ICMA response to the IOSCO Consultation Report on Pre-Hedging

21 February 2025

Introduction:

ICMA welcomes the opportunity to respond to the IOSCO Consultation Report on Pre-hedging.

ICMA promotes well-functioning cross-border capital markets, which are essential to fund sustainable economic growth. It is a not-for-profit membership association with offices in Zurich, London, Paris, Brussels and Hong Kong, serving over 620 member firms in nearly 70 jurisdictions globally. Its members include private and public sector issuers, banks and securities dealers, asset and fund managers, insurance companies, law firms, capital market infrastructure providers and central banks. ICMA provides industry-driven standards and recommendations, prioritising three core fixed income market areas: primary, secondary and repo and collateral, with cross-cutting themes of sustainable finance and FinTech and digitalisation. ICMA works with regulatory and governmental authorities, helping to ensure that financial regulation supports stable and efficient capital markets.

ICMA's response to this consultation was provided by ICMA's Pre-Hedging Working Group, which has been formed with sell-side, buy-side and market infrastructure provider members out of ICMA's Secondary Market Practices Committee (SMPC). The response has been provided in the context of international bond markets, and solely in regard to secondary bond markets.

Executive summary:

- ICMA members are of the view that existing code and guidance, such as the FX Global Code (2021, last updated 2024), and specifically the FMSB Standard for the execution of Large Trades in FICC markets ("FMSB Standard", 2021) and FMSB Pre-hedging: case studies Spotlight Review ("FMSB Spotlight Review", 2024) are sufficient for the markets they cover and that any further recommendations from IOSCO should be aligned with those existing codes and practices. Furthermore, ICMA members believe that no further prescriptive rules should be introduced as a result of any future IOSCO recommendations.
- Given the diverse nature of market dynamics and liquidity, asset classes, execution methods and investor sophistication around the globe, we believe IOSCO should provide high-level principles only and allow firms to tailor their internal procedures accordingly.
- Principle based recommendations will also make it easier to implement/consider across asset classes (e.g. equity v OTC markets) which are structurally different

markets.

- In the case of IOSCO deciding to move forward with recommendations on pre-hedging, ICMA members believe that IOSCO should consider embedding proportionality as an overarching principle for implementation of such recommendations. How a liquidity provider implements the recommendations should depend on factors such as the nature of the market, the size and complexity of the transaction, among others.

  Firms and other market participants should ensure that existing codes and guidance are applied consistently. In this context, and as highlighted throughout our response to this consultation, ICMA members would like to refer specifically to the principles and examples under the FMSB Standard and FMSB Spotlight Review. Further and more specific thoughts are provided through our various responses below.

- With respect to the differentiation between various execution channels (as requested by IOSCO under various questions), ICMA members would like to highlight that there should not be any bi-furcation or unlevel treatment between OTC and electronic trading, referring also to the long-established principle of technology neutrality in regulatory action according to which, different media and channels should be treated equivalently. We note that this is in line with what is stated under the FMSB Spotlight Review in that "*pre-hedging principles should be consistent across execution methods*".

Q1: Do you agree that this is the correct definition of pre-hedging? If not, how would you define pre-hedging?

ICMA response:

ICMA would like to emphasise that in line with the definitions under the FX Global Code and the ESMA Call for Evidence On Pre-hedging ("ESMA CfE"), both referenced by IOSCO under Chapter 5 of this consultation report, the IOSCO definition should also include that pre-hedging should be undertaken with the intention to benefit the client.

While IOSCO notes that existing industry codes and standards "may apply inconsistently" – these existing codes and standards should serve as a foundation for IOSCO's definition of pre-hedging and the related recommendations. This would better align the recommendations with widely adopted industry practice and, in doing so, drive greater consistency across the market.

In regard to the diagram on page 24 of this consultation report, ICMA members would like to point out that if the IOSCO pre-hedging definition already includes that pre-hedging takes place "in compliance with applicable laws and rules, including those governing frontrunning, trading on material non-public information/insider dealing, and/or manipulative trading". Therefore, there is no need for Step 1 (pink window) in the diagram, which would effectively be asking the same question i.e. whether pre-hedging activity is compliant with local laws.

Q2: Do you agree with the proposed types of genuine risk management? Are there other factors not mentioned in this report that should be considered for determining genuine risk management?

ICMA response:

ICMA members agree with the proposed types of genuine risk management outlined in the report, however we note that this list should not be considered exhaustive.

Q3: Do you agree that pre-hedging of wholesale transactions should be acceptable where there is sufficient liquidity in the underlying instrument/s to hedge after the trade is agreed to? Please elaborate.

ICMA response:

ICMA's general response to this question would be "Yes". However, whilst ICMA members to not disagree with what is mentioned under point 2**.**, ***Available liquidity*** on page 27/28 of this consultation report, our more detailed response to this question would be that it is not practicable to define the term "sufficient liquidity". As has been seen in other regulatory files such as the MiFID/R bond market transparency and deferral regime frameworks), ICMA would like to stress that it is challenging to define what constitutes a "liquid" instrument and a "liquid" market, as it depends on a large number of factors such as the sub-bond category, issue size, time of day, market situation overall etc. which is also in parts stated by IOSCO under point 3. ***Market Conditions*** on page 28 where it says "Liquidity can be difficult to predict and is not static. Even in very liquid markets the level of liquidity can vary depending on the time of day (e.g., market opening and closing periods) and market conditions on the day (e.g., around market-sensitive news announcements)."

Q4: Can there be a genuine need to pre-hedge small trade sizes in liquid markets for risk management purposes?

ICMA response:

ICMA's general response to this question would be "yes", however, and in line with our comments under Question 3, it would be difficult to exactly define what constitutes a small trade size, as again this is very different and depending on a large number of factors as highlighted above. The concepts of "size" and "liquidity" are fluid concepts.

Q5: Where a dealer holds inventory should they first consider using such inventory to offset any risk connected with an anticipated client transaction or should they be allowed to pre-hedge?

ICMA response:

ICMA's view is that dealers should be allowed to pre-hedge. Inventory should be one consideration for a dealer, but a dealer should not be required to use such inventory before using pre-hedging. The rationale being that liquidity providers may choose to hold inventory for many varied reasons, and the existence of a flow that needs to be pre-hedged should not automatically trigger a liquidity provider exiting that inventory.

Whilst we would agree that existing inventory can be one consideration prior to deciding whether to pre-hedge; it should not be mandatory to dealers to use inventory, given that dealers will have different trading book structures for different desks and purposes.

Q6: What factors should dealers consider in determining the size of pre-hedging an anticipated client transaction (e.g., size, instrument type, quotation environment)? Should there be an upper limit for the pre-hedging amount? If so, what type of limits (e.g., percentage based, Greek based) are appropriate for consideration? Please elaborate your response in relation to bilateral OTC transactions and for competitive RFQ systems including those in electronic platforms

ICMA response:

ICMA members do not think that there should be a prescribed upper limit for the pre-hedging amount.

We would like to refer to case studies in the FMSB Spotlight Review which sets out key considerations for liquidity providers in their approach to pre-hedging, but does not include upper limits for pre-hedging amounts. As stated in the FSMB Spotlight Review on page 10, "Pre-hedging should be reasonable relative to the size and nature of the anticipated transaction taking into account the prevailing market conditions."

In line with this statement, ICMA members think that no specific limits should be put in place and instead, the amount pre-hedged should be proportional to the risk traded and nature of the transaction. There are a wide range of factors involved in assessing the reasonable amount to pre-hedge – these include, but are not limited to, position of a liquidity providers' book at point of request, the likelihood of additional near-term related trades, overall market liquidity, and the number of liquidity providers in competition. In general, we would not envisage a scenario where pre-hedging is close to or higher than 100%.

Consistent with the case studies under the FMSB Spotlight review (see Case Study 1a) on page 12, in a competitive RFQ, a liquidity provider should consider a range of factors, including the liquidity of the instrument and the number of liquidity providers in competition (if known), when considering how to pre-hedge, with the intent to benefit the client and to minimize market impact.

In the context of RFQs to multiple parties, from a liquidity provider perspective it is not always possible for the dealer to assess how many other firms they are in competition with and how likely they are to win the trade and this has a practical impact on how any cap on pre-hedging activity would have to be implemented. Therefore, while the considerations highlighted by the FMSB remain relevant, it is not feasible to have a prescribed or formulaic limit.

Furthermore, and as stated in the Global Foreign Exchange Committee: Commentary on Principle 11 and the role of pre-hedging in today's FX landscape on page 11, "liquidity consumers should be aware of the risks associated with the transactions they request and undertake, and should regularly evaluate the execution they receive. Liquidity consumers should also consider if there are any unintended consequences for liquidity providers by virtue of the way in which they present their orders e.g. asking a larger number of liquidity providers for a large RFQ simultaneously may increase the likelihood of an adverse effect on price."

With respect to voice trading vs electronic trading, ICMA members would like to highlight that "pre-hedging principles should be consistent across execution methods" (see FMSB Spotlight Review page 9), referring also to the long-established principle of technology neutrality in regulatory action according to which, different media and channels should be treated equivalently. In other words, standards around pre-hedging should apply equally to automated and algorithmic trading as they do to manual trading.

Q7: Do you agree with the concept of client benefit described above?

ICMA response:

ICMA agrees with IOSCO that pre-hedging should be undertaken with the intention to benefit the client.

We agree that the benefit to the client can take various forms, including price, speed of execution, mitigation of market impact, size of trade, overall liquidity provision etc. Dealers should evaluate the client's overall execution outcome when evaluating the benefit to the client.

Q8: Do you believe that financial benefits derived from pre-hedging by the dealer should be shared with the client? What proportion of the benefit to be shared with the client would be fair? Please elaborate.

ICMA response:

ICMA members disagree to financial benefits being shared with the client. This would interfere with the dealer acting in its principal capacity.

Furthermore, we would like to highlight that the way in which this question is posed is asymmetric in that it does not suggest that financial losses incurred by the dealer would be shared with the client either.

As per our response to Question 7, the benefit to the client can take many forms and it is overly simplistic to think that such benefit can be apportioned.

Q9: Should pre-hedging always be intended to achieve a positive benefit for the client or is it enough that a dealer pre-hedges for its own risk management and does not detrimentally affect the client?

ICMA response:

As highlighted also under Question 1 of this consultation, ICMA members would agree with pre-hedging being intended to benefit the client, with the definition of pre-hedging under Principle 11 of the FX Global Code on page 18 stating that "Pre-Hedging is the management of the risk associated with one or more anticipated Client orders, **designed to benefit the Client** in connection with such orders and any resulting transactions", and also with the ESMA definition (specifically in this context point iv) in its Call for Evidence conducted in 2022 which states on page 7 that: "any trading activity undertaken by an investment firm, where (i) the investment firm is dealing on its own account, and the trading activity is undertaken, (ii) to mitigate an inventory risk which is foreseen due to a possible incoming transaction, (iii) before that foreseeable transaction has been executed; and **(iv) at least partially in the interest and benefit of the client** or to facilitate the trade**.**

Whilst pre-hedging can be performed for dealer risk management, such risk management should be undertaken with the ultimate aim of benefitting the client.

The client should have the right to question the market practice and the dealer should be able to demonstrate that the principle intent was to improve the outcome for the client, and did not act directly against the client's benefit, either for a specific transaction or on an ongoing basis.

Q10: Should dealers be able to demonstrate the actions they took to minimise the market impact of their pre-hedging trading? In the event of not entering the anticipated client transaction, are there any considerations for the dealer to minimise market impact and maintain market integrity prior to unwinding any pre-hedging position?

ICMA response:

Whereas it is understood that the overall goal is to minimise the market impact of pre-hedging, it is difficult to specify what action exactly needs to be undertaken to minimise such risk in each individual situation. Given that situations may vary and are depending on many market factors (such as market liquidity, instrument, general market conditions, geography). ICMA members do not think that any concrete rules should be prescribed as a result of the IOSCO consultation report and potential recommendations in this regard. It would also be difficult to isolate the market impact of any individual action taken by a dealer when undertaking pre-hedging, as simultaneously other actions/movements are taking place in the market and various factors are influencing the market at the same time.

ICMA also notes that it would be a huge burden on the industry to implement such a specific framework without a clear benefit, and from a practical perspective, it would be difficult for dealers to implement for the reasons set out above.

Other industry codes (such as the FX Global Code and FMSB Standard) highlight a number of considerations for liquidity providers while leaving flexibility for how they are applied according to the nature of the market and transaction. For example, the FMSB Standard states on page 8 under Core Principle 7 that "Pre-hedging should only be undertaken when… (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."

Dealers should also act in line with existing market abuse principles.

Q11: Do you agree with this recommendation on appropriate policies and procedures for pre-hedging? If not, please elaborate.

ICMA response:

Procedures can vary according to different market conditions, depending on which pre-hedging techniques can be different. Therefore, policies and procedures must not be overly prescriptive.

ICMA Members would like to refer to existing codes and guidance on this topic (such as the Global Foreign Exchange Committee: Commentary on Principle 11 and the role of pre-hedging in today's FX landscape Section 8.: Disclosures and controls around pre-hedging on page 10 that states: "In order to engage in pre-hedging, liquidity providers should have in place procedures for handling client orders fairly and in accordance with the Code, including all the applicable Principles. These procedures are part of an appropriate control and compliance framework, which will also include oversight for the accurate monitoring of a liquidity provider's pre-hedging activities to validate that they are consistent with the Code."), as well as the FMSB Standard Core Principle 10 on page 10 stating that: "Market participants should implement such policies and associated control processes as necessary to demonstrate adherence to this Standard" and furthermore that: "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."

Q12: What type of disclosure would be most effective for clients? Why?

ICMA response:

ICMA members believe that it would be sufficient to provide general information about the use of pre-hedging techniques in the form of upfront disclosure.

As per IOSCO findings and client experiences, upfront disclosures are commonly used by dealers, but vary from dealer to dealer. The disclosures are often covered by the Terms of

Business (ToB) of a firm where pre-hedging is often one of a range of matters covered. As a result, the disclosures can often be buried deep in the contractual terms and might sometimes be easily overlooked. In order to ensure clients are fully aware and understand the liquidity provider's full potential to pre-hedge trades, these disclosures should hold a more prominent position in the ToB. See also ICMA response to Q14 regarding the minimum content of upfront disclosure.

In specific cases, dealers may inform the client on a case-by-case basis, for example as stated under FMSB Standard Core Principle 7 on page 8, as follows: "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."

In the context of the determination of a large trade and factors to consider thereunder, we would also like to refer to the following wording stated under FMSB Standard Core Principle 6 on page 8: … "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."

Q13: Should upfront disclosure be applicable irrespective of factors such as the size and complexity of the transaction and/or other factors such as level of client sophistication? Are there any key challenges for dealers to providing pre-trade upfront disclosures?

ICMA response:

Whether a trade is large or not contains an element of subjectivity, and ICMA would therefore refer to existing industry codes (such as the FX Global Code or FMSB Standard) which disagree with the use of any (quantitative) materiality thresholds.

Further thoughts have also been provided under the ICMA response to Question 12.

In relation to defining what constitutes a large trade, ICMA members would agree with the wording in the FMSB Standard as mentioned under Core Principle 6 on page 8as follows: "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."

Q14: What should be the minimum content of any upfront disclosure? Please differentiate between bilateral OTC transactions, competitive RFQs and pre-hedging in the context of electronic transactions.

ICMA response:

Upfront disclosure is related to client consent. The client hereby relies on the dealer to make an informed decision given their market knowledge. To the extent that any specific upfront disclosure on pre-hedging be required, ICMA members are of the view that the minimum content the upfront disclosure should contain would be the dealer's definition of pre-hedging, including the information that the dealer might use pre-hedging as a means to manage risk, with the intention to benefit the client and minimise market impact (see definition of pre-hedging as has been discussed under Question 1), and also its general rationale for when it would be applied and the type of transactions and the circumstances in which the dealer would apply pre-hedging.

When comparing various different communication/trading/execution channels (such as bilateral vs multilateral and electronic vs non-electronic, as well as bilateral or multilateral RFQ via algorithmic trading), ICMA would like to highlight that in general, and also in the context of pre-hedging, there should not be any bi-furcation or unlevel treatment between OTC and electronic trading. (this is valid also in the case of the following questions). Therefore, if any new requirements for pre-hedging were to be introduced, they should be applied equally to every channel and regulators should not differentiate. This was highlighted already in our response to Question 6.

Q15: Should trade-by-trade disclosure be proportional to factors such as the size and complexity of the transaction and/or other factors such as level of client sophistication? What should be the minimum content of trade-by trade disclosure? Please differentiate between bilateral OTC transactions, competitive RFQs and pre-hedging in the context of electronic transactions, in particular in electronic trading platforms.

ICMA response:

ICMA would like to refer to the response provided under Question 13 and also to the FMSB Standard Core Principle 6 on page 8 (which looks at "Communications between client and dealer on Principal basis") stating: "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."

We would also like to refer to the FMSB Standard statement under Core Principle 7 (in relation to "Pre-hedging on Principal basis") on page 9 as follows: "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."

Clients can ask for disclosures from their dealers as part of a bilateral relationship today.

Q16: Are there any challenges or barriers to trade-by-trade disclosure in the context of competitive RFQs and in the context of electronic trading? Please elaborate.

ICMA response:

ICMA members would argue that whilst upfront disclosure (including information that the dealer might use pre-hedging as part of an execution technique through different execution channels) might be beneficial to the client and feasible from a trading perspective, any trade-by-trade disclosure as well as post-trade disclosure of pre-hedging (as discussed under Questions 17 and 18) may not be practicable nor beneficial. ICMA members would agree with the arguments mentioned against trade-by-trade disclosure as mentioned on pages 36 and 37 of this consultation report.

Trade-by-trade disclosure should therefore be considered based on the type of client and nature of the transaction. The necessity for trade-by-trade disclosure & client consent should be determined by the dealer based on market impact of pre-hedging, sophistication of client etc – and in line with existing industry codes.

In line with our comments under Question 13 and Question 15, and again referring to FMSB Standard Core Principles 6 and 7, and in relation to the execution of large transactions, the dealer should determine whether the potential transaction constitutes a large transaction and "whether disclosure should be made on a trade-by-trade or other basis" (as quoted under Q15 already).

Q17: Would clients benefit from post-trade disclosures about the dealer's pre-hedging practices in a transaction?

ICMA response:

ICMA would like to highlight that there are significant limitations around post-trade disclosures. Referring to the FMSB Spotlight Review page 9: "isolating and evaluating the actual impact of any pre-hedging activity on the market is challenging, notably in a flow context. Pre-hedging takes place in a dynamic market environment and therefore attributing price movements to specific pre-hedging activity can be difficult. Furthermore, while the intent of pre-hedging is to benefit the client, this does not mean that there is a guarantee in every case that pre-hedging will result in a better price for the client."

In addition to the above, ICMA members would also like to state that ex-post disclosures have limited use as a firm cannot prove what would have happened should pre-hedging have not taken place.

Furthermore, dealers should not be required to provide any commercially sensitive information to clients (as mentioned also in our response to Question 8).

Dealers should, however, be willing to discuss these topics with clients on a case-by-case basis. As stated under the FMSB Spotlight Review on page 11: "In the case of a large trade, if reasonably requested by a client, and subject to appropriate confidentiality and information handling restrictions, liquidity providers should provide the client with information on the pre-hedging activity undertaken and, where possible, the general observed impact of such pre-hedging activity on the client execution".

As mentioned under Question 15 as well, clients can and should reasonably be able to ask for disclosures from their dealers as part of a bilateral relationship.

Furthermore, liquidity providers should ensure their employees adhere to an internal code of conduct and be prepared to provide evidence of this compliance to their clients.

Q18: Should the nature and form of post-trade disclosure be agreed between the client and dealer at the start of their engagement on an anticipated transaction and be proportional to factors such as the size and complexity of the transaction and/or other factors such as level of client sophistication?

ICMA response:

See ICMA response to Question 17.

Q19: Are there any barriers to post-trade disclosure? Please differentiate between bilateral OTC transactions, competitive RFQs and pre-hedging in the context of electronic transactions, in particular in electronic trading platforms.

ICMA response:

See ICMA response to Question 17.

Q20: Do you agree that clients should have the ability to explicitly inform the dealer that they do not want pre-hedging to take place in relation to a specific transaction (or revoke explicit or implicit consent to pre-hedging)? Are there any circumstances under which the dealer would not be obliged to follow the new client instructions? If not, what are the potential issues or risks to clients of this approach? Please elaborate your response to the question for bilateral OTC transactions, for competitive RFQ systems and for those in electronic trading platforms.

ICMA response:

ICMA notes point 4 under Chapter 8 (page 42) of this consultation report stating that "If a client does not want pre-hedging to be used, the client could consider informing the dealer." In this context, ICMA members are of the view that clients should have the ability to inform their dealer that they do not want pre-hedging to take place in relation to a specific transaction, regardless of trading channel/trading protocol.

ICMA would also like to highlight that as per the FX Code and ESMA CfE definitions, pre-hedging is designed to benefit the client and hence, under the aspect of treating clients fairly and in order to achieve best outcomes for the client, it is important for clients to understand that pre-hedging may be an important tool/technique to be used by the dealer and familiarise themselves with their dealer's pre-hedging practices.

ICMA would also like to refer to the wording on pages 27 and 28 of this consultation report in relation to pre-hedging which states: "Dealers may also consider both the liquidity available to manage the outright risk of the financial instrument or the basis risk associated with hedging the financial instrument using a correlated instrument that may result from an anticipated transaction (e.g., using derivatives to manage interest rate risk or credit risk from a corporate bond). It may be difficult to pre-hedge outright risk in a short period of time due to lack of liquidity available for the financial instrument of the anticipated transaction. Instead, the dealer may focus on pre-hedging its risk exposures for an anticipated transaction by trading in more liquid correlated instruments."

Given that pre-hedging can take place also in correlated instruments, from a practical perspective it may be very difficult to establish in which instruments a dealer cannot trade anymore, once a client request-for-quote was received with an instruction from the client to not pre-hedge.

Q21: Should dealers be required to obtain explicit prior consent to pre-hedge for certain types of transactions? Please elaborate your response to the question for bilateral OTC transactions, for competitive RFQ systems and for those in electronic trading platforms.

ICMA response:

See ICMA response to Question 20.

Q22: Should stand-alone post-trade reviews be conducted for pre-hedging? How would this improve supervision of pre-hedging activities? Could this review be also used to respond to client requests for post trade review of execution practices?

ICMA response:

ICMA's view is that supervisory oversight arrangements should be proportional to the risk traded and cost to implement.

In this context, liquidity providers should determine the appropriate post-trade review process consistent with their compliance and supervisory arrangements and proportional to the nature of the market and transactions type.

ICMA also note the limitations around post-trade reviews whereby isolating the market impact of pre-hedging activities is challenging as it takes places in a dynamic market environment and therefore, attributing price movements to pre-hedging can be difficult. See also ICMA response to Question 17.

Regarding leveraging post-trade reviews to respond to client requests, we reiterate the complexities and challenges associated with post-trade client disclosures [previously mentioned in our response to Question 17], while noting that, as highlighted by the FMSB Spotlight Review page 11 (post trade section): "In the case of a large trade, if reasonably requested by a client, and subject to appropriate confidentiality and information handling restrictions, liquidity providers should provide the client with information on the pre-hedging activity undertaken and, where possible, the general observed impact of such pre-hedging activity on the client execution".

Q23: Do you think it is reasonable (in terms of costs and benefits) to require dealers to have internal controls to ensure differentiation between pre-hedging and inventory management?

ICMA response:

ICMA's view is that the requirement to differentiate pre-hedging vs inventory management trades would be disproportionate, impractical and the operational cost would outweigh the benefit.

For example, it would mean that dealers would need to tag different trades which would be a complex undertaking operationally. It would post a significant cost to firms and is not practicable.

Q24: What level of detail would be sufficient to have adequate records of pre-hedging activity to facilitate supervisory oversight, monitoring and surveillance?

ICMA response:

ICMA members would think that supervisory oversight, monitoring and surveillance should focus on larger trades and higher risk activities.

Q25: Do you believe that the industry codes already meet some or all of the recommendations? If so, please explain in detail how.

ICMA response:

ICMA would like to encourage IOSCO to leverage the FX Global Code and FMSB Standard and FMSB Spotlight Review. These existing industry codes are important and are supported and have been produced by the input of a large number of industry participants. These existing codes are best to define best practices and should be the core effort.