

Q1. Do you agree that the proposed scope of the regulation of electronic trading is appropriate in terms of
(i) the types of electronic trading, which include internet trading, DMA and algorithmic trading?
(ii) the types of products primarily covered by these proposals namely securities and futures contracts that are listed or traded on an exchange?
(iii) the persons to whom the proposals apply?

Ok

Q2. Do you agree that an intermediary should be ultimately responsible for the orders sent to the market through its electronic trading system and for the compliance of the orders with applicable regulatory requirements?

If not, why not?

No, it is impossible to know the ultimate intention of any client order. Markets are volatile and subject to sharp and immediate moves. It should not be the intermediary's responsibility to determine if a client order is reasonable unless there are specific guidelines provided by the exchange or regulators. Appropriate trade bust or rebooking rules should be in place at the exchange level instead. For example, both Sun Hung Kai and Standard Chartered had over 10% gap moves recently. If a broker has to determine if each order is reasonable, the client who reacts to the news first but is restricted to placing an order is at a disadvantage. Hindsight is 20/20. In a world where micro-seconds matter this is an unreasonable burden to place on any intermediary.

Q3. Do you agree that an intermediary should effectively manage and adequately supervise the design, development, deployment and operation of the electronic trading system it uses or provides to clients for use?

If yes, are the proposed requirements sufficient? If not, why not?

Not in the way proposed. It is fine to have one person responsible for the system but it is not reasonable to require that person to have access to all levels of intellectual property within the design, development, deployment and operation of the electronic trading system.

Q4. Do you agree that an intermediary should ensure the integrity of the electronic trading system it uses or provides to clients for use, including the system's reliability, security and capacity, and have appropriate contingency measures in place?

If yes, are the proposed requirements sufficient? If not, why not?

The guidelines are too broad as written.

System controls: what is erroneous? If you want brokers to implement measures to prevent sending erroneous orders, the regulators need to provide specific guidelines and what is an erroneous order. If a bid/ask spread widens and someone lifts and offer 5% higher, is that erroneous? What if positive market rumors were circulating that later prove to be false – what if they were true?

System Reliability: It says "ALL" modifications should be adequately tested. This is too broad. If a broker is not reliable, it will lose clients. Please let the brokers self-regulate themselves here. Each firm should

individually determine what is suitable for their business model. The measures as written require added unreasonable costs and risks to brokers. Ultimately, as written, they will curtail innovation.

System Capacity: By forcing brokers to regularly stress test for capacity is a costly and onerous process. Simple math can determine one's requirements. The fact is the SEHK has severe limits on their own side on both the front and back end systems which are only partially being addressed with the upgrade to the Orion system. For example, we could all perhaps use 100 transactions per second ("TPS") per stock API instead of the draconian 1 TPS currently offered by the exchange (even 100 TPS could arguably not be enough throughput for a client who would like to make two sided quotes for all stocks in the Hang Seng and China Enterprise Indices). Of course a firm could purchase 100 TPS but that may not be economically viable. What if the client just referenced decides to submit 100's of quotes but doesn't execute enough trades to cover the costs of the additional APIs. This should not be an item in the ordinance as there is a cost to capacity and thus is a business and economic decision for each firm. Each new gateway, phone line and API is expensive and firms should only be required to add additional layers if economically viable.

Q5. Do you agree that an intermediary should keep, or cause to be kept, proper records on the design, development, deployment and operation of its electronic trading system? If not, why not?

Absolutely not in the way this is proposed. There must be reasonable insurance that intellectual property remains within a firm. Quite often the documentation is the code itself. Open documentation of design within a firm and especially outside (there is no guarantee that a regulator or third party consultant hired by a regulator will not utilize what they learn from another's code or documentation if employed elsewhere) cannot be a requirement.

Q5. Do you agree that an intermediary should keep, or cause to be kept, proper records on the design, development, deployment and operation of its electronic trading system? If not, why not?

No, the records are private and should not be exposed to external parties.

Q6. Do you agree with the proposed periods of record keeping?

If not, why not?

No, depends on what documents are required for storage.

Q7. Do you agree that, in providing internet trading or DMA services, the proposed pre-trade controls should be put in place by an intermediary? If yes, are the proposed requirements appropriate? If not, why not?

No, unless a definition of an erroneous order can be provided for ALL firms to follow or

it is stricken from this section. Again, the erroneous order handling should be at the exchange level and not the broker. It will only lead to business moving to those brokers who offer less restrictive controls. I.e. as the proposal is written there is a disincentive to put in place strict controls for fear that one may lose business to other firms.

Q8. Do you agree that, in providing internet trading or DMA services, an intermediary should conduct post-trade monitoring to reasonably identify any order instructions and transactions which may be manipulative or abusive in nature?

If not, why not?

No, unless specific guidelines are provided. This is a job for the regulator and exchange. How can a broker determine what is manipulative or abusive? Some for example think HFT methods are evil while exchanges seem happy embracing HFT volumes and methodologies. The scope as written is too broad and open to too much interpretation.

Q9. Do you agree that an intermediary should establish minimum client requirements for its DMA services and assess whether each client meets the requirements before granting DMA services to a client?

If not, why not?

Yes

Q10. Do you agree that an intermediary should not allow its client to sub-delegate the DMA services to another person unless the client is a licensed or registered person or an overseas securities or futures dealer? Do you agree with the proposed definition of "overseas securities or futures dealer"?

If not, why not?

Not sure

Q11. Do you agree that an intermediary should establish and implement effective policies and procedures to reasonably ensure that persons involved in the design and development of, or approved to use its algorithmic trading system and trading algorithms are suitably qualified?

If not, why not?

This is common sense and should not be in the ordinance. It just adds another layer of unnecessary bureaucracy that is open for interpretation.

Q12. Do you agree that an intermediary should ensure that the algorithmic trading system and trading algorithms it uses or provides to clients for use are adequately tested to ensure that they operate as designed at all times?

If not, why not?

The way the measure is written – no. No reasonable firm is going to intentionally release code that has errors as there is a huge disincentive already in place – it is called the market. The market is not kind to

those who make mistakes. There should be REASONABLE measures in place for testing but using the word "ENSURE" is simply unrealistic and impossible to guarantee.

Q13. Do you agree that an intermediary should have effective controls to ensure the integrity of its algorithmic trading system and trading algorithms and that they operate in the interest of the integrity of the market?

If yes, are the proposed requirements for risk management sufficient? If not, why not?

Once again, the ordinance uses the word "ensure". It should say "reasonably ensure". Otherwise, the risk of doing business in Hong Kong becomes extreme.

In addition, the ordinance as proposed is requiring brokers to perform regulatory functions on a post trade review. Without proper guidelines on what is manipulative and abusive behavior, this is an unreasonable demand.

Q14. Do you agree that an intermediary should keep, or cause to be kept, proper records on the design, development, deployment and operation of its algorithmic trading system and trading algorithms?

If not, why not?

Q15. Do you agree with the proposed periods of record keeping and details of the records to be kept?

If not, why not?

There must be assurances that intellectual property remain protected both within and without a firm. The requirements to produce documentation on the design and development not only add an enormous cost to firms but put all firms operating in Hong Kong at risk. The privacy and secrecy obligations are not enough. Employees of regulators and exchanges often move into the private sector.

Q16. Do you agree that where an electronic trading system is provided by third party service provider, an intermediary should perform appropriate due diligence to ensure that the intermediary meets the proposed requirements set out in paragraph 18 of and Schedule 7 to the Code of Conduct in its use of the system?

If not, why not?

Q17. What is your view on requiring an intermediary to make arrangements with a service provider for the purpose of meeting the proposed requirements on record keeping?

Q16. Do you agree that where an electronic trading system is provided by third party service provider, an intermediary should perform appropriate due diligence to ensure that the intermediary meets the proposed requirements set out in paragraph 18 of and Schedule 7 to the Code of Conduct in its use of the system?

If not, why not?

Q17. What is your view on requiring an intermediary to make arrangements with a service provider for the purpose of meeting the proposed requirements on record keeping?

Third party providers also need to ensure their intellectual property is protected. The SFC should consider independent certification for vendors.

Comment:

It is our opinion that the proposed ordinance is too broad in scope placing tremendous cost and obligations on HK intermediaries. Many of the proposed measures - particularly erroneous pricing – should be enforced at the exchange, rather than the brokerage, level.