FICC MARKETS STANDARDS BOARD

Standard for the execution of Large Trades in FICC markets

I Introduction

1. The FICC Markets Standards Board

The FICC Markets Standards Board (FMSB) was established in 2015 in response to the Fair and Effective Markets Review (FEMR) in the UK with a mandate to issue clear and practical guidance designed to improve conduct and raise standards in the wholesale fixed income, currencies and commodities (FICC) markets. FMSB is building a body of Standards and Statements of Good Practice (SoGPs) over time, prioritising those areas where FMSB member firms (Member Firms) consider there is a lack of clarity in the standards of behaviour expected of market participants, or a lack of understanding of the issues relevant to a product or transaction type, or evidence of poor conduct.

2. Applicability of FMSB Standards

FMSB members[1] agree to adopt the Standards in their business practices (where relevant) and to evidence adherence through an annual Statement of Commitment. The Member Firm confirms annually that it is committed to conduct its FICC market activities (its 'Activities') in a manner consistent with the Core Principles contained in FMSB Standards, and to have internal policies, procedures and controls reasonably designed to give effect to those Core Principles where they are applicable to its Activities, in a manner that is commensurate with the nature of its Activities in the relevant entity or jurisdiction. That confirmation is expected to apply to all FMSB Standards issued in final form in the calendar year prior to the year in which the confirmation is made.

The details of FMSB member firms are available at fmsb.com.

Standards are published on FMSB's website and non-member firms and their affiliates are encouraged to consider them. In this way, Standards are also made available to users of wholesale FICC markets (e.g. corporates, investors and other end-users) so that they may be made aware of their existence and FMSB's expectation of market conduct.

3. Relationship with law and regulation

FMSB Standards and SoGPs do not impose legal or regulatory obligations on Member Firms, nor do they take the place of regulation. In the event of any inconsistency, applicable law, rules and regulation will prevail. In developing Standards and SoGPs, certain regulators may have commented on their drafting, alongside Member Firms and other bodies, such that the Standards and SoGPs, once finalised and published, are intended to represent an authoritative statement of global good practices and processes. However, they are not normally endorsed by regulators. Where they are endorsed by a regulator, this will be made clear on the face of the Standard or SoGP in question.

4. Relationship with other industry codes ('Codes')

Other Codes already exist in relation to certain FICC markets, such as the FX Global Code, while others are in the process of being produced. There will be some overlap between FMSB's work and such other bodies and FMSB will seek to ensure it adopts a consistent approach in cases of overlap wherever possible, and will seek to avoid issuing a Standard or SoGP where the subject matter is already covered adequately by existing regulation or a Code issued by another body. It may draw attention to Member Firms of an existing code and request that Member Firms consider its applicability and act in a manner consistent with it, where appropriate.

[1] Full, Associate, and Corporate Members commit to adhere to the FMSB Standards that are relevant to their business. Information about FMSB membership is available at fmsb.com/who-we-are/

II Standards for the execution of Large Trades

1. Explanation

This Standard sets out expected behaviours for participants in the fixed income, currencies and commodities (FICC) markets. Although the nature of a Large Trade (defined below) will vary across FICC markets, the Core Principles in this Standard are relevant and applicable across asset classes.

This Standard is intended to:

i. Reduce information asymmetries between dealers and clients in relation to the execution of Large Trades and enhance the understanding of clients as to the method of execution and potential impact of Large Trades on the market and price the client receives. Addressing these information asymmetries is likely to be particularly important for clients that execute Large Trades on an infrequent basis;

ii. Clarify and codify the principles governing the pre-hedging of Large Trades. Principle 11 of the FX Global Code ('FXGC') sets out pre-hedging guidelines for client trades executed in the FX market and this Standard extends principles compatible with the FXGC to the fixed income and commodities markets;

iii. Establish clear expectations with regard to client confidentiality given the potentially heightened impacts of information leakage in the context of Large Trades both within a firm and outside where knowledge of an anticipated transaction among other market participants, if acted upon, could move the market price against the client; and

iv. Ensure that clients communicate with dealers in a transparent manner so as to not have a detrimental impact on the effectiveness of the execution of a Large Trade by the dealer.

While this Standard is concerned with behaviours relating to the execution of Large Trades, many of the Core Principles outlined may be of relevance to all dealer-client trading activity. The rationale for focusing on Large Trades is due to the heightened conduct risks associated with their execution and the greater potential market impact of such activity compared with smaller transactions.

2. Scope and applicability

This Standard applies to all participants in the wholesale FICC markets in Europe, subject to any applicable local regulatory restrictions. This Standard does not apply to primary issuances but could apply to transactions, including hedging transactions, associated with a primary issuance. Market participants may elect to apply this Standard in other jurisdictions.

The 10 Core Principles set out in this Standard are applicable to the execution of all Large Trades between dealers and clients, including those executed using an algorithmic execution method (for example, 'volume weighted average price' or 'time weighted average price' transactions).

When executing a Large Trade, a market participant may either act as an agent or a principal. The obligations applicable to market participants when executing Large Trades will differ according to the capacity in which the dealer is acting. The Core Principles in this Standard are therefore arranged to reflect this distinction, with Section III applying to Large Trades executed in an agency capacity and Section IV applying to Large Trades executed in a principal capacity. The relevant topic, associated Core Principles and their applicability to agency or principal business are summarised in the table below.

	Capacity	
Topic	**Agent**	**Principal**
Communications between client and dealer	Core Principle 1	Core Principle 6
Pre-hedging	Core Principle 2	Core Principle 7
Client confidentiality	Core Principle 3	Core Principle 8
Client obligations	Core Principle 4	Core Principle 9
Guidelines for Large Trades	Core Principle 5	Core Principle 10

3. Definition

The following definitions are used for the purposes of this Standard.

Term	Definition
'Large Trade'	A transaction or set of transactions, which is, or together are, substantially larger than the observed liquidity in the relevant product market around the time of execution, and which could be reasonably expected to have a material impact on prices in the market or related markets. This is a relative, rather than absolute, concept and will generally be based on an assessment of liquidity and volatility measures. Large Trades may be executed pursuant to a request for quote ('RFQ') or client order. This Standard does not distinguish between Large Trades executed pursuant to an RFQ or client order or consider any regulatory obligations that might be associated with either.
Principal	Principals act on their own behalf and there is no obligation to execute a transaction until both parties are in agreement. Principal activity involves taking on one or more risks in connection with a transaction, including market and credit risk. Where the acceptance of a transaction grants the principal executing the transaction some discretion, it should exercise this discretion reasonably, fairly, and in such a way that is not designed or intended to disadvantage the client.[2]
Agent	An agent executes transactions on behalf of the client pursuant to the client mandate, and without taking market risk in connection with the transaction.[3]

[2] See Principle 8 of the FX Global Code (August 2018) available at www.globalfxc.org/fx_global_code.htm.
[3] Ibid.

4. Nature of Large Trades

What constitutes a Large Trade will vary by market, product, time period, geography and other factors that could impact liquidity. Accordingly, it is for the parties to a transaction to consider, before the execution of the trade(s), the potential impact of the trade(s) on the relevant market based on a commercially reasonable assessment of the relevant factors.

Large Trades by their nature will often have some level of market impact as they are executed or hedged. That in turn can lead to price volatility, and dealers face potential conflicts of interest between managing their own risk exposure, while avoiding creating undue pressure on the market. This Standard seeks to establish principles for how market participants should behave in relation to the execution of Large Trades and so assist market participants to deal with those issues.

Trading activity in one market may have an impact in other related markets and this should be taken into account by market participants when executing a Large Trade.

III Principles applicable where executing a Large Trade in an agency capacity

1. Communication between agent and client

Core Principle 1: When a Large Trade is contemplated dealers should (at an early stage where practicable) communicate to the client that the trade may be large in the relevant market.

Given their deep market knowledge, dealers are generally best placed to determine whether a transaction (or group of transactions) is likely to constitute a Large Trade. Where the dealer has the requisite information to make such a determination, before execution of a transaction, it should make a reasonable assessment of whether such transaction is likely to constitute a Large Trade in the relevant market based on the information available to it at that point in time. Where Large Trades are contemplated, the dealer is responsible for communicating this to the client and taking reasonable steps to inform the client of factors it considers relevant for transactions characterised as Large Trades, such as the:

i. Role and capacity in which the dealer is acting;

ii. Execution strategy, e.g. timing or potential market impact of the transaction;

iii. Management of confidential information flows relating to the execution of the Large Trade, both by the client and the dealer; and

iv. Criteria that may prompt a discussion to pause, break up into smaller lots or terminate/pull the Large Trade.

The factors outlined in (i)-(iv) above, or a sub-set or variant thereof, depending on the context, may be communicated to the client in the form of an oral or written disclosure. 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.

2. Pre-hedging

Core Principle 2: When acting as agent, pre-hedging is never permitted in the relevant market.

Pre-hedging is not permissible in a scenario where the dealer is acting as agent. For an illustration of this Core Principle, see Annex 1, example 1.

3. Maintaining client confidentiality and disclosure

Core Principle 3: Dealers should not disclose the details of Large Trades to other market participants unless required to give effect to the clients' instructions and to execute the transaction. Dealers should also ensure that they treat all clients fairly.

Disclosing to other market participants

Details of Large Trades will usually be strictly confidential and information in relation to them should not be disclosed to other market participants.

Particular care needs to be taken by a dealer when executing a Large Trade not to communicate the fact of the Large Trade to another market participant unless required to give effect to client instructions and to execute the transaction.

Internal information sharing

Any internal sharing of information provided by the client to the dealer in relation to the execution of a Large Trade should be in accordance with applicable law and the FMSB's 'Information and Confidentiality for the Fixed Income and Commodities markets Statement of Good Practice'[4].

Fair treatment of clients

In order to help ensure the fair treatment of clients, dealers should:

- Make clients aware of general practices around the handling of client transactions. This may be achieved by way of disclosure to clients; and
- Act in accordance with Core Principles 1 and 2.

4. Client obligations

Core Principle 4: Clients should communicate in a transparent manner that is clear, accurate and not misleading.

Clients should communicate with dealers in a transparent manner that is clear and accurate when conducting transactions which are deemed to be Large Trades. Misleading information should not be provided by the client in relation to a transaction (or group of transactions) that constitutes a Large Trade, even where this is to protect confidential or material non-public information.

A client should communicate in a transparent way but, for the avoidance of doubt, it is not obliged to disclose information. The client must instead ensure that any information that is communicated is not misleading. This is particularly important to ensure that the dealer is able to service the client, which may only be possible where the dealer has access to all relevant information.

See example 6 in Appendix 1 of FMSB's Information and Confidentiality Statement of Good Practice for an illustration of good and inadequate practices with regard to such information disclosures.

5. Guidelines for Large Trades

Core Principle 5: Market participants should implement such policies and associated control processes as necessary to demonstrate adherence to this Standard.

Dealers should have control processes in place to ensure that Large Trades executed on an agency basis are not pre-hedged.

[4] See Section 3 of FMSB's 'Information and Confidentiality for the Fixed Income and Commodities markets Statement of Good Practice', October 2019 available at fmsb.com/wp-content/uploads/2019/10/ Information-Confidentiality-SGP_V6.4-FINAL.pdf ('FMSB's Information and Confidentiality Statement of Good Practice')

IV Principles applicable where executing a Large Trade in a principal capacity

1. Communication between principal and client

Core Principle 6: When a Large Trade is contemplated dealers should (at an early stage where practicable) communicate to the client that the trade may be large in the relevant market.

Given their deep market knowledge, dealers are generally best placed to determine whether a transaction (or group of transactions) is likely to constitute a Large Trade. Where the dealer has the requisite information to make such a determination, before execution of a transaction, it should make a reasonable assessment of whether such transaction is likely to constitute a Large Trade in the relevant market based on the information available to it at that point in time. Where Large Trades are contemplated, the dealer is responsible for communicating this to the client and taking reasonable steps to inform the client of factors it considers relevant for transactions characterised as Large Trades, such as the:

i. Role and capacity in which the dealer is acting;

ii. Execution strategy, e.g. timing or potential market impact of the transaction;

iii. Management of confidential information flows relating to the execution of the Large Trade, both by the client and the dealer; and

iv. Market performance, for example where the market performs in an unexpected manner.

The factors outlined in (i)-(iv) above, or a sub-set or variant thereof, depending on the context, may be communicated to the client in the form of an oral or written disclosure. A disclosure does not need to be made on a trade-by-trade basis. Factors influencing the frequency and content of the disclosure may include the expertise of the client, the nature of the client relationship and frequency with which the client enters into comparable transactions.

The dealer and the client are expected to make their own independent decisions regarding whether to execute the transaction between them, and neither party should rely on the other for the accuracy or completeness of any information or the expected or actual performance of the parties' activities.

2. Pre-hedging[5]

Core Principle 7: Pre-hedging should only be undertaken where: (i) the dealer legitimately expects to take on market risk and the pre-hedging is undertaken at the dealer's own risk; (ii) the trading activity is reasonable relative to the size and nature of the anticipated transaction; (iii) it aims to minimise the impact of the activity on the market; and (iv) it is designed to benefit the client and not executed in a manner that is meant to disadvantage the client.

Pre-hedging is the management of the risk associated with one or more anticipated client trades. Pre-hedging is undertaken where a dealer legitimately expects to take on market risk in circumstances where such dealer does not have an irrevocable instruction from the client. Pre-hedging may assist dealers in providing increased liquidity to their clients and

[5] See Principle 11 of the FX Global Code (August 2018) and Pre-Trade and Execution Principle 6, LBMA Global Precious Metals Code (April 2018).

improving the expected quality of execution. However, trading in anticipation of a client order or following the receipt of an RFQ may, in certain circumstances, give rise to market abuse concerns or conduct risks. For example, if a dealer enters into a transaction for its own benefit, ahead and on the basis of its knowledge of a potential Large Trade, to take advantage of the anticipated impact of such Large Trade on the market price of the instrument or related instruments, this may amount to insider dealing under the Market Abuse Regulation[6].

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.

Pre-hedging should be carried out in line with the following principles:

i. It should only occur where the dealer legitimately expects to take on market risk and is undertaken at the dealer's own risk;

ii. It should be reasonable relative to the size and nature of the anticipated transaction taking into account prevailing market conditions (such as liquidity);

iii. It should aim to minimise the impact of the activity on the market and be designed to facilitate the transaction; and

iv. It should be designed to benefit the client[7] and executed in a manner that is not meant to disadvantage the client.

Pre-hedging may take place at a portfolio level or otherwise than on an individual transaction basis in which case dealers should ensure that the management of their anticipated aggregate positions is consistent with these principles.

Dealers will need to carefully assess these principles and relevant applicable law in light of the specific facts of any given scenario.

Examples of the application of Core Principle 7 can be found in Annex 1, examples 2 and 3. In addition, the core principles as set out in FMSB's 'Risk Management Transactions for New Issuance Standard'[8] and 'Reference Price Transactions Standard'[9] may apply to the hedging of certain transactions which are Large Trades.

3. Maintaining client confidentiality and disclosure

> **Core Principle 8**: Dealers should not disclose the details of Large Trades to other market participants unless required to give effect to the clients' instructions and to execute the transaction. They must also ensure that they treat all clients fairly.

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[6] See, for example, MAR 1.3.2G of the FCA Handbook at www.handbook.fca.org.uk/handbook/MAR/1/3.html

[7] 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.

[8] July 2018, available at fmsb.com/wp-content/uploads/2019/03/Risk-Management-Transactions-for-New-Issuance-standard-Final-3-July-2018_v5.pdf.

[9] November 2016, available at fmsb.com/wp-content/uploads/2017/05/2016-001-FMSB-Std_ReferencePriceTransactions_FIMarkets_Final-Updated.pdf.

Disclosing to other market participants

Details of Large Trades will normally be strictly confidential and information in relation to them should not be disclosed to other clients.

Particular care needs to be taken by a dealer when executing a Large Trade not to communicate that fact of the Large Trade to another market participant unless required to give effect to client instructions and to execute the transaction.

Internal information sharing

Any internal sharing of information provided by the client to the dealer in relation to the execution of a Large Trade should be in accordance with applicable law and the FMSB's Information and Confidentiality Statement of Good Practice.

Fair treatment of clients

In order to help ensure the fair treatment of clients, dealers should:

- Make clients aware of general practices around the handling of client transactions. This may be achieved by way of disclosure to clients;
- Consider the market impact of any pre-hedging activity or where the dealer unwinds its position; and
- Act in accordance with Core Principles 6 and 7.

4. Client obligations

Core Principle 9: Clients should communicate in a transparent manner that is clear, accurate and not misleading.

Clients should seek to be open and transparent with dealers when conducting transactions which are deemed to be Large Trades. Misleading information should not be provided by the client in relation to a transaction (or group of transactions) that constitutes a Large Trade, even where this is to protect confidential or material non-public information.

A client should communicate in a transparent way but, for the avoidance of doubt, it is not obliged to disclose information. The client must instead ensure that any information that is communicated is not misleading. This is particularly important to ensure that the dealer is able to service the client, which may only be possible where such dealer has access to all relevant information.

Examples of the application of Core Principle 9 can be found in Annex 2. See also example 6 in Appendix 1 to FMSB's Information and Confidentiality Statement of Good Practice.

5. Guidelines for Large Trades

Core Principle 10: Market participants should implement such policies and associated control processes as necessary to demonstrate adherence to this Standard.

Dealers should have policies in place to clearly define the governing principles and circumstances in which pre-hedging can take place.

Dealers should also ensure that appropriate monitoring and controls are in place to identify and prevent trading in advance of client transactions in a manner inconsistent with applicable law.

Annex 1 Examples of risk management activity

Set out below are illustrative and non-exhaustive examples of the application of certain core principles from this Standard. The examples are stylised and should not be understood, or interpreted, as precise rules or prescriptive and comprehensive guidance.

Core Principle 2 where dealer is executing Large Trade as an agent

	Example	**Assessment against Core Principle 2**	**Rationale**
1	A client asks the dealer to buy a large volume of certain fixed income instruments on its behalf at market price. The dealer has made clear to the client that it will be acting as agent and will add a fee. In addition, the client was made aware that this is a Large Trade in this market. In advance of execution, the agent seeks to 'pre-hedge' the client transaction. Any profit associated with this activity will not be passed to the client. The agent subsequently executes the Large Trade and charges its fee.	Inconsistent with Core Principle 2 ✗	Core Principle 2 provides that when acting as agent, 'pre-hedging' is never permitted. The agent takes on no market risk and may be deemed to be front running the client trade.

Core Principle 7 where dealer is executing Large Trade as principal

	Example	Assessment against Core Principle 7	Rationale
2	A client approaches a dealer for a quote in relation to a Large Trade. The dealer either: (i) declines to provide a quote and starts acquiring the relevant security in the market for its own account on the basis of the RFQ; or (ii) accepts the quote but trades aggressively in a manner that does not aim to minimise the market impact of such activity and is meant to disadvantage the client.	Inconsistent with Core Principle 7 ❌	The dealer appears to be using the confidential information provided by the client for its own proprietary benefit. In (i) the dealer declines to provide a quote and therefore does not anticipate taking on market risk and hence cannot be legitimately pre-hedging in accordance with Core Principle 7. Under (ii) the dealer does not seek to minimise the impact that any pre-hedging activity is likely to have on the market and executed the pre-hedging in a manner meant to disadvantage the client.
3	A client approaches a principal (the seller) asking to buy a certain volume of a product that exceeds the inventory the seller has available. The client request does not constitute an irrevocable instruction. In order to obtain the necessary volume and hence offer a price to the client, the dealer needs to purchase the product in the market. The seller may take price guidance from the market, trade in the market as principal to obtain the necessary volume and then seek to offer the position to the client. The seller purchases the relevant product(s) in a way that seeks to minimise the price impact of their activity on both the market and the client.	Consistent with Core Principle 7 ✔	The seller is seeking to enter the market and obtain the necessary inventory. While this is in advance of receiving an irrevocable instruction and offering the position to the client, in light of the size of the client transaction, pre-hedging is desirable in order to facilitate the client trade and improve the quality and price of execution.

Annex 2 Examples of appropriate and inappropriate communications when dealing as principal

Set out below are illustrative and non-exhaustive examples of the application of Core Principle 9. The examples are stylised and should not be understood, or interpreted, as precise rules or prescriptive and comprehensive guidance.

	Example	Assessment against Core Principle 9	Rationale
	A client asks a dealer to provide a quote ('spread') in relation to the purchase of a significant volume of certain fixed income instruments. The dealer has made clear to the client that it will be acting as principal. In addition, the client was made aware that this is a Large Trade in this market. In advance of execution, the principal asks if the instruction represents the entirety of the client's interests.		
1	The client confirms this to be the case, when in fact the client has approached a number of other dealers asking them to provide a quote. The client subsequently instructs all dealers to, simultaneously, execute the transaction.	Inconsistent with Core Principle 9 ✗	The dealer may be on risk for the spread quoted and may find that the market it seeks to execute the client instruction in is not as liquid as anticipated given the other transactions that have been simultaneously executed. As a result, the spread may no longer be achievable.
2	The client declines to answer this question in accordance with internal policy.	Consistent with Core Principle 9 ✓	The client is not obliged to disclose information to the dealer.
3	The client makes reference to the fact that it has broken up the transaction and may approach other dealers to execute those as, and when, they see fit.	Consistent with Core Principle 9 ✓	