ACT LEADING TREASURY PROFESSIONALS

GIVING DIRECTION

BRIEFING NOTE:

FX GLOBAL CODE

GUIDANCE FOR CORPORATES

JULY 2017

Briefing note

FX GLOBAL CODE: GUIDANCE FOR CORPORATES

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Executive Summary

This Briefing Note is written with corporates in mind and therefore highlights those points of particular relevance to them.

The ACT recommends that all readers of this Briefing Note review the entire 'FX Global Code' and 'Report on Adherence' when deciding the most appropriate response for their organisation.

What is the FX Global Code?

The purpose of the FX Code is to promote the integrity and effective functioning of a robust, fair, liquid, open and transparent FX market in which Market Participants can confidently and effectively transact in a manner that conforms to acceptable standards of behaviour.

The FX Global Code (FX Code) is a voluntary code setting out principles of good practice in the wholesale foreign exchange market (FX market). The FX Code does not impose legal or regulatory obligations on Market Participants but, by identifying good practices, it is intended to serve as a supplement to local laws, rules and regulations.

Why was it developed?

The FX Code was developed in response to a number of incidents that resulted in a loss of trust in the effective functioning of the FX market. It was developed by a partnership between central banks and Market Participants from 16 jurisdictions around the globe to provide a common set of guidelines for the wholesale foreign exchange market.

Who does it apply to?

Although the FX Code is voluntary, it is intended to apply to all Market Participants.
A Market Participant is defined as an entity that is active in the FX markets as a regular part of its business – this definition captures corporate treasury departments when entering into external FX transactions.

Importantly, whilst it applies to all Market Participants, there is a concept of **proportionality** embedded in the FX Code. That is to say, the FX Code is expected to apply to all Market Participants, but the details of how it may apply can depend on the nature and extent of their activity in the FX market. Broadly, the steps that a very active Market Participant that engages in complex transactions takes to align its practices with the Code may be different to those taken by less active participants.

How is it structured?

The FX Code is principles based, to encourage active consideration of how best to integrate the desired behaviours into the day-to-day activities of Market Participants (and to avoid adherence becoming a box ticking exercise).

It is organised around six leading principles covering:

- Ethics:
- Governance:
- Execution
- Information Sharing:
- Risk Management and Compliance:
- Confirmation and Settlement Processes

The process of adoption

The 'Report on Adherence'[1] sets out a blueprint for the widespread adoption of the Code.
One key element of this blueprint is the suggested approach for Market Participants to take when planning how to adopt the FX Code's principles into the day to day activities of the treasury team.
It recommends that they consider:

- How the FX Code is **embedded** in a market participant's practices;
- How a market participant will subsequently **monitor** its practices against the FX Code; and
- How a market participant might **demonstrate** its adherence to the FX Code.

Although voluntary, central banks and regulators are taking a close interest in the implementation process and the publishing of statements of commitment to this Code by Market Participants.

What does it mean for corporates?

The FX Global Code imposes a series of Rights and Obligations on all Market Participants[2], including corporates:

- Obligations: adoption of the FX Code (as appropriate) to embed good practice in the day to day activities of the organisation
- Rights: an expectation that counterparties in the FX market have adopted the standards of good practice and behaviours expected under the FX Code

All FX Market Participants have a role to play in promoting and upholding good practices in the market as a whole.
This can be achieved through leading by example, by having similar expectations of counterparties and other Market Participants and by helping to raise awareness of the FX Code in their market interactions.

The widespread adherence to the voluntary FX Code will only come about if firms judge it to be in their interest and take the practical steps to ensure the FX Code is sufficiently embedded in their practices

From a corporate perspective, encouraging counterparties to adhere to the FX Code raises the bar for good practice across the entire market - which can only be beneficial in the long term.

Key points:

- The FX Code is global
- The FX Code is voluntary
- It applies to anyone who is 'active' in the FX markets – a Market Participant
- It is principles based – to encourage participants to actively think about what they are doing
- The FX Global Code is not designed to provide definitive answers, but it should help identify the right questions when thinking about good practice
- Proportionality is key – i.e. the nature, complexity and scale of market activity will inform the steps a Market Participant takes to adhere to the Code
- Adoption of the FX Code is best achieved by embedding, monitoring and demonstrating adherence
- There is one overarching principle: "Market Participants should strive for the highest ethical standards."

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[1] Report on Adherence to the FX Global Code http://www.bis.org/mktc/fxwg/adherence_report.pdf
[2] Speech by Sarah John, Head of Sterling Markets Division, Bank of England
http://www.bankofengland.co.uk/publications/Pages/speeches/2017/982.aspx

What should I do next?

- Read this briefing note for an overview
- Read through the FX Global Code identifying those principles that may be relevant for your organisation
- Read the Report on Adherence for guidance on how to integrate the FX Code into the organisation
- Undertake a Gap Analysis between your organisation's existing policies and procedures and the principles set out in the FX Code
- Identify any changes required in day-to-day activities in order to adopt the FX Code
- Develop an implementation plan and timeline to share internally and with internal/external auditors if appropriate
- Decide whether (and who) will sign the Statement of Commitment
- Discuss with your counterparties how the FX Code will alter their behaviour

Market Participants should be familiar with the FX Code, how it might be relevant to them and their counterparties, and consider how they can adopt the FX Code in a proportionate manner.

What is the FX Global Code?

The FX Global Code (FX Code) is a voluntary code setting out principles of good practice and providing a common set of guidelines for the wholesale foreign exchange market. It does not impose legal or regulatory obligations on Market Participants but, by identifying good practices, it is intended to serve as a supplement to local laws, rules and regulations.

The FX Code replaces several different Codes which previously existed in various corners of the FX market.
In the UK, this was the NIPs Code (Non-investment Products), which has now been superseded by a combination of the FX Code, the UK Money Markets Code (covering unsecured deposits from the old NIPs Code as well as repos and securities lending previously covered elsewhere), and the Global Precious Metals Code (covering bullion).

The FX Code covers all of the wholesale FX industry - the sell side, the buy side, infrastructure providers, bank and non-bank participants; central banks and private sector; developed and emerging markets.

Its intended reach is global - it was developed by a partnership between central banks and Market Participants from 16 jurisdictions around the globe to provide.

The steps different Market Participants will take to align their activities with the principles of the FX Code will differ, reflecting the size, complexity, nature and extent of their engagement with the FX market. The FX Code has been purposely drafted to enable proportionate adoption and adherence.

In summary, there are three important points worth highlighting:

- It's a single code for the whole industry (universal)
- It's a global code and
- It is voluntary

Why has the FX Global Code been developed?

The foreign exchange market is arguably the oldest, largest and yet one of the most rapidly evolving financial markets in the world. However, its very nature has thrown up a number of challenges:

- Changes in technology have levelled the playing field for Market Participants, but at times these changes have left less active players at an information disadvantage;
- No single regulatory body oversees the foreign exchange market. Instead, participants have been guided by regional regulations, multiple codes of conduct and numerous sets of best practices; and, most importantly
- The global financial crisis, followed by several very specific incidents in the foreign exchange market, has contributed to a loss of public trust in Market Participants and in their ability to act in the best interests of end-user clients and in the effective functioning of the FX market.

In response to these challenges and, specifically, in order to restore trust in the foreign exchange market, the decision was taken to develop an FX Global Code to deliver:

- A single global approach
- A common set of principles to which all Market Participants could commit enabling participants to effectively and equitably navigate a rapidly changing market

"One of the guiding principles underpinning our work is that the FX Code should promote a robust, fair, liquid, open and transparent market. A diverse set of buyers and sellers, supported by resilient infrastructure, should be able to confidently and effectively transact at competitive prices that reflect available market information and in a manner that conforms to acceptable standards of behaviour."[3]

[3] Opening Remarks at the launch of The FX Global Code: Guy Debelle http://www.globalfxc.org/docs/gd_remarks.pdf

To whom does it apply?

Simply put, the FX Global Code applies to all Market Participants.

"For the purposes of this document [the FX Global Code], a "Market Participant" is a person or organisation (regardless of legal form) that:

i. is active in FX Markets as a regular part of its business and is engaged in the activity of the purchase or sale of one currency against another, or in transactions designed to result in gains or losses based upon the change in one or more FX rates, such as derivatives, whether deliverable or non-deliverable, either directly or indirectly through other Market Participants; or
ii. operates a facility, system, platform, or organisation through which participants have the ability to execute the type of transactions described in i.; or
iii. provides FX benchmark execution services; and
iv. is not considered a retail market participant in the relevant jurisdiction(s)

As a guide, the following types of persons or organisations would generally be expected to engage in FX Market activities as Market Participants, as described in (i) – (iv) above:

- financial institutions;
- central banks, except where this would inhibit the discharge of their legal duties or policy functions;
- quasi-sovereigns and supranationals, except where this would inhibit the discharge of their organisational policy mandate;
- asset managers, sovereign wealth funds, hedge funds, pension funds, and insurance companies;
- **a corporate treasury department, or Corporate Treasury Centre entering into external (non-group) transactions either on its own account or on behalf of the parent companies, subsidiaries, branches, affiliates, or joint ventures of the group it represents;**
- family offices running treasury operations;
- benchmark execution providers;
- non-bank liquidity providers; firms running automated trading strategies, including high-frequency trading strategies, and/or offering algorithmic execution;
- brokers (including retail FX brokers); investment advisers; aggregators; and analogous intermediaries/agents;
- remittance businesses, money changers, and money services businesses in their interactions in the wholesale FX Market;
- E-trading platforms;
- affirmation and settlement platforms; and
- any entity classified as an FX Market Participant in the relevant jurisdiction(s) "[4]

The FX Code is expected to apply to all Market Participants, but the details of how it may apply will depend on the nature and extent of their activity in the FX market. .
This concept of **proportionality** is fundamental to the FX Code and is expanded further below.

[4] FX Global Code

How is the FX Code structured?

The FX Global Code is **principles** rather than rules based. There are several reasons why this approach was adopted:

- The diverse constitution of the global FX market (the level of sophistication of both Market Participants and the various international markets themselves) means that a principles based approach can be more easily adapted and adopted by the very diverse constituents.
- A principles based approach is designed to make Market Participants actively **think** about how they might implement the FX Code (rules, especially if voluntary, are 'easy' to either arbitrage or just ignore).
- The combination of a principles based approach and the adherence mechanisms being adopted by various central banks and other regulators (e.g. including links to the Senior Managers regime in the UK) mean that the FX Code is flexible.

The FX Code is organised around six leading principles:

- **Ethics:** Market Participants are expected to behave in an ethical and professional manner to promote the fairness and integrity of the FX Market
- **Governance:** Market Participants are expected to have a sound and effective governance framework to provide for clear responsibility for, and comprehensive oversight of, their FX Market activity and to promote responsible engagement in the FX Market
- **Execution:** Market Participants are expected to exercise care when negotiating and executing transactions in order to promote a robust, fair, open, liquid, and appropriately transparent FX Market
- **Information Sharing:** Market Participants are expected to be clear and accurate in their communications and to protect Confidential Information to promote effective communication that supports a robust, fair, open, liquid, and appropriately transparent FX Market
- **Risk Management and Compliance**: Market Participants are expected to promote and maintain a robust control and compliance environment to effectively identify, manage, and report on the risks associated with their engagement in the FX Market
- **Confirmation and Settlement Processes**: Market Participants are expected to put in place robust, efficient, transparent, and risk-mitigating post-trade processes to promote the predictable, smooth, and timely settlement of transactions in the FX Market

Each principle in the FX Code is predicated on transparency and disclosure. Providers of services need to be transparent about the products that they offer and the ways in which they execute a transaction. Similarly, it is incumbent upon the buyers of those services to understand what they are purchasing, to ask questions about how an order will be executed, and, when necessary, to provide clear guidance about their preferences.

The FX Code principles have been developed to be relevant for all Market Participants, enabling broad commitment to the FX Code. All corporates should be familiar with, and operating under the leading principles set out above as simple statements of best practice**.**

Under each of these leading principles, there are a number of further principles (55 in total), many of which will also be relevant to corporates, although some less so.

The principles are written in plain language and should be easily read and understood by Market Participants. The principles are supplemented by a suite of examples (including examples particularly relevant to corporates) to illustrate their practical application.

The importance of proportionality

Of particular relevance to corporates, the FX Code incorporates the principle of proportionality in order to strike a balance between respecting diversity whilst retaining consistency in a global initiative

- across jurisdictions, both in terms of market structure and the regulatory treatment of FX, and
- amongst Market Participants

The foreword of the FX Code explicitly acknowledges that **"the steps that different Market Participants take to align their activities with the principles of the Global FX Code will necessarily reflect the size and complexity of the Market Participant's FX Market activities, and the nature of the Market Participant's engagement in the FX Market, and will take account of Applicable Law"**[5]

Many of the high-level principles within the FX Code require Market Participants to exercise judgement when implementing the FX Code. This approach is in line with the voluntary nature of the FX Code and encourages Market Participants to carefully consider whether their actions are consistent with the FX Code principles.

For example, the FX Code sets out principles for consideration when designing a risk management framework, but acknowledges that what constitutes an effective framework will vary substantially between different Market Participants based on the nature of their activities.

The process of adoption

Although the FX Code is voluntary, to be effective it will need to be widely adopted and adhered to by Market Participants across the FX market. The failure of previous codes to gain widespread adoption has been recognised and considerable work has been done to ensure that the FX Code gains the necessary level of traction in the market.

Specifically, the FX Working Group (FXWG)[6] has developed a recommended approach to adoption and adherence. The approach is developed with all Market Participants in mind, and is sufficiently flexible that it offers corporates of all levels of complexity a pathway through the adoption process that can be adapted to suit their particular requirements.

The Report on Adherence to the FX Global Code[7] sets out A Blueprint for Achieving Adoption which is organised around four key tenets, the key elements the FXWG believe will be required for the FX Code to be successful:

i. The Code should be clear, relevant and reflect good practice in the FX Market;
ii. It is the responsibility of Market Participants to take appropriate steps to adopt the Code in their day-to-day practices and culture;
iii. It is the role of central banks to lead by example and demonstrate their commitment to promoting and maintaining good market practice; and
iv. It is important that Market Participants and central banks maintain an active engagement with the Code and have appropriate structures in place to ensure that it remains relevant.

Focussing on the second of these: adoption, the FXWG identified three key elements that Market Participants will need to consider in order to establish an effective framework for adopting and adhering to the FX Code and the following section is largely transcribed from their report and covers:

- How the FX Code is **embedded** in a market participant's practices;
- How a market participant will subsequently **monitor** its practices against the FX Code; and
- How a market participant might **demonstrate** its adherence to the FX Code.

[5] FX Global Code
[6] FX Working Group – established by central banks to facilitate the creation of the FX Global Code http://www.bis.org/about/factmktc/fxwg.htm
[7] Report on Adherence to the FX Global Code http://www.bis.org/mktc/fxwg/adherence_report.pdf

Embed the FX Global Code

It is important for Market Participants to embed the FX Code in their day-to-day operations and help create a strong culture, both within their organisation but also in the market as a whole.

- In their own organisations, Market Participants will need to assess whether their practices are consistent with the guidance within the FX Code, for example, by undertaking a review of existing policies and procedures and, where necessary, taking appropriate and proportionate steps to align practices with the Code.
- More broadly, Market Participants have a role to play in promoting and upholding good practices in the FX market as a whole. This can be partly achieved through leading by example, but can also be supported by having similar expectations of counterparties and other Market Participants and helping to raise awareness of the FX Code in interactions with such parties.

For some Market Participants, for example, appropriate steps to embed the Code may include reviewing existing policies and procedures, and assessing the appropriate levels of senior management oversight; others may want to establish dedicated staff training on the FX Code or embed the principles within the FX Code into existing training. The approach of individual Market Participants will reflect the size and complexity of their FX activities and the extent of their engagement in the FX market.

Monitor adherence to the FX Code

Market Participants that have embedded the FX Code into their policies and procedures should establish appropriate mechanisms to monitor how effectively they have done so.

- In their own organisations, Market Participants may look to the text of the FX Code itself for some practical guidance on how to monitor adherence to the FX Code but ultimately Market Participants should exercise their own judgement of what is appropriate taking into consideration the principle of proportionality.
- More broadly, the Global Foreign Exchange Committee (the 'owner' of the FX Global Code going forward, replacing the FXWG) will monitor the FX market's progress in embedding the FX Code in day-to-day practices and the wider evolution of the prevailing culture in the FX market.

Demonstrate adherence

By publicly demonstrating their adherence to the FX Code, Market Participants raise the profile of the FX Code, and provide other Market Participants with a means for comparing potential counterparties and service providers.
One reason for a public demonstration of adherence is that firms are more likely to adhere to the FX Code if they believe that their peers are doing so too.

To facilitate this the FXWG has developed a **Statement of Commitment**[8] which Market Participants can use publicly, or bilaterally, to support key objectives of the FX Code.

The Statement of Commitment provides a single, common basis by which each Market Participant can represent that it:

i. supports the Code and recognises it as a set of principles of good practice for the FX Market;
ii. is committed to conducting its FX Market activities in a manner that is consistent with the principles of the Code; and
iii. considers that it has taken appropriate steps, based on the size and complexity of its activities, and the nature of its engagement in the FX Market, to align its activities with the principles of the Code.

It will be up to each Market Participant to decide whether and how to use the Statement.
The concept of proportionality is embedded in the Statement of Commitment.

[8] See appendix and Statement of Commitment http://www.globalfxc.org/docs/statement_of_commitment.pdf

PRO FORMA STATEMENT OF COMMITMENT TO THE FX GLOBAL CODE

("Institution") has reviewed the content of the FX Global Code ("Code") and acknowledges that the Code represents a set of principles generally recognised as good practice in the wholesale foreign exchange market ("FX Market").

The Institution confirms that it acts as a Market Participant as defined by the Code, and is committed to conducting its FX Market activities ("Activities") in a manner consistent with the principles of the Code.

To this end, the Institution has taken appropriate steps, based on the size and complexity of its Activities, and the nature of its engagement in the FX Market, to align its Activities with the principles of the Code.

Institution name: ____

Date: ____

The Future

As it is crucial that the FX Global Code remains up to date and evolves as the market evolves in order to maintain its relevance, the FX Code will be collectively owned, maintained and updated by the Global Foreign Exchange Committee (GFXC)[9]. This will continue the public sector – private sector partnership which has supported the development of the FX Code.

The GFXC will regularly assess whether new information or market developments warrant updates or additions being made to the FX Code.

Source Materials

This report has drawn extensively on the following materials, effectively summarising those points of most relevance to the corporate audience.

Global FX Committee Press Release: Global code of conduct sets out good foreign exchange market practice (25 May 2017)
http://www.globalfxc.org/press/p170525a.htm and associated links to speeches by Guy Debelle and David Puth

Foreign Exchange Working Group: Report on Adherence to the FX Global Code (May 2017)
http://www.bis.org/mktc/fxwg/adherence_report.pdf

FX Global Code: http://www.globalfxc.org/docs/fx_global.pdf

Statement of Commitment: http://www.globalfxc.org/docs/statement_of_commitment.pdf

Speech by Sarah John, Head of Sterling Markets, Bank of England given at a briefing on the financial markets code of practice to the Association of Corporate Treasurers, Bank of England (June 2017).
http://www.bankofengland.co.uk/publications/Pages/speeches/2017/982.aspx

[9] http://www.globalfxc.org/

Appendix

PRO FORMA STATEMENT OF COMMITMENT TO THE FX GLOBAL CODE

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The Institution confirms that it acts as a Market Participant as defined by the Code, and is committed to conducting its FX Market activities (“Activities”) in a manner consistent with the principles of the Code.

To this end, the Institution has taken appropriate steps, based on the size and complexity of its Activities, and the nature of its engagement in the FX Market, to align its Activities with the principles of the Code.

Institution name: ____

Date: ____

THE ACT WELCOMES COMMENTS ON THIS REPORT

Please send your comments to

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