Is the Global Code of Conduct in Trouble Already?

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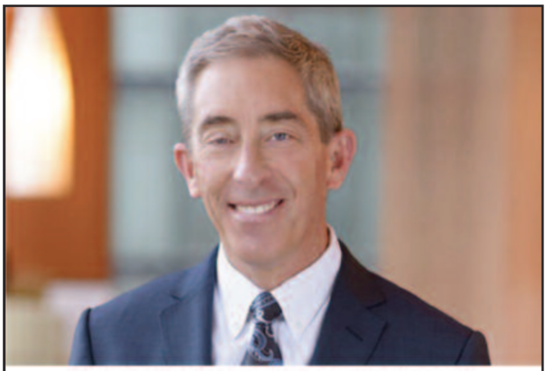
The opening panel discussion of this year's Profit & Loss Forex Network Chicago conference featured an unusually frank and honest discussion about the challenges associated with implementing the FX Global Code of Conduct.

It has been well documented that buy side firms have been much slower than their sell side counterparts to commit to the Global Code, with one panellist at Profit & Loss Forex Network Chicago highlighting that of the 452 entities that have signed the statement of commitment only 23 were asset managers. Indeed, they noted that of the asset managers that have signed the Code, the majority trade currency as their primary business, or even as their sole focus.

"I wondered why more asset managers hadn't signed up and so I printed off a copy of the Code and I sat down and went through it from the perspective of an international equity manager, because those managers have to settle their equity transactions in local currency so they do participate in the FX market," said Michael DuCharme, director, currency solutions, at Mesirow Financial.


Michael DuCharme, Mesirow Financial

DuCharme went on to explain that as he was reading it, he kept a tally of which principles applied to sell side firms and which ones applied to buy side firms. While DuCharme found that all of the principles applied to the sell side, only about 50% were relevant to buy side firms.

"So from a buy side perspective I could reasonably think that [the Code] doesn't really apply to me and so I'm not really that interested in it," he added. "And then also, as I was going through the Code, scrolling through all the different entities, I noticed there was one bank that popped out at me as a signatory to the Code that had recently been in the news because it had overcharged clients for FX trades. And then I sighed a bit and thought that, from a buy side perspective, nothing has really changed."

One interesting analogy used by DuCharme during the discussion to highlight one of the major challenges associated with the Code was a punch-line from Pirates of the Caribbean, a popular Disney film from 2003. In the film certain characters manage to continually evade almost certain death at the hands of the pirates by invoking the "Pirates Code", until the villain of the film, Captain Barbarosa, ultimately declares that the Pirates Code is "more what you call guidelines than actual rules" and therefore ignores it.

"So I just don't know if I have a lot of confidence in the Code," said DuCharme.

Another issue emphasised on the panel was just the sheer amount of ethics and compliance documents that staff at many financial services firms have to read through and agree to – with one speaker saying that across four different documents they're expected to read, understand and commit to 241 pages of documentation every year.

“This made me think about Apple's terms and conditions, or any other online contract that we all look at, scroll really quickly through to the bottom, and click accept because really the only other option is to put the phone back in the box. If you don't say accept, or if you don't sign the attestations that you're going to comply with the Code, you might as well go and look for another job,” said DuCharme.

The response to this pessimism regarding the Code from another panellist was, essentially, that if the FX industry doesn’t rally around it then it is likely to be hit with much more onerous regulation.

“I'm acutely aware that a lot of the misconduct started in the sell side, so I completely understand the view that some buy side might have of: why is this important to us, if it wasn’t our fault? But I think the reality is that [the Code] is important to all of us because we are in a privileged position to get together as an industry and effectively self-regulate by defining the standards that do make sense in a way that appeals to the entire broad church of foreign exchange,” they said.

The speaker continued: “The alternative we should reasonably expect is exactly the kind of regulatory framework that we observe in other asset classes and that may be, and I say this respectfully, decidedly less pleasant and potentially a lot more expensive than the reality of what we have today.”

They argued that the sell side has been much quicker to commit to adhering to the Code due to the massive fines that have already been levied against some of those firms, and therefore they understand the advantages associated with adherence. By contrast, the speaker said that the buy side hasn’t yet recognised the value of the Code to their business, but claimed that going forward conduct issues will become a bigger consideration for asset owners before they hand over assets and mandates to these buy side firms.

“So eventually it becomes almost a commercial differentiator, or a license to operate, for want of a better expression,” they said. “We’re not there yet, but I think that’s very much the direction of travel and when it comes to adherence the magic really starts to happen when there is an obvious commercial benefit to adherence rather than it being viewed as a bit of unnecessary and unwanted homework.”

On this point, another speaker echoed that for the Code to gain widespread adoption, the demand for adherence has to come for the asset owners, arguing the sell side will never demand that its buy side clients sign up to the Code.

“I can guarantee that’s not going to happen,” they concluded.