

THE INVESTMENT ASSOCIATION



Sub-Custodian Timestamping

Why more needs to be done

The Investment Association (IA) champions UK investment management, a world-leading industry which helps millions of households save for the future while supporting businesses and economic growth in the UK and abroad. Our 250 members range from smaller, specialist UK firms to European and global investment managers with a UK base. Collectively, they manage £8.5 trillion for savers and institutions, such as pension schemes and insurance companies, in the UK and beyond. The UK investment management industry is the largest in Europe and the second largest globally.

Background

In February of 2020, the IA published a “Best Practice Guide for Sub-Custodian Timestamping for FX Trades”¹. This paper was aimed at long-standing concerns regarding reject code transparency in the FX space.

As frequent participants in FX markets, the Investment Association’s (IA) members are keen to ensure that FX markets function well and continue to serve the interests of investors. In order to do this, and to meet their obligations to their clients, they require sufficient data to allow them to monitor the results and effectiveness of their FX trades.

One such category of data is timestamps. When trading, an asset manager will look to receive from their counter-party, at the very least, a timestamp for when the order was received, and when it was executed – these will be provided, ideally, on a millisecond basis.

This data is vital in helping investors meet their obligation with regard to best execution and other regulatory and supervisory requirements, as well as to manage their own FX risk and hedging activities.

Asset managers will often delegate their FX trading to a custodian who then trades on their behalf. This may be done for a variety of reasons, including to take advantage of a custodian’s expertise in this area, or to benefit from a multinational custodian’s trading advantages in third countries. In such instances, a custodian trading on behalf of asset managers should provide their clients with the relevant timestamps for a given trade.

In some instances, a client will delegate a trade to a custodian that requires a trade to occur in an emerging market jurisdiction where that custodian does not have a local desk. In this instance, a custodian will delegate the trade to a local subcustodian, who performs the trade

¹ Investment Association Best Practice Guide for Sub-Custodian Timestamping for FX Trades
<https://www.theia.org/sites/default/files/2020-02/20200213-subcustodiantimestampingforfxtradesbestpracticeguide.pdf>



on their (and therefore the custodian's client's) behalf.

In recent years, our members have raised concerns that in many instances where a trade has been delegated by their custodian to a sub-custodian, they are not receiving back timestamps at anywhere near the level of accuracy required.

For example, they may receive timestamps that are accurate only up to the nearest minutes, or even, in some cases receiving only the day on which a trade takes place.

This lack of precision makes accurate analysis of the quality of a given FX trade very difficult, which in turn has a negative impact on ability of asset managers to manage risk for themselves and their clients. Given the speed at which FX markets move, it has been noted by members that any timestamp that is more than a few seconds wide makes effective transaction cost analysis largely impossible.

Member concerns were heightened by the fact that some custodians appeared to offer more accurate timestamps than others, suggesting that this data was available if needed.

It is therefore vital that this issue is addressed.

The IA's paper therefore looked to identify where local market structural and regulatory issues may genuinely impede precise time-stamping, and then set out a series of best practice recommendations addressing:

- Engagement between clients and custodians
- Transparency of custodians' approach to trading, sub-custodian appointment, and time-stamping in emerging markets; and
- Custodians regularly reviewing and applying commercial pressure to their sub-custodians to ensure, where possible, that data provision is improved.

These recommendations were published after extensive consultation with a number of custodians who agreed that they provided an eminently achievable framework for improved provision of sub-custodian timestamps.

A Lack of Progress

Despite this, members have been disappointed in what they see as a lack of progress in improving the provision of sub-custodian timestamping.

The IA recognises that the COVID-19 pandemic greatly affected the plans of the industry, and that in such circumstances it is natural that there would have been some delay to the implementation of this project.

Nonetheless, the IA notes that while many custodians are able to offer the hoped-for level of timestamping, in some cases the provision of timestamps remains inadequate.

Next Steps

The FX Global Code, under Principle 36, requires that *"Market Participants should keep a timely, consistent, and accurate record of their market activity to facilitate appropriate levels of transparency and auditability and have processes in place designed to prevent unauthorised transactions."* It further states that *"Information should be made available to*



Clients upon request, to provide sufficient transparency regarding their orders and transactions to facilitate informed decisions regarding their market interactions.”

The IA and its members therefore call on custodians to continue to implement the recommendations of the Best Practice guide, and to, where necessary, apply pressure on their sub-custodian partners in order to achieve all possible levels of reform.

The IA looks forward to engaging with custodians and all key stakeholders to ensure progress that benefits the market as a whole.