Wash Trade

FAQ

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1. **Who is considered a market participant?**

For the sole purpose of this FAQ, a market participant is defined as any person initiating or executing a transaction directly or through an intermediary, and any person for whose benefit such a transaction has been initiated or executed. A market participant also includes any individual, firm or agent, or group such as a floor, firm, execution desk or voice broker, that is involved with the placement, negotiation or execution of a transaction.

2. **What is a wash trade?**

A wash trade is a transaction or a series of transactions executed in the same Commodity Contract and delivery month or Option series at the same, or a similar, price or premium for accounts of the same Principal.

> The term **"Principal"** as used herein shall mean an individual or entity with a beneficial interest in an account.
>
> The term "**same Principal**" as used herein shall mean accounts that are owned by the same person, entity, or a parent and its 100% wholly owned subsidiaries, or subsidiaries that are wholly owned by the same parent and *shall also include accounts that have common ownership that is less than 100%.*

A wash trade occurs when there is an act of entering into, or purporting to enter into, transactions with no intent to obtain a *bona fide* market position or activity that gives the false appearance of an executed transaction(s), but does not subject the such Principal to any market risk or change in position or aid in price discovery. Wash trades are prohibited by the Commodity Exchange Act and Exchange Rule 4.02(c) which prohibit the execution of such trades. Any market participant who initiates, places, accepts or accommodates a transaction in a manner that the participant(s) knew or should have known would result in a wash trade will be violation of Exchange Rule 4.02(c). Additionally, an inference of intent to self-trade will be made by the Exchange if the market participant should have known, based on the unique characteristics of the market and other factors described herein, that the orders placed could create a wash result.

3. **Can a market participant who receives simultaneous buy and sell orders for the same Principal accept them? Is there a duty to inquire if the orders are for different Principals?**

Upon the receipt of **simultaneous buy and sell orders**, a market participant should inquire with the individual(s) who placed the orders to determine if such orders are for the same Principal. During that inquiry if the orders were placed on behalf of an omnibus account(s), the market participant, then, should further inquire to determine if the orders are for different Principals whose accounts are within the omnibus account. No matter the circumstance, if the orders are for the same Principal, the market participant may choose to accept or not to accept the orders. If the orders were accepted and ultimately trade opposite one another, in full or in part, any of the market participants involved in the placement or execution of such orders, that knew or should have known that the activity would result in a wash trade(s) may be in violation of Exchange Rule 4.02(c).

If it is determined that buy and sell orders placed at or near the same time are for different Principals, such orders must be executed in accordance with Exchange Rule 4.02(g). This Rule, however, prohibits market participants from contemporaneously entering both buy and sell orders for the same Commodity Contract in the same delivery month or Option series via a Crossing Order ("CO") unless such orders are for different Principals. Please see the Exchange's **Pre-Execution Communications FAQ** for further information regarding prohibited cross trading.

4. Why does a market participant receiving simultaneous buy and sell orders have a duty to inquire if the orders are for different Principals?

The CFTC and the Exchange have held that a market participant (including account executives and third-party brokers) may not knowingly participate in the execution of wash trades and, therefore, has an independent duty to inquire about the propriety of buy and sell orders placed for simultaneous execution. There may be circumstances that require a market participant to go beyond mere acceptance of the assertion made by the party placing the orders and take additional steps to ensure that the orders in question do not violate the prohibition on wash trades.

Upon request, the market participant receiving the orders shall provide sufficient correspondence demonstrating that an inquiry regarding whether the orders were for different Principals was made. If there is no documentation to support the inquiry, the market participant that accepted/executed the orders may be found to have been in violation of Exchange Rule 4.02(c) if the activity results in a wash trade(s).

5. What should a market participant do if they cannot determine if simultaneous buy and sell orders are for the same or different Principals?

The market participant should proceed with caution and may refuse to accept the orders to avoid the potential for executing wash trades. However, if the orders are accepted, and assuming the market participants have no knowledge of improper customer intent, regulatory risk may be mitigated by taking steps to ensure that they are not executed opposite each other, such as by ensuring that one order is entered and executed prior to the entry and execution of the second order. If the orders ultimately trade opposite one another, in full or in part, any of the market participants involved that knew or should have known that the activity would result in a wash trade(s) may be in violation of Exchange Rule 4.02(c). Please see FAQ #6 for further details.

In either case, the market participant should self-report the situation to the Market Regulation Department.

6. If simultaneous buy and sell orders for the same Principal are entered for a legitimate purpose, how should a market participant execute the orders to ensure compliance with Exchange rules?

If a market participant receives simultaneous buy and sell orders at or near the same time for the same Principal for execution on the Electronic Trading System ("ETS"), Order Records, including order tickets, emails or instant messages, as defined within Rule 6.08(a)(i), must be generated upon receipt and maintained. The Order Records must include order details and evidence the time of receipt, to the nearest minute, by means of an electronic time-stamp or other automated timing device. One of the orders should then be entered on the ETS and executed in full prior to the entry of the second order. A record of the second order including time of placement will be required because it was not entered on the ETS immediately upon receipt. This will ensure that the orders are not executed opposite each other and will provide a clear audit trail with respect to the entry and execution of the orders. For additional guidance on the appropriate recordkeeping requirements, please refer to Exchange Rules 6.07 and 6.08.

Simply ensuring that there is a delay between the entry of the buy and sell orders may not, depending on the terms of the orders and market conditions, preclude the orders from trading in whole or in part against each other. To the extent that the orders trade opposite each other, or are executed at nearly the same price, the result would be a transaction that incurred no market risk or change in position and, therefore, may be deemed a violation of Rule 4.02(c) irrespective of the fact that the orders were entered at different times.

7. **Is it acceptable to place simultaneous buy and sell orders for the same Principal with the same market participant for execution on a discretionary ("DRT") basis?**

If the market participant placing the orders does so simultaneously or nearly simultaneously and execution of the orders results in a wash trade, or if both orders are executed opposite the same third party (i.e., an accommodator), it is possible that the party placing the order, any party transmitting the order, the market participant executing the order and the accommodator(s) will be the subject of an enforcement action brought by the Exchange for engaging in an wash trades.

Depending on the circumstances, the placement of buy and sell orders for the same Principal, in addition to providing the executing market participant discretion over quantity disbursement, automated placement system(s), order type (e.g. iceberg or market order), price and/or time, may be viewed as an implicit request to negate the customer's market risk by directly or indirectly executing the orders against each other. The fact that the trade is not prearranged and is executed competitively may not protect the parties from liability if the execution of the orders produces a wash result and the parties knew or should have known the activity would produce such a result.

8. **Is it acceptable to place a buy order(s) with one market participant for execution and place a simultaneous sell order(s) for an account with the same Principal to a different market participant for execution?**

The potential for liability in this situation is significant. If the orders trade against each other in whole or in part, or if both orders are executed opposite the same third party, an inference may be drawn that there was intent to execute a prohibited wash trade. The fact that the trade is not prearranged and is executed competitively on the ETS may not protect the parties from liability if the execution of the orders produces a wash result. Any party involved in the placement or execution of the orders may be the subject of an enforcement action brought by the Exchange for engaging in a wash trade.

9. **If buy and sell orders are placed near the same time by the same Person or account, does the market participant receiving the orders have a duty to inquire whether the orders are for different Principals?**

All parties involved in this scenario should understand their duty to inquire whenever the same Person or account submits opposing orders in the same market on behalf of the same Principal or account. When buy and sell orders for the same product, similar quantity or price, or account are received at or near the same time, the party submitting the orders for execution on the ETS should recognize their need to inquire whether the orders are for different Principals. The party submitting the orders must be able to demonstrate that it engaged in due diligence prior to entry if such orders trade opposite one another and were ultimately for the same Principal. Any market participant involved, including the party entering the orders onto the ETS, who knew or should have known that the activity could result in a wash trade(s) may be found to be in violation of Rule 4.02(c).

10. **Under what circumstances does trading opposite your own orders on the trading platform violate Exchange rules regarding wash trades?**

Market participants are prohibited from entering both buying and selling orders for the same Commodity Contract for future delivery in the same delivery month or Option series unless such orders are for different Principals. It is a violation of Exchange Rule 4.02(c) for a market participant to enter an order on the ETS that [~~he~~]they knew or should have known would trade against a resting order on the other side of the market for the same Principal. Please review the Exchange's **Pre-Execution Communications FAQs** for acceptable execution methods for orders placed for different Principals.

11. Does the Exchange provide market participants any wash trade prevention features and is it mandatory for certain market participants?

The Exchange offers the usage of Self Trade Prevention Functionality ("STPF") to market participants. STPF resides within ICE's trading engine and provides various configurations to prevent self-trading of orders entered with the same STPF ID.

Currently, proprietary traders with direct market access ("DMA") who utilize algorithmic trading applications are ***required*** to utilize the Exchange's STPF to prohibit self-trading. Proprietary traders are defined as any entities or individuals that trade for their own account, or their company's account. Market participants who are not required to utilize the Exchange's STPF are advised to opt-in to the Exchange's STPF or employ tools that reduce the likelihood of self-matching, particularly if they frequently submit orders on both sides of the market that may trade against each other on more than an incidental basis.

For additional STPF information please refer to the Exchange's **STPF FAQ**.

12. Will the Exchange's STPF prevent all types of self-trades?

No. The STPF does not apply to derived orders from spreads or other strategies that may trade with outright orders. The STPF only prevents self-trading between orders in the same market, specifically outright-to-same-outright orders and spread-to-same-spread orders.

Generally, self-trades resulting from implied orders will be viewed as unintentional unless there is evidence indicating that a market participant intended for such orders to match opposite one another.

13. Is it a violation of Rule 4.02(c) if independently initiated buy and sell orders associated with the same Principal inadvertently match against each other?

If buy and sell orders which are placed by independent decision makers for accounts that reflect the trading of separate business units of the same Principal coincidentally match each other when executed, it would not be considered a violation of Rule 4.02(c) provided that the orders were entered without prearrangement, neither person had knowledge of the other party's order and the orders were not otherwise intended to match with each other. For these types of transactions, the parties to the trade must be able to demonstrate the independent control of the accounts and that the transaction had a bona fide business purpose for each party to the trade.

14. Is it permissible for a market participant to execute buy and sell orders opposite one another for the same Principal for the purpose of effecting a position transfer or to resolve an error?

No. In these circumstances, if the buy and sell orders trade in whole or in part opposite one another, the Exchange may deem any market participant involved in the initiation, placement, negotiation, execution or accommodation of a transaction that knew or should have known it was done for such purposes to be in violation of Exchange Rule 4.02(c).

Market participants should be aware that the Exchange does allow the transferring of an open position(s) that involves **no** change in beneficial ownership or to correct errors made in the clearing of a trade(s) provided that the transfer occurs within three Business Days after the date on which the error occurred, in accordance with Exchange Rule 4.37, "Transfer Transactions Not Required to Be Made Competitively."

15. Is it a violation of Rule 4.02(c) if independently initiated orders placed by different proprietary traders or Automated Trading Systems ("ATS") within the same market participant match against each other?

The Exchange recognizes that certain market participants have various proprietary trading operations composed of individual traders or a team of traders who, through fully independent trading decisions, manually place orders or operate ATSs. These strategies, although for the same Principal, may coincidentally match with each other when executed. If such orders were entered without prearrangement, were not otherwise intended to match with each other, and did not cause price or volume aberrations, such trades are not considered to be in violation of Rule 4.02(c), provided that the market participants can demonstrate such independence. However, if such orders resulted in trades that may have caused market disruption or unusual price or volume movements, even if coincidental, the activity may still be considered a wash trade and/or a violation of other Exchange rules.

Market participants should have and enforce policies to preclude affiliated traders who enter orders for the same Principal and have access to or knowledge of each other's orders from trading opposite each other. Additionally, market participants are responsible for monitoring their ATSs and for deploying them in a manner that minimizes the potential for the creation of wash results.

16. If orders entered by a single ATS or multiple ATSs controlled by the same individual trader or for the same team of traders ultimately match opposite one another, would the Exchange consider the trade to be a wash trade?

In these scenarios, such trades may be in violation of Rule 4.02(c) or other Exchange Rules, such as Rule 4.04, if they occur on more than an infrequent basis or if the trader(s) knew or should have known that the orders would trade opposite one another. It is recommended in this circumstance that the market participant employ functionality that will minimize the potential for the ATSs' buy and sell orders to match with each other, including the Exchange's STPF.

Market participants should also ensure that each strategy's Authorized Trader IDs ("ATIDs") are appropriately registered to the individual or group of individuals who operate the ATS or ATSs. If multiple ATS strategies are operated or controlled by the same individual or team, which submit orders in the same instrument, and have potential to trade opposite themselves, each strategy should have its own unique ATID.

17. Under what circumstances does unintentional or incidental matching of buy and sell orders from the same Principal violate Rule 4.02(c) or other Exchange rules such as Rule 4.04?

Unintentional and incidental matching of buy and sell orders for the same Principal generally will not be considered a violation unless such activity causes price or volume aberrations or occurs other than on an incidental basis. Additional factors for consideration include, but are not limited to, the number of self-trades; the market participant's usage of STPF to reject self-trades; and whether the matching or STPF rejections caused significant market interruptions or system anomalies that limited the ability of market participants to trade, engage in price discovery, or manage risk. The frequency of incidental self-matching for the same Principal in any circumstance will be evaluated in the context of the activity of the trader, trading group, or algorithm(s). Staff may expand the time period of review to determine if a pattern exists by comparing the trades and volume of wash/self-trades to the market participant's activity in the instrument traded. More than *de minimis* self-trading in this context will result in additional regulatory scrutiny and may be deemed to violate the prohibition on wash trades.

As a reminder, market participants are responsible for monitoring their trading, whether manual or automated, and are strongly encouraged to adjust their trading strategies or employ functionality designed to minimize, or eliminate altogether, the possibility of buy and sell orders matching opposite other proprietary traders, ATSs or independent decision makers of the same Principal.

18. Does the wash trade prohibition only apply to transactions entered or executed on the ETS?

No. The Exchange prohibits wash trading for all trade types, including but not limited to Crossing Orders ("CO"), Block Trades and Exchange for Related Positions ("EFRPs"). However, some exclusion may apply for Off-Exchange transactions which are detailed below:

1) **Block Trades** - The Exchange permits block trades in all futures and options contracts between different accounts of the same Principal, and would not deem a wash trade to have occurred if it can be demonstrated that each block trade meets the following requirements:

   i. The block trade price must be executed at a fair and reasonable market price;
   ii. Each party must have a separate and independent legal bona fide business purpose for engaging in the trades; **and**
   iii. Each party's decision to enter into the block trade must be made by a separate and independent decision-maker.

2) **EFRPs** - The accounts involved in the execution of an EFRP transaction must be:

   i. Independently controlled with different beneficial ownership; or
   ii. Independently controlled accounts of separate legal entities with the same beneficial ownership; or
   iii. Independently controlled accounts within the same legal entity, provided that the account controllers operate in separate business units.

"Independently controlled" means that the parties have separate accounts with separate operations (whose positions, even when exactly opposite, cannot be offset except by trading on the electronic platform) and that there is independent control of decision making with respect to transactions for such accounts.

If the Block or EFRP trade(s) do not meet the requirements set forth above, the transaction may constitute a wash trade prohibited by Rule 4.02(c). For more information please refer to the IFUS **Block Trade FAQ** and **EFRP FAQ** for additional guidance.

19. Are there unique considerations with respect to Rule 4.02(c) in the context of Exchange-sponsored volume incentive programs?

Market participants who participate in Exchange-sponsored programs with incentives tied in whole or in part to meeting specific volume thresholds should take proactive steps to prevent transactions between accounts of the same Principal, including utilizing the STPF offered by the Exchange.