

## **2004 Changes to the *Guidelines for Foreign Exchange Trading Activities***

The Foreign Exchange Committee published its first version of the ***Guidelines for Foreign Exchange Trading Activities*** in 1979. As the industry evolves and trading processes change, the Committee periodically updates this paper. In 2004, the changes indicated below have been introduced into the ***Guidelines***. The most recent version of the ***Guidelines*** can always be found on the Foreign Exchange Committee's public website: [www.newyorkfed.org/fxc](http://www.newyorkfed.org/fxc).

### **1. How to resolve trade-related problems**

- Amend **Resolution** section, first paragraph, to read: Disputes, however, are inevitable, and management should establish clear and policies and procedures for ***resolution at the senior management level with a transparent audit trail. For example, in many markets difference checks are exchanged.*** Informal dispute resolution practices that sometimes develop in the market can be inconsistent with sound business practices. ***For example, the use of points is not an appropriate means of trade dispute resolution, and for some counterparties in some jurisdictions the use of points may be contrary to regulatory or supervisory guidance.***
- Add footnote number 8: The Committee's guidance and recommendations on the use of points are included in the 1987 Annual Report (page 18), the 1988 Annual Report (pages 6-8), the 1989 Annual Report (pages 15-23), and the 1991 Annual Report (page 25). A U.S. regulatory policy statement prohibiting the use of points is included in the Committee's 1990 Annual Report (page 28).

### **2. Dealing with *unnamed* counterparties**

- Revise the section to read: Trading foreign exchange on an unnamed basis refers to the practice whereby an investment manager trades on behalf of a client without revealing its identity to the dealer in order to maintain client anonymity. Such practices constrain a dealer's ability to assess the creditworthiness of their counterparties and comply with "know your customer" and anti-money laundering rules and regulations. These conditions expose dealers to clear and significant legal, compliance, credit, and reputational risks, as well as heighten the risk of fraud. In addition, such practices pose a risk to the broader financial sector given the increased risk of fraud.

It is recommended that investment advisors and dealers alike implement measures to eliminate the practice of trading on an unnamed basis.<sup>1</sup> Specifically, investment advisors and foreign exchange intermediaries should develop a process to disclose client names to a dealer's credit, legal, and compliance functions prior to the execution of foreign exchange trades. In turn, dealers should establish procedures to ensure the strict confidentiality of the intermediary's clients and restrict the disclosure of this information to the front office except in the event of default. This could include a confidentiality agreement whereby the dealer agrees that only its credit, legal, and compliance functions will have access to the client name. The use of identification codes, or similar identifier systems, has been achieved in other markets.

- Add footnote number 10: Trading on an unnamed basis is often confused with trading on an undisclosed basis (when an intermediary does not explicitly acknowledge that it is acting as an agent at any point in the relationship).
- Add footnote number 11: A detailed discussion of the risks of unnamed counterparty trading is included in the Committee document, *Information on Unnamed Counterparty Trading*. The Committee's guidance on the issue can be found in several letters to market participants available on the public website, [www.newyorkfed.org/fxc](http://www.newyorkfed.org/fxc). Other industry groups are also actively discouraging this practice in regional codes of conduct and best practices. The Bank of England's Joint Standing Committee revised their Non-Investment Products Code, a reference source used for regulatory review of financial institutions and investment managers in the United Kingdom, to include best practices similar to those outlined above.

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