

**TRADE PRACTICE  
RULE ENFORCEMENT REVIEW  
ICE FUTURES U.S.**



**Division of Market Oversight**

**December 2, 2016**

## **I. Rule Enforcement Review Scope**

The Division of Market Oversight (“Division”) has completed a rule enforcement review of the trade practice surveillance program of ICE Futures U.S. (“ICE Futures” or the “Exchange”).<sup>1</sup> The review focused on compliance with two core principles under Section 5(d) of the Commodity Exchange Act (“Act” or “CEA”),<sup>2</sup> as amended by the Dodd-Frank Wall Street Reform and Consumer Protection Act (“Dodd-Frank Act”),<sup>3</sup> and Part 38 of the Commission’s regulations. Specifically, the Division’s review focused on Core Principles 2 (*Compliance With Rules*)<sup>4</sup> and 12 (*Protection of Markets and Market Participants*),<sup>5</sup> and Commission regulations

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<sup>1</sup> Rule enforcement reviews prepared by the Division are intended to present an analysis of an exchange’s overall compliance capabilities during the period under review. Such reviews deal only with programs directly addressed in the review and do not assess all programs or core principles. The Division’s analyses, conclusions, and recommendations are based, in large part, upon the Division’s evaluation of a sample of investigations and other exchange documents. This evaluation process, in some instances, identifies specific deficiencies in particular exchange investigations or methods but is not designed to uncover all instances in which an exchange does not address effectively all exchange rule violations or other deficiencies.

The findings and recommendations in this rule enforcement review are limited to the Exchange and its products. This rule enforcement review, and the findings and recommendations herein, represent the view of the Division only, and do not necessarily represent the position or view of the Commission or of any other office or division of the Commission.

<sup>2</sup> 7 U.S.C. 1 et seq.

<sup>3</sup> See Dodd-Frank Wall Street Reform and Consumer Protection Act, Pub. L. 111-203, 124 Stat. 1376 (2010).

<sup>4</sup> Core Principle 2 – Compliance With Rules:

- A. IN GENERAL – The board of trade shall establish, monitor, and enforce compliance with the rules of the contract market, including-
  - i. access requirements
  - ii. the terms and conditions of any contracts to be traded on the contract market; and
  - iii. rules prohibiting abusive trade practices on the contract market.
- B. CAPACITY OF CONTRACT MARKET – The board of trade shall have the capacity to detect, investigate, and apply appropriate sanctions to any person that violates any rule of the contract market.
- C. REQUIREMENT OF RULES – The rules of the contract market shall provide the board of trade with the ability and authority to obtain any necessary information to perform any function described in this subsection, including the capacity to carry out such international information-sharing agreements as the Commission may require.

<sup>5</sup> Core Principle 12 – Protection of Markets and Market Participants:

38.150; 38.152, 38.153, 38.155, 38.156, 38.158, 38. 159; and 38.650–651.<sup>6</sup> The Division’s review of the Exchange’s trade practice surveillance program covered the period from March 1, 2014 to February 28, 2015 (“target period”).<sup>7</sup>

In conducting this review, Division staff interviewed officials and staff from the Exchange. The Exchange also provided a demonstration of the electronic systems that it uses to perform trade practice surveillance. The Division also reviewed numerous documents produced by the Exchange’s staff, including the following:

- policies and procedures for conducting trade practice surveillance;
- investigation documents and associated work product for a sample<sup>8</sup> of the trade practice reviews, complaints (“pre-case matters”) and cases related to potential trade practice violations that were closed during the target period;<sup>9</sup>
- minutes of meetings of the Board of Directors and the Regulatory Oversight Committee (“ROC”) held during the target period; and

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The board of trade shall establish and enforce rules—

- A. to protect markets and market participants from abusive practices committed by any party, including abusive practices committed by a party acting as an agent for a participant; and
- B. to promote fair and equitable trading on the contract market.

<sup>6</sup> See Appendix B for a table of Core Principles and Regulations Reviewed. Because the substantive requirements of Core Principle 12 that relate to trade practice surveillance are similar to those of Core Principle 2, the Division has evaluated compliance with Core Principle 2 and the selected regulations listed herein rather than conduct a separate review of Core Principle 12 and its associated regulations, Commission regulations 38.650-651.

<sup>7</sup> The Exchange’s trade practice surveillance program was previously reviewed in the Division’s February 2, 2010 rule enforcement review, which covered the target period from June 1, 2007 to June 1, 2008.

<sup>8</sup> To ensure a sufficient sample size, the Division reviewed at least half of each category of trade practice matters closed during the target period (*i.e.*, 234 of 407 trade practice reviews, 7 of 10 complaints, and 41 of 61 cases).

<sup>9</sup> See Section II for an overview of trade practice reviews, complaints, and cases. In Appendix A, see the analysis under § 38.153 for a description of trade practice reviews and complaints (both of which are pre-case matters), and the analysis under § 38.158 for a description of cases.

- reports from the Exchange’s tracking system for the disposition of trade practice reviews, complaints, and cases.

The Division analyzed the Exchange’s trade practice surveillance program to determine whether the program was in compliance with the core principles and Commission regulations stated above, and whether the Division has identified any deficiencies with, or recommendations for, the program. For purposes of this report, a *deficiency* is an area where the Division believes that the Exchange is not in compliance with a Commission regulation and must take corrective action, and a *recommendation* concerns an area where the Division believes that the Exchange should improve its compliance program.

As set forth below, the Division found that the Exchange generally demonstrated compliance with Core Principles 2 and 12. The Division made no recommendations regarding compliance with Commission regulations 38.150; 38.152, 38.155, 38.159 and 38.650–651. It made one recommendations pursuant to Commission regulation 38.153, one recommendation pursuant to Commission regulation 38.156, and one recommendation pursuant to Commission regulation 38.158. The Division also found one deficiency pursuant to Commission regulation 38.158.

The Division provided the Exchange an opportunity to review and comment on a draft of this report on October 20, 2016. On November 4, 2016, Division staff conducted an exit conference with officials from the Exchange to discuss the findings, deficiency, and recommendations set forth in the report.

## II. Summary of Findings, Recommendations, and Deficiencies

### A. Findings without Recommendations or Deficiencies

1. Rulebook (Core Principle 2, Commission regulations 38.150, 38.152)

- The ICE Futures Rulebook (“Rulebook”) sets forth access requirements, terms and conditions of contracts to be traded on the Exchange, and rules prohibiting abusive trading practices on the Exchange. The Division found that the Rulebook prohibits the trade practice violations enumerated in Commission regulation 38.152.

2. Staff and technology (Core Principle 2, Commission regulations 38.155, 38.156)<sup>10</sup>

- The Exchange’s regulatory program is administered by the Market Regulation Department, which comprises employees based in New York and Chicago. Chicago-based staff focuses on natural gas, physical environmental, and electricity (“Energy”) products; New York-based staff focus on precious metals, softs, and financial commodities (“Non-Energy”) products.
- The Division found that the Exchange maintains sufficient compliance department staff to conduct trade practice surveillance in compliance with Core Principles 2 and 12. At the conclusion of the target period, the Exchange employed 22 individuals in the Market Regulation Department responsible for identifying trade practice violations.
- The Division found that the Exchange’s automated trade practice surveillance tools comply with Commission regulation 38.156. The SMARTS system is a third-party automated trade practice surveillance database and analytic tool that provides alert functionality. In addition, the Exchange uses ICEcap, a proprietary database application that helps staff to detect trade practice violations on a T+1 (trade date + one day) basis.

3. Capacity to detect and investigate rule violations (Core Principle 2, Commission regulation 38.153)<sup>11</sup>

- The Exchange’s trade practice surveillance program is divided between pre-case matters (trade practice reviews and complaints) and cases. Trade practice reviews are generated as a result of the Exchange’s review of

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<sup>10</sup> See below for a recommendation related to Commission regulation 38.156.

<sup>11</sup> See below for a recommendation related to Commission regulation 38.153.

trade and messaging data. Complaints arise from internal Exchange sources or external sources (including Commission staff) by email, physical mail, phone, or in-person communication.

- Division staff determined that the Exchange adequately conducted investigations of complaints during the target period. For each complaint, investigators identified and retained information relevant to the complaint, including messaging and order data, and thoroughly analyzed whether the complaint warranted being opened as a case.
  - During the target period, the Exchange initiated four potential spoofing cases and closed two potential spoofing cases. In December 2015, the Exchange adopted a dedicated Disruptive Trading Practices Review program in which investigators, on a monthly basis, are directed to identify disruptive messaging or trade activity, including spoofing. Patterns are identified and profiled through monitoring of real-time alerts. In determining which alerts and patterns warrant further inquiry, the Exchange directs Market Regulation staff to consider following factors: (a) pre-position orders that appear to benefit from new large orders after the cancellation of those large orders, (b) ratio of orders to cancellations compared to product thresholds, (c) activity from a trader that deviates from the trader's typical behavior, (d) profit or loss in relation to trades that triggered an alert, and (e) the entry or cancellation of third party orders that appear to have been made in response to the messages or trades that triggered the alert.
4. Investigations and investigation reports (Core Principle 2, Commission regulation 38.158)<sup>12</sup>
- Cases are conducted by investigators and initiated by referral from a pre-case matter or upon receipt of sufficiently detailed external information. Investigators review relevant data, such as account statements, customer account documents, and electronic communication data. Investigators collect documents from market participants through document requests and conduct interviews with relevant persons.
5. Ability to obtain information (Core Principle 2, Commission regulation 38.159)
- The Rulebook provides Compliance staff and disciplinary committees with the ability to obtain testimony and books and records from Exchange members and market participants in investigations and hearings.

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<sup>12</sup> See below for a deficiency relating to Commission regulation 38.158.

## B. Findings with Recommendations

1. Capacity to detect and investigate rule violations (Core Principle 2, Commission regulation 38.153)
  - The Exchange stated that all of its trade practice reviews<sup>13</sup> were conducted for all trade dates in the target period.<sup>14</sup> The Division, however, was unable to confirm that all such reviews were actually conducted. The Non-Energy Trade Practice Review Log<sup>15</sup> shows gaps<sup>16</sup> during which time trade practice reviews do not appear to have been completed for Non-Energy products.<sup>17</sup> For example, Wash Trade Reviews are listed as having been conducted for four out of the 12 months of the target period. The Non-Energy Trade Practice Review Log does not indicate that other trade practice reviews, including the Trading Ahead Review, the Trading at Settlement Review, and the Block Trade Review, were conducted at all during the target period.
  - The Division also found a lack of documentation in trade practice reviews regarding the scope of trade dates reviewed. A majority of the monthly Non-Energy trade practice review files examined by the Division typically contained trade and messaging data for only a single day, rather than an entire month.
    - **Recommendation: The Division recommends that all of the Exchange's trade practice reviews be conducted for all trade dates. Further, the Exchange should maintain documentation sufficient to demonstrate that such reviews, including those that require only minimal investigation, were conducted.**
2. Automated trade surveillance system (Core Principle 2, Commission regulation 38.156)

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<sup>13</sup> See the analysis pursuant to 38.153 – Trade Practice Reviews – Trade Practice Review Procedures for a list of trade practice review programs established by the Exchange.

<sup>14</sup> The Exchange stated that reviews requiring only minimal investigation were not recorded.

<sup>15</sup> See the analysis pursuant to 38.153 – Detecting Rule Violations regarding the Exchange's system for tracking matters.

<sup>16</sup> The Division notes that the Energy Trade Practice Review Log did not contain such gaps.

<sup>17</sup> The Division notes that for all reviews other than Crossing Order Reviews, the March 2015 Compliance Manual failed to specify the frequency with which reviews should be completed (*e.g.*, weekly, monthly, or quarterly). The December 2015 Compliance Manual specifies that all trade practice reviews will be conducted on at least a monthly basis. In January 2016, the Exchange stated that all trade practice reviews are conducted on a monthly basis.

- The Division found that the Exchange did not retain and could not replicate the parameters used to generate exception report alerts for trade practice reviews. Such information is not only useful for the Division in evaluating the Exchange's trade practice surveillance program, but could also assist the Exchange in determining whether the scope of its alert parameters and report queries are properly calibrated to detect potential trade violations.<sup>18</sup>

- **Recommendation: The Exchange should retain or have the capability to replicate the parameters used to generate trade practice review exception report alerts.**

3. Investigations and investigation reports (Core Principle 2, Commission regulation 38.158)

- The Division identified 13 Non-Energy Cases closed during the target period that lacked an analysis of other potential patterns of abuse that may have occurred on additional trading days. In five of these cases, the investigation reports stated that the scope of the investigation was expanded to include additional trade dates, but there was no evidence of such expansion in the investigation files. The Exchange stated that undocumented expanded reviews may have been conducted in a number of cases, but without documentation, the Division cannot verify that the expanded reviews occurred.

- **Recommendation: The Division recommends that the scope of all trade practice investigations be expanded as appropriate to look for patterns of abuse, for example, by including a review of additional trading days, and that such expansions be documented.**

### C. Findings with a Deficiency Requiring Corrective Action

1. Investigations and investigation reports (Core Principle 2, Commission regulation 38.158)

- Market Regulation closed 61 trade practice-related cases during the target period. Counting from the time each case was initiated and ending the date the case was closed, cases were open for an average of 461 days. Thirty-three cases were closed in one year or less, including 19 cases open for more than 180 days. Twenty-eight cases were open for more than one

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<sup>18</sup> During the review, the Exchange provided lists of the number of exceptions triggered by two of the ICEcap reports (RFC Exception Analysis and TAS Exception Report), and the number of alerts triggered by SMARTS alerts, but this information would not be sufficient to allow the Exchange to adjust the scope of alert parameters and report queries.



year, including twelve cases that remained open for two years or more. Of the 28 cases that were open for more than one year, the Division identified 10 cases without sufficient mitigating circumstances to justify the length of time the case was open. In addition, the Division identified three trade practice reviews that were open for more than 365 days without sufficient mitigating circumstances.<sup>19</sup> Commission regulation 38.158(b) requires that investigations be completed in one year or less, absent mitigating circumstances.

- **Deficiency: As required by Commission regulation 38.158(b), the Exchange must complete investigations in one year or less, absent mitigating circumstances.**

Additional details regarding the facts and analysis relevant to the Division's review are contained in the Compliance Matrix in Appendix A.

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<sup>19</sup> See the analysis pursuant to 38.153 – Trade Practice Reviews – Trade Practice Review Timeliness.

## Appendix A Compliance Matrix

CFTC Regulation	Findings Regarding Exchange's Compliance	Deficiencies and Recommendations
<b>Core Principle 2 – Compliance with Rules</b>		
§ 38.150 Core Principle 2	The ICE Futures Rulebook (“Rulebook” or “Exchange Rules”) sets forth access requirements, terms and conditions of contracts to be traded on the Exchange, and rules prohibiting abusive trading practices on the Exchange.	No deficiencies or recommendations.
§ 38.152 Abusive trading practices prohibited	Chapter 4 of the Rulebook prohibits the trade practice violations enumerated in Commission regulation 38.152. <sup>20</sup>	No deficiencies or recommendations.
§ 38.155 Compliance staff and resources	<p>The Exchange’s regulatory program is administered by the Market Regulation Department, which comprises employees based in New York and Chicago. Chicago-based staff focus on natural gas, physical environmental, and electricity (“Energy”) products, whereas New York-based staff focus on precious metals, softs, and financial commodities (“Non-Energy”) products.<sup>21</sup></p> <p>The Division found that the Exchange maintains sufficient compliance department staff to conduct trade practice surveillance. Employees based in New York and Chicago are responsible for identifying trade practice violations in their respective product categories. At the conclusion of the target period, the Exchange employed 22 individuals responsible for identifying trade practice violations. Fourteen of those individuals were employed in the New York office: a Vice President of Market Regulation, a Chief Compliance Officer, an Assistant General Counsel, a Compliance Systems Manager, two Compliance Managers, and eight individuals serving as investigators or analysts. Eight individuals in the Chicago office were responsible for conducting trade practice surveillance:<sup>22</sup> a Director of Market Surveillance, a</p>	No deficiencies or recommendations.

<sup>20</sup> See Exchange Rules 4.02, 4.04, and 27.23.

<sup>21</sup> The Exchange offers the following categories of non-energy products: agriculture, credit, equity derivatives, FX, freight, interest rates, metals, and U.S. environmental products.

<sup>22</sup> Chicago staff are also responsible for conducting market surveillance.

	<p>Manager of Market Regulation, and six analysts.<sup>23</sup> The Vice President of Market Regulation reports to the Regulatory Oversight Committee and the Senior Vice President General Counsel, Corporate Secretary.</p>	
<p><b>§ 38.156</b> Automated trade surveillance system</p>	<p>The Exchange uses two automated systems to conduct trade practice surveillance. The Exchange's policy is to adjust alerts and reports as needed.</p> <ul style="list-style-type: none"> <li>• <b>SMARTS</b>: Third-party automated trade practice surveillance database / analytic tool with alert functionality. Used for real-time monitoring and reconstruction of trading activity. Provides a graphical view of trading in a specific market at a specific time. For order, trade, and clearing information, SMARTS provides compilation, retrieval, sorting, filtering, and analysis functionality. The following are examples of alerts available in SMARTS as of March 2015: Price Spike, Participant Volume Spike, Bait &amp; Switch, Energy Block Trade Report, Unusual Order Traffic, and the Interval Price Limit Hold Alert.</li> <li>• <b>ICEcap</b>: Proprietary database application that allows staff to detect trade practice violations on a T+1 (<i>i.e.</i>, trade date plus one day) basis. Allows for trade reconstruction based on order, trade, and clearing information. Provides reports that track give-ups, traders, block trades, cancellations, cleared allocation, counterparties, and clearing members. The following are examples of reports offered by ICEcap as of March 2015: Account Change Report, Allocation &amp; Claim Transaction Review, Automated Trader Management System Detail Report, Authorized Trader Exception Summary Report, Block Trade Pre-Hedging Reports, Block Trade Exception Report, Cancelled Trade Review, Cleared Allocation Review, Cleared Trade Review, Counterparty Company Trades, Counterparty Trader Trades, Cross/Washing/Prearranged Report, Customer Type Indicator Comparison, EIA Front-running Report, Electronic Audit Trail Review, Wash Trade Reports, End of Day Reports Futures or Options, High Volume Request for Crosses, Market Profile Summary, Mass Quotes Order Review, Order Review, Order &amp; Trade Review, Order Review GTC, Potential Money Pass Report, Request for Cross Exception Analysis, RFC/RFQ Review, Single User Profile Summary, TAS Exception Report, TEAR Detail, TEAR Summary, Time &amp; Sales, Trade Review, Trade Summary Report, Trader Firm Trading Ahead Review, CM Trading Ahead Summary, Trading Ahead Using Give-Ups, and UDS Lookup.</li> </ul>	

<sup>23</sup> As of January 2016, the Exchange employed 23 employees who were responsible for identifying trade practice violations. Fourteen of those individuals were employed in the New York office: a Vice President of Market Regulation, a Chief Compliance Officer, an Assistant General Counsel, a Compliance Systems Manager, two Compliance Managers, and eight individuals serving as investigators or analysts. Nine individuals in the Chicago office were responsible for conducting trade practice surveillance: a Director of Market Surveillance, a Manager of Market Regulation, and seven analysts.

	<p>The Division found that the Exchange did not retain and could not replicate the parameters used to generate exception report alerts for trade practice reviews. Such information is not only useful for the Division in evaluating the Exchange’s trade practice surveillance program, but could also assist the Exchange in determining whether the scope of its alert parameters and report queries are properly calibrated to detect potential trade violations.<sup>24</sup></p>	<p><u>Recommendation</u> The Exchange should retain or have the capability to replicate the parameters used to generate trade practice review exception report alerts.</p>
<p><b>§ 38.153</b> Capacity to detect and investigate rule violations</p>	<p><u>Detecting Rule Violations</u><sup>25</sup></p> <p>The Exchange’s trade practice surveillance program is divided between pre-case matters (trade practice reviews and Complaints) and cases. Pre-case matters are tracked in trade practice review logs.<sup>26</sup> Cases are tracked in Service Now, a database application.</p> <p>Market Regulation has the ability to issue warning letters and summary fines directly from cases, before cases are referred to the Business Conduct Committee (“BCC”).<sup>27</sup> For trade practice violations, sanctions greater than summary fines and warning letters can only be imposed after a case is referred to the BCC. Sanctions cannot be imposed directly from pre-case matters.</p> <p><u>Collecting Information and Documents</u></p> <p>Pursuant to Rule 21.04, ICE Members, employees of ICE Members, and non-member market participants are required to submit testimony and books and records upon request from compliance staff or the BCC.</p>	<p>See below under “Trade Practice Reviews – Conduct of Trade Practice Reviews” for a recommendation.</p>

<sup>24</sup> During the review, the Exchange provided lists of the number of exceptions triggered by two of the ICEcap reports (RFC Exception Analysis and TAS Exception Report), and the number of alerts triggered by SMARTS alerts, but this information would not be sufficient to allow the Exchange to adjust the scope of alert parameters and report queries.

<sup>25</sup> Division staff primarily relied on the requirements set forth in the March 2015 Compliance manual to assess the Exchange’s capacity to detect and investigate rule violations.

<sup>26</sup> During the target period, the Exchange tracked pre-case matters for energy products in a log separate from other pre-case matters. The Exchange stated that as of February 2016, all pre-case matters and cases are now tracked in Service Now.

<sup>27</sup> Market Regulation can refer cases to the BCC if Market Regulation believes it would be appropriate to issue a fine greater than a warning letter or a summary fine. The BCC makes determinations regarding whether rule violations may have occurred. Additionally, in contested matters, the BCC conducts evidentiary hearings to determine if rule violations did occur.

<p><b>§ 38.153</b> Capacity to detect and investigate rule violations (continued)</p>	<p style="text-align: center;"><b><u>Pre-Case</u></b></p> <p style="text-align: center;"><b>Trade Practice Reviews</b></p> <p><u>Trade Practice Review Procedures</u></p> <p>During the target period,<sup>28</sup> the Exchange had established six review programs (“trade practice reviews”),<sup>29</sup> listed below, that seek to identify trade practice violations on a regular basis:<sup>30</sup></p> <ul style="list-style-type: none"> <li>• <u>Cross/Wash/Prearranged Trade Review</u>: Seeks to identify instances where cross orders and prearranged trades were not exposed for the minimum period of five seconds before execution.</li> <li>• <u>Trading Ahead Review</u>: Seeks to identify instances in which a member or firm directly or indirectly trades for a personal account while in the possession of an executable customer order that is subsequently executed at a less favorable price than that of the personal trade.</li> <li>• <u>Trading at Settlement Review</u>: Examines transactions occurring during the closing period.</li> <li>• <u>Cross Trade Review</u>: Seeks to verify that orders input as Crossing Orders when opposing orders are placed by a trader with common control over accounts, or when orders are to be executed based on pre-execution communication.</li> <li>• <u>Wash Trade Review</u>: Seeks to identify trades that have been executed with the intent to avoid taking a bona fide position exposed to market risk.</li> <li>• <u>Block Trade Review</u>: To ensure that block trades are executed only in contracts where block trades are permitted, by eligible contract participants, at a fair and reasonable price, that accurate records are kept, and block trades are reported properly.</li> </ul> <p>Trade practice reviews focus on trading or messaging data exceptions identified in a given month, and the</p>	
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<sup>28</sup> The list below represents programs that were in effect as of September 2010 and March 2015. The Division notes that program procedures changed slightly from the September 2010 Compliance Manual to the March 2015 Compliance Manual. For example, reviews relating to open outcry trading were removed, trading ahead reviews were expanded include the Clearing Member level, and the number of block trades to be reviewed in the Block Trade Review increased from 5 sample trades to 10 sample trades. The following reviews were new as of the March 2015 Compliance Manual: Money Pass (seeking to identify transactions executed for the purpose of transferring money from one account to another, typically pre-arranged off-Exchange), Block Trade Pre-Hedging (focusing on pre-hedging involving block trades), and the Block Trade Submission Review (targeted review focusing on whether block trades are reported in a timely manner).

<sup>29</sup> Market Regulation also conducts ad hoc reviews of alerts and exception reports to detect trade practice violations.

<sup>30</sup> See the analysis under 38.153 – Trade Practice Reviews – Conduct of Trade Practice Reviews for a recommendation addressing gaps in review logs.

<p><b>§ 38.153</b> Capacity to detect and investigate rule violations (continued)</p>	<p>Exchange’s procedure is to conduct all such reviews once per month.<sup>31</sup> The Exchange requires analysts to review trade, time, and sales records. Where appropriate, analysts are directed to request and examine records held by market participants. In rare situations, Exchange staff may ask initial, “off the record” questions of market participants during a review; “on the record” questions are asked only during cases.<sup>32</sup> Reviews are tracked in trade practice review logs. During the target period, reviews relating to non-energy products were stored in a separate log (“Non-Energy Trade Practice Review Log”) from reviews relating to energy products (“Energy Trade Practice Review Log”).</p> <p><u>Disposition of Trade Practice Reviews</u></p> <p>Trade practice reviews are closed in one of two ways. If staff determines that a rule violation may have occurred, a case is opened. If staff determines that no potential rule violation occurred, the trade practice review is closed. All decisions to close trade practice reviews are approved by managers or senior staff. Dispositions are noted in the review logs. The Exchange does not require formal written reports to be drafted for trade practice reviews.<sup>33</sup></p> <p><u>Trade Practice Reviews Opened During Target Period</u></p> <p>The Exchange opened 411 trade practice reviews during the target period, 345 of which related to energy products (“Energy trade practice reviews”), and 66 of which related to non-energy products (“Non-Energy trade practice reviews”). Among the 345 Energy trade practice reviews, 328 reviews (95 percent) were closed during the target period, while 17 reviews (5 percent) remained open at the end of the target period. Alerts triggered in the SMARTS system were the most common type of Energy trade practice review, accounting for 134 reviews (39 percent). Other common categories of Energy trade practice review included wash trade reviews, which accounted for 67 Energy reviews (19 percent); cross and pre-arranged trade reviews, which accounted for 55 Energy reviews (16 percent); front-running reviews, accounting for 30 Energy reviews (9 percent); money pass reviews, accounting for 28 Energy reviews (8 percent); block</p>	
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<sup>31</sup> In January 2016, the Exchange stated that all trade practice reviews are conducted on a monthly basis. The Division notes that for all reviews other than Crossing Order Reviews, the March 2015 Compliance Manual failed to specify the frequency with which reviews should be completed (e.g., weekly, monthly, or quarterly). The December 2015 Compliance Manual specifies that all trade practice reviews will be conducted on at least a monthly basis.

<sup>32</sup> As noted in the analysis pursuant to 38.153 – Pre-Case – Trade Practice Reviews – Disposition of Trade Practice Review, reviews can be referred to cases where potential rule violations are identified. As noted in the analysis pursuant to 38.153 – Detecting Rule Violations, sanctions cannot be issued directly from pre-case matters (complaints and trade practice reviews).

<sup>33</sup> For Non-Energy trade practice reviews, formal reports were drafted during the target period. For Energy trade practice reviews, review details are listed in the Energy Trade Practice Review log.

<p><b>§ 38.153</b> Capacity to detect and investigate rule violations (continued)</p>	<p>pre-hedging reviews, accounting for 18 Energy reviews (5 percent); trading ahead reviews, accounting for 12 Energy reviews (3 percent); and trading at settlement reviews, accounting for one Energy review (less than 1 percent).</p> <p>The majority of the 66 Non-Energy trade practice reviews (50 reviews, 77 percent) were closed during the target period. Sixteen reviews (24 percent) remained open at the conclusion of the target period. Cross trade reviews were the most common type of review among the 66 Non-Energy trade practice reviews, accounting for 61 reviews (92 percent). Wash trade reviews accounted for four reviews (6 percent).<sup>34</sup></p> <p><u>Trade Practice Reviews Closed During Target Period</u></p> <p>The Exchange closed 407 trade practice reviews during the target period. Energy reviews accounted for 347 reviews (85 percent), while Non-Energy reviews accounted for 60 reviews (15 percent). From the 347 Energy trade practice reviews, four trade practice-related cases were initiated. From the 60 Non-Energy trade practice reviews, four trade practice-related cases were initiated.</p> <p><u>Timeliness of Trade Practice Reviews</u></p> <p>As noted above, the Exchange closed 347 Energy trade practice reviews and 60 Non-Energy trade practice reviews during the target period. For Energy reviews closed during the target period, the average duration was nine days, and one such review was open for greater than 90 days.<sup>35</sup> For Non-Energy reviews closed during the target period, the average duration was 122 days, and 34 such reviews were open for greater than 90 days, four of which remained open more than 365 days. Of the four reviews open for more than 365 days, the Division identified three reviews without sufficient mitigating circumstances to justify the length of time the reviews were open.<sup>36</sup></p>	
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<sup>34</sup> In addition, reviews of Exchange for Swaps accounted for one review (2 percent).

<sup>35</sup> Because the Energy Trade Practice Review Log lacked an open date, this section counts the date of underlying market activity as the open date for Energy reviews.

<sup>36</sup> The Division reviewed three out of the four reviews that were open for more than 365 days. See the analysis pursuant to 38.158 – Timeliness of Cases for a deficiency regarding timeliness.

<p><b>§ 38.153</b> Capacity to detect and investigate rule violations (continued)</p>	<p><u>Conduct of Trade Practice Reviews</u></p> <p>Division staff reviewed 234 of the 407 trade practice reviews (57 percent) that were closed during the target period and identified several issues. Although the Exchange stated that all of its trade practice reviews<sup>37</sup> were conducted for all trade dates in the target period,<sup>38</sup> the Division was unable to confirm that all such reviews were actually conducted. The Non-Energy Trade Practice Review Log<sup>39</sup> shows gaps<sup>40</sup> during which time trade practice reviews do not appear to have been completed for Non-Energy products.<sup>41</sup> For example, Wash Trade Reviews are listed as having been conducted for four out of the 12 months of the target period. The Non-Energy Trade Practice Review Log does not indicate that other trade practice reviews, including the Trading Ahead Review, the Trading at Settlement Review, and the Block Trade Review, were conducted at all during the target period. The Division also found a lack of documentation in trade practice reviews regarding the scope of trade dates reviewed. A majority of the monthly Non-Energy trade practice review files examined by the Division typically contained trade and messaging data for only a single day, rather than an entire month.</p> <p>During the target period, the Exchange initiated four potential spoofing cases and closed two potential spoofing cases. In December 2015, the Exchange adopted a dedicated Disruptive Trading Practices Review program in which investigators, on a monthly basis, are directed to identify disruptive messaging or trade activity, including spoofing. Patterns are identified and profiled through monitoring of real-time alerts. In determining which alerts and patterns warrant further inquiry, the Exchange directs Market Regulation staff to consider following factors: (a) pre-position orders that appear to benefit from new large orders after the cancellation of those large orders, (b) ratio of orders to cancellations compared to product thresholds, (c) activity from a trader that deviates from the trader’s typical behavior, (d) profit or loss in relation to trades that triggered an alert, and (e) the entry or cancellation of third party orders that</p>	<p><u>Recommendation</u></p> <p>The Division recommends that all of the Exchange’s trade practice reviews be conducted for all trade dates. Further, the Exchange should maintain documentation sufficient to demonstrate that such reviews, including those that require only minimal investigation, were conducted.</p>
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<sup>37</sup> See the analysis pursuant to 38.153 – Trade Practice Reviews – Trade Practice Review Procedures for a list of trade practice review programs established by the Exchange.

<sup>38</sup> The Exchange stated that reviews requiring only minimal investigation were not recorded.

<sup>39</sup> See the analysis pursuant to 38.153 – Detecting Rule Violations regarding the Exchange’s system for tracking matters.

<sup>40</sup> The Division notes that the Energy Trade Practice Review Log did not contain such gaps.

<sup>41</sup> The Division notes that for all reviews other than Crossing Order Reviews, the March 2015 Compliance Manual failed to specify the frequency with which reviews should be completed (e.g., weekly, monthly, or quarterly). The December 2015 Compliance Manual specifies that all trade practice reviews will be conducted on at least a monthly basis. In January 2016, the Exchange stated that all trade practice reviews are conducted on a monthly basis.



<p><b>§ 38.153</b> Capacity to detect and investigate rule violations (continued)</p>	<p>appear to have been made in response to the messages or trades that triggered the alert.</p>	
	<p style="text-align: center;"><b><u>Pre-case</u></b></p> <p style="text-align: center;"><b>Complaints</b></p> <p><u>Complaint Procedures</u></p> <p>Complaints are received from internal Exchange sources or from external sources (including Commission staff) by e-mail, physical mail, phone, or in-person communication. The Exchange’s procedure as of March 2015 was to log complaints in one of two ways: as <i>complaints</i> in review logs,<sup>42</sup> or as <i>cases</i> in Service Now, the case database.<sup>43</sup> After receiving complaints, analysts review Exchange information to determine if any potential rule violations have occurred.</p> <p><u>Disposition of Complaints</u></p> <p>Complaints are closed in one of two ways. Where Exchange staff determines that no potential rule violations have occurred, the complaint is closed. Otherwise, an investigation is opened.<sup>44</sup> Managers approve all decisions to close complaints. The Exchange does not require written reports to be drafted for complaints that do not become investigations.<sup>45</sup></p> <p><u>Complaints Opened During Target Period</u></p> <p>The Exchange opened 11 trade practice-related complaints during the target period: 10 were related to Energy products (“Energy Complaints”), whereas one related to non-Energy products (“Non-Energy Complaints”). All 10 of the Energy Complaints were closed during the target period. The sole Non-</p>	<p>No deficiencies or recommendations.</p>

<sup>42</sup> See the analysis pursuant to 38.153 – Detecting Rule Violations for a description of how pre-case matters are tracked.

<sup>43</sup> If a complaint is sufficiently detailed as to warrant initiating a case upon receipt, the complaint will be opened as a case, rather than a complaint. This section addresses complaints that were opened as complaints. For complaints that were opened as cases, see the analysis pursuant to 38.158 – Investigations and investigations reports, below.

<sup>44</sup> As noted below under “Complaints Closed During Target Period,” none of the complaints closed during the target period were referred to cases.

<sup>45</sup> For Non-Energy Complaints, formal reports were drafted during the target period. For Energy Complaints, complaint details are listed in the Energy Trade Practice Review Log.

<p><b>§ 38.153</b> Capacity to detect and investigate rule violations (continued)</p>	<p>Energy Complaint remained open at the conclusion of the target period.</p> <p><u>Complaints Closed During Target Period</u></p> <p>The Exchange closed 10 complaints during the target period, seven of which were reviewed by the Division. No Non-Energy Complaints were closed during the target period; all 10 complaints were Energy Complaints. Of the closed complaints, no trade practice cases were initiated, and the seven complaints reviewed were closed with no action. The most common product at issue in the complaints was the Algonquin Citygates Basis Future, which accounted for two complaints (10 percent). Other products at issue in the complaints included the ERCOT North 345 KV Real-Time Peak Daily Fixed Price Future contract, the NYISO Zone A Day-Ahead Peak Daily Fixed Price Future contract, the Henry LD1 Fixed Price Future contract, the HSC HPL Pool Physical Fixed Price Spot contract, and the ISE New England Massachusetts Hub Day-Ahead Peak Mini Fixed Price Future contract.</p> <p><u>Timeliness of Complaints</u></p> <p>Each of the 10 Energy complaints closed during the target period had an average duration of eight days. Seven complaints were closed in less than seven days, whereas two complaints were open for more than seven days but less than 30 days. One complaint remained open for 30 days or more, but less than 45 days.</p> <p><u>Conduct of Complaints</u></p> <p>Based on Division staff's review of seven of the 10 complaints closed during the target period (70 percent), the Division determined that the Exchange adequately conducted investigations of complaints during the target period. Investigators identified and retained information relevant to complaints, including messaging and order data, and thoroughly analyzed whether complaints warranted being opened as cases.</p>	
<p><b>§ 38.158</b> Investigations and investigation reports</p>	<p><u>Case Procedures</u></p> <p>The Exchange's procedure is to initiate cases either directly upon receipt of sufficiently detailed external information<sup>46</sup> or by referral from a pre-case matter.<sup>47</sup> <del>When a case is initiated, it is assigned a case</del></p>	<p>See below for a deficiency and a recommendation.</p>

<sup>46</sup> See the analysis pursuant to 38.153 – Pre-case – Complaints – Complaint Procedures for a description of how complaints can be opened directly as cases.

<p><b>§ 38.158</b> Investigations and investigation reports (continued)</p>	<p>number. Exchange staff also draft a case assignment sheet listing the Exchange investigator, the Exchange manager, and the case number. During the course of an investigation, investigators are required to collect and analyze relevant data, including account statements, customer account documents, and electronic communication data (e.g. telephone recordings, emails, and instant messages). The Exchange’s policy is for information to be collected from market participants through document requests and added to case files. Investigators are directed to conduct interviews with relevant persons, including customers, and employees of members and non-member market participants (e.g. traders), and floor brokers. Interviews are generally tape recorded.</p> <p>Logs of cases are stored in Service Now, a database application. Among other information, the database tracks the case number, the open date, the close date, a short description of the case, the case result, and the case source. Although Service Now broadly identifies the source of each potential violation (e.g. customer complaint, Compliance group, ICE Market Surveillance group), during the target period, for cases involving non-energy products (“Non-Energy Cases”), it lacked a field indicating the originating complaint or trade practice review number.<sup>48</sup></p> <p><u>Case Disposition</u></p> <p>Market Regulation investigators close cases subject to approval by supervisors and the Chief Compliance Officer or the Director of Market Surveillance.<sup>49</sup> If Market Regulation determines that no rule violation occurred or finds insufficient evidence that a rule violation occurred, an investigation is closed with no further action. If Market Regulation determines that a rule violation may have occurred and violation(s) are viewed to be minor, Market Regulation has the authority to issue a warning letter or a summary fine of up to \$10,000. Summary fines can be issued for recordkeeping violations, improper cross trading violations, data reporting violations, order entry requirements violations, and failing to provide books and records within the prescribed time period. Where violations are found and Market Regulation seeks to impose a sanction greater than a warning letter or summary fine, the investigation will be referred to the BCC.</p>	
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<sup>47</sup> See the analysis pursuant to 38.153 for a description of trade practice reviews and complaints.

<sup>48</sup> The Exchange stated that as of February 2016, after the target period, the Exchange had integrated Trade Practice Review Logs into Service Now, which provides the Exchange the ability to connect cases and pre-case matters.

<sup>49</sup> The Chief Compliance Officer is based in New York, whereas the Director of Market Surveillance is based in Chicago.

**§ 38.158**  
Investigations and  
investigation reports  
(continued)

When investigations are closed, investigators are directed to draft investigation reports that include an analysis regarding whether rule violations occurred and disciplinary action recommended, if any. The Exchange’s procedure is for such reports to be approved by supervisors and senior staff.

Cases Closed During Target Period

A total of 61 trade practice-related cases were closed during the target period, 54 of which (88 percent) had been opened prior to the target period. The majority of the cases were Non-Energy Cases (48 cases, 79 percent), whereas energy products accounted for 13 cases (21 percent) (“Energy Cases”).

Cases categorized as relating to block trades were the most common type of case for the closed cases, accounting for 13 cases (21 percent). Other categories of cases involved wash trades, which accounted for 10 cases (16 percent); cross trades for 10 cases (16 percent); money pass for nine cases (15 percent); request for quote violations for eight cases (13 percent); trading at settlement issues for six cases (10 percent); price spike for two cases (3 percent); layering for one case (2 percent); flickering for one case (2 percent), and automated trading system issues for one case (2 percent).

Of the closed cases, the most common dispositions were that the cases were referred to the BCC or closed with no action, both of which accounted for 19 cases each (31 percent each). The 19 cases in which no action was taken against any respondent involved 35 respondents. Twenty-nine respondents were referred to the BCC. Summary fines were issued in 18 cases (30 percent) involving 21 respondents, who received a combined total of \$143,000 in summary fines. Warning letters were issued in five cases (8 percent), involving 29 respondents.

Timeliness of Cases

Of the cases closed during the target period, counting from the time each case was initiated and ending the date the case was closed, cases were open for an average of 461 days. Thirty-three cases were closed in one year or less, including 19 cases open for more than 180 days. Twenty-eight cases were open for more than one year, including twelve cases that remained open for two years or more. Of the 28 cases that were open for more than one year, the Division identified 10 cases without sufficient mitigating circumstances to justify the length of time the case was open. In addition, as noted above, the Division identified three

Deficiency

As required by Commission regulation 38.158(b), the Exchange must complete investigations in one year or less, absent mitigating circumstances.

<p><b>§ 38.158</b> Investigations and investigation reports (continued)</p>	<p>trade practice reviews that were open for more than 365 days without sufficient mitigating circumstances.<sup>50</sup> Commission regulation 38.158(b) requires that investigations be completed in one year or less, absent mitigating circumstances.</p> <p>The Division identified instances in which the underlying conduct preceded the case initiation date by a significant period of time. Because the case initiation date used in the counts above does not reflect when the conduct that gave rise to the case occurred, the Division also calculated case duration using the underlying conduct date. Using this methodology (“extended case counting methodology”), the average duration of cases was 514 days. Thirty-seven cases remained open for more than 365 days, 14 of which remained open for 730 days or more. Based on the analysis above, the Division is concerned with the length of time the Exchange takes to complete cases. When a significant period of time elapses between the conduct at issue and the date the case was closed, transgressions may continue to occur without the deterrent effect of sanctions.</p> <p><u>Conduct of Investigations</u></p> <p>Division staff reviewed 41 of the 61 cases (67 percent) closed during the target period and identified an issue warranting a recommendation. The Division identified 13 Non-Energy Cases closed during the target period that lacked an analysis of potential patterns of abuse that may have occurred on additional trading days. In five of these cases, the investigation reports stated that the scope of the investigation was expanded to include additional trade dates but there was no evidence of such expansion in the investigation files. The Exchange stated that undocumented expanded reviews may have been conducted in a number of cases, but without documentation, the Division cannot verify that the expanded reviews occurred.</p> <p><u>Warning Letters</u></p> <p>As noted above, the Exchange issued warning letters to 29 respondents based on trade practice investigations closed during the target period. In its review of warning letters involving trade practice violations, the Division found no instances in which the Exchange issued warning letters to the same individual for the same violation in a 12 month period.</p>	<p><u>Recommendation</u></p> <p>The Division recommends that the scope of all trade practice investigations be expanded as appropriate to look for patterns of abuse, for example, by including a review of additional trading days, and that such expansions be documented.</p>
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<sup>50</sup> See the analysis pursuant to 38.153 – Trade Practice Reviews – Trade Practice Review Timeliness.

<b>§ 38.159</b> Ability to obtain information	The Rulebook provides compliance staff and disciplinary committees with the ability to obtain testimony and books and records from Exchange members and market participants in investigations and hearings.	No deficiencies or recommendations.
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## Appendix B

### ICE FUTURES RULE ENFORCEMENT REVIEW TABLE OF CORE PRINCIPLES AND REGULATIONS REVIEWED

#### **§ 38.150 Core Principle 2.**

(a) In general. The board of trade shall establish, monitor, and enforce compliance with the rules of the contract market, including:

(1) Access requirements;

(2) The terms and conditions of any contracts to be traded on the contract market; and

(3) Rules prohibiting abusive trade practices on the contract market.

(b) Capacity of contract market. The board of trade shall have the capacity to detect, investigate, and apply appropriate sanctions to any person that violates any rule of the contract market.

(c) Requirement of rules. The rules of the contract market shall provide the board of trade with the ability and authority to obtain any necessary information to perform any function described in this section, including the capacity to carry out such international information-sharing agreements, as the Commission may require.

#### **§ 38.152 Abusive trading practices prohibited.**

A designated contract market must prohibit abusive trading practices on its markets by members and market participants. Designated contract markets that permit intermediation must prohibit customer-related abuses including, but not limited to, trading ahead of customer orders, trading against customer orders, accommodation trading, and improper cross trading. Specific trading practices that must be prohibited by all designated contract markets include front-running, wash trading, pre-arranged trading (except for certain transactions specifically permitted under part 38 of this chapter), fraudulent trading, money passes, and any other trading practices that a designated contract market deems to be abusive. In addition, a designated contract market also must prohibit any other manipulative or disruptive trading practices prohibited by the Act or by the Commission pursuant to Commission regulation.

#### **§ 38.153 Capacity to detect and investigate rule violations.**

A designated contract market must have arrangements and resources for effective enforcement of its rules. Such arrangements must include the authority to collect information and documents on both a routine and non-routine basis, including the authority to examine books and records kept by the designated contract market's members and by persons under investigation. A designated contract market's arrangements and resources must also facilitate the direct supervision of the market and the analysis of data collected to determine whether a rule violation occurred.

**§ 38.155 Compliance staff and resources.**

(a) Sufficient compliance staff. A designated contract market must establish and maintain sufficient compliance department resources and staff to ensure that it can conduct effective audit trail reviews, trade practice surveillance, market surveillance, and real-time market monitoring. The designated contract market's compliance staff also must be sufficient to address unusual market or trading events as they arise, and to conduct and complete investigations in a timely manner, as set forth in § 38.158(b) of this part.

(b) Ongoing monitoring of compliance staff resources. A designated contract market must monitor the size and workload of its compliance staff annually, and ensure that its compliance resources and staff are at appropriate levels. In determining the appropriate level of compliance resources and staff, the designated contract market should consider trading volume increases, the number of new products or contracts to be listed for trading, any new responsibilities to be assigned to compliance staff, the results of any internal review demonstrating that work is not completed in an effective or timely manner, and any other factors suggesting the need for increased resources and staff.

**§ 38.156 Automated trade surveillance system.**

A designated contract market must maintain an automated trade surveillance system capable of detecting and investigating potential trade practice violations. The automated system must load and process daily orders and trades no later than 24 hours after the completion of the trading day. In addition, the automated trade surveillance system must have the capability to detect and flag specific trade execution patterns and trade anomalies; compute, retain, and compare trading statistics; compute trade gains, losses, and futures-equivalent positions; reconstruct the sequence of market activity; perform market analyses; and support system users to perform in-depth analyses and ad hoc queries of trade-related data.

**§ 38.158 Investigations and investigation reports.**

(a) Procedures. A designated contract market must establish and maintain procedures that require its compliance staff to conduct investigations of possible rule violations. An investigation must be commenced upon the receipt of a request from Commission staff or upon the discovery or receipt of information by the designated contract market that indicates a reasonable basis for finding that a violation may have occurred or will occur.

(b) Timeliness. Each compliance staff investigation must be completed in a timely manner. Absent mitigating factors, a timely manner is no later than 12 months after the date that an investigation is opened. Mitigating factors that may reasonably justify an investigation taking longer than 12 months to complete include the complexity of the investigation, the number of firms or individuals involved as potential wrongdoers, the number of potential violations to be investigated, and the volume of documents and data to be examined and analyzed by compliance staff.

(c) Investigation reports when a reasonable basis exists for finding a violation. Compliance staff must submit a written investigation report for disciplinary action in every instance in which compliance staff determines from surveillance or from an investigation that a reasonable basis exists for finding a rule violation. The investigation report must include the reason the



investigation was initiated; a summary of the complaint, if any; the relevant facts; compliance staff's analysis and conclusions; and a recommendation as to whether disciplinary action should be pursued.

(d) Investigation reports when no reasonable basis exists for finding a violation. If after conducting an investigation, compliance staff determines that no reasonable basis exists for finding a violation, it must prepare a written report including the reason(s) the investigation was initiated; a summary of the complaint, if any; the relevant facts; and compliance staff's analysis and conclusions.

(e) Warning letters. No more than one warning letter may be issued to the same person or entity found to have committed the same rule violation within a rolling twelve month period.

#### **§ 38.159 Ability to obtain information.**

A designated contract market must have the ability and authority to obtain any necessary information to perform any function required under this subpart C of the Commission's regulations, including the capacity to carry out international information sharing agreements as the Commission may require. Appropriate information sharing agreements can be established with other designated contract markets and swap execution facilities, or the Commission can act in conjunction with the designated contract market to carry out such information sharing.

#### **§ 38.650 Core Principle 12.**

The board of trade shall establish and enforce rules:

- (a) To protect markets and market participants from abusive practices committed by any party, including abusive practices committed by a party acting as an agent for a participant; and
- (b) To promote fair and equitable trading on the contract market.

#### **§ 38.651 Protection of markets and market participants.**

A designated contract market must have and enforce rules that are designed to promote fair and equitable trading and to protect the market and market participants from abusive practices including fraudulent, noncompetitive or unfair actions, committed by any party. The designated contract market must have methods and resources appropriate to the nature of the trading system and the structure of the market to detect trade practice and market abuses and to discipline such behavior, in accordance with Core Principles 2 and 4, and the associated regulations in subparts C and E of this part, respectively. The designated contract market also must provide a competitive, open and efficient market and mechanism for executing transactions in accordance with Core Principle 9 and the associated regulations under subpart J of this part.