

# Legal Initiatives

**THE FOREIGN EXCHANGE COMMITTEE TURNS FREQUENTLY TO ITS** associate organization, the Financial Markets Lawyers Group (FMLG), for legal advice and support. The FMLG, sponsored by the Federal Reserve Bank of New York, consists of in-house attorneys active in the foreign exchange market. Members represent various financial institutions, including commercial and investment banks. A senior member of the Federal Reserve Bank of New York's legal staff chairs the group.

The FMLG supports the Committee by

- reviewing its new documentation and publications prior to circulation,
- briefing the membership on pressing legal issues,
- advising on Committee actions, including lobbying efforts, and
- emphasizing the need for consistent industry documentation related to foreign exchange transactions and collaborating with other industry groups on documentation issues.

## **FMLG ACTIVITIES IN 2000**

In 2000, the FMLG worked on a wide variety of initiatives with a number of industry groups. Many of the projects were directly related to the Foreign Exchange Committee's work, reflecting the close relationship between these two bodies. Additional projects involved collaboration with other organizations and focused on assisting the broader financial markets. Some of this work is reviewed below.

### **Monitoring the Progress of the Commodity Exchange Act's Modernization**

Throughout 2000, the Committee and the FMLG were attuned to the urgency of reforming the Commodity Exchange Act (CEA). Reform of the CEA would

- a) provide more legal certainty for many products,
- b) promote the productive growth of derivative securities, and

- c) mitigate obstacles to financial market innovation that may have occurred under the present CEA.

In consultation with the FMLG, the Committee often joined other industry groups in lobbying for these initiatives. Efforts included sending letters to the Commodity Futures Trading Commission (see page 93), to House Banking and Financial Services Committee Chairman James Leach (page 95), and to Speaker of the House J. Dennis Hastert and House Minority Leader Richard Gephardt (page 97).

Passage of the Commodity Futures Modernization Act in late 2000 achieved many of the goals identified by the Committee and the FMLG.

#### **Cross-Product Master Agreement**

The FMLG collaborated with the Bond Market Association (BMA) in drafting and publishing the Cross-Product Master Agreement. This agreement, which incorporates existing product-focused master agreements, acts as a contractual superstructure that will encompass other bilateral master agreements. In February 2000, the Federal Reserve Bank of New York, the FMLG, and the BMA sponsored a conference to introduce this document and outline its benefits to the general financial community.

#### **Collateral Annex**

The Collateral Annex provides examples of contractual terms for one-way collateralization of for-

foreign exchange or currency option transactions governed by the Committee's various master agreements. Use of the document is strongly encouraged as a way to improve risk management. It is reprinted on pages 31-45 of this report and can be found on the FMLG's web site, <[www.newyorkfed.org/fmlg](http://www.newyorkfed.org/fmlg)>. In addition, a user's guide to the Collateral Annex is available on the same web site.

#### **Working with EMTA**

The FMLG continued to work closely in 2000 with the Emerging Markets Traders Association (EMTA). In recent years, EMTA has made considerable efforts to clarify the documentation for the non-deliverable forwards (NDFs) market, a difficult task given the diversity of this fragmented market. The Committee and the FMLG have warmly endorsed EMTA's efforts. Working groups formed by EMTA that include members of the FMLG, traders, and other legal and operational staffs have agreed on templates for several specific NDF currencies, thus making considerable strides in standardizing trading documents and terms.

In addition, in the interest of improving the efficiency of foreign exchange trading, particularly for emerging market currencies, the Committee and the International Swaps and Derivatives Association (ISDA) have provided on-line access to an updated version of Annex A of the 1998 *FX and Currency Options Definitions*. Annex A gives traders in emerging market currencies a list of the

accepted trading sources and specifications associated with each currency.

#### **Barrier Options**

Members of an FMLG subgroup have agreed on standard confirmations for two widely used barrier options instruments: the European knock-out/knock-in and the one-touch binary barrier options. These sample templates are reprinted on pages 59 to 67. Institutions are urged to consider using these formats to improve clarity in this market. In 2001, the FMLG subgroup will turn its attention to the development of standard terminology for the evolving barrier options market.

#### **Preparing for CLS**

The development of the CLS (Continuous Linked Settlement) Bank is an important event in the foreign exchange market. Recognizing this importance, the FMLG formed a subcommittee to study issues related to the CLS Bank and plans to monitor closely its impact on the market and on published industry documentation.

#### **Other Initiatives**

- a) Following Poland's legislative action requiring Polish-language documentation for certain Polish-related transactions, the FMLG, in coordination with other industry groups, produced a Polish translation of the International Foreign Exchange Master Agreement (IFEMA) documents.

- b) The FMLG addressed specific issues raised by Greece's entry into the European Economic and Monetary Union (EMU) by amending the Protocol document, first published by the FMLG in October 1998. The EMU Protocol offers suggested language for the IFEMA set of master agreements that could be adopted, if needed, on a bilateral basis between two counterparties.
- c) The FMLG played an important role in promoting and organizing an international conference on the importance of netting.

Held in Mexico City on November 9 and 10, the conference was sponsored by the Federal Reserve Bank of New York, the Center for Latin American Monetary Studies, and the World Bank.

The purpose of the gathering, which attracted more than ninety individuals from seventeen countries, was to inform policymakers and legislators in Latin American and Caribbean countries about the benefits of netting and the need to adopt netting laws that would provide certainty to foreign exchange

transactions. FMLG members provided contact names for the invitation list and participated in presentations.

Throughout the year, the FMLG also strengthened its ties with the European Financial Markets Lawyers Group, a legal industry association affiliated with the European Central Bank.

- d) The FMLG continued to provide its membership with up-to-date netting opinions for its published documentation in key jurisdictions.