European Central Bank – Changes to the FX Global Code

Leigh Meyer, Marco Heil

FX Global Code – Guiding Principles

The FX Global Code (FXGC) is a set of principles of good practice for foreign exchange market participants.
It aims to promote the integrity and effective functioning of the wholesale foreign exchange market.
It identifies the principles, values, behaviours and practices required for a fair and transparent market.

- Ethics
- Governance
- Information Sharing
- Execution
- Risk Mgmt. & Compliance
- Confirmation & Settlement

Introduced in 2013	Code is voluntary	Citigroup has signed up to the FXGC	Central banks must act as an example
The FXGC does not have legal or regulatory requirements	Drives investments and procedures	Statements of Adherence are publicly registered	Employees must have the right levels of knowledge
Puts a priority on ethics and conduct	Required for membership of FX Market Contact Group.	Competitive advantage	Annual reviews with a deeper review every three years

FX Global Code – Key Change – Access to Confidential Information

Principle

- PRINCIPLE 19 Market Participants should clearly and effectively identify and appropriately limit access to Confidential Information.

Problem Statement

- Operations should have appropriate segregation of duties, both internally within Operations and within the Business line.
- Operations should not see Material Non-public Information unless necessary.

Solution

- **Designated staff with appropriate tag**
- **Private** – those who have, or need access to Material Non-Public Information (otherwise referred to in some jurisdictions as Inside Information, or Unpublished Price Sensitive Information or UPSI), collectively referred to as 'MNPI', as part of their day-to-day responsibilities
- **Public** – those who do not need access to such information or for which access would prevent them from being able to perform their day job, such as trading or advising on or recommending securities to clients.

Key Issues

- Full review of public / private designation.
- Formal communications of tagging designation.
- Process to bring public-side staff 'over-the-wall' for specific private transactions.

FX Global Code – Key Change – Intraday and End-of-Day Funding

Principle

- PRINCIPLE 53 Market Participants should have adequate systems in place to allow them to project, monitor, and manage their intraday and end-of-day funding requirements to reduce potential complications during the settlement process.

Problem Statement

- Visibility intraday to finality of incoming and outgoing payments differs per country / ccy.
- Impact of failed / late incoming payments.
- Sharing of nostros between lines of business creating potential for cross impact / accountability / exception allocation / interest verification.

Key Issues

- Capturing and normalising accurate and matched real-time data.
- Data quality/content – may improve with evolution of ISO 20022.

Solution

- Real time same day nostro reconciliation.

FX Global Code – Key Change – Managing Operational Risk

Principle

- PRINCIPLE 29 Market Participants should have adequate processes to manage counterparty credit risk exposure, including where appropriate, through the use of appropriate netting and collateral arrangements, such as legally enforceable master netting agreements and credit support arrangements.
- PRINCIPLE 35: SETTLEMENT RISK Market Participants should take prudent measures to manage and reduce their Settlement Risks as much as practicable, including by settling FX transactions through services that provide PVP settlement where available prompt resolution measures to minimise disruption to trading activities.

Problem Statement

- Introduction of a process that mitigates the risk associated with FX Settlement.
- The settlement risk limit control check is introduced at payment generation providing an online and intraday limit check for all settlements. The settlement risk appetite is determined by the existing settlement risk limit per counterparty. These limits will include any failed settlements and any earmarked funds for future settlements.
- In the event settlement limit is breached then trades will revert to Delivery Versus Payments (DVP). As trades are reconciled the data will replenish the credit availability per counterparty.
- “No Confirmation No Pay” guideline

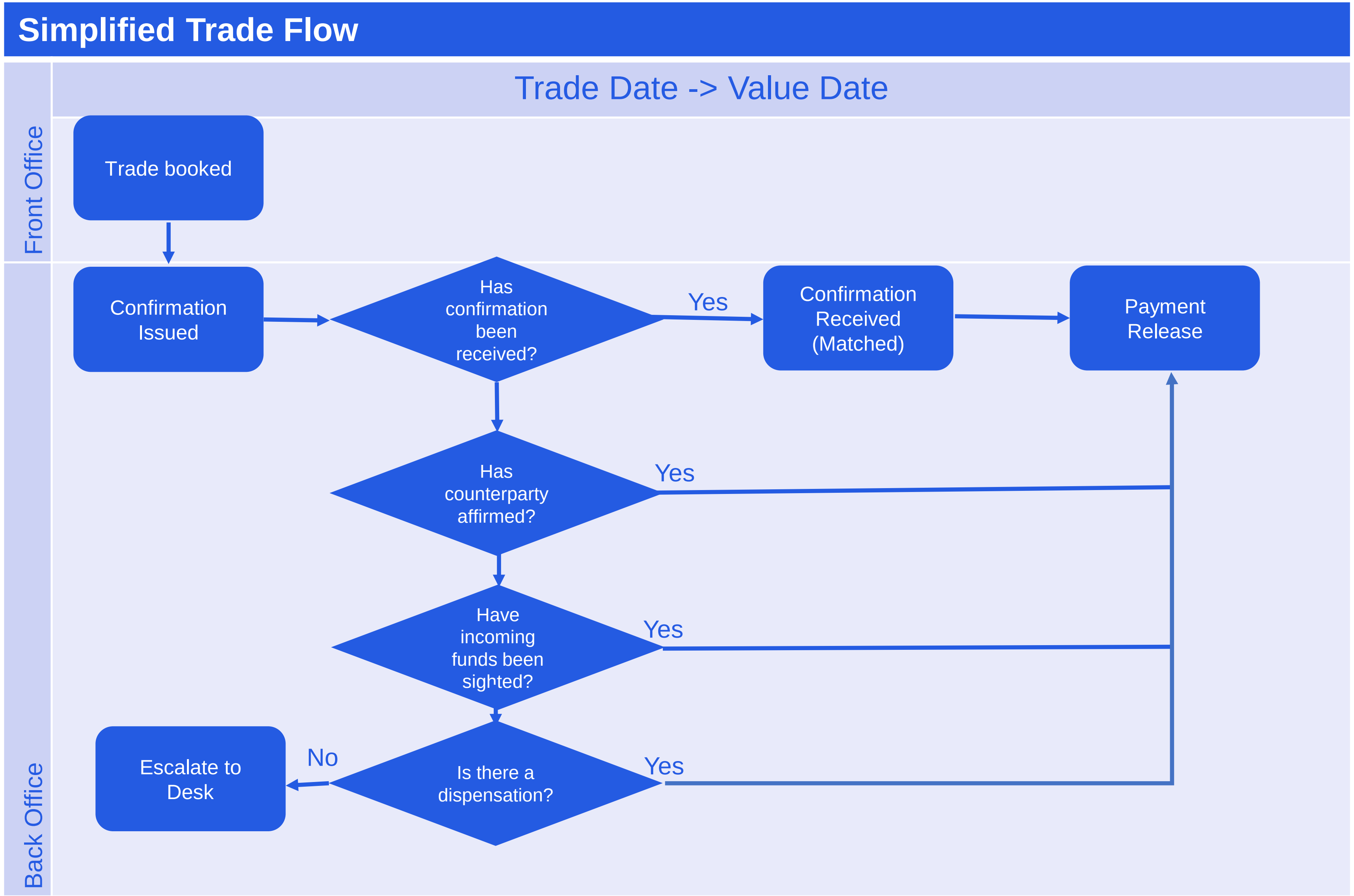
Key Issues

- Socialisation and embedding of process with key stakeholders.
- Employee training and attestation.
- Exception management (e.g., priority of trade vs availability of confirm due to end of day).
- Confirmation timeliness and client behaviour

Solution

- Adoption of confirmation channels and capabilities.
- Continuous Linked Settlement (CLS) – maximise use of PvP.
- Payment Period Capacity (PPC) implementation – Citi specific solution.

FX Global Code – Key Change – No Confirmation No Pay



- Simplified, the guidelines stipulate that without confirmation from our counterparty that we will require:

  - Affirmation

OR

  - Sight of funds

OR

  - Approved Dispensation

Before release of payment obligation.

FX Global Code – Key Change – Managing Operational Risk

Settlement Risk Waterfall

CLS Settlement	Cleared Centrally	PvP / DvP Solutions	Bilateral Netting	Gross Settlement
		Removes Principal Risk		
Removes Principal Risk	Removes Principal Risk	Can be Net or Gross	Reduces Principal Risk	Full Principal Risk
Retains Some Operational Risks	Retains Some Operational Risks	Retains Some Operational Risks	Significant Operational Risks	Can Reduce Operational Risks

Maximise

Develop

Standardise

Questions and Answers

Tour the Table

1. How does your institution control the adherence to the principles?
2. Where do you see the advantages / disadvantages of such a Global Code?
3. What would you like to see added / changed on the Global Code?