

The Tokyo Foreign Exchange Market Committee (hereafter ‘TFEMC’) has carefully examined ‘ancillary electronic trading system (hereafter AETS)’. The latest technological innovations have made it possible to introduce various AETS which cannot necessarily fall under the traditional concept of ‘Over The Counter(OTC)’ trading schemes. We have examined the issue because there were concerns that the ever-increasing use of such trading systems might significantly influence the overall trading practices in the foreign exchange market in many ways. The wider acceptance of the AETS may enhance liquidity into the FX interbank market. At the same time, in order to benefit from such effects, it is necessary for the users of these systems to understand and observe the customs and codes of conduct of the interbank market.

As a first step in the actual examination of AETS, TFEMC took up ‘EBS Prime’ service provided by EBS. This approach was adopted because the unique and prominent role played by EBS in the foreign exchange market, as an indispensable ‘market infrastructure’, would probably result in a greater market impact of EBS Prime, compared with other systems with similar functions.

The following report, ‘The Study Of Ancillary Electronic Trading Systems(hereafter “The Report”)’ is the result of the discussion at The Market Research Sub-Committee of TFEMC on the potential impact of AETS, focusing mainly on the trading customs, and codes of conduct, and on other issues pertinent to market participants. The Market Research Sub-Committee releases The Report, in hopes of achieving effective usages of AETS by sharing its views on such schemes with market participants. By doing so it hopes to enhance market functioning and prevent unnecessary troubles, with a view to fully realizing benefits of the scheme.

The Report covers the discussion, the scope of which was based on currently available information. TFEMC looks forward to continue its close monitoring of the use of the AETS and resuming discussions if necessary.

5th Jul, 2004

Tokyo Foreign Exchange Market Committee
Chairman Tetsuji Ogino

The Study Of The Ancillary Electronic Trading System

1. EBS Prime

(1) Outline of trading arrangements

The outlines of trading arrangements under EBS Prime is described in Attachment.

EBS holds that legally all trades concluded through EBS Prime between market participants and EBS Prime Bank (hereafter 'EPB'), not affected in any way by arrangements between EPB and EBS Prime Customer (hereafter 'EPC'), are trades between market participants and EPB. This means that EPB will be solely responsible for the trades against other market participants.

(2) Potential impact of the introduction

EBS is one private sector vendor in the foreign exchange interbank market. Meanwhile, the 'EBS Spot Dealing System' provided by EBS is widely used in the interbank market and has become an important 'market infrastructure'. When we consider that EBS Prime is a service based on the 'EBS Spot Dealing System', the impact of the introduction of EBS Prime on the interbank market would be significant, and thus warranted examination relating to market liquidity, trading customs, and codes of conduct.

(a) Market liquidity

EBS Prime provides opportunities for a wider range of market participants to fully access the interbank market. This may enhance market liquidity in the interbank market, which may, in turn, result in enhancing the functioning of the interbank market.

(b) Trading customs

When a market participant, who is relatively less active in the interbank market, trades more actively through EBS Prime, there is a possibility that their behavior may influence trading customs in the interbank market.

Considering that, according to EBS, all trades concluded under EBS Prime become trades between market participants and EPB, not affected in any way by arrangements between EPB and EPC, influence would be strongest in the cases described below under (3)(a).

(c) Codes of conduct

When a market participant, who is relatively less active in the interbank market, trades more actively through EBS Prime, there is a possibility that their behavior

may influence respective codes of conduct in the interbank market.

Particular concern is the possibility of a market participant remaining as a participant in the EBS Spot Dealing System while trading under another counterparty's name (EPB's name) as EPC under EBS Prime. If features of EBS Prime, especially anonymity, are exploited, there is a possibility that some participant may violate or go beyond accepted codes of conduct in the market without risking its reputation. This has implications over various codes such as the 'Model Codes' and the (Tokyo's) 'Code of Conduct'(hereafter 'Interbank model codes').

(3) Recommendations for market participants

In order to prevent negative influences to market customs and codes of conduct outlined in the preceding section, market participants should adopt measures and recognize their roles as described below.

(a) EBS Prime Bank

- As noted above, it is understood that an EPB bears complete responsibility to other market participants regarding trades concluded under EBS Prime (see Attachment). EPB is expected to be fully committed to discharging such responsibilities. This should result in a sound development of trading under EBS Prime. Furthermore, an EPB should recognize that trades concluded over EBS Prime could have significant implications over the reputational risk it faces, and should manage the risk accordingly.
- In order to maintain a functional trading environment in the interbank market, in the following situations, EPB is to demonstrate the same standards of commitment to both EBS prime trades and trades for its own account. (Trade between Market Participant Bank and EPB in STEP 2, look into the chart in Attachment)
 - ① Responding to inquiries from market participants regarding trades concluded through EBS Prime (*)
 - ② Responding to claims that there has been a 'hit or taken by mistake' situation by either its EPC or the counterparties of the trade.
 - ③ Effecting CLS settlements, when the trade is eligible for CLS Settlement; and
 - ④ Extending collateral coverage when trades between EPB and another market participant are subject to collateral arrangements, such as CSA.
- In order to ensure that interbank codes of conduct are adhered to, EPB should provide guidance to EPC, on matters concerning codes of conduct, maintaining secrecy and other interbank trading customs. In particular, EPB should be most

vigilant in preventing code violations by an EPC such as manipulation of market prices by exploiting anonymity offered by EBS Prime (see (2)(c)).

- EPB will be in position to obtain trading information not available to it through trading for its own account by monitoring EBS Prime trades. EPB must not violate the interbank codes of conduct by misusing such information.

(* Note on appropriate responses to inquiries

- EPB should ensure that its contact point for inquiries handled regarding EBS Prime trades are widely known in the market. EPC should always make inquiries to EPB regarding trades concluded through EBS Prime, and it is inappropriate to contact the counterparty of EPB directly for inquiries in view of institutional arrangements regarding EBS Prime.
- The front desk is desirable as the contact point handled regarding inquiries of concerning EBS Prime trades, in view of the fact that appropriate actions must be taken promptly in many instances, such as 'hit or taken by mistake' situation. If the front desk is not bestowed with this function, the section in charge must have a capacity equivalent to the front desk or so as to take appropriate actions promptly.
- It is desirable for an EPB to put in place arrangements, for responding to inquiries from market participants and EPC with respect to EBS Prime trades during any time of the day in which EPC might trade over EBS Prime, regardless of EPB's normal business hours including holidays.

(b) EBS Prime Customer

- EPC should maintain sound trading practices under EBS Prime, in view of its status as an interbank market participant. Also, EPC should adhere to interbank codes of conduct, especially maintaining secrecy and other interbank trading customs taking advice from its EPB as necessary.
- In particular, EPC should not violate in any way interbank codes of conduct, such as manipulation of market prices by exploiting anonymity offered by EBS Prime (see (2)(c)).
- More opportunity to access interbank market via EBS Prime may change the trading style and risk appetite on the trading floor of an EPC. It is desirable for an EPC to recognize that it may be necessary to review its risk management infrastructure or reporting procedures accordingly.

(c) EBS

- It is hoped that EBS would monitor developments pertaining to the impact of trading activity over EBS Prime on trading practices and codes of conduct, and take

appropriate actions as necessary with a view to maximize the advantages offered by EBS Prime .

- During the discussion at the Market Research Sub-Committee, there was a suggestion that disclosing the names of EPC's to the users of EBS Spot Dealing System would have a restraining effect against deviations from interbank codes of conduct, such as manipulation of market prices exploiting anonymity offered by EBS Prime (see (2)(c)).

(d) Market participants in general

- It is desirable for market participants to fully understand the merits and risks of relations arising from the EBS Prime system in the light of their own business activities referring to this Report as necessary.

2. Ancillary Electronic Trading System

TFEMC will carefully monitor schemes other than EBS Prime, which may influence trading customs and codes of conduct in the interbank market, and examine them as it becomes necessary.

It is desirable for market participants to sufficiently understand of the merits and risks of AETS and exercise their own business judgment before participating in a particular system.

EBS Prime

Overview

EBS Prime allows banks with strongest reciprocal credit on EBS Spot to provide their customers (EBS Prime Customers – EPCs) with the best prices on the EBS Spot Dealing System.

EBS Prime offers EBS-approved banks the ability to access and deal on tighter EBS Spot prices available through EBS Prime Banks (EPBs) that have strong bilateral credit.

EBS Prime will allow EPCs to trade (Bid/Offer) at prices that EPBs can see.

EPCs will see 'dealable' prices that are much closer to EBS 'best'.

EBS Prime increases liquidity and provides better access to the best price for all banks.

The EBS Prime Bank can charge the EBS Prime Customer for the use of their credit. This charge can be facilitated on the EBS system via a pip spread agreed by EPB and EPC on the dealt price.

The EBS Prime Bank is legal entity and principal for all EBS Prime trades with EBS market participants. The EBS Prime Customer will only see the EBS Prime Bank as counterparty to trades and Market participants will also only see the EBS Prime Bank as the counterparty.

Note: EBS is considering future enhancements to the system that will enable "name in the market" for EPCs. In this case, the market participant would also see the name of the EBS Prime Customer on the deal ticket, although the legal counterparty will remain as the EBS Prime Bank. There are no plans to permit EBS Prime Customers to see the name of the market participant as counterparty to the EBS Prime Bank.

Two tickets/transactions are generated through EBS Prime – a deal between the EBS Prime Bank and the EBS Prime Customer, and a deal between the EBS Prime Bank and the Market Participant.

EBS Prime Customer

An EBS Prime Customer must meet all EBS Spot criteria (excluding Credit):

- Be a recognised member of the FX inter-bank community
- Be accepted as a trading partner on competing systems (D2-2)
- Be heard through a voice broker
- Be able to obtain credit with EPB

All existing EBS Customers qualify to be a EPC.

EBS will not recommend any particular EBS Prime Bank to a prospective EBS Prime Customer. EBS will at all times remain neutral and not participate in contract negotiations between the EPB and the EPC.

EBS Prime Bank

An EBS Prime Bank must:

- Be an existing EBS Spot Customer
- Have strong bilateral credit and access to prices on a global basis.

Legal Documentation Requirement

1. EBS Prime Bank Agreement including the EBS Prime Terms and Conditions - Parts A & B to be signed by EBS and the EPB, and the EPB must sign the Specified Site Appendix even if there is only one site.
2. Customer Agreement including EBS Prime Terms and Conditions - Parts A & D to be signed by EBS and the EPC, and the EPC must sign the Specified Site Appendix even if only one site.
3. EBS Prime Dealing Rules - No signatures required. Will be provided to both EPB and EPC.
4. Service Agreement – two separate agreements are required, to be signed between (i.) EBS and the EPB & (ii) EBS and the EPC. Both the EPB and the EPC must sign the Specified Site Appendix even if only one site.
5. EPC - EPB may agree/negotiate a separate agreement to be signed between EPB and EPC. EBS would not participate in this negotiation in any way.
6. EBS Prime Set-Up Form and Legal Status Form (if not already a Spot customer)

EBS Prime Benefits

EBS Prime Banks:

- Increased revenue opportunity from using credit that might otherwise remain unutilised
- Increased FX market share
- Potential for increased business with EBS Prime Customers
- The ability to build relationships with and cross-sell other products and services to EBS Prime Customers
- Increased profile within the FX community
- Potential for increased access to Emerging Markets

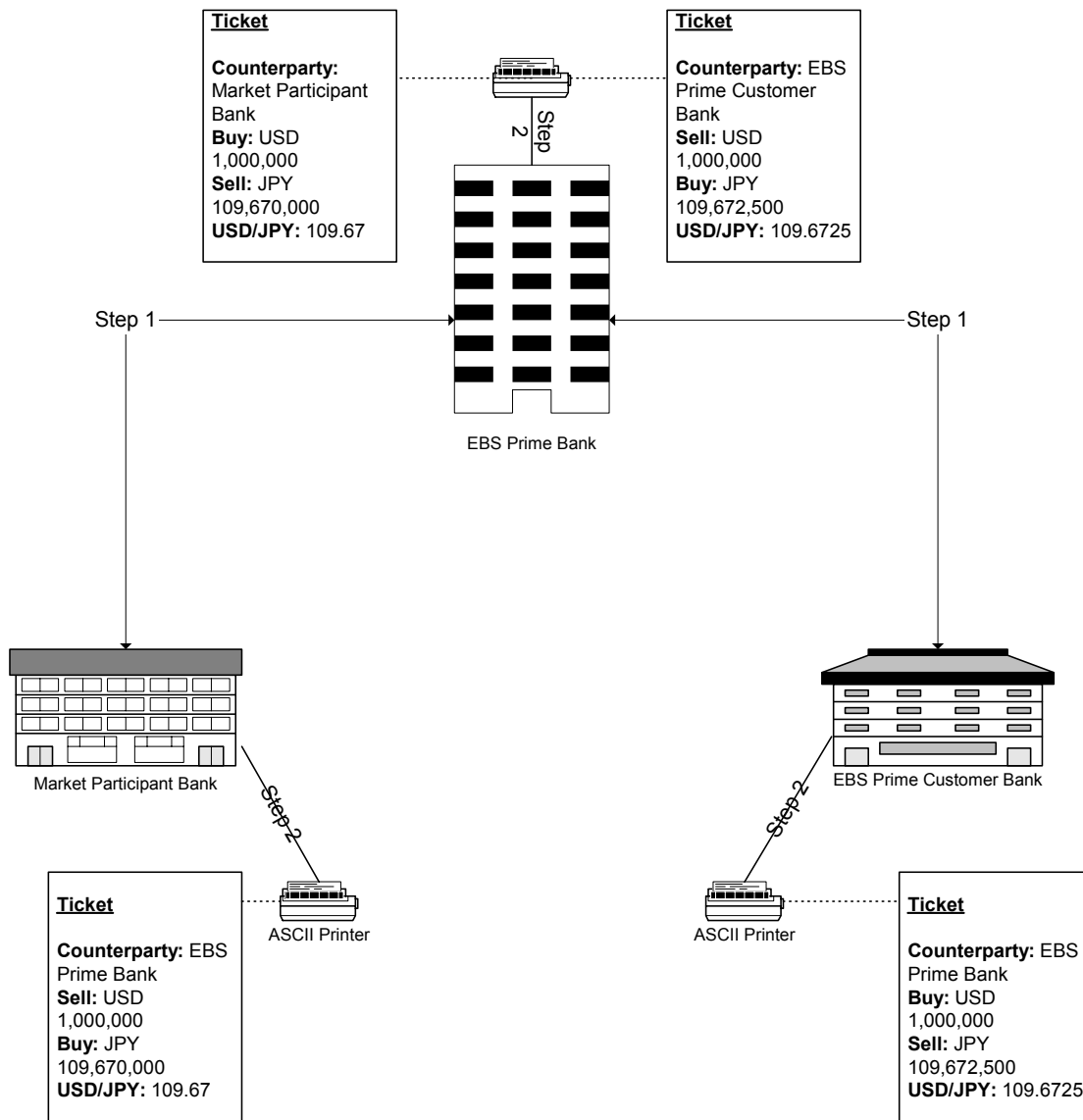
EBS Prime Customers:

- Access to consistently tighter spreads and greater liquidity from the world's leading banks
- Ability to see and trade on prices previously unavailable due to credit limitations
- Increased probability of dealing on bid/offer

EBS Market Participants:

- Increased access to counterparties
- Increased access to liquidity
- Access to better prices (“at the right time and right amount”)

EBS Prime Deal - USD/JPY \$1million



EBS Prime Deal Process

Step 1: EBS Prime Customer hits the Offer submitted by the Market Participant Bank at 109.67 for \$1mio. Alternatively, the EBS Prime Customer submits a bid of 109.67 for \$1mio into the system and is matched with the Market Participant.

Step 2: 2 deals are confirmed and relevant tickets generated. One deal is between the Market Participant Bank and the EBS Prime Bank. The Other deal is between the EBS Prime Customer and the EBS Prime Bank. The EBS Prime Bank is charging the EBS Prime Customer 1/4 pip. This is reflected in the rate and amounts traded between the EBS Prime Bank and the EBS Prime Customer. In this example, the EBS Prime Bank makes a profit of JPY 2,500 (\$22.80) for the deal.

The EBS Prime Bank is the principal legal counterparty for the deal with the Market Participant and for the deal with the EBS Prime Customer.