# FSB Final Recommendations for FX Benchmark Reform

# Coverage Report

2 October 2014

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# FINANCIAL TIMES

Forex markets face further regulations
Financial Times
By Sam Fleming
30 September 2014

Participants in foreign exchange markets have been warned they may face further regulatory change even after implementing a long-awaited series of recommendations aimed at removing the taint affecting the sector.

A task force set up by the Financial Stability Board on Tuesday set forth 15 reforms aimed at overhauling the $5tn currency markets following allegations surrounding the crucial 4pm forex fixing.

The report from the global umbrella group said it expected the industry to accept all of the ideas, which include tougher rules aimed at minimising conflicts of interest within banks and a well-flagged widening of the window of time during which the key forex benchmark is calculated.

But the report cautioned that further change could still follow down the line – with Britain already consulting on including the 4pm fix in a list of benchmarks that are policed by regulators.

“Investigations into alleged misconduct are ongoing across a range of markets, and it is possible that the authorities will ultimately conclude that regulatory change is needed to promote or ensure appropriate behaviours and/or to implement the recommendations of this report,” the report said.

The FSB started to scrutinise the London-dominated global forex market in February after a sprawling investigation by regulators and prosecutors into benchmark-rigging allegations piled on pressure to reform a largely unregulated industry.

Its proposals suggest that the key window during which the 4pm fix is calculated be extended from the current period of one minute to make it less prone to manipulation, with industry feedback pointing to a five-minute window.

However regulators shelved a previous suggestion that would have created a global “utility” to match fixing orders placed by market participants, saying it wanted to allow industry-led initiatives to move ahead.

The FSB report said that banks need to implement tough procedures separating the wok of handling fixing orders from other business, reducing the potential for manipulation to occur.

“Firms should establish distinct and separate processes for managing fixing flows as part of their effort to ensure that customer and flow information is appropriately protected,” the FSB said.

It noted that such changes were “not costless” and could reduce banks’ capacity to absorb the risk from transactions, but it insisted this did not overshadow the benefits of reform.

The FSB also called for codes of conduct governing the sector to be much clearer about what information can be shared between market-makers.

Marshall Bailey, President of the ACI, an industry group, said: “The formal adoption of an international set of standards for ethical conduct and behaviour across the global financial industry will provide clarity and guidance on what is expected of all market professionals, from day traders to senior executives.”

James Kemp, Managing Director of the FX division of the Global Financial Markets Association said: “There may well be challenges and costs in implementing the changes, but enhancing confidence in the market is crucial and the industry will adapt to embrace these recommendations.”

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Bloomberg

## Global Regulator Backs FX Revamp After Rigging Scandals

Bloomberg
By Jim Brunsden and Ben Moshinsky
30 September 2014

A panel of global regulators, responding to a manipulation scandal that's shaken the financial industry, backed measures to make it harder for traders to exploit key benchmarks in the $5.3 trillion-a-day currency market.

The Financial Stability Board said it supports extending the width of the trading window used to calculate foreign-exchange rates to five minutes in a rule overhaul that also includes measures to address potential conflicts of interest between banks and their clients.

"The incentive to manipulate is always going to be there: what we have to make sure is the ability to actually do it is reduced," Rosa Abrantes-Metz, a professor at New York University's Stern School of Business, said in a telephone interview. The FSB report "talks about many things, such as no sharing of information among traders beyond what is necessary, but that should have been in place for a long time."

At least a dozen regulators on three continents are investigating whether traders in the world's largest financial market colluded with counterparts at other firms to manipulate benchmarks used by money managers and pension funds to determine what they pay for foreign currency. More than 25 traders have been fired or suspended across the industry.

4 p.m. Fix

The FSB, which brings together regulators, central bankers and government officials from the Group of 20 nations, proposed changing how the most popular benchmarks from WM/Reuters are calculated, including extending the one-minute windows in which rates including the key 4 p.m. London fix are set.

"Changes have to be made and FX more broadly may need to be brought within regulation," Sharon Bowles, a former head of the European Parliament committee dealing with financial regulation, said by e-mail. "The issue of not just culture but an absence of ethics has to be tackled. Too much has been accepted as normal even by some professional investors."

Widening to five minutes, in line with the median response in a public consultation, "strikes a balance between reducing incentives for manipulation while at the same time still ensuring the fix is fit for purpose by generating a replicable market price," the Basel, Switzerland-based FSB said in a report today.

‘Appropriate Width’

The FSB backed away from setting the industry standard window itself, recommending “the appropriate width of the window should be determined, and regularly reviewed, by WM in consultation with market participants.”

“The size of the window should not be fixed for all time nor, ideally, dictated by the authorities,” the group said.

Other recommendations from the FSB include more detailed codes of conduct for currency trading, and that “index providers should review whether the foreign-exchange fixes used in their calculation of indexes are fit for purpose.”

The FSB recommended that “banks (and other FX dealing intermediaries) establish and enforce their internal guidelines and procedures for collecting and executing fixing orders including separate processes for handling such orders.” Firms should “establish distinct and separate processes for managing fixing flows,” the group said.

Due Diligence

Asset managers “should conduct appropriate due diligence around their foreign-exchange execution and be able to demonstrate that to their own clients if requested,” according to the FSB.

“Investors need confidence in the administration of benchmarks, so we welcome the FSB’s recommendations” and a previous report from the International Organization of Securities Commissions, Richard Metcalfe, director of regulatory affairs at the Investment Management Association, said by e-mail.

“We note the focus on a variety of factors and players in both reports,” Metcalfe said. “They consider not just administrators but indices that embed FX rates, investment fund mandates and of course trading activity. With rigorous policing by supervisors, they will be a step towards restoring confidence in FX benchmarks,” Metcalfe said.

Tightening the rules for currency benchmarks would spur some banks to close down their foreign-exchange arms, according to State Street Corp.

“Is it worth setting up all these extra controls, hiring additional people, setting up a separate space, or do you want to just get this off your plate?” State Street senior managing director Chip Lowry said on Sept. 25 in Chicago. “My guess is some banks will exit the business.”

Price ‘Distortions’

State Street spokeswoman Lucy Davidson didn’t immediately return a message left on her phone.

The FSB plan was welcomed by associations representing banks and traders as a step forward in combating manipulation of key rates.

"Lengthening the time frame in which to fix the benchmark rate would limit opportunities for manipulation and make it far less likely that large volumes of business would create distortions in market price," the ACI, a foreign-exchange industry group, said in an e-mailed statement.

The FSB is led by Mark Carney, governor of the Bank of England, and consists of regulators and central bankers from around the world that seek to standardize global financial rules.

Loss-Absorbing Buffer

The board, which reports to the G-20, set up a task force last year to try to repair or replace tarnished benchmarks in the wake of attempts to manipulate the London interbank offered rate, or Libor. It said in February that it would extend this work into currency-market benchmarks.

A longer window would "foster more confidence that the benchmark is a truer reflection of the actual supply and demand for the currency at that point," said Richard Reid, a research fellow for finance and regulation at the University of Dundee in Scotland.

The FSB is seeking agreement on a range of policies before G-20 leaders meet in Australia in November, at the heart of which is a package of measures aimed at ending implicit government support to large financial firms. This includes requiring banks to hold an additional loss-absorbing buffer that can be quickly written down in a crisis and amending derivatives contracts to allow regulators to suspend them in a crisis.

WM/Reuters rates are published hourly for 160 currencies and half-hourly for the 21 most-traded. The benchmarks are based on trades in a minute-long period starting 30 seconds before the beginning of each half-hour. The most widely used is the 4 p.m. London fix.

WM Co. said in an e-mailed statement that it "fully supports" the FSB proposals.

Bloomberg LP competes with Thomson Reuters in providing news and information, as well as currency-trading systems and pricing data. Bloomberg LP also distributes the WM/Reuters rates on Bloomberg terminals.

Regulator Backs Foreign-Exchange Revamp to Deter Rigging
Washington Post
30 September 2014

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Industry Supports FSB's Proposals for Fixing the Fix…
Profit & Loss
2 October 2014

The Financial Stability Board released its final report on foreign exchange benchmarks on Tuesday (30 September), which is aimed at repairing the reputation of an industry struggling with accusations of collusion around the FX rate benchmarks.

The FSB's recommendations for market reform, which includes suggestions garnered during an industry consultation, focus on five areas: the calculation methodology of the WM/Reuters 4pm London benchmark rates; recommendations from an International Organisation of Securities Commissions (IOSCO) review of the WM fixes; the publication of reference rates by central banks; market infrastructure in relation to the execution of fix trades; and the behaviour of market participants around the time of the major FX benchmarks (primarily the 4pm fix).

The FSB's main recommendation is to widen the fixing window beyond the current 60 seconds. The report notes that market feedback suggests widening the calculation window to five minutes for the major currencies, but the FSB recommends that, "WM should determine the appropriate width in consultation with market participants". For less liquid currencies, the board proposes that the window should be wider than for the major currencies.

The FSB also advises that WM should incorporate price feeds and transactions data from "a broader range of sources" to increase its coverage of the FX market during the fixing window.

It supports the development of industry-led initiatives to create independent netting and execution facilities for transacting fix orders, such as a central utility.

In addition, the report encourages banks to tighten up their internal guidelines and procedures for collecting and executing fixing orders, highlighting the importance of implementing codes of conduct that explicitly detail what level of information sharing between market-makers is or is not allowed.

Importantly, it recommends that fixing transactions should be priced in a manner that is "transparent and is consistent with the risk borne in accepting such transactions", but doesn't designate whether that should be done through a bid-offer spread or a fee structure.

Lastly, it recommends that asset managers, including those passively tracking an index, should conduct "appropriate due diligence" around their FX execution and be able to demonstrate that to their own clients if requested.

In general, the industry has welcomed the FSB's recommendations. Both the Foreign Exchange Professionals Association (FXPA), a newly launched trade body that represents a full array of participants in the FX markets, and the GFMA welcome the FSB final report.

"The report outlines numerous areas that all participants in this industry should focus on and acknowledges there may be challenges and costs associated with the changes. However, bringing transparency and increasing confidence in the FX market is critical and many of these recommendations will be embraced by market participants," says the FXPA in a statement.

ACI – The Financial Markets Association also supports the release, which it believes is a "positive step for the industry" that will provide greater clarity for markets, investors and global policymakers.

Marshall Bailey, president, ACI, says: "The importance and value of these recommendations cannot be understated and is a positive step towards improving the reputation of the FX industry and creating a fairer and more efficient market."

He stresses the need for global coordination in reforming the market to ensure that regulatory and ethical arbitrage doesn't occur. "A code of conduct that applies across all regions should also be introduced if they are to have a real and lasting impact," he adds.

ACI says it agrees with the recommendation of widening the fixing window to five minutes, which it proposed in its response to the consultative paper. "Lengthening the timeframe in which to fix the benchmark rate would limit opportunities for manipulation and make it far less likely that large volumes of business would create distortions in market price," says Bailey.

Similarly, the Investment Management Association (IMA), which represents the UK investment management industry, believes that the recommendations will contribute to reviving investors' confidence in the administration of benchmarks.

"We note the focus on a variety of factors and players in both reports – they consider not just administrators but indices that 'embed' FX rates, investment fund mandates and of course trading activity. With rigorous policing by supervisors, they will be a step towards restoring confidence in FX benchmarks," says Richard Metcalfe, IMA director of regulatory affairs.

Responding to the specific recommendation regarding the WM approach, the WM Company replies: "We will continue to evaluate our methodology to align, where appropriate, with the FSB final recommendations as outlined in their report. In keeping with our policies, any proposed methodology enhancements will be subject to our internal review and governance process after which we will seek feedback from clients on the proposed changes."

Although broadly welcoming the FSB's proposals as a "great first step", Jim Cochrane, director, transaction cost analysis (TCA) for FX product manager at Investment Technology Group (ITG), doesn't think that they will solve the issues surrounding the Fix. "It is an antiquated methodology, which is criticised in the report itself. There needs to be a full overhaul of the benchmark itself so that everyone trusts it – and the methodology has to be carefully considered and open to everyone," he suggests.

Like Metcalfe, he believes that greater oversight of the industry is needed in order to enforce good behaviour. "The report notes that the governance is informal and insufficiently tailored to the benchmark determination business. If there is no formal oversight, then there is no way to hinder or hamper illegal activity in the future," he explains. "The calculation is important, but oversight is equally important as it will promote good behaviour."

Simon Wilson-Taylor, president and CEO of Molten Markets, agrees that these recommendations won't completely solve the issues, but argues that the document as a whole is significant in that it "shifts the balance sufficiently to take the heat out of the London 4pm Fix, which is what we all wanted to achieve in the first place".

"Additionally in the report, the FSB acknowledges that there is a cost to providing this service and that cost needs to be recognised. They don't prescribe exactly how that should be done, i.e. through a spread or fee, but are sending a message to the buy side that they need to understand how this service is being paid for," he adds.

Michael Sparkes, director, analytical products and research at ITG, believes that many of the proposals are consistent with an orderly and efficient market – i.e. no collusion or sharing of information inappropriately – and should be supported by everyone. In addition, he highlights recommendation 15, which relates to asset managers' due diligence and their ability to demonstrate best execution.

"That is very much a work in progress, and where TCA comes into the picture," he says. "It's not just looking at the specific trading landscape at the point of the trade and whether it was the right price at that point in time, but whether it was the right point in time in the first place. It is about standing back and looking at the bigger picture of trading in the FX market, as well as the specifics around the 4pm Fix. That is quite important and it is good that they included it in debate."

Wilson-Taylor, like Sparkes, emphasises recommendation 15. "The most important conclusion was at the end when they talked about the obligation of the fund manager. Fund managers have always known this but pushed it to one side. The thought leaders are appreciating the need to analyse the quality of execution to determine if they are honouring their fiduciary duty."

He reports seeing a change in fund managers' behaviour. "When the story first blew up, they moved away from the 4pm Fix but still a WM rate. Many have argued for some time that the association with the WM is too difficult to explain to their clients, the asset owners, so they want to change the process – such as moving to a self-constructed TWAP through the trading peak in London."

Lastly, Sparkes points out that while the FSB is an important voice within the industry, it is one step removed from effecting change. "Actions will have to be taken by other parties, either by the industry itself through industry-led initiatives, or by regulators or law makers at different levels, nationally, regionally and globally," he says.

FSB Said to Back Five-Minute WMR Fixing Window
Profit & Loss
28 September 2014

The proposal for widening the WM/Reuters 4pm London fixing window to five minutes has been broadly accepted at the Financial Stability Board (FSB) plenary meeting in Cairns, according to industry sources.

The FSB's proposal to extend the fixing window beyond the current 60 seconds was one of 15 recommendations aimed at reforming market practices around the use of FX benchmarks (Squawkbox, 17 July). The FSB is expected to publish a final report on all the recommendations within days.

The regulator embarked on a month-long industry consultation period, which ended 12 August, and received 36 responses in total from asset managers, banks and industry associations. Over half (57%) of those that responded to this particular recommendation were in favour of such a move, while 29% were not convinced and 14% were against it. Of those that supported a wider fixing window, almost half (47%) specified a five-minute timeframe, while 27% proposed a length between 10 to 30 minutes.

ACI – the Financial Markets Association, along with PGGM Investments, National Australia Bank and the Japanese Bankers Association, specifically proposed extending the fixing window to five minutes. David Woolcock, vice chairman of the ACI Forex Committee (ACIFXC), says, "From our point of view, we felt that a widening of the fixing window, in addition to increasing the number of sources putting prices in, makes it less likely that a large volume of business would create market price distortions."

He adds: "But I don't think that the problem is the methodology of the Fix – it is the behaviour of traders before the Fix."

Many experts, including those that endorsed a wider fixing window, advocate the need for other market reforms in order to address allegations that traders colluded and used client information improperly to influence pricing, which have plagued the FX industry for over a year and resulted in more than 30 senior FX traders being suspended or fired.

Andrew Woolmer, managing director, New Change FX, believes that the length of the fixing window is a minor question, arguing that focusing on such a adjustment is like "fiddling around the edges as Rome burns".

“This is an incredible misreading of the problem – almost an irrelevance,” he says. “It doesn’t address the whole problem with 4pm Fix, which is that the price is badly skewed away from the longer run average prices of the day and acts against the interest of the majority of the users of the Fix.”

The FSB plenary in Cairns also reportedly approved proposals that banks segregate orders for the fixings from trading desks, which some banking sources believe has created the greatest controversy.

A Reuters’ source reported that the FSB “decided that the fixing flows will be separated from other flow business through a system of Chinese walls”, which could include traders physically sitting on a different floor.

“Obviously that will be very difficult for a small bank,” Woolcock says. “I think a better way forward is to have a higher standard of confidentiality. This means that all information regarding the Fix is considered highly confidential and any passing of that information, whether internally or externally, should be regarded as a breach of best practice and subject to the strong sanctions we have seen announced by HM Treasury in the UK and by the European Commission. I personally would welcome that.”

The FSB is to publish its report by end-September and will present it to a G20 summit in Brisbane in November.

FSB Unveils FX Benchmark Recommendations
Waters Technology
By James Rundle
1 October 2014

The Financial Stability Board (FSB) has released its final report into foreign-exchange (FX) benchmarks, where it lists a number of recommendations related to the calculation of the "fix" and trading conduct.

The FSB is an international body comprising the European Commission, Group-of-20 (G20) nations and members of its predecessor, the Financial Stability Forum (FSF), chaired by Mark Carney, governor of the Bank of England. The report analyzes the calculation methodology of benchmarks such as the London 4 p.m. fix, along with increased trading activity around the fix and how this affects market stability, as well as how potentially abusive trading can occur.

Included among its 15 primary recommendations are suggestions for widening the window in which the fix is calculated. Currently, trades that take place 30 seconds on either side are used, but the report suggests that this could be widened to five minutes, centered on 4 p.m., for the most active currency pairs, and longer for less active ones, although it shied away from recommending a definitive time period. It also wants WM and Reuters, which calculate the fix, to include a wider range of data, provided this satisfies legitimacy and quality concerns.

"The FSB document is a good blueprint for developments in the FX market, and many of the recommendations reflect the way that any efficient market should work," says Jim Cochrane, director of transaction-cost analysis for FX at agency broker ITG. "The specific proposals on the 4 p.m. fix are welcome in that they will increase transparency in an antiquated system."

Codes of Conduct

Furthermore, the report suggests that internal procedures designed to avoid conflicts of interest inside firms should be strengthened, particularly at dealer banks, while asset managers should also be able to demonstrate to their clients that they have undertaken proper due dilligence around their FX executions. A code of behavior, already suggested by various FX-related trade bodies, should also be implemented. Other suggestions include limiting the sharing of information between participants to what is strictly necessary for trade execution.

"Ideally, there would be no confusion about what can and can't be shared, but in reality, ambiguity remains, as there isn't a clear and consistent definition of private information. This is absolutely critical and must be addressed by regulators and adopted across all financial markets," says Marshall Bailey, president of trade body ACI. "A singular definition used across the industry will provide much needed clarity and transparency, and leave no room for confusion. Regulators should consider employing the more conclusive term of confidential information, which is clearly defined in the ACI Model Code."

Regulators and law enforcement bodies around the world are investigating allegations of criminal behavior regarding manipulation of the fix. While the report makes direct reference to these, it stresses that it has not seen the evidence being considered by those investigations, and is wholly independent to them.

The full FSB report can be found here. The FX benchmark group is co-chaired by Guy Debelle, assistant governor, financial markets, at the Reserve Bank of Australia, and Paul Fisher, deputy head of the Prudential Regulation Authority, at the Bank of England.

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FOREX MAGNATES A News Source for The Industry

FSB Releases Final Report on FX Benchmarks, WMR Poised to Change?
Forex Magnates
By Jeff Patterson
30 September 2014

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The Financial Stability Board (FSB) has released the final and latest version of its report dealing with FX benchmarks, along with supplemented recommendations for notable measures for reform for FX markets.

The FSB is a multinational entity designed to observe and help facilitate proper transparency and compliance measures for market participants across 24 countries. The most recent FSB report comes on the heels of an earlier report published back in July, which received widespread interest.

More specifically, the report deals with the WM/Reuters (WMR) 4pm London fix produced by the WM Company and its inherent effect on the FX market. This construct has been the source of unwavering attention, given the allegations of manipulation presently convulsing the institutional FX industry.

These Recommendations Include:

1. The calculation methodology of the WMR benchmark rates
2. Recommendations from a review by the International Organization of Securities Commissions (IOSCO) of the WM fixes
3. The publication of reference rates by central banks
4. Market infrastructure in relation to the execution of fix trades
5. The behavior of market participants around the time of the major FX benchmarks (primarily the WMR 4pm London fix)

According to Marshall Bailey, President of ACI, Financial Markets Association, in a recent comment on the recommendations outlined by the FSB, “The ACI welcomes the guidance outlined in today’s report from the Financial Stability Board. It is a positive step for the industry and will provide clarity for markets, investors and global policymakers. The importance and value of these recommendations cannot be understated and is a positive step towards improving the reputation of the FX industry and creating a fairer and more efficient market.”

Moreover, adding, "We are pleased the FSB's recommendations are closely in line with many of the ACI's responses to the consultative document, including the widening of the fix window to five minutes. As the ACI has long maintained, it is not the fix that is broken, but rather the manner in which a few individuals use it."

"Restoring faith in the industry and stamping out practices which undermine the effectiveness of the financial markets is a key priority, and the need for consistent education on what is and isn't acceptable behavior is paramount. The formal adoption of an international set of standards for ethical conduct and behavior across the global financial industry will provide clarity and guidance on what is expected of all market professionals, from day traders to senior executives," Bailey added.

Prior Allegations Provide Framework for Recommendations

As a result of illicit manipulation allegations of FX rates, the FSB Plenary formed a working group to help moderate, focus on, and ultimately serve as a watchdog for FX benchmarks. Officially, the mandate of the group was to undergo analysis of the FX market structure and incentives that may yield particular types of trading activity around the benchmark fixings.

The paramount goal of these measures, as stipulated by the FSB, is the aim of delivering a marked improvement in market structure and overall conduct by its participants. However, this also underscores the need for additional regulatory changes to help ensure the administering of appropriate actions and behaviors.

Ultimately, "The 4pm benchmark broadly works well but although but it certainly needs some repair, which the FSB has addressed, a replacement is not needed. There are already multiple benchmarks available that have not been deployed by the market and are yet to be proven effective. The 24-hour nature of FX reduces the effectiveness of benchmarks such as VWAP and TWAP, and deployment would be extremely costly and require significant changes in legal documents, client contracts and performance measurement agreements," reiterated Bailey.

Final report from FSB on FX Benchmarks and commentary from FMA president
Automated Trader
30 September 2014

The FSB has released the final version of its report on foreign exchange (FX) rate benchmarks. This report has been prepared in light of discussions with a range of FX market participants, along with submissions received in response to an interim report published in July 2014 for wider public consultation.

The report sets out a number of recommendations for reform in the FX markets and in the benchmark rates that have been identified as pre-eminent by market participants - in particular, the WM/Reuters (WMR) 4pm London fix produced by the WM Company. These recommendations fall into the following broad categories:

- the calculation methodology of the WMR benchmark rates;
- recommendations from a review by the International Organization of Securities Commissions (IOSCO) of the WM fixes - this review is included in the report published today, and is also being published separately by IOSCO;
- the publication of reference rates by central banks;
- market infrastructure in relation to the execution of fix trades; and
- the behaviour of market participants around the time of the major FX benchmarks (primarily the WMR 4pm London fix).

The work of the FSB in this area was initiated in response to concerns raised in 2013 about the integrity of FX benchmarks. These concerns stemmed particularly from the incentives for potential market malpractice linked to the structure of trading around the benchmark fixings. As a result, the FSB Plenary formed a working group to focus on FX benchmarks. The mandate of the group was to undertake analysis of the FX market structure and incentives that may promote particular types of trading activity around the benchmark fixings. The group was tasked to propose possible remedies to address these adverse incentives as well as to examine whether there is a need and scope to improve the construction of the benchmarks themselves.

Based on discussions with the relevant market sectors, the FSB believes that all the recommendations above can and will be accepted and implemented by the market groups concerned. This should deliver a substantial improvement in market structure and conduct. But investigations into alleged misconduct are ongoing across a range of markets, and it is possible that the authorities will ultimately conclude that regulatory change is needed to promote or ensure appropriate behaviours and/or to implement the recommendations of this report.

Marshall Bailey, President, ACI - The Financial Markets Association commented:

The ACI welcomes the guidance outlined in today's report from the Financial Stability Board. It is a positive step for the industry and will provide clarity for markets, investors and global policymakers. The importance and value of these recommendations cannot be understated and is a positive step towards improving the reputation of the FX industry and creating a fairer and more efficient market.

Global coordination is absolutely imperative if we are to succeed in reforming the market without creating unintended consequences such as regulatory and ethical arbitrage. A code of conduct that applies across all regions should also be introduced if they are to have a real and lasting impact.

We are pleased the FSB's recommendations are closely in line with many the ACI's responses to the consultative document, including the widening of the fix window to five minutes. As the ACI has long maintained, it is not the fix that is broken, but rather the manner in which a few individuals use it.

Restoring faith in the industry and stamping out practices which undermine the effectiveness of the financial markets is a key priority, and the need for consistent education on what is and isn't acceptable behaviour is paramount. The formal adoption of an international set of standards for ethical conduct and behaviour across the global financial industry will provide clarity and guidance on what is expected of all market professionals, from day traders to senior executives.

The FSB's proposal on widening the fixing window

The ACI agrees in full with the recommendation of widening the fixing window to five minutes. Lengthening the time frame in which to fix the benchmark rate would limit opportunities for manipulation and make it far less likely that large volumes of business would create distortions in market price.

The FSB's proposal on the sharing of information

Ideally, there would be no confusion about what can and cant be shared, but in reality ambiguity remains, as there isn't a clear and consistent definition of "private information". This is absolutely critical and must be addressed by regulators and adopted across all financial markets. A singular definition used across the industry will provide much needed clarity and transparency, and leave no room for confusion.

Regulators should consider employing the more conclusive term, "confidential information" which is clearly defined in the ACI Model Code.

The FSB's proposal on a central utility for trade matching

A central utility is not a panacea, and regulators seem to understand that. It is just one idea that has rightly been consulted upon and there are commercial solutions being developed quite rapidly in the market that are similar to what the FSB has proposed.

The ACI recognises the value of specific utilities for their specific purposes, but concentration in a single global point for trade matching would pose a significant risk for the market in the event of failure. It could result in unnecessary risk and potentially create more problems than it solves.

CLS is an example of how the market can respond to these kinds of challenges. It was designed to mitigate settlement risk in FX transactions and was backed by regulators and trading institutions alike. Now it is seen as a vital part of FX infrastructure, and demonstrates what the industry and regulators can achieve by working together and coordinating their efforts globally. We would like to see any new central clearing platforms evolve in a similar fashion and the market remain free to decide which solution to use for itself.

The FSB's proposal on an alternative benchmark calculation

The 4pm benchmark broadly works well but although but it certainly needs some repair, which the FSB has addressed, a replacement is not needed. There are already multiple benchmarks available that have not been deployed by the market and are yet to be proven effective.

The 24-hour nature of FX reduces the effectiveness of benchmarks such as VWAP and TWAP, and deployment would be extremely costly and require significant changes in legal documents, client contracts and performance measurement agreements.

The FSB's proposals on codes of conduct

The ACI gladly welcomes this recommendation. Formally adopting a code of conduct such as the ACI's Model Code on a global scale will provide much needed clarity and consistency on ethical behaviour and best practice. Implementing an internationally applicable code of conduct will provide a solution to a number of key issues affecting the industry and underpin the internal procedures set by institutions.

The FSB's proposal on fixing transaction fees

A key advantage of using an agency model is that the costs and risks taken onboard by the price-maker are clear. However, it must be considered that the fees may not accurately reflect the risks taken onboard by the sell-side and therefore the use of this model may distort pricing.

Additionally, it must be ensured that an agency model is kept entirely separate from any principal activity.

At present, the buy-side already has a choice between agency and principal pricing. There are concerns that documenting this option could potentially have unintended consequences.

The buy-side should continue to have options and will likely adopt a model that allows agency and principal pricing.

Financial Stability Board guidance is positive step
Institutional Asset Manager
30 September 2014

Marshall Bailey, President, ACI – The Financial Markets Association – welcomes the Financial Stability Board's latest guidance…

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Forex markets face further regulations
Euro2day
30 September 2014

Participants in foreign exchange markets have been warned they may face further regulatory change even after implementing a long-awaited series of recommendations aimed at removing the taint affecting the sector.

A task force set up by the Financial Stability Board on Tuesday set forth 15 reforms aimed at overhauling the $5tn currency markets following allegations surrounding the crucial 4pm forex fixing.

The report from the global umbrella group said it expected the industry to accept all of the ideas, which include tougher rules aimed at minimising conflicts of interest within banks and a well-flagged widening of the window of time during which the key forex benchmark is calculated.

But the report cautioned that further change could still follow down the line – with Britain already consulting on including the 4pm fix in a list of benchmarks that are policed by regulators.

“Investigations into alleged misconduct are ongoing across a range of markets, and it is possible that the authorities will ultimately conclude that regulatory change is needed to promote or ensure appropriate behaviours and/or to implement the recommendations of this report,” the report said.

The FSB started to scrutinise the London-dominated global forex market in February after a sprawling investigation by regulators and prosecutors into benchmark-rigging allegations piled on pressure to reform a largely unregulated industry.

Its proposals suggest that the key window during which the 4pm fix is calculated be extended from the current period of one minute to make it less prone to manipulation, with industry feedback pointing to a five-minute window.

However regulators shelved a previous suggestion that would have created a global “utility” to match fixing orders placed by market participants, saying it wanted to allow industry-led initiatives to move ahead.

The FSB report said that banks need to implement tough procedures separating the wok of handling fixing orders from other business, reducing the potential for manipulation to occur.

"Firms should establish distinct and separate processes for managing fixing flows as part of their effort to ensure that customer and flow information is appropriately protected," the FSB said.

It noted that such changes were "not costless" and could reduce banks' capacity to absorb the risk from transactions, but it insisted this did not overshadow the benefits of reform.

The FSB also called for codes of conduct governing the sector to be much clearer about what information can be shared between market-makers.

Marshall Bailey, President of the ACI, an industry group, said: "The formal adoption of an international set of standards for ethical conduct and behaviour across the global financial industry will provide clarity and guidance on what is expected of all market professionals, from day traders to senior executives."

James Kemp, Managing Director of the FX division of the Global Financial Markets Association said: "There may well be challenges and costs in implementing the changes, but enhancing confidence in the market is crucial and the industry will adapt to embrace these recommendations."

# News On Invest

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News on Invest
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Regulator Backs Foreign-Exchange Revamp to Deter Rigging
Global Association of Risk Professionals
30 September 2014

A panel of global regulators, responding to a manipulation scandal that's shaken the financial industry, backed measures to make it harder for traders to exploit key benchmarks in the $5.3 trillion-a-day currency market.

The Financial Stability Board said it supports extending the width of the trading window used to calculate foreign-exchange rates to five minutes in a rule overhaul that also includes measures to address potential conflicts of interest between banks and their clients.

"The incentive to manipulate is always going to be there: what we have to make sure is the ability to actually do it is reduced," Rosa Abrantes-Metz, a professor at New York University's Stern School of Business, said in a telephone interview. The FSB report "talks about many things, such as no sharing of information among traders beyond what is necessary, but that should have been in place for a long time."

At least a dozen regulators on three continents are investigating whether traders in the world's largest financial market colluded with counterparts at other firms to manipulate benchmarks used by money managers and pension funds to determine what they pay for foreign currency. More than 25 traders have been fired or suspended across the industry.

4 p.m. Fix

The FSB, which brings together regulators, central bankers and government officials from the Group of 20 nations, proposed changing how the most popular benchmarks from WM/Reuters are calculated, including extending the one-minute windows in which rates including the key 4 p.m. London fix are set.

"Changes have to be made and FX more broadly may need to be brought within regulation," Sharon Bowles, a former head of the European Parliament committee dealing with financial regulation, said by e-mail. "The issue of not just culture but an absence of ethics has to be tackled. Too much has been accepted as normal even by some professional investors."

Widening to five minutes, in line with the median response in a public consultation, "strikes a balance between reducing incentives for manipulation while at the same time still ensuring the fix is fit for purpose by generating a replicable market price," the Basel, Switzerland-based FSB said in a report today.

‘Appropriate Width’

The FSB backed away from setting the industry standard window itself, recommending “the appropriate width of the window should be determined, and regularly reviewed, by WM in consultation with market participants.”

“The size of the window should not be fixed for all time nor, ideally, dictated by the authorities,” the group said.

Other recommendations from the FSB include more detailed codes of conduct for currency trading, and that “index providers should review whether the foreign-exchange fixes used in their calculation of indexes are fit for purpose.”

The FSB recommended that “banks (and other FX dealing intermediaries) establish and enforce their internal guidelines and procedures for collecting and executing fixing orders including separate processes for handling such orders.” Firms should “establish distinct and separate processes for managing fixing flows,” the group said.

Due Diligence

Asset managers “should conduct appropriate due diligence around their foreign-exchange execution and be able to demonstrate that to their own clients if requested,” according to the FSB.

“Investors need confidence in the administration of benchmarks, so we welcome the FSB’s recommendations” and a previous report from the International Organization of Securities Commissions, Richard Metcalfe, director of regulatory affairs at the Investment Management Association, said by e-mail.

“We note the focus on a variety of factors and players in both reports,” Metcalfe said. “They consider not just administrators but indices that embed FX rates, investment fund mandates and of course trading activity. With rigorous policing by supervisors, they will be a step towards restoring confidence in FX benchmarks,” Metcalfe said.

Tightening the rules for currency benchmarks would spur some banks to close down their foreign-exchange arms, according to State Street Corp.

“Is it worth setting up all these extra controls, hiring additional people, setting up a separate space, or do you want to just get this off your plate?” State Street senior managing director Chip Lowry said on Sept. 25 in Chicago. “My guess is some banks will exit the business.”

Price ‘Distortions’

State Street spokeswoman Lucy Davidson didn’t immediately return a message left on her phone.

The FSB plan was welcomed by associations representing banks and traders as a step forward in combating manipulation of key rates.

"Lengthening the time frame in which to fix the benchmark rate would limit opportunities for manipulation and make it far less likely that large volumes of business would create distortions in market price," the ACI, a foreign-exchange industry group, said in an e-mailed statement.

The FSB is led by Mark Carney, governor of the Bank of England, and consists of regulators and central bankers from around the world that seek to standardize global financial rules.

Loss-Absorbing Buffer

The board, which reports to the G-20, set up a task force last year to try to repair or replace tarnished benchmarks in the wake of attempts to manipulate the London interbank offered rate, or Libor. It said in February that it would extend this work into currency-market benchmarks.

A longer window would "foster more confidence that the benchmark is a truer reflection of the actual supply and demand for the currency at that point," said Richard Reid, a research fellow for finance and regulation at the University of Dundee in Scotland.

The FSB is seeking agreement on a range of policies before G-20 leaders meet in Australia in November, at the heart of which is a package of measures aimed at ending implicit government support to large financial firms. This includes requiring banks to hold an additional loss-absorbing buffer that can be quickly written down in a crisis and amending derivatives contracts to allow regulators to suspend them in a crisis.

WM/Reuters rates are published hourly for 160 currencies and half-hourly for the 21 most-traded. The benchmarks are based on trades in a minute-long period starting 30 seconds before the beginning of each half-hour. The most widely used is the 4 p.m. London fix.

WM Co. said in an e-mailed statement that it "fully supports" the FSB proposals.

Bloomberg LP competes with Thomson Reuters in providing news and information, as well as currency-trading systems and pricing data. Bloomberg LP also distributes the WM/Reuters rates on Bloomberg terminals.