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Securities and Futures Commission,
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Hong Kong
2012

21st September

FPL submits reference paper on Risk Management Guidelines

Dear Sirs,

Thank you for the opportunity to submit this paper on Risk Management Guidelines as a follow up to the Securities and Futures Commission's ("SFC") consultation on the proposed regulation of electronic trading in Hong Kong. We attach this reference paper in the spirit of providing the SFC with relevant industry opinion for consideration in relation to this important regulatory initiative in Hong Kong for the consultation period ending 24 September 2012.

The attached paper, developed by the FIX Protocol Ltd ("FPL") Americas Risk Management Working Group with input from Asian and EMEA groups, provides guidance on risk management best practices in global electronic trading for institutional market participants. The objective of the paper is to provide information around risk management and encourage firms to incorporate best practices in support of their electronic trading platforms, across a range of asset classes. The recommended risk controls offer the global financial services community with a set of guidelines that aim to systemically minimise the inherent risks associated with executing electronic algorithmic and direct to market ("DMA") orders.

FPL is a not-for-profit industry standards organisation that sits at the heart of the global electronic trading community. It is industry-driven, independent and neutral, with a membership that comprises of over 260 firms from the global financial services industry. FPL aims to address the business challenges impacting the trading community through the use of standards.

Central to these efforts is the continuous development and promotion of the FIX Protocol, the non-proprietary, free and open de-facto messaging standard used for pre-trade, trade and post-trade communication globally. It is used in all asset classes including equities, derivatives, foreign exchange and fixed income. FIX is utilised by virtually every major stock exchange and investment bank as well as the world's largest clearing houses, clearing firms, central clearing corporations, investment managers and money managers. Of note amongst the FPL membership, is the Canadian (IIROC) and Australian (ASIC) regulatory bodies, both of whom use FIX for their market surveillance and reporting requirements.

Please see the Appendix to this letter below for an overview of the use of the FIX Protocol in the regulation of the electronic trading, the benefits to regulators and market participants, and working examples from different jurisdictions.

In summary, in addition to having a role in helping facilitate ongoing institutional feedback from trading practitioners, such as the attached risk management best practices paper, FPL believes we can also assist the SFC and the industry by being a standard point of reference for trade data semantics and message formats, which will facilitate quicker and less costly implementations, and allow regulators and market participants to more easily monitor compliance.

FPL would welcome the opportunity to further discuss this paper with the SFC and participate in further industry discussions on this topic. We hope that the broad membership of industry professionals working with FPL can assist you as you look to implement these important regulatory initiatives.

Thank you for your consideration.

Sincerely,

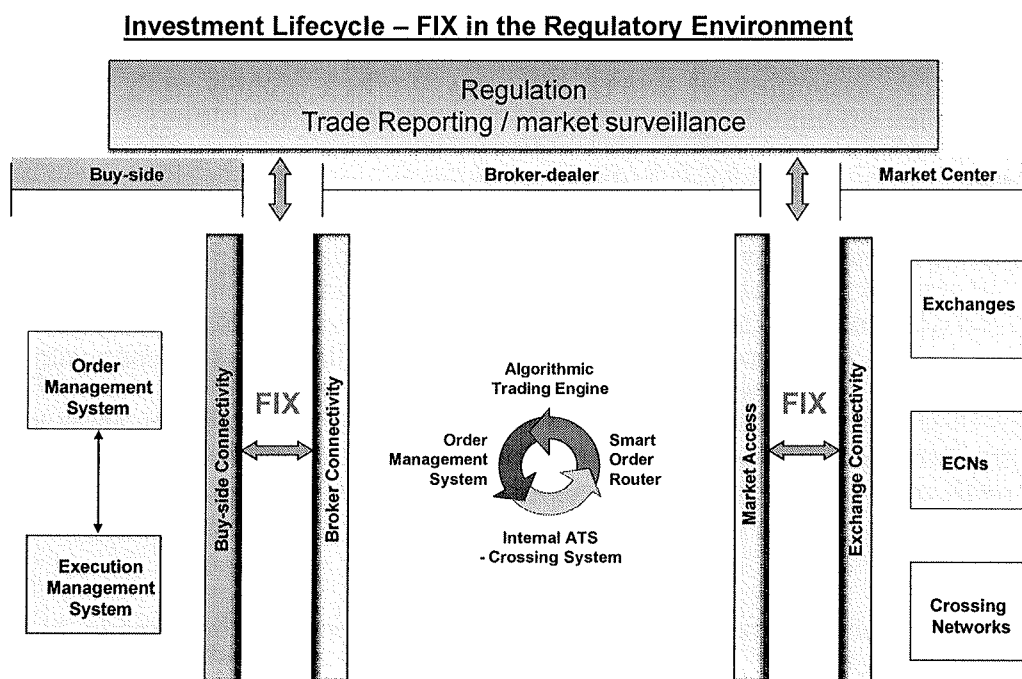
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Appendix: FIX in the Regulatory Environment

Appendix: FIX in the Regulatory Environment

HOW FIX FITS IN REGULATION:

FIX sits naturally in this regulatory role, as the figure below illustrates:



THE BENEFITS OF FIX FOR REGULATION:

The practical benefits to regulatory authorities utilizing FIX, and the market participants they regulate, include;

- *Standard point of reference:* Especially where large market participants are already using FIX; where new regulations require new reporting, a single technical solution can be worked out that can then be applied quickly across all those using the same protocol
- *Quicker implementation:* The process by which new rules are implemented can be shortened and made more efficient
- *Faster processing:* The information to the regulator can be delivered in such a way that the processing of that information is made easier
- *Data completeness:* Ensuring that the required information is flowing efficiently through the different layers is relatively more simple if the existing information flows can be used
- *Semantics consistency:* Leveraging an established semantics dictionary through the trading life cycle onto regulatory reporting obligations minimizes data loss, and misinterpretation ensures data completeness
- *Reduces regulatory burden to market participants:* The regulator can, where necessary, gain access to standardised information flows with respect to its rules, in a way that simplifies both aggregation of the information (to give a market-wide view), and to monitor compliance, while minimizing the cost of reporting obligations.

FPL ENGAGED WITH THE REGULATORS:

FPL is working with regulators to meet regulatory requirements in the following areas:

- Surveillance
- Reporting
- Risk Management

EXAMPLES OF FIX / FPL IN THE REGULATORY ARENA:

Below are some examples of where FPL has worked closely with some of the regulatory bodies on important regulatory initiatives across the globe:

Asia Pacific

- Australian Securities and Investments Commission (ASIC) - wanted to enhance surveillance across multiple markets yet minimize the impact on those it regulates.
 - ASIC wanted to ensure that the protocol it mandated for regulatory market data was in-line with global practices, cost-effective and a flexible standard.
 - ASIC looked at previous implementations, such as IIROC, and liaised with FPL on gap analysis of requirements and existing versions of FIX.
 - Standard implementation already met almost all requirements – very small extension pack identified and provides new standard for other exchanges and regulators.
 - As FIX is an open standard - this version of The FIX Protocol is readily available to all.

Americas

- Commodities Futures Trading Commission (CFTC) enhancements made to the FIX Protocol to support:
 - Listed Futures Market Surveillance
 - Trade capture reports from exchanges
 - Orders and executions from exchanges
 - Dodd-Frank Act Reporting for listed derivatives and OTC derivatives
 - Large Trader Reporting for futures from clearinghouses and brokers/FCMs (Part 16 and Part 17)
 - Large Trader Reporting for commodities swaps from clearinghouses and brokers/FCMs (Part 20)
 - Margin Position, Collateral Posted, Cash Payments and Collections, End of Day Positions for Futures, Options, IRS, CDS and commodity swaps from clearinghouses (Part 39)
 - Reporting of OTC derivatives transaction and related trade events from swap data repositories (SDR) (Part 43 and Part 45)
 - Regulatory reporting of transactions-level trade data using the TradeCaptureReport in the FIXML syntax.
- Financial Industry Regulatory Authority (FINRA) enhancements made to the FIX Protocol to support:
 - OTC Reporting Facility (ORF)
 - Trade reporting from executing parties and exchanges of OTC Equity Securities and Restricted Equity Securities
 - Trade Reporting and Compliance Engine system (TRACE)
 - Trade Reporting of Securitized Products (Asset-Backed and Mortgage-Backed Securities)

- Trade Reporting for OTC Corporate Bonds and Agency Debt (Corporates and Agencies)
- NASDAQ ACT Technology Modifications related to Short Sale Reporting Changes
- OATS Reporting

- Securities and Exchange Commission (SEC) - enhancements made to the FIX Protocol to support:
 - Identifiers required to assist broker-dealers and trading centers in complying with the following Regulation NMS rules:
 - Order Protection Rule (Rule 611)
 - Sub-Penny Rule (Rule 612, also known as Minimum Pricing Increment Rule)
 - Regulation SHO - high level mapping changes made to FIX to comply with the regulation.
 - FPL has responded to SEC concept releases relating to Securities Transaction Settlement and the Consolidated Audit Trail.

- Futures Industry Association (FIA) FPL working with to enhance FIX Protocol to support:
 - Swaps data repository reporting natively in FIX
 - Pre-trade credit check for clearing certainty - this would help meet the CFTC Rule 1.72 and 1.73 - this rule is applied for not only OTC derivative but is being considered also for listed futures.
 - Additionally the Futures Industry Association is sponsoring an initiative to extend the FIX Protocol to support pre-trade credit limit check for clearing certainty, specifically to meet Dodd-Frank Rule 1.72 and 1.73. The extension proposal will be submitted to FPL's Global Technical Committee for review and inclusion into the FIX Protocol. This initiative will eventually allow firms who use FIX for trading to also use FIX for pre-trade risk management, initially for cleared OTC derivatives.

- In collaboration with the X9 (Accredited Standards Committee, which is part of ANSI) to design a ISO-9000 style quality management system (QMS) process for HFT. This will leverage previous work done by FIA Principal Traders Group (FIA PTG) and FIA European Principal Traders Association (FIA EPTA) in their "Recommendations for Software Development and Change Management" paper released earlier this year. The aim is to make this an ANSI standard and then take it to ISO.

- Investment Industry Regulatory Organization of Canada (IIROC) - enhancements made to the FIX Protocol to support:
 - IIROC's FIX based market regulation feed specification for trade reporting and market surveillance.

- Listed derivatives markets such as CME, ICE, NYSE LIFFE, Eurex and MEFF are supporting FIXML for derivatives clearing. CME (and to some extent ICE) also uses FIXML for clearing of OTC derivatives.

EMEA

- CESR (Committee of European Securities Regulators):
 - FPL submitted a proposal for an industry led solution for the establishment of a European Consolidated Tape.

FPL responded to the following proposal - CESR Technical Advice to the European Commission in the context of the MiFID Review – Equity Markets, small number of new fields and enumerations were added to the FIX Protocol to comply with the MiFID changes.

- ESMA (European Securities and Markets Authority):
 - Buy and sell side firms are currently utilizing FIX for ESMA Rule 220/2012 for monitoring, auditing, and tracking algo data elements in equities, foreign exchange, and listed futures and options.
 - FPL responded to a consultation on technical regulatory requirements for the regulation of OTC Derivatives, CCPs and Trade Repositories, recommending that ESMA strive to utilize common semantics for reporting requirements to trade repositories that are similar to other jurisdictions to ensure higher levels of data quality and reduce implementation costs.
- FIX suggested by industry to service MiFID's Messaging Requirements.