GFXC - PUBLIC REQUEST FOR FEEDBACK (MAY 2021)

SUBMISSIONS *(As of 1 June)*

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Background

We are committed to the principles and good practice outlined in the FX Global Code. In response to the Global Foreign Exchange committee (GFXC)'s April 2021 request for industry feedback on proposals arising from its 3-year review of the FX Global Code, we offer comments related to 'pre-hedging' and 'last look,' as those terms are used in the Code. We urge the drafters of the Code to carefully consider these comments, which address significant concerns we have with the current guidance around pre-hedging and last look.

Our comments are provided on the basis that these comments will not be attributed to us by name, if published.

Pre-Hedging

Pre-Hedging comments:

1. Mirroring the FICC Markets Standards Board Standard for the execution of Large Trades in FICC Markets (FMSB Large Trades Standard), we propose adding a footnote to clarify the benefit clients receive from pre-hedging. FMSB Large Trades Standard footnote 7 states "Examples of where pre-hedging is considered to be designed to benefit the client include, but are not limited to, where a pre-hedging strategy is designed with a view to: (i) facilitating client transactions; (ii) ensuring the effective provision of liquidity to fulfil client transactions; and/or (iii) improving the quality of execution of associated client transactions. This principle does not require the direct pass-through of any financial benefits derived from pre-hedging by the dealer to the client."

2. We propose removal of the statement "pre-hedging should be more of an exception than the norm" given that, based upon publically available disclosures of liquidity providers, it is clear that full discretion is retained by the liquidity provider to engage in trading, market making and risk management activities, including pre-hedging and hedging, at their own discretion.

In addition to the two key comments above, we offer additional comments designed to bring additional clarity to the Code's treatment of pre-hedging and, in so doing, achieve appropriate consistency with the FMSB Large Trades Standard.

1. We note that principle 11 of the Code defines pre-hedging as "the management of the risk associated with one or more anticipated Client orders", however in our opinion it would be beneficial for the guidance paper to clarify that "orders" in this context should be interpreted to mean "trades". The draft suggests a "voice one-way request for quote (RFQ)" is the best illustration of an anticipated order, but we would contend that under the commonly accepted meaning FX participants would see an RFQ as a distinct concept to an order. Thus we suggest the guidance seeks to align with the FMSB Large Trades Standard which defines pre-hedging as "the pre-hedging is the management of the risk associated with one or more anticipated client trades".

2. We propose removal or clarification of the statement “However, the liquidity provider anticipates in good faith (that is, has reasonable expectations) that the liquidity consumer will accept the quote in which case it will become a confirmed transaction” as we are unclear of the scenarios in which it would be unreasonable for a liquidity provider to expect that a quote could result in a confirmed transaction. Indeed, if a liquidity consumer was requesting a quote without such an intention for it to result in a confirmed transaction it may need to be considered whether they could be committing an offence under market abuse legislation.

3. In the sentence “Larger FX orders also have heightened conduct and market risk, and therefore should be handled with particular care and attention, and within the overall guidance of the Code, in order to minimize their market impact and achieve best execution for the client”, we suggest the reference to “achieve best execution for the client” is replaced by a statement such as “achieve an appropriate outcome for the client”. The purpose being to avoid confusion about the scope and applicability of regulatory obligations surrounding best execution in FX markets.

4. We note the statement “In general, when conditions potentially warrant pre-hedging, liquidity providers should strive, at the time of the request, to communicate the potential implication of the order on market liquidity and price” and suggest that this is updated to mirror relevant language in the FMSB Large Trades Standard, specifically “Pre-hedging should only be undertaken where the client has been made aware in advance that pre-hedging may take place and could have an impact on the market price of the instrument. The dealer should consider, taking into account factors such as the expertise of the client, the nature of the client relationship and frequency with which the client enters into comparable transactions, whether it is necessary to make such disclosure on a trade-by-trade or other basis.” We make this suggestion both for consistency purposes and to be clear that the intention of the guidance paper is not to mandate per trade pre-hedging disclosure.

5. We suggest the word “compliance” is removed from the statement “Limit orders should also receive heightened compliance monitoring” in order to reflect that such monitoring may take place within the first line of defense or second line or both depending upon how liquidity providers have elected to structure themselves in terms of the operation of monitoring controls.

<u>Last Look Comments:</u>

We employ last-look symmetrically, and are vocal supporters of this approach across the industry.

Separately, and with regards to drafting specifically, we would suggest the following amendments and clarifications to the ‘last look’ draft guidance paper:

1. The use of the term “current price” (vs quoted price) is not clear. We suggest that rather than “current price” – it would be preferable to refer to the “price at the end of the hold period / last look window”. Whereas the driver for Last Look should be to determine whether a quoted price in respect of which a trade request is received remains “current” (ie within the LP’s price

tolerance for execution), it is important to specify the point in time at which the assessment is made; otherwise the term “current” is confusing.

2. Recommendation 2 (ex ante disclosures): this includes a recommendation that “LPs should disclose information about the expected length of the last look window”. Given that the length of the hold time applied for Last Look purposes is informed by various factors (latency, counterparty trading behavior etc), we would query whether communication of the “expected length” of the last look window is feasible. We propose that Last Look hold time may be disclosed to counterparties upon request.

Last Look

1 - We wonder if Figures 2 and 3 should be adjusted to reflect the firmness of quotes (or not) and the communication/messaging flows of the trades. This could we believe be easily be accomplished by noting in Figure 2 that dealers do NOT receive a request to trade which may be reviewed, while the converse would be true in Figure 3.

2 – On Page 5, the paper states: "*In a non-central matching model, the LP exposes itself to the risk of receiving requests to trade from many LCs simultaneously, or can be subject to requests that are received significantly later than the time of the quote. LPs manage risks such as this through the validity and price check processes."*

- **We note that the paper indicates that requests can be made "significantly later" than the time of quote. Given that market LPs are exposed to latency risk based in milliseconds we fear that violent and quick price movements post quote (and price movements during/after the trade request by LC) are potentially being overlooked.**

6- Page 8 – The paper state "*To help LCs access this information and allow for greater comparability across LPs, the GFXC has produced a Disclosures Cover Sheet for LPs that includes the following fields that are relevant to last look practices*."

- **We wonder if the proposed approach with respect to the Cover Sheet will differ from that suggested at the March 2021 GIFXC Meeting? Notably, guidance as to how the CS should be employed vis a vis other LP disclosures would be appreciated.**

7 – On Page 8 – it states "*LPs should disclose information about the expected length of the last look window to their LCs."*

- **LPs should be provided the option of course to let individual counterparties know the length of their window outside of the written disclosure (ie upon counterparty request).**

Pre Hedge

1 - Page 3 – The paper suggests that LPs should only hedge "*orders that are large relative to the available liquidity in the market at the time of the order and that could have a significant market impact*".

- **We would suggest that this example should be non-exclusive and that there are other circumstances where pre-hedging is indeed appropriate.**

2 - Page 5 – The paper provides 3 advantages of pre-hedging (building inventory, lower hedging costs, ability to test liquidity).

- **We believe this language should be more inclusive, for example: "among other benefits, 3 examples are:…".**
- **One additional benefit that comes to mind is reduced market impact / disruption, which goes hand in hand with the hedging cost point though with a different angle — not explicitly to benefit the client, but to fulfill a dealer's duty as a professional market participant.**

3 – Pages 5/6 state: "The intent of any pre-hedging by the liquidity provider should always be to benefit the liquidity consumer and help facilitate the transaction … Intent is a difficult concept to demonstrate. It exists in the mind of a liquidity provider….Despite an intent by the liquidity provider to provide a benefit to the liquidity consumer and to limit the market impact of a trade, pre-hedging may result in an adverse outcome for ...

- **Rather than describe the scenario in generalized terms, consider instead replacing these sections with more concrete language, such as:**

- **"Factors to consider for the Liquidity Provider in a decision to pre-hedge**
- **A,**
- **B,**
- **C**

- **Factors to consider for the Liquidity Consumer in a decision to pre-hedge**
  - **A**
  - **B**
  - **C"**

4 - Page 5 – in relation to client communications, the draft states that that "*In general, when conditions potentially warrant pre-hedging, liquidity providers should strive, at the time of the request, to communicate the potential implication of the order on market liquidity and price. In addition, and depending on the client relationship and the perceived urgency of the trade, liquidity providers should also strive to outline alternative options for executing the trade to limit its market impact. The frequency and extent of any such discussions may also depend on the sophistication of the liquidity consumer and the perceived size of the market impact of the trade*."

- **Given that disclosures may not be required or appropriate in all circumstances, we suggest qualifying the obligation to communicate as "when appropriate" or similar.**

5- Page 6 (End of section 5) states**: "**To assess whether pre-hedging benefits a liquidity consumer, liquidity consumers and providers should regularly review the effectiveness of the execution post-trade to see whether the expected outcome was delivered (see guidelines in Principle 9 and 36)."

- **We believe that this sentence should be removed. It would be practically accomplish this given the very many factors that determine market moves, plus it implies an ongoing monitoring. We do not believe it would benefit clients so establish such a monitoring requirement.**

Paris, 31st of May 2021

Dear members of the Global Foreign Exchange Committee,

In response to the collaboration request issued on the 11th of May 2021 by the Global Foreign Exchange Committee (GFXC) related to draft guidance papers for the usage of 'pre-hedging' with the FX Markets, ACI Financial Markets Association (ACI FMA), after a long, complex and detailed process of work and cooperation with its Committees and Working Groups, hereby presents its contributions.

We would like to point out that ACI FMA is available for any necessary clarification regarding the presented response.

We are utterly available to collaborate with the GFXC in the completion of this process. Therefore, and with that objective, please feel free to contact the ACI FMA through:

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Sincerely,
Kim and Rui

Summary of ACI FMA:

ACI Financial Markets Association (ACI FMA) is a leading global trade association representing the interests of professionals in the wholesale financial markets community. Established in 1955, ACI FMA is focused on enhancing best market practice and supporting Market Participants to adhere to principles of ethical conduct. ACI FMA is an international association with 60 National Associations worldwide representing over 8.000 members.

Please refer to Addendum 1 on page 4 for a more detailed description of ACI FMA and its core values.

Pre-Hedging

Pre-hedging is the management of risk associated with anticipated Client orders in principal-based, over-the-counter markets to facilitate effective market functioning. A Liquidity Provider (“LP”) conducting pre-hedging should act with integrity, aiming to attain risk reduction and to minimize the impact of trades that are expected to have a significant effect on market prices.

A Request-For-Quote (“RFQ”) consists of an anticipated order given that the LP has to provide a firm quote, while the decision of whether to accept the quote and execute a trade lies with the Liquidity Consumer (“LC”). Pre-hedging in the context of RFQ comprises any associated trading activity between the time that the LC requests the firm quote and accepts it (thus creating a confirmed transaction) or closes the RFQ without confirming the transaction (for example by rejecting the quote or by allowing the quote to expire). Since it is at the LC discretion to trade, the LP is exposed to potential market risk in case of rejection and if the position has been partially or fully hedged.

The intention of pre-hedging is to facilitate order execution and to reduce the potential market impact of filling an order aiming to achieve a better price outcome. Therefore, it is essential that the pre-hedging activity does not deliberately disadvantage Clients and that Market Participants have aligned their expectations for the execution. Transparency and clearly established guidelines and controls governing pre-hedging are essential to avert misconduct. Unauthorized trading practices like front-running, relying on the use of Confidential Information provided by Clients, have an adverse impact on market prices and are completely opposed to pre-hedging practices that aim to achieve best execution for Clients which effectively supports the functioning of the FX Market. It is therefore essential for any pre-hedging activity to be undertaken with the intention of achieving these goals, although LP endeavours to offer the best possible execution prices could result in potential inherent conflicts of interest that should be outlined and disclosed.

Pre-hedging facilitates transactions that could significantly impact market prices reducing the risk arising from this type of anticipated flows. However, regardless of pre-hedging, an order may have a market impact depending on the size and level of liquidity in the market at the time of execution. Therefore, it may be difficult to assess the benefit for Market Participants. Despite the intent, pre-hedging has an impact on the effectiveness of the execution that should be reviewed post-trade and should be subject to compliance monitoring.

ACI FMA firmly believes that the GFXC guidance paper should set a transparent and comprehensive framework for pre-hedging aligned with the principles of the FX Global Code.

Addendum 1: History of ACI FMA:

ACI Financial Markets Association ("ACI FMA") is a global non-political, non-profit association of wholesale financial market participants. ACI FMA was established under the French Law of 1901 based on mutual recognition of markets professionals, with the objective of developing the profession, without discrimination of any sort.

Its main mission is to be a leading, global association of wholesale financial markets professionals, contributing to market development through education, best market practices, technical advice and networking events.

Since 1955, ACI FMA has represented the interests of individuals in professional trading, broking, operations, regulatory and compliance activities in global financial markets.

Focused on three core values of Membership, Education and Ethical Conduct, ACI FMA is committed to supporting Market Participants to operate at the highest standards of ethical conduct and best market practice. Specifically, these values represent:

✓ Membership: ACI FMA counts over 8,000 individual members representing 60 National Associations globally

✓ Education: Accredited, portable qualification and certification of professional and ethical standards to Market Participants worldwide

✓ Ethical Conduct: ACI FMA members are expected to maintain the highest ethical conduct in adherence with global Codes relevant to them.

ACI FMA members are proud to represent individual responsibility and benefit from a network of global peers who place great emphasis on the best possible practices in our profession, in the same way as modern regulatory regimes and industry Codes.

Through cooperation with ACI FMA, an entity can demonstrate that concrete steps are being taken to ensure all the staff have been trained to the highest ethical standards of conduct and that they understand their individual obligation.

ACI FMA members are longstanding proponents and influencers of ethical conduct and good market practices to financial markets professionals.

ACI

FINANCIAL MARKETS ASSOCIATION EST.1955

Paris, 31st of May 2021

Dear members of the Global Foreign Exchange Committee,

In response to the collaboration request issued on the 11th of May 2021 by the Global Foreign Exchange Committee (GFXC) related to draft guidance papers for the usage of 'last look' within the FX Markets, ACI Financial Markets Association (ACI FMA), after a long, complex and detailed process of work and cooperation with its Committees and Working Groups, hereby presents its contributions.

The ACI FMA would advocate that it should be incumbent on both Liquidity Provider and Client/Liquidity Consumer to articulate and ascertain transparent and specific requirements regarding the execution of an order at the time of instruction and this should, for example in the case of 'stop-loss' orders, include language regarding the potential for/acceptance of slippage. This is to ensure that both parts are fully aware of and in agreement with how the order should be executed.

We would like to point out that ACI FMA is available for any necessary clarification regarding the presented response.

We are utterly available to collaborate with the GFXC in the completion of this process. Therefore, and with that objective, please feel free to contact the ACI FMA through:

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Last Look

The issue regarding last look in principle 17 has created a great deal of market 'noise' and interest and the expression of dissatisfaction by certain potentially self-interested Market Participants as to how the issue has been dealt with in the current FX Global Code. ACI FMA welcomes clarification and determination on the part of the Global Foreign Exchange Committee (“GFXC”) in this matter. The FX Global Code's objective is to support effective, efficient, fair and transparent markets.

The ACI FMA is supportive of and welcomes the GFXC's 3 recommendations that:

1. Ensure a fair and effective last look process through fairness and predictability in the process design;

2. Enhance ex-ante disclosures - i.e., a Liquidity Provider (“LP”) should disclose whether it employs last look and if so, it should ensure that their ex-ante disclosures provide sufficient information for a Liquidity Consumer (“LC”) to be able to understand the implications of the LP’s last look policy for their trading;

3. Information should be available to regularly evaluate the handling of trade requests that, for example, a LP should be sharing.

Specifically, we would comment that the use of last look as a risk control mechanism is intended to confirm that operational, credit and price prerequisites to trade are met. FX market-making in a highly volatile market exposes the LP to the risk of trading at a price deviating from the current market price, but it is paramount to specify the criteria applied by the Market Participants to accept or reject a request to trade against its quoted price. Since the LP has sole discretion to trade, based on validity and price check processes, the Client is exposed to potential market risk in the case of rejection. A LP should ensure the fairness and predictability of the process and the promptness of the decision should be defined using a time threshold. Last look, as it pertains to rejection of a stale quote and thus a failed match, the checking of credit, permission, risk and liquidity exposure, as well as system and message integrity, are legitimate reasons for a prospective trade to be rejected as is price latency and technical misprice. However, all other uses of last look, including the delaying of acceptance of a trade by a Market Participant in relation to price are potentially open to inappropriate behaviour and are therefore discouraged, unless adequate safeguards to detect any form of abuse against the Client or the market exist, nor should any attempt be made to take advantage of the other Market Participant’s intentions.

Therefore, ACI FMA believes that the GFXC paper should provide guidance regarding the suitable duration of the required 'checks and balances' and the information parameters of such the checks used in the process of last look by a LP. Furthermore, this should be disclosed to the LC. However, this guidance, for the definition and disclosure of last look should not be too prescriptive, as it must be proportional to the type of business and technology of the LP.

A LP can apply price checks symmetrically or asymmetrically. A symmetric check that rejects trade requests on a price that exceeds the defined tolerance level, regardless of if it is in favor of the LP, renders the last look procedure more transparent since an asymmetric price check tends evidently to lead to trades being accepted when the price moves in favour of the LP. Therefore, market-makers should preferably apply symmetric last look on a consistent basis. It is recommended that Market Participants using asymmetric last look should have available a detailed explanation as to how the practice does not disadvantage those Clients subjected to the practice and the respective measures in place to prevent a sub-optimal outcome.

The use of last look to enable a Market Participant to quote another Market Participant with the intention of mitigating any market risk to ensure an appropriately applied markup is earned, is akin to a Market Participant acting in a riskless-principal role. When deploying this type of “automated Cover and Deal" execution using last look to ensure no market risk is taken, Market Participants need to manage their relationship by determining their roles on a trade-by-trade basis when its use is selective. Usage of this mechanism exposes the recipient Market Participant to the last look practices of the ultimate provider of the liquidity and not that of the counterparty. If “automated Cover and Deal” is used in all circumstances, Market Participants should reflect this as a standing agreement in their terms of business which defines their roles and responsibilities in the riskless-principal relationship.

The inherent characteristics of the last look process should be fairness and predictability, setting a transparent framework that will minimize the risks for all Market Participants with appropriate definitions and disclosures that facilitate the evaluation of trade execution by a LC. Trade practices from a LP encompassing an unusually long or unpredictable last look window or the subsequent misuse of Confidential Information provide a clear indication of inappropriate use of last look.

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GFXC Public Request for Feedback
Pre-hedging and Last Look
ANZ Response

Pre-Hedging Paper

- The paper on Pre-Hedging contains minor changes in the body of the document compared to prior the draft. The paper remains very clear that the intent of pre-hedging should be to the benefit of the client and market functioning (even if it doesn't always eventuate that way). It also states market participants should strive to have clearly aligned expectations for the execution of, especially larger, FX orders, whether pre-hedging is applicable or not.
    - ANZ supported the key message put forward in the paper, that the intent of pre-hedging should be to the benefit of the client and market functioning.
    - ANZ has Material Sized Transaction (MST) guidelines in place and more recently, Trading and Sales Practices Guidelines have been modified to include the requirements **for informed consent** in relation to pre-hedging. ANZ continues to work through various scenarios and refine its internal policies and practices in-line with the paper's recommendations.
- It is important to note that the updated paper does not include any further guidance on situations where the LP pre-hedges but does not win the deal (anticipated order does not become firm) other than LP will bear any consequent profit and loss on the pre-hedged position.
    - In-line with ANZ's prior feedback, ANZ was hoping the Code may provide some additional clarity on this type of scenario and recommend the resulting position is immediately cleared or at the discretion of the LP whether to clear or hold.
- The paper has slightly clarified the terminology around when pre-hedging is not meant to apply - *"Principle 11 is not meant to apply to situations where the liquidity provider is managing their ongoing inventory risk by anticipating general order flow, including the risk management of reasonably expected near term demand (RENTD)."*
    - ANZ supports this clarification and is consistent with internal discussions and examples around pre-hedging.
- The paper states the LP should regularly review the effectiveness of the execution post-trade to see whether the expected outcome was delivered.
    - ANZ would recommend this occurs post an MST or alternatively via an annual review, which would provide evidence of monitoring the effectiveness.
- The Paper states pre-hedging should not disadvantage the client but recognises that pre-hedging may be detrimental in exceptional circumstances
    - ANZ concurs with this view.
- Previously the paper was focussed on 'large' transactions but this has been replaced with trades that could have 'significant market impact' or could 'significantly impact market prices'.
    - ANZ suggests some additional clarity could be provided as the use of the term 'significantly' may/will be open to interpretation unless defined more clearly. ANZ has its own internal view of what classifies as an MST.

- There is a comment in section 6 - Potential impacts from pre-hedging (page 7/17): regarding execution options including #5 which states '*Clearly indicate that the RFQ is exclusive, rather than in competition as – all other things being equal – that will tend to reduce (without necessarily eliminating) the need for the liquidity provider to have to pre-hedge due to reduced information leakage regarding the order*'.
    - ANZ does not agree with this as risk of information leakage is not a reason to pre-hedge, nor is pricing in competition a reason to pre-hedge, rather pre-hedging is linked to an anticipated order and managing the risk associated with this anticipated order (always acting in the best interests of the client). ANZ questions the relevance of this point and whether it is necessary to include in the paper.
- Note the updated paper removes the recommendation to segregate SLO and order execution
    - This is in-line with ANZ's prior feedback and recommendations.
- In terms of controls and disclosures around pre-hedging…
    - Most of this is currently in place at ANZ. Markets Surveillance would cover much of this around pre-hedging activity and conflicts of interest. Significant work has gone into limiting access to confidential information relating to order flow; training is rolled out on an ongoing basis, including annual refreshers; client disclosure documents and more.
- Additional illustrative trading scenarios have been included in *Appendix 2*.
    - ANZ supports the example illustrative trading scenarios provided and are aligned with how ANZ operates
    - ANZ would recommend that the examples are included in the Code's Annex for Illustrative Examples.
- The notion of informed consent is not <u>explicitly</u> discussed or referenced in the paper. It is inferred in various places though per below points:
    - *Transparency about execution or pre-hedging practices also allows a liquidity consumer to determine whether they should potentially adjust their order or method of execution, or perhaps even trade with a different liquidity provider.*
    - *In general, when conditions potentially warrant pre-hedging, liquidity providers should strive, at the time of the request, to communicate the potential implication of the order on market liquidity and price.*
    - *Liquidity providers should strive to outline alternative options for executing the trade to limit its market impact. The frequency and extent of any such discussions may also depend on the sophistication of the liquidity consumer and the perceived size of the market impact of the trade.*
    - *Liquidity consumers should understand how their orders are handled so as to make informed choices.*
    - *Liquidity providers should communicate their pre-hedging practices to liquidity consumers in a manner that allows a liquidity consumer to fully understand and be aware of the potential impact on their execution.*
    - *If in doubt as to whether Principle 11 applies in any such requests, best practice would suggest an open discussion between the liquidity consumer and provider to align expectations.*

- *(with regard to Limit Orders), liquidity consumers and providers should be clearly aligned whether discretion will or will not be applied, desired, or expected.*
  - ANZ acknowledges the Global Code and the underlying principles are intended to serve as a supplement to any and all local laws, rules and regulations. Australian institutions are obligated and governed by the *Corporations Act*, which references the notion of informed consent. Given the recent publicly reported litigation in Australia and the US around the topic of informed consent, ANZ would recommend the GFXC consider some additional wording to provide greater clarity on the **receipt of informed consent.**

Last Look (LL) Paper

- Guidance has been rewritten from the previous paper and the GFXC has sought to be more 'principles-focused' rather than prescriptive. As such there are a lot more 'should' than 'must'.
  - ANZ supports this approach and is in-line with ANZ's prior feedback that certain sections were too granular and had moved away from a principles based approach.
- 3 key recommendations in the paper:
  1. Liquidity providers should ensure fair and effective last look process
     - ANZ agrees that LL should be a fair and effective process, although questions the recommendation that the LP should strive for predictability. How is predictability achieved? Could there be an expectation that predictability is evidenced?
     - Hold times should be the same whether rejecting or accepting a trade
       - ANZ are consistent with this guidance
     - LPs should minimise the hold time as much as possible thereby minimising uncertainty for the client. LPs should *promptly* make their decision to accept or reject
       - ANZ agrees, LPs should seek to minimise hold times and uncertainty for the client as appropriate. However, ANZ believes this is open to interpretation and would suggest is in part technology dependent and/or even client behaviour dependent. Ultimately the LPs should be clear in their disclosures to the client how LL is being applied, while noting ANZ does not currently disclose hold time.
     - Do not use confidential information
       - ANZ agrees and complies with this view. ANZ has processes in place for this as well as internal controls around LL processes, including surveillance. LL trade metrics are reported at ANZ's monthly Electronic Governance Forum for review and discussion.
     - Statement that LPs should not conduct trading activity that utilises the information from the client's trade

- ANZ agrees and complies with this statement.

2. <u>LPs should enhance ex-ante disclosures</u>

- Recommendation to disclose at a minimum, explanations regarding whether, and if so how, changes to price in either direction may impact the decision to accept or reject the trade, the expected or typical period of time for making that decision and more broadly the purpose for using last look'.
  - ANZ agree this seems reasonable and supports this although noted this would require updates to our client disclosure documents. ANZ's internal Electronic Trading Procedures and Operating Manuals would cover this recommendation though.
  - ANZ's client disclosure states the purpose for using LL and includes the key themes/points:
    - *The purpose of last look is primarily to reduce the risk of trading on a stale price due to latency and technology constraints, to protect ANZ against certain trading behaviour such as aggregation, order splitting or previous quote selection, and as a risk control mechanism.*
  - ANZ's internal Electronic Trading Procedures is more prescriptive and also capture explanations on changes in prices in either direction as well as the impact on accept/reject (noting ANZ applies symmetric LL). The Procedures summarise LL as:

    Deal acceptance criteria form an important part of the interaction with the client in an Electronic Trading environment. ANZ may reject orders for the following reasons:
    - *Potential for market disruption*
    - *Insufficient credit*
    - *Operational reasons such as malformed or incorrect trade messages*
    - *Price deviation or latency*
    - *Internal risk limits*
    - *To protect ANZ against certain trading behaviour such as aggregation, order splitting or previous quote selection*
- Recommendation that LP's should disclose the expected length of the last look window
  - ANZ does not currently disclose this. ANZ sees this as a difficult matter as the length of the window is likely to change over time with new technology, requiring updating of disclosures.
- Disclosure including the methodologies used by ANZ for their price checks

  - ANZ applies LL symmetrically and this is disclosed as such to customers accordingly.

3. Information should be available to regularly evaluate the handling of trade requests
   - The LP should provide information to the LC that will allow the LC to evaluate the handling of trade requests by the LP
     - Although ANZ supports this in principle, work would need to be undertaken to ensure rejection reasons are standardised and ANZ would need to ensure 3rd party platforms will be able to provide the rejection reasons to the LC.
   - LPs should be recording trade rejection information for orders and transactions and be able to disclose it at a trade-by-trade level at the time of the rejection where requested by LCs.
     - ANZ do not currently send this type of information relating to LL externally, ANZ only sends a price rejection. Internally though, this information on why validators accept or reject every trade is available and retained. As such, ANZ would be able to disclose to the LCs if requested.

- Validity and price checks are outlined in the paper
  - ANZ is consistent with the validity and price checks. ANZ's Last Look and Credit checks run in parallel. System logic has been set such that if the credit checker takes longer than Last Look, Last Look will not complete until the credit checks have been completed.
- The estimation of the 'current price' is at the discretion of the LP
  - ANZ supports this view.
- Price check states that it is typically 'a value defined in terms of price, usually in currency pips or basis points'.
  - ANZ already provided feedback on this that we use % of spread – we would again recommend this be included in the guidance (reason being the % of spread auto calibrates to allow greater tolerances in more volatile market conditions).
- The paper states LP's should disclose if they source liquidity using cover and deal –
  - ANZ does not do cover and deal but agrees LPs should disclose this.

GFXC Request for Feedback – May 2021

Draft Guidance Paper 2: Last Look

DRAFT – GFXC Execution Principles Working Group Report on Last Look

1. Introduction

Last look is a practice utilised in Electronic Trading Activities whereby a Market Participant receiving a trade request has a final opportunity to accept or reject the request against its quoted price. This practice has been the subject of much discussion within the industry.

Principle 17 of the FX Global Code (the Code) specifically covers the topic of last look.[1] Following the initial publication of the Code in May 2017, the Global Foreign Exchange Committee (GFXC) amended the text of Principle 17 in December 2017 to provide tighter guidance around trading activity during the last look window.[2] A subsequent report on such 'Cover and Deal' trading activity was published by the GFXC in February 2019.[3]

Notwithstanding the publication of this material, the practice of last look garnered the most feedback when the GFXC surveyed Market Participants in 2019 on suitable areas of focus for the Three-Year Review of the Code. Many Market Participants still had questions and concerns on last look practices, and opinions on this topic remained diverse. Respondents noted that the quality and detail of ex ante disclosures on last look practices could vary widely, including regarding the methodologies used by liquidity providers for their price checks and, relatedly, the length of the last look window. Clearer disclosure on the usages of 'cover and deal' activity during the last look window was also sought. Greater clarity was sought on the appropriate treatment of rejected trade information and, to enhance the capacity of liquidity consumers to evaluate their trade execution, greater accessibility of trade information (including the reasons for trade rejections) was desired.

This paper has been developed by the GFXC to promote wider knowledge and understanding of last look, the role that it plays in the functioning of the FX market, and the appropriate application of last look as a practice. The paper concludes with three recommendations to help address the concerns expressed in the GFXC's earlier survey:

- Liquidity providers should ensure a fair and effective last look process;
- LPs should enhance ex-ante disclosures;

[1] The current (August 2018) version of the Code is available at https://www.globalfxc.org/docs/fx_global.pdf.
[2] See the GFXC's Request for Feedback on Last Look: https://www.globalfxc.org/docs/gfxc_response_paper_dec17.pdf.
[3] See https://www.globalfxc.org/docs/the_role_of_cover_and_deal_arrangements.pdf.

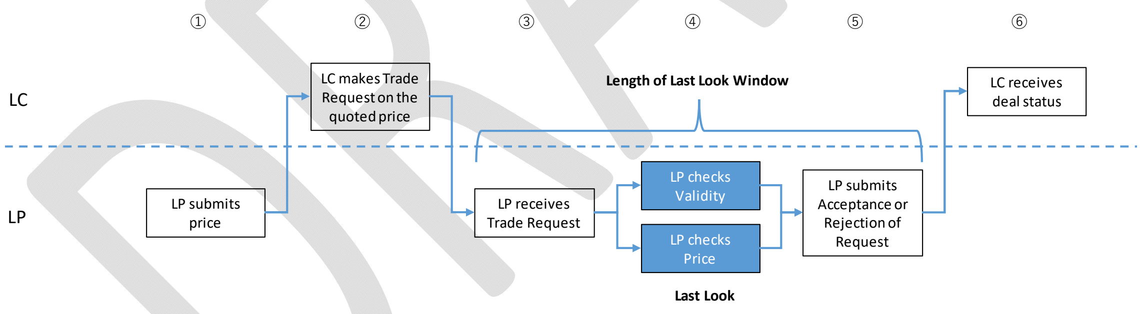
- Information should be available to regularly evaluate the handling of trade requests

This paper should be read alongside the Code, specifically Principle 17, which is included in Appendix A. In its Three-Year Review of the Code, the GFXC agreed that the text of Principle 17 remains appropriate. This guidance paper is not part of the Code. It is acknowledged that the topic is technical in nature and that a wide spectrum of opinion exists on specific aspects of this practice; accordingly this paper is principles-focused and not intended to be prescriptive.

2. What is Last Look

As noted in Principle 17 of the Code, last look is "a practice utilized in Electronic Trading Activities whereby a Market Participant receiving a trade request has a final opportunity to accept or reject the request against its quoted price," and "if utilized, last look should be a risk control mechanism used in order to verify validity and/or price." A stylized workflow of last look is shown below, with the Market Participant quoting prices designated as a Liquidity Provider (LP) and the Market Participant making trade requests on those quoted prices designated as a Liquidity Consumer (LC).

Figure 1: Illustrative Workflow of Last Look



Validity Check

The validity check "… should be intended to confirm that the transaction details contained in the request to trade are appropriate from an operational perspective and there is sufficient available credit to enter into the transaction contemplated by the trade request" (Principle 17).

The specific credit-check metrics and the method by which these checks are undertaken can differ widely by Liquidity Provider (LP), as can the length of time required to conduct the check. In cases where an LP is providing quotes on an electronic Request-For-Quote (RFQ) basis, credit may be 'carved out' at the time of the quote request, which may lessen the requirement to check again at the time of a trade request. In the case of indicative streaming prices, LPs will use the last-look process as a final check to ensure sufficient credit limit is available for the trade being undertaken.

Price Check

Principle 17 of the Code states that "the price check should be intended to confirm whether the price at which the trade request was made remains consistent with the current price that would be available to the Client."

In conducting a price check, an LP compares the quoted price to its estimation of the current price. The estimation of the current price is at the discretion of the LP. The degree to which the quoted price is consistent with the current price is defined in terms of 'price tolerance'. This is typically a value defined in terms of price, usually in currency pips or basis points.

Principle 17 provides guidance that LPs should disclose how "… changes to price in either direction may impact the decision to accept or reject the trade." LPs apply a price check symmetrically or asymmetrically. As the name suggests, a symmetric check applies the same price tolerance level symmetrically around the current price. The LP will reject any trade request on a price that exceeds the defined tolerance level, regardless of whether it is in favor of the LP or the LC.

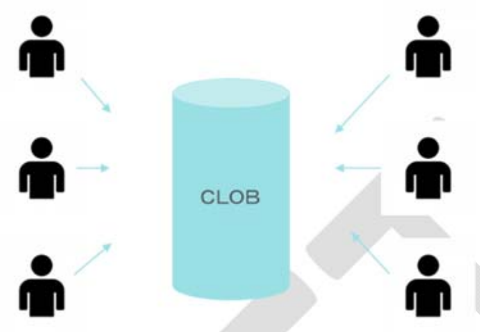
In an asymmetric price check, the application of the tolerance level is asymmetric around the current price. Such an approach tends to lead to trades being accepted when the price has moved in favor of the LP, while trade requests are rejected if the price moves beyond the tolerance level against the LP. Relatedly, some LPs may utilize a price improvement mechanism, such that the LP will accept the LC's trade request at an improved price in cases where the market has moved in favor of the LP, rather than rejecting the trade.

3. The Role of Last Look in the OTC FX Market

To understand the role of last look in the over-the-counter (OTC) FX market, it may be useful to compare the differences between it and a centralized matching model.

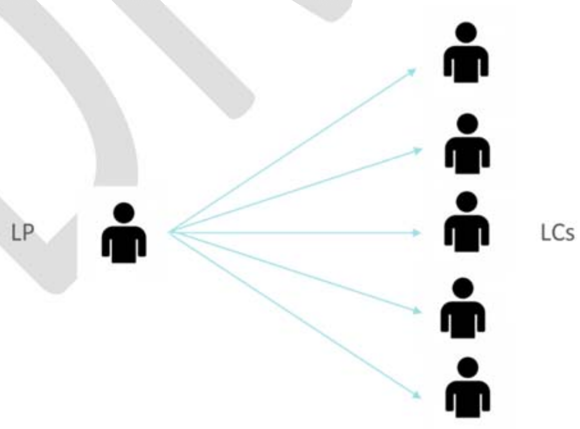
Market participants using a centralized matching trading venue submit their desired transaction amount and price, and transactions are completed when opposite interest is matched on the central limit order book (CLOB). In this sense, the submitted prices represent 'firm liquidity' as once interest is matched, participants are obligated to commit to the transaction. There is no risk of transacting an amount larger than the interest shown to the venue by the market participant. Figure 2 illustrates this model.

Figure 2: Centralized Matching model



The sequence in which a trade is established is fundamentally different in the non-central matching electronic trading model in which most electronic FX transactions are executed. FX transactions are often dealt in this way to allow for market participants of varying sizes to settle a high volume of transactions across many different currencies. LPs simultaneously stream many indicative FX quotes, which allows for access to potential FX liquidity by many LCs in the market. When an LC sends a request to trade on the LP's indicative price, the LP determines whether or not to accept the client's request at that price, as part of the last look process.

Figure 3: Non-Central Matching Model



In a non-central matching model, the LP exposes itself to the risk of receiving requests to trade from many LCs simultaneously, or can be subject to requests that are received significantly later than the time of the quote. LPs manage risks such as this through the validity and price check processes. One consequence, however, is the possibility of trade rejections. When a trade request is rejected, it may have direct bearing on the execution cost of the LC. The LC not only loses the opportunity to trade on the quote that was provided, they may subsequently transact on a worse price.

It should be noted that there are venues in the FX industry that use firm quotes and do not utilize last look. LCs can compare features and choose where and who to trade with.

4. Treatment of Trade Information from Trade Requests

As noted in Principle 17, "the Market Participant has sole discretion, based upon the validity and price check processes, over whether the Client's trade request is accepted or not, leaving the Client with potential market risk in the event the trade request is not accepted."

Principle 17 explicitly disallows the use of last look for the purposes of information gathering with no intention to accept the Client's request to trade. Confidential Information arises at the point the Market Participant receives a trade request at the start of the last look window, and use of such Confidential Information should be consistent with Principles 19 and 20 on Information Sharing. Using last look inappropriately could potentially be characterized by relatively low trade acceptance rates, differences in the time taken to accept or reject and/or significant market movement against the LC when a request-to-trade is rejected.

The Code also provides guidance that LPs should not conduct trading activity during the last look window that utilizes information from the Client's trade request. Such activity includes price adjustments as well as hedging activity that incorporates information from the LC's trade request, before accepting/rejecting the trade request. These activities would risk signaling to other market participants the LC's trading intent and could move market prices against the LC. If the requests are then rejected, this could disadvantage the LC.

The only exception to this guidance are 'Cover and Deal' arrangements which feature all of the following characteristics:

1. An explicit understanding that the Market Participant will fill the Client's trade request without taking on market risk in connection with the trade request by first entering into offsetting transactions in the market; and
2. The volume traded in the last look window will be passed on to the Client in its entirety; and
3. This understanding is appropriately documented and disclosed to the Client.

5. Recommendations

Last look is a feature of the OTC electronic FX market. As each LP has its own last look policy, without clear explanation the nature of its last look process may be difficult for other market participants to understand. In line with the guidance in the Code, the following recommendations are provided in order to alleviate concerns covering three areas – the designing of fair and effective last look processes, the disclosures to be made, and the provisioning of sufficient information for evaluating trade execution.

Recommendation 1: Ensure a fair and effective last look process

- As LPs are in the position of holding sole discretion over accepting or rejecting an LC's trade request, LPs should strive for fairness and predictability in designing their last look processes.

- During the last look window in which an LP is conducting its checks, the LC is potentially exposed to market risk as the market price may move prior to acceptance, and there is also the possibility that their trade request will be rejected altogether. In the interest of fairness, LPs should aim to minimize this period of uncertainty for the LC and therefore LPs should promptly make their decision to accept or reject a trade. As stated in Principle 17, "the price check should be intended to confirm whether the price at which the trade request was made remains consistent with the current price that would be available to the Client".

- The guiding principle of fairness also applies to the treatment of rejected trade information. Through conducting its validity and price checks, the LP will undoubtedly come to possess Confidential Information regarding the LC's intention to trade. Confidential Information should not be used by the LP for reasons other than the purpose for which it was given, as per Principles 19 and 20 of the Code. An example of misuse would be for an LP to use rejected trade information as an input to make real-time trading decisions that could harm the interest of LCs by exposing them to further market risk.

- LPs should note that the guidance in Principle 17, including references to 'clients', applies to all counterparties, whether named or anonymous.

- As the design of the price and validity checks are often proprietary and not always observable externally, LPs should ensure that there are sufficient internal controls and management oversight in place around their last look processes. This will serve to provide LCs with confidence that they are being treated in a manner which is consistent with the Code's principles.

Recommendation 2: Enhance ex-ante disclosures

- In line with Principle 17 of the Code, LPs should disclose whether they employ last look and, if so, they should ensure that their ex-ante disclosures provide sufficient information for LCs to be able to understand the implications of the LP's last look policy for their trading. To help LCs access this information and allow for greater comparability across LPs, the GFXC has produced a Disclosures Cover Sheet for LPs that includes the following fields that are relevant to last look practices.

    - LPs should disclose whether their price check is applied symmetrically or asymmetrically. Both methods exist in the market, but the choice of price check logic could materially impact the predictability of the LP's last look processes and therefore the outcomes for the client. Asymmetric price checks introduce greater complexity for LCs in monitoring the effectiveness of their execution and so it is particularly important for LCs to understand the circumstances in which they are used.

    - LPs should disclose information about the expected length of the last look window to their LCs.

    - LPs should disclose if they source liquidity using 'Cover and Deal' arrangements during the last look window , meeting all of the requirements for such trading activity that are set out in Principle 17 of the Code. It will be important for LCs to understand the circumstances in which Cover and Deal arrangements are used, such as whether it only applies to certain currency pairs or during certain operating hours.

Recommendation 3: Information should be available to regularly evaluate the handling of trade requests

- Principle 17 encourages LCs and LPs to engage in a dialogue regarding the handling of trade requests. As much of the relevant information resides with the LP, LPs should be sharing sufficient information for LCs to be able to evaluate their trade execution.

- In cases of trade rejection, LPs should be able to disclose, at least, a high level reason for the rejection that is clear and unambiguous, such as whether it was due to failing a validity or price check. LPs should be accurately recording trade rejection information for orders and transactions and be able to disclose it at a trade-by-trade level at the time of the rejection where requested by LCs.

- With appropriate transparency from LPs, LCs should be able to determine whether their methods of execution continue to meet their needs over time, including whether to trade with LPs that are using last look. A trade rejection due to a price check should be an indication that the market has moved between the time the quote was provided by the LP and the time the LP received the request to trade.

  - High rejection rates with an unusually long or unpredictable last look window may be an indication of inappropriate use of last look by LPs.
  - A consistently strong market reaction that occurs when dealing with a specific LP may be an indication of undesirable information leakage or a suboptimal hedging strategy by the LP.
  - If an LC's trade requests are regularly rejected due to price checks, they may need to consider looking at the market impact of their own trades. While it is difficult to definitively attribute post-trade market movement to any one reason, sharp rate changes should make an LC reevaluate their execution strategy.

<End of Document>

Appendix A – Global FX Code, Principle 17

Market Participants employing last look should be transparent regarding its use and provide appropriate disclosures to Clients. Last look is a practice utilised in Electronic Trading Activities whereby a Market Participant receiving a trade request has a final opportunity to accept or reject the request against its quoted price. Market Participants receiving trade requests that utilise the last look window should have in place governance and controls around its design and use, consistent with disclosed terms. This may include appropriate management and compliance oversight.

A Market Participant should be transparent regarding its last look practices in order for the Client to understand and to be able to make an informed decision as to the manner in which last look is applied to their trading. The Market Participant should disclose, at a minimum, explanations regarding whether, and if so how, changes to price in either direction may impact the decision to accept or reject the trade, the expected or typical period of time for making that decision, and more broadly the purpose for using last look.

If utilised, last look should be a risk control mechanism used in order to verify validity and/or price. The validity check should be intended to confirm that the transaction details contained in the request to trade are appropriate from an operational perspective and there is sufficient available credit to enter into the transaction contemplated by the trade request. The price check should be intended to confirm whether the price at which the trade request was made remains consistent with the current price that would be available to the Client.

In the context of last look, the Market Participant has sole discretion, based upon the validity and price check processes, over whether the Client's trade request is accepted or not, leaving the Client with potential market risk in the event the trade request is not accepted. Accordingly, and consistent with related principles in the Global Code:

Last look should not be used for purposes of information gathering with no intention to accept the Client's request to trade.

Confidential Information arises at the point the Market Participant receives a trade request at the start of the last look window, and use of such Confidential Information should be consistent with Principles 19 and 20 on Information Sharing.

Market Participants should not conduct trading activity that utilises the information from the Client's trade request during the last look window. Such trading activity would include (1) any pricing activity on E-Trading Platforms that incorporates information from the trade request and (2) any hedging activity that incorporates information from the trade request. Such activity would risk signaling to other Market Participants the Client's trading intent and could move market prices against the Client. In the event that the Client's trade requests were subsequently rejected, such trading activity could disadvantage the Client.

This guidance does not apply to an arrangement that features all of the following characteristics:

1. An explicit understanding that the Market Participant will fill the Client's trade request without taking on market risk in connection with the trade request by first entering into offsetting transactions in the market; and
2. The volume traded in the last look window will be passed on to the Client in its entirety; and
3. This understanding is appropriately documented and disclosed to the Client.

It is good practice for Market Participants to be available to engage in a dialogue with Clients regarding how their trade requests have been handled, including the appropriate treatment of information associated with those trade requests. Such dialogue could include metrics that facilitate transparency around the pricing and execution of the Client's trade requests and assist a Client in evaluating the handling of its trade requests in order to evaluate whether the execution methodology continues to meet its needs over time.

CITADEL | Securities

May 31, 2021

GFXC Secretariat
Global Foreign Exchange Committee

Re: GFXC Request for Feedback on a Draft Guidance Paper on Last Look

Dear Sirs:

Citadel Securities appreciates the opportunity to provide feedback to the Global Foreign Exchange Committee (the "GFXC") on the draft guidance paper on "last look" (the "Guidance Paper").[1]

I. The FX Market Should Transition Away From Last Look

First, we take this opportunity to reiterate our longstanding position that the widespread use of "last look" in the FX market impairs overall market transparency, fairness, and competition. We urge policymakers to lead an orderly market-wide transition away from "last look" in favor of firm pricing.

As evidenced by the Guidance Paper, the justifications offered for the continued market-wide use of "last look" lack rational basis. Despite the attempt to depict the FX market as unique, with a "non-central matching model,"[2] fragmentation is endemic in many global financial markets (both equities and non-equities). Liquidity providers successfully navigate this fragmentation, quoting firm prices (and managing the allocation of risk and capital) simultaneously across numerous multilateral venues and, particularly in non-equities markets, also through a number of additional channels, such as bilateral streams. From a market structure perspective, the only truly unique characteristic of the FX market is the continued market-wide use of "last look."

The implications of relying on indicative pricing are significant. By definition, indicative pricing may not be executable, meaning that assessments of current market pricing and liquidity are distorted. In addition, indicative pricing impairs efforts by clients to accurately measure transaction costs, as the economic impact of the "last look" window and potential trade rejections must also be considered. These adverse impacts are particularly pronounced during times of market volatility.

Competition and innovation have expanded the use of firm pricing in non-equities markets, such as the global interest rate swaps market. Concrete steps should be taken to foster the increased use of firm pricing in the FX market, including:

- Requiring multilateral venues to implement appropriate pre-trade risk controls to

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[1] https://www.globalfxc.org/consultative_process.htm?m=72%7C429.

[2] Guidance Paper at page 5.

enable liquidity providers to effectively manage risk and credit allocations;[3] and

- Ensuring liquidity providers are appropriately incentivized to provide firm pricing (including through market maker programs or other platform features, such as (a) clearly distinguishing firm prices from indicative prices, (b) displaying an adjusted indicative price to account for the percentage of trades rejected by a liquidity provider, and (c) notifying clients if there is a better firm price available on the platform regardless of trading protocol used).

II. Feedback on the Guidance Paper

Notwithstanding the above, we provide the following feedback on the Guidance Paper:

- The Guidance Paper states: "LPs should note that the guidance in Principle 17, including references to 'clients', applies to all counterparties, whether named or anonymous."[4]

  This is helpful clarification; however, further guidance is required regarding how to provide the required disclosure under Principle 17 on anonymous trading platforms. As we commented in response to the recent anonymous trading proposals, Principle 17 requires liquidity providers to fully disclose any "cover and deal" trading activity that utilizes information from the client's trade request during the last look window. Given the definition of 'client' as further clarified by the Guidance Paper, the Code should ensure that this required disclosure occurs on anonymous trading platforms, with the platform operator facilitating the provision of the disclosure on an anonymous basis and the liquidity provider entirely responsible for its accuracy.

- The Guidance Paper states: "LPs should disclose information about the expected length of the last look window to their LCs."[5]

  We agree; however, as we commented in response to the recent disclosure proposals, the current draft disclosures do not require liquidity providers to disclose the expected length of the last look window. Instead, the proposed disclosures only require liquidity providers to provide maximum and minimum "hold times." While this term is not defined, it does not appear to take into account that the time required to conduct an initial price check may vary significantly between liquidity providers. As a result, solely disclosing "hold times" that follow an initial price check does not provide clients with information regarding the expected length of the entire last look window. Consistent with the Guidance Paper, we strongly recommend that liquidity providers be required to disclose maximum and minimum durations for the entire last look window, which is the most important consideration for clients.

[3] A market-wide utility for credit checking may also merit consideration.

[4] Guidance Paper at page 7.

[5] Guidance Paper at page 8.

- The Guidance Paper states: "In cases where an LP is providing quotes on an electronic Request-For-Quote (RFQ) basis, credit may be 'carved out' at the time of the quote request, which may lessen the requirement to check again at the time of a trade request."[6]

  This statement raises a question regarding how "last look" is used during an RFQ trading protocol. The draft Guidance Paper on pre-hedging states that "In the case of Principle 17, the liquidity consumer is sending a specific order requesting to trade on an *indicative* quote that has already been provided (streamed) by the liquidity provider." This suggests that "last look" could be used in a request for stream (RFS) trading protocol, but not a typical RFQ trading protocol, where a client requests a firm quote from a liquidity provider. Further clarification should be provided regarding when "last look" (as opposed to pre-hedging) might be used during an RFQ trading protocol.

* * * * * * * * * *

We appreciate the opportunity to provide comments to the GFXC. Please feel free to call the undersigned at (646) 403-8200 with any questions regarding these comments.

Respectfully,

/s/ Stephen John Berger

Managing Director

Global Head of Government & Regulatory Policy

[6] Guidance Paper at page 3.

May 31, 2021

Global Foreign Exchange Committee Secretariat
Sent via email: codefeedback@globalfxc.org

RE: Request for Feedback on Draft Guidance Papers for Pre-Hedging and Last Look

Dear GFXC Secretariat,

The Foreign Exchange Professionals Association (FXPA)[1] appreciates the opportunity to provide feedback to the Global Foreign Exchange Committee (GFXC) on the draft guidance papers for pre-hedging and last look.[2]

As we stated in our letter on the GFXC's request for feedback on the proposed cover sheets, the FXPA remains a strong supporter of the Code and its stated aim to promote a robust, fair, liquid, open, and transparent market, which is very much in line with FXPA's own principles. The FXPA, as an Association, fully supports the adoption of the Global Code's principles.[3]

We worry, though, that the guidance papers – like the cover sheets – will be viewed and internalized by those in the industry as more than what the GFXC intended them to be – i.e., guidance. Even with the disclosures in the guidance papers that they are "not part of the Code" and are "principles-focused and not intended to be prescriptive," their format and detailed commentary on pre-hedging and last look, including a section titled "Recommendations" in the last look paper, suggest that a market participant would need to align its processes and procedures with these papers in order to be in compliance with the Global Code. A Statement of Commitment, moreover, could be read to imply that the market participant has aligned itself with the Global Code *and* these guidance papers. In short, the FXPA is concerned that the papers will quickly become inextricably linked with the Global Code, and participants will be put under pressure to adopt the recommendations therein (incurring both the costs to do so and the liability for noncompliance).

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[1] The FXPA represents the collective interests of professional FX industry participants, including buy-side, exchanges and clearing houses, trading platforms, technology companies, banks and non-bank market participants, among others, to advance a sound, liquid, transparent and competitive global currency market to policymakers and the marketplace through education, research and advocacy. The following comments do not represent the specific individual opinion of any one particular member. For more information, please see www.fxpa.org.

[2] GFXC, *GFXC Publishes Request for Feedback on Draft Guidance Papers for Pre-Hedging and Last Look* (May 11, 2021), https://www.globalfxc.org/press/p210511.htm.

[3] *See FXPA Endorses Global Code for FX Market*, FXPA (May 25, 2017), https://fxpa.org/fxpa-endorses-global-code-for-fx-market/.

Put simply, at a time when the industry and regulators are trying to encourage additional commitments to the Global Code, adding an additional layer of complexity in the form of, for example, *recommendations* in a *guidance paper* expanding on *principle* in a voluntary *code of conduct* may prove to be a step too far to convince additional FX market participants, particularly buy side firms, to sign up for the Global Code.

Recommendation #1: The FXPA recommends that the guidance papers provide additional clarity on their intended use beyond the disclosures already present in them. If being published solely as an educational perspective to improve market understanding, then the papers should state so and explicitly provide that market participants who choose not to follow some (or all) of the paper's guidelines would *not* be deemed to be out of compliance with the Global Code. If being offered as more than an educational resource and there is an expectation that participants adhere to the papers' recommendations, then the substance of the papers should be incorporated directly into the Global Code, a path the GFXC recently pursued with proposed amendments to the Global Code.

The FXPA also recommends specific changes to the guidance papers, as further discussed below.

I. <u>Draft Guidance Paper 1: Pre-Hedging</u>

Recommendation #2: In Section 6, the GFXC suggest several execution options for liquidity consumers to "understand how their orders are handled to as to make informed choices about which liquidity provider they choose to transact with." The FXPA notes that several of these execution options are not easily implemented in markets that trade electronically. For example, in a market with electronic trading and liquidity providers using algorithms or other automated infrastructure, a liquidity provider could not receive an accommodate a liquidity consumer's request for prices without any pre-hedging (number 4) or incorporate whether a request for quote is exclusive or competitive. To adopt these protocols for highly liquid markets would require a transition from electronic to voice markets.

Recommendation #3: The FXPA recommends that the GFXC review the use of market terms in the guidance papers, generally, to ensure they reflect the way a broad cross-section of market participants use the terms. For example, in Section 7.1, stop-loss orders should be clarified to align with the industry's use of the term. First, some market participants do not consider a stop-loss order to be a firm order, as the trade is not considered done until the client agrees to the final price (i.e., the client can walk away). Second, the FXPA encourage the GFXC to further socialize the comment in the guidance paper discussion regarding a "stop-loss order becoming an 'at the market' order once trigger is hit." In this case, a stop-loss order becoming an at the market order is not something that reflects how many market participants engage in the market and describe these order types. Generally, market participants rely on stop-loss orders to sell at a certain price in order to minimize risk, while an at the market order can introduce significantly more slippage due to rapidly changing market prices.

Recommendation #4: The FXPA recommends that the request for quote (RFQ) guidance to clients should be clarified to align with how venues implement the RFQ functionality, while also clarifying that the guidance does not place any expectations on venues that they must implement this functionality. At present, this functionality does not yet exist universally in the market.

Recommendation #5: The FXPA recommends that the guidance paper reference what the GFXC believes that buy side participants should and should not do in regard to placement of orders that could be pre-hedged. Given the particular interest in increasing buyside commitment to the Global Code, clarifying what the guidance paper means for this segment of the FX market would be a meaningful improvement.

Recommendation #6: The FXPA recommends that the guidance paper clarify how it applies to trading venues, all of whom should not be placed in a position to police the pre-hedging activities of liquidity providers. Trading venues have a limited view into the larger marketplace, and are ill suited (based on their function and access to real-time information across trading venues) to monitor this type of behavior. The FXPA encourages the GFXC to consider, perhaps in lieu of a guidance paper, to issue an examples-based FAQ document describing how to employ this guidance and some clarification of its meaning in various environments, trading formats, and circumstances.

II. <u>Draft Guidance Paper 2: Last Look</u>

Recommendation #7: The FXPA recommends the paper include references to what types of trading venues (anonymous, etc.) the guidance would or would not be applicable, and clarification that operators of trading venues will not be required to enforce these provisions / recommendations where not possible to do so. Trading venues are not liquidity providers. Trading venues cannot police the last look practices of liquidity providers, who are best positioned to describe, deploy, and oversee their last look practices.

Recommendation #8: The FXPA recommends clarity around the statement that "LPs should be able to disclose, at least, a high level reason for the rejection that is clear and unambiguous, such as whether it was due to failing a validity or price check." Some e-trading platforms may have some last look controls embedded in their systems, so this raises questions as to who is responsible for the accuracy, collection, and presentation of rejection reasons to the liquidity consumer. Furthermore, developing a consistent standard across trading platforms for liquidity consumers with respect to trade rejection information could be complicated, burdensome, and, potentially, a solution does not provide meaningful benefit to liquidity consumers. The FXPA cautions against such a significant undertaking without input from a broad array of market participants.

Recommendation #9: The FXPA believes the guidance paper, and the Global Code, should not adopt recommendations or principles with respect to symmetric vs asymmetric price checks. The FXPA supports adequate disclosure by liquidity providers so that liquidity consumers can make informed decisions about last look liquidity prices in the market.

* * *

The FXPA stands ready to work with the GFXC on the issues discussed herein. Should the GFXC wish to discuss these comments further, please contact the undersigned at chairman@fxpa.org.

Sincerely yours,

Chip Lowry
Chairman

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28 May 2021

RE: The Global FX Committee request for industry feedback on draft guidance papers for the practices of 'pre-hedging' and 'last look'

HSBC greatly welcomes the opportunity to respond to the Global FX Committee's (GFXC) request for industry feedback on draft guidance papers for the practices of 'pre-hedging' and 'last look'. From its inception, HSBC has been strongly supportive of the work of the GFXC and in particular, supportive of the creation and maintenance of the FX Global Code, in providing a common set of guidelines promoting the integrity and effective functioning of the wholesale FX market. HSBC appreciates the efforts of the GFXC working groups which have put together these guidance papers, and the intended outcomes to promote wider knowledge and understanding of these pratices and the roles they play in the effective functioning of the FX market.

Draft Guidance Paper 1: Pre-Hedging

HSBC agrees that pre-hedging, where designed to benefit the liquidity consumer, and carried out in line with the best practices set out in Principle 11 of the FX Global Code, is an effective risk management tool used to facilitate execution of client trades that could have significant market impact. HSBC agrees that liquidity providers should have in place procedures for handling client orders fairly and in accordance with the FX Global Code, in particular where pre-hedging is being undertaken. Enhanced dislcosures and communications with clients promote wider understating of pre-hedging practices among market participants, and in particular how pre-hedging is used as a tool to facilitate reduced market impact resulting from trading activity.

The paper however currently states that Principle 11 of the FX Global Code is not applicable to confirmed fixing orders but that nonetheless any hedging of the fixing order should be consistent with the Code. HSBC believes that the additional expectations of principled conduct outlined in Principle 11 are in fact applicable in this case, as they should apply whenever the final client price is still to be determined and whether hedging or pre-hedging is taking place, and as such HSBC applies these conduct best practices when executing fixing orders in the FX market.

Draft Guidance Paper 2: Last Look

HSBC agrees with the key points set out in the draft guidance paper on last look. The guidance makes a clear distinction between a Central Limit Order Book and a support liquidity market and correctly highlights the importance of last look to the well-functioning of the latter. HSBC believes however, that the application of an additional hold time is hard to justify as it leads to a potentially detrimental outcome for clients, and it is for this reason that HSBC does not apply any additional hold times in the application of last look. The efficacy of last look is sometimes blurred through a lack of clear distinction or through a clear delineation between it and the application of additional hold times. HSBC therefore recognises the value that the definition in the guidance will provide in resolving this issue.

In recognition that additional hold times continue to be applied by some other market participants, in the interests of transparency and fairness it should be made very clear to consumers where the liquidity they receive is subject to an additional hold time. HSBC believes that the appropriate place for this is with clear and unambiguous disclosures. This should also be true in the case of ECNs who facilitate liquidity from sources subject to an additional hold time.

Hedging activity that incorporates information from a liquidity consumer's trade request during the last look window should not be permitted (as stated in Section 4 of the paper, and consistent with Principles 17 and 19 of the FX Global Code). Additionally, where a liquidity provider rejects a trade request, HSBC agrees that the liquidity provider should not use the confidential information from that trade request for reasons other than the purpose for which it was given, as stated in Section 5 of the paper.

Conclusion

HSBC would like to reiterate its thanks to the GFXC and members of each working group for their efforts in compiling feedback following the 3-year review of the FX Global Code, and writing these guidance papers to support the ongoing effective functioning of the FX market. HSBC strongly believes that this work is vital in continuing the good work of the GFXC and market participants in enhancing good conduct standards and practices within the FX market. HSBC would like to thank the GFXC for the opportunity to comment on these guidance papers.

Yours sincerely

Richard Bibbey
Global Head of FX, EM Rates and Commodities, HSBC

MAY 2021

GLOBAL FOREIGN EXCHANGE COMMITTEE
PRE-HEDGING AND LAST LOOK PRACTICES

Response from Insight Investment

Insight Investment is a strong supporter of the FX Global Code and is represented on two working groups that are currently providing feedback for the Three-Year Review of the Code. We are responding to the GFXC request for feedback on Draft Guidance Paper 2: Last Look

We agree that the quality of ex ante disclosures vary widely on last look practices and welcome the work being done on Disclosure Templates to enable greater comparison between these practices and importantly, to make them more easily accessible to Liquidity Consumers. We also welcome the addition of a guidance paper on the topic of Last Look to the Code and broadly support the main recommendations contained within this draft. There is however one area where we believe the Code could provide greater clarity:

The paper states that “if utilised, last look should be a risk control mechanism used in order to verify validity and/or price”. This infers that the use of an extended window where the LP can access multiple price updates before determining whether to accept the trade is not best practice. We would welcome a distinction between the hold time needed for an LP to complete their price and validity checks and the hold time applied to the trade acceptance process with the introduction of language such as ‘additional hold time’. This distinction could then be integrated into the Liquidity Provider Disclosure Cover Sheet providing LCs with further clarity.

Recommendation 1 states that “LPs should aim to minimise the period of uncertainty for the LC and should promptly make their decision to accept or reject a trade”. We would recommend a change of this language to “LPs should aim to immediately make their decision to accept or reject a trade after the completion of their required price and validity checks”. The rationale for any additional hold time applied beyond these checks could be captured using free type fields in the Liquidity Provider Disclosure Cover Sheet.

IMPORTANT INFORMATION

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May 31st, 2021

TO: Global FX Committee

RE: GFXC Request for Feedback on Draft Guidance for Pre-Hedging and Last Look

The Investment Association (IA) champions UK investment management, a world-leading industry which helps millions of households save for the future while supporting businesses and economic growth in the UK and abroad. Our 250 members range from smaller, specialist UK firms to European and global investment managers with a UK base. Collectively, they manage £8.5 trillion for savers and institutions, such as pension schemes and insurance companies, in the UK and beyond. The UK investment management industry is the largest in Europe and the second largest globally.

The IA has long been supportive of the Global FX Code, and welcomes the opportunity to provide input into the Global FX Committee's request for feedback on draft guidance for the practices of pre-hedging and last look. As users of FX markets, our members have a keen interest in ensuring that those markets function to a high standard and that FX market participants operate according to global best practice.

This response collates the views of our members on both draft sets of guidance. We welcome further discussion of any of the points raised in our response.

Last Look

The IA retains strong concerns around the current drafting of the Last Look guidance paper, specifically the ambiguity around how Last Look can be applied, and whether the use of additional holding times (AHT) can be incorporated.

Currently, the definition of Last Look often covers two similar but crucially distinct practices.

Firstly, liquidity providers are given the opportunity to accept or reject a deal from a client.

This control allows them to check the price remains valid while also performing necessary client checks to ensure a trade remains within operational risk limits.

However, some liquidity providers also apply an additional artificial hold time before conducting the price check. Different clients are often subject to different AHTs. This fact, alongside holding times longer than is necessary to complete price checks, would appear to run afoul of Principle 17's statement that "*If utilised, last look should be a risk control mechanism used in order to verify validity and/or price.*" It would appear in this instance instead to be an effort on behalf of the liquidity provider to maximise profit while mitigating loss. The IA notes that this will have a negative effect not only on our members as investors, who must therefore re-trade rejected trades at a worse price, but also their clients. The IA therefore views this practice as unacceptable.

The wording in the current guidance simply requires that LP's *"promptly make their decision to accept or reject a trade"*, with no further details on what is meant by "promptly". This ambiguity provides too much lee-way to liquidity providers in how they apply Last Look and in particular AHTs.

The IA therefore asks that the GFXC update the guidance to restrict the use of AHTs, and highlight that Last Look should not be utilised for the purposes of profit optimisation.

Furthermore, our members have raised concerns regarding the use of asymmetric price checks. Clients should be asked their choice as to whether asymmetric price checks can be applied, with symmetric applied as the default.

Pre-Hedging

The IA considers that pre-hedging should really only be viable in extreme trading conditions, for restricted currencies with little data availability, or outside normal trading hours, and should not be permitted for electronic requests.

The IA is concerned about the use of pre-hedging as a tool in normal day to day activity to make prices. Given the abundance of market data available in most currency pairs and the analytics available to traders on the desk in terms of analysing volumes, spreads, volatility, correlations or other factors, there should be little need for traders to pre hedge flow in the modern day.

With regard to the following statement in the guidance:

"The intent of any pre-hedging by the liquidity provider should always be to the benefit of the liquidity consumer and help facilitate the transaction. Any pre-hedging should be done in a manner so that it is not meant to disadvantage the client nor cause market disruption."

The problem is that it is not clear to what extent pre-hedging is done to benefit the client, and it is very difficult to prove, as noted in the guidance itself:

"Intent is a difficult concept to demonstrate. It exists in the mind of a liquidity provider. Similarly, the benefits arising from pre-hedging can be very difficult to show, either ex-ante or ex-post, given the complexity of managing even a large order in the context of an active market making operation. It is also clear that pre-hedging may not always lead to a better out come for the liquidity consumer."

To provide an example, if a market is 10/12, and trader moves the mid to 12 in pre-hedging, the quote will be 11/13, rather than 11/12.5 to account for the fact that the trader has inventory on his book. This negatively impacts the consumer. There is no way of calculating the benefit/price improvement gained from allowing the bank to pre-hedge.

The IA is particularly concerned that the ambiguity contained in the above statement on intent may essentially allow banks an ‘out’, with traders potentially able to argue that any action they take is valid given their own interpretation of client intentions.

If a decision is taken to pursue the use of pre-hedging, it should be only after due consideration that this is the only viable option available.

The IA therefore asks that the guidance around the use of pre-hedging be made much more restrictive.

We would be delighted to discuss further any of the matters raised in our response.

Hugo Gordon
Policy Specialist, Capital Markets

Global FX Code: Draft Working Papers on Pre-Hedging and Last Look (May 2021)

JPMorgan Feedback

Pre-Hedging Paper

JPMorgan is broadly comfortable with majority of the report's 9 sections, but we have suggestions for revision on the following sections:

Section 3: When is pre-hedging potentially applicable (Pg 4 of 17)

Larger FX orders also have heightened conduct and market risk, and therefore should be handled with particular care and attention, and within the overall guidance of the Code, in order to minimize their market impact and ~~achieve best execution for~~ **aim to benefit** the client. This includes setting out clear expectations for their execution, including the guidelines governing any pre-hedging when applicable.

Section 5. Assessing the potential benefit provided by pre-hedging

To assess whether pre-hedging benefits a liquidity consumer, liquidity consumers and providers should regularly review the effectiveness of the execution post-trade to see whether the expected outcome was delivered (see guidelines in Principle 9 and 36).

JPM proposes that this specific text is removed or replaced with text that re-iterates the key points regarding order and execution data retention and availability that are detailed in Principles 9 and 36.

The text as it stands implies an obligation to perform post execution reviews which appears somewhat in conflict with elements of Principle 36 which state that:

'Market Participants should keep an accurate and timely record of orders and transactions that have been accepted and triggered/executed, to create an effective audit trail for review and to provide transparency to Clients where appropriate'

Whilst also stating:

'Information should be made available to Clients upon request, to provide sufficient transparency regarding their orders and transactions to facilitate informed decisions regarding their market interactions'

Also, the assessment of whether an 'expected outcome' was delivered can be very subjective and affected by extenuating circumstances

JPM would suggest that this proposed text is not required in light of the existing Global Code Principle 9 and 36 provisions, and would create confusion for both banks and clients

Appendix 2: Illustrative trading scenarios

Scenario 3: Liquidity consumer asks for a firm bid price in EUR/MXN in large size. The liquidity provider has been running a long USD/MXN position expecting it to go higher, but decides to sell a large part of the position before providing the EUR/MXN quote, with the intent to lock in the P&L on the existing USD/MXN position before the liquidity consumer's trade could negatively affect the USD/MXN market price.

JPM proposes the removal of this specific scenario. The scenario as written creates ambiguity as to when Liquidity Providers are able to manage both their own existing risk positions or other client flows when in receipt of a new client RFQ. It would be preferable to address permissible pre-hedging or risk flattening to better manage the ambiguity.

JPM would propose that the scenario be replaced with a scenario that more specifically covers the Principle 11 elements that refer to Market Participants continuing to conduct on-going business, including risk management, market making and execution of other client orders.

Last Look Paper

JPMorgan is broadly comfortable with majority of the report's 5 sections, but we have suggestions for revision on the following section:

Recommendation 3: Information should be made **available** upon request by Liquidity Consumers **to ~~regularly~~ evaluate the Handling of trade requests**

JPM would propose that the recommendation specify that information should be made available upon request, which is in line with JPM's own disclosures and we would imagine consistent with other liquidity providers.

Principle 17 encourages LCs and LPs to engage in a dialogue regarding the handling of trade requests. As much of the relevant information resides with the LP, LPs should upon request, share ~~be sharing~~ sufficient information for LCs to be able to evaluate their trade execution.

Date: May 31, 2021

To: GFXC Secretariat
Global Foreign Exchange Committee ('GFXC')

Cc: Chair of the GFXC, Guy Debelle

LMAX Group Feedback on GFXC Draft Guidance Paper 2: Last Look

Information about the respondent:

LMAX Group is a global financial technology company and the leading independent operator of multiple institutional execution venues for FX and crypto currency trading. With offices in 9 countries and a global client base, the Group builds and runs its own high performance, ultra-low latency exchange infrastructure, which includes matching engines in London, New York and Tokyo.
The LMAX Group portfolio includes LMAX Exchange, LMAX Global, LMAX Digital.

LMAX Exchange, the Group's institutional FX exchange and an FCA regulated MTF, operates a central limit order book (CLOB) with streaming, no 'last look' liquidity only, supplied by institutional market makers, banks and non-banks.

Trading on LMAX Exchange is governed by the LMAX Exchange Rulebook which does not permit 'pre-hedging' and 'last look' practices, thus ensuring efficient market structure and transparent, precise, consistent execution to all market participants, including funds, banks, proprietary trading firms, brokerages and asset managers.

LMAX Group www.lmax.com

Feedback on GFXC Draft Guidance Paper on Last Look:

1. Introduction

As an operator of a leading institutional FX exchange and the first market participant to commit to the FX Global Code, LMAX Group believes that the FX Global Code has improved standards in the self-regulating FX industry.

Though significant progress has been made with the introduction of the Code, many Market Participants still have diverse opinions and concerns on some industry practices, including the use of 'last look' on public multi-dealer venues. We welcome the committee's consultation process and welcome the opportunity to provide feedback on GFXC Draft Guidance Paper on Last Look.

2. LMAX Group viewpoint on the practice of 'last look':

The LMAX Group view on 'last look' hasn't changed for a decade – we believe it should not exist on public multi-dealer platforms. Although, we recognise that 'last look' may still have its place in the disclosed bi-lateral trading relationships (i.e., bank to specific client) if both counterparties prefer to trade with 'last look'. However, we would always recommend no 'last look' execution, given the complexities and diverse nature of disclosures. LMAX Group believes that ‘last look’ should not exist on public trading venues - it’s a matter of fairness and transparency.

In our view, ‘last look’ creates potential for market abuse, that has already been evidenced by recent scandals and legal investigations for the misuse of ‘last look’ by some of the most reputable global financial institutions. LMAX Group believes that the need for ‘last look’ has become largely obsolete; the technological advancements and availability of real-time streaming market data, enabling instantaneous price checks, have entirely eliminated the need for ‘last look’ as a risk management tool.

The practice of ‘last look’ that doesn’t exist in any other asset class, erodes trust in FX trading at the time when the industry needs to reinstate much-needed transparency and fairness in FX markets. In fact, the support of non-standard and discriminatory ‘last look’ pricing by anonymous multi-dealer platforms, owned by RIEs (Recognised Investment Exchanges) taints the reputation of these RIEs as those responsible for market structure and regulation.

At LMAX Group, we believe we have a responsibility to deliver efficient market structure for our clients.

Our view is that the robustness of the market is diminished by ‘last look’ and the discretionary nature of the duration of ‘last look window’. Fairness is a key element of any market and we believe it’s impaired by allowing pre-hedging during the ‘last look’ window and not requiring Market Participants to pass on price improvement to Clients. Furthermore, liquidity is affected by the resulting *liquidity mirage* and fragmentation enabled by ‘last look’. Finally, openness is deterred by Market Participants having sole discretion over the use of controversial practices.

We’d be happy to engage with the GFXC and fully support the intent but would respectfully disagree with principle 17.

3. *LMAX Group feedback on recommendations in the GFXC draft guidance paper on ‘last look’:*

- **Recommendation 1: ensure a fair and effective ‘last look’ process on public venues**

  Ultimately, LMAX Group is calling for a level playing field, a prerequisite for any efficient market, as well as standardisation across public exchanges as a minimum.

  The outlined principles of fairness and effectiveness around the use of ‘last look’ practice are a good first step, but we would argue these proposals do not go far enough. If ‘last look’ is to exist on public multi-dealer venues, we would suggest that there should be a standardised rulebook for all counterparties.

  The recommendation to LPs to minimise hold time also does not go far enough. We would argue that hold time needs to be standardised and minimised to the time required for a price check; and of course, LPs need to guarantee confidentiality of rejected trade information.

  Finally, we believe discretion should be removed from Market Participants on how they treat price changes, resulting from market fluctuations during ‘last look’ window, and require them to pass the full price improvement on limit orders to Clients, in exactly the same way price slippage is treated.

- **Recommendation 2: Enhance ex-ante disclosures for public venues**

  Whilst well intentioned and absolutely correct for bi-lateral trading relationships, the recommendation to enhance ex-ante disclosures for public multi-dealer trading venues is misguided and transfers the complete responsibility on the Client for understanding ‘last look’ related disclosures (driven by the sole discretion of the Market Participant). This is all without removing the conflict of interest between the two parties and without equipping the Client with capabilities and tools to have an informed dialogue with the Market Participant. As a result, draft guidance reinstates sole control over execution with Market Participants and doesn't contribute to levelling out the playing field between Market Participants and the Clients.

- **Recommendation 3: Information should be available to regularly evaluate the handling of trade requests**

  Whilst we would welcome added disclosure, we would suggest the additional administration burden might not have the desired effect. In most cases, we would expect market participants to keep a record of all trades (inc. rejected trades) in any case.

4. Summary of LMAX Group feedback

In summary, our view on 'last look' has not changed. We are supportive of the Global Code and the efforts the industry is taking to enhance regulation, but we would view these latest draft guidance as not going far enough to protect the interests of all stakeholders for public multi-dealer execution venues.

If 'last look' is to exist on public multi-dealer execution venues, we would strongly recommend that a standardised rulebook be drawn up for all market participants, rather than the scatter gun approach we currently have. That being said, whilst we can understand why 'last look 'might be employed on a bilateral basis between consenting parties, we would strongly support the removal of last look in public execution venues.

We would recommend the guidance paper should update its recommendations to include specific standards around the use of last look. We believe that setting standards around the following parameters and processes should be 'quick wins':

- Standardised hold time – establish a norm around the time needed for pre-trade price checks
- Rules around LPs using the 'rejected order' information for their own trades should be standardised across the market
- Symmetrical application of price check, which we believe should be easy to implement

APPENDIX I

LMAX Group Feedback on Last Look practices in the Foreign Exchange Market (viewpoint submitted in 2017)

Response to Specific Consultation Questions:

As the first market participant to commit to the FX Global Code, LMAX Exchange welcomes the opportunity to provide feedback on Last Look practices in the Foreign Exchange Market.

Though the FX Global Code is a positive starting point for restoring trust in the FX industry and creating globally consistent guidance, LMAX Exchange doesn't believe that the Code goes far enough on restricting or banning the potential market abuse that can result from the use of 'pre-hedging' and 'last look', in its wording of Principle 17.

Questions: Principle 17 of the Code states that "*During the last look window, trading activity that utilises the information from the Client's trade request, including any related hedging activity, is likely inconsistent with good market practice because it may signal to other Market Participants the Client's trading intent, skewing market prices against the Client, which (1) is not likely to benefit the Client, and (2) in the event that the Market Participant rejects the Client's request to trade, constitutes use of Confidential Information in a manner not specified by the Client".*

LMAX Exchange agrees that any trading activity, utilising the Client's order information, during the 'Last Look' window does not benefit the client and at the very least, constitutes use of confidential information in a manner not specified by the client. Furthermore, we are not aware of any situation or scenario where pre-hedging during the 'Last Look' window can be beneficial to the client or where clients benefit from skewed market prices against their orders, caused by information leakage during the 'Last look' window.

The current wording in Principle 17 effectively legitimises pre-hedging, which could stand accused as front-running during the 'Last Look' window. Legitimate working of a client order will be indistinguishable from unethical front-running for pure profit-making utilising privileged Client's order information. Front-running is considered 'unethical practice' in capital markets, defined as *'unethical practice whereby someone with advance knowledge of a specific market order in, say, shares, bonds or a currency from a client steps in ahead and buys for their own account. When the client's usually much larger order is executed and drives up the price, the private purchase can be sold at a profit'*. Thus, if front-running is acknowledged as 'unethical' across all asset classes, why isn't there a stronger stance in the Global Code on pre-hedging activity during the 'last look' window?

Thus, as a direct response to the consultation questions, LMAX Exchange recommends removing **'likely'** from **'likely inconsistent with good market practice'** in the wording of Principle 17, referring to 'any hedging activity during the last look window utilising the information from the Client's trade request.

Longer-term, LMAX Exchange believes that the Code should ban 'last look' at least on anonymous multi-dealer trading venues; it can be argued that the practice may still have its place in the disclosed bi-lateral trading relationships (i.e., bank to specific client), if both counterparties prefer to trade with 'last look'. Banning 'last look' will avoid any potential for market abuse, that has already been evidenced by recent scandals and legal investigations for the misuse of 'last look' by some of the most reputable, global financial institutions. LMAX Exchange believes that the need for 'last look' has become obsolete; the technological advancements and availability of real-time streaming market data, enabling instantaneous price checks, have entirely eliminated the need for 'last look' as a risk management tool. The practice of 'last look' that doesn't exist in any other asset class, erodes trust in FX trading at the time when the industry needs to reinstate much-needed transparency and fairness in FX markets.

LMAX Exchange viewpoint on the practice of 'last look':

1) Advances in trading technology have replaced the need for 'last look' with more superior risk management tools:

The practice of 'last look' is a legacy business solution to an historic technology problem. As is the case now, market makers reasonably wanted to protect themselves against sudden fluctuations in the market (as described in Principle 17 of the FX Global Code of Conduct[1]) when they didn't have robust technology to stream prices without introducing enormous amounts of new market risk into their businesses. At the time, the obvious patch for the shortcoming in technology and the continued desire to responsibly manage risk while at the same time increase the breadth of the business' market making reach, was to introduce what is now known as 'last look'. Today, the same financial institutions have invested greatly in people, technology platforms, and electronic trading is no longer a small offshoot of a bank's core FX business it is the core FX business. This attraction of resources and advances in technology platforms across the marketplace, also calls for the evolution of market standards and best practices.

Our view is clear at LMAX Exchange. We can process over one hundred million orders per day, cancel and replace orders in sub-one-hundred microseconds, perform seven million real time risk calculations per second, and conduct pre-trade credit checks instantaneously. Technology has moved on dramatically, and the same needs and rationalisations for 'last look' are no longer the same.

In today's environment, we feel it creates an uneven playing field biased against clients, whether they are cognisant of it or not, and equally as important, against financial institutions who are trying to create a new market order with greater transparency and equality, yet are forced to compete with those who are not yet willing or mandated to do so. It can be a very daunting task if not every market participant operates to the same level of standards.

LMAX Exchange is not a proponent of 'last look' for numerous reasons, including the possible abuses and optionality that it introduces into pricing. LMAX Exchange, along with a small handful of other venues, is demonstrable proof that trading without 'last look' is a wholly viable option for both market makers and the clients who take their liquidity. Moreover, by doing so, these participants disassociate or distance themselves from a practice which is open to abuse, while at the same time improving both the transparency and quality of execution in the market place. This is not a transition that takes place overnight, but sooner, rather than later, market participants will have to accept the mature, transparent nature of the foreign exchange market and its place and status with other mature asset classes and their markets and realise the practice of 'last look' is no longer defensible.

2) 'Last look' creates a disorderly market and liquidity mirage in the anonymous multi-dealer execution environment:

Though LMAX Exchange believes the need to use 'last look' has become obsolete, it can be argued that the practice may still have its place in the disclosed bi-lateral trading relationships (i.e., bank to specific client), if both counterparties prefer to trade with 'last look'.

The situation is different on anonymous multi-dealer platforms, where clients are trading on anonymous quotes streaming from multiple LPs, each using 'last look' according to their own discretion. Furthermore, 'last look' on multi-dealer platforms allows LPs to quote more venues

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[1] Principle 17, p.21 *'..last look is a risk control mechanism used in order to verify validity and/or price. The validity check should be intended to confirm that the transaction details contained in the request to trade are appropriate from an operational perspective and there is sufficient available credit to enter into the transaction contemplated by the trade request. The price check should be intended to confirm whether the price at which the trade request was made remains consistent with the current price that would be available to the Client'*

than they are willing to fill, causing a liquidity mirage and increased fragmentation, in turn leading to disorderly markets.

3) ***The 'last look' practice significantly diminishes the trader's control over execution quality and costs, thus creating opportunities for market abuse and undermining any regulatory initiatives aiming to impose stricter controls over execution factors:***

Discretion over the LP's use of 'last look' and its consequences on the trade execution quality have been evidenced in our recent white paper 'TCA and fair execution. The metrics that the FX industry must use'. The paper, containing the analysis of the independent data set of over 7 million trades (both firm and 'last look' liquidity), revealed the significant level of discretion used by 'last look' liquidity providers regarding:

- The length of 'last look' window or discretionary hold time before order execution – constituting one of the most significant hidden trading costs (e.g., 100 milli-seconds of hold time can cost the client up to $25/million[2])

- The bias in passing the underlying market behaviour on limit-orders to clients – our analysis demonstrated that clients trading on 'last look' liquidity were not getting the full price improvement, costing them up to $40/million[3] in unrealised value from price improvement

Such discretion highlights the potential for market abuse of 'last look' – for detailed analysis, please refer to Appendix I, containing selected chapters from the LMAX Exchange white paper 'TCA and fair execution. The metrics that the FX industry must use'.

Furthermore, the level of discretion that LPs have over the order during the 'last look' window makes it impossible for trading institutions to have sufficient control over execution quality, in turn undermining any regulatory efforts that impose stricter levels of responsibility on traders for achieving best execution.

To this extent, we believe that in the context of 'last look' liquidity MiFID II best execution standards are unattainable for the buy-side. Only when trading on firm liquidity, the buy-side participants are able to 'take all sufficient steps' to obtain best possible results for execution factors such as price, costs, speed, likelihood of execution and settlement, size and nature of the trade[4].

4) ***Ongoing scandals and investigations related to the abuse of 'last look' provide further evidence that the practice is misused and in turn deters trust in the FX marketplace:***

Asymmetrical application of 'last look', failure to pass fully and transparently price improvement to clients as well as consistent use of pre-hedging during 'last look' window are examples of 'last look' abuse in the recent scandals and ongoing investigations:

- Barclays Bank fined $150m for abuse of 'Last Look' by the NYDFS (November 2015)
- Legal claim by NFA brought against FXCM and Effex Capital (February 2017)
- Legal claims filed by Alpari (US) against 6 banks for abuse of 'Last Look' (July 2017)

5) ***Not banning or taking a stricter stance on 'last look' diminishes the Code's intentions:***

The Code's intentions are stated as follows: *'to promote a robust, fair, liquid, open, and appropriately transparent market in which a diverse set of Market Participants, supported by resilient infrastructure, are able to confidently and effectively transact at competitive prices that*

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[2] 'TCA and fair execution. The metrics that the FX industry must use', Part II - Quantifying the cost of hold time, p.60-63
[3] 'TCA and fair execution. The metrics that the FX industry must use', Part II - Quantifying the value of price improvement, p.50-55
[4] MiFID II Best Execution obligation

reflect available market information and in a manner that conforms to acceptable standards of behaviour'.

Our view is that **robustness** of the market is diminished by 'last look' and the discretionary nature of the duration of 'last look window'; **fairness** is impaired by not banning pre-hedging during the 'last look' window and not requiring Market Participants to pass on price improvement to Clients; **liquidity of the market** is affected by liquidity mirage and fragmentation, enabled by 'last look'; **openness** is deterred by Market Participants having sole discretion over the use of controversial practices.

- **The use of 'last look' at a sole discretion of a Market Participant creates conflict of interest with the Client and takes away from the Client control over execution quality and trading costs.**

  The Code rightfully states that during the 'last look' window the Client is left with 'potential market risk in the event the trade request is not accepted'. Since this is a substantial risk, the Code needs to elaborate on the benefits for the Client to trade with 'last look' and make it obligatory for the Market Participant to pass on all the benefits that may arise from 'last look' execution to the Client. To this extent, the Code needs to raise awareness of different types of liquidity available, firm and 'last look', and provide examples and guidance to help Clients make informed choices when selecting the appropriate liquidity for their trading strategies.

- **Standardised application of price improvement vs price slippage to Client limit orders needs to be enforced on 'last look' liquidity.**

  The Code needs to take a strong stance that Market Participants are required to pass full price improvement, resulting from market fluctuations during 'last look' window to the Client, in the same way as they treat price slippage. By not giving full price improvement on a 'last look' stream, though fully disclosed, the Market Participant is disadvantaging the client, which contravenes Principle 8.

- **Monitoring and enforcing 'correct use' of information from the Client's trade request during the 'last look' window is close to impossible on multi-dealer platforms.**

  Information about the Client's order, in advance of 100% execution, is valuable and open to abuse. Even if the information is not used for hedging activity, it can be used for future pricing by Market Participants (i.e., determining, spreads, fill ratios, hold time).

  Principle 17 proposes, as a good market practice, that Market Participants engage in a dialogue regarding the handling of their trade requests with Clients. This proposal is constructive and relatively easy to implement and enforce in bi-lateral disclosed trading relationships. Unfortunately, on multi-dealer platforms where Clients are trading on 'last look' liquidity streaming from many different LPs (each with different disclosures about the use of 'last look') and where information is passed around in milliseconds / or even micro seconds, it becomes very difficult, if not impossible, for Clients to monitor whether their trade requests are treated in accordance with disclosures and confidentiality.

  Furthermore, the encouragement of the dialogue between the Client and the Market Participant is too reliant on the following assumptions about the FX marketplace:
  - Lack of conflict of interest between Market Participants and the Clients;
  - Open access for every Client, whether big or small, to have the same dialogue with every Market Participant, who may be pricing their orders;
  - Full awareness and understanding by Clients of all available execution alternatives and the associated trading costs for each alternative.

  Unfortunately, the FX marketplace doesn't operate in accordance with the above assumptions:
  - Until Market Participants are required to pass full price improvement, when using 'last look', to the Client, the inherent conflict of interest exists between the two parties;

- Unless there is standardisation of the use of 'last look' by LPs for each specific multi-dealer venue, it's impossible for all clients to have similar information access to LPs' disclosures and to have the same access to each LP to discuss individual disclosures;
- Finally, in the context of the OTC-traded FX marketplace that operates without centralised pricing benchmarks, the only way clients can make informed choices about the liquidity source for their execution strategy is to conduct FX Transaction Cost Analysis (TCA). Compared to equities, FX TCA methodology is still in its infancy - it doesn't address differences between execution costs on firm vs 'last look' liquidity and it hasn't reached sufficiently wide adoption by the marketplace to become a useful blueprint for Clients in their dialogue with Market Participants.

Effectively, Principle 17 places the complete responsibility on the Client for understanding 'last look' and 'pre-hedging' related disclosures (driven by the sole discretion of the Market Participant), without removing the conflict of interest between the two parties and without equipping the Client with capabilities and tools to have an informed dialogue with the Market Participant. As a result, Principle 17 reinstates sole control over execution with Market Participants and doesn't contribute to levelling out the playing field between Market Participants and the Clients.

Detailed Recommendations:

Short-term:

- Remove **'likely'** from **'likely inconsistent with good market practice'** in the wording of Principle 17, referring to 'any hedging activity during the last look window utilising the information from the Client's trade request;

- Remove discretion from Market Participants on how they treat price changes, resulting from market fluctuations during 'last look' window, and require them to pass the full price improvement on limit orders to Clients, in exactly the same way price slippage is treated;

- Raise the level of awareness of execution alternatives for the Clients and promote a standard set of metrics that Clients can use to calculate total trading costs for each alternative. For this, the FX TCA methodology needs to be developed to capture a comprehensive set of metrics that measures execution quality across both firm and 'last look' liquidity. The development of such FX TCA methodology needs to be an industry-wide initiative, intended to equip Client with the ability to make informed choices and have dialogues with Market Participants about the use of 'last look' on a level playing field. LMAX Exchange has made some headway in developing FX TCA methodology able to capture the nuances both liquidity pools (*see the latest TCA white paper*). LMAX Exchange would welcome cooperation from industry participants to develop the methodology further and would be happy to contribute to any industry-wide activity targeted at educating the marketplace about execution alternatives.

Longer-term:

- LMAX Exchange believes that once 'pre-hedging' is forbidden during the 'last look' window and Market Participants have to pass full price improvement to Clients, the practice of 'last look' will cease to exist by itself, as in today's electronic FX marketplace which operates in micro-seconds, Market Participants have much more superior risk management tools than 'last look';
- However, if the conflicts of interest between Market Participants and Clients, inherent in current wording of Principle 17, are not addressed, it would be a far more efficient use of industry/regulatory resource to ban 'last look'. Eliminating potential for abuse whilst insuring fair and transparent treatment is to not allow either 'pre-hedging' or 'last look'.

The Moscow FXJSC feedback to the Global FXC, May 2021

Feedback on draft guidance papers for the practices of of 'pre-hedging' and 'last look”.

Dear Global FX Committee,

After publication of Request for Feedback and reading the discussion of the papers in the public domain The Moscow FXJSC gathered for video conference to discuss whether the guidance and recommendations within the draft papers appropriately cover the issues relevant to these principles.

The “Pre-Hedge” guidance gives a good explanation of the matter especially with illustrative examples to separate hedging and pre-edging activities which are often mixed due to trigger nature of firm orders places with liquidity provider. However due to the requirement that Pre-hedging must be designed to benefit the Client and considering that it’s very difficult to prove the benefit we support the recommendation to avoid pre-hedge if possible. So, we would like to add that FX Code could be prescriptive that “**by default” settings of liquidity provider must be “to not use pre-hedge of clients anticipated orders”.** We think that the only legitimate way of using any pre-hedge activity is to get the explicit liquidity consumer consent for that.

We also would like to raise the concern that there is a need for special guidance paper for hedging of limit orders. As it was mentioned in the paper “*For limit orders that do not allow for any liquidity provider discretion to execute, any transactions conducted ahead of the trigger raise more serious conflict of interest concerns. Depending on the jurisdiction, these conflicts may also present concerns about unlawful front-running. Given this increased concern with limit orders, liquidity consumers and providers should be clearly aligned whether discretion will or will not be applied, desired, or expected*”. We are totally agreed with the point, and we feel that FX Global Code principals are not enough for the coverage of this most important matter.

The Last Look guidance started a very sound discussion. We are generally agreed on the recommendations provided in the paper:

Recommendation 1: Ensure a fair and effective last look process

Recommendation 2: Enhance ex-ante disclosures

Recommendation 3: Information should be available to regularly evaluate the handling of trade requests.

Additionally, we would like to suggest including clear recommendation that “**by default” settings of liquidity provider must be “to use symmetrical last look”.** We think that the only legitimate way of using asymmetrical last look is to get the explicit liquidity consumer consent for that.

We think that usage of additional holding time (AHT) is not appropriate by default and must be clearly articulated to the client before application. So, **by default” settings of liquidity provider must be “to not apply and additional holding time”.** If a client would like to get tighter spreads in return for the right for LP to use AHT then he needs to get explicit liquidity consumer consent for that.

We think that disclosures must be organised in such a way that they can be used by ECNs to let liquidity consumers choose liquidity providers with the proper last look setup. For example, there must be short and clear questionnaire as example:

1) Do you apply additional holding time?

2) If yes, what is the maximum holding time you apply to client orders?

3) Is the last look on your side symmetrical or asymmetrical?

4) Do you use client order information within the last look window?

5) Do you practice cover and deal?

.

Draft Guidance Paper: Last Look

As a signatory of the FX Global Code of Conduct, NAB welcomes and supports its valuable role in establishing a harmonised set of expectations and standards for the FX market. The periodic refresh of the code is significant to allow for continual refinement of the guidance in response to evolving market concerns and practices.

It is our view that last look plays an important role in FX market functioning given the highly dispersed set of execution venues, but comes with the potential for misuse, which has been the subject of regulatory enforcement in recent years. It is therefore imperative that the FX Global Code provides enough guidance for participants, both liquidity providers and consumers, to achieve a common understanding of what is deemed acceptable in principle and in practice. Whilst for the large majority of participants the detailed nuances of last look may not be a significant factor in choosing where or with whom to deal, knowing that their liquidity providers have attested their adherence to the FXGC should give meaningful assurance that they are being treated fairly regardless.

The draft updated guidance on last look issued proposes three recommendations. NAB agrees with the increased emphasis on fairness as the central principle in the implementation of any last look, which we consider requires any price tolerance check to be symmetrical in favour of either party, and the response should not build in extended delays. We believe that there should be some further clarification for the industry around how to interpret the term “promptly” with regard to the guidance on the last look duration, to achieve consistent practices that are fair to all liquidity consumers and maintain a level playing field for liquidity providers. NAB also agrees with the improved disclosure guidance to ensure the key fairness and quality factors of each maker’s last look practices are clear, as well as the sharing of detailed data available upon request.

NAB supports the publication of the Code to provide clear guidance on Last look’s purpose and acceptable utilisation to ensure interpretation across the industry is consistent to prevent abuse. Whilst the revised guidance strives to articulate a fair and effective last look process, it would benefit further by better resolving the ambiguity on the treatment of delayed responses which allows participants to potentially utilise Last look as a mechanism to manage profitability rather than a control mechanism to verify validity and/or price.

Draft Guidance Paper: Pre-Hedging

NAB supports the draft guidance on pre-hedging as it provides the necessary detail including scenarios on the appropriate use of pre-hedging in today’s market. The paper clearly explains (i) what is pre-hedging (ii) when it can be used, and (iii) the potential impact it can have on prices quoted to the market and the end consumer.

Feedback on:

1) **Pre hedging.**
The guidance and recommendations in the draft papers appropriately covers the issues on handling of RFQs, Orders and Controls frameworks. However, pre-hedging related disclosures, client communication and coming up with "comprehensive agreements before transacting," may prove challenging.

2) **Last Look.**
The guidance on conducting validity and price checks is covered adequately. Recommendations to ensure fair and effective last look process; without a prescriptive application of additional hold time (AHT) is a practical approach.

The recommendations within both the draft papers cover the issues relevant to Principles 11 and 17.

Pre-hedging

Whist we agree and support the proposed guidance of the paper, we are keen to have further guidance on the specifics of hedging an FX Option (or any other illiquid product) over a certain period and how we should treat requests for similar products or trades in this time frame.

Last Look

On Page 9;
"A consistently strong market reaction that occurs when dealing with a specific LP may be an indication of undesirable information leakage or a suboptimal hedging strategy by the LP."
We believe the wording ""suboptimal hedging strategy" should not be used in this paper. The "suboptimal" being very vague and not referring to a definition of what an "optimal hedging strategy" would be. The hedging strategy is the LP decision and has no link with the Last Look topic addressed by this document.

UBS AG London Branch
5 Broadgate
London, EC2M 2QS

www.ubs.com

May 27, 2021

UBS Feedback on GFXC Last Look Guidance Paper

As requested by the GFXC, we wanted to submit feedback on the Last Look Guidance Paper which we feel is in a good place and adequately covers and addresses the main points relating to this complex topic.

While the paper in its current form does not present any fatal flaws for UBS, we wanted to note one point relating to the Price Check section of the paper.

As written, the paper seems to imply that a price improvement mechanism can only apply under an asymmetric application of Last Look, as evidenced by the following sentence:

"Relatedly, some LPs may utilize a price improvement mechanism, such that the LP will accept the LC's trade request at an improved price in cases where the market has moved in favor of the LP, rather t han rejecting the trade."

The important word here is "relatedly" as it explicitly links the price improvement mechanism to the asymmetric last look framework described earlier in the paragraph.

However, we note that a price improvement mechanism can also be applied to a symmetric last look framework whereby trades are rejected if prices have moved against the LP, but are accepted at an improved rate for the LC if they have moved in favor of the LP. The net outcome of a price improvement framework is the same if it is applied to either an asymmetric or a symmetric last look framework.

Consequently, we would suggest that the above sentence be presented as a standalone paragraph at the end of the Price Check section and that the word "Relatedly" be either removed completely, or replaced with the word "Furthermore".

Should you have any further questions, please contact Adrian Boehler, Global Head of FX Distribution on the following email address: adrian.boehler@ubs.com

Vanguard

May 28, 2021

Secretariat
Global Foreign Exchange Committee

Dear Secretariat,

Vanguard appreciates the opportunity to provide feedback to the Global Foreign Exchange Committee (GFXC) in response to the Request for Feedback on the “Last Look” Guidance Paper (Guidance Paper).

At Vanguard, our mission is straightforward: To take a stand for all investors, treat them fairly, and to give them the best chance for investment success. While we would prefer that the practice of “last look” not exist in the FX market, we believe that there is significant room for improvement in transparency and disclosure around the “last look” practice. The recommendations contained in the Guidance Paper are a step in the right direction, but leave room for further enhancement in pursuit of greater transparency and disclosure. Examples of potential additions to the Guidance Paper which would further improve transparency and disclosure include requiring:

- the use of “plain talk” disclosures
- that disclosures are made on an annual basis
- adoption of standardized client reporting on a regular basis that includes the percentage of orders, notional amount and estimated slippage/impact for any orders subject to “last look”
- that Liquidity Providers explain why asymmetric price checks are utilized (if applicable)
- an independent attestation to the effectiveness of controls related to “last look”

We commend the GFXC for its continued efforts to improve FX markets for investors. Please feel free to contact us with any questions regarding our comments.

Vanguard
Michael Eyre, CFA
Global Head of FX Trading

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28 May 2021

GFXC Secretariat
Global Foreign Exchange Committee(“**GFXC”**)

Dear GFXC Secretariat,

As a price maker and price taker in the foreign exchange market, Westpac Banking Corporation has last look functionality for the purposes of credit checks, regulatory, integrity and latency checks. It does not use the concept of ‘hold time’.

In response to the **Request for Feedback on the Draft Guidance Paper 2: Last Look.**

We reiterate our feedback from September 2017:

> To facilitate electronic trades, “last look” for checking of credit, regulatory checks, integrity (i.e. dealing on the price that represents the correct price for that volume and date) and for genuine latency in dealing between price maker and client (including client ECN portals) needs to take place to ensure the robustness of the end to end process. “Hold times” as defined by adding a time buffer to understand if the trade will be profitable, is a practice we do not support.
>
> Hold times is an activity that does not benefit clients. If price makers believe they need hold times to facilitate trading then there is the alternative option of widening the price. Currently hold times gives the price maker a ‘free-option’ that is to their benefit over the client and the rest of the market i.e. quote tighter, win the deal, reject if unprofitable rather than pricing appropriately and potentially not winning the deal in the first place to another price maker who does not have hold times but a better implied rate when rejection rates are taken into account.

The current guidance paper does not address the issue of hold times. Firstly, regarding Recommendation 1: Ensure a fair and effective last look process, we suggest the following wording be amended from:

- During the last look window in which an LP is conducting its checks, the LC is potentially exposed to market risk as the market price may move prior to acceptance, and there is also the possibility that their trade request will be rejected altogether. In the interest of fairness, LPs should aim to minimize this period of uncertainty for the LC and therefore LPs should promptly make their decision to accept or reject a trade. As stated in Principle 17, “the price check should be intended to confirm whether the price at which the trade request was made remains consistent with the current price that would be available to the Client”.

To:

- During the last look window in which an LP is conducting its checks, the LC is potentially exposed to market risk as the market price may move prior to acceptance, and there is also the possibility that their trade request will be rejected altogether. In the interest of fairness, LPs should aim to minimize this period of uncertainty for the LC and therefore LPs should make their decision to accept or reject a trade with no delay. As stated in Principle 17, “the price check should be intended to confirm whether the price at which the trade request was made remains consistent with the current price that would be available to the Client”.

The word “promptly” is ambiguous, as it can be defined to mean with “little or no delay”. Our view is that a price check should occur with no delay once all last look checks have been completed, as per our above stated view on the practice of hold times.

Secondly, Recommendation 2: Enhance ex-ante disclosures, we suggest the following wording be amended from:

- LPs should disclose information about the expected length of the last look window to their LCs

To:

- LPs should disclose if they use a hold time, as well as information about the length of the hold time to their LCs

We do not believe that requiring LPs who do not use hold times to provide the expected length of the last look window is relevant to the intent of the code as it compares completing last look checks as quickly as systematically possible to pre-defined hold times. This recommendation, in its current form, gives the impression that hold times are within best practice for last look which we do not agree with.

Yours Sincerely,

Vanessa Bailey
Director, eFICC & Execution
Westpac Institutional Bank

On behalf of,

Emma Norman
Global Head of eFICC & Execution
Westpac Institutional Bank

To: Global Foreign Exchange Committee ("**GFXC**")

28 May 2021

Dear Sirs

RE: GFXC Request for Feedback: Last Look

XTX Markets Limited ("**XTX**") welcomes the opportunity to provide feedback to the GFXC in respect of draft guidance to the Global FX Code (the "**Code**") relating to last look. XTX is an adherent to the Code and strongly supports its principles, and the work of the GFXC, in promoting the integrity and effective functioning of the wholesale foreign exchange market. XTX was actively engaged in the development of the Code and has played an active part in submitting its views on last look to the GFXC working group.

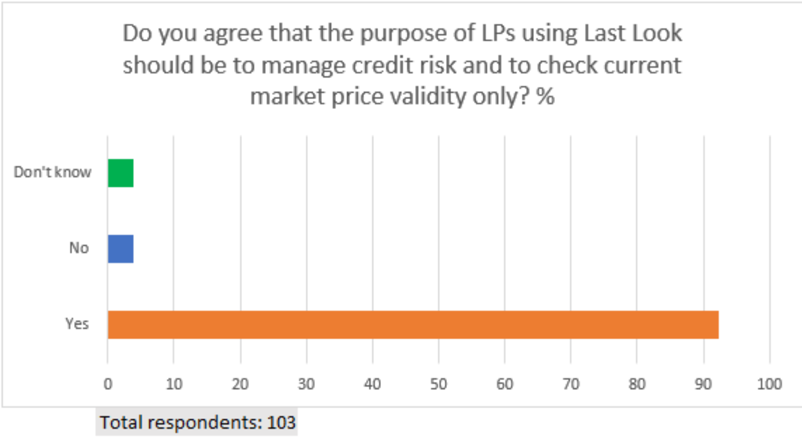
We understand that the purpose of the last look guidance paper is to provide clarity around the use of last look and to promote a wider knowledge and understanding of the appropriate application of last look as a practice. However, there is a fatal flaw with the paper: the fundamental question of 'what is the purpose of last look in respect of the price check?' has not been addressed. There are two differing views in the market in respect of this:

1. A risk control mechanism used by liquidity providers to verify that the price at which the trade request was made remains consistent with the *current* price available to that client.

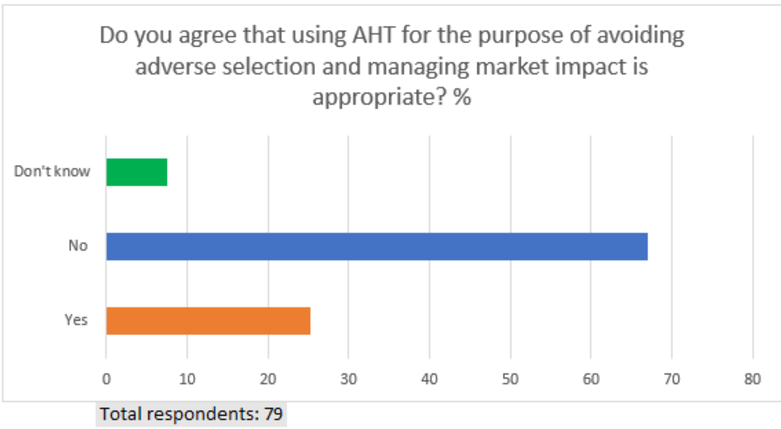
2. A profit optimisation mechanism whereby liquidity providers may add an additional hold-time prior to performing a price check for the purposes of determining "adverse selection" or "market impact", whereby the acceptance/rejection logic is based on the *future* development of prices for that client.

XTX strongly believes that last look should only be used as a risk control mechanism and that any use of last look for profit optimisation is inconsistent with Principle 17 of the Code. With reference to actual client data, the enclosed last look paper published by XTX shows that there are some major liquidity providers who use last look for profit optimisation implying that the current wording of Principle 17 can be widely interpreted. It also shows the costs to a client of its flow being managed in this way. Principle 17 of the Code states: *"A Market Participant should be transparent regarding its last look practices in order for the Client to understand and to be able to make an informed decision as to the manner in which last look is applied to their trading*". The paper evidences that this is not currently the case.

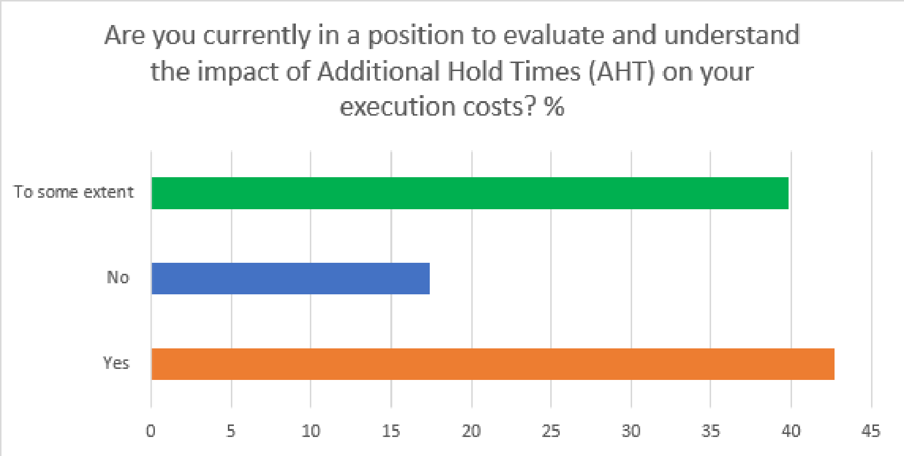
We have strongly encouraged our buyside clients to sign their adherence to the Code and provide feedback via the public comment process. Some do intend to provide feedback but many are prevented from doing so due to internal policy constraints or time constraints due to the short feedback period. As it is vitally important for this consultation to reflect views from all market participants, we conducted an anonymous survey of our clients. The survey was sent to XTX's client base consisting of 250 global institutions who in aggregate trade tens of trillions of dollars of spot FX annually. We received 103 responses from 101 different institutions, 46% based in EMEA, 23% based in the Americas and 31% based in the Asia Pacific region. In terms of institution type, 35% of the respondents were banks, 17% were hedge funds, 8% were asset managers, 12% were retail aggregators or brokers and 28% were other institutions (e.g. non-banks, brokers etc). Therefore, the results of this survey reflect the view of significant market participants from all regions and sectors in the wholesale FX market. The results of the survey are as below:



An overwhelming majority of respondents are of the view that last look should be used only as a risk control mechanism i.e. option 1 outlined at the beginning of this response. As evidenced in our paper, this is not how a number of liquidity providers are using last look (option 2 outlined at the beginning of this response).

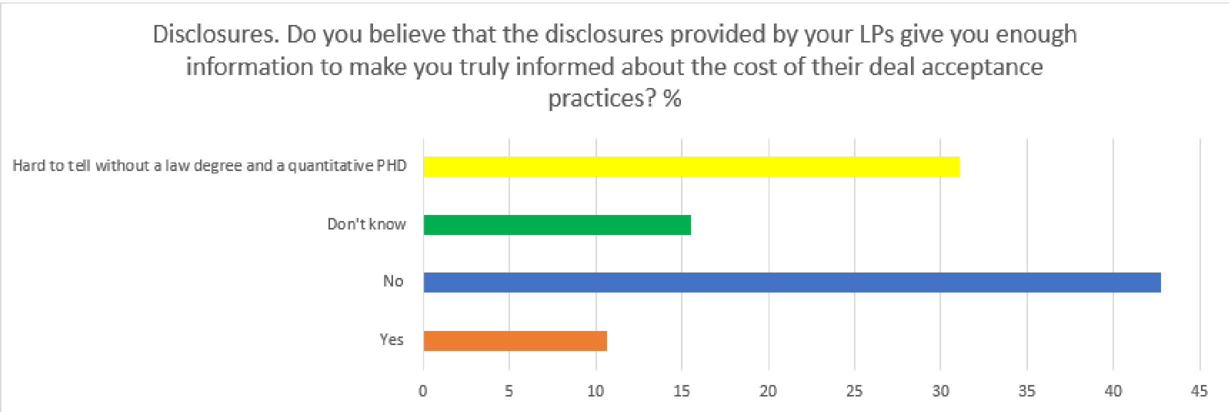


A significant majority of respondents are of the view that Hold Times should not be used for the purpose of avoiding adverse selection and managing market impact. As evidenced in our paper, a number of liquidity providers are using last look for these purposes (option 2 outlined at the beginning of this response).



Total respondents: 103

The majority of respondents were not in a position to fully evaluate and understand the impact of Hold Times on their execution costs.



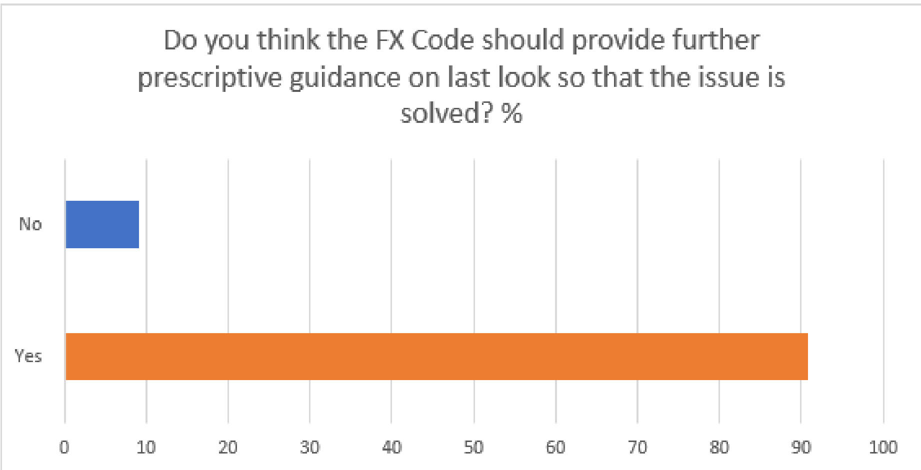
Total respondents: 103

Do you agree that the following items should be specifically disclosed by LP's?

	Answers	Responses (%)
1. Client specific AHT	Yes	95
	No	3
	Don't know	2
Total respondents: 102		
2. The use of any such AHT to manage market impact and adverse selection		
	Yes	92
	No	3
	Don't know	5
Total respondents: 103		
3. The maximum and minimum AHT applied to that LP's clients		
	Yes	87
	No	5
	Don't know	8
Total respondents: 103		
4. Changes in a client's hold time should be disclosed via a specific notification		
	Yes	89
	No	6
	Don't know	5
Total respondents: 102		

The majority of respondents believe (1) they do not have sufficient disclosures from their liquidity providers to make an informed decision about the use of last look on their trading; and (2) liquidity providers should be making further disclosures around their use of additional hold times and the purpose of last look.

This very clearly indicates that market practices and disclosures are not meeting the standard required by Principle 17 of the Code i.e. "*A Market Participant should be transparent regarding its last look practices in order for the Client to understand and to be able to make an informed decision as to the manner in which last look is applied to their trading*". Only 11% of respondents felt that that they had sufficient disclosures regarding last look practices.



Total respondents: 98

The vast majority of respondents believe that the draft guidance does not go far enough and that the GFXC needs to provide more prescriptive guidance as to the use and purpose of last look. This echoes the results of the GFXC's own survey in 2019 which highlighted Principle 17 / last look as the topic most respondents wanted to see amended[1].

The message from XTX and our clients is clear: there is continuing frustration around the lack of clarity and detail on the purpose and application of last look. Clients do not have enough information to make an informed decision as to how last look is being used by their liquidity providers and fully evaluate the associated execution costs. The industry needs further transparency, clarity and detail on the purpose and application of last look. Without such clarity, potential conduct issues remain around the use of last look; issues that were intended to be resolved by the Code.

The issues can be resolved by adding the following to the guidance, as outlined in further detail in the "Conclusions" section of our paper:

- Adding the following sentence, to provide clarity on the purpose of last look: "Last Look should not be used for the purpose of profit optimisation such as managing adverse selection or market impact";

- Hold Times should be zero or as short as is technically feasible for a single price check to verify the price matches the liquidity provider's prevailing rate and risk limits;

- Hold Times to be consistent across all clients based explicitly on median tick to trade. See page 29 of our paper for some suggested language); and

- All Hold Times to be clearly disclosed to each client as it applies specifically to them, including clients being notified of any changes made to Hold Times.

Thank you for the opportunity to comment. Please do not hesitate to contact us if you would like to discuss further. We are also willing to participate in any further GFXC working groups convened to discuss last look and/or the feedback in relation to the guidance paper.

Yours faithfully

Z Y Amrolia

Zar Amrolia
Co-CEO
XTX Markets Limited

[1] Question 21(b): https://www.globalfxc.org/docs/gfxc_survey_results_Jan20.pdf

XTX MARKETS

LAST LOOK MYTHS DEBUNKED

MAY 2021

LAST LOOK: A LONG LOOK

There is now a public commentary period[1] around the topic of Last Look at the three year anniversary of the FX Global Code[2].There is a general feeling in the industry that the issue of Last Look has been dealt with via disclosures and the issue has been sorted. However, as this paper will argue, there is further improvement that the industry can make around this topic.

Principle 17 of the FX Code states that Last Look can only be used for the purposes of risk control:

> *"If utilised, last look should be a risk control mechanism used in order to verify validity and/or price. The validity check should be intended to confirm that the transaction details contained in the request to trade are appropriate from an operational perspective and there is sufficient available credit to enter into the transaction contemplated by the trade request. The price check should be intended to confirm whether the price at which the trade request was made remains consistent with the current price that would be available to the Client."*[3]

However, because of the lack of a precise definition of Last Look, different industry participants have interpreted the FX Code in different ways and Last Look is still utilised by some Liquidity Providers ("LP's") for the purposes of managing "market impact" and "adverse selection" (i.e. profit optimisation) across many venues and bilateral relationships with their clients. In the view of XTX Markets this is clearly inconsistent with Principle 17 of the FX Code.

Using actual client data, we will show that the use of Last Look for the avoidance of adverse selection (i.e. avoiding the "losing" trades (from the LP's perspective) in a client's portfolio) and for managing market impact (i.e. the post-trade change in the market price after a client's trade has been executed) constitutes an invisible tax on clients and a distortion of their true costs of execution, which we will also quantify.

[1] Full consultation paper and details as to how to provide feedback can be found here: https://www.globalfxc.org/consultative_process.htm?m=72%7C429"
[2] "FX Global Code: A Set of Global Principles of Good Practice in the Foreign Exchange Market." Globalfxc.org, 1 Aug. 2018, www.globalfxc.org/docs/fx_global.pdf. Referred to throughout as the "FX Code".
[3] Extract from Principle 17 of the FX Global Code

To start with it makes sense to define Last Look. Last Look is actually constructed of two separate, but related, practices:

1. The right of the LP to accept or reject a trade request (or offer to deal) from a client. This is fundamental to OTC markets and should absolutely be allowed. This control allows LP's to check that the price remains valid in order to protect themselves against latency in their price construction, slow connections to clients etc. It also allows LP's to check client transactions to ensure that they fit within market, credit and operational risk limits. This check against the current price and against limits is vital to the safe provision of liquidity to the market by LP's and is a fundamental tenet of OTC trading. This check can incorporate a small delay in line with the amount of time that it takes an LP to create a new price i.e. the "latency" in its price construction. This is how Last Look is defined in our view in the FX Code.

2. Additional Hold Time ("AHT"). This is the practice of artificially holding client trade requests (or offers to deal) once they arrive within an LP's system for a defined period of time before applying the price check and making the decision to accept/reject the trade request. In many instances the validity/operational checks will have been completed for a considerable period of time before the price check is applied, as the figure below illustrates with LP 2.

Note: *This is an illustrative example. LP 1 is not applying an AHT but responds in 10ms as this is how long it takes for it to complete its operational checks. LP 2 responds in 130ms and this is largely due to the AHT of 125ms that it applies before completing its price check, which itself takes 5ms.*

The difference between these two is absolutely central to the discussion. No one in the market objects to (1), however, the issues arise with the application of (2): the Additional Hold Time (AHT).

Principle 17 of the FX Code clearly states that Last Look can be used for risk control purposes but not for the purposes of optimising profitability. Using hold times for as long as you need to ensure your price is current is an acceptable practice. However, some LP's are using varying hold times per client and using hold times for longer periods than it takes for them to complete their price check.

How can holding transaction requests and offers-to-deal in a way that varies by client, varies month by month, varies between trade acceptances and trade rejects, and is for a disproportionately long period, be anything other than profitability optimisation - be it profit maximisation or loss mitigation (two sides of the same coin)?

In this paper, we will show clearly why the use of of AHT by some LP's acts against clients and why LP's apply different settings to their clients, not for the purpose of controlling risk but for optimising profitability.

Additionally, we will make a strong argument for why you should all care and why it is critical for an industry that prides itself on its ability to self-regulate, to be applying the FX Code to set the highest standards, rather than setting a low bar or a framework that means that clients need a law degree and a quantitative PhD to understand the behaviours of their LP's.

AT THE OUTSET, WE'D LIKE TO POSE WHAT SHOULD BE A FAIRLY SIMPLE QUESTION......WHICH OF THESE PRICES GIVES THE LOWEST COST OF EXECUTION

A. 20.1/20.9 with an asymmetric AHT of 20 ms on acceptances and 100ms on rejects (reject rate 5%)

B. 20/21 with an AHT of Zero (reject rate 0.5%)

C. 20.5/20.5 with an AHT of 200ms with an asymmetric price tolerance applied (reject rate 10%)

D. Hard to say for sure but I wish it was just 20/21 and I got done

If you struggled to answer the question easily or answered D , then read on.

PROFIT IN THE BLINK OF AN EYE

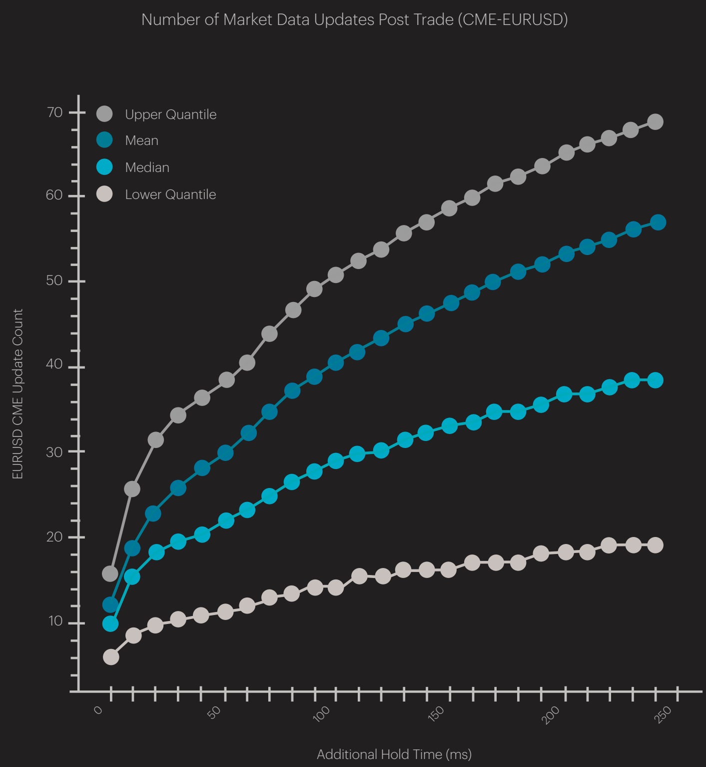
As previously mentioned, although Principle 17 of the FX Code defines Last Look as the price / validity check, looking at the disclosures of certain LP's, many do not explicitly distinguish between Last Look and Additional Hold Time; rather they allow the two to be conflated which, it turns out, is very handy for an LP who wants to use Additional Hold Times to optimise its profitability.

First of all, the price check should be conducted to ensure that the trade request price remains consistent with the current price that would be available to that client. Why would an LP need to wait an additional period before checking that? The FX Code says that the check should be done against the current price, not "at some price in the future at a time determined by the LP". LP's would say that they need to hold the trade request in order to receive the latest price updates from the primary FX Markets to then carry out the current price check.

So how long does it take to receive these updates and check a price? The fastest market data feeds from the primary FX venues in spot FX - which all major LP's subscribe to - update every 5/ms. However, some LP's have Additional Hold Times of 200ms (although many retain the right to extend that period during volatile markets). 200ms - the time it takes for a human eye to blink - doesn't sound a lot of time, does it? What's the big deal?

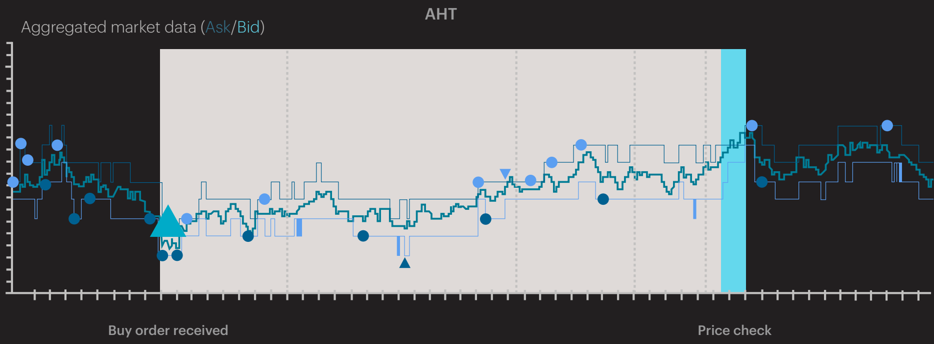
Well, in 200ms, there are an average of 50 price updates for EURUSD on the CME alone (as per the figure below). Now imagine being an LP and also seeing all the price activity on EBS, Reuters, CBOE, LMAX, Currenex, GainGTX, Euronext etc.

Chart produced by XTX using CME data from the period 2020/12/21 - 2021/03/19.



These updates during the AHT are valuable for profit optimisation. Consider the below scenario: because the LP applies an AHT, it can see the market went up after the offer-to-deal was initiated, and after it was received, and then reject the unprofitable buy order. The more updates the LP can see, the easier it is to predict the likely P&L of the trade.

An LP can even set itself fill rate targets (per client) and commercially optimise its logic so that it focuses on rejecting the most unprofitable trades within its reject “quota”. In other words, not all rejects are equal; it is quite possible for the LP to have a relatively low reject rate but absolutely optimise their outcome.



Note: *This is an illustrative image only, showing a price stream continuing to tick during an AHT. This gives the LP an option to see the future before deciding whether or not to accept the trade.*

Imagine taking this to the extreme and saying that an LP could price choice all day long and then select the trades that they wanted to keep, and those they wish to avoid, by watching the market evolve after the trade request has been submitted by the client.

In extreme, this would be obviously ridiculous - like a bookmaker only deciding to accept a bet after the race had finished. Ah, but what if it wasn't after the race had finished but after say one furlong, or two furlongs, or just before the final furlong? What time would be acceptable? How much of the race should the bookmaker be able to see before deciding whether to accept the bet or not?

Prima facie, this looks bad. Maybe it is because some LP's have poor infrastructure to do their price checks? Let's look at that argument in a little more detail: if AHT is due to the latency of a price check on the LP's own systems, why would any AHT applied in order to meet this current price check be different according to who the client is? And yet LP after LP applies different hold times to different clients. How do we know this? It is in their disclosures....

"After you send an order to us and the [LP systems] receive that order we may place it in a queue for a period of time. That period of time may vary between 0 and 200 milliseconds."

"In addition to applying "last look" trade acceptance parameters to our electronic quotes, [LP] may, for some counterparties, also apply a hold time. Based on observed quote update times at a number of different electronic trading platforms, [LP] has determined that 300 milliseconds is currently the maximum hold time that may be configured for any client."

What possible reason, if not profit optimisation, could exist for holding different clients for different periods? That would mean certain behaviours could be construed as "not complying with the FX Code" or at best "not complying with the spirit of the FX Code". Well, it seems many LP's think otherwise and in reality, of course, this is already happening. How do we know? It is in their disclosures, like these from a major global bank LP......

"Upon receipt of your electronic offer to execute a transaction at a price and quantity, whether in response to an indication of interest or otherwise, [LP] will determine whether, and at what price, to accept all or any part of your electronic offer, after assessing that electronic offer against a variety of pre-trade factors. These factors may include, among others, available inventory, liquidity, prevailing market prices, anticipated loss or gain based on the [LP] 's analysis of the market and the [LP] 's trading experience with you and/or other market participants, credit and product terms and filters the [LP] may employ for the purpose of implementing credit limits, position limits or other limits on your electronic trading activities. These factors may be changed from time to time without notice to you and may differ from those applied to other counterparties. Due to the speed of the market and execution delays (including time delays that the [LP] may elect to impose on a counterparty-by-counterparty basis, in light of the risks inherent in its electronic market making and risk management activities), the price available for execution of any transaction with you may change between the time of submission of your electronic trade request and the time that you receive a response to your electronic offer, even if the lapse of time is small. This may result in rejection of all or

part of your electronic offer, including in cases where the market has moved favorably to you, even though we may choose to accept electronic offers where the market has moved favorably to us. If we determine to execute, the costs or benefits of any price changes may, in our discretion, be retained by us."

But surely LP's have a right to behave differently to handle so-called "toxic" flow? Of course they do, and there is a perfectly good, tried and trusted mechanism for that - it is called spread. Tougher flow should attract a wider spread and better flow should attract a tighter spread. Management of "adverse selection" and "market impact" is synonymous with "profit optimisation". Avoiding the worst trades in any client's portfolio is of course vital to the return that the LP can generate from that client's flow. The fair way to do this is by having better, more informed, pricing and pricing that does not have significant latencies built into it.

Some LP's will of course say that removing AHT altogether would create a technology race to zero that would not be beneficial to clients but would increase barriers to entry to market makers. Whilst we believe that AHT should be essentially prohibited, if the market consensus were to allow a short AHT to prevent this theoretical race to zero, what is proportional and would represent a reasonable AHT? Well, one simple method would be for LP's to explicitly link their AHT to their median "tick to trade" time, defined as the time it takes an LP to receive a relevant market data update and make the next price. This "median tick to trade" should be a reasonable benchmark for all LP's. We would like to see public disclosures of these times. It is not an inherently difficult calculation for any LP engaged in electronic market making and does not represent a significant overhead.

But do we really need to be so prescriptive? Surely these are issues that can all be covered by disclosures, right?

DISCLOSURES OR DISCLAIMERS?

Many LP's advocate for a broader, less prescriptive, approach arguing that the FX Code should be principles based and that there should be a general assumption of *caveat emptor* (buyer beware). Further, they argue that *caveat emptor* should be applicable because there are clear disclosures as to trading practices of LP's in the public domain.

So, let's look at some sets of disclosures and see how clear they are. These have been anonymised but come from a major global bank LP in the eFX space.

"Along with risk management, regulatory, and staleness checks, LP performs a price check. If the market price for a Transaction is at a level beyond a counterparty-specific threshold applied by LP's trade acceptance logic after receipt of a client request to trade, LP will reject the trade request. LP may take into consideration a counterparty's historical trading characteristics in setting various parameters, including those relating to last look."

"If the above checks have passed and the order is in scope for a price check, the price check will determine whether the order is accepted or rejected. In the price check, we compare the price we are prepared to make available to you in the relevant currency pair at that point in time with your order price request."

"Any actual hold time that is applicable will be set out in our FIX trade reject message. This means that the last look trade acceptance checks described above will not occur until the particular hold time period has elapsed.LP applies a hold time solely to evaluate whether an intervening price movement has occurred."

Reading through these disclosures it is difficult even for relatively sophisticated market participants such as ourselves to understand the practices being deployed and whether or not they are consistent with the FX Code or good market practice. We can only therefore assume it is even harder for the typical client to have a picture of exactly what is going on. At any rate, these hardly form the basis for "informed consent".

OR CONSIDER THESE EXCERPTS FROM A NON-BANK (EMPHASIS IN TEXT BELOW IS OUR OWN):

1. "LP may reject orders asymmetrically. LP believes that a symmetrical execution tolerance will impact the counterparty inan adverse manner.[4]"

2. "LP will utilize "Pre-Hedging" as permitted by the FX Global Code. LP may pre-hedge counterparty trade requests where the quote provider is acting as principal, and does so for the benefit of the counterparty. If LP does pre-hedge a counterparty trade request, all of the prehedged quantity will be passed through to the counterparty, unless express counterparty agreements or exchange rules prohibit partial fills.
LP engages in pre-hedging with the intent to advantage the counterparty with optimal fill rates, but also may receive a benefit from pre-hedging the transaction."

3. "At times, LP may deploy orders as pre-hedges in order to facilitate a counterparty trade request. This strategy can possibly result in an "over-hedge" of the amount initially requested by the counterparty."

4. "All of your order data obtained by LP may be used by LP and provided to counterparties on an anonymous and aggregated business for the purpose of data analysis, risk management, compliance and proprietary trading. Order data includes, but is not limited to, the following:

- Orders executed in full or part;
- Cancelled or expired orders;
- Indications of interest;
- Quotes;
- Positions;
- Trade; and
- Other data and analytics utilizing order data."

Unlike the previous examples, these are perfectly clear. Would you as a client agree that pre-hedging, over-hedging, and use of unfilled order information is acceptable market practice so long as it is disclaimed to you in a disclosure document? So if you can't trust the disclaimers....

[4] See section headed "What about symmetric and asymmetric logic?" below for an explanation of symmetrical acceptance / rejection logic

IN DATA WE TRUST

One client has been kind enough to allow us to use their data to illustrate the behaviour of some of the largest LP's in the market in the period February through April 2020.

This client's liquidity pool consists broadly of 5 of the world's largest FX banks plus XTX. The following tables show the behaviour of all those LP's during that three month period. For the sake of clarity, and without divulging any information about who the client or LP's are, this client executes a significant amount of flow in two books (amongst others) – one of which trades on a Full Amount basis and one of which trades on a Sweep (aggregated) basis.

It is important to note that Round Trip Times are measured at the 95th percentile and can be affected slightly by single day technological anomalies but the data is broadly representative. Note also that all LP's are cross-connected with the client in a single major data centre so there is no difference in latency of connection and that latency could be measured in less than 1-2 milliseconds. Each book trades tens of thousands of trades each month and well in excess of $1.5bio every day.

Let's take the Full Amount book first. Looking through February, March and April of 2020, we notice how LPD changes Additional Hold Time in March. Acceptances remain as before in February BUT rejects go from 10 to 125 ms. Nonetheless, there is an undeniable shift in Additional Hold Time that clearly has nothing to do with technology or additional latency, as acceptances can clearly be handled at the same speed as in February. In April, as markets start to calm again, the logic changes again and now acceptances are at 75ms and rejects are still at the extended 125ms. However, the reject rate is low so the impact on the client is somewhat minimised, at least during normal market conditions. In other words, the option is there for the LP but it simply doesn't have that much value in relatively benign markets or execution styles.

But of course, options are more valuable when volatility increases as we can see when we look at the behaviour in the sweep book. Now, by definition, it does not take any longer to accept or reject a trade on a sweep book than a full amount book. You may expect the reject rate to be slightly higher as tolerance settings for deal acceptance are likely to be lower as the flow can be expected to be somewhat tougher (as is normal and expected in aggregated trading books). Nonetheless, notice that in general, most LP's employ longer hold times in the sweep book than they do in the Full Amount book. Why could that be - could it be to see more of how the market evolves after the request?

CLIENT DATA FULL AMOUNT BOOK

Feb - 20	Round Trip Time		Client Data Full Amount Book	
Full Amount	Accepts	Rejects	Reject Rate	Mkt Share
LPA	20	40	1.0%	20%
LPB	20	20	0.5%	14%
LPC	10	10	4.5%	18%
LPD	10	10	0.3%	16%
LPE	10	10	4.2%	11%
XTX	10	10	0.0%	21%

Mar - 20	Round Trip Time		Client Data Full Amount Book	
Full Amount	Accepts	Rejects	Reject Rate	Mkt Share
LPA	20	30	1.9%	19%
LPB	20	20	0.9%	7%
LPC	10	10	7.1%	7%
LPD	10	125	0.1%	31%
LPE	10	10	17.4%	15%
XTX	10	10	0.2%	20%

Apr - 20	Round Trip Time		Client Data Full Amount Book	
Full Amount	Accepts	Rejects	Reject Rate	Mkt Share
LPA	20	20	1.3%	21%
LPB	20	20	0.8%	9%
LPC	10	10	3.3%	13%
LPD	75	125	0.1%	23%
LPE	10	10	2.0%	14%
XTX	10	10	0.3%	14%

Data provided by a client.

But most significantly, notice the reject rates: LPA - from an already high 12% in February to 57.6% in March and LPD from 3.1% in February to 60.6% in March. Both though obviously continue to price tightly as they win high market shares in both months.

Of course, March 2020 was volatile and market spreads were wider but why would that matter if, as an LP, you could price tightly as you simply don't have to stand behind the trades because you can "select the portfolio". Notice how the LP's that obviously price wider win less share (LPB, LPC and XTX) but have MUCH lower reject rates – they are crowded out by LPA and LPD. For the sake of clarity, the sample set here is significant and 60.6% represents more than 5000 rejected trades in the month. What this data highlights is that some LP's are clearly using the Last Look (and in particular the Additional Hold Time) to "select a portfolio" of trades.

CLIENT DATA SWEEP BOOK

Feb - 20	Round Trip Time		Client Data Sweep Book	
Sweep Book	Accepts	Rejects	Reject Rate	Mkt Share
LPA	30	75	12.0%	14%
LPB	100	100	2.4%	11%
LPC	50	50	2.6%	9%
LPD	125	125	3.1%	27%
LPE	10	20	15.1%	21%
XTX	10	10	3.0%	18%

Mar - 20	Round Trip Time		Client Data Sweep Book	
Sweep Book	Accepts	Rejects	Reject Rate	Mkt Share
LPA	20	10	57.6%	18%
LPB	100	100	3.6%	8%
LPC	10	10	5.7%	9%
LPD	75	75	60.6%	25%
LPE	10	10	15.6%	22%
XTX	10	20	2.3%	16%

Apr - 20	Round Trip Time		Client Data Sweep Book	
Sweep Book	Accepts	Rejects	Reject Rate	Mkt Share
LPA	20	20	8.2%	13%
LPB	100	100	3.7%	6%
LPC	10	10	7.6%	12%
LPD	75	75	2.3%	24%
LPE	10	10	4.0%	29%
XTX	10	10	1.0%	10%

Data provided by a client.

XTX believes this behaviour is inconsistent with the FX Code. The data also shows how difficult it is, even for sophisticated clients, to determine which of these LP's is providing a good service. It is impossible to ascertain the costs associated with each LP, and the total costs incurred, without using sophisticated independent analytical tools.

THE COST OF AHT

The total cost of execution is made up of two parts. The observable or "visible spread" and the invisible cost associated with AHT. But do we know what the total true cost of AHT applied across clients in the market is? No, it is almost impossible to calculate of course because there are so many moving parts - not least the visible cost but especially the invisible cost. The very fact that LP's try so hard to retain variable AHT as a mechanism, and spend so much time obfuscating clients around the cost suggests it is considerable. Later in this section, we will explain how we performed a multi-factor analysis of the cost but, for now, let's keep the discussion relatively simplistic. Does it actually cost clients anything or is this just in the way that the yield on a client's flow is apportioned between the LP's?

By definition, these mechanisms distort true price competition. In particular, the cost of the AHT applied and the Last Look mechanisms (rejection/acceptance) applied by some of the LP's in the March 2020 example above imply that the redistribution between LP's is very significant indeed.

Should clients care about this if it is just a redistribution of yield? Yes they should - ultimately real LP's with a genuine alpha based skew, risk capital and real interest to deal, can be crowded out and their value undermined and eroded. That can lead to the best pricing LP's being excluded from the mass of the client's flow and hence affect their ability to price the client in the future or when really needed. That is neither good nor fair for the client as it will ultimately result in wider spreads.

But hang on, is it really a zero-sum game? LP's often attempt to frame the discussion as a simple trade-off between spreads and rejections (visible costs and slippage costs). A Head of FX Sales at a tier-one bank explained in FX Markets that, for him, last look is not merely a risk control mechanism as defined in the FX Code but another commercial pricing lever to be used with clients.

"We have a dialogue about [how] this much pause [AHT] is going to relate to this much improvement in spread. Does that work for you? If it doesn't then we need to reapproach it. ... Similarly, who am I to say to a customer who comes to me and says, 'I don't care if you reject me 80% of the time, I want 0.2 pip spreads?' Who am I to say that he can't have that? As long as it is a transparent and open conversation then I think it can work because there can be mutual benefits going both ways."

However, if one looks more deeply at this, we quickly realise that in a best-case scenario for the client, an LP can only price choice (i.e. the value provided to the client is bounded), but the value extracted by the LP from ever longer AHTs and higher rejections can grow in an unbounded manner.

In major instruments such as EURUSD and USDJPY, LP's are no longer able to reduce their 'Visible Costs' (spread) any further. If a client does not forcefully impose limits on AHT/Rejections, the client will over time see their true cost of execution rise as LP's extract additional value through slippage which cannot be passed back to clients through the spread. Slippage in major instruments represents an insidious tax on end client execution costs. In other words, this is not a zero-sum game because the costs imposed on the clients are unbounded, whereas the LP's costs are, by definition, limited.

It's important to remember that some LP's who do not use AHT (XTX is one but not the only one, e.g. JPM, HSBC) have to rely on pricing wider to defend themselves against more directional flow and so they will, by nature, win less trades and have the value of the uniqueness of their price eroded by those LP's using these tactics. Therefore, the outcome becomes self-fulfilling. The best LP's may be crowded out and those that maximise their yield using these mechanisms are able to cherry pick the flow that they want leaving the rest to pick up the trades the AHT wielding LP's do not want. And the client of course has the impression that those LP's are underperforming and their top LP's are those with the high market share using AHT to their advantage.

Whilst the above is all true, we did attempt to ascertain the true cost of AHT applied to client portfolios. The results are interesting.

Referencing the work by Oomen (2016)[5] on pricing within an aggregator, and utilising real market data, we simulate pricing from multiple LP's and generate an aggregate pricing stack equivalent in nature to what a buy side client would observe. We then simulate the activity of a 'noise trader' and demonstrate that a client's effective spreads are not constant given an allowed limit on rejections; meaning higher tolerable rejections lead to higher effective spreads. The interested reader is referred to the Appendix for further details of the methodology.

[5] Oomen, R. (2016). Execution in an aggregator. Quantitative Finance, [online] 17(3), pp.383–404. Available at: http://eprints.lse.ac.uk/67454/1/Oomen_Execution%20aggregator_2016.pdf.

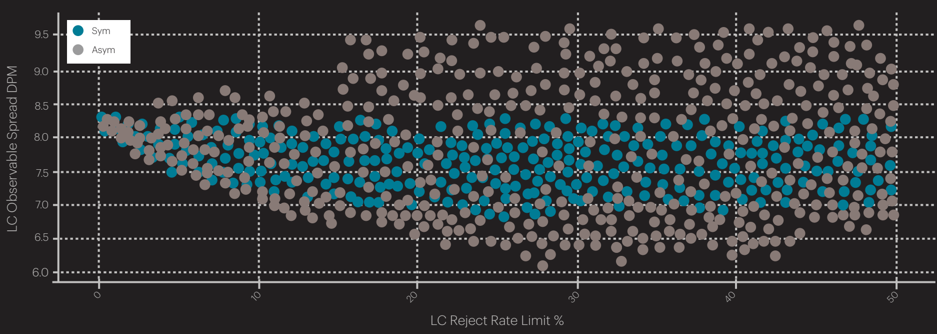
THE RESULTS OF THE MODEL ARE SUMMARISED IN THE BELOW FIGURE WHERE EACH POINT REPRESENTS A UNIQUE SET OF STARTING CONDITIONS AND LIMITS THAT THE CLIENT PLACES ON THEIR LP'S AND DEMONSTRATE:

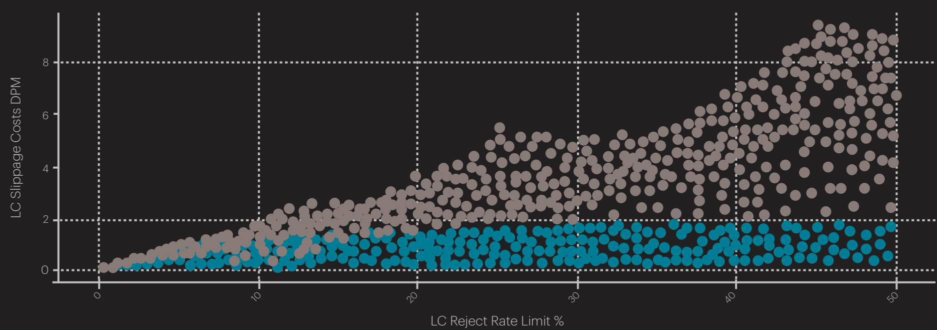
1) The change in visible spread: visible spreads shrink to a limit as rejections increase;

2) The change in slippage: slippage costs increase unbounded as rejections increase; and

3) The change in true cost: as a client tolerates higher levels of rejection their true costs will grow in a manner that is difficult to predict;

Impact of LC Reject Rate Limits in Execution Cost Transparency





Impact of LC Reject Rate Limits in Execution Cost Transparency

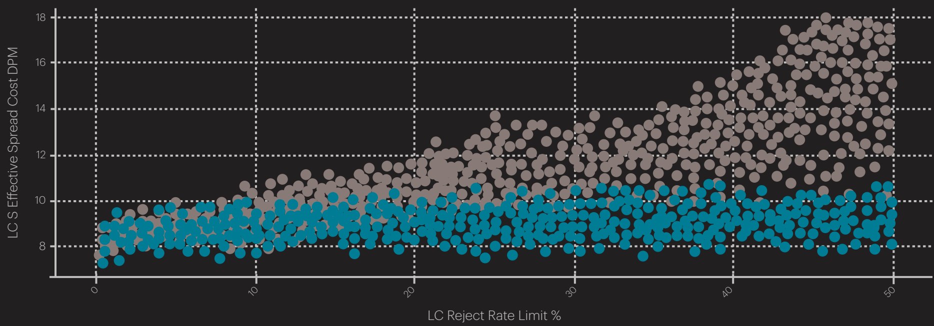


Chart: *Simulation data produced by XTX using internal market data. See Appendix for methodology.*

Regardless, it is clear that the client's effective spreads are not constant given an allowed limit on rejections. Higher tolerable rejections lead to higher effective spreads as LP's extract unbounded value from slippage but are bounded in pricing non-negative spreads (especially in the case of asymmetric tolerances).

This demonstrates that the argument that client slippage costs are compensated for through spread competition amongst LP's is not strictly true.

Of course, it may well be that you think performing an analysis such as this ought to be unnecessary in a market which is *"robust, fair, liquid, open, and appropriately transparent" (FX Code objective statement*). Requiring a quantitative modelling PhD to understand the true cost of execution probably is not a feature one would associate with a market defined by those characteristics.

WHAT ABOUT SYMMETRIC AND ASYMMETRIC LOGIC?

The subject of symmetry emerges around treatment of price movements between the submission of the "offer to deal" and the completion of the price validity check (regardless of at what point that check occurs). Most LP's allow a "price tolerance" i.e., an amount by which the LP's price may have moved when checked against the price referenced in the "offer to deal". That tolerance is usually measured in "pips" or fractions thereof, although it can be zero. Symmetric treatment requires that the price tolerance is applied equally regardless of the direction of the price change i.e., regardless of whether the trade has moved in the LP's favour or against the LP. Such tolerance is often used to ensure that rejection rates are not excessively high and is an entirely reasonable and well intentioned practice. However, in certain circumstances, LP's apply "asymmetric tolerance" - this means that the LP accepts trades that have moved beyond the tolerance when it is in their favour and they reject when it moves beyond the tolerance against them.

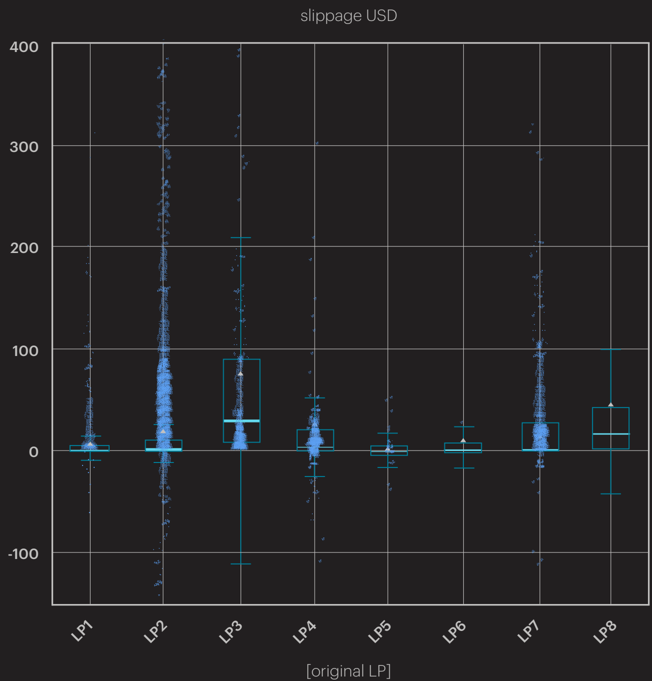
The first thing to note is that, when it comes to bilateral client flow, there is zero justification for using default asymmetric acceptance logic for what the FX Code defines as a "risk control mechanism". Asymmetric logic simply means that the LP will fill the client at the original (now off-market) rate if the market moves in the LP's favour; but reject the client if the market moves in the client's favour. The reason asymmetric logic exists is that it is more profitable for an LP than symmetric logic on the same flow. This is zero-sum: the client loses precisely whatever the LP gains.

It would be one thing to allow a limited number of sophisticated clients to opt-in to asymmetric logic, following crystal clear disclosures and confirmation the clients have an ability to quantify the cost to them. However, certain top-tier LP's still use asymmetric logic as their default setting for clients. Yes, really. A client must specifically opt-out to get treated symmetrically! Do those clients have the analytic transaction cost tools to measure the impact on them, making a fully informed decision, or are they even aware?

Symmetric logic should be preferable to asymmetric logic from a client's point of view. However, even when the logic is applied perfectly symmetrically, it is not the case that the client outcome will be symmetric. The majority of rejects will still occur when the market has moved against the client, rather than in their favour. Symmetric logic or not, this is assuredly not a 50/50 scenario that balances out over time. There is an oft-stated refrain from LP's that "I use a long AHT to maximise the chances that I can fill the client at the end of the last look window". Let's see how likely that is to happen in reality.

Below is an analysis of reject data, provided by a large retail broker. The majority of LP's use symmetric last look logic and yet the outcomes are visibly skewed against the client. This means the slippage cost is far more often positive (if buying, the price moves higher when the client tries again after being rejected) than negative (if buying, the price moves lower when the client tries again after being rejected).

Boxplot grouped by original LP



Analysis produced by XTX, using data provided by a client.

The reason for this is that market movements post receipt of a trade request are not random: for various reasons the price movement upon receipt of a client trade request is likely to be in the same direction of the client trade request, on average. The takeaway is simple: even with symmetric logic, the client will have the wrong kind of slippage on average. The longer the AHT, the more the slippage and thus cost to the client grows and contrary to that oft stated refrain, the reality is that "the longer the AHT, the more likely the LP is to reject you".

So now that we have ascertained that Additional Hold Times are too long, opaque and costly, and that the trading logic of asymmetric rejects is an arcane tool designed again for profit optimisation, let's debunk some other myths.

MYTH 1 : REGIONAL BANKS CAN'T PRICE AS QUICKLY AS THE BIG PLAYERS. WON'T THEY BE CROWDED OUT?

Not at all. This is a red herring. One only needs to review the Risk Magazine article of 2019 "How the Top 50 dealers tackle forex last look"[6] to see that banks such as ING, Santander, TD, Westpac, SEB, Credit Agricole (to name a few) all disclose clearly that they do not apply an AHT. If they can do it, why can't some of the largest global LP's?

In actual fact, the reverse is true - regional banks are crowded out by the large global AHT wielding players. Again, think of the logical extreme of the LP who prices choice and then only selects "winning trades". That LP is distorting real competition, keeping valuable axes and skews offered by regional players away from clients through artificially saying "I have interest to deal on both sides of the market", when in fact they "only have interest in trading on one side of the market" (they just can't tell you which side yet……).

The arguments around regional banks not being able to have such competitive technology and therefore needing some additional protections are also moot points. Regional banks are, in the broadest sense, trading with clients who are less technologically aware and less sophisticated than large institutional clients - i.e. corporates, insurers, standalone pension funds etc. These are not clients with heavily directional flow let alone "toxic" flow and again those that do have such clients should use spread as the means to protect themselves, not AHT.

[6] Rega-Jones, N. "How the top 50 dealers tackle forex last look." Risk.net., 08 Aug. 2019, https://www.risk.net/derivatives/6888556/how-the-top-50-liquidity-providers-tackle-forex-last-look.

Take these disclosures from Santander[7] which are clear and informative.

> *"Due to the different checks and controls being performed, as described above, an answer to a deal request may not be immediate. However, we wish to make it explicit that, for the purpose of performing price verifications under "Last Look", Santander does not apply any pre-determined Holding Period, also sometimes referred to as 'latency buffer', and trade requests are confirmed as soon as all the relevant checks and controls have been performed. As a general matter, a Holding Period may involve holding a trade request for a prescribed time delay before the price check is performed (the 'Holding Window'), in order to allow the liquidity provider to see the latest market data updates before applying the price check. Santander does not apply a Holding Window to any trade requests (Zero Hold Time) in respect of our spot FX business. The last look price and/or validity check will be applied as soon as our systems receive the trade request."*

Additionally, our suggestion in the conclusions of this paper that AHT be either removed completely or be capped according to the LP's median "tick to trade" would level the playing field, allowing LP's with genuinely more latent pricing-stacks to align their AHT with their own latencies.

MYTH 2 : LIQUIDITY PROVIDERS HAVE GLOBAL CLIENTS TRADING ON GUIs VIA THE INTERNET WITH LOTS OF LATENCY. ISN'T THAT A REASON FOR AN AHT?

This is also a red herring.

It is true that there is natural latency when a client clicks on a GUI in another part of the world. However - even if that trade request takes an hour to arrive - once it has arrived at the LP's server, it doesn't take any longer to compare this trade request's reference price against the current price on the server than it would for any other order. The AHT clock only starts ticking once the offer to deal has been received by the LP.

Because this is the most benign flow that exists, most LP's will simply add tolerance. This means that orders may be filled even if, due to natural latency, they are slightly off market - in either direction - vs the current reference price. This of course does not require an artificial hold time. Truly global banks with large GUI franchises across connectivity challenged regions such as HSBC and JP Morgan both seem to manage this without AHT.

[7] https://www.santander.com/en/landing-pages/foreign-exchange-disclosure-notice

MYTH 3 : LIQUIDITY PROVIDERS NEED AHT TO TRADE ON ANONYMOUS VENUES

What about where the LP does not know the end client or even believes that the person they are trading with is NOT a client. This occurs on ECNs. All ECNs allow the LP's the right to use an AHT and employ last look. Again, there is no issue with the fundamental right of any LP to determine when a trade is executed, that is, as explained above, an expected and necessary behaviour in OTC markets. The real question is the validity of the AHT. In the case of ECN trading, not every price stream is bespoke and multiple "clients" or "tags" are often connected to the same price stream from the LP. This is different to bilateral trading which is done 1-2-1. As a result, there is some justification for the AHT. It helps LP's to price tighter on the stream than the client with the worst flow deserves whilst allowing protection against those worst clients.

Nonetheless, the ultimate protection mechanism does exist on ECNs - that is removing certain tags from an LP's pricing stream(s). This can be done pretty simply and easily. And of course, the old solution of pricing those tags wider, or that whole stream wider, also exists.

Whatever the rights or wrongs of using AHT on an ECN, there is no doubt that all LP's across the ECN could be held to the same AHT (or none) and that pricing by LP's would therefore be like-for-like and truly comparable. Levelling the playing field in this way would, at a minimum, be beneficial for the transparency of pricing. We know that some ECNs, notably CBOE FX, but others also, have been shortening the maximum hold time that LP's can use over the last 1-2 years; this is a good start but those times could be significantly shorter.

Alternatively, the ECN could, as a neutral intermediary, apply the price check on behalf of the LP, using their latest advertised price. This removes one of the biggest conflicts of last look as the LP would only be made aware of a trade request once it had passed this independently applied price check. Should a trade request fail the price check - i.e. the LP's price had moved and was no longer available - the LP would simply not be sent the trade request. LP's would retain the right to perform validity checks and a credit check before confirming execution of the trade request but these are not controversial and account for a tiny proportion of rejects.

MYTH 4: PRICE IMPROVEMENT

Some Liquidity Providers suggest that they use AHT to be able to offer Price Improvement to their clients. However, price improvement is unintuitive. It sounds like a good thing. Imagine a client sends a buy trade request in a 10 / 12 market. Before the request is received by the LP, the market ticks down to 9 / 11. The LP price improves and fills the client at 11 rather than 12. This sounds helpful! However, there is really no guarantee that the same LP who had the best offer in the 10 / 12 market is still the best offer in the 9 / 11 market. The fairest thing to do is reject the trade request and let the client poll all of their providers again and select the best price, rather than fill a captive trade request at what may not be the best price available.

There is also a danger that price improvement as a practice becomes acceptable - this runs altogether new risks similar to those which exist in US retail equities. The practice of price improving the client does not mean that the end client (quite possibly a retail customer) will necessarily benefit (or indeed see the best price that was actually available to them at the time of trade). It also becomes all too easy for large players to use their scale advantage to offer price improvement across a whole portfolio of trades, with a lack of clarity that the improvement ever benefits downstream clients, especially retail customers. This is a slippery slope that we think would be well avoided in the FX market.

If clients wish to receive the market price at the time of LP receipt of the offer to deal, they should send a market order and get filled at the prevailing rate regardless of whether or not it is an improvement versus the market rate at the time of the attempted execution.

CONCLUSIONS

We hope this paper has made you better informed on the topic of Last Look and how LP's are using it in a manner that we interpret is inconsistent with the FX Code. It is worth remembering this statement from Principle 17 of the FX Code:

> *"A market participant should be transparent regarding its Last Look practices in order for the client to make an informed decision as to the manner in which last look is applied to their trading"*

Do you really believe, given the above, that this standard is being satisfied from your perspective?

We would make the following very simple recommendations to improve the situation and which we believe all LP's should feel comfortable applying. This would help make trading practices fair and efficient for all market participants, as well as meet the objectives of the FX Code outlined above. It would also mean that many of the issues with regard to disclosures would simply vanish as they would no longer be applicable.

1. DEFINE Last Look correctly by splitting the definition between Last Look per se (the right of the LP to be the contract determinant) and the AHT applied by LP's.

2. Update the FX Code to specifically PROHIBIT the use of AHT for any reason related to profit optimisation, specifically including for the avoidance of adverse selection and the management of market impact.

Our suggestion would be to include wording along the following lines:

> *"LP's should remember that the client has an unknown liquidity exposure during the Last Look window and therefore aim to minimise this period of uncertainty. An offer to deal should only be held for such period that it takes for the LP to perform the price check, confirming the price at which the trade request was made against was consistent with the price that would have been available to the client at receipt of offer to deal."*

We recognise that this very clean definition, which does not allow for any Additional Hold Time, may not be acceptable to the consensus of market participants, so perhaps we could also suggest a slightly weaker language which aims to allow LP's to see a single price update before they perform the price check. This HAS to be related to the time that it takes an LP to see one further price update - this price update would not represent a price change, merely the next price update. This means that LP's and clients are protected where the market does not update for considerable periods of time, e.g. Scandinavian currencies outside European hours. As referred to earlier in the document, we call this the "median tick to trade". The suggested wording then becomes:

"LP's should remember that the client has an unknown liquidity exposure during the LL window and therefore aim to minimise this period of uncertainty. A trade request should only be held for such period that it takes for the LP to perform the price check, confirming the price at which the trade request was made remains consistent with the current price that would be available to the client. Where a client's pricing stream updates at a slower rate than the LP receives external reference market price updates, (e.g. throttled streams), it may be reasonable for an LP to wait until it receives the next external reference market update following receipt of the trade request before completing its price check."

Given the problems of creating a truly clean definition that cannot be easily gamed or "mis-interpreted", we also feel it would be helpful for the FX Code to add some examples of what would represent good market practice and what would not. Such clear guidance would enable Compliance departments to more easily ensure that the practices of LP's are in line with the spirit of the Code.

So, an example of good market practice based on the first wording above could read:

"LP takes 5 ms to receive an external market data reference update. Trade request is received at T+0. Price check is begun always at T+0 regardless of market data update speed etc and all checks are undertaken against the current price regardless of whether or not the market data reference update has been received."

This approach has the advantage of being very clean and there is no requirement for additional disclosures. Everyone would play by the same rules and there would be no feasible use of Last Look as a commercial tool, as the Code originally foresaw.
Example for the second wording could be along these lines:

LP takes 5 ms to receive an external market data reference update. Trade request is received at T0, trade should be checked as soon as practical, so hold time would be limited to the time taken to complete the price check.

In the event that the client's stream updates at a rate slower than every 5ms, any hold time should be limited to a maximum 5ms and the trade request price should be checked against the price which the LP would then make for that client. Any *hold time in excess of 5 ms in this example would be considered to be an example of an unacceptable practice. The price check process should ideally be commenced immediately at T0 but certainly no later than T0+5ms.*

In the event that the LP updates the client price in a time less than 5 ms, the price check should be commenced immediately as the price is updated. By definition, this time will be before T0+5 ms.

In the event that the LP updates the client price in a time greater than 5 ms, the price check should be commenced no later than T0+5 ms. This covers the situation where the client pricing is throttled by the technology provider or the LP themselves.

Additionally, under both wordings, the following could be used as an example of what would be considered unacceptable/acceptable/best market practice:

LP takes 5 ms to receive an external market data reference update. Trade request is made at T0. Any check which involves the price check starting at a time greater than T0+5ms would be considered UNACCEPTABLE and only immediate price checks would be considered BEST market practice.

For example, trade request received at T0, credit and operational check started immediately. Credit and operational checks complete at T0+25ms. Potential practices would be:

Price check is commenced at T0 but completed multiple times up to completion of credit and operational checks. This would equate to an undue hold time. UNACCEPTABLE

Price check is commenced at T0+25ms. This would equate to an undue hold time. UNACCEPTABLE

Price check is commenced between T0 and T0+5ms. NOT BEST BUT ACCEPTABLE

Price check is commenced at T0. BEST

These examples hold for all clients and all LP's - if LP's have slower market data updates than others, they can utilise a slightly longer hold time so that they are not simply picked off but for all major participants, the additional hold time would be practically removed. This would be a very positive development for the market whilst allowing regional banks and those without the fastest market data to continue to participate effectively.

In addition, we would suggest the following simple but very important wording be added:

> *There is no justification for commencing price checks at different times based on the client identity or flow type. To do so would be inconsistent with acceptable market practice.*

The FX Code should make a clear statement that profit optimisation issues of adverse selection and managing market impact should be handled using spread.

Of course, we accept as would everyone we believe, that there may at times be exceptional circumstances where any LP is unable to guarantee to meet these thresholds, e.g. if they have technology issues etc but that should not preclude an outcome that mirrors these suggestions.

3. DEFAULT deal acceptance logic to be SYMMETRIC.

Thank you for taking the time to read this paper. We would urge you to file a public comment letter (https://www.globalfxc.org/docs/Draft_GFXC_Last_Look_Guidance_Paper.pdf) by May 31st 2021. If you don't have the time or resources to do this then we would ask you to complete a simple, confidential survey (answers will only be used in aggregate) – there are only eight questions and it is multiple choice.

Click here to complete: [Survey: Last Look and Additional Hold Times]

[Click here for XTX eFX disclosures]

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APPENDIX

METHODOLOGY APPLIED TO ASCERTAIN TRUE COST OF AHT TO CLIENT PORTFOLIOS

In order to determine this, we model a typical last look protocol and allow LP's over time to adjust their settings (spreads, AHT, price check tolerance) to account for gains/losses on the resulting accepted trades. Trade requests generated by the client are routed to the LP with the prevailing best bid/(ask) in their aggregator. The LP then applies AHT to control for adverse selection and/or market impact, and once this period has elapsed the LP performs a price validity check against the most recent price available to the client.

If the client allows for asymmetric acceptance criteria, the trade will be accepted if the price movement (requested price vs current price) is within a tolerance/direction that favours the LP. If the client prohibits asymmetric acceptance, the trade will be accepted if the price movement is within a tolerance regardless of direction.

If the trade is rejected another trade request is generated and routed to the LP with the newly available best bid/(ask) in their aggregator, the price level of the original request is cached to calculate the subsequent slippage/effective spread.

As the model runs, effective spread earned by each LP is monitored, LP's suffering from a negative/(positive) effective spread will act in their own economic interest and will perform one of the three below actions:

• Widen pricing; reduces market share but allows the LP to accommodate greater adverse selection in the aggregator

• Decrease trade acceptance tolerance; reduces the likelihood of an individual trade request being accepted

• Increase AHT; increases the option value available to the LP at the point of price validity check (end of AHT)

This process continues until the simulation reaches an equilibrium state whereby LP's see no marginal benefit from modifying their settings.

[XTX]
MARKETS

<u>Other feedback received via LFXCs/Personal views via email</u>

<u>Pre-hedging</u>

Anonymous 1:

I found the comment in the third example in the Pre-Hedging paper - "Appendix 2: Illustrative trading scenarios" section a little confusing on first review. That may just be how I interpreted it, but I was slightly unsure about the part highlighted in green below:

"Liquidity consumer asks for a firm bid price in EUR/MXN in large size. The liquidity provider has been running a long USD/MXN position expecting it to go higher, but decides to sell a large part of the position before providing the EUR/MXN quote, with the intent to lock in the P&L on the existing USD/MXN position before the liquidity consumer's trade could negatively affect the USD/MXN market price."

Pre-hedging column - "No, the activity described in this scenario is inconsistent with Principle 11".

It might be slightly clearer if it was changed it to read:

"No, but the activity described in this scenario is inconsistent with Principle 11".

Anonymous 2:
"The document is very well written and clearly shows the differences. I would have one more idea. We are talking about orders where there may be price implications due to size. Now the document is in the interest of the buy-side (LC) and very well written.

What is perhaps missing now is that of course it should not be the case that liquidity consumers request prices for large tickets (e.g. a sell order), liquidity providers pre-hedge, the price drops, and the liquidity consumer denies the price request and then starts trading (buying in this example) on the other side in the market. This is not allowed nowadays and maybe you can relate this example to principle 9 and 12.

As I said, this is just an idea and I don't see it as a necessity."

Anonymous 3:
Some short comments:
o Overall I think that the paper is sound. I do think that the paragraph at the bottom of Page 3 ("Other types of request……….") begs a number of questions that will ultimately have to be handled, and it may help to underline the importance of bilateral negotiation between MPs.
o In Figure 1 on Page 4 I think that it would be clearer to say "Full market risk remains with the liquidity consumer".
o (Bottom of paragraph 2 on page 5 should be 'potential' not 'potentially')

<u>Last Look</u>

Nil

I welcome the opportunity to provide a response to the GFXC working group paper on the Principle of Last Look, a critical area of Market practise that continues to be front of mind for all Market Participants.
I am providing my response as a financial markets independent with 30 years experience in Corporate and Institutional banking primarily within the FX industry.
I was a contributor to the original FX GLobal Code through my membership on the Australian FX Committee in 2015 and the Australian representative on the Global FX Committee in 2017/18. More recently I was part of the working group considering the issue of Riskless Principle.
Please note that my response is a personal opinion and will not be on an anonymous basis.

The primary question to be considered is whether the paper covers the issue relevant to the principles stated in the Global FX Code (FXGC) and whether there are issues which are relevant to the principles of the FXGC that are not covered in the draft guidance paper.

Principle 17, Last Look;

Last Look (LL) relates specifically to electronic trading and focuses on trading in the LL window. A Liquidity Consumer (LC) sends a specific order requesting to trade on an indicative quote that has been provided by Liquidity Provider (LP) as such has provided Confidential Information to the LP and that LP cannot trade on this information.
I note that there were several changes to the text of Principle 17 post the 90-page feedback from Market Participants in 2017 and it remains today a topic of discussion within the market community.

(1) Comment on recommendation 1.

Paper states that LPs should strive for fairness and predictability in the design of their LL processes.
The complexity of the detail in a specific LL data relating to trade acceptances and rejections relative to spreads at millisecond point of time means that to anyone other than technical experts there may be difficulty in determining what is fair.
Given this complexity I believe that prescriptive guidance by the working group is warranted on what is fair in terms of total hold times and the breakdown of hold times ex the time it takes to check validity and price, if any.
The paper states that LP should promptly make their decision to accept or reject a trade.
In the 2017 review statistics were presented that showed that for LL windows of 100-200ms duration, that this is the equivalent to receiving 20-40 principal market updates, I do not believe that this to be fair and reasonable.
If this practise is still commonplace in today's market then there should be further guidance given to its validity.
It could be suggested that the example above is comparable to a voice trader checking a large number of broker quotes before committing to a price that has been provided as an indicative quote that has already been provided by the LP.

(2) Comment on recommendations 2 and 3.

The paper states that LP should disclose information about the expected length of the LL window to their LC''s.
LP should be sharing sufficient LL information for a LC to be able to evaluate their trade execution.
The paper states that high rejection rates with an unusually long or unpredictable LL window may be an indication of inappropriate use of LL by LP's.
How is a LC to determine what is unusually long without specific reference data from the industry on what is reasonable?
Guidance should be provided on industry averages and standard times for minimum validity and primary price checks so that LL hold times which vary significantly from these times can be questioned.
Significant additional hold times net of these times are unlikely to be best practise but the market requires objective data to validate.

End.

Mark Lawler

30 May 2021.

I welcome the opportunity to provide a response to the GFXC working group paper on the Principle of Pre-hedging, a critical area of Market practise that continues to be front of mind for all Market Participants.
I am providing my response as a financial markets independent with 30 years experience in Corporate and Institutional banking primarily within the FX industry.
I was a contributor to the original FX GLobal Code through my membership on the Australian FX Committee in 2015 and the Australian representative on the Global FX Committee in 2017/18. More recently I was part of the working group considering the issue of Riskless Principle.
Please note that my response is a personal opinion and will not be on an anonymous basis.

The primary question to be considered is whether the paper covers the issue relevant to the principles stated in the Global FX Code (FXGC) and whether there are issues which are relevant to the principles of the FXGC that are not covered in the draft guidance paper.

Principle 11, Pre-hedging;

(1); The issue relating to the ownership of profit and loss resulting from pre-hedging activity;

The draft document states in section 5 that 'the intent of any pre-hedging trading by the Liquidity Provider (LP) should always be to benefit the Liquidity Consumer (LC) and help facilitate the transaction.'
The interpretation of the word 'benefit' will lead to confusion within the market as a common understanding of the term could equally apply to price outcome for the LC and/or trade completion.
Whilst the report in a previous point states 'where an anticipated order has been prehedged, but does not become a confirmed transaction, a LP owns any consequent profit or loss on the pre-hedged position,' no reference is made to any consequent profit derived by a pre-hedged position when the transaction is confirmed.
Pre-hedging activity does not require the direct pass through of any financial benefit derived from prehedging by the dealer to the client. In this instance the benefit to the LC is derived by the inventory build up, which provides an opportunity by the LP to show a price and/or a potentially tighter spread to the LC than would normally be the case for the initial notional price request had pre hedging not occurred. Further the benefit is based on the execution fulfilment in terms of liquidity and completion of the client transaction at point of time request.

The issue of potential financial benefit to the LP resulting from prehedging activity is a common discussion point within the market and further guidance relating to its delivery would be beneficial.

(2)- Fixing orders

The paper states orders received by LP's for FIX execution are firm orders and therefore any order activity done before, within or after the actual calculation window are deemed the result of hedging not prehedging.
Given that hedging activity is likely to occur before the commencement of the FIX window, an extension of the present FIX window fixing period of five minutes should be considered so that it better captures hedging activity to better reflect the eventual FIX rate.
The previous lengthening of the FIX window from one to five minutes in 2017 provided a beneficial outcome for the market in terms of lessening the stress of execution for significant orders at a point in time by traders and ALGO's alike.
A look again at the length of the Fixing window, on the basis of continual improvement, ensuring the length of the window captures as much of the relevant trade activity associated with the FIX is warranted.

(3)-Illustrative trading scenarios, the issue of execution risk on Stop Loss trades;

With reference to Scenario 5 where a LC gives a LP a stop loss order to sell 500 Mio USD/YEN at 105, the example states that trading activity with respect to the order is deemed hedging as the execution risk has been transferred to the LP.
It also states that there is an expectation by the LC of a specific fill rate at or close to the Stop Loss order rate.
Whilst the execution risk is transferred to the LP once the order is received as it is a firm order, the outcome of the fill rate is still ultimately based on best endeavours, even if there was an LC instruction for the stop execution to be close to the trigger level, and the actual fill rate is generally not guaranteed.
The LP takes on the risk transfer at the time when the market at their determinant has traded at the specified Stop Loss order price but the actual resultant price outcome risk from the Stop loss trader remains with the LC once the stop loss level is triggered.
The worked example only makes a brief reference to 'potential slippage'; perhaps further clarification of this risk would enhance the example.

(4)-Issue relating to terminology and definition.

The paper defines LP trading activity related to pre-hedging and hedging on the basis of confirmation of risk transfer from the LC.
It also refers to the conditions of 'anticipation of risk' and 'anticipation of execution'. It states that an order can be either anticipated or firm, whereby firm orders can be hedged whilst anticipated orders before confirmation can be pre-hedged.
The report complicates its terminology by then attempting to define the differences between Stop loss and Standing orders to those given for the FIX, on the basis of anticipation of execution, based on a market trigger level.

End.

Mark Lawler

30 May 2021.

Feedback on Last Look practice in FX

Dear GFXC,

Appreciate the opportunity to provide feedback on Last Look.

My opinion on Last Look practice is that hold time window by a LP should NOT be used in anyways for profit optimization whereby the LP is checking the market impact of the trade or possibility of adverse selection to make a decision on accepting or rejecting that trade.

The only valid use of hold time window by LP can be for either credit check or to check the validity of the current price. This should a be a pre-defined, definitive, minimal and consistent window.

I believe there should be a guidance on the points below:

1. Purpose of using Last Look Hold time window
2. Exact duration of Last Look hold Time window
3. Implied consistency of its use across all FX clients i.e. limits and purpose shouldn't vary from client to client on bilateral relationships

Hope this feedback is helpful. Please keep me involved in any conversations on this topic going forward.

Many Thanks and Best Regards,

Peter Tan

FX Dealer

KGI Securities (S) Pte Ltd

Feedback on Last Look practice in FX

Dear GFXC,

Grateful for allowing me an opportunity to provide feedback on Last Look Practice.

My opinion on the hold time window for last look by a Liquidity Provider should NOT be used in any way for profit optimization.

Not fair for a LP to check on the market impact of an order sent to them or check on the possibility of an adverse order selection to make a trading decision before accepting or rejecting that trade.

The only valid use of hold time window by LP can be for either credit check or to check on the sanity of a current price. This should be within a pre-defined, definitive, minimalistic and consistent window.

I believe there should be some guidance on the points below:

1. Purpose of using Last Look Hold time window
2. Exact duration of Last Look hold Time window
3. Implied consistency of its use across all FX clients i.e. limits and purpose should not vary from client to client on bilateral relationships

Hope this feedback offers a meaningful assistance on the last look practices.

Please keep me abreast on any future development or discussion in topics similar this.

Thank you very much.

Best Regards,

Garryl Lee

Head of FX Products

KGI Securities Singapore

PS: The opinion offered is strictly on a personal basis and it does represent the stance of the company I worked for.