
Financial Industry Regulatory Authority

CHRIS HEYMEYER
National Futures Association

IKE GIBBS
ConocoPhillips

DEAN PAYTON
Chicago Mercantile Exchange

MARK FABIAN
IntercontinentalExchange

JOE MECANE
New York Stock Exchange

GREG MOCEK
McDermott Will & Emery

KEN RAISLER
Futures Industry Association
Sullivan & Cromwell, LLP

MICAH GREEN
Patton Boggs, LLP

TYSON SLOCUM
Public Citizen

ANDREW LO
Massachusetts Institute of Technology

PARTICIPANTS (CONT'D):

Panel Three:

TOM GIRA
Financial Industry Regulatory Authority

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JOE MECANE
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P R O C E E D I N G S

(9:31 a.m.)

MR. PEASE: Good morning and welcome to CFTC's roundtable discussion on disruptive trading. My name is Robert Pease. I'm counsel to the director of Enforcement. With me today are Mark Higgins, also counsel to the Director of Enforcement; Jeremy Cusimano, economic advisor to the Director of Enforcement; Steve Seitz, attorney from the Office of the General Counsel; and our moderators for the morning session, Steve Sherrod, the director of Market Surveillance; and Andre Kirilenko, a senior financial economist from the Office of the Chief Economist.

In Dodd-Frank, Congress specifically enumerated three practices as being disruptive of commodity markets. Section 747 of Dodd-Frank states that "it shall be unlawful for any person to engage in any trading, practice or conduct on or subject to the rules of a registered entity that violates bids or offers, demonstrates intentional or reckless disregard for the orderly execution of transactions during the closing period, is, is of the character of, is commonly known, as spoofing," and spoofing is defined as bidding or offering with the intent to cancel the bid or offer before execution.

In addition, Congress gave the Commission the authority to make and promulgate such "rules and regulations as in the judgment of the Commission are reasonably necessary to prohibit the trading practices" enumerated in the statute and "any other trading practices that are disruptive of fair and equitable trading."

On October 26th of this year, the Commission approved an Advanced Notice of Proposed Rulemaking on disruptive trading practices. In that ANOPR, the Commission asked 19 questions and invited comments from the public on each of the issues raised by the ANOPR. This roundtable is one effort to seek comments on the questions posed by the ANOPR. We invite all of today's panelists, as well as those attending today, to send their comments on disruptive trading practices to disruptivetrading@cftc.gov.

I want to thank our distinguished panelists for agreeing to appear today and to share with us their insights and thoughts on disruptive trading practices. Our first panel consists of experienced market participants who have faced many of the issues that we will discuss today. We want to thank the panelists not only for their time, but in this budget crisis period, also having paid their own way to this roundtable.

We're broke. Our panelists are John Hyland from the U.S.

Natural Gas Fund, Rajiv Fernando from Chopper Trading; Adam Nunes from Hudson River Trading Group; Cameron Smith from Quantlab Financial; Liam Connell of Allston Trading; Don Wilson from DRW Trading Group; Joel Hasbrouck from NYU; Gary DeWaal of Newedge; Mark Fisher of MBF Clearing; and John Lothian of John J. Lothian & Company.

Before we begin, there are a few housekeeping issues. This event is being transcribed by a court reporter who will be taking a verbatim transcript. This event is also being listened to by members of the public via listen-only teleconference. Because we are not webcasting this conference, I ask that each speaker state their name before they speak so that those on the telephone will know who is speaking.

For the panelists, please turn your name cards sideways if you want to speak so that the moderator will know to call on you. We will have a 15-minute break around 11:00 this morning.

A few other ones, as I said, the meeting is being recorded. The microphones are push-to-talk, please press your microphone and speak directly into it. When your indicator light appears red, your microphone is on. When you finish talking, please press the microphone again to turn it off. Please refrain from putting your BlackBerry or cell phone on the table as they will cause audio interference.

We will not have opening presentations, instead we will go right to the questions posed by the ANOPR. With that, I will turn it over to our two moderators, Steve Sherrod and Andrei Kirilenko. Thank you.

MR. SHERROD: Okay, I'm having technical problems now.

Good morning. Thanks for being with us. We have a lot of questions to cover in the morning panel and we have a lot of interesting people that we want to hear from, so as a suggestion -- and it's only my suggestion because I'm just a moderator -- I'd like to group our questions, and we're passing around a copy of the questions out of the Advanced Notice of Proposed Rulemaking, and I would like us to group our thoughts around different groups of the questions.

So, roughly speaking, maybe the first six questions that we could handle together, then question seven separately, eight through 11, and then probably the next three questions, 12, 13, 14, separately, and 15 through 19 as a block. That might help us manage our time just a little bit better, but we want to make sure we hear from each of you, so don't hesitate to raise your hand, put your card on end, to chime in, because we are really interested in hearing your opinions.

MR. HIGGINS: And Steve, just for housekeeping, for the people on the telephone, the numbers that you referenced also correspond to the ANOPR question numbers, correct?

MR. SHERROD: That's correct. All right, so I'm going to start, I guess, with John Hyland on my left and we'll work our way around and we'll work our way back in the other direction. So, with that, John, I'd be very interested to know your views on the first set of questions.

And if you don't have any views, that's okay, too. We can wait until you do.

MR. HYLAND: We're dealing with questions one through -- which did you say?

MR. SHERROD: One through six.

MR. HYLAND: One through six.

MR. SHERROD: So, these are the general questions at the beginning.

I apologize if we didn't get organized this way.

MR. HYLAND: When you were telling us what questions we were going to be following I didn't have the question -- they hadn't made it around, so I wasn't able to mark them up appropriately.

This is John Hyland. I'm with the United States Natural Gas Fund, or more specifically, I'm with the United States Commodity Funds, which is an operator of a number of different exchange traded commodity funds of which United States Natural Gas is one.

Looking around the panel I probably represent a slightly different viewpoint than many of the other participants here in that I probably am representing the viewpoint not just of passive commodity index funds, which my group certainly is, and there are a number of others like that in the United States, but also looking around I'm probably representing what I would describe as the natural longs and the natural shorts in the marketplace -- large players who are not intraday players, who are not liquidity providers, who are not market makers, who are not looking to make, you know, a small amount of -- you know, a fractional share 1,000 times an hour, but instead are typically taking large positions that extend over days, weeks, months, and who are therefore -- many of the topics that we're discussing today -- spoofing, others -- simply don't fit into -- or even algorithmic trading -- don't fit into the profile of the kind of trading that gets done by players like ourselves or others, therefore our comments -- or my comments and, as I said, sort of acting as a representative for the passive index world generally or for the natural longs and natural shorts generally -- our comments are, you know, we are totally in favor of cracking down on manipulative behavior, we're totally in favor of cracking down on disruptive trading practices. We have two concerns; concern number one is that in attempting to take action against those who engage in some of these practices, most of which appear, looking at the questions, to be ones that are being executed intraday at a very high speed, in cracking down on them we have a concern that this could lead to an overall reduction in liquidity, which would certainly affect those of us who are not involved in the trenches intraday -- interday, but who do have to, you know, move in and out as liquidity demands if you're the passive indexers or if you're the natural short who's the hedger as your physical book changes.

So, we have a concern that the unintended consequence would be for the liquidity to be driven off so you throw out -- in driving out the bad practices, you're also going to drive out good practices, we'll see a reduction in liquidity.

Our other concern is that there could be a view here that somebody who is a, you know, natural short, so somebody hedging 10,000 contracts of crude oil because they're, you know, long a bunch of physical, and who's matching up with somebody who wants to be a natural long, which in this case would be the passive index fund because essentially if you listen to Gorton and Rouwenhorst, we're in a business of selling price assurance to the physical hedgers. The mere fact -- where we're concerned is that in talking about disruptive practices, particularly around the closing period, that if PG&E or Chevron wants to sell 10,000 contracts at the close and I want to buy 10,000 contracts at the close, that somehow the mere size of the trade that we're doing could be described as disruptive, even though from an economic standpoint they're a natural seller and I'm a natural buyer, and so we have a concern that -- not only that in the case of the liquidity issue, that the baby gets thrown out with the bathwater, but also that this could be -- that the final conclusion here could be sufficiently vague enough that the -- that you could take what would normally be considered perfectly acceptable trades without the slightest hint that there's anything manipulative or disruptive about them and simply, because it's politically convenient, describe them as being, uh, that's too large a trade. We don't really want Chevron selling 10,000 oil contracts to United States Oil.

So, those are our two concerns. Looking at this --

MR. PEASE: How do you think we can provide clarity, particularly with the -- this is Bob Pease -- with the issue that you just raised about large trades during the closing period?

MR. HYLAND: Well, you do specifically reference a practice in here dealing with closing -- you know, the matching up of closing prices -- or buyers and sellers at the close which is buying the board, which is certainly not something that I think likely lends itself to misinterpretation but, you know, when you start talking about orderly execution I think, you know, you would have to specifically state that size by itself is not a factor in determining whether trades at the close are disruptive.

If you naturally have -- you know, if Chevron wants to roll 10,000 contracts short because they're long, the physical, and we're the other side of that trade, the fact that it's 10,000 is 10,000. You would simply have to say that size by itself is not a factor. It would have to be other facts and circumstances, you know, buying the board or spoofing or what have you, that creates the -- that crosses the line and allows it to be described as being disruptive. Otherwise I can tell you, you know, all the large, physical hedges are going to be really cranky with you.

So, I mean, I think that -- from our standpoint, that's a factor. Within these other things, I mean, when you are somebody in our situation, if there is spoofing going on and to the extent that it -- you know, we don't trade during the day. I don't care what the price is at 11:00 or 12:00 or 1:00, I care what the prices is at 2:30, but to the extent that spoofing or these other practices do in fact ultimately affect the 2:30 price, we are probably the loser and therefore we're all in favor of cracking down on these, but once again I'll just leave it with the comment, we're worried that you will drive out the good with the bad, that we'll lose liquidity, and in seeking to eliminate disruptive trading practices, you'll do that, but you'll buy greater market volatility because the pool will be thinner -- will be shallower, and as we all know from growing up as children, that it's more dangerous to jump into a swimming pool that doesn't have a lot of water in it than it is to jump into a swimming pool that does have a lot of water in it.

MR. FERNANDO: Hi, I'm Raj Fernando, CEO of Chopper Trading. We trade several asset classes, cash and futures. We do some high frequency trading, some algo trading, some longer term trading going to days and even weeks. I support the CFTC's effort to ensure that markets operate in an orderly way that's fair for all participants. I think I have basically three main points to get across today. That's one of them.

Second, it's imperative for there to be a multilayered, coordinated approach with risk controls and market checks to ensure market stability. And third, any trading practices with the intent or reckless intent to manipulate markets and disrupt fair and equitable trading should be prohibited. Anyone in violation should be held accountable.

I think it's important to note that our markets, for the most part, are incredible efficient right now, incredibly liquid right now, and the bid-offer spreads are incredibly tight right now, and whatever regulations that are put forward, we do not want to hurt that part of the market.

MR. SHERROD: Do you want us to -- tell us -- this is Steve again -- tell us a little bit more what you mean by the multiple levels of checks. Is it your obligation as a trader? Or -- we're kind of bleeding over into another question about what pre-trade risk check should be your responsibility and what should be the executing brokers responsibility if you're using one of those?

MR. FERNANDO: Well, I'll speak for my firm. We have several layers and redundant risk checks all up and down our whole company. As the nature of proprietary trading, this is our money, we have no investors, and we are going to be very careful to make sure that nothing goes wrong.

If after it goes from our firm, the clearinghouse is left making sure that we are being responsible and anything that we don't pick up, the clearinghouse will have to pick up. From there it goes to the exchange and the exchange is going to make sure the clearinghouse is doing their duty to make sure that these risk checks are in place all the way down the line.

MR. SHERROD: Any particular pre-trade risk management checks that you rely upon?

MR. FERNANDO: We have dozens and we are very -- they are very thorough and we're very diligent about it and we have dozens of people in our company that do nothing but keep track of this.

MR. NUNES: Hi, I'm Adam Nunes from

Hudson River Trading. Thanks for having me here to share our views on these topics.

So, I just want to start out, and it's something that John touched on, just as far as, you know, putting in these and kind of throwing out good practices with bad, you know, I think the first thing to lay out is eliminating bad practices and disruptive practices is going to make the market more liquid and more efficient overall. It will allow legitimate practices to occur without the risk of being manipulated and I think overall that's going to be good for end users and good for, you know, firms like those around the table.

So, in getting into the questions, you know, I think that first off, additional guidance, you know, as laid out in the release, is going to be necessary. The -- I think a few short sentences on this is not going to be sufficient to, you know, cover the activities that we need.

One of the things that is, I think, critical, is just kind of looking at the landscape. We have a number of exchanges across futures and equities that have rules that, you know, certainly cover, you know, C, which is the spoofing aspect, that typically talk about bona fide orders, bona fide quotes, and, you know, the prohibition against submitting orders or quotes, you know, with the intent of, you know, effectively manipulating others to act in a way that they otherwise wouldn't. So, you know, FINRA Rule 5210, Section 9 of the SEC -- of the Securities & Exchange Act, lay those out and there are a number of other exchanges. I think it's Rule 432 at the CME and CBOT, that lay out -- and I think maybe 514 -- that lay out, you know, these exact things and I think if you look at the way that they describe, you know, what's described here as spoofing, it does it in a manner that isn't overly prescriptive. You know, we obviously don't want to put ourselves in a position where you can do something slightly different and it doesn't meet the definition, you know, so there's certainly kind of the intent aspect of this that's important to cover, but when you get beyond that having, you know, kind of having the rule that lays out the overall activity, if there are specific practices within that that can be enumerated -- the FSA put out a release on layering as an example where they didn't have to change the rule, they just said, you know, we have this rule, this type of behavior, we believe, is covered by the rule -- it is extremely helpful to market participants because, you know, it takes something that, you know, perhaps was in a gray area, maybe much closer to black than white, but it makes it crystal clear and allows firms to put in the, you know, the procedures and processes to ensure that they're not engaging in activity that, you know, that would have that character.

The other thing that I think is important in looking at these things is looking at a pattern in practice. There are likely to be legitimate activities that can happen randomly and not particularly often that could in that single instance, look like something that could be, you know, manipulative or spoofing or whatever it is, but that, you know, just happened randomly as an occurrence of firms sending a lot of orders into the market, and that would differ quite a bit from seeing that pattern, you know, happen, you know, time and time again, day over day, so I think that looking at things from that perspective, certainly from a surveillance standpoint, is going to be effective and, you know, I think if you look at per se violations, if you do A, B, then C, you know, then you've definitely violated versus seeing the pattern in practice of that type of activity is going to be more effective in, you know, in kind of spending the Commission's resources and, you know, finding people who are breaking rules.

Just specifically to violating bids and offers, that, you know, should generally be for firms that trade, you know, electronically, something that's going to be enforced by the exchange. It raises a couple of topics in my head, one is just the interaction between the floor and the electronic market and how that works. And the second would be in the instance where you have products that are listed across multiple exchanges, how that would be applied.

MR. HIGGINS: Adam, if I could interrupt. Sorry, this is Mark Higgins. Could you just describe the difference between markets, as you speak, with the violating of bids and offers? And then secondly, if you view that prohibition in 747 of Dodd-Frank as being a per se violation? Or are there facts and circumstances that should be considered when looking at violating bids and offers?

MR. NUNES: Yeah, I think the equities markets provide a pretty good example where they have Reg. NMS that governs trading across venues that list the same -- you know, the same security or the same contract and the options market have something quite similar where they provide a framework that, you know, basically says you must have processes and procedures in place to reasonably avoid trading through a displayed better offer and then, you know, more or less a sub-framework on that that lays out how one should do that, and I think that that is definitely a workable format from, you know, from a market participant's perspective. It allows you to, you know, set up a framework and set up a system that will be compliant, but we're operating in a world where it has a lot to do with technology and if you drop a packet that contains a quote, you're not going to see that quote, you know, until you re-request it and get it back 100 milliseconds later, and that's really a fact of the electronic trading life. So, it's not going to be perfect, but it can be extremely close to perfect.

So, I think having the processes and procedures in place is the right approach. You know, it seems hard to believe that a firm that's 99.999 percent compliant with, you know, never trading through, drops a quote and that's a per se violation and they're fined for that where they have a system in place that, you know, is very robust.

So, I guess moving on a little bit more, I think the other thing here is, you know, when we look at disruptive trading practices and the intentional reckless disregard for orderly execution, to me that is going to be a very difficult one to define. It seems like it would be very difficult and I think John hit on this very well, to put a contract limit on orders because there are large players who have a lot of exposure to hedge.

Similarly, it's very difficult to put all participants -- and this is not just, you know, the trading firms, but end users, in a position of being judged after the fact, you know, when they put an order in that, you know, that they put thought into, that they chose an execution strategy that they thought was going to be effective, and it just so turned out it didn't work and that, you know, to me again just gets into, you know, do you have appropriate policies and procedures around what you're doing and how you're doing it, and do you have effective supervisory and controls around that where if you do, then that should minimize the likelihood of that happening, but I don't see how we can eliminate it, and putting, you know, all users in a position of being judged after the fact, I think, puts them in a difficult position.

There was one that I -- question five -- that I specifically wanted to address which I think gets to -- I'm sorry, it was question six -- just gets to order activity as opposed to executions only where I think that from my perspective it's pretty clear that we should be looking at both orders and executions across, you know, basically all of the things that -- well, I guess violating bids and offers has to be an execution, but you know, across intentional and reckless disregard for orderly execution as well as spoofing. I think that, you know, certainly with spoofing it's often just going to be orders. So, I think that looking at orders as well as executions is appropriate.

MR. KIRILENKO: Adam, thank you. This

is Andrei Kirilenko. Thank you for those very last comments that you made. I think that perhaps to make things a little bit more general, sort of some general comments, is that these disruptive practices, in a way you could think of them as extending the Commission's jurisdiction into the area of orders rather than executions. Executions typically have to do, you know, with when manipulation is being looked at, attached to that was executions, or as these specific areas are in the area of sort of orders and order submission, and there is a reason for that, and the reason for that is being -- is that in anonymous electronic markets, there is a lot -- you know, the market participants communicate to each other and communicate with the market by submitting, cancelling, and modifying their orders, and therefore, that's where the jurisdiction should move into, and so one of the sort of broader questions, to the extent that other participants could comment on it, is where should that boundary be? Where should that regulatory boundary be for the Commission? And how well should it be defined? Should it be defined very clearly or should it be defined clearly in some areas and be left in principle in other areas and some would be (inaudible) circumstances?

I understand that as some of you have already said, that the more clearly it is defined, the better you can define policies and procedures so that you don't overstep over these boundaries. However, there might be some areas where that boundary will be moving as the market is developing, so to the extent that you and others would like to comment on the sort of general terms of where that boundary should be, would be very useful.

MR. HIGGINS: Just before you speak, Adam, I just want to recognize that Commissioner O'Malia is here. He heads our Technology Advisory Committee, and so we thank him for his participation.

MR. HYLAND: This is a question -- this is John Hyland. This is a question for Robert, actually. If I make -- under current rules, if I make a bid or an offer with the intent to cancel the bid or offer before execution, let's ignore how you're going to prove that in a court of law, let's just say I do it, is that under current CFTC regulations an acceptable practice, bearing in mind that I'm not a securities lawyer?

MR. PEASE: Well, one of the things we want to do today is put as much meat on the bones as we can to what it means to cancel bids or offers, what would be legitimate practices, what would be reasons. That's why we want to hear from you all today, as different types of practices. What is a legitimate business purpose to be canceling the orders before execution? Are there such legitimate purposes or should there be an automatic ban? When does it become disruptive to the market?

So those are the issues that we actually want to hear from you all on today.

MR. HIGGINS: And to that point, John, I just want to echo that we're here to listen and to the extent staff does say anything that sounds like an opinion, it's just staff's opinion, not the opinion of the Commission or any other staff members. So, I just want to make that clear.

MR. NUNES: I have a question, hopefully -- so, to Andrei's question, were you asking that specific to question B? Or was that for, you know, basically A, B, and C?

MR. KIRILENKO: I was asking it respect to all A, B and C.

MR. NUNES: Yeah, so I think that, you know, drawing a line between the Commission's jurisdiction over orders versus execution, from my perspective, the Commission does and should clearly have jurisdiction over both, you know, their activity taking place in commodities in the U.S. and, you know, from my perspective, you can't look at -- you know, you can't have an execution without an order, so from my perspective I don't understand why you would separate the two.

You know, getting to Robert's question, just kind of more generally on the practice of submitting orders and canceling them, you know, I believe you should send orders because you want them to be executed and that there's not really another reason to legitimately send them to market. But there are a number of legitimate reasons why you may end up canceling them and frankly why you may have a relatively high proportion of them that are canceled. Some of those are less in the futures market in the U.S. just because there are fewer venues trading the same product. But, you know, they're typically going to just boil down to market conditions, you know, whether related products have -- you know, the price has moved or the price of that product has moved, and then a firm's risk profile. So, I may have taken a position in a related product that led me to no longer want to buy the product that I'm quoting, so, you know, the CME has limits on what your order to execution ratio is and so this is unlikely to be, you know, at present, a major issue in the futures market.

On the equities market where you may be

trading across, you know, a dozen or well over that venues, and you're layering the book to provide liquidity across multiple venues, you could have one hundred or hundreds of bids and offers out and as you're adjusting your position based on related products moving, based on that product moving, based on your risk position, you can end up with a relatively low order to execution or a relatively high order to execution ratio, you know, for legitimate reasons just because you have a lot of risk out there and a lot of orders out there because as a liquidity provider, you don't know where the next order's going. It could go to one of dozens of venues that trade that product.

So, I think the issue in the futures world is already a lot smaller just because you don't have that, you know, but we're managing our risk and we're trying to do that in a way that, you know, we're sending orders that we want to execute, but we can change our mind, you know, due to risk factors, you know, in a short timeframe.

MR. PEASE: What would be a short timeframe in your mind?

MR. NUNES: The timeframe could be extremely short. I think that one area that you can look at is, you know, does someone have a pattern and practice of sending orders, like let's pretend that an exchange can process an order, send out the quote in one millisecond and then it takes a millisecond for someone to respond to it. In that world, like, if you're canceling an order in less than two milliseconds, then no one effectively has the chance to interact with it unless it's by chance that they happen to be sending an order.

Now, a firm can do that, you know, for perfectly legitimate reasons because they sent an order and, you know, immediately after sending it got an execution they no longer wanted that risk, but if you have a pattern and practice of doing that, and you see that that's an activity that a firm engages in, you know, that from my perspective is certainly worth asking questions about why that can be legitimate and what they're trying to do with that activity.

But that just kind of to me gets back to the per se versus pattern and practice approach to this.

MR. FERNANDO: Can I make a quick comment? This is Raj Fernando, Chopper Trading. I could give a perfectly legitimate reason why I would put in an order with no intent to have it executed. Say I'm trading bond futures at the Mercantile Exchange, the Board of Trade, and my limits are set for 100 lot and I want to change it to a 200 lot. So, I go through my risk procedures and have it checked. I put 200 (inaudible) off the market with an intent to cancel it just to make sure my risk procedures went through correctively. I have no intent for that trade to ever be actionable. Is that a violation? I think there's no reason that should be.

So, I think it is dangerous to be getting pigeonholed with too many rules that could open up a whole can of worms here.

MR. NUNES: I'm not going to comment on that. But what -- from my perspective what does matter and what you can add on to what Rajiv said is, was there intent to manipulate someone else to get someone else to do something? So, whether or not that's legitimate, what is clearly not legitimate would be sending in, you know, 1000 lot because it's going to lead people to think there's more demand, you know, in the market than there truly is in order to get them to, you know, either join the bid or in order to lift the offer.

So, you know, from that perspective -- and that does get into the intent, not just to cancel, which is laid out here, but the intent to manipulate, which I think is also, you know, critically important.

MR. SMITH: I'm Cameron Smith. I'm from Quantlab and I don't know if it's fortunately or unfortunately but I'm going after Adam who seems to have a lot to say about a lot of this and stole a lot of my lines, I think. But what I'll do is I'll reiterate a few of, I think, the key points there.

I do think, like Adam does, that we need to elaborate on these -- these rules need to be filled out a bit and there needs to be more material and I think what really needs to be there in my mind is some notions of intent or phrases like "for the purpose of" to the extent that quotes are entered or trades have an impact on the market, they have to be done with a requisite intent or -- and there's a lot in the equity market, as Adam also mentioned. There's several good examples of that. I think Section 9 of the 34 Act has some language like that. FINRA has a few rules. There's the rule on quotations -- what was that, 5210? And the CME also has -- so, I think there's already rules out there.

My concern here is that these rules, lacking that, can capture a lot of activity that we -- I don't think that the intent is to capture and I should note, I think John sort of brought this out and maybe I'll say it more directly, and that is, while I suspect a lot of these rules were aimed at controlling automated trading, I think when you really think about these practices and think about what this says and apply it to what really goes on in the market, natural buyers and sellers are the ones who are actually trying to avoid market impact. So, in a certain way you could say that they're the most likely to engage in practices that are intended in a certain way to deceive, right, because they're trying to avoid -- they're trying to do a lot of product. They don't want the price to run away from them. So, they're going to dribble it out, maybe they'll even, if they're buying, maybe they'll put a sell order in occasionally just to moderate that price move. Who knows? I mean, but they're the ones that are more likely to have price impact, and I'm sure that's not the intent and that's why I think we've got to be really careful with these rules and make sure that there's an intent portion of them, otherwise we are going to discourage legitimate, important trading by end users, natural buyers and sellers, and we certainly don't want to push that off the exchange and in the OTC markets because if there's some uncertainty as to whether or not they're compliant.

So, I think that point may be kind of missed because like I said, I do think that these rules seem to be aimed at automated trading but yet perversely, I think that it really actually creates more concern for an institution because I think they're the ones that are actually more engaged in the things described here because of the nature of their trading and the impact it has on the market.

Automated traders typically trade in relatively small sizes. We're not going to have the same kind of market impact as an institution or a big natural buyer and seller who has real positions to hedge.

MR. CONNELL: My name is Liam Connell. I work for Allston Trading, a proprietary broker-dealer that trades in electronic markets, in futures, and in equities.

I think a lot of my points have already

been covered. I think one point I'd like to make is that, you know, Allston Trading supports the mission of the CFTC to maintain orderly markets and to prohibit deceptive practices and manipulative trading. My concern is that, you know, what might determine disruptive trading is going to be dependent both on the venue and, you know, the technology capabilities of that venue and the specific market that that venue is supporting. And, you know, I'm concerned that very rigid rules will not take that into account.

My other concern is that some of the wording about the illiquid markets, we want to ensure that we don't drive liquidity away from those illiquid markets. I think participants should be allowed to take -- you know, to take liquidity that's available in those illiquid markets and if we lay down too many rules in relation to that, we may drive liquidity away from those illiquid markets when we really want to encourage liquidity in those illiquid markets.

And then my concerns, and considering we have 19 questions and these are the first six, I will yield the floor.

MR. WILSON: This is Don Wilson. I'm the founder and CEO of DRW Trading.

So, I think that one of the most important things that we would like to see out of this process is that the rules are clearly defined. If rules are not clear, or if rules are backward looking, in other words, an order, which winds up moving the market a lot is after the fact deemed to be disruptive merely because it moved the market a lot, not because there was any intent to move the market a lot, and if that then is deemed to be a disruptive order and a violation, the central marketplace will be significantly harmed. Exactly the intent of the, you know, the intent of Dodd-Frank was obviously to bring more transparency to the marketplace and actually exactly the opposite will be achieved. I think that what will happen is that market participants who have large orders to execute will conclude that the regulatory risk of entering the large orders into the marketplace are -- is too great and they will instead execute the orders most likely as block trades or some other privately negotiated transaction so that they don't have to take on that regulatory risk.

It would have obviously very adverse effect on the central market place.

As far as some specific comments on the first six questions, as far as violating bids and offers, I think that it's important to differentiate between the securities markets and the futures markets. Adam, you know, describes the way that the securities markets work and there seems to be a pretty good system there, a mechanism.

In the futures markets an identical futures contract which -- contract specifications, which is listed on two different exchanges and is cleared at two different clearinghouses, will frequently trade at different prices because different market participants will have a desire to be -- to buy one instead of another, maybe for

-- because they're offsetting a different risk at different places. Frequently we see in the energy markets the relationship between the ICE and NYMEX trade at a spread merely because the order flow is all one way and at some point people get tired of buying one and selling the other, they run out of capital, and so the spread tends to trade at a premium or deficit. I don't think that there's anything inherently wrong with that. That's just the way that the market works and so I think it's very important to differentiate between securities and futures and understand that different futures on different exchanges, or even a mini future and a big future, both listed on the same exchange, can trade for very good reasons at different prices. I also think that, you know, a futures contract which is traded in the pit may trade at a different price than a futures contract traded on the screen, and that's just market dynamics and order flow. I don't think that that's -- you know, that the CME generally treats those as different ticker symbols even although ultimately the contacts wind up in the same open interests.

So, I think that, you know, some careful consideration needs to go into, you know, what is expected to be caught in the violating bids and offers framework.

As far as canceling orders and where you draw the line, what's okay and what's not okay, you know, my general thought is that somebody who enters a large order, who really has no intent of buying but actually wants to sell, you know, or has no intent of selling but actually wants to buy, so, is entering an order in the opposite direction to what they actually want to do, and demonstrates a repeated pattern of entering those orders, getting other people to join them, pulling them and then, you know, going the other way -- I think that it's fair to say that that's an unacceptable practice.

On the other hand, it's quite common for people to enter orders that are larger than they actually want to transact because, for instance, the allocation algorithm is a pro rata algorithm.

The market participants generally believe that that's an acceptable practice and I think it is because at least the market participant is not signaling intent -- an intent to buy when they want to sell or sell when they want to buy.

Now, Cameron brings up an interesting point which is that for large end users who are trying to move large orders through the central market may find it beneficial to occasionally, you know, if they're buying, enter sell orders or if they're selling, enter buy orders, in order to make their activity a little bit less transparent to the marketplace so that they can execute at better prices. And I think that it's an interesting question to ask whether the intent would be to ban that type of behavior, which, from the perspective of the person executing the large order, really isn't intended to be manipulative, it's merely intended to improve their execution. I think that's a question that should be carefully considered.

As far as disruptive trading on the

close, again I think that it's very important to not put in place rules which prevent people from executing orders in the closing period. Generally there are lots of good reasons that people need to execute large orders in the closing period that have nothing to do with manipulating the closing price. There are lots of reasons for taking off risk at the end of the day. And so I think that the definition of those rules around, you know, what is and is not acceptable in the closing period needs to be carefully considered. Certainly an intent to manipulate the closing settlement price by engaging in inefficient execution is something that I think is unacceptable, but merely entering a large order, even if it winds up moving the closing price, is -- should be an acceptable activity.

And then just one last comment, the question about buying the board in an illiquid market, you know, I think that people who have hedges to execute or, you know, otherwise need to enter large orders and move large amounts of risk need to have the flexibility to do that in the most efficient way possible and certainly buying the board, which just means that you're simultaneously buying several different contract months, for instance, may be the most efficient way and prudent way of executing that order and reducing that risk.

So, I don't think that there's inherently anything wrong with that.

MR. SHERROD: Don, would your opinion be different if someone were adding risk rather than reducing risk?

MR. WILSON: Well, I think that it really comes down to intent. If somebody is, you know, purposefully trying to -- you know, and I think that there was an example cited somewhere of somebody in the egg market, you know, purposefully moving the price and, you know, after they bought the board and bid up the price, then they, you know, cleaned out the whole book and then they bid a one lot significantly higher, I think that it's fair to say that that activity, there was some intent in that activity because they were executing it as inefficiently as possible.

So, I think that that's really where I draw the line, not so much whether it's risk adding or risk reducing.

MR. PEASE: What type of clarity would you suggest -- this is Bob Pease -- would you suggest that we add if we go forward and define these types of rules so that you can know more in advance what would be prohibited rather than being subject to an investigation after the fact?

MR. WILSON: Well, again, I think that intent is a really helpful criteria to put in this stuff and, yeah.

MR. HIGGINS: This is Mark Higgins. If I could just jump in for a second. It seems that a theme that is coming through so far is that intent is the all-important determining factor. I just had a question as we continued along the line here. Are there certain practices that are so bad that on their face you'd like to -- you think they should be prohibited because they're disruptive of fair and equitable trading, without having to go into an assessment of the intent or the facts and circumstances underlying a specific trade? And I throw that open to the entire panel. I don't know if anybody has a special view, but maybe Joel, if you want to take that one.

MR. HASBROUCK: I'm Joel Hasbrouck. I'm a professor at the Stern School at New York University. And my area of specialty is mostly empirical analysis of market data.

I've looked at an awful lot of high frequency data, some from futures markets, but mostly from equities markets.

My first point is that we're here today because of, really, technology and it's important to remember that this technology is not yet mature. So, we're trying to hit a moving target here and in this kind of regulatory environment, I think it's better to be a little bit conservative, leave markets room to evolve and then impose regulation to address the worst excesses.

Now, this does not say, you know, we

shouldn't be concerned about another May 6th -- circuit breakers, price limits, great, but I think it's difficult to get definite rules in detail about prohibitive bidding, offering, or trading practices that aren't going to constrain the efficient evolution of markets.

A couple of specifics, one, the process at the close, we know from other markets that one procedure seems to work pretty well which is a single price call auction at the close. You have a period where orders can be entered, an order and balance is published, beyond a certain point, submissions and cancellations that aggravate that imbalance are prohibited, and then you have a clearing in an orderly fashion. It seems to work well in equities markets and some futures markets and options markets abroad.

Another point, and Adam raised this question about multiple markets trading essentially the same thing, and he raised it in connection with a violation of bids and offers, that is trade-throughs. Now, Reg. NMS in the equity markets did address that but it's important to remember that that was contingent on markets being "fast", that is, if you wanted your prices to be protected, you had to be in a position to respond pretty quickly. So, for example, Reg. NMS would not apply in a situation like side- by-side trading where you have a contract traded on Globex and the pit, the pit being essentially a manual open outcry market would be considered slow and it's quotes would not be considered eligible for protection.

Lastly, the question has come back again and again to intent. I'm so leery of defining rules or prohibiting practices based on intent because as markets and strategies evolve, so many things that look illegitimate at first, often very rational and constructive rationale can be attributed to it. For example, in equities data, I have seen certainly extreme cases of somebody changing the bid and offer maybe 84,000 times in two or three minutes, and that, to my eye, is spoofing and should probably be prohibited, but if

I look at the intent of a rapid cancellation and resubmission, I think, you know, why do we change our bids? Well, we change our bids and offers because the information has changed somehow. And well, how rapidly are we getting new information? When it was a floor market, we'd get new information, maybe one update ever ten seconds but in an electronic market where we are continually monitoring all the news feeds and all the market prices from other securities, those updates are essentially coming continuously.

I would put it out there that I could, I think, justify practically -- for a person who monitored those feeds, I think it would be very difficult to establish an intent as opposed to a legitimate purpose.

Thank you.

MR. KIRILENKO: Thank you, Professor Hasbrouck. This is Andrei Kirilenko from the CFTC. I have a question for you, perhaps, that you can comment on. You said that -- you said something very interesting, you said that the rules have to take into account the evolving technology in the marketplace and to that extent, these rules, how would you try to put it into these specific rules? What -- how would you advise to put specific technology that is available now, and evolving technology in the future?

MR. HASBROUCK: First, I don't know -- I think rules based on intent in evolving technology are impractical. They can certainly be written, but I think were any cases to be brought, I think they'd be relatively easy to defend.

I don't do this work myself, but I know people who do and of course, as do you, and it's very easy to constructively come up with alternative explanations for a given pattern of behavior.

So, what would you do? First, I think a rule that's directed specifically at spoofing is probably too narrow. I recognize that that is in the Dodd-Frank bill, but I think it's going to be based on intent and I would not be in a position of wanting to -- of having to define it.

If you think that the problem is bids and offers that are being quoted too rapidly, then you could do what at least one market has done which is prohibit cancellations below a certain time threshold. You want to put a bid out there, it has to be good for at least 100 milliseconds. Rules like that sort of get away from intent and really address very narrowly the particular thing at the moment that seems to concern us. So, I would say that would be one example.

MR. FERNANDO: Can I comment on that?

MR. SHERROD: Sure, go ahead.

MR. FERNANDO: This is Raj Fernando, Chopper Trading. If there was some kind of minimal time limit to holding bids and offers, I'll speak for my firm, if we're making markets in the treasury complex and we had a certain amount of timeframe we have to keep a bid in the five-year future and we're trying to get a hedge up from the five- year cache, all that will make us do as a firm is widen out our bids and offers which will provide less liquidity and the spreads will all widen and it will be extremely detrimental to this market.

MR. NUNES: This is Adam from Hudson River Trading. Just one thing to add to that is from my perspective rules should generally be technology agnostic. You know, I've lived through electronic trading since, you know, the late '90s and 100 millisecond rule in 1999 would have been somewhat absurd because it took seconds to get orders executed whereas today, you know, that would be over 100 times longer than the fastest, you know, exchange can respond to something, so codifying timeframes like that -- and if you look at Reg. NMS, it's one second -- one second in the equities world is a material delay at this point whereas one second ten years ago would have been really fast for a lot of markets.

So, from my perspective, unless there is something specific to the use of technology, it's agnostic. You know, firms are using technology to do things that humans used to do and they're just using, you know, the efficiency and leverage that they get out of it. They're not necessarily doing anything particularly different.

And I just wanted to add one thing to what Don and Joel said on the Reg. NMS thing. One of the other things Reg. NMS assumed is that the product was fungible. So, you know, if you buy a stock on one exchange you can get out of it in another, where that's not present in the futures market and that's, you know, kind of a fundamental aspect to the violating bids and offers and I just raised it as to me it raised issues that weren't -- that were broader than, you know, when you're greeted on its face, it's like electronic markets take care of that, we don't need to worry about it. It raised these other issues that are much more thorny.

MR. SHERROD: Thanks, Adam. Can we turn to Gary and then we'll get back to you?

MR. DEWAAL: Hi, Gary DeWaal here from Newedge. And I think it's helpful as I prepared for this -- first of all, for those who don't know

Newedge, we're a global broker and one thing that we may be a bit different is that we look at things holistically. We look at asset classes, we do business, we broker financial assets, we don't care really whether they're future securities or cows walking in on the street, and that sort of may permeate some other comments I make throughout the day.

When I thought about these comments I also thought about my own background. My own background was I actually started in this industry on your side of the table, I started as a CFTC enforcement attorney. Obviously now I'm a general counsel of this big global broker and when I was in law school I supported myself by being a stringer for the New York Times, so I think of these things in terms of headlines and the headlines I have on this are -- and some of this is repetitive, but the first headline is, what does this mean, okay? This is an incredibly vague provision and I think what's somewhat misleading is to look at this provision -- the provisions that we're here to address today -- in isolation.

Well, they're not in isolation. This is Section of what is Section 4(C)(a) of the Commodity Exchange Act, and I think that in analyzing this section, you've got to compare it with some other sections. Okay? And that's what makes it, to me, so confusing because I'm an old guy and certainly I've been around for a long time and the basic prohibitions of 4(C)(a), which were considered the trade practice offenses -- and I'm looking particularly at 4(C)(a)(2)(b) has a very standard provision which basically says it's illegal to cause prices to be recorded -- registered or recorded that are not true or bona fide. Okay? And in fact if you look at a lot of the enforcement cases over the years, you'll notice that whenever they charge someone with a wash sale, when they charge someone with an accommodation trade, this or that, they always say, and non bona fide. So, it was always this offense coupled with something else.

Now, what's also interesting about -- if you look at this 4(C)(a), it sort of has a really interesting preamble. It talks about, it's unlawful for any person to offer to enter into, enter into, confirm the execution of a transaction. So, it very clearly takes the whole framework from orders, execution, et cetera, and then of course it goes to the offense.

You compare that to the physical structure of the provision that we're looking at today, which is 4(C)(a)(5) -- very, very confusing because there's no parallelism. You have a provision, as I said, that's been around for a long, long time, and now you're talking about it's unlawful to engage in any trading, practice, or conduct. Okay. Right off the bat I don't know which -- you know, trading I think I have an idea of, practice, maybe, conduct, how do those three things differ from each other? How do they differ from entering into, offering to enter into, or confirm the execution of a transaction? Whether I'm from the CFTC side trying to prosecute a case or I'm from my side trying to defend a case, words have to have meanings, and it's not clear, even before I get to the substance, what we're talking about because the distinction between the historical language of 4(C) and this new language is so dramatic that I don't know what it means.

So, that's my first issue. The second problem is, even the construct of this 4(C)(a)(5) by itself is remarkable. Now, you know, I can't -- my firm doesn't let me trade futures, but if I just went through the plain language and I was a retail investor buying gold futures who was a bit lucky and was seeing the price rise and I was making money every day and I tried to protect myself by trailing it with stop orders. Well, and I was hoping that my stops would never get elected because that would mean that I was making money every day. Well, now I realize I've just violated the Commodity Exchange Act, because it says, it's a violation for any trading -- okay, so theoretically, one stop-order is any trading -- if my intent is to cancel the bid or offer before execution. Well, I really want to cancel that stop order because it means my price has risen higher and I can cancel that order and put in another trailing stop order.

So, you know, to me that's the first headline. This is just way too vague. Now, again, you know, how can you fix it? And I think that's one of the goals you hear, what can we do to make it better? Well, I think, again, intent, absolutely. I mean, you can't have incidental, you can't have accidental, I'm not even sure you want to have negligent, I'm not even sure how recklessness fits into this although obviously it's part of (5)(b), but it seems to me you need actually two components because what we're talking about is, as far as I think what's going on, and again, maybe I'm wrong, maybe who knows, the intent is to cause a non bona fide price. We're back to that theme of non bona fide price because, you know, the intent -- that's what the markets are all about. We're all concerned about the integrity of prices, okay, so all these things are bad because at the end of the day somehow prices are affected, and the most common prices, you know, trumpers (inaudible) can play is back in 4(C)(a)(2)(b), non bona fide price. Okay? So now I'm asking, well, if that's the thing we're striving to prohibit, why am I even here? Why did I need this provision? It seems to be completely redundant of something that's been around for a very, very long time, you know, tried and true, and we still don't understand it. I mean, we know that the intent to cause a non bona fide price is a bad thing and it's something that's actionable and the CFTC's got lots of cases on that.

So, it seems to me, ironically, the way you fix this new provision 4(C)(a)(5) is basically by going back to the old provision and applying the standards that are there making this new provision entirely redundant and unclear, but unfortunately that's "not the way" that lawyers handle something, because obviously if something is here it's got to mean something different because that's always what they teach you in law school. If the language is here, it's something different, it's got to mean something else, and I've got to tell you, I don't know what it means because I keep going back to the fix, the fix is already there and this is something uncommon.

So, now where would I go from here? Well, I do think the best thing that I have heard is what Adam suggested, you know, I think -- and I think Joel just suggested it also -- technology changes dramatically and it's not -- we haven't seen the end of this. I mean, you know, I'm going back to, you know, my first days when I was in the Commission and I literally sat -- I went down to the floor of the COMEX and stood outside the gold trading rink to watch what was going on and I think of where life is today, it's just remarkable and the one thing we know about technology is that the speed of change collapses. So, the magnitude of change that occurred over 20 years or 30 years, will now occur over the next generation, will occur over 15 and then it'll keep on -- and we have no idea where it's going to go.

So, I do think that, you know, the way

to deal with it -- you know, I think it was a mistake in the statute, frankly, to talk about spoofing because I really don't know what spoofing is except getting some kind of, you know, internet solicitation that probably is meant to take my money, and I'm not sure of the definition of spoofing can be agreed upon by the ten people around this table. And by the way, my mother used to always tell me that whenever you put quotes around a word, it's because you really don't know what it means, so don't do that in a paper -- she was an English teacher -- don't do it in a paper.

So, I do think what Adam suggested and Joel implied is a better way, which is I think that here I think that the exchanges probably are in the best position to say what kind of specific conduct, now and again, they think is problematic. Okay. So, if there's something specific that is bothersome, fine, then deal with it in a guidance, deal with it in something so that folks like Don, before they go out into the trading -- before they go out onto the screens, know what they can't do specifically, and then you'll have the flexibility of withdrawing it and changing it as conditions change along the line.

I've always been struck, to a certain extent, that the clearinghouses and the exchanges get to live in a world of principles-based regulation and the rest of us are all micro managed to death, and here I think there really is a benefit for a principles-based regulation. I mean, we're stuck with this provision of statute which frankly is bad law, you know, to me it was not necessary, and frankly confuses the situation, and to me the only way to get out of it at this point now is in fact to -- you know, for the exchanges who I think are closest to it -- and by the way, I think that the problems that we're going to have are different from exchange to exchange. I don't think that the kind of problematic trading that may exist on one exchange is necessarily replicated on all the exchanges. Some things may be unique. I mean, obviously LME is not in the United States, but the kind of circumstances that are unique to the LME may have no applicability to other exchanges because of the nature of the trading there. And obviously some of the exchanges still have open outcry pits versus electronic. Some exchanges have mini versus maxi contracts, and as Don has said, we also have situations where you've got contracts now which are traded on multiple facilities but are basically the same contract.

So, it seems to me that you've got to sort of get the exchanges get much more involvement here. I think that, you know, to the extent that they've got specific concerns, let them issue specific guidance as to things that are problematic and should be avoided. That gives the guidance. But I've got to tell you, if it was considered a technical correction, I would work on repealing this provision which I just absolutely think is unnecessary in light of 4(C)(a)(2)(b).

MR. SHERROD: Moving on to Mark Fisher.

MR. HYLAND: Gary, tell us how you really feel.

MR. DEWAAL: I'm a little bashful about expressing my true views, but --

MR. SHERROD: I was going to stick with Gary for just a minute. This is Steve Sherrod again. So, what I hear you saying -- I just want to make sure I've got it right -- besides all the other commentary about congressional intent, you suggest that perhaps we should adopt a principles-based approach so that we require the exchanges to address the concepts in 4(C)(a)(5)?

MR. DEWAAL: Yes. I think, again, I think that at the end of the day, you know, the specific issues are better within the jurisdiction of the exchanges. I'm just -- and, again, I think I'm going to defer to the guys who trade day-to-day, I'm just looking at this more broadly -- but it just seems to me that there are nuances on each exchange, that that could get fouled up with some kind of broad based provisions.

MR. SHERROD: Okay, thanks. Now we'll move on to Mark.

MR. FISHER: Hi, I'm Mark Fisher from

MBF and I'm very happy that Gary went before me because if you think Gary speaks his mind -- I know some of you know me, you have no idea.

I'm sure also that half the people in this room, when I get done in the next ten minutes, are going to want to choke me, but, you know what, it is what it is.

By way of background, I am a clearing firm. I'm also (inaudible) firm, I'm also an index creator, I also used to be in the dinosaur days, probably the largest local in New York, and I'm also an academic, so I basically cover the background and I think what really, if I understand the question here, is the Commission is looking for specific answers, specific things, and I'm going to put through a lot of specific points that I'm sure half of you are not going to agree with, but I figured if I got done here with -- I might as well just speak really how I feel, and I'm sorry if I offend anybody.

First of all, everyone -- the electronic revolution that's taken place, the technology I'll talk about, is based on one word: Speed. Call it what you want, everybody in this room who's trading is basically a speed merchant and what we basically have to do is say, what type of technology is it that's going ahead and who's faster than who? Colocations, the amount of money being spent on colocations, the amount of speed, how quickly you can (inaudible) and everything else, versus the technology that goes in and lets you play chess better. If you're going to be a bad chess player, if you're, you know, Jim Simons from Renaissance and you're using your technology to trade based on how you play chess, great. But this is all based on speed.

I think the reason why all this is taking place is because there's a fear that (inaudible) in the marketplace is evaporating. May 6th, the flash crash, you know, took away a lot of people from the market trading, they're not going to be back. They got stopped out on crazy prices, filled to ridiculous levels, and there's an easy solution that no one's going to like. I don't know if any of you have been to NASCAR, but if you go ahead and you're on a wet track or there's an accident, okay, just slow everybody down, everybody, you know, until you go ahead and markets are -- go back to some type of normalcy. And in terms of closes, the easy thing to do, and the suggestion that Joel (inaudible) is the right one. You know, come to a single price, but use the motto where basically everything is transparent, every single day at 3:40 in the afternoon, I believe, they post every single market imbalance and every single stock, so it's completely transparent. Make everything transparent and then slow everything down. If you're concerned about closes, slow the closes down. Slow it so that -- and the exchanges all have the mechanism, it's called throttling. They could do it whenever they wanted to. I think the CFTC has the authority if they wanted to also mandate throttling and in terms of market duress, in terms of periods of, you know, when you know things are going to get crazy, slow everything down.

In terms of the indexes, I still don't understand why an index is rolled over five days, John. Why isn't it rolled over in four days, why isn't it rolled over in 15 days? Because the longer period of time that you roll an index, the less impact you'll -- the less impact those rolls have over the marketplace and the less important closes become.

Why is a close the basis for any index anyway? Why has the close become such an important price for an index? Why shouldn't it be a view-of over a period of a day so that you don't have to target the close? And I don't mean just you, I mean every index. And some of this would go away.

The fact that, you know, canceling any order with the intent to cancel, well, I don't know of anyone who (inaudible), puts in orders in the pre-market between 5:45 and 6:00, but every that's there is canceling every order because it's all just a speed game, how quickly I can get my spreads in, so everyone bombs the exchange, for lack of a better word, I don't mean -- you know, bombs the exchange with speed, how fast is someone's colocation, to go ahead and be the first one on the gold spread, to be the first one on the t-bond spread, to be the first one in the TAS market, right, with the intent that if they don't get -- if they're not first, second, fifth, sixth in the queue, they cancel those orders. They're all canceled before the market opens at 6:00, but in that preopening window, every order is done with the intent to cancel.

In terms of credit, okay, of all these orders that are going directly without any credit checks, I mean, my big concern is that we're going to have another May 6th and it's all based on speed, it's all going to be based on the fact of a lack of accountability of credit checks. I think the SEC is starting to address the problem now with -- you know, in terms of who can actually go direct and who actually has to be slowed down. I haven't seen anything about that in the commodity world. In the futures world I've seen that, in terms of trading the close. Well, if I'm a roll participant and I'm going ahead and I'm, you know, trading the roll of the GSCI index or an AIG index or whatever it may be, it's all transparent. All the rolls should be transparent, not just the USO rolls, not -- it should be that every roll is completely transparent so everyone's on a level playing field, and if you are the creator of an index of a roll, you should not be able to go ahead and in-house that roll yourself, you should have to go ahead and have that roll executed in a marketplace so that you can't have Bank A go ahead, create an index, and Bank A's prop desk go ahead and in-house that roll. Inherently, that's insanity because it's very simple to see what takes place in the close now versus TAS, or what takes place in the close now versus a large order, but until the OTC markets are integrated, which now you have jurisdiction over, which is going to take a number of years, a lot of the stuff that takes place in the closes is because of stuff that's completely, you know, non transparent right now, you know, based on an OTC market, based on knock outs, based on knock ins, based on things that, you know, are not even -- that no one can see.

If you go ahead and look at -- if you look at what's worked, the CME stop price mechanism, which slows you down, works. What does it do? Slows everybody down. Okay? I think that, yes, I mean, I'm not a lawyer, I'm not a regulator, okay, but I've actually been everything else in this industry. I talk way too much, but the point being is, I've been there. Okay? Basically all that's really happened is, you know, technology has taken the local from the floor and put it to you guys upstairs, but you know what, if we don't go ahead and police our own markets in terms of speed and allow the confidence in the markets to stay (inaudible), you know what, so everything slows down for five minutes in the close, so there's no edge in that five minutes to (inaudible) against a T-bond. Big deal. Okay?

But you go ahead and have a lot more people be -- you know, the confidence of the markets will be there.

The ECN model place should be there for OTC markets, basically, you know, like with the NASDAQ-ARCA model, you can place everything -- place them, you can see all the bids and offers (inaudible) and ECNs, whether it be ICAP, this one, that one, you could see all the markets on one screen, and in fact, everyone should be able to trade every market. It shouldn't be that a market participant who qualifies as an ECP, or whatever it may be, should have to go ahead and go through hoops to be able to go ahead and trade on a market. You know, as long as you qualify, you should not have to go -- you should be able to trade in those markets to make tight enough markets. There are some markets you can't even trade on unless you get permission from the exchange itself even if you do qualify.

The VWAPing of closes and the VWAPing of (inaudible) and of trading (inaudible) and what I call the non transparent (inaudible) which take place if you're an index provider -- index creator as well as an index liquidity provider to your own index, you know, if everybody -- if every index was as transparent as John's index, the amount of volatility would go away a lot. The fact that you have all these proprietary people -- traders at different houses that go ahead and be able to in-house their own rolls against their own -- against what their sales force sold, for me, without the marketplace being able to see, is a humongous problem. And I think that whether you're right about every single thing -- you know, the rules are wrong or the rules shouldn't be wrong or the rules are right but now they're wrong -- I'm not really sure -- or all the rules are wrong -- I'm not really sure what the question is. The point being, you know, specific suggestions -- if we're all down here, instead of just going ahead and saying, yes, we all agree that Dodd-Frank -- let's roll up our sleeves and give the Commission specific suggestions to help them make rules that are going to make sense. Intense, very important, right? Obviously, right? But I think that if we're here, let's have one committee that actually says specific things, and if we get ourselves into trouble we have lawyers to go ahead and say, well, he really didn't mean it. You know? Let's do that as opposed to just, you know, just talking pie in the sky stuff.

MR. SHERROD: Hey, Mark. You're going to have another shot, but I want to get around at least once and let John have one shot before we take a break and then we'll start back this way. Thanks.

MR. LOTHIAN: Sure, I'm John Lothian. I'm a futures broker, commodity trading advisor, new media entrepreneur. I've been a prop trader, I've done a lot of different things within the markets and am a keen observer of all the markets.

You know, first off, futures markets are about two things, they're about price discovery and risk transfer, okay? The price discovery process is an auction process. The futures markets is different from the securities market in that it's more of a request for quote type of market.

I equate a lot of all of this to where we came from in terms of open outcry markets, okay, so for example, if I offer something in an open outcry market, as soon as I drop my hands, I'm off, the offer is no longer good, okay, and quite frankly, I can't keep my hands up all day, okay, even if I had an offer that was good for all day long, okay, and was the market. So, there's always going to be, you know, sell six at eight, I'm off, okay, type of thing. So, what I'm trying to do is I'm trying to discover where the price is so 100 at 8, okay, well, quite frankly size matters when somebody wants to come into the market and they're going to pay more attention to that size.

A lot of the orders and canceling and stuff that we get as part of that price discovery process is part of the noise in the market in discovering where people are going to trade, and quite frankly, there are practices that happen in open outcry in terms of, you know, here's a noisy pit, so guys are going to come, run over to that pit to trade because they were attracted by that noise. If you see trades in the electronic market and size in the electronic market that's really noise within the market, guess what, you're going to run over there and you might trade or you might be caused to trade because you see a particular type of behavior or action.

All those things happen in open outcry, they still happen in markets and it's perfectly legal and acceptable.

John, all trading is algorithmic, okay, whether you know it or not, okay. If you hand an order to a broker and the broker's got 100 to buy and he goes into a trading pit, he's going to go, you know, two bid for 50, okay? He has algorithmically decided to not impact the market by splitting the order in half, and two guys are going to go, sold, and he's going to go 50-50, okay, and that was an algorithmic trade that the broker executed on your behalf, okay? Electronic algorithms do the same type of a thing. They are hiding from the market volume so as opposed to trying to influence the price by showing excessive size, they're trying to influence the price by showing minimal size. Okay? How is that any different?

In terms of intent, short of water boarding the developers of the systems, I'm not sure how you get an answer as to what the intent is.

MR. SHERROD: We can do that.

MR. LOTHIAN: Yeah, in terms of closing ranges, you know, that is some of the most chaotic trading in an open outcry environment that you will see, okay? Short of prearranged trading, short of something to make it more orderly, it's going to be always chaotic in terms of the noise coming out of the trading pit, the pitch -- the open and the close are going to be the two most disorderly times in terms of the amount of noise coming out. There are some tools that are used, as were pointed out, the TAS, or the trade at settlement, where the settlement type of process is important. That is a technique that can be offered by exchanges in order to mitigate some of the volatility on the close, and that in and of itself is something that's traded during the day where you can trade plus the settlement or minus the settlement and take care of that, and that can alleviate some of that, but it also takes away from some of the, perhaps, natural price discovery process. It's also a deterrent for continuation of open outcry because a lot of the trade in some of the open outcry pits that still exists, revolves around the roll and revolves around those closing prices during the roll and all of that, so if you make it more electronic, you are going to hurt those legacy markets.

You know, the recurring theme in terms of spoofing that I hear is equating to the Potter Stewart quote about pornography, and that is, I don't know how to define it, but I know it when I see it. I went on the internet last night, I said, okay, what's spoofing, I looked it up. Now, without being self-serving here, it shows up on Wikipedia, you know, for a spoofing attack, there's a list for spoof of 9 or 10 different types of things on Wikipedia but none of them have to do with trading, okay, so there's no definition there. There is a definition on a page within MarketsWiki which is in quotes, which means that it's a little undefined and it's only got one source of one story, okay, so it's a very undefined type of a term within the industry. You know, do guys in open outcry bid or offer more than they are really willing to trade? Yes. Can people hit them? Yes, if they get them before their hands come down.

MR. SHERROD: That's probably a perfect segue to a break if we could start back with you at 11:15, and we'll start talking about spoofing. That work?

MR. LOTHIAN: Sounds great.

MR. SHERROD: Thanks, so we'll start back at 11:15, about 15 minutes.

MR. PEASE: For those who are here, please make sure that you've signed in. We want to keep a record of everybody who has attended this roundtable today and there are sign-up sheets out in the front. And we would like to get started with the second half of our morning panel.

MR. SHERROD: I want to very quickly thank everyone again, this is Steve Sherrod, and give Cameron, kind of last shot at our first block of questions because I skipped you earlier, and then we're going to move on to other blocks.

MR. SMITH: Thanks. Yeah, I just wanted to respond to a couple of the things that I had heard coming around from the other side of the table there. One was that a couple of the gentlemen had mentioned that intent is difficult to prove and therefore maybe we should dispense with that requirement. I think it's absolutely critical to have something in this rule that says something to the effect of, you know, entering quotes, or what have you, for the purpose of creating a false appearance or to deceive or to manipulate, and without that I think it's going to lead to, again, as I talked about earlier, uncertainty and actually, I think, reducing order flow from the natural buyers and sellers. I don't think it so much affects the automated traders.

So, that's one very important point. The other point had to do with slowing down the market, which I don't know how directly related that is to the actual proposal, but, you know, to the extent we have a concern of excessive use of capacity, Joel mentioned 84,000 orders he saw, or something, over some relatively short time period. To me that's not a regulatory issue directly where somebody needs to bring an action because they've decided that that's too many orders. Again, I think those have to be limited to instances where they're doing it for the purpose of, that, again, you need intent. And finally, I don't think it should matter if it's difficult to prove intent. Either you have a case and you can prove somebody's doing it for a certain reason, or you don't, and, you know, you can dispense with intent and that would probably increase your conviction rate, but I don't know that that's a healthy thing to have a high conviction rate. I know I used to live in Romania and they had a -- people told me they had a very high confession rate there, but I don't know if that is something that we want to emulate.

But on the speed of the market, we know by definition that slowing the market down has a cost, right, because it makes the market less efficient. Is it a huge cost? It's hard to say, but we know it's greater than zero, and I would just submit on that, what's the problem we're trying to solve? What is the benefit? Are our markets really as unhealthy as some people are claiming? Every time I see studies, even Joel recently did one, I'm not seeing anything that leads me to believe that the markets have never been more efficient, more healthy, and more liquid, so to the extent we're trying to solve a problem, I'm not sure what it is. There's just some vague notion of investor confidence because there's mutual fund outflows.

I was just at a conference the other day, Dan Matheson from CFSB gave a great presentation where he showed that in a historical context mutual fund outflows are a blip, that there are several other years going back to 2000 where there's much greater out flow, and that actually a lot of what's going on is that people are flowing into ETFs and out of mutual funds, so there's this competition there. And that's being missed.

So, I don't want to even accept this premise that we have to restore investor confidence by intentionally adding trading costs to the market. I think that's just the wrong direction to go in. Again, I don't know how related that is, but I don't like to leave those comments floating out there lest they gain some legitimacy. Thank you.

MR. FISHER: Can I respond to that, because obviously -- right? I mean --

SPEAKER: Can I control you?

MR. FISHER: You could try.

MR. SMITH: Your comments on indexes were pretty good, though.

MR. FISHER: Real quick. Okay? Looking at the flash crash, right, the CME stop market functionality actually helped that day, right? What's the functionality of that stop logic? What did they actually do? What did the market do? They slowed the market down. No, no, real quick, those are rhetorical questions. In fact, at the CME conference a couple weeks ago, Naples, Florida, Paul Jones put on a presentation that said that the only reason -- one of the reasons why the market came back after the crash is because eventually CME shut the market all together for a period of time. Is there a cost? Sure there's a cost. But the market came back from only because they shut the market. Okay? And they stopped the market completely from trading.

And so I would say to you, as much of an algorithmic trader you are, I'm sure I'm nowhere near in the league as you are, I'm just saying investor confidence is the reason why all these rules of Dodd-Frank have been passed, because if investor confidence was higher, half the rules that Gary was talking about wouldn't even have gotten through. So, again, I think it's kind of shortsighted just to say, protect speed, protect speed. I think everything's on the table. That's it.

MR. NUNES: Well, just to respond to that quickly, and hopefully mediate a little bit. I think it's the case that there's a difference between having safeguards in place to make the market more resilient, which is things like limit up, limit down, stop spike logic, that I'm guessing, by and large, automated traders agree with and endorse, and frankly to the extent that they work and are effective, they'll make the market better because they -- you know, without them, we're adding risk to the market it doesn't need and reducing that risk will be good overall, versus just the general notion of, slow everything down, and I think to that point, you know, Cameron's right, that unless there's some intent or belief that that's going to improve price discovery, trading costs and just overall market quality, there's no reason to do that. So, I think having the resiliency absolutely, and things like limit up, limit down, and stop spike, make a lot of sense, and we support them, but it's more just a matter of kind of the blanket notion of, it's too fast, slow it down, and that's where -- like, why would we make the market worse if we don't have to?

MR. SHERROD: And I'm going to get -- I'm going to suggest a slightly different format for our next hour or so. We're going to try to cover a number of blocks of questions and we're going to skip a few because the next question, seven, will be dealt with by the second panel, so the next topic I'd suggest is to discuss any input you want to give us on spoofing, which are in questions eight through 11, and if you want to give your input just put your name card on end and we'll get to you, and otherwise you can respond as the people that have specific input, because we have about three or four blocks of questions, and if my math is correct, at the rate we're going, we're not going to make it.

So, we do want to get a chance to get specific input, if you have it, on spoofing.

MR. NUNES: So, I think I can be reasonably quick on this. Adam Nunes from Hudson River Trading.

So, I'm going to just focus in on question nine and hit a few points there. So, 9A deals with submitting and canceling bids or offers to overload quotation systems. I know that spoofing is in quotes and it's not well defined, but I don't think that's what it is. That's some different thing that, you know, doesn't seem like a good practice and seems like it should be prohibited if somebody's doing, you know, trying to overload systems and somehow benefit from that. But I don't know that it fits the character of what we're describing as spoofing.

MR. SHERROD: Should we call it something else, like denial of service?

MR. LOTHIAN: Quote stuffing.

MR. SHERROD: Quote stuffing?

MR. NUNES: Sure. From my perspective, it's unclear to me how that can be effective. If you overload a system it's unclear to me how you can benefit from overloading the system, but if someone's figured that out, we should find some way to make that not happen.

MR. HIGGINS: Adam, if I could follow up -- this is Mark Higgins. If you don't agree that that is the definition of spoofing, what in your view would be spoofing --

MR. NUNES: Right, so --

MR. HIGGINS: -- and are there other specifically named practices in the trade that you're aware of that you think should be specifically enumerated?

MR. NUNES: Yeah, I think when you get to B and C, and frankly, from my perspective, spoofing is just a subset of a broader thing, and if you look at this in the context of the rules that it tends to be a part of, it tends to be a part of rules that are much more broad and have to do with, you know, sending out false crop reports, right? So, it's basically just manipulating the market in general and spoofing is, you know, kind of one aspect of that but, you know, it's one very narrow aspect of that, but it should be looked at in the context of that, right. Price discovery on exchanges is about incorporating information and some of that information is going to be macro, some of it's going to be things like crop reports that are going to be specific, but some is going to be supply and demand, so spoofing, you know, tends to be specific to that portion, but it's part of a bigger thing.

When you get into submitting and canceling multiple bids or offers, in order to, you know -- or for the purpose of what it says here, causing a material price movement, I don't know why materiality needs to be in there. If you're manipulating the price by one or two ticks, I don't know why that's okay, if it's not okay to do it by six or seven ticks. So, I would just argue, if you're entering bids or offers, if you're executing at successively higher prices for the purpose of, you know, manipulating others and creating a false appearance in the market, it shouldn't matter by how much you do that. You know, I think Don spoke well about, you know, when people are executing, they're trying to minimize their price impact, you know. If you're executing in order to maximize your price impact, then there's likely some reason you're doing that, so I think when you get to that, I don't know why materiality matters, orders matter, executions matter. It's really a matter of, you know, if every time you bid for 1,000 contracts, why do you end up selling five and not executing the 1,000?

So then, you know, clearly on C, which is submitting and cancelling multiple bids or offers to create an appearance of depth -- yes. I think that makes sense to be a part of it and I noted, you know, earlier, and Gary talked about non bona fide prices, this all fits into that, it's just describing that in a way that's -- you know, provides more clarity.

So, I think that's one part. The other part that I wanted to talk about is, you know, question 10, which gets to, what if you get a partial fill. Well, from my perspective, a partial fill does not eliminate the activity, it's really a pattern and practice of activity and, you know, we kind of live in a trading environment that's probabilistic, so if something works, you know, a high proportion of the time where you're able to manipulate the market and make money, you're going to factor in, sometimes somebody's going to hit my bid and I'm not going to make money on that trade, but by and large, if you look at the activity they're engaging in, the pattern of activity would likely be profitable or they'd stop, but, you know, saying, well look, it's a firm bid, somebody could trade with it, and the fact that somebody happens to, a small proportion of the time, doesn't in my mind exempt that activity.

MR. PEASE: Would it fall under the definition -- this is Bob Pease -- Adam, of spoofing, or does it get another label when you have a partial fill?

MR. NUNES: Oh, I think it's -- it's the same label, right, and, sorry but it does go to the intent of that order. If you enter, you know, a five contract sell with the inside market or trade (inaudible) inside, then enter several 500 lots on the bid side with the intent of, you know, manipulating someone to lift your offer because you've given them the appearance that there's more demand than there is, and, you know, after your offer is filled, whatever happens, you wipe out all those bids because you have obtained your objective, it doesn't mean someone can't trade with part or all of your bid, you're just looking at, what's the probability they do that versus the probability that they lift my offer.

So, from my perspective, when you see that type of activity, they don't know what the outcome is but they probably have a good idea of the probabilities of the outcome, so they don't control whether or not someone hits their bid or not, they control the activity they engage in, so from my perspective you can look at the pattern of outcomes and you should be able to distinguish that from legitimate activity and, you know, typically if you see them do that where they enter that on the bid side a few seconds later, maybe they're entering it on the -- they're entering a five lot on the bid and hundreds of contracts on the offer to, you know, unwind the trade.

So, from my perspective, the outcome -- I guess, the pattern of activity that they engage in is what matters. They can't control who lifts their offer, who hits their bid. So, I think that's one aspect.

The other thing that I just want to address is, there seems to be a notion that somehow spoofing and the life of orders or the speed with which they're entered and canceled, are kind of tightly connected and I don't think that

that's necessarily the case. You could have those orders sit out on the market for several seconds. If they, you know, if they determine that the product's not very volatile and there's an extremely low likelihood of them being traded with, it's not the case that, you know, they're just entered and canceled, entered and canceled. That's probably a less effective way to get somebody to engage in the activity you're trying to get them to engage in.

MR. SHERROD: I'm going to turn to Gary and then Mark.

MR. DEWAAL: Yeah, I mean, I think that intellectually we sit here and say, well, what is spoofing. We all sort of think of it, well, it's the bad placing of orders and pulling them back real quickly, but I'm not sure where that gets you as enforcement folks, I don't know where it gets us as the industry, again, and I think Adam's correct, I think that there's two things that have to be done because, as I said before, this is a bad statute.

I mean, I think clearly all these offenses -- it's not just the issue of spoofing, I think there does have to be an intent, there does have to be a causation, and there has to be the intent to cause either an artificial or a non bona fide price. I think then what is also necessary is to clearly define what's not within this universe because the problem is, it's out there right now, and again, it's got to mean something because otherwise Congress wouldn't have written it. I think it's very important that it be defined to say that it's not meant to be accidents, it's not meant to be negligence, it's not meant to prohibit block trades, it's not meant to require best execution, it's not meant to prevent legitimate strategies to facilitate the execution of bona fide orders, and it's not meant to prevent price volatility or rises or falls in prices, and I think that one of the problems that you guys have that all agencies have, is that you're reactive to things that happen in the public sphere and obviously the politicians want to respond to it and you get stuck with it, but I think it's very, very important because of this provision -- and I'm going to assume it's not going to be repealed anytime soon -- that those two elements are included -- what all these elements must have, the intent, the causation, artificial and non bona fide price, and what it's not meant to prohibit.

MR. HIGGINS: Just a quick follow-up, Gary, though by your formulation, it ceases to become a disruptive trading practice. It starts to look a lot more like a manipulation and that may be a theme that I've heard, you know, quite a bit this morning, but it seems to me that if Congress put a manipulation prohibition and other bad acts separate from disruptive trading practices, and so, you're right, assuming that Congress means what it says and does things deliberately, this should mean something other than what you've just formulated.

MR. DEWAAL: Sure, but then I'm going to Joel, and since I see he wants to speak next, I've never understood the difference between a price that comes about -- the problem with the price that comes about as a result of manipulation, which is 6(c), and a non bona fide price under 4(c). Okay? I mean, again, that goes back to the Commodity Exchange Act when it was first adopted. It's out there, so there's clearly a problem, but I think that we always speak in terms of an artificial price and somehow an artificial price is either the non bona fide price or a price comes out as a result of manipulation.

MR. HIGGINS: My comment was actually more of a question although it didn't probably have a question mark at the end, and that is, where does the line get drawn for you and for others, perhaps, between disruptive trading practices, which we had -- and manipulation?

MR. DEWAAL: I mean, I think -- again, I think that in the end the answer is, there's not a big fundamental difference because in the end, both are meant to affect the price and the price that results is an artificial price. I mean, let's -- again, as I think John said very, very eloquently, this is an auction market. Okay? The only thing we care about at the end of the day is the price, and there are the prices that come about because of normal forces of supply and demand, and then there's something else, and again, you know, I wasn't around as far back as the original adoption of the Commodity Exchange Act, but, you know, there are different routes to that artificial price, there's the route through trade practice violations, the wash sales, the accommodation trades, in the old days, you know, the illegitimate cross trades, things like that, and there's a route through manipulation. The courts have, you know, come up with different tests for the different elements, okay, so we know that there are different characteristics, but in the end we're speaking about a price that does not come about through the normal forces of supply and demand.

MR. SHERROD: Mark?

MR. FISHER: Real quick, I think one of

the things that should definitely be distinct from spoofing is because what I described before about the pre-market order flow, you know, whether you're putting in spreads, whether you're putting in TAS, whatever type of orders you're putting in, limit orders, I would say that if you look at -- I listen to the energy markets, 99 percent of those orders are canceled, more than 99 percent are canceled before the market even opens, so I think that all those pre market orders, which would be completely exempt from any type of spoofing whatsoever.

The second thing I think that the Commission should be aware of is, and it happens more in the less liquid times of markets -- overnight, 6:00 and on, you know, 4:00 to 5:00 in the afternoon, is what I would call, you know -- which is a kind of spoofing but not really, I think, the way it's put out here, is there are orders that are put out there, small orders, two to sell, three to sell at a price, and what these orderers have then done is, if a quantity is tried to buy of say 50 or 100 or 200 or 500, these orderers sniff out that there's a large order and immediately they'll go ahead even though they sold two, they'll take a loss and buy 20 at a higher price thinking, okay, algorithmically that these orders, they're basically racing these orders. This doesn't typically happen as much during highly liquid times, but this happens especially, you know, from 6:00 at night to 2:00 -- until London opens, there's a tremendous amount of orders that are being put in, I'll sell two at this price, if I can fill -- and I see the order that's trying to buy it from me is a 50 lot order that's unfilled, I'm immediately going out and buying 20 lots and racing that order, hoping that order is then going to come (inaudible). I don't know if that's spoofing or not, but that's probably, you know, some type of spoofing, fishing, whatever you want to call it -- fishing (inaudible), but some kind of a word along those lines.

MR. SHERROD: Sniffing works for me.

Joel?

MR. HASBROUCK: Thank you. I was going to say that spoofing was any practice with an intent to deceive, but then I thought about the last time I tried to buy a new car and I concluded that both me and the dealer could have been arrested.

Instead, let me just -- the first time I've encountered the term spoofing was perhaps about five years ago in connection with a case I'm briefly going to describe the elements of and because I think it generalizes.

In the equities market there is a practice of retail brokers who will agree to execute customer trades at the national best bid or offer, so the trader in question was putting in a limit order to change, when he really wanted to sell, he put in a limit order to buy. He raised the national best bid and then sent his order to his broker forcing his broker to buy at the higher price.

And when I think about the manipulation

cases -- and I don't think there's a big difference -- they often involve a price that's being used as a reference price for some other transaction, for example, if you have a trade at settlement and it's a large volume and you're going to be buying, then I would perhaps want to consider spoofing any activity that would try and depress the settlement price because I'd be putting in orders that would be against my ostensible economic interest.

But beyond that I think it's difficult to really pin this down, so I'd leave it there.

MR. FERNANDO: Raj Fernando, Chopper. I think it's important to note that exchanges do regulate all of these practices and it would probably be important for the CFTC to work with these exchanges but one of the functions of the local, who is the ex-pit guy who's now gone upstairs on the computer screen, is price discovery and if somebody is showing a bid for 1,000, he might be flat, he might be showing a bid for 1,000, or say he's long and he's hoping he can sell the offer -- by showing the bid for 1,000 the guy on the computer screen right next to him might say, this guy's playing games, I'm going to hit his bid and make him sell to me a tick lower, and these are normal practices in the marketplace by locals that are there to provide liquidity and this is common market activity and I think it's important to not box in with these specific rules and more, work closely with the exchanges and see what is and what is not manipulation and with intent or reckless intent to harm these markets.

MR. SHERROD: John?

MR. LOTHIAN: I'm going to disagree with Adam and agree a little bit with Raj there because if I'm putting 500 lots into the market, those are actionable orders, okay, and there are some traders that are attracted by not only price, but also size. So, if there are, you know, on steps down -- on five steps down there's 500 lots, I might go, you know what, I've got 2,500 to sell. If I come into the market I know it's going to move the market five ticks anyway because of the way that they sniff out big orders, I'm just going to go ahead and take it for an average of three ticks worse.

As a trader, I might not even care what is on either side other than just making sure that there's adequate size to be able to handle my order without it, you know, influencing it as much. So, if it's an actionable order, it's an actionable order, it's part of the price discovery process, even if it's part of somebody's strategy or game or whatever, it's a bona fide order within the market.

There are some practices that I have seen that I would describe as spoofing that are similar to the one that Joel described in terms of the stock example, okay, so we have price bands within futures, you can't execute an order outside of a price band of the last trade, okay, and so let's say you have a gold order, the price band's $10, there's a gold order in an off month, it's off $10 -- it's off $15, okay? I go and I buy that market $15 higher. I know that that order's going to be busted because I'm going to call the exchange and I'm going to say, hey, that order was outside the $10 price band, okay, and so -- but immediately after I did that order I go ahead and I bid within the price band, you know, so here's this guy who thinks he sold it at $15 and, you know, and now he comes in and he's bidding for it $5 lower or something like that, you know, because he's trading, and I hit that. So now I've sold something $10 higher and really the trade above is going to be busted, and so now he's paid $10 higher.

So, gaming the system like that using the rules and some of those bands, those types of things I would qualify as spoofing.

MR. SHERROD: So, let me see if I can repeat very quickly. So, a trader would enter an order within the price band but outside the no-bust range and then ask to have it busted --

MR. LOTHIAN: Right.

MR. SHERROD: -- and then trade in the other direction?

MR. LOTHIAN: Right. Right.

MR. SHERROD: Okay, got it. Cameron?

MR. SMITH: I just wanted to make a couple quick observations. One, I think some of the difficulty here when we discuss spoofing is it is such a narrowly defined practice and I was just going to suggest another bit of terminology. I think just gaming is probably a better word because it's more inclusive, so I don't know if you could get Congress to change it, because it's so narrow that you really do want to capture executions and quote activity and a combination thereof, and then folding that in with, of course, intent and done for some purpose to mislead.

So, that's one observation. It's just, I think that term is just very narrow and, I think, unnecessarily restricts you and your enforcement abilities.

The other one is just, to kind of point out again, I guess to not be constructive in that sense, that this is difficult. I started out in the equity markets and one of the axiomatic things that I always heard about when you were trading equities is that -- and just to pick on Goldman because I guess that's okay these days -- but they go high bid, right, and then you would see a flood of orders over SelectNet, Goldman selling, and you could see it was Goldman, and that was, you know, basically how you traded, and so when you think about these common trading practices, at least common in the equities markets back in early 2000, you know, I don't know if there's a good analogue here in the futures markets, I think, again, as I said before, I think to some extent institutions are going to try to limit their market impact through something similar, that we need to contemplate these things, which I think generally people think, well, that's trading, and how do we avoid capturing those things in here. Maybe we want to capture them, but I don't think we do. So, there's a really -- not a bright line between what I would call old- fashioned trading, you know, again, maybe to limit market impact, and then where do you get into this -- well, I just introduced the new term, gaming. I think it's a real challenge. I wish I could give you a little pithy definition that would capture it all, but it's not easy.

MR. NUNES: If I can just raise one thing. I think John raised an important point, and having been around when the equities markets went from being more manual to where it required, effectively, human response, to where they went to automatic execution, I think that there was a general feeling that things like putting out actionable orders that are automatically executable would, you know, eliminate or at least, you know, reduce dramatically, the ability to, I don't know, spoof or whatever you want to call it, and there's a fundamental question which is, if you're putting orders out that are taking risk, can you be defined as spoofing? And that's important to answer. From my perspective, looking at a pattern and practice of outcomes, where you could see -- I think I said it earlier -- every time you want to sell 1,000 you end up buying 5, if that's your pattern and practice I would argue that, you know, from a probability standpoint you can do it in an electronic market and that it's not just something that is, you know, more akin to what you would have called backing away in the manual days where you put something out that you don't mean to honor it and when someone calls you on it you say, oh, that's no good, I was in the process of changing that.

MR. KIRILENKO: This is Andrei Kirilenko. I have a question to those of you who have trading algorithms that are actually trading and I'd like to ask you if you have anything embedded in your trading algorithms whether there's automated execution or fast trading, high frequency trading that looks at the imbalances of the shape of the order book on the buy and the sell side and reacts to it, and whether or not you've been affected by -- whether you have instances in your trading activity where your algorithms reacted to an imbalance which may have been caused by spoofing, maybe someone particularly put a large order in so the buy and the sell side now appear imbalanced, and that triggered your trading and then caused something -- caused you to trade without necessarily -- and then you discovered that you probably may not need it to. Have there been instances like that and do your algorithms -- are actually designed to do that?

MR. NUNES: So, I think one example of that is FINRA recently had an enforcement case that was settled where if you read through the action -- and I think they kind of defined it as layering, which seems to be another term that fits the definition of what we're talking about, and I believe in the -- whatever they call -- the notice that they put out on that, they noted that the activity, you know, either was designed to or ended up capturing, you know, automated trading systems through that type of activity.

MR. SHERROD: I want to move on then to another question and if anyone wants to comment on question 12, should the Commission specify an additional disruptive trading practice beyond the closing period for particularly large orders? Don?

MR. WILSON: Yeah, this is something that I talked about earlier a little bit but I think it's really important to emphasize that whether in the closing period or during the regular trading day, if the framework is to kind of look back and see whether or not an order wound up moving the market a lot, if it moved the market a lot, then clearly it was disorderly and to then say, well, therefore you've broken a rule, it -- a framework like that would have just a chilling effect on the central order book and would definitely cause people to avoid entering large orders in the central order book and instead entering -- and, you know, use the block trading market, privately negotiate the trades, which would just have a horrible impact on the quality of markets as a whole.

MR. HYLAND: Let me jump on something -- the mere fact that you enter in -- this is John

Hyland -- the mere fact that you enter in large orders outside of the closing period and that it ends up impacting the price I would have thought would just be the normal result of supply and demand and therefore would not in itself qualify as disorderly execution. In this particular context of question 12, I'm not exactly sure therefore what disorderly is unless your, you know, order shows up with tattoos and drunk or something. I mean, what is disorderly execution in this context?

MR. SHERROD: That's what we were hoping you would shed some light on.

MR. HYLAND: Any time.

MR. CUSIMANO: This is Jeremy Cusimano. Don, you mentioned a potential risk of migration to block trades. In CME's rules they have a list of market factors that you need to consider when executing block trades that would kind of govern orderly execution of block trades. Do you think the CFTC should be prescriptive in that nature in defining what an orderly or disorderly execution would be?

MR. WILSON: Well, the CME gives kind of general guidelines about, you know, reasonable amount from -- you know, reasonable distance from the current market, you know, recognizing the size of the order and all this kind of stuff. I think that, you know, if the CFTC -- I mean, an example of the type of guidance that would be very unhelpful would be the following: You know, if a large order -- and you could define large order -- if a large order moves the market by more than a certain amount, then we deem it to be disorderly. I mean, again, that would be just looking at things after the fact and essentially trying to intervene in the supply/demand, you know, or the attempts of the market to find fair value and to sort through the changing of the supply and demand in the marketplace.

So, as I said earlier, I think it's very important to define these rules clearly, so from that perspective, you know, more definition is better, but I could certainly envision some prescriptive definitions that would be very harmful.

MR. SHERROD: John?

MR. LOTHIAN: If there were prescriptive rules for the block trades, I think that would hurt innovation within the market in terms of exchanges competing because that's one of the areas where they have competed traditionally over the years.

In terms of disorderly markets, you know, when you talk about today versus 10 years ago or something like that, with electronic markets, it's really hard to say that you have a disorderly market, it's just moving, okay? A disorderly market, no offense, Mark, would have been NYMEX when they went, you know, fast market, not held for an entire month, you know, type of thing while energy prices were all over the place. Okay? So, you couldn't tell whether your orders were good or not or whatever because the brokers weren't being held. That was a disorderly market.

There are things that happen in the

marketplace that create disorderly outcomes in terms of the prices moving. Sometimes those are when a customer is being liquidated, okay? At the point where, you know, a large position needs to be liquidated in the market, and it may be in illiquid markets, it may be a situation, like the old saying, you know, you eat like a pigeon and poop like an elephant, okay, that's going to have some big market impact.

We -- you know, I was at a brokerage firm in the early '90s, a broker got some customers the wrong way in the middle of the floods. In order to meet margin calls he spread them up into the next year's crop, which was really not reducing risk but adding -- but it reduces margins, the accounts were debit, we systematically worked with a member of the clearinghouse -- or the clearing broker, to exit the positions, but when you're in red (inaudible) beans, you -- and there's not much out there, you've got to work the order and we worked the order, worked the order, we thought we were out of everything, but the broker lied to the person from the clearing firm about getting out of everything, and Tuesday morning after Memorial Day, or whenever, we ended up with stuff still on and the floods were at their peak and the risk manager of the clearing firm, somebody different now, said, get me out. And the price discovery process was you could call disorderly because the price of the spreads moved a dollar and a half, but that was the price discovery process and that was, you know, the economic interest of the clearing firm needing to be defined because it was no longer the customer's position.

So, sometimes things happen within the price discovery process that are not rational or, you know, to a market maker or to a trader, it's part of the chaos of the market.

MR. FISHER: Mark Fisher. I think one of the issues with block trades that should be looked at a little bit is when block trades -- block orders are leaned on. Typically a broker will come up and say, hey, (inaudible), blah,

blah, blah, and he says -- and the broker says, well, I'm (inaudible) good for 500. You know, and then someone works against that order and says, are you still there, are you still there, and they're basically using that order as an out for that thing.

That practice which is obviously not transparent to the marketplace in allowing one person to use the market over everyone else as opposed to saying, hey, make me a market -- two-sided market (inaudible). It's different than the OTC marketplace saying, I'm 60 (inaudible) and allowing someone to work against that order. That to me doesn't seem, for lack of a better word, kosher.

MR. SHERROD: Joel, did you --

MR. HASBROUCK: I think that the large trade problem is in a sense going to go away like it has in the equities markets. The size of equity trades has dropped dramatically with the rise of electronic trading. The New York Stock Exchange used to define a block trade as 10,000 shares or more. There are virtually zero of those now. It's not that people don't have large trading needs, it's just that the technology and using the technology intelligently, has worked in the directions of people feeding these orders to the price discovery process over time.

MR. SHERROD: So, Joel, just to follow up, if someone is feeding a large order, they're buying repetitively small amounts, at some point does that become disorderly if they're buying without regard to the price impact?

MR. HASBROUCK: Again, as an economist I have to beg off trying to make a definition of disorderly that's -- you know, certainly they will be taking into account the price impact of their trades but as John said, there are many situations ranging from rational behavior to outright stupidity where that would be their illegitimate intent.

MR. CUSIMANO: Sorry, Jeremy Cusimano again. I think we've heard a couple times from different folks what would not be considered disorderly, but is there a way that we can create guidelines or at least a frame of reference that's based on some type of market norms that would be able to be used as a benchmark for what might be orderly and what might be disorderly?

MR. WILSON: Since I answered the question by telling you what you shouldn't do before, let me take another stab at it. The -- you know, I think that certainly somebody who intentionally enters an order in a disorderly manner, in order to maximize the price impact of the order, that obviously has some kind of manipulative intent to it, and I think we can all agree that that activity should be banned. Now, I think that it already is because in the process of doing that somebody would, you know, move the price to an artificial level and, you know, to an inappropriate level, they would be doing so intentionally by purposefully executing the order as poorly as possible. You know, again, I think that if you don't have that intent element there, and you let the definition be, you know, and you leave open the possibility that somebody who nearly executes an order inefficiently, maybe because they were nervous, they were panicked, they felt that they needed to get the order done quickly because they were about to -- you know, some event was about to happen, whatever it is, I think that if you leave open the possibility that in doing that somebody is breaking a rule, you really risk pushing them out of the central market. You think you really risk saying to people -- you know, you risk people making the decision, you know what, I just don't want to take the regulatory risk of executing this order in the central market, I'm going to call up somebody and get a block order done.

MR. NUNES: If I can just add on to what Don said, you know, we all have incentives to execute orders as efficiently as possible and to limit the price impact, so typically, I think in the example that he gave, there would be some other interest in that product where, you know, someone might hold 100,000 contracts of it and have, you know, a settlement price or some event that, you know, their execution is tied to, where they say, well, I have 100,000 long on this and I want to price it in a certain way, so if I inefficiently execute 5,000 contracts, I may be able to move the price, you know, in a way that would advantage the other 95 I have. So, I think, you know, typically we all have an incentive not to execute orders in a way that maximizes the price impact, so I think it's often going to be the case that you would want to look at why it is that they're doing it. In some examples they may not be trying to maximize the price impact, but they may be trying to get off a hedge where, you know, they're neutral as to what the price is. As long as they get the trade done, you know, they're hedged and they don't have a true interest in that price. It still doesn't mean that they're going to do it in an inefficient way, but I think typically when you see that type of behavior there is some other reason that's worth understanding.

MR. SHERROD: So, Gary, give us that

specific list.

MR. DEWAAL: Well, I mean, I actually sympathize with Don as a trader because, again, and I'm just a practical guy, you've got to go back to the statute that we have. It's bizarre. Look at A, there's no reference to intent, there's no reference to reckless. Look at B, which is the one we're talking about, which is orderly execution, it includes a standard of intent or reckless. Then look at C, which talks about spoofing, only deals with intent. Okay? So you've got market -- you've got trade practice offenses which are unclear and yet there's three different standards right within the plain language of the statutes. You have to say what this is not, okay, because the problem is, the standards are -- even just using the plain language -- are so different for each sub-offense that if you don't say what it's not, poor traders will have no idea what they can or cannot do. What is the difference when you say violates bids or offers? Because it says intent or reckless in

B, or intent in C, it suggests that an accidental violation of bid offer in A, could be an offense. That can't be it. That will completely dry up liquidity. If the traders think that an accidental violation of a bid order offer could cause a big problem, that's significant.

The statute that Congress has forced you, unfortunately, to have to say what these things are not or we're going to have problems, or people are going to live with this knife over their head.

Stop smiling, Mark.

MR. SHERROD: Raj?

MR. DEWAAL: You can't give your opinion that way.

MR. HIGGINS: It doesn't get recorded in the transcript.

MR. FERNANDO: I think -- this is Raj Fernando. I think transparency is incredibly important and we need to do everything we can to bring more of these orders that are off the market to the exchanges. This would alleviate the credit default catastrophe that we had two years ago, but one of the things that was just brought up could be a slippery slope. If you're long to market and the market is breaking and it's very liquid and you get out very inefficiently, and it moves the price even more, but if you're short the market and you want to sell more and you sell more inefficiently, that's bad? This is all a part of the price discovery and I think as long as all market participants have access to these markets, we have to let price discovery take its course.

MR. SHERROD: Liam?

MR. CONNELL: I just want to make two brief points. You mentioned basing rules on kind of normative rules and normal market conditions. I mean, isn't -- isn't it when the market isn't performing normally that we have to be concerned about? I mean, wasn't May 6th an example that keeps on being brought up? And that's why I think it's very dangerous to make very, very specific rules that might really hurt you when you want market participants to participate. And just a second point is, we're talking about May 6th, when the main criticism of a lot of trading firms is that they didn't trade, not that they traded, and, you know, again, I think we've got to take that into account when we put rules together that we're not discouraging people from trading in public markets when perhaps they're most needed. That's just the point I wanted to make.

MR. LOTHIAN: I agree with the transparency issue. I mean, one of the biggest things about the translation of many of these practices from an open outcry environment into an electronic is that the anonymity of the electronic market allows things to occur that in an open outcry environment would have been self-policed by the pit, by the pit committee, by the exchange themselves. If somebody is repeatedly offering something and they're offering it above their size, the pit knows that they're not going to trade that big and they're going to ignore them and they're going to not trade with them. In an electronic market where there's surety of trade and anonymity, you don't have that, and so I think the surveillance issue at the exchange is really, really important because those are the people that can actually really dig down deep into that data and to look at that.

You know, the issue of disorderly trading, to me, disorderly trading would be when a high degree of orders -- of executed trades, are being canceled, okay, are being, you know, ignored or, you know, canceled so that people don't know what trades that they have on. Okay? To me that is -- because that's when I'm going to withdraw from the market if I'm a market maker or participant because I need to know what I have on, and if you look at May 6th why people pulled out of the market, it's because they couldn't depend upon the quotes and the markets had moved so much that they weren't sure what trades that were going to stand or not, and, you know, we had disorderly markets back in 1999 in the gold market when it first went over $1,000 and it traded for a few days and we -- this again was an open outcry environment, but you didn't know whether you were filled or not. Orders were unable, you know, there were technological reasons why all of that occurred and all of that, but when you don't have, you know, an acknowledgment of a filled order or a cancellation of a trade in an efficient manner, then that would create what I would consider a disorderly market.

MR. SHERROD: Andrei?

MR. KIRILENKO: Since a number of you mentioned the flash crash, I have a question that some of you may be interested in commenting on, and that is, should there be -- what do you think is the role of executing broker and should we sort of revisit the role of executing brokers in automated execution of large trades above and beyond the role of --

MR. SHERROD: How about we do that on the next panel?

MR. KIRILENKO: Sounds good.

MR. SHERROD: Okay. We're going to do that on the next panel because we have about 15, 20 minutes for this panel and we're going to have the panel talk about question seven, the role of executing brokers, right after this, but let's turn to the last block of questions, 15 through 19, and talk about what role the Commission should play in promulgating rules for algorithmic trading, automated trading systems, so if anyone would like to comment on our questions 15 through 19. John?

MR. HYLAND: Let me jump in as probably one of the people here who, notwithstanding John's definition, does not engage in algorithmic trading, but I think what would be helpful is if we defined algorithmic trading, because if we use John's, then we're all doing it, but if we're talking about electronic trading done with a computer program that is allowed within certain parameters of it's programming to pick and choose what it buys, when it buys, how it bids, how it lists offers, et cetera, if that's algorithmic trading, then, you know, we don't do that, but I just want to make sure that's what we're talking about as opposed to John's much broader definition of what it was.

MR. PEASE: Why don't we accept that definition for the purposes of this discussion?

MR. SHERROD: Joel.

MR. HASBROUCK: I'm glad we got that clarification because otherwise the alternative to algorithmic trading would be random trading.

But I'd like to -- I think concerns about algorithmic trading are ultimately going to come down to the point that Mark raised earlier which is speed, in that a slow algorithm, I don't think would concern anybody at this table, but a very, very fast one might and in this connection, I think it is worthwhile for the commission to consider, and I concur with Mark on this, steps to slow the market down. And the reason is, technology is generating more and more rapid speeds of trading, of course, and lower latencies, but I think it's important to realize that this is ultimately an arms race. Nobody really cares whether their order gets in with, you know, 50 milliseconds or 5 milliseconds, as long as they're first. And a race to be first is ultimately much more unstable than simply people trying to be fast because they deliver more value to their customers.

So, I think that given a particular state of technology, it makes sense to consider rules that are based on time and would slow the market down.

MR. PEASE: And which rules would you propose?

MR. HASBROUCK: I was afraid I'd be pinned down to specifics. Basically -- I will give you some examples of some things that have been tried in other markets. One is very high frequency price limits. Another is randomly delaying --

MR. SHERROD: Joel, let me slow you down. What do you mean by very high frequency price limits?

MR. HASBROUCK: Oh, instead of having say daily price limits, very strict variations about the most recent bid offer or transaction price. So, you limit the speed with which prices can move.

Other solutions that have been tried in other markets are not handling orders in serial fashion, but batching them and having high frequency call auctions once every 30 seconds, one minute, however often enough it seems to be consistent with orderly trading. But ultimately where we're headed with this race for speed, it is going to have to be destabilizing. The analogy was drawn, I think Mark drew it between computers that can play chess and computers that can react quickly. It's not one or the other, there's a tradeoff. If you require the chess- playing computer to make a move in one millisecond, it will not be a very well thought out move.

MR. PEASE: Okay, professor, I don't think you'd let your students get away with that answer. You've told us what others have done. What we're trying -- we already know -- we should know, for the most part, the universe of what some other rules are. What could we or should we consider in terms of any restrictions on how algorithms would be disrupting our markets?

MR. HASBROUCK: I think you should consider -- if I had to be pinned down to one thing -- strict price limits.

MR. SHERROD: Raj?

MR. FERNANDO: I have a question -- John, do you trade?

MR. HASBROUCK: I haven't traded since I was 23.

MR. FERNANDO: Okay. The markets have changed quite a bit since then and right now these markets are as illiquid -- as liquid, excuse me, and the bid offer spreads are as narrow as they have ever been. If a retail customer wants to go to the New York Stock Exchange, it's not an eighth wide anymore, there's no specialist getting in the middle, it's a penny wide, all they want to do, so if someone is trying to hedge their 401(k), it is as efficient for this end user as it has ever been and we do not want to do anything to disrupt that.

And going on speed -- you know, the issue of speed, right now in cars you have functionality that allows airbags to go off in milliseconds and save lives because speed has brought this and safety checks are now in place that would never have been with not for the advent of speed and technology along with this.

MR. HASBROUCK: In normal market times the technology has brought us greater liquidity and greater benefits for investors. It has also brought us the first May 6th.

MR. FERNANDO: I will argue that May 6th was not any fault of high frequency trading. In fact, if anything, there needs to be more coordination amongst the ECNs and that one order that sold, I think, 75,000 E-Mini and S&P contracts, the majority of that order was filled on the way up, not on the way down.

MR. SHERROD: I'm going to turn to Don because he's making notes.

MR. WILSON: Sure, so, this is Don Wilson. You know, I think that when we talk about

-- when we talk about speed and we talk about, you know, the concerns about, you know, the so-called arms race, I think that it's important to really think about, you know, what risks are we trying to prevent, and, you know, certainly the May 6th flash crash brought about a number of interesting questions and important things that I think that we should consider. But, you know, one of the things that's generally highlighted as a concern about this, you know, ever increasing sensitivity to latency is that perhaps somebody who's engaging in high-frequency trading will mistakenly unleash a barrage of orders that will, you know, disrupt the entire marketplace.

Now, I think we all know that that's not what caused the May 6th flash crash, but it's a legitimate concern that I think that, you know, should be discussed. Now, the way that we at DRW go about, you know, minimizing the possibility that something like that would happen is we have a whole host of pre- and post-trade checks in place. Many of those practices that we use are -- and many of the practices that many of our competitors used, are actually summarized in a recently published paper by the FIA PTG which talks about the direct market access, best practices, and specifically in the sequel paper, the risk controls that trading firms should have in place.

It's my view that firms which take, you know, which take prudent measures to put, you know, carefully thought out procedures in place can really -- in conjunction with exchanges that provide some pre-trade checking functionality, it's our belief that these risks can really be mitigated and so I think that the right solution, rather than trying to slow down the market, is actually to think about, you know, ways in which we can really encourage people to use these procedures.

Now, I mean, specifically when it comes to this rulemaking, one of the things that we could talk about -- you know, question 19 asks the question, should algorithmic traders be held accountable if they disrupt fair and equitable trading? It's a good question. And our view is that algorithmic traders that have not put in place reasonable procedures to ensure that, you know, that something like this doesn't happen absolutely should be held accountable because these are people who didn't take proper care. I think that people who are really diligent about this stuff and yet, you know, perhaps something winds up happening anyway, should be held to -- you know, that's probably a different circumstance.

MR. HIGGINS: Don, this is Mark Higgins, section 720 --

MR. SHERROD: Mark, before you get started, let me just do a timing consideration. We have about six minutes or so before we start to run over and we probably have five people that want to talk.

MR. HIGGINS: This is just a yes or no type answer that I'm hopefully going to solicit, and that is, section 720 also -- and it's the subject of another panel so I'll be really brief

-- creates the opportunity for the Commission to promulgate rules that are reasonably necessary to prohibit disruptive trading and what you speak about triggers my thought on that. Do you think that a rule requiring people to pre-test algorithms would be a wise thing? And if so, why?

MR. WILSON: Yeah, I think that's way too granular. I don't think that the algorithms themselves are what people should be concerned about. I think that it's the systems and the possibility that systems inadvertently enter a bunch of erroneous orders, regardless of what the algorithm is supposed to do or the testing of the algorithm or any of that kind of stuff.

MR. SHERROD: Gary, your last thought?

MR. DEWAAL: Well, I mean, following up on what Don said, I mean, I think the world can be divided into the purposeful big problems which are the things, I think, we were talking about before, the trade practice, the intent to cause a non bona fide price, and then we've got the accidental big problems which is, you know, either stupidity to, maybe it is recklessness. Okay? And it seems to me that the way you address them is in fact different, the way you approach them. I think that, you know, the intent to not cause -- the intent to cause a non bona fide price is properly done through prescriptions, thou shalt not, okay. I think it's wrong to have the accidents, because they have big impacts on the market, but I think the best way to do it is by holding the industry, as Don has suggested, to reasonable practices. If the industry itself has come up with recommendations and they're followed and they show an evidence of if you do these kind of things then, you know, you're working reasonably to prevent the bad kind of things accidentally, I think then that's almost like a safe harbor. You know, if something should go wrong but you've still done all these good things, to me that's a reasonable type of event.

And again, the threshold is the intent. If the intent is to do something bad, then there's no safe harbor. Okay? If it's an accident, okay, or even maybe to the point of reckless but, you know, where do you go on accepting the recommendations of best practices or whatever we call them? To me, those are defensible up to a certain level.

MR. CUSIMANO: Steve, this is Jeremy Cusimano. Something I'd like to, based on Don's point and Gary as well, if people could roll into their final comments their thoughts on whether they be best practices or safety measures or reasonable measures, however you define them, should those be, however they're determined, requirements at some level, be that at the exchange or of the CFTC or of the FCM, should those be requirements for those who are operating automated trading systems?

MR. SHERROD: And for the record, Gary shook his head no. But I'm going to turn to Cameron.

MR. SMITH: Actually, it turns out my comment's on point to what you were just asking and that is, I think again looking at the equity market might be useful. They have -- FINRA has rules about supervisory procedures that are reasonably designed to achieve a specific purpose. So, I think it would be a mistake to get very granular and proscribe which kinds of procedures you have because every trading system is different, every firm operates differently, but to the extent that you have rules in place -- procedures in place, you go, you do an exam -- this is how it worked on the ground, the examiner comes in, let me see your procedures that prevent fat fingers and runaway algorithms, whatever, looks pretty reasonable, check. Okay? Then I think every firm, it's incumbent on them to have those, and you could either have that supervisory procedure rule in the CFTC rules or you could require exchanges to have such a rule, you could do it either way, but I think that's generally the approach and again I think there's some model out there we should be looking carefully at, and creating that.

Another quick point I want to make just

on this whole speed thing that keeps coming up is that there seems to be some false notion that speed, the faster the orders come, the less well considered they are, and I just think that'd be news to all my PhDs back in Houston who are working hard to make predictive algorithms. I mean, I wish trading was so easy that all you had to do was be fast, and actually to the extent that speed was everything, that just means your tick size is terrible and the tick size is too wide, and therefore no one can compete on price and trading does become a race and I can explain that. But to the extent you have an appropriate tick size, you have to have predictive abilities and so the speed thing, this notion that somehow speed means that the trades are less well considered and there's more likely to be problems, I just don't think is true at all, that we all have some element of predictive modeling in these models or else you're not going to be profitable.

MR. NUNES: Just one thing to add to that. I think that when you look into the supervisory and control systems, that should not be something that's specific to automated firms. You know, there's no reason that within a manual firm somebody can't fat finger an order and they should have those same types of controls in place to catch that before it gets to the exchange.

MR. SHERROD: Thirty seconds, guys. Mark?

MR. FISHER: My concern with speed is just during terms of market duress and although Chopper Trading may feel that the professor -- my professor, actually -- is off base, okay, you could talk to people who have traded a hell of a lot more than you and I have, like a (inaudible) investment, will go ahead and back up what the professor just said 1000 percent. Again, speed is fine except that value players are afraid of speed, perception or not, so in times of market duress to bring value players into any market, the perception of speed is really what it is more than whether the speed really causes the problem or not. People don't want to put orders into a market if they feel that speed's going to out do them.

MR. SHERROD: John Lothian?

MR. LOTHIAN: John Lothian. I just wanted to say I didn't like what I was hearing in terms of demonizing algorithms. Algorithms are a very important part of our markets towards keeping them stable and orderly and efficient. Okay? The May 6th event was not the only time that the stock market has gone down like that. There have been lots of other events throughout history where that has occurred that had nothing to do with technology or algos or anything of that.

The very first book that I ever was recommended to read in these markets was The Extraordinary Popular Delusions and the Madness of Crowds, okay, and sometimes stuff happens because of that. There's always going to be fear and greed present in the markets and people are going to do silly things at the wide spectrum of those emotions.

MR. SHERROD: John Hyland?

MR. HYLAND: Reminding everybody that, you know, we -- my firm doesn't represent really the trading side or the algorithmic trading side, I'm just going to leave sort of like a 50,000 foot high view of this. If I was the Commission, if I was Commissioner O'Malia and I was sitting here listening all this time, I think the things that I would most take away in terms of implementing, admittedly, an incredibly flawed passage, is what Gary and Adam say. This cannot be implemented per se. Whatever you do it's got to be patterns and practices, facts and circumstances, otherwise you're going to screw everything up.

There has to be intent, otherwise you're just going to get stomped by a federal judge who's going to toss you out anyway.

I think those are the important things that you're not going to be able to come up with a firm framework, and I say this as somebody -- you know, whatever you do is going to hurt them probably more than it's going to hurt me, but that's just my observation from being here for a few hours.

MR. SHERROD: Cameron, do you want to have the last word on this one?

MR. SMITH: Oh, no thanks.

MR. SHERROD: Okay, Raj, you'll get the last word.

MR. FERNANDO: Price breakers are an important part in the market and if there was good coordination between the CFTC and the exchanges in setting up proper price limits and price breakers, a lot of these catastrophes can be avoided.

MR. PEASE: Thank you all very much for your time. This has been a very interesting, informative panel. Thank you for coming here today and thank our moderators, Steve and Andrei, for your time as well.

MR. HIGGINS: And for the folks on the phone, we will be breaking for lunch between 12:30 and 1:30, rejoining at 1:30. Thank you.

(Whereupon, at 12:33 p.m., a luncheon recess was taken.)

A F T E R N O O N S E S S I O N

(1:31 p.m.)

MR. PEASE: Well, welcome back, folks. We'll start Panel 2.

Let me start -- before I introduce our panelists, let me begin again with a few housekeeping items. The event is being transcribed by a court reporter, who will be taking a verbatim transcript.

The event is being listened to by members of the public via listen-only telephone. Because we are not webcasting this, we ask each speaker to identify themselves each time that they are speaking so that those on the telephone will know who is talking.

For the panelists, turn your name sideways if you want to speak so we can recognize you.

We're not going to have opening presentations, so we'll go right to the questions posted by the ANOPR. For this panel, we'll be dealing with questions primarily 1, 7, and 14.

Push the microphone -- push the button to talk on the microphone, and please make sure that you don't put your BlackBerry or cell phone near the microphones or it will cause potentially some interruptions.

And now I'd like to introduce our panelists. Again, my name is Robert Pease. Mark Higgins is here. Steve Seitz and Jeremy Cusimano will be moderating this session. And we have another distinguished group of panelists: Tom Gira from FINRA; Chris Heymeyer from NFA; Ike Gibbs from ConocoPhillips; Dean Payton from CME; Mark Fabian from ICE; Joe Mecane from New York Stock Exchange; Greg Mocek from McDermott Will & Emery and also representing the Commodity Markets Council; Ken Raisler from Sullivan & Cromwell, also here on behalf of FIA; Micah Green from Patton Boggs; Tyson Slocum from Public Citizen; and finally Andrew Lo from MIT.

Thank you all for volunteering to come here today at your own cost, volunteering not only your time but your expense in getting here. We very much appreciate it. You have a challenge ahead of you. The panel this morning was quite forthright in their opinions and not hesitant at all to express them, and we expect nothing less of this panel.

So, the questions we're going to be dealing with are questions from the ANOPR -- are questions 1, 7, and 14, and we'd like to focus the discussion as much as we can on those. The first one is, Should the commission provide additional guidance as to the nature of the conduct as prohibited by the specifically enumerated statutory provisions? We can start with that, and we'd like to go around the table, and we have one hour with this panel, and, Tom, we'll start with you.

MR. GIRA: Okay. Hi. My name is Tom Gira. I'm from FINRA. You know, I think -- this is a very good question, and I think there's always been kind of a tension between giving very specific -- kind of very specific rules that will address a particular conduct versus more general rules that might be more flexible and capable of addressing market activity and trading activity as it evolves. So, I think it's important to try to be as explicit as possible, but I think it's important to kind of understand that -- I think you want to have rules that can be accommodating of future changes.

MR. HEYMEYER: Well, thank you very much. On this particular piece, this particular question, I've got a couple of thoughts, and I guess I should start real quickly by saying that I'm very grateful to the Commission and to all of you for having all of us here today and this morning. You really brought together a lot of talent from the industry.

And on this particular issue I agree with Gary DeWaal that unfortunately it is bad law.

I guess I should start by saying I've been in the futures industry now for over 30 years. I started as a runner on the floor of the Board of Trade. I was a clerk. I was a broker. I was a trader in the pit. I started in SCM with my partner in 1985, and we had a big local business and a very good grain hedging business, which we sold to Penson in 2007, and we kept the proprietary trading SAT, and I have recently been running the proprietary trading company, and that's really what I spend most of my time doing.

Although my thing says the National Futures Association, I am still affiliated with Penson -- the FCM -- and I serve as the vice chairman of the board of the National Futures Association, the vice chairman of the board of the Futures Industry Association; and I say all of that because I've spent a fair amount of time through the years -- I think I was on -- I've chaired or vice chaired or served on 40-something committees at the Board of Trade back when it was a mutually owned organization, and I've spent a lot of time in trying to come up with ways that stop disruptive practices in the trading pits and on the closes and big arguments about how to settle prices and trying to weigh and balance the interest of the public, the commercial users, the market makers, the liquidity providers; and I think all of the people that were here today that you've gathered -- as I say, you've brought a very diverse and talented group here, and they all have come because these markets -- to many of us, this is -- these are -- this is our -- these are our lives, and the markets are -- the integrity of the marketplaces are very important to all of us, and it's very difficult to -- and I appreciate your challenge of trying to come up with language that can legislate -- that carries out the legislation as it's directed for you all to consider trying to make sure that there aren't disruptive practices.

And then specific of course, your question was, Should the Commission provide additional guidance as to the nature of the conduct that's prohibited by the specifically enumerated practices in A through C? And the problem, as Gary DeWaal pointed out this morning is unfortunately it's bad law. It wasn't done with forethought as to an abusive practice that everybody had admitted was a problem in the marketplace. And abusive -- there wasn't evidence of that. CFTC -- I don't think it lost cases where they felt like they needed "spoofing" authority, as we called it earlier, and so it leaves the CFTC with considering what's been directed by the law of the land.

And, again, I compliment you all on bringing a lot of people who are talented, experienced, and concerned. And they know -- they need to be brought back to consider problems where there are issues, where there are really problems. And so I guess I would call on the Commission, which a lot of people said this morning, where there is the discretion of making rules or not. For the most part, we'd probably end up with -- I would recommend that the Commission not make rules and not try to come up with language for many of these practices that aren't, particularly that I've noticed, a problem.

The exchanges have a lot of power and authority to regulate these markets, disruptive practices, and what's come to be known as "spoofing," and so I agree with a lot of what was said this morning. We have to be very careful about trying to write language that could create more problems than what we've had.

So, that's my piece from -- and I'll be happy to comment some more later. But I again thank the Commission for bringing all these people here today.

MR. GIBBS: This is Ike Gibbs, ConocoPhillips. I'll echo Chris' thank you, so I really appreciate the opportunity to join this group.

We heard a lot earlier today about the potential impacts of, you know, more specific rules on the market. I'll offer the perspective of a compliance officer who's tasked with putting in controls to ensure that the business that we operate is conducted in an appropriate manner.

You know, when I think about my role and my responsibility and how we would be impacted by, you know, more granular rules versus what I'll call more principle- based rules, it ultimately comes down to an issue of resources. You know, the more specific the rules are, if you apply something that carries some type of a strict liability measure, in many cases that's easier for us. It's easier from both a human resource perspective and sometimes from a systems resource perspective. One that is less prescriptive, that has perhaps an intent element, usually is more resource intensive. But at the end of the day, those resources are resources and we are good at figuring out how we will manage our resources.

But when I think about my job as a compliance officer, I usually try to describe it to people with a picture, and I use a bell curve as an example. On the tails you have probably -- on each tail you have -- probably 10 percent of the issues that we deal with are either black and white, and the remainder of the issues that we deal with in the middle are gray. At the end of the day, it's our ability as risk managers, because that's really what compliance officers are -- we are a type of risk manager -- it's our ability to operate within that gray zone that helps our companies navigate those issues, and we either make money, we either lose money. And sometimes we make good decisions and sometimes we make bad decisions. But at the end of the day we are comfortable and we're tasked with dealing in that gray zone. And so what I would suggest to the Commission is it's good for us to have specificity; it's good for us to have an understanding of what is considered to be appropriate and not appropriate. But we would really prefer to see a scenario where the Commission is not overly prescriptive. We're given guidance as to what's appropriate and what's not appropriate, but we would like to retain some flexibility to use our judgment, our ability to assess what's happening in the marketplace, why we are doing certain things to judge whether there is appropriate conduct or inappropriate conduct.

Thanks.

MR. PAYTON: All right, thank you. This is Dean Payton from CME Group, and I think a lot of what was talked about this morning was pretty well on target. I mean, I think that as people look at this new section of the Act, they are very much concerned about the lack of clarity in terms of what these disruptive practices mean. And, you know, there's certainly going to be concern about if people do not have the clarity that they need in order to determine whether or not to participate in these markets, if you chill that participation it's going to impact liquidity in a way that actually has a perverse effect relative to what Dodd-Frank was trying to do.

You know, that being said, I think everybody at the table this morning and everybody here today, you know, from the standpoint of whether they're a market participant, a market operator, or a regulator, I think we all have the same objectives in mind -- right? -- which is to have a market that is, you know, free from manipulation, free from fraud, free from abuse of customer orders; and I think that, you know, overall market disruption is a certain part of that. But we need to be very, very careful -- right? -- that we're not conflating volatility with being a disruptive practice, and I think that sometimes these issues get politicized in terms of how these markets are operating, and I think that, you know, we can distinguish certain types of activities being problematic, but I think it's very, very critical, as many people said this morning, that we talk about there being an element of intent -- right? -- to disrupt the market and, you know, if we want to include as part of intent an extreme recklessness standard, which is very close to an intent standard, I think that people can likely get comfortable around that. But anything short of that really creates a situation for market participants where they are concerned about whether or not they should participate in this market, because is there going to be some kind of post-hoc analysis that's done based on something that they entered in good faith in the marketplace.

MR. FABIAN: Hi. Good afternoon. It's

Mark Fabian from ICE.

I'd just like to again thank the Commission for giving us all the opportunity to weigh in on the new regulations and some of the topics that you're discussing today. And I apologize if I'm being redundant from things that were said this morning or things that were just said just now today at the table, but I think ICE would agree that, you know, we definitely want to continue to have orderly markets that promote efficiency and price discovery without disruption or any improper attempts to manipulate price or set prices that are not reflective of market value.

But having said that, as a number of people said, I think that a lot of these items that are listed in A, B, and C -- specifically, as they are listed -- require a lot more thought in terms of what would be considered volatile or not. And, as Gary pointed out this morning -- I thought was a very good point -- the discrepancies between some of the terminology used in A, B, and C -- for instance, in B there are the terms "reckless" and "intentional"; "intentional" appears in C; and neither "reckless" nor "intentional" appears in A. So, it is somewhat misleading and confusing to those who are trying to understand it.

And as many have also said, you know, the last thing we want to do is promote some type of regulation or strict rules that will discourage participants from entering these markets, providing liquidity. If we do that, you know, we're going to reduce the amount of liquidity in market, which will thereby reduce the efficiency. And then in cases where -- you know, we talked about this morning large orders impacting the market -- when you reduce the liquidity, smaller orders could provide the same type of impact on a less liquid market the large order may provide on a liquid market.

So, in general I think, like everyone has said, there needs to be caution taken in how tightly prescribed any rules or guidelines are, and I think, as Dean pointed out, we need to --

you know, if there's -- well, I think everybody has agreed intent is something that is required to -- when you look at a disruptive market or potentially disruptive trading practice, and I think a pattern is also required. That was mentioned several times this morning as well.

In that instance, when you talk about recklessness, I think we also need to make sure that we or the Commission gives us real guidance on what the difference between intent, recklessness, and then just negligence is and make sure that there is a clear distinction between those three terms and what is meant by each of those terms and that just plain activity that was not done with intent or with a reckless nature would not rise to the level necessarily of violations of these suggested regulations.

MR. LO: My name is Andrew Lo, and I want to thank the CFTC for inviting me to participate in this panel.

At the start, I want to just, in the matter of full disclosure, mention that in addition to my affiliation at MIT, I'm also affiliated with an asset management company, AlphaSimplex Group.

With regard to question 1, I suppose that my own perspective is somewhat different from some of the other members of the panel. I realize that the CFTC is charged with responsibility of responding to Dodd-Frank, but frankly I feel that the Dodd-Frank bill may be premature in many of its mandates. In fact, I find it interesting that the bill was passed in July, a full six months before the Financial Crisis Inquiry Commission has reported its findings. And there's a lot that we don't yet know about some of the issues that Dodd-Frank is trying to address. So, the first point I would make is that it's critical to develop a much deeper understanding of the kinds of practices that we want to call disruptive before we start passing rules as to how to address those issues.

The second point I want to make is that I suspect that there are two separate issues going on with regard to paragraphs A through C and with the discussions that we're having about disruptive trading practices.

The first issue has to do with relatively narrow kinds of behavior that the CFTC has already been very much aware of and engaged in dealing with, including manipulation and fraud.

But there's a second and larger issue that motivates the Dodd-Frank part of the bill that we're talking about today, which is a relatively new phenomenon in the financial landscape that we're living in, and that's systemic risks of financial markets, risks that really don't affect any one or two parts but the system as a whole. And if we think about disruptive trading practices from this broader perspective, first of all we see that it's a much different animal than any of the other issues that the CFTC or the SEC has had to deal with over the last several years. And it really is an outcome of changes in technology and the fact that technological innovations have outstripped our ability to manage them effectively with the rules that we've developed.

So, I would encourage the CFTC and all of us to think a little bit more broadly not so much about proposing one or two rules that may deal with the narrow issues -- because I believe the narrow issues, while they're important we already have many rules that deal with them -- but, rather, to think more expansively about how to deal with the larger issues, including a definition of disruptive trading practices.

You know, unlike pornography, I'm not even sure I know disruptive trading when I see it, and so there's a great deal more effort that's required for us to be able to get to the point where we can start thinking about what it really means. And the CFTC and the SEC have led the charge with a number of recent studies that I think are great examples of the kinds of forensic analysis that need to be conducted before we get to the point where we're able to pass the appropriate rules to deal with this larger issue.

Thank you.

MR. MECANE: Joe Mecane from NYSE Eronext. At the risk of reiterating some of the points that were already made, I think a lot of what we're talking about is finding a balance. I don't think there's a right or wrong answer on one side or the other of this particular debate. But I think what's changed in the context behind a lot of the issues that we're talking about is the huge rate of automation and technology that's been brought into the trading space -- you know, different levels and different products but clearly moving in a consistent direction. And the balance that I think we're trying to find is between certainty for market participants, which obviously leads to people's propensity to offer liquidity into the market. The more certainty people have about what algorithms and what practices are permitted versus not permitted, the more likely they'll be to commit capital to the market to maintain robust bids and offers.

And the counter side to that is that

it's probably unrealistic to expect that we can descriptively carve out exactly what type of behaviors are not permissible and at the same time, to the extent that we do find very prescriptive rules for what types of behaviors aren't permitted, people will find ways around them, and then you end up in the situation where you've so narrowly defined or too narrowly defined what practices are permitted that people end up working around them.

So, the right balance needs to be struck between giving enough credible guidance to participants about what practices are okay and, you know, not being so prescriptive to the point where people find loopholes or can operate in a way that circumvents the original intent of the rule.

MR. MOCEK: I echo the comments thanking you for the invitation to speak today.

Am I on? Gregory Mocek on behalf of Commodity Markets Council. Before we get into the question in particular that's on the table, question 1, from 10,000 feet I think -- and although clarity is very important, and that was clearly evident this morning from the three-hour discussion amongst the panel participants -- what we're facing is that the Commission is in a situation where it's rushing to complete multiple rules, more rules than they've ever attempted to digest in the history of the Commission in 12 months, and the rules that have finite time tables where they have to be completed by next summer generally.

I can tell you after now sitting on this side of the fence, after 10 years in government, the perspective from the commercial end users from the financial institutions, from the trading community, is that the rules are coming with such velocity it's akin to drinking out of a fire hose in the middle of winter on the sidewalk. And given that these are very important rules that are going to change the whole industry, the thought may be -- and just to try to put it the mind of the Commission, maybe the prudent thing to do is go back to Congress and say we need much more time to complete these rules rather than finishing at the end of 12 months. Just something to think about, because I know, just trying to interpret them for clients, and what could come down the pike is unbelievably hard, and in many ways it's like looking into a crystal ball.

But with regard to question 1 and the additional guidance on the nature of the conduct that we're talking about here, whether it's A, B, or C, the Commodity Markets Council clearly thinks there needs to be guidance. I mean, not to reiterate what was said this morning on vagueness, but there are a lot of issues on vagueness and these concepts that we don't need to rehash here today. And the vagueness is going to chill legitimate trading. There's no doubt about it.

But the vagueness is also going to impede the ability of the Enforcement Division to bring cases. I've dealt with that before with you guys, and it was tough having a vague statute. We constantly had to think about how we were going to be creative in dealing with vagueness in certain situations, and it was tough, and it made our jobs really hard. And I have to tell you, this section of the statute 4(c) has been challenged for vagueness in the '70s with regard to fictitious sales and the government lost, because the statute was too vague in the context of a criminal proceeding.

So, as the court will review the terms, whether it be "spoofing" -- and I'm not quite sure I know what spoofing is, and I'm not quite sure I know what the Enron loophole is either, even though Ken supposedly wrote it -- you know, there's a lot of issues that have been around that have multiple meanings.

But the court isn't going to go through the process and say okay, wait a second here, is there a common understanding or meaning to the terms that -- or in the statute, and the answer is, after this morning's conversation -- this conversation -- is no. The court's going to go through an analysis as is there a prior judicial construction, and the answer is no. The court's going to go through an analysis and say, Is there a treatise out there? Are there terms commonly used in the industry to define these terms that are in the statute? And the answer is no. And then the final answer is a ruling that says that the statute is unconstitutionally vague.

So, you know, given that analysis, I think it is evident that we need to clearly think how these things can be defined and you -- it's undoubtable that you've got to clarify these vague issues, because from your perspective as well as the industry's perspective, you can't have them laying out there, because you'll never be able to use them. If you do use them, it's going to be problematic. There's more practical issues -- and this is going to go too long, so I'll wrap up -- there's more practical issues to think about in the context of the concepts themselves and how the industry is structured, things like violating a bid and an offer.

How do you get in a situation where you

violate a bid and an offer in an over-the-counter market where it's a thinly traded market and you don't really know what the bid or the offer really is in the market or in a phone broker market, which are legitimate. They're going to be around for a long time, even though people think that they're not.

You know, those markets -- you've got prices in those markets and how are you going to make sure that, you know, you can deal with those issues? It's a practical implication that you've got to think about. How do you define the term "closing period"? It's easy to define the term "closing period" presumably in a designated contract market. Are you planning on defining that period in a SEF? Because it's an issue that's going to be applicable the way the statute is written, presumably. Maybe it won't. But it's going to be an issue. And in the area of spoofing, how do you spoof when it's not electronic? Can you spoof when it's not electronic? Maybe. But it's something to think about.

I yield the rest of my time to Dr. Raisler.

MR. RAISLER: Thank you. Ken Raisler with Sullivan & Cromwell on behalf of the FIA, and again thank you for inviting us and for putting this program together.

I would like to rephrase the question one slightly. Do we need additional guidance? The answer is absolutely yes, but on the issue not of conduct that is prohibited but actually conduct that is not prohibited.

Those of us who followed -- and Greg being one of course -- this industry for a while, I've always felt that we have on the one hand the CFTC's authority in the areas of manipulation, attempted manipulation, and bona fide trading. And on the other hand, we had the exchange's ability to provide discipline and monitor the market and ultimately, because of the membership market, declare conduct detrimental to the interest of the exchange if they were uncertain as to what the violation was but were still unhappy with it.

I'm not aware that there was a gap in that world, and this statutory provision seems to imply a gap. I think it's incumbent on the Commission in the first instance if they wanted to pursue rules, and it would be my suggestion not to do so but to explain what that problem is that's trying to be solved here -- I think that's really a missing element. And the problem of course is acute, because it's not just a vagueness issue, but the threat of an enforcement action applying these vague standards is chilling to the marketplace and could obviously discourage activity in the market.

What's happened here is the language -- I think Gary DeWaal did make the point -- and I'm sitting in his chair, so I'll echo it -- is that the terms here are not easy to follow. They're (sic) seemingly adoption to some extent of some securities law concepts -- they don't really have a very clear application.

Violating bids and offers, as Greg mentioned -- how does that work in the OTC market? There are a number of people advocating with respect to the SEF market. There'll be RFQ-type markets. Those -- you may not select the best bid or best offer. Block trades fundamentally violate a bid offer -- a best bid -- best offer environment. So, clarity is absolutely essential there.

Orderly execution of transactions during the closing period -- John Hyland talked about size of trade. It shouldn't be a criteria. There's a whole variety of things that should not be prohibited. This one I think is extremely vague and scary because of the recklessness standard that's associated with it.

Spoofing -- you know, our research indicates that there are two administrative cases at the FCC in 2004 and 2006 that describe spoofing I think, as the professor from NYU illustrated, associated with the NBBO environment. Hard to imagine how that even applies to the futures world or how it should be applied. So, I guess my recommendation here would be not to be adopting rules but to adopt clarification.

To the extent that there needs to be more done to deal with disruption, the first course of action should be to work with the exchanges -- I guess that's sort of what the next panel is about -- but to get them to address the issues that you think are necessary. I mean, Dodd-Frank did amend the core principle No. 4, which is the core principle that has enhanced language about not just the exchanges have the responsibility to monitor, but now they have the obligation to have the capacity and responsibility to prevent manipulation and distortions and disruptions in the market. And they talk about do market surveillance compliance and enforcement practices. So, I think that's really where the attention should be directed, and if the exchanges are not doing their job, then the CFTC has recourse there. I don't see the idea of using the threat of enforcement to be a helpful one for the industry or for the CFTC or from the standpoint of what Congress was trying to accomplish.

MR. GREEN: Micah Green with Patton Boggs, and I've been in this building long enough to know that the best way to establish a bona fides at any meeting like this is to say I agree with what Ken said. (Laughter)

But, seriously, I represent several companies that are in the automated trading business, as well as companies that are in the brokering business and particularly consider themselves potentially part of the swap execution facility world. So, while I associate myself with the remarks that have been talked about as it relates to prescriptive versus principle based, there needs to be enough clarity to have an ability to comply with the rules. But if clarity is so precise, you'll probably get it precisely wrong, so there needs to be flexibility. You also don't want to stifle innovation and the use of technology to make markets more efficient and more liquid and more transparent. Yet, at the same time, you don't want such vagueness that it makes it impossible to not only comply with but to enforce. So, where that balance is -- I'm sure all of us will be happy to comment on where you come up with the balance. It's very difficult for us to tell you exactly where that balance is.

But I do want to also reiterate something that Ken touched on. You can't look at each section of the statute in a silo, because there's an interrelated nature to it. This is in Title 7, the title dealing with derivatives. The derivatives market is not the equity market; it's not the futures market. It is a new marketplace that's been designed by the statute, the derivatives market, and that market is either going to be cleared or uncleared. And uncleared transactions can be executed one way, and cleared transactions have to be executed in a precise way as described by the statute. And that precise way is a competitive environment but through intermediaries -- but not a single intermediary -- through exchanges or swap execution facilities.

It does not define a marketplace that is a monopolistic, solid marketplace where execution clearing and everything is wrapped up into one place. It is a competitive environment, and the rules, whatever they are, have to be consistent with that competitive environment.

I know we're going to talk later about putting responsibilities on execution facilities, but I just think it's very important that as you look at -- from a compliance standpoint, when you look at the desired -- have flexibility enough to encourage innovation and growth of the markets, you also have to recognize that it is a different marketplace than the traditional futures and the traditional equity marketplace.

MR. SLOCUM: Hi, I'm Tyson Slocum. I direct the Energy and Climate Program at Public Citizen. For those unfamiliar with my organization, we're a national, nonprofit group. My salary and the operations of our organization are funded by the generous contributions of over 120,000 families across the United States. These members are typically not the Warren Buffetts of the world but hardworking families who, from my perspective, want access to energy prices that are set in transparent functional ways. And I think that advances in technology, not to sound like an anti-technology lyddite here, but I think that there can be no question that there have been trading practices built upon very complex algorithms and high-frequency trading practices that exceed the ability of regulators to ensure that my constituents have access to a transparent marketplace.

And I think that we need to, rather than get down in the weeds of trying to determine which technologies are legitimate, which ones are disruptive, and which ones are creating competitive advantages for different firms, I think we need to question whether or not these advances in technologies employed with high-frequency trading and these complex algorithms are far beyond the ability of our hardworking public servants at regulatory agencies to be able to protect consumers from abusive practices.

So, when I read about banks designing algorithms mainly to attack their competitors' algorithms, or where billions of dollars or hundreds of billions of equities or commodities are traded on autopilot at best, or at worst in specific ways to create harm against their competitors, I think we need to figure out where this conflicts with the public interest. And until we have regulators that are on equal footing in terms of funding capabilities, in terms of their access to technology, I don't think that we should continue to allow these across-the-board, high-frequency trading programs to continue.

Thank you.

MR. PEASE: Let's move to question No. 7, and we'll switch the order for question No. 7, Should executing brokers have an obligation to ensure the customer trades are not disruptive trade practices in the similar circumstances of the subparts of that question? And what -- let's see --

MR. HIGGINS: And in so doing, Micah -- this is Mark Higgins for the people on the phone -- one thing that you sparked in my head is that I seem to interpret from your comments that there may not be a one-size-fits-all disruptive practice and instead there are nuances, if you will, between marketplaces and the manner in which trades are executed and are cleared. And so in your comments to question 7 -- if you could try to highlight some of the distinctions between them, that would be helpful, but let's start with Tyson if you have a response to question 7.

MR. SLOCUM: Yeah, well, I think that it needs to be incumbent upon brokers and banks to justify how their trading algorithm programs, how their employment of high-frequency trading is consistent with maintaining a transparent and orderly market; and I think at this point, again, the capabilities of the very competent enforcement staff are being absolutely overwhelmed. And every time that we think that we might have gotten a handle on some of these very complex trading schemes, the traders are always going to be hundreds of steps ahead of regulators simply because of the assets dedicated by banks and brokers to ever increasingly complex trading algorithms. And the question is, is it consistent to allow these trading practices to flourish? Is it consistent with the Commodity Exchange Act's emphasis on ensuring transparent and orderly markets? And I think that we've gotten smart -- we've gotten too smart in terms of getting ahead of ourselves in allowing the technologies to dictate the pace of the markets rather than the other way around.

MR. CUSIMANO: Sorry, excuse me, Micah?

MR. GREEN: Yeah.

MR. CUSIMANO: Just -- Jeremy Cusimano. I would like to, if I could, add to this question and for purposes of this discussion, if -- we're referring to algorithmic traders or high-frequency traders that may not necessarily deal with executing brokers as an intermediary and where if they have direct access, could you also include in your discussion perhaps the role of the clearing firms in this process in their pre-trade checks or controls?

MR. GREEN: Yeah. Let me first just respond a little bit to what Tyson said. I think the goal of this statute and the goal of the CFTC and the SEC and the goal of this roundtable and the panel earlier today is to try to figure out ways that you can route out disruptive trading practices while not destroying a market structure that actually has created a very low-cost, efficient means of transacting, which ultimately, if done properly and cleanly, benefits not only the market participants involved in the transaction but the consumers who openly consume that product or commodity. So, I think everyone agrees with that goal. If there's, God forbid, a plane crash because of poor maintenance, you don't shut down the air traffic control system and stop flying; you figure out what the problem is, fix the problem, and recognize that air travel is a good thing for the economy overall. So, I think it's a similar sort of thing. So, I think we all share the same goal. The question is: How do you do it and do it as precisely as possible so you don't overshoot and have unintended consequences that ultimately will cost everybody in the marketplace whether you're a consumer or a trader all the way across the line.

But, to get to the point I think, yes, there is a slightly different dichotomy if you have direct access. If you obviously go through an intermediary and that intermediary is the only place where you can transact that business, that intermediary can see everything and to be able to judge whether or not a practice is disruptive or fraudulent because they see the breadth of the marketplace. If it's a competitive environment, in fact they can only see the marketplace that's kind of within their school box. They can see what's going in their schoolyard, but they can't necessarily see what's going in the schoolyard of a competitive execution platform or facility.

Only a regulator or a self-regulator can really do that with the protection of antitrust and whatever.

So, really, I think, you know, it really becomes then a partnership between the customer and the execution facility to the extent that the execution facility has a series of rules that are consistent with whatever the regs that come out of this building are going to be. But that doesn't mean that they can probe into what every client is doing, because that client may be transacting somewhere else as well. In fact, they may actually be transacting somewhere else outside the U.S., too. So, global coordination on this is probably also an important thing.

So, I do think it becomes more complicated because the marketplace that's been -- this -- you know, that's been designed in Dodd-Frank for the derivatives marketplace is a competitive one, not a monopolistic-styled one.

MR. RAISLER: Ken Raisler. I think we need to be extremely careful here. I think for the same reasons we just finished discussing on the last go-around about the vagueness of these provisions and Professor's Lo's comment about not even knowing when you look -- not -- you know, unlike pornography, you don't even know disruptive practice when you see it. Imposing these kinds of obligations on an executing broker, particularly after the fact when you decide that this was disruptive under whatever that standard is and say you should have known it before the trade was executed is, I think, an extremely dangerous development.

I think the same concern motivates me to advocate a principle-based approach to this kind of oversight rather than a rules-based specific requirement to take into account that there are different trading environments, that the customers are different one from the other, that the technology is continuing to evolve, and so therefore trying to put a rigid structure around it in a point in time is, in my view, constitutes a mistake.

On the principle-based approach there has been a lot of work done in this area both in the context of direct market access and through executing broker environments, and certainly there is an understanding that the executing brokers along with the exchanges and along with the algo and high-frequency trader all have responsibilities, and nobody should shirk from those responsibilities to establish an appropriately defined control environment.

The NFA has been working on that; the exchanges have been working on that; and just to promote the client here a little bit, the FIA has been working on that. And the FIA has two reports, both in 2010, one actually before the flash crash, one more detailed after, market access risk management recommendations, including recommendations in the area of direct market access.

To have as a responsibility, the executing brokers deal with things like having a kill button to stop trading; having pre-trade and post-trade risk and position limits and controls; having fat-finger quantity limits, repeated automated execution throttles, and the like, all set forth in the report. And then more recently, along with their principle trader group members, they've come up with recommendation for risk controls for trading firms. And that process of best practices continues to evolve in the industry.

Certainly with the Commission's help, the exchange's help, and the community's help I think we can get to the right place. But prescriptive rules is not the way to go.

MR. HIGGINS: Ken, just before we leave you, because it relates to the FIA materials that you talk about, part of Dodd-Frank section 747 also talks about the Commission's ability to promulgate rules that are reasonably necessary to prohibit disruptive trading practices, and so is what you're talking about that latter category of 747? And if so, would you, the FIA -- or if anybody has a thought on this -- support and be proponents of a requirement that market participants, whoever they may be, institute programs to ensure that their trading is not disruptive, not necessarily getting to that level of granularity that folks seem to want to avoid to give flexibility for their various systems but something more general but have it be a requirement such that if you don't have that, you're in violation?

MR. RAISLER: Certainly, our -- on behalf of the FIA, I mean, our bias would be toward looking at working with the exchanges as members of those environments. We have obligations that they impose and that that again is the concept of having a reasonable control environment pursuant to whatever the evolving technologies are make sense, but it's much more effective I think on a principle basis to do that through an exchange interface or a SEF interface or whatever the marketplace interface is rather than having a rule coming out of the Commission. I think the language on reasonable necessary also has the word "may" before it, and so, you know, I'm saying that if -- the Commission should step in if it's convinced that the environment, the community, the players, the traders, the brokers, and the exchanges are not doing their job. In my opinion, all of them have a very strong incentive to do their job so I wouldn't think that would be a necessary step for the CFTC to take.

MR. MOCEK: With regard to -- Greg Mocek, with regard to imposing an obligation on the broker to ensure the trades are not disruptive, I don't think you need to impose that obligation on the brokerage firm given the tools that you already have. For example, you've got aiding and abetting under section 13 that you could use to go after a broker who actually is participating in a scheme or as it was in the past, willful now. With swaps it's reckless. Under the new Dodd-Frank law, you can use that tool in your toolbox to pursue misconduct, and if it's their own employees, beyond the customer, you can obviously use 166.3 as a (inaudible) supervise employees or any other sections of the statute.

But I think what we're talking about here is really not so much imposing an obligation as they've been traditionally imposed on the statute, but the discussion is imposing an obligation of prevention. And that's a much higher standard to be imposed upon the industry where you actually have to prevent the disruptive behavior however "disruptive" is defined. And I don't think -- you know, to a large degree, that's never been mandated under the statute, and it creates practical implications because to say that a FCM, for example, has an obligation to somehow prevent disruptive trading practices in an algo, if I'm running an FCM, I probably want to take a good, hard look under the engine -- under the hood and look at the engine to determine what that algo's all about and maybe even have my PhDs look at it. Well, that's not practical, because no one wants to reveal, you know, the secret sauce.

So, I think in many ways it would be really hard to mandate, and you already have certain tools in your toolbox to use to go after the activity.

MR. MECANE: This is Joe Mecane. I think there's -- or I think about the question at multiple levels. I think the first level is around allowing customers direct access into markets where they might not be a member, and what seems prudent in that case is ensuring that there isn't the ability for someone to circumvent, exchange marketplace-type rules as a result of the fact that they are not a direct member and they're utilizing the membership of an executing broker. And so ensuring that there's a standard in place that encompasses rule adherence in that type of executing broker-customer relationship is I think one level.

The other level and where it obviously gets more complicated is around customer utilization of executing broker-supplied algorithms and where the division falls in terms of whether those algorithms could be disruptive to the market or utilized in a way that is in fact disruptive.

And I think there's a few levels to that question also, and I would lump them into two broad headings, one being algo development and the other being algo utilization. And each of those probably requires their own set of requirements and their own set of principles that have to be adhered to.

On the algo development side, clearly the executing broker in that case should have some standards applied to them in terms of -- and a lot of those requirements already apply through supervisory-type requirements, but at the same time there is probably an opportunity to give more clarity and to develop best practices and more principle-based approaches that the executing brokers could adopt in order to have certain standards that as algorithms are developed they do adhere to.

The utilization question is harder, because that gets into training issues; it gets into, you know, how do you ensure that once you give the gun to someone they don't use it inappropriately.

And those are the harder questions, and I think in a way there's a feedback loop back to the first point, because you could have standards around ensuring that the customer using those algorithms has some preventative measures or some protections, pop-up windows, things along those lines to let them know when they might have an order that shouldn't pass some risk check or could have a disruptive effect on the market. You know, there could be standards imposed in terms of training and utilization of algorithms, but clearly, you know, going to the other extreme of, you know, having a full-proof rule that encompasses all different types of prohibited-type utilization of algorithms that applies through to the customer isn't a practical solution.

MR. LO: This is Andrew Lo. So, from my perspective as a portfolio manager, I was always taught that the reason they called them brokers is all they do is they make you broker and broker.

(Laughter) So, it's not clear to me that imposing the affirmative obligation for brokers to determine whether or not a client is engaged in disruptive behavior is even feasible, because it's not clear that their expertise or their economic interests are going to be focused in a direction that will allow them to make that determination.

But I think the larger issue is one that has been repeated on a number of occasions by others on the panel, which is it's very difficult to require that brokers have this obligation if we don't define very clearly what disruptive trading practices are. In particular, it seems to me that there are two aspects of disruptive trading practices that really need to be specified. One is intent, and the second is a continuing pattern of behavior. And I realize that these two criteria raise the bar for any enforcement action, but it seems to me that to get to the heart of this issue of disruptive trading practices, you have to have both, and it's not clear to me that brokers are in a position to be able to make that determination for all the reasons that were described.

Let me just conclude with two very concrete examples, because I think that it's very difficult -- at least for me -- to talk about disruptive trading practices without coming up with some hypotheticals so that we can understand what the motivation for this potential set of rules might be.

One example is something that was highlighted by the excellent report that was put together by the joint CFTC-SEC project on the Flash Crash of May 6, 2010. That report highlights the fact that this so-called Flash Crash had many different causes, and while the media has focused on this single entity that submitted a 75,000-contract sale order for SMP E-minis the afternoon of May 6, the question is, Was that considered disruptive? It certainly was a disruptive market, and one could argue that if the single entity did this recklessly and intentionally that that was a disruptive trade.

But according to the joint CFTC-SEC report, that entity had submitted the order in order to hedge a large equity exposure. And we generally think of hedging as a good thing for the clients.

So, it's not clear, even in that case of the Flash Crash, and we know a great deal about that day thanks to this joint report, whether or not that would be considered a disruptive trade.

Second example is something that was reported today in the Wall Street Journal. The Wall Street Journal had an article that reported that a single trader apparently controls between 50 to 80 percent of the London Metal Exchange's copper stores among its warehouses. One trader controls over half the inventory of copper today.

Now, is that considered a disruptive trade? Certainly. If that trader has some problem financing that position and has to unload it, there's going to be serious repercussions for that unwind.

But, on the other hand, we don't know who the trader is; we don't know what the intention of the trader is; we don't know what the objective is. So, in both of these cases, I'm arguing that there's enough vagueness and ambiguity that it would it be virtually impossible to require their brokers to make any kind of affirmative determination of whether or not their practices are disruptive.

Thank you.

MR. FABIAN: Mark Fabian. In response to this question, I don't know that there's a need for additional obligations from beyond what currently exists for executing brokers with respect to their customers. I mean, when you look at the pre-trade controls or risk controls that are out there, they stem from exchanges having order size, position size, credit controls. If the exchange level on accounts, then you go to the clearing firms that have similar controls implemented and even third-party front ends offer different types of risk control.

So, from that perspective, there's a lot of pre- trade controls that are out there at many different levels, and I would say that in respect to our ability to take action or regulate those activities, we have -- as mentioned, exchanges have supervisory rules that require that firms, members, supervisor, employees -- very similar to 166.3 -- and we also have -- and also that it applies not only to exchange members but anybody that comes to an exchange with direct access signs an agreement with an exchange that makes them subject to the exchange rules as well.

And we also have rules that require that if any of our clearing firms become aware of actual or constructive knowledge that potential trading practices -- illegal or improper trader practice exists or may exist, they're also required to notify the exchange.

So, I think there's a number of things out there, from an exchange perspective, as well as controls at the firm levels that -- you know, as well as supervisory regulations -- that I think at this point I don't know that there's any additional obligation that's necessary on an executing broker.

MR. PEASE: Dean, could I skip you since you're since you're going to be on the next panel and we're almost out of time and I wanted to let Ike, who will not be on the next panel, speak?

MR. PAYTON: Sure.

MR. GIBBS: Sure, and I'll be brief on this, because I think it's been pretty well covered. But our position is, you know, the short answer is no, we don't think that the executing brokers should be in a position of having to be the arbiter of whether a trade is disruptive or not.

And I think Micah and Andrew have really covered what I think are the two most important points. First, in a competitive market it's unlikely -- or it's highly likely that an executing broker probably will not be able to see the whole scope of information that could even lead to that type of conclusion. And then I think, even more importantly, if you read in an element of intent, even if the broker saw the full book of business, there will always be underlying facts and circumstances that a broker, based on just simple knowledge of what's in the book, would not be able to come to a conclusion as to whether something was disruptive or not. So, we really think that, you know, at the end of the day, you know, this is more of a fact- finding scenario that has to do much deeper than just looking at the executing broker as being kind of the gatekeeper for whether something is disruptive or not.

Thanks.

MR. PEASE: I think we're about out of time on this panel, and the other panel will -- some of you will be back on the next panel. I want to thank you all very much for helping us to address at least two of these questions here today. Thank you again for your time, and we'll take about a 15-minute break and then begin with our last panel.

(Recess)

MR. HIGGINS: Okay, we'll get started in

a minute, so if folks want to grab their seats that'd be great.

Okay, we're going to get started again. This is our third and final panel. It's entitled Exchange Perspective on Disruptive Trading, and then also Potential New Disruptive Trading Practices. For the folks on the phone, there's no corresponding questions to this panel. Instead, what we're going to try to do is generate a dialogue, and we're going to start by asking a somewhat provocative question, and that is, you know, What are you observing on your markets that is disruptive? And just sort of maybe start with a non-exchange person.

Professor Lo, if you want to kick that off.

MR. LO: Sure. Andrew Lo. So, from the perspective of the academic research that's been done, over the last 10 years there's been a significant change in financial market dynamics without a doubt. Part of that has to do with advances in technology so that trading now happens at the speed of light, and the combination of algorithms, as well as the demand for the use of those algorithms by institutions and individuals, has really made markets far faster than we've ever contemplated. At the same time, the growth of the hedge fund industry has really changed the dynamics of market prices in very different ways.

It used to be the case, say in 1998, that the hedge fund industry was considered a bit of a cottage industry, but over the last decade we've seen enormous growth in assets as well as in sophistication of hedge funds in deploying a variety of different strategies.

One case in point is the comparison between what happened during August of 1998 in the wake of the LTCM debacle versus what happened in August 2007, the so-called quant meltdown that afflicted equity market neutral managers and spread far beyond those markets shortly thereafter.

In the first instance, August of 1998, we had a liquidity crisis that really focused on fixed income arbitrage trading. There was virtually no spillover effect equity markets.

In 2007, we had a liquidity crisis due to sub- prime mortgage problems, and the spillover effects occurred in every corner of the financial market.

In August of 2007, we had an equity market unwind that created repercussions in a variety of markets. But for many of us that were trading in currency markets, our August 2007 occurred in July with the unwind of the carry trade.

So, over the course of the last 10 years, the financial marketplace has gotten extraordinarily crowded. That's a good thing in one respect, because liquidity has been very high. There's been a lot of market participation. But at the same time, liquidity can be withdrawn at a moment's notice. So, in that respect, the kind of market dynamics that we see -- the May 6, 2010, the so-called Flash Crash -- the consensus among academics is that these kinds of events are not anomalies, but they are becoming more and more prevalent and they're likely to occur. And it's really the confluence of a variety of forces that have made the financial system much more precarious than ever before, which is why in the previous panel I argued that we focus not so much on individual rulemaking activities among regulatory agencies but, rather, focusing on the systemic approach to try to understand how the system has changed and what kinds of regulations need to be put into place that deal with those kinds of systemic exposures.

Thank you.

MR. HIGGINS: And, Joe, do you have any thoughts on this issue?

MR. MECANE: Sure. I don't know that I'd necessarily classify it as an issue yet, but I'll highlight I guess one developmental aspect that at least is a topical theme that we're dealing with -- and, you know, stepping back, what we've really seen evolve, especially on the equity side, just given a lot of the developments that

Andrew referenced and some other items that we're familiar with. But as technology has gotten more and more prevalent in the space, as the cost of technology has continued to increase, the speed at which transactions happen just continues to reach new levels. We've quickly gone from measuring things in seconds to milliseconds to now microseconds. Millionths of a second is the amount of time duration that we're using to measure quotes and transaction speeds.

At the same time, two parallel developments have really been around quote competition, meaning in the new world what generally determines success especially among the algorithms and the high-frequency trading strategies has been getting to the inside first and fastest. And compounding that, we've also seen an explosion on the equity side and increasingly on the option side, and just the fragmentation across all the different venues. And so what that all leads to when you put it all together is just an explosion in message traffic, which has truly been exponential over the last few years. And I think there's been a lot of dialog, a lot of public speculation about, you know, quoting and do we need to slow down the markets, et cetera, and I don't think that's really the right issue that needs to be addressed. But I do think there's two things that it raises. One is just around capacity utilization in the industry and some of the free-rider concerns that come along with, you know, the fact that there isn't a lot of cost, though. There isn't a lot of tax on utilizing quotes and bandwidth and quoting very frequently.

And then the second issue, which I think is more of an issue for Tom Gira but is one that we struggle with also, is surveilling the activity in the markets and understanding -- you know, a lot of the things that we were talking about on the last panel in terms of putting standards in place and having principles out there in terms of what types of behaviors are permissible and non-permissible is one aspect.

The second aspect from a regulatory standpoint is once you have those principles in place, how do you surveil for it? And with the amount of traffic that exists, I don't think the answer is to necessarily impact that amount of traffic but just making sure that we have adequate resources and capabilities to surveil for patterns and practices.

MR. HIGGINS: And before we go to you, Tom, I just want to ask you, Joe, do you think you have the systems in place to drink from the fire hydrants, so to speak?

MR. MECANE: I mean, I'll answer half the question, and then Tom's organization does a lot of the market surveillance work for us, so I'll defer to him. But what I would say is on the exchange side we've done, I'd say, two primary things. One is we've put -- we have a lot of procedures, requirements, rules in place that are meant to minimize the amount of disruptive behavior that can occur. So, we have a lot of rules around the open, the close in terms of the types of orders and the timing of orders, things along those lines. We have LRPs or pauses when something comes in that's disruptive. So, we have things designed to catch items that might be disruptive.

We also have a number of internal monitoring tools where we look for normal activity, things that might warrant referral to a regulator or more investigation, but, you know, not to put Tom on the spot but a lot of the day-to-day market surveillance is done on our behalf by FINRA.

MR. PEASE: Tom and when the other -- Dean and Mark, when you also go -- we've heard a lot today about how very few understand what the disruptive trading practices are that are specified in Dodd-Frank, but do you survey for these regardless of whether you understand them or not? And are there other areas that you do surveillance on or other areas, as Mark has indicated, where you want to -- where do you see it going next in terms of potentially disruptive practices that we should be on the lookout for?

MR. GIRA: This is Tom Gira speaking, and again maybe this is a little bit of background about FINRA, and admittedly this is going to have kind of a securities bent to it. So, it may not be, you know, completely applicable on a futures site. But, what we've seen is the real fragmentation of the market on the equity side, and along with that, though, over the last couple of years at least, we started to see some consolidation on the regulatory side. So, for a variety of reasons, both the NASDAQ stock market and recently the New York Stock Exchange have made decisions to outsource their surveillance obligations to FINRA. And so by doing that, we now have a window into 80 percent of the equity market. And so what that allows us to do is to frankly see a larger part of the elephant. I think in the past, every exchange was kind of looking at it independently, and I think you do see, unlike on the futures side, there's a lot more multiple trading, there's a lot more cross-market trading by participants. And because of that, you know, in the first panel there was some -- you know, I think it is a lot different when you're talking about a market where you have one order book and then just kind of one market based (inaudible). It's substantially different I think when you've got the ability for market participants to, for example, try to impact a closing spin on one market by putting orders in on another market knowing that those orders will be reacted to, and then you get a (inaudible) execution on the market that you were -- that you have your closing order in.

And so what we find is that firms are, in some cases -- and it's a spectrum. I think most firms, you know, have adequate procedures in place and are trying to do the right thing, but there are some firms that are consciously, I think, trying to spread their activity across multiple marketplaces to be under the radar screen. And so we have brought -- and if you want to call it spoofing, we did bring a case against

Trillium, which was called a layering case where you had firms putting in kind of orders on side of the market to try to, frankly, bait other algos to react and then hit an order that was placed on the other side of the market. And we are seeing that increasingly. We're seeing variations of that. We're seeing scenarios where rather than layering with smaller orders, somebody might put it in a very large block order that's away from the inside so it doesn't have an execution risk, and they might do some wash sales to make it look like that block is getting executed, again trying to get momentum in the marketplace. We've been able to prosecute those cases using, you know, traditional anti-fraud rules and anti-manipulation rules.

But one of the troubling things that we are seeing in terms of patterns is direct market access, and then so increasingly we're seeing some firms that are setting up shop outside of the U.S., and they have direct market access into the U.S. and they're very, very aggressive, and so I think the last panel where we were talking about should there be obligations on the executing brokers -- I think -- again, with the securities experience I think our -- that I would be -- you know, sometimes it's almost like executing brokers are aiding and abetting and kind of facilitating that activity. So we do think it's very important that they're kind of -- that gatekeeper there. So, I think it's a different set of issues because of the fragmented market, but we are seeing a lot of activity that's preying on, frankly, the disaggregation sometimes of the markets. And one of the things that the Commission -- the SEC has proposed that FINRA's been very supportive of is the (inaudible) the New York Stock Exchange and NASDAQ and (inaudible) markets as they have a broader consolidated order trail, and so what we've got now is pockets of audit trails that aren't really linked. And so this consolidated audit trail would impose, you know, a common standard of capturing orders, trades, and quotes across all marketplaces and having the same moniker that would attach to a firm -- would attach to that firm where it's trading on any market so that you could more readily put together the pieces of the puzzle as you're looking at the activity of a firm or the activity of a customer.

MR. HIGGINS: Chris, if we can move to you before we get to electric exchanges that are here and ask you to respond wearing your NFA hat -- if you would.

MR. HEYMEYER: Well, they -- from NFA's perspective, the hard part here is what's disruptive, right? And with regard to the members of NFA, CTA, CPOs, introducing brokers, and FCMs, it's very difficult for those companies to -- in all due respect for the brokers to know what the customers are doing, because the customers don't want the broker to know what they're doing, and it could be -- and the hard part is -- I'm not even sure if I know it when I see it. If you get a big order like the (inaudible) order, for the FCM to question that order before it goes in, they could be liable for questioning it because it's a hedge order, right? So, why are you holding up our order that's hedging for our public customers?

So, then it's really difficult for those registered entities without the power of the data that you can see and that the exchange on the futures side of the exchanges can see to get -- to see and to recognize something that looks either abusive or disruptive.

MR. HIGGINS: But, Chris, let me draw an analogy to retail banking, which folks will probably be aware. If I try to move more than $9,999 between accounts at a bank or try to withdraw it, I trigger some sort of reporting requirement to the bank and then to the government. Should the executing broker not have some sort of similar requirement where that, as Tom was getting to, somebody with offshore direct-market access or not using the executing broker have some obligation without having to try to necessarily identify what's disruptive? I mean, certain things should, on their face, be curious given past patterns and practices, and so, you know, what liability should, if any, the executing brokers have?

MR. HEYMEYER: Well, somebody comes in with more than $9,000 in cash to a broker, they have to report it to. That's one thing. But if somebody wires out $3 million, they got the money in their account, it's very difficult to understand what they're doing. Now, certainly if they're wiring money in and out into different accounts, there's -- you would raise questions. And it gets into practice, and it gets into defining what's a disruptive practice. And that gets -- there are a lot of laws in place now that raise standards for the brokers to be aware of certain activities they mentioned. There are certain things that the brokers look for that don't pass the smell test. If somebody's wiring money in and out and it goes to a certain place out of the country or something and it's got a pattern to it. And they can see certain things like that. But that -- the standards today -- it would be very difficult to impose on the brokers a standard for them to understand an abusive practice without knowing what the whole book looks like. It's very difficult to legislate that aside from the basic standards that are in place today. And it's just difficult to say, and it's easy to sit and try and impose that kind of a standard on the brokers, but it's -- and I've -- as I say, I've cleared lots of people through my 20 years, and I've seen a lot of things, and some of them I would say have been something I didn't like and we've gone after it and either asked them to go someplace else or asked them to leave and they'd go right down the street. And then I've seen them go up and down the street. But that's -- it's a difficult standard to try to prescriptively write and define. That's all I'm saying, that you've a challenge in trying to do it prescriptively.

MR. HIGGINS: And now let's move to our exchanges, Dean and Mark, and when you opine on this question, in particular I'd like to have you not only talk about what you're seeing in your market as disruptive but also how you address an issue Tom raised, which is are you talking to each other and if so how and how do you ensure that, you know, one person's not doing something on ICE to effect CME's position or a position they had on CME and vice versa. So, thanks.

MR. PAYTON: Well, I think there's a couple of places -- I'm sorry? Oh, sorry, this is Dean Payton from CME Group. So, I think there's a couple of issues, right? I think, one, when we talk about disruption, I still believe that in many people's mind when we talk about disruption we're talking about price moves in the marketplace, right? There's that type of disruption, and there's the manipulative type of disruption that we're talking about with some of the articulated disruptive practices that are in 4(c), right?

On the risk side of the equation -- right? -- it goes back to what Professor Lo was talking about in terms of systemic risk -- right -- to the broader marketplace, and I think that, you know, if you look at how speed has evolved even over the last five years -- right? --

along with that the risk management capabilities of firms and exchanges have evolved as well.

So, in terms of protecting against, you know, those kinds of systemic issues, I mean, at CME group today we have fewer error trades than we've ever had, right? That's not by accident, right? Volume is up. Participation is up, right? But the number of error trades is down. And that's because, you know, we've worked hard just as other exchanges have to really put in place technology that avoids the types of conduct that could lead to disruption.

So, now, if you're doing the things on an exchange level and the firms are doing what they should be doing on a risk management level on their side, a lot of the potential for systemic-type of disruptive conduct really goes away, at least in the context of, you know, the idea that you're going to have an algorithm go awry that's going to cause some, you know, cataclysmic event in the marketplace, right? So, if we're putting in place things like price banding and protection points for market orders and stop orders, we have maximum order quantities, we have messaging throttles, we have stop logic that, you know, pauses the market when there's a transitory liquidity gap.

All those things taken together -- right? -- impact what is happening in terms of the ability for a particular player or a combination of players to disrupt the market in that capacity. That's not to say -- right -- that there's, you know, any perfect way -- right? -- to prevent every possible error in the marketplace, but I think that if we're doing the things that we need to do on the risk management side at every level -- right? -- in that chain, then, you know, the marketplace is going to be very well protected in that regard.

And exchanges -- right? -- continue to evolve. I mean, we just put our Globex credit controls in place and made them mandatory in 2010, right? There's another element of that going into effect in 2011. People are continuing to employ technology to actually monitor the technology. So, you have algorithms monitoring algorithms -- right? -- to ensure that, you know, the inputs that are coming into these algorithmic trading models, you know, aren't flawed in a way that's going to cause issues there.

So, the risk side I think is very, very critical, so we have technology. We do go in and do things like clearinghouse risk management reviews where they're going in to each of our clearing firms -- right? -- on a regular basis, talking to them about their risk management practices, particularly in the arena of direct access and obviously broader issues around operational risk as well and credit risk.

So, I guess in short, the risk side of things needs to be monitored -- right? -- very effectively, and everybody has a role in that -- right? -- from the customer to the clearing firm to the exchange.

The other side of the equation that I think 4(c) gets at, you know, more specifically, are disruptive practices that really I think have largely a manipulative bent to them, right? And I think that from an exchange perspective, again we have worked very hard to build and anticipate the types of technology capabilities that we need in order to police the markets effectively.

So, you know, whereas today we're taking in 4- to 5 billion, you know, order and market data messages a month -- right? -- it's only because we built the infrastructure several years ago to be able to take in that kind of data and be able to work with that data very efficiently, very quickly. We can look at that data, every audit trail element on a real time basis -- right? -- at every investigator in the analyst's desk, and that's, you know, hugely powerful. But we're always, you know, looking to continue to refine those capabilities as well. I mean, we've built, you know, new functionality, you know, over the course of the last year that, you know, provides us with live alerting capabilities.

So, on a real time basis, if a position

exceeds a particular threshold or somebody's 50-day moving average, we get immediate alerts. Same on the volume side. We share that with our clearinghouse risk management folks. We've now built many capabilities to, you know, identify at a very granular level both, you know, at a minute, an hour, a day where there are volume and price spikes, actually down to a second, where there are volume and price spikes during the day.

And, you know, we have a whole slate of additional, you know, programs that we're building in 2011, so that's a constant process. I mean, I think to -- Tyson had said earlier -- you know, he suggested that the regulators are a hundred steps, you know, behind where the trading community is. But I don't think the fact that we have, you know, a great deal of speed and a significant amount of messaging if we built the right systems and have the right audit trails that we can't reconstruct that activity on a very, very granular basis. I mean, we know, you know, who the users are in our markets, what time they've made every click of the mouse, or everything the black box did down to the millisecond, and, you know, that allows you to reconstruct what you need to reconstruct in order to determine where there are issues.

Just quickly to the earlier question as to kind of what kinds of things that, you know, we're looking at in the context of our markets, you know, there are things that we identify from time to time that look like they're problematic, and typically when we see those things we either write a rule -- right? -- to address it or we put out an advisory that relates to one of our current rules. So, you know, for example, in the early part of the year we had concerns about what was going on during our pre-opening period and what, you know, the indicative opening price that -- you know, there appeared to be some potential game playing during that period. So, we created an advisory notice, put the marketplace on notice as to what specific type of conduct we had concerns with and that that we would prosecute under our rules related to conduct inconsistent with just and equitable principles of trade. And we put that out to the community so they have clarity. They're on notice. They know what the issues are that the exchange is concerned about and will prosecute.

Similarly, you know, we had an issue with trading at settlement -- all right? -- and this was really a structural issue, right? Because of the way that the trading at settlement worked -- right? -- there was a significant advantage to being first in, right? It had a FIFA-based algorithm, and so what we would see is prior to the market opening, participants would be sending in order messages, because as soon as that window opened -- right? -- they wanted to be the first in. So, what we would see is people sending in a ton of messages in order to increase the probability that they would be first in, and so as soon as that window opened you'd have a ton of messaging going in and you'd have, you know, potential latency concerns during that period where we saw the excessive messaging. So, we looked at that, but again we addressed it through rulemaking and advisory. We basically changed the structure so that it's no longer permitted to enter an order to the system -- right? -- until after that state change message has been put out by Globex. So, if you actually put an order in before the state change goes to pre-open, that's a violation of our rules. We'll see that, because we see every rejected order -- right? -- that comes to the exchange, and so the problem is essentially solved, right? We no longer see the, you know significant increase in messaging prior to the pre-open. It doesn't have an effect on the efficiency of, you know, of our data.

So, you know, there are other issues like that. We've put out a new money pass rule -- right? -- where we saw some issues related to people passing money. We added clarity by putting that rule out and making clear that that's not an appropriate use of the marketplace. You know, we certainly have things that we're continuing to look at. I think that broadly would fall into what might be considered spoofing -- right? -- and I think that, you know, from our perspective it's certainly much different in context than what's played out, you know, in, you know, the revised 4(c) provisions.

MR. HIGGINS: And just on that point, although spoofing was addressed earlier, you might want to avail yourself of the opportunity to just identify the differences, in your view, of spoofing.

MR. PAYTON: Well, you know, I think that the big thing is that again there needs to be clarity that the idea that at the time you enter an order if you don't have the intent to trade that that's necessarily a violation. If you don't clarify that, there's a host of, you know, orders that would potentially go in that aren't going to be executed -- right? -- that there's a probability that they may not be executed.

You know, Gary was given an example earlier about stop orders, but, you know, I may have an order that I put in that is only going to be executed under very specific circumstances and very specific market conditions. If those change -- right? -- and they could change in a millisecond, five milliseconds, or five minutes -- that order is going to be cancelled. There's nothing inherently problematic about that.

But where you have situations that somebody is entering an order that they don't intend to execute with the specific intent to mislead other market participants and then exploit that deception for their own benefit -- right? -- that's a situation where, again, we would look at that and say, you know, this is conduct that is, you know, potentially inconsistent with just and equitable principles of trade or is uncommercial and address that conduct accordingly. But, you know, the difference there -- right? -- I think is clearly the intent to deceive and to exploit that deception.

MR. PEASE: So, you catch that on your -- you would prosecute this on your catch-all provisions.

MR. PAYTON: Correct.

MR. PEASE: Equivalent of manipulation without needing -- you don't feel a need -- I mean, your role is to identify the specific one, for example, that are listed at 747.

MR. PAYTON: Now, that -- I think that's correct, Bob. The only caveat I would say is that, you know, there may be circumstances again, as we've done in other cases, where if we identify very specific conduct that we want to give clarity to the marketplace about, then we would typically do that through an advisory or a rulemaking.

MR. HIGGINS: And then just before we move to Mark, if you could, Dean, talk a little bit about how CME interfaces with other platforms where people can execute trades.

MR. PAYTON: Yeah, I think that this is certainly one of the challenges -- right? -- for an SRO and is certainly something that we've talked about with the Commission in the past that we do think that where we're talking about cross-market and cross-asset class issues that

that is an area that I think is important for the federal agencies who have visibility into all of that to look at.

That being said, we don't ignore that by any stretch. I mean, we're obviously members of the Intermarket Surveillance Group, which includes all of the domestic and international securities exchanges, as well as many of the futures exchanges. We are able to -- in any matter that we have, you know, particular concerns about, we're able to share information with one another and basically conduct the types of investigations that we need to conduct.

I mean, the same is true, you know, and we've dealt with this for obviously decades with respect to cash market activity, right? If we see something in our futures market -- right? -- that is problematic and we think it's related or potentially related to cash market activity, we have the ability to go in from those participants and get that related activity.

So, I think from an SRO perspective,

it's certainly not a perfect model. I mean, we have great, great visibility into what's going on, on our markets. We certainly have cooperation from, you know, other markets that, you know, may be impacted or related to the markets that we trade, but there's a different level of visibility than you have as a direct SRO.

MR. HIGGINS: Thank you. And now, Mark, you're going to do cleanup for us here.

MR. FABIAN: Cleanup committee. I guess I would start off by saying, you know, part of the purpose that we're here today is there's an ever-changing environment out there obviously, and it seems to be accelerating from where it was 20 years ago. But in a regulatory world, and I know Dean would probably agree with this, you know, once you've identified an activity on an exchange that seems to be problematic or is in violation of the rules and you prosecute a few cases and you're successful in that, then somebody comes up with a new method or a new practice that becomes problematic. And once you've identified that practice and taken some actions on it, then the focus may change. So, it's an ever- revolving process and, you know --

MR. HIGGINS: Let me just interrupt you, because that sounds like so long as you're first you get a free bite of the apple, and how do you mitigate against that?

MR. FABIAN: No, I'm not saying that.

MR. HIGGINS: Okay.

MR. FABIAN: I mean, you know, you identify the activity, and once, you know, these cases have actions taken against them, it stops with -- it's -- what I'm trying to get at is it's a constantly changing environment. People are constantly looking for new ways, you know, to come up with different types of practices, and, you know, until it becomes evident that it's a problematic practice, you know, it will continue to evolve like that I think, and that's not necessarily true for the trading population as a whole, but, you know, there's the one office out there that, you know, engages in those types of practices. So, what I'm trying to get at is the exchange has to be constantly flexible. You have to have rules that you can adapt in various circumstances. Your systems have to be flexible. You have to constantly review your systems to make sure that you have the capacity to look for different types of new trading that may surface or you may hear about or learn about.

In terms of trying to mitigate effects on markets from trading in those markets -- you know, we've talked about price banding. Well, the exchanges -- electronic exchanges have price banding. We have certain types of orders, stops with protections, stops with limits, market orders that are limited by, you know, reasonability or some other degree of price banding that helps to mitigate the impact of orders on a market, buy-in ratio policy.

We've talked about measuring the number of messages that come in for a trade -- things of that nature being spoke about their systems. We have a number of systems -- T+1 systems -- that we have developed over the past couple of years. Obviously, you know, we've only been trading -- at least speaking on behalf of ICE Futures U.S., which was a completely open outcry system prior to 2007, we've developed systems over the past couple of years that have improved our capacities tremendously.

We recently implemented a tool that allows us to look at the markets real time, replay the markets real time, see the order book, and, you know, get down to a very granular level of detail in terms of the timing and even graphing of the markets real time.

So, you know, like I said, it's constantly changing. You're constantly trying to adapt, and as Dean mentioned, you know, we have many rules out there that already exist that we use. We have a misconduct rule that's like a catch-all. We have rules that prohibit manipulation or attempted manipulation. We have rules that prohibit fictitious bids and offers both on the floor and electronically. So, you know, there's a lot of tools at our disposal that we can use to identify or at least prosecute trading patterns that may come up from time to time.

You mentioned certain new practices. TAS is -- Trading at Settlement is a tool that we began using -- and NYMEX I think had it prior to us. Interestingly enough through communication with NYMEX, when they learned that we were going to start TAS trading, colleagues at NYMEX said, you know, be careful, we've seen this in our markets, you might want to preempt it by putting out a notice. They gave us some, you know, advice heads up on it. We put out a notice specific to TAS, what we believed would constitute improper trading with respect to trading at settlement.

So, similar to the CME when we identify a trading pattern or activity that we think is problematic, we put out advisories notifying people what we think is wrong with it and the potential for action and what types of rules we would take action under or if we think there's a new rule that needs to be put in place, we will do so.

You know, one thing I would like to point out. There's been some discussion throughout the day about high-frequency algo trading, and from our perspective we don't treat a high-frequency algo trader any different than the individual independent trader that's on our platform using it. We view them all the same way. One engages in an improper activity we're going to go after them just as much as any other either automated system or individual.

We also don't particularly put a lot of focus on the closes. You know, when it comes to disruptive trading practices, you want to look at the whole bag. They could happen any time during the day, and as I think was mentioned this morning, you know, sometimes particularly during the overnight periods when it's less liquid, you know, there could be issues there. But that's not to say that we don't look at the close; we obviously do look at the close or the settlement period for specific types of activity and we have. And we have pursued cases there as well.

So, if I can answer any questions, I'd be glad to.

MR. PEASE: Thank you. Professor, Lo, I'd like to ask you a question.

You've cautioned us to go slowly in identifying a procedure with any further rulemakings on disruptive trading practices, and that's good advice. But we have -- the Commission has a number of options obviously that it can go and a number of directions it can go in. Three statutory provisions that we've talked about off and on today will become effective whether the Commission engages in the rulemaking or not one year after the date of Dodd-Frank. Do you think we should provide clarity to those three provisions or leave them as the statute has them? And if so, would you suggest any specific areas that we should focus on?

MR. LO: This is Andrew Lo. Obviously the Commission has a responsibility to respond to the charges that it's been given, and so providing clarity even to the extent of what may not be covered would be just as useful as being able to provide explicit guidelines as to what is covered. So, certainly clarity I think is key in the proper functioning of any kind of market environment.

But I hope that it doesn't stop there, because I believe that this is an opportunity for the Commission to go far beyond the simple rulemaking activities that most regulatory bodies engage in. And, in particular, it seems that there's one innovation that could be extraordinarily beneficial not only for this particular instance but for many future instances, and that is the ability to conduct forensic investigations of issues that are going to be emerging from time to time, because while disruptive trading practices are difficult to define, I think we all agree that having a disruptive market is not in anybody's interest. So there is an issue here, but the issue may not be easily addressed by one or two rules, and so it seems like the Commission has an opportunity to address this on an ongoing basis.

In fact, in one sense, the Commission's very mandate of maintaining open, competitive, and financially sound markets is really the exact opposite of disruptive markets, so in that sense monitoring and addressing issues about disruptive trading practices is something the CFTC's always been charged to do.

But one way to respond explicitly to Dodd-Frank, in addition to providing clarity on the points that were raised, is to create a permanent investigatory body much like the National Transportation Safety Board that the CFTC engages in forensic analysis, emerging issues that could become disruptive trading practices and then develops proposals of perhaps new rules or new practices that addresses them.

For example, one of the issues that was raised earlier was the fact that the single entity on May 6 submitted an extraordinarily large sell order of 75,000 contracts. Well, that's not necessarily a disruptive trading practice from the perspective of that individual, but it certainly can disrupt the market. So, effectively what we're saying is that markets have capacity limits.

Well, why is that such a surprise? If we think about this room that we're in today, this room has an occupancy limit and you're not allowed to go over that; otherwise you violate the fire code. The reason is that if there's a fire, it's going to be awfully hard to get 500 people out of this tiny room. Well, if there are capacity limits for physical spaces, shouldn't there be capacity limits for markets as well? And wouldn't a simple solution be to post occupancy limits or volume limits such that if you exceed them, certain activities are prohibited or ultimately curtailed to limit that kind of danger?

That's an example of a one-off decision of a particular kind of disruptive trading practice that can only come about from an analysis of the data and a more logical deliberation as to what particular kinds of practices you want to limit.

The point is that these kind of practices will change over time, and whether it's spoofing or pinging or any number of practices that could evolve over time, it's important to have some kind of analysis on an ongoing basis. So, one way to respond to this Dodd-Frank initiative is to create that investigatory body so that on an ongoing basis the CFTC can continue to monitor these issues as they emerge.

MR. HIGGINS: Thank you. Any last thoughts before we wrap up the final panel? Okay, seeing no hands shoot into the air, we'll adjourn. Thank you all for your time, and thanks to the audience and the people who are on the telephone as well. Thank you.

(Whereupon, at 3:31 p.m., the PROCEEDINGS were adjourned.)

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CERTIFICATE OF NOTARY PUBLIC

DISTRICT OF COLUMBIA

I, Irene Gray, notary public in and for the District of Columbia, do hereby certify that the forgoing PROCEEDING was duly recorded and thereafter reduced to print under my direction; that the witnesses were sworn to tell the truth under penalty of perjury; that said transcript is a true record of the testimony given by witnesses; that I am neither counsel for, related to, nor employed by any of the parties to the action in which this proceeding was called; and, furthermore, that I am not a relative or employee of any attorney or counsel employed by the parties hereto, nor financially or otherwise interested in the outcome of this action.

Notary Public, in and for the District of Columbia

My Commission Expires: April 14, 2011