Explanatory Note: Global Precious Metals Code

The Global Precious Metals Code (‘Code’) sets out a common set of principles to promote the integrity and effective functioning of the global market. This Explanatory Note (‘Note’) provides guidance on how the Code may be used and implemented, it does not replace or supplement the Code. It is intended to provide an overview of the Code, particularly for Market Participants that are not subject to financial regulation.

This Note will be reviewed and updated periodically to reflect frequently asked questions.

Chapter 1: Background and Key Principles

This section provides high-level detail on the purpose, scope and application of the Code.

Key highlights include:

- The Code applies to all Market Participants actively involved in the global Over-The-Counter (OTC) wholesale trading market for Precious Metals;
- The Precious Metals market covers a broad spectrum of participants. Market Participants are encouraged to apply the Code proportionally to their business activities, taking into account their size and complexity; and
- In the event of conflict between the Code and Applicable Laws and Regulations, then the Applicable Laws and Regulations would prevail.

Chapter 2: Ethics

Principles 1 and 2 of this chapter, will apply to all Market Participants irrespective of size or complexity. Acting honestly, fairly and with integrity must underpin the way Market Participants conduct business activity, guide decision making and shape the industry.

Conflicts of interest can potentially undermine a firm’s culture. It should be noted that Principle 3 requires that conflicts are managed. A conflict of interest in itself is not necessarily wrong, or unethical, however, any such conflict should be subject to appropriate arrangements.

Market Participants should put in place appropriate and effective arrangements to eliminate or manage conflicts of interest. This could include:

- Segregation of duties and/or reporting lines;
- Establishing information barriers (for example, physical segregation of certain departments and/or electronic segregation);
- Altering staff duties when such duties are likely to give rise to conflicts of interest;
- Providing training to relevant staff to enable them to identify and handle conflicts of interest;
- Establishing declaration policies and/or records for identified conflicts of interest and personal relationships as well as for gifts and corporate entertainment received; and
- Policies and controls on Personal Dealing.

Chapter 3: Governance, Compliance and Risk Management

Under Principles 1, 2 and 3, all Market Participants should have appropriate governance, risk and compliance frameworks that facilitate responsible participation and provide for oversight of their market activity. There should also be clear and defined escalation routes. The frameworks would differ depending on the type of organisation, size and role in the market. Proportionality is therefore key when Market Participants implement these Principles.

By way of example, a large financial intermediary would be expected to have a compliance and/or risk and internal audit departments who can provide for independent assessments over their market activities and can also review any potential improper practices. On the other hand, small non-financial intermediaries may not have all these functions. Under such circumstances, participants should ensure that review of their market activity is conducted by someone independent from those executing transactions in the market. For example, firms' trading staff should not be leading a review of the effectiveness of and adherence to the risk management and compliance framework.

Additionally, under the policies and procedures as referenced in paragraph 3.2.1, firms should communicate to staff and external parties their procedures for reporting concerns about potentially improper practices and behaviours (including but not limited to cases of illegal, unethical, or questionable practices and behaviours) confidentially and without fear of reprisal or retribution. This can be achieved by making the policies and procedures available to all staff and/or through training sessions. Any escalation, should be reviewed carefully, ensuring that if and when a decision is taken to investigate the matter further, this is done by someone independent of the person/function that is the subject matter of the issue. This could include an independent senior manager and/or an external resource.

Under Principles 4, 5 and 6, Market Participants should be guided by proportionality. Market Participants should assess the risks and use the recommendations provided to address those risks. Some of the best practices listed in these principles are applicable for large financial institutions and may not be appropriate for smaller commercial enterprises.

Paragraph 3.4.1 and 3.5.1 provides a list of ideas that could help ensure an effective compliance and risk management framework. It is to be noted, that where it is advised that Market Participants provide for periodic reviews, assessment and testing of compliance and risk management frameworks, this does not always need to be carried out by an internal audit function, but could be done for example, by management as long as the review/test is carried out by an independent person/function, who is not the subject of the review and/or test. For small and medium-sized companies, which do not have internal audit function or internal controlling function to test formally the application of policies and processes, it would be sufficient, for example, for management to carry out a regular assessment of the compliance and risk management framework.

Under 3.5.2, Market Participants should note, that there are a number of approaches to monitoring and controlling risks related to trading activity. These practices could comprise, but are not limited to:

- The regular monitoring of trading activities, including the identification and internal escalation, as appropriate, of failed, cancelled or erroneous trades;
- Automated or manual monitoring systems to detect actual or attempted market misconduct and market manipulation. Relevant staff should be qualified to detect trading patterns that may suggest unfair or manipulative practices. Market Participants may use certain statistics or metrics to flag behaviour warranting further review, such as off-market rates, repetitive orders and unusually small or large orders. There should be appropriate processes whereby suspicious practices can be promptly reviewed and escalated as appropriate;
- Verification of the valuations used for risk management and accounting purposes, conducted by staff independent of the business unit that owns the risk;
- Independent reporting on a regular and timely basis of risk positions and trader profit/loss statements to the relevant risk management function or senior management, as appropriate, including a review of exceptional deviations of profit/loss from expected levels;
- Prompt and accurate capturing of transactions so that risk positions can be calculated in an accurate and timely manner for monitoring purposes;
- Regular reconciliations of front, middle, and back office systems, with differences identified and their resolution tracked by staff independent of the business unit;
- Timely reporting to a senior body or individual(s) when risk limits have been breached, including follow-up action to bring exposures within limits, and any appropriate measures to prevent a recurrence; and
- Appropriate controls around proper order and quote submission, such as kill switches or throttles in the case of electronic trading submissions. These controls should be designed to prevent the entry or transmission of erroneous orders or quotes that exceed pre-set size and price parameters as well as financial exposure thresholds.

Finally, Principle 6 requires Market Participants to make sure the risk management and compliance controls in place are appropriate. Again, for smaller organisations, this does not mandate the requirement for an internal audit function, but does require the review and assessment to be carried out by someone independent of the control functions.

Chapter 4: Information sharing

All Market Participant should respect and follow any confidentiality obligations that they have, and this should be communicated to all relevant staff.

Under principle 5, Market Participants are again reminded of taking a proportional approach. Providing a list of approved modes of communication and recording communication lines is regarded as best practice. Such recording of lines of communications may be useful and can assist in the:

- Speedy and effective resolution of differences and disputes; and
- Identification through surveillance of instances of inappropriate behaviour, either by staff or by clients.

Chapter 5: Pre-Trade and Execution

Chapter 5 highlights the due diligence requirements and responsible business practices that all Market Participants are expected to adopt. This Chapter also provides guidance when executing transactions.

Market Participants are encouraged to first review their business model, clarify what capacity they act within the market, the types of transactions they enter into, and, where relevant, the processes and procedures around any Mark-up applied. By way of example, if a Market Participant does not act as agent or operate an E-trading platform, then guidance under sections 5.4.5 and 5.4.6 would not be applicable.

The appropriate processes to monitor Mark Up as described in section 5.7.4, will be determined by the Market Participant itself. Such monitoring may be done within the regular trading monitoring system, for example, the identification of off market rates.

Principles under 10 and 11 make clear that Market Participants must not transact with the intent of colluding, disrupting or abusing the functioning of the market.

Chapter 6: Post trade

The Principles set out in chapter 6 direct Market Participants to follow best practice when dealing, confirming and settling trades to avoid a loss of trust in the market, increased error rates or possible market disruption. The standards laid out in the Code will help markets function efficiently for all participants.

Market Participants should note that although this section is focused on trades, it is up to the individual organisations if they wish to extend the application of section 6 to transactions as well. In this Code, a “trade” should be understood as an operation carried out by Market Participants directly involved in the trading of precious metals, which could include unallocated trading, spot or forward deals. A “transaction” will be understood as an operation performed by industrial companies, active in the sale/purchase of physical precious metals products, such as ingots or coins.

It is important that confirmations or equivalent methods of confirming trades and payment instruction details are considered part of a robust and efficient settlement process. Under 6.6.2, it has been advised that best practice for setting up SSIs is to require approvals from two people. This is deemed best practice so as to minimise mistakes. However, it is possible for smaller organisations who do not think it is possible to have this ‘double check’ in place, to address this appropriately and in a way that is more practical for the organisation.

Furthermore, in certain circumstances where trades are matched through a trading platform or at the pre-settlement stage by respective settlement agents, no further action may be required. Where no automatic confirmation or matching process exists, market participants should strongly consider the exchange of relevant information with their counterparty at the point of trade to ensure timely settlement.

Annex 5: Statement of Commitment

How should the statement be used and what are the benefits?

The statement supports the objectives of the Code such as enhancing transparency, efficiency and functioning in the Precious Metals market. To that end, it provides a means by which (i) Market Participants can signal their intention to adopt and adhere to the Code's best practices and (ii) Market Participants and other parties can objectively assess the operational and compliance infrastructure of other Market Participants. Market Participants can use the Statement publicly, by publishing it on their website, or bilaterally, by providing it directly to other Market Participants, such as existing or prospective Clients, or where relevant, by providing it to a relevant industry association in support of its membership.

What does using the Statement represent?

It represents that a Market Participant:

(i) Has made a determination to support the Code and recognises it as a set of principles of best practice for the Precious Metals market;

(ii) Is committed to conducting its market activities in a manner that is consistent with the principles of the Code; and

(iii) Considers that it has taken appropriate steps, based on the size and complexity of its activities, and the nature of its engagement in the market, to align its activities with the principles of the Code.

Ultimately, the decision of what steps should be undertaken in support of a Market Participant's Statement, and in what manner, resides with each Market Participant, reflecting an appropriate internal assessment. For some Market Participants, appropriate steps may include reviewing their practices in light of the Code and establishing and maintaining policies, procedures and controls reasonably designed to support their commitment. In addition, Market Participants might assess the appropriate levels of senior management oversight and establish dedicated staff training or embed them into existing training procedures.

What processes should a Market Participant consider implementing before using the Statement?

Market Participants should consider what type of governance and approval processes would be appropriate for them to implement in connection with their use of the Statement. These processes will vary between Market Participants, but it is anticipated that the individual or group of individuals responsible for approving the Market Participant's use and publication of the Statement will have appropriate oversight of the Market participants market activities and the authority to make statements of the type contained in the Statement. A Market Participant's assessment of the appropriateness of their own implementation policies and practices should be made independently from the assessment by other market participants.

When should a Market Participant start using the Statement?

As noted above, Market Participants may take different steps to support their use of the Statement. The time taken to implement such steps may vary depending on the current practices of the Market Participants size and nature of their business. It is anticipated that most will need approximately 9-12 months to put in place compliance measures before being able to commit to the Statement.

How frequently should a Market Participant review/renew their Statement?

Given that the nature of a Market Participant's business may change over time, Market Participants that use the Statement should consider what steps they will take to review their activities for alignment with the Code's principles. The steps taken should reflect the size and complexity of the Market Participant's market activities and the nature of its engagement in the market. Whereas some Market Participants may consider setting a regular schedule for review, others may vary their approach based on how their business changes over time.

It is anticipated that the Code will be updated from time to time to reflect emerging issues, changes in the market and feedback from Market Participants and others. Upon publication of future updates to the Code, Market Participants should consider renewing their Statement having regard to the nature of the updated provisions as well as the size and complexity of their market activities and the nature of their engagement in the market.