Remarks

Treasury Market Best Practices Conference

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I would like to take a few moments of your time before our panel discussions to discuss the development and work of the TMPG and to provide a broad overview of the product of that work, the "Treasury Market Best Practices" document.

First, in the interest of housekeeping, allow me to describe the structure and content of today's conference. Following this part of the program there will be two panels, each scheduled for one hour and 15 minutes. The first panel is entitled, "Best Practices for Trading Activity" and John Roberts will moderate that panel. John Ramsay will moderate the second panel, entitled "Maintaining a Robust Control Environment". Mr. Ramsay and Mr. Roberts are both members of the TMPG. As you can see, from the program, not all of our panelists are members of TMPG and we hope that this mix of views and vantage points will allow the panels to discuss these issues from many perspectives while sharing views of market participants inside and outside the working group. We are looking forward to a very interactive dialogue and an open sharing of ideas and opinions.

As for the format, each moderator will give a short overview of the relevant best practices and ask panelists specific questions related to these best practices. At that point, the panel will be open for audience Q&A. Questions can be submitted in written form on the card provided in your packet or the old-fashioned way by raising your hand and we will get a microphone to your seat. We would appreciate if you could announce your name and affiliation before presenting your questions. There will be a break in between panel discussions and, compliments of our hosts at the New York Fed, a box lunch will be available as you leave today.

One disclaimer and one reminder. First, the reminder: please be aware that there *are* members of the press in attendance here with us today. Second, the disclaimer: all of today's panelists and moderators are here representing their own personal views as market participants. Those views may or may not be the views of the firms that they represent.

What we hope to accomplish today, with your feedback and participation, is a clear checkpoint on the work and output of the TMPG to date, and hopefully some guidance on our work going forward. It is our intent to provide insight into the evolution of the best practices document, as well as the basic themes and principles that we attempted to build into the text. It is important that we all look at the document as the best way to memorialize what we can all agree to be the current standard of best practices for participants in the Treasury market and related financing markets.

Let me share a quick history of the TMPG. In November of last year, representatives of the New York Fed met with senior business and compliance representatives of the 22 primary dealers to discuss practices to strengthen the market integrity of the U.S. Treasury Market. The discussion focused on ways to strengthen market practices in the Treasury market so as to maintain its status as the deepest and most liquid sovereign debt market in the world. Following that meeting, it was clear that a continued dialogue among private sector market participants could begin a process to formalize a group of best practices to achieve that goal.

On February 9, the New York Fed announced the formation of the TMPG. The role of this private sector group is to strengthen market integrity by promotion of best practices in the Treasury market. The TMPG is composed of representatives from dealers, buy-side firms, and custodians in the Treasury market and is intended to encourage dialogue and offer recommendations for practices in the Treasury cash, repo and related markets. The membership of TMPG provides a diverse cross-section of dealers and buy-side firms and offers input from all areas of expertise relevant to these discussions. The committee's membership, as you can see, offers input into the process from the vantage point of the trading desks (cash, repo and derivatives), legal, compliance, operations, settlements, and administration. This group has been able to stick to an extremely ambitious timetable to produce the best practices document as well as the work and content that they will share with you today. The significance and consequence of the issues facing the TMPG combined with the extraordinary commitment of the group has enabled us to present what we believe to be a giant step forward in our ongoing efforts to preserve and enhance the integrity and liquidity of the U.S. Treasury market and related markets through market-based recommendations and practices.

As the group began work on the document, we decided to divide the process into a few core themes and principles. We focused on four key areas of market participant behavior that if addressed appropriately could provide the basis for a comprehensive set of guidelines that would be both relevant and practical for all participants in the Treasury market.

The group established some broad yet clear guidelines for our work and based all that you see in the document around these basic, yet integral themes:

1. The best practices must intend to support the integrity and efficiency of the Treasury cash, financing, and derivatives markets. The TMPG believes that all market participants benefit when the marketplace remains efficient and liquid.
2. Best practices are just that; they are principles, not rules. The group firmly believes that principles are a far better approach than strict, prescriptive rules for guiding behavior in a dynamic and evolving marketplace.
3. The group stresses that members of the market place have composed these best practices *for* members of the marketplace. Similar to other industry best practices, these best practices do not come with regulatory authority. Rather, we believe that these best practices affirm existing notions of good market conduct and serve to establish a common guide that all market participants should consider as they evaluate the operation of their businesses.
4. We concluded that in the interest of a level playing field for all participants that our work should not be limited to any participant sector. So, as a result, the best practices document is aimed at all market participants. The integrity and efficiency of the market can only be maintained if all market participants are

striving towards these and other ethical standards. To that end, the best practices that you see today are intended not only for dealers but also for any market participant active in the wholesale Treasury market, including brokers, buy-side firms (leveraged and real money), investors, custodians, foreign central banks and hedge funds.

5. It was an early decision by the group that these best practices be open to interpretation. Because we expect and intend that these practices to be useful and to be utilized by all market participants, there are designed elements of the document that allow for each participant to interpret the document's application for their own business. Each market participant could interpret these practices slightly differently as they consider the size of their business operation, and the role they play as dealer, broker, investor, or custodian. However, all interpretations and applications should share one common element and that is to ensure ethical trading objectives and outcomes.

   As participants make interpretations, the group encourages managers to focus on intent as a key determinant of the review process. I fully expect that what you will hear today from our panelists will highlight the fact that even our speakers will have different interpretations of the document and its application. Readers of the document should always consider whether they are meeting the spirit of the best practices, not simply some minimum standard. When appropriately applied, the best practices document can serve as a roadmap to enable trading managers and compliance managers to efficiently and practically measure and address potential franchise, regulatory, or organizational risks. And, of course, it never hurts to overstate the obvious; these best practices do not trump or absolve firms from their responsibilities to follow the law. Market participants should always ensure that that they are following applicable laws at all times and should avoid illegal activities such as price manipulation.

With that backdrop, the design of the document was isolated into four key topics, (1) Promoting Market Making and Liquidity; (2) Maintaining a Robust Control Environment to Monitor Questionable Trading Practices; (3) Managing Large Positions with Care; and (4) Promoting Efficient Market Clearing.

Our panels will dig much deeper on the content of these areas but, briefly, each of these four key components of the document serve to highlight very specific areas of participant behavior and then combine in a complementary fashion with each other to create a roadmap for ethical market practices. Depending on your role in the market, most or all of these practices will be applicable to your business operation:

- **Promoting Market Making and Liquidity** focuses on transparency issues as well as management oversight. The section focuses on specific best practices such as timely trade reporting and the avoidance of practices such as shorting repo at zero.

- **Maintaining a Robust Control Environment to Monitor Questionable Trading Practices** focuses on the role of compliance and the importance of internal control procedures. It supports the active ongoing interaction between trading supervision and formal compliance and addresses the complementary nature of that interaction. This section also provides some specific “yellow flag” types of activities that could highlight potential risks. Compliance review thresholds, such as large positions and specialness, will be different from one firm to the next. Likewise, the standards that each firm sets in its own control environment will change over time as the market grows and changes. We believe that this document provides a flexible roadmap that will continue to be relevant as the market evolves. We hope that it helps business managers and compliance professionals to establish their own internal standards and controls based on but not limited to these best practices. This can enable firms to identify and monitor trading behaviors and to provide guidance with the goal of establishing the concept of intent as a core principle.
- The section on **Managing Large Positions with Care** addresses the additional responsibilities associated with large positions. Large short or long positions in a security are not necessarily problematic, but large positions present the holder with a greater set of responsibilities, full stop. In a liquid market, a large position may not have a negative impact on market liquidity. However, managers and compliance professionals through these practices are encouraged to ensure that the control environment is designed to identify and stop or prevent trading strategies with the intent of disrupting market liquidity. In this section and throughout the document we stress the responsibility of shorts *as well as longs* to make every attempt to identify and act on market clearing prices in the interest of liquidity.
- Under the fourth section, **Promoting Efficient Market Clearing,** we focus on good settlements practices with specific attention paid to problematic behavior such as holding the box or slamming the wire. We also highlight the best structure for settlement- a positive organization of responsibilities between the financing desk and the settlements group.

So, as we move to the next part of the today’s conference, I would like to note that the TMPG is an ongoing effort and we see the best practices document as a dynamic and relevant product of that work. Based on today’s work and the feedback we hope to get, we can continue to upgrade and enhance this document. So, if there are general or specific suggestions that you may have or areas that you think we have missed, we encourage your participation and I can assure you that the TMPG will consider your feedback today and in the future in a thoughtful and responsive manner. All of our speakers, panelists and moderators will be available in the Q&A periods, so please direct your questions accordingly. We are open for business and look forward to your participation. Because these issues raise questions for most of us, it is important that we continue a two-way, interactive dialogue around them and share perspective. We hope to continue that dialogue today.