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Australian Securities and Investments Commission
Level 5, 100 Market Street
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Attn: Dior Loveridge and Joseph Barbara

Via email: marketstructure@asic.gov.au

10 May 2013

Dear Sirs

IMC PACIFIC PTY LTD – RESPONSE TO ASIC CONSULTATION PAPER CP 202

Thank you for this opportunity to provide comment in response to ASIC Consultation Paper CP 202 *Dark liquidity and high-frequency trading: Proposals* (Consultation Paper). On behalf of IMC Pacific Pty Ltd (IMC), a company within the global IMC Financial Markets group, we provide below:

a) a brief overview of IMC (Section A);

b) an executive summary of IMC's views in response to the Consultation Paper (Section B); and

c) a more detailed discussion of those views (Section C).

A. IMC PACIFIC PTY LTD

1. IMC Pacific Pty Ltd, trading as IMC Financial Markets, is a wholly-owned subsidiary of IMC Financial Markets, a Netherlands based global proprietary trading firm established in Amsterdam in 1989. Since its establishment, IMC has specialised in making a market for a range of financial products, including derivatives, equities and ETFs, on exchanges around the world. In addition to Amsterdam, IMC presently has subsidiaries or offices in Chicago, Hong Kong, Zug and Sydney. Collectively, IMC trades across markets in Europe, the United States and the Asia Pacific region, including Hong Kong, Japan and Korea. On the ASX and ASX 24 market platforms IMC is a registered market maker of Exchange Trade Options (ETOs) and Contracts for Difference (CFDs).

2. The comments provided below reflect IMC's experience of over 20 years trading in these various markets and our observations of both regulatory and technological developments in these jurisdictions. We hope that ASIC will find our comments useful in further developing its proposals on dark liquidity and high-frequency trading.

B. EXECUTIVE SUMMARY

3. IMC agrees with the approach taken by ASIC to assess the impact of dark liquidity and high-frequency trading on market quality and integrity, and generally agrees with the proposals. In summary, IMC:

    a. supports proposals to improve fairness to all users of crossing systems;

    b. supports minimum disclosure requirements for course-of-sales reports on T+3, and would favour transparency and integrity of the market over privacy for principal traders; and

    c. supports enhancements to the current Market Integrity Rules to address manipulative trading practices.

4. However, IMC does have reservations about some of the proposals that may have undesired effects on market quality and integrity, and may not achieve the desired regulatory outcomes. In summary, IMC:

    a. opposes the introduction of minimum resting times, and believes that such a requirement would significantly widen spreads, reduce liquidity and move additional volume to dark venues; and

    b. opposes changes to tick sizes for specific categories of securities, and notes that we are yet to see the impact of existing regulatory changes.

C. COMMENTS

High-frequency trading

Excess messaging and market noise

5. IMC notes the Commission proposes to introduce a minimum resting time of 500ms for small orders. IMC is strongly opposed to the imposition of a minimum resting time for any products on the grounds that such a requirement is likely to significantly widen spreads, reduce displayed liquidity on lit markets, and push more volume to trade on dark venues (especially in the case of low tick price stocks). IMC submit that the regulatory benefit of such a requirement is minimal as compared to the detriment to market quality and legitimate trading activities of market participants.

6. IMC submits that a minimum resting time for small orders would result in a number of undesirable consequences for the market. Market participants would stop quoting small order size at tight spreads due to the increased risk involved, and this would reduce overall liquidity. The result of wider spreads would also mean the meaningful price improvement hurdle for trading on a dark venue would be lower, and more of the remaining liquidity would subsequently shift to those venues.

7. The Consultation Paper suggests that the regulatory benefit of eliminating small fleeting orders is one of minimising their impact on market integrity, efficiency, and investor confidence. IMC submit that market participants who enter small fleeting orders which have such an impact can already be adequately dealt with under existing market misconduct provisions and the scope of these powers will be further enhanced should the Commission adopt the proposed changes to 5.7.2 of the Market Integrity Rules.

8. With regard to the proposed sizes of 'small orders' more generally, IMC submits that the proposed size for the ASX SPI200 Index Future is much too large. The current proposal of three index futures contracts means a 'small order' (subject to the minimum resting time) can have a notional value of approximately $375,000. This appears to be significantly out of proportion to the cash limit of $500, and would have a significant impact on the market for these contracts, especially considering the average trade size for Q3 2012 was less than 2 contracts[1]. IMC submits that if the Commission is minded to adopt the small order resting time proposal, Index Future contracts should be excluded.

9. If the Commission is ultimately minded to adopt the proposal, IMC further submits that market makers may be unfairly affected by the restriction and should be exempt. Market makers are required to provide continuous quotes and to respond to quote requests, and any restriction on amending or cancelling small orders would have a negative impact firstly on the ability of a market maker to hedge it exposure (due to a constrained ability to react to changes in prices), and on their ability to determine an accurate theoretical price (due to stale orders remaining in the order book).

10. IMC also submits that the implementation of any such requirements should be at the exchange level rather than through the systems of individual brokers, and note that a centralised solution would minimise the overall costs of implementation.

Manipulative trading

11. IMC supports proposals to enhance the current Market Integrity Rules to address manipulative trading practices. Additional guidance from ASIC in relation to trading practices, circumstances, and strategies considered to be illustrative of manipulative activity would likewise be welcomed as it would provide both greater clarity to participants involved in, or concerned about, algorithmic trading.

Dark Liquidity: Proposals for crossing system operators

Fairness to all users

12. IMC supports the proposals of the Commission to address appropriate regulation and transparency of crossing systems and crossing system operators. Specifically, IMC believes that the proposals in relation to fairness to all users of crossing systems are important to ensure both adequate disclosure of policies and procedures for each system, and to avoid discrimination amongst users of these systems.

Dark Liquidity: Other proposals

Tick sizes

13. IMC is not in favour of reduced tick sizes for specific securities, and note that such changes would likely lead to a reduction in displayed liquidity for these securities.

14. The apparent desired regulatory outcome, of minimising volume shifting to dark venues unnecessarily, may yet be achieved by the Commission's existing (yet to come into effect) requirement for meaningful price improvement. However, any measures of change in market

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[1] p3, Market Quality Indicators: ASX Equity Index and Interest Rate Futures, September Quarter 2012 http://www.asx.com.au/documents/products/market-quality-indicators-20121116.pdf

integrity and quality due to this existing requirement would be obscured by a change to tick sizes for some securities (or, for that matter, the imposition of minimum resting times).

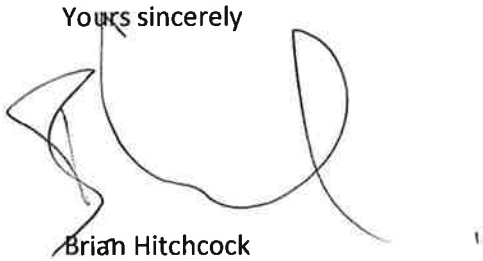
Course-of-sales disclosure (T+3)

15. IMC supports the Commission's proposal for minimum disclosure requirements in T+3 reports. Even as a principal trader itself, IMC would prefer that course-of-sales reports favour transparency and integrity of the market over the protection of individual participants' principal trading activities.

16. Similarly with regard to the question of crossing systems, IMC also supports the disclosure of which system each trade has been matched.

Thank you again for this opportunity to respond to the Consultation Paper. IMC would be pleased to discuss the matters raised in this response further at the convenience of ASIC.

Yours sincerely



Brian Hitchcock
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