IA POSITION PAPER ON LAST LOOK

The Investment Association ('the IA') represents UK investment managers and has over 220 members who collectively manage more than £6.9 trillion of behalf of clients in the UK and around the world.

The IA is keen to ensure that FX markets are fair and effective, which ultimately benefits our members and their end clients, and helps investment managers to maximise their contribution to economic growth.

The practice of Last Look – whereby a Market Participant receiving a trade request has a final opportunity to accept or reject the request against its quoted price – has received considerable industry and press attention in recent months. There are concerns that the use of Last Look provides dealers with a significant information advantage and disadvantages client execution.

Last Look may have valid applications in order to protect Market Participants from taking on too much risk. Investors also note that not "Last Looking" is not necessarily an indication of good behaviour or quality of execution in and of itself. For example, some HFTs (or banks) could use pools which have no Last Look to rapidly manage their risk ahead of less speedy market participants. Such behaviour could potentially create more market impact than otherwise.

Nonetheless there remain concerns about the way in which Last Look is sometimes applied, particularly with regard to:

- Last Look policy and process transparency;
- Unacceptable practices;
- Data disclosures and timestamps

The Investment Association has therefore developed a position paper on the use of Last Look, setting out recommendations for how these concerns may be best addressed by liquidity providers and venues.

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GUIDELINES FOR LIQUIDITY PROVIDERS ("LPs")

GENERAL POLICY & INTERNAL PROCESSES

Investors are concerned about the lack of transparency around the use of Last Look.

The extent to which Last Look practices may be used may vary depending on LPs' internal policy and processes.

To help understand LPs use of Last Look and to provide a fair comparison, investors would value greater transparency on LPs' general last look policy and procedures.

IA Recommendation:

- LPs to provide each client with a clear internal definition of last look and process of use.
- This should be provided annually, and at any point where changes to the Last Look policy are made.
- Investors understand that different LPs will have different Last Look price tolerances. In order to aid fair comparison, banks should make investors aware of the Last Look price tolerance of orders. This should be made clear upfront in the terms of business.

DISCLOSURE ON SPECIFIC TRADES - STANDARD REASON CODES

Buy-side firms are often unclear as to when their individual trades have been rejected as a result of the application of Last Look, and why Last Look has been applied. This makes it difficult to assess the impact of Last Look on execution.

IA Recommendation:

- The IA considers that the LP should formally inform clients when Last Look is applied on a trade, and explain why the trade has been rejected, drawing from a standard set of reasons, namely:
    - Price tolerance, in order to protect the liquidity provider
    - Price improvement for the client. This should be discussed and agreed with the client as not all clients may be able to technologically accept price improvement.
    - Internal Credit Checks/Breaches
    - Latency
- This information should be passed to the venue in real-time, in order that the user may more easily analyse this information across all LPs.

UNACCEPTABLE PRACTICES

Information leakage is possible, and potentially prevalent, in LPs where electronic traders and voice traders can see the electronic trades and Algo orders.

This applies not only to filled orders or orders passed to the market, but also on orders which are rejected either by the LP or at the venue.

Due to the lack of transparency and potential for misuse of information leakage, there are some specific instances in which the IA considers that the use of Last Look is unacceptable. These include:

- Pre-hedging during the Last Look window.
- Trading activity based on the information derived from rejected trades
- Trading activity based on information derived from RFQs which are in progress or those that are not won

IA Recommendation:

- All LP's should make a statement directly to clients to the effect that they do not engage in any of these practices. This should be made clear upfront in the terms of business. A model for such a statement can be found below

> *"Where last look applies, XXXXX [nor any subsidiary*] is not active in the market during the last look window in relation to your trade request. Further, if your trade request is rejected, XXXXX is not active in the market after the last look window in relation to your rejected trade request. XXXX is only active in the market in relation to your trade request after it has been accepted."*

VENUES

The venues play a crucial role in understanding some parts of their participants' behaviour. They should accept some responsibility for policing the behaviour and whilst they cannot oversee activity across markets they can play a part in offering pools of liquidity from providers whose service matches what IA members regard as best practice, such as those providers making the disclosures described above.

IA Recommendation:

- In order to aid investors, venues should sign up to the Global Code of Conduct, and should make their Last Look policies available to clients.
- Investors note that in many cases even where a venue might sign up to the Code not all of the LPs using the venue will do the same. Therefore it is important for investors to know whether a venue requires LPs using it to sign up to the Code.

DATA DISCLOSURES AND TIME-STAMPING

To properly examine Last Look, and the impact it has on investment managers and their clients, buy-side institutions need to be able to measure its use. As part of this, members need time stamps, accurate to the millisecond, and other disclosures.

IA Recommendation:

- At a 'base case' minimum, all trades should include data and accurate time-stamping for the following:
    - CCY Pair
    - CCY bought/sold
    - Amount bought/sold
    - Direction (buy or sell)
    - Price
    - Product (e.g. spot, FWD, FX Swap, NDF)
    - Submitted by the Buy Side firm
    - Received by the LP
    - Rejected by the LP
    - Completed by the LP
- Ideally however disclosures would go further. The following data should be available from the executing bank. We would also encourage multi-bank platforms to store and provide this data, which, in addition to the above, would also include:
    - Venue (The ECN upon which the order was filled e.g. EBS)
    - When the order was passed to the 3rd party source of liquidity
    - When the order was received by the 3rd party
    - When the order was rejected (and reason code) by the 3rd party
    - PM Order Inception (Time order is originated by the portfolio manager in a standardised)
    - Desk Arrival (Time order arrives at the execution desk)
    - Market Arrival (Time order is submitted for execution)
    - Strategy (Category Type for Algos)
    - Algo Name (Specific Name of Algo)
    - Algo Style (Category Execution Style for Algos e.g. Passive)
    - Limit (Limit price of an Algo if available)
    - Execution Type Execution Style for Algo child slices (e.g. Passive)
    - Trade Type (Method of execution e.g. Voice)
    - Channel (The platform over which the trade was executed, e.g. FXAll)

- Channel (The platform over which the trade was executed, e.g. FXAll)
- Counterparty (Executing counterparty or broker)
- Portfolio (Identifier for portfolio or account from which the trade originated)
- Trader (Trader responsible for the trade)
- Manager (Manager of the portfolio being traded)
- Desk (Investment Desk managing the trade)
- Value Date (Maturity date for the Forward or Swap trade)
- Forward Points (Forward points in basis points)
- Forward Rate (Forward Rate)
- Order ID (Unique ID for the order)
- Parent Order ID (Unique ID for the parent order)
- Client Order ID (Unique ID for the order that the client associates with)
- Notes (Custom comments associated with the trade)

ALGOS – CHILD ORDER VISIBILITY

A 'child order' occurs when an algorithm breaks one or more large orders ('parent orders') into a series of smaller trades.

Algos traditionally have low levels of transparency as to how child orders are handled – for example, if they are being completed, or if they have been Last Looked. Improved transparency is vital in helping to allow members to conduct long term analysis on the performance of LPs and venues as:

- Without it, whilst a member may be able to judge the cost versus arrival price or expected cost, it may not allow the member to see what they are paying away on individual orders
- Overall performance may look good versus an expected benchmark but this may mask costs that are being lost in individual executions
- There are concerns about signalling risk and information leakage during the Last Look window.

Only with this information can members determine the full cost of Last Look, as at least as much potential value is lost on rejected orders as on filled orders.

IA Recommendation:

- It is hugely important to have all child order details, including rejected orders as well as fills, delivered as part of the data and time-stamping disclosures requested above.