Public Comment on ***Proposed Regulatory Framework for Financial Benchmarks***

Argus Media's response to the
MAS Consultation on Proposed Regulatory Framework for Financial Benchmarks

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Please find below Argus Media's comments on the MAS Consultation Paper on *Proposed Regulatory Framework for Financial Benchmarks*.

1. About Argus Media

- Argus Media is an independent media organisation whose activities include publication of price assessments for physical energy and related commodities. Argus Media's services are created by an international editorial operation with news bureaus located in the world's principal energy centres under the editorial direction of an editor-in-chief, who reports to the chief executive and who has responsibility for the quality of content. Its well trained journalists operate according to a rigorous and transparent Editorial Code of Conduct and an Ethics Policy (available at: www.argusmedia.com/About-Argus/How-We-Work) that align with the highest standards of journalistic best practice, including the avoidance of conflicts of interest. The company has been active in Singapore for more than 23 years.

- Argus Media is not a financial services company. It is an independent media organisation that reports on energy and commodity markets but is not a participant in the markets and has no vested interest whatsoever in the level of prices in those markets. Its worldwide reputation and continued business success depend on maintaining that independence.

- Argus Media's publishing business faces competition from other specialist commodity media agencies such as ICIS, Platts, RIM, Opis, OMR, e-petrol, IHS McCloskey, Kortes, CRU and Metal Bulletin; other news agencies such as Thomson Reuters, Bloomberg and Dow Jones; information services such as Markit and SNL; commodity exchanges; and broker firms that produce price indexes. Commodity market participants are able to choose which information agency to use, and which prices reported by such agencies to use as benchmarks. The high level of competition in this marketplace drives standards relating to the integrity of an organisation's services.

2. Specific characteristics of commodity markets

- Physical commodity markets are unlike financial markets and so are their benchmarks. Key differences are that:
  - many commodities are heterogeneous, in their quality and in their uses, unlike financial markets, which deal in uniform instruments;
  - a physical energy commodity market evolves from, and around, the physical infrastructure of the industry; and
  - energy companies add value by moving energy down the supply chain from producer to consumer, optimising the value of its production and the cost of its supply through the market. Spot trading is carried out generally for marketing or supply, although the degree to which it is central to a company's operations depends on individual circumstances. Spot trading is executed in a discretionary fashion.

Please see Appendix A for further discussion of the specific characteristics of commodity markets and the fundamental differences compared with financial markets.

3. Regulatory considerations in respect of commodity market benchmarks

- Argus Media fully agrees with MAS, in echo of IOSCO's comments, that "a one-size-fits-all regulatory approach towards financial benchmarks may not be appropriate given the diversity of types of financial benchmarks" (paragraph 1.2). Argus Media also agrees with MAS' comment that "a calibrated approach focusing on certain financial benchmarks would be a more proportionate regulatory response" (paragraph 4.2).

- Argus Media is concerned about the idea that an overarching Regulatory Framework can be developed that would be fit-for-purpose for all benchmarks, given that markets, sectors and benchmark providers are so diverse. Any such principles would need to be adaptable to the disparate global universe of benchmarks. Adaptability is necessary to allow for the specific characteristics of commodity markets, which differentiate such markets from financial markets. Adaptability is further required to allow for the identification of price benchmarks in commodity markets by journalistic enterprise as practised by price reporting agencies (PRAs) such as Argus Media.

- Any new regulatory framework needs to be appropriately applied to the specificities of physical commodity markets in a way that is compatible with IOSCO's *Principles for Oil Price Reporting Agencies* (the PRA Principles)[1]. A synopsis of the IOSCO PRA workstream, prepared by IOSCO Committee 7, is reproduced in Appendix B. Argus Media notes MAS' participation in the IOSCO Committee 7 work to produce the PRA Principles. As recommended and encouraged by IOSCO, Argus Media is now applying the PRA Principles to all its commodity price assessments used as benchmarks.

4. Summary of key points in the consultation response

- Argus Media fully supports legislation that prohibits and sanctions any deliberate act of benchmark manipulation. But it requests a safe harbour to cover genuine mistakes in information voluntarily provided to PRAs, as has already been established in other leading international jurisdictions, so as to avoid deterring the voluntary flow of information to PRAs for market transparency purposes.

- Argus Media suggests clarification around the definition of benchmark as it applies to commodities, to ensure spot and physical forward commodity contracts are clearly excluded and to ensure consistency with the definition set out by IOSCO in the PRA Principles.

- Although MAS currently only intends to designate SIBOR, SOR and NDFs under the proposed regime, Argus Media notes that the regime appears intended to be extendable to commodity benchmarks produced by PRAs. Unfortunately the proposed regime is not "generic" in that sense and would not, in practice, be suitable for commodity benchmarks produced by PRAs.

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[1] IOSCO FR06/12, 5 October 2012 (http://www.iosco.org/library/pubdocs/pdf/IOSCOPD391.pdf)

Argus Media has attached its responses to the individual consultation questions. Argus Media is available to provide further information and detail as required to assist MAS.

Argus Media responses to consultation questions

1. **MAS seeks views on the proposed definition of "financial benchmark"**:

   The Proposed Regulatory Framework for Financial Benchmarks represents a general regime in relation to any and all benchmarks under a proposed definition of "Financial Benchmark" that Argus Media believes is too broad. The Proposed Regulatory Framework for Financial Benchmarks may be proportionate to the systemic risk posed by interest rate benchmarks such as the Singapore Interbank Offered Rate (SIBOR), the Swap Offer Rate (SOR) or foreign exchange spot benchmarks used in the Non-Deliverable Foreign Exchange market, but it is not proportionate with respect to PRA commodity benchmarks because the context in which PRAs operate is entirely different. Further reasons are set out in detail in response to question 3.

   While the consultation paper designates three specific financial benchmarks, the subsequent definition of "financial benchmark" is overly broad, and the proposed regulatory framework leaves open the possibility that other benchmarks may be designated at a later stage.

   MAS proposes to define "financial benchmark" as:

   (1) Any price, estimate, rate, index or value that is –
   (a) Calculated periodically using a formula or other methodology; and
   (b) Used for reference to determine –
   (i) the interest payable or other sums due on deposits or loan agreements;
   (ii) the price, value or performance of any capital markets product as defined under the SFA or investment product as defined under the Financial Advisers Act ("FAA"); or
   (iii) the price, value or performance of any product offered by any entities regulated by MAS;
   (2) Or such other price, estimate, index or value as MAS may prescribe.

   Argus Media believes this definition either already captures commodity benchmarks produced by PRAs, or could be extendable in scope to include them.

   One of the criteria proposed by MAS for designating a financial benchmark is its systemic importance to global financial markets (para. 4.3). This criterion is balanced by MAS taking into account factors such as the degree of discretion involved in the benchmark setting process, and the public interest. As a result, it is unclear how these criteria may be applied in practice, leading to regulatory uncertainty, and the concern remains that many of the proposals are not proportionate for wide application.

   In Argus Media's view, the proposed regulatory template would not, in practice, be suitable for commodity price assessments published by Argus Media and its competitors that are used as benchmarks. This point is discussed in more detail in our response to question 3.

   In relation to limbs 1(b)(ii) and (1)(b)(iii) of the proposed definition of "financial benchmark", Argus Media notes that it is unclear whether this scope could include the price of a spot physical commodity contract or physical forward contract, if for example these are offered (ie transacted) by an entity regulated by MAS — such as the physical commodity trading desk of the Singapore branch of a financial institution. But this would be inconsistent with approaches to financial benchmarks in other jurisdictions, which do not include the price of spot physical and physical forward commodity contracts if these prices are not used as references in derivatives contracts. Argus Media encourages MAS to clarify that the price of spot physical and physical forward commodity contracts is not intended to fall under the proposed definition of "financial benchmark".

   Further, Argus Media would encourage MAS to ensure that its definition of "financial benchmark" is consistent with the definition of commodity benchmarks developed by IOSCO in its PRA Principles document, and that MAS makes explicit that commodity benchmarks are excluded from the financial benchmarks legislation being proposed for Singapore. IOSCO defines commodity benchmarks in the PRA Principles document as "any commodity price assessment that is referenced in derivatives contracts".

2. **MAS seeks views on the proposal to amend the SFA to prohibit specifically the manipulation of financial benchmarks and to introduce criminal and civil sanctions for such misconduct:**

Argus Media supports legislation that prohibits and provides for effective and proportionate sanctions for deliberate acts (including deliberate attempted acts) of market manipulation including the manipulation of benchmarks. Argus Media considers this is one important component to underpin market integrity. As MAS notes in paragraph 3.1, benchmark manipulation may already be an offence under various existing legislation and Argus Media has always understood this to be the case. However, to the extent that further clarification is considered beneficial, Argus Media would support a specific provision to prohibit the deliberate manipulation of any financial benchmark.

Argus Media would at the same time like to emphasise the importance of ensuring that inadvertent errors in information provided by market participants to a benchmark publisher such as Argus Media and other commodity PRAs, are not captured by any anti market/benchmark manipulation provisions.

Recalling that all information is provided by market participants to PRAs on a wholly voluntary basis, it is vital that this voluntary flow of information is not destabilised by measures that could see a market participant risk civil, or even criminal sanction, as a result of a mere inadvertent error in information they provide to a PRA. Faced with such disproportionate risk, market participants would undoubtedly reduce or even fully cease providing information to PRAs for the purpose of market transparency. This would result in less transparent commodity markets and would foster conditions where market integrity is inherently lower. It would undermine the integrity of price assessments and benchmarks published by PRAs, no doubt directly contrary to the intent.

The importance of providing a 'safe harbour' to ensure that inadvertent errors in information provided to PRAs are not caught by anti-benchmark manipulation provisions has already been recognised in other major international jurisdictions.

In the US, the Dodd-Frank Act contains a specific safe harbour clause:
''(C) GOOD FAITH MISTAKES.—Mistakenly transmitting, in good faith, false or misleading or inaccurate information to a price reporting service would not be sufficient to violate subsection (c)(1)(A)." [Dodd-Frank Act Section 753]

Similar provisions are contained within the European Union's REMIT regulation (EU 1227/2011), which covers European energy (power and gas) markets: *"Forms of market manipulation include......**deliberately** providing false information to undertakings which provide price assessments or market reports with the effect of misleading market participants acting on the basis of those price assessments or market reports; ....."* [REMIT Recital 13, emphasis added]

Equivalent provisions can also be found in the draft Market Abuse Regulation currently being finalised by the European Parliament and European Council:
*"(d) transmitting false or misleading information or providing false or misleading inputs **where the person who made the transmission or provided the input knew or ought to have known that it was false or misleading**, …. which manipulates the calculation of a benchmark"* [latest draft Market Abuse Regulation[2], emphasis added]

Argus Media therefore urges MAS to ensure that any new legislation in this area is consistent with other major international jurisdictions and contains a clear 'safe harbour' ensuring that genuine errors in information provided to PRAs are not captured by anti-manipulation provisions. This would ensure that Singapore establishes a well-calibrated and proportionate regime, would avoid unwittingly deterring the voluntary flow of information to PRAs for market transparency purposes and therefore would support the integrity of commodity benchmarks published by PRAs.

[2] 2011/0295(COD) 11384/13, http://register.consilium.europa.eu/pdf/en/13/st11/st11384-ad02re01.en13.pdf

3. **MAS seeks views on the proposal to regulate benchmark setting activities relating to "designated benchmarks", where such benchmarks will be designated based on the consideration of the factors stated in paragraph 4.3:**

Argus Media notes the MAS comment that it "does not intend to regulate the setting of all financial benchmarks" (Section 4.2), and agrees that a calibrated approach focusing on certain financial benchmarks would be a more proportionate regulatory response. While noting that MAS has not expressed any view indicating a likelihood that a commodity benchmark published by a PRA could be made a "designated benchmark" by MAS, nevertheless Argus Media notes that the proposed regime set out in the Consultation Paper appears intended in principle to be extendable to PRA commodity benchmarks.

It is therefore important for Argus Media to set out its view that the proposed regulatory regime — as described in sections 5 and 6 of the Consultation Paper — would not, in practice, be suitable for commodity price assessments published by Argus Media and its competitors that are used as benchmarks. In this sense, the regime is not "generic", but is understood to have been principally designed to apply to the specific circumstances of particular interest rate and FX mechanisms, which typically are panel-based monopoly mechanisms that have the exclusive objective of producing interest rate and FX benchmarks for the purposes of trading. Each of (a) the submitters of information, (b) those sponsoring the benchmark setting mechanisms, and (c) those using the benchmarks for purposes of trading, are likely to be regulated financial services firms or to be acting on behalf of regulated firms. Moreover, all are likely to have establishments in Singapore.

The context in the case of energy and other commodity price assessments and benchmarks is entirely different. Unlike SIBOR, SOR and NDFs, this is not an environment where many of the activities are carried out by financial services firms that are already regulated in respect of their general business activities. Argus Media and its competitors are not financial services entities but independent news agencies, operating in competitive international markets, whose principal business purpose as news agencies is producing a wide range of news and market price information relating to energy markets. Only a tiny percentage of their published price assessments are used as benchmarks, and it is their subscribers, and not themselves, that decide whether to use a price assessment as a benchmark. Only a small minority of their subscribers are regulated financial firms using these price assessments for trading purposes.

The proposed regulated activity of "administering a designated benchmark", as designed for SIBOR, SOR and NDFs, would not be practicable, affordable or proportionate for application to editorial operations such as those at Argus Media.

In relation to the proposed regulated activity of "providing or transmitting information or expressions of opinion", the sources of market information available to Argus Media's journalists are located throughout the world, are often not established in Singapore and are rarely employed by regulated financial services entities. The proposal that providing information should become a regulated activity would not be practicable and would risk reducing transparency in wholesale energy markets if attempted.

Argus Media would point to the warnings in this regard made by IOSCO about what it described as "precipitous regulation": *"Because data are submitted [to PRAs] on a voluntary basis, precipitous regulation of PRAs or requirements that oil market participants who submit data to PRAs submit all of their transaction data potentially could result in some oil market participants to decrease or even cease their submission of data to PRAs."* [Principles for Oil Reporting Agencies, FR06/12, p8]. The same is of course true for any physical commodity market, not simply oil.

In short, the current MAS consultation does not take account of the different characteristics of benchmark creation in markets beyond SIBOR, SOR and NDFs, and in particular in physical commodity markets. Should, therefore, MAS ever consider bringing other benchmark activities into regulation through designation, there will be a need for new public consultations, including new impact assessments, which may well result in the need to amend the new Part of the SFA currently contemplated for the legislation (paragraph 4.4). The assumption appearing to underpin MAS' Consultation Paper — that all other types of benchmarks can be accommodated within the proposed framework — is unfortunately not correct.

4. MAS seeks views on the proposal for SIBOR, SOR and FX Benchmarks to be designated, thus subjecting the benchmark setting activities related to these benchmarks to regulation:

Argus Media has no comment on this proposal insofar as it relates specifically to SIBOR, SOR and FX Benchmarks. However should there be consideration at any point of making a PRA commodity benchmark a "designated benchmark", please refer to the discussion on this point in Argus Media's response to question 3.

5. MAS seeks views on the proposal to issue best practice guidance to regulated financial institutions to only use a financial benchmark if it is satisfied that the benchmark administrator has effectively implemented the IOSCO Principles:

Argus Media notes that paragraphs 1.2 and 4.8 of the Consultation Paper refer to the "IOSCO Principles" as meaning the proposed Principles for Financial Benchmarks, currently being drawn up by IOSCO. However, Argus Media would like to draw to MAS' attention that in relation to commodity benchmarks produced by PRAs, IOSCO has finalised and promulgated the Principles for Oil Price Reporting Agencies ("PRA Principles")[3].

IOSCO's PRA Principles were drawn up by IOSCO in collaboration with the International Energy Agency (IEA), International Energy Forum (IEF) and Organisation of the Petroleum Exporting Countries (Opec), during a detailed and specific two-year workstream under G20 mandate. The PRA Principles were published in October 2012 and endorsed by the G20 in November 2012.

In its final report on the PRA Principles, IOSCO states that: "Although the PRA principles were developed in the context of PRAs and oil derivatives markets, PRAs are encouraged to implement the principles more generally to any commodity derivatives contract that references a PRA assessed price without regard to the nature of the underlying." [FR06/12, p7]

Therefore Argus Media respectfully requests that if MAS is minded to issue best practice guidance to regulated financial institutions as contemplated by question 5, such guidance should clarify that in relation to any commodity benchmark published by a PRA, the relevant norms are the IOSCO PRA Principles (FR06/12).

6. MAS seeks views on the proposal to require entities carrying out the regulated activity of "administering a designated benchmark" to be licensed by MAS:

7. MAS seeks views on the proposed admission and ongoing requirements for Administrators:

Argus Media understands that MAS currently has no plans to license the activity of "administering a designated benchmark" in relation to any benchmark other than SIBOR, SOR and FX Benchmarks (as further defined in the Consultation Paper).

[3] IOSCO FR06/12, 5 October 2012

While noting that MAS has not expressed any view indicating a likelihood that a commodity benchmark published by a PRA could be made a "designated benchmark", and therefore its "administration" become a licensable activity, nevertheless Argus Media notes that the proposed regime outlined set out in the Consultation Paper appears intended in principle to be extendable to PRA commodity benchmarks.

However, the contemplated regime is not, in practice, suitable for commodity price assessments published by PRAs such as Argus Media and used as benchmarks. Should, therefore, MAS ever consider bringing any such benchmark activities into regulation through designation, there will be a need for new public consultations, including new impact assessments, which Argus Media anticipates would result in the need to amend the new Part of the SFA currently contemplated for the legislation (paragraph 5.1).

Please refer to the detailed discussion on this point in Argus Media's response to question 3.

8. MAS seeks views on the proposed regulation of Submitters:

9. MAS seeks views on the proposed admission and ongoing requirements for Submitters of designated benchmarks:

10. MAS seeks views on the proposal to include powers to compel entities to be Submitters to designated benchmarks:

Argus Media understands that MAS currently has no plans to regulate "submitters" in relation to any benchmark other than SIBOR, SOR and FX Benchmarks (as further defined in the Consultation Paper).

While noting that MAS has not expressed any view indicating a likelihood that a commodity benchmark published by a PRA could be made a "designated benchmark", and therefore any "submitter" to such a benchmark become licensable, nevertheless Argus Media notes that the proposed regime outlined set out in the Consultation Paper appears intended in principle to be extendable to PRA commodity benchmarks.

However, as discussed in detail in response to question 3, the contemplated regime is not, in practice, suitable for commodity price assessments published by PRAs such as Argus Media and used as benchmarks. Should, therefore, MAS ever consider bringing any such benchmark activities into regulation through designation, there will be a need for new public consultations, including new impact assessments, which may well result in the need to amend the new Part of the SFA currently contemplated for the legislation (paragraph 6.1).

The commodity markets are not an environment where many of the activities are carried out by financial services firms that are already regulated in respect of their general business activities. Argus Media and its competitors are not financial services entities but independent news agencies, operating in competitive international markets, whose principal business purpose as news agencies is producing a wide range of news and market price information relating to energy markets. Only a tiny percentage of their published price assessments are used as benchmarks, and it is their subscribers, and not themselves, that decide whether to use a price assessment as a benchmark. Only a small minority of their subscribers are regulated financial firms using these price assessments for trading purposes.

The proposed regulated activity of "providing or transmitting information or expressions of opinion", as designed for SIBOR, SOR and NDFs, would not be practicable, affordable or proportionate for application to many of the sources of market information available to Argus Media's journalists. The proposal that providing information should become a regulated activity would risk reducing transparency in wholesale energy markets if attempted, as many sources would decide to cease all co-operation with PRAs as an easier and safer alternative to regulation (see below for further discussion).

The provision of information by market sources to PRA journalists is wholly voluntary, and it is very difficult to envisage how compulsion might work in practice in international commodity markets. Argus Media wishes to emphasise the very significant detrimental effect on the flow of information to PRAs that would be caused by what IOSCO refers to as "precipitous regulation" of market sources to PRAs: "*Because data are submitted [to PRAs] on a voluntary basis, precipitous regulation of PRAs or requirements that oil market participants who submit data to PRAs submit all of their transaction data potentially could result in some oil market participants to decrease or even cease their submission of data to PRAs.*" [Principles for Oil Reporting Agencies, FR06/12, p8]. The same is of course true for any physical commodity market, not simply oil.

This was further emphasised recently by UK energy regulator Ofgem, which in echo of IOSCO's words warned that attempts to regulate sources that contribute information voluntarily could lead to withdrawal of co-operation by market participants. Ofgem says this would represent "a breakdown in the quality of the price assessment process with negative consequences for the market and consumers"[4].

As IOSCO and Ofgem have both warned, precipitous regulation of market sources contributing information voluntarily to PRAs in respect of commodity markets could lead to a cessation in the provision of this information. In predicting the likely reaction of such sources to such regulatory risk, Ofgem commented: "The simplest way to mitigate this risk may be to withdraw co-operation and to decline to provide it."[5]

Given the highly diverse and international nature of commodity markets, in which market participants operate at levels of scale varying from some of the largest companies in the world to small distributors, and in different jurisdictions, it is difficult to envisage how a mandatory regime could be implemented in practice on market sources that provide information to Argus Media's journalists. Most participants in physical commodity markets are not regulated financial services firms, and large numbers are not located in Singapore.

Therefore Argus Media urges MAS to be fully cognisant that in respect of any PRA commodity benchmark contemplated in the future to be made a "designated benchmark", the regulation of "submitters" to that benchmark in a manner principally designed for financial markets and without sufficient consideration of the different nature of commodity markets, would undoubtedly prompt many participants in the physical commodity markets to stop voluntary reporting to the PRA. Far from supporting the integrity of PRA benchmarks, a reduction in the flow of information to PRAs would reduce market transparency and undermine the integrity of their benchmarks, directly contrary to the intended objective.

Argus Media believes a more effective way to reinforce the integrity of PRA commodity benchmarks is for regulators such as MAS to encourage full reporting to PRAs, and to make clear that genuine inadvertent errors in information provided to PRAs will not be caught by anti-benchmark manipulation provisions. This last point can be achieved by incorporating a clear "safe harbour" clause (see response to question 2) in any legislation.

[4] Ofgem, 90/13, 6 June 2013
[5] Ofgem, 90/13, 6 June 2013

Appendix A

Specific characteristics of commodity markets and the fundamental differences compared with financial markets

Interest rate and other financial markets are different from physical commodity markets

Financial markets are unlike physical commodity markets and so are their benchmarks. Key differences are that:

- a physical energy commodity market evolves from, and around, the physical infrastructure of the industry;
- energy companies add value by moving energy down the supply chain from producer to consumer, optimising the value of its production and the cost of its supply through the market. Spot trading is carried out generally for marketing or supply, although the degree to which it is central to a company's operations depends on individual circumstances. Spot trading is executed in a discretionary fashion; and
- many commodities are heterogeneous, in their quality and in their uses, unlike financial markets, which deal in uniform instruments.

The physical infrastructure of the energy industry means that it cannot operate like a securities or interest rate market. Securities are traded in discrete units by a simple electronic transfer of ownership. In financial markets, the timing of purchases and sales is linked to market circumstance and the positions and strategies of market participants. In contrast, energy must be transported through specialised infrastructure, with all the constraints and limitations associated with that infrastructure, including breakdown and delay, which together determine the timing of purchases and sales. For example, oil has physical bulk that must be transported through shipping, pipelines and storage, creating large distinct units of purchase and sale that can only be transacted between aptly equipped and similar market participants.

Regulations that are suitable for financial markets can therefore be inappropriate in markets that operate around the utilisation of infrastructure. In the oil, coal and LNG markets, unit size of trade and timings of delivery can, by necessity, be forced to vary because of variable elements such as the weather. Standardised contracts in oil must have flexibility because crude oil and refined products are produced in non-standardised forms. Even the elements of standardised contracts, such as quality, volume and timing of delivery, must have operational tolerance.

In the physical world of energy commodities, flexibility is essential because the goal of spot trading is to optimise companies' operations as they move commodities from one location to another. The key concern of companies that operate in the energy commodity industry is the added value they provide in one or more sectors of the supply chain. Spot trading may help optimise a company's operations, but if the costs and risks associated with regulation are too great then companies may withdraw from spot markets, damaging market transparency.

The agreement of purchase or sale is only one small element in a complicated physical transaction that may take weeks to complete. The spot sale is negotiated several weeks before loading, while the delivery may be several weeks after loading. Between loading and delivery, transportation must be chartered, quality checked and confirmed, loading or injection must take place and offtake or delivery must be completed.

Commodity markets are complex and diverse

An unpublished report on oil price reporting agencies (PRAs) prepared for the IEA, IEF, Opec and IOSCO by consultants Liz Bossley and Dr John Gault (June 2011) recognised the complexity in price identification: "Oil prices and oil price reporting can appear to be very complex and lacking in transparency. There are reasons for this complexity, which, when understood, can go a long way towards clarifying the meaning of oil prices published by the PRAs and explaining the differences amongst their price assessments."

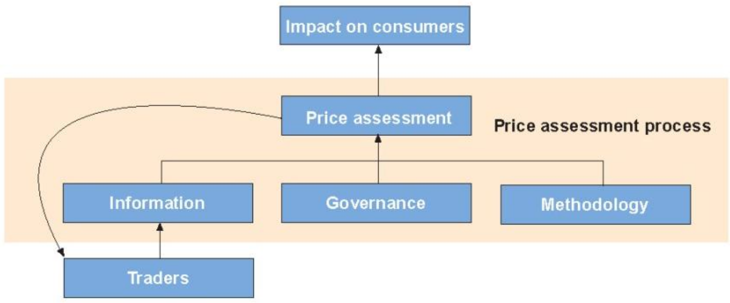
In formulating the PRA Principles published in October 2012[1], IOSCO — assisted by the IEA, IEF and Opec — specifically recognised:

- that "PRAs meet a legitimate physical market need, have increased transparency [and] have facilitated hedging activities"[2];
- "the realities and complexities of the physical market for oil, which are nonstandard and diverse"[3];
- "substantial variations between the services offered, price assessment methodologies and policies used by different PRAs"[4]; and
- that "because data are submitted on a voluntary basis, precipitous regulation of PRAs or requirements that oil market participants who submit data to PRAs submit all of their transaction data potentially could result in some oil market participants to decrease or even cease their submission of data to PRAs"[5].

UK gas and electricity market regulator Ofgem published *Pricing benchmarks in gas and electricity markets – a call for evidence* on 6 June 2013. It states: "In considering the relationship of these issues to the Libor investigation, we concluded that although there might be some potential similarities, the risks to energy markets are lower due to the fundamental differences between the two benchmarking processes. The Libor rate is based on contributions from market participants; PRAs, unlike Thomson Reuters who formulate Libor, have the discretion to disregard unreliable data; and there are multiple PRAs operating in energy markets."[6] These fundamental differences greatly reduce the potential for conflicts of interest of the type that contributed to the Libor fixing scandal.

Ofgem provides a useful illustration to show how the price reporting process works in energy markets[7].

The key inputs to the price assessment process



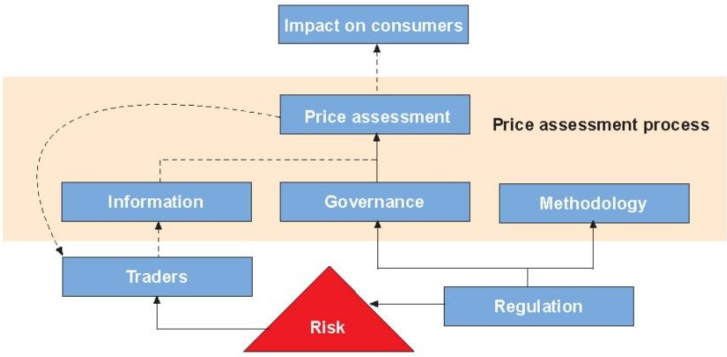
— *Ofgem*

The important impact of market transparency and the role of PRAs in facilitating efficient markets can be clearly demonstrated. For example, in Europe it was the developing liquidity on the traded natural gas markets and the reporting on market growth that directly allowed many European markets to break the oil-linked pricing model. This oil price link had kept European consumer gas prices artificially high for years while the actual value of gas fell. Without the growth of trade and the development of reliable price assessments for traded gas (done almost exclusively by PRAs as the vast majority of trade was and still is over the counter) it would not have been possible for European gas importers to challenge the key supplier's dominance of European supply and its dogged insistence on oil-linked pricing.

[1] IOSCO FR06/12
[2] IOSCO FR06/12, p5
[3] IOSCO FR06/12, p6
[4] IOSCO FR06/12, p9
[5] IOSCO FR06/12, p8
[6] Ofgem, p9
[7] Ofgem, p13

The special vulnerabilities of price identification processes in energy markets to inappropriate regulation

The potential impacts of reguation on the price assessment process



— *Ofgem*

Ofgem also provides an illustration showing the potential impacts, both positive and negative, of regulation on the price reporting process in energy markets[8]. Solid lines to the right show positive impacts and broken lines to the left and at the top show potential negative impacts of regulation.

In commenting on this illustration, Ofgem writes:

> *2.18 Various forms of regulation can impact on this process. The impacts may be positive. Some types of regulation may drive an emphasis on strong governance and transparent methodologies, which in turn can increase confidence of the market in that they understand how price assessments are made and the processes set out are adhered to.*
>
> *2.19. However, some types of regulation may also introduce risks to the process. In particular greater regulatory scrutiny of the information flows could introduce a perception of risk (irrespective of whether the risk is real) to those providing the information. Regulation should increase the quality of information provided, but could reduce the willingness of parties to provide it. Information is provided on a voluntary basis and the simplest way to mitigate this risk may be to withdraw cooperation and decline to provide it. This is turn can lead to a breakdown in the quality of the price assessment process with negative consequences for the market and for consumers.*
>
> *2.21 Good information is essential for a well-functioning market. It is therefore very important for both regulators and market participants alike to consider this relationship and ensure that the market continues to have good quality information available.*

Ofgem's warnings about the significant risks from increased regulatory scrutiny of information flows in energy markets echo earlier warnings in the conclusion of the *Principles for Oil Price Reporting Agencies: Final Report* prepared by IOSCO with the collaboration of the IEA, IEF and Opec:

> "It is important to understand that these principles recognize that there is no requirement on any physical market oil participant to submit transaction data to PRAs. Because data are submitted on a voluntary basis, precipitous regulation of PRAs or requiring that oil market participants who submit data to PRAs submit all of their transaction data potentially could result in some oil market participants to decrease or even cease their submission of data to PRAs."[9]

It is important to emphasise that Ofgem and IOSCO are regulatory agencies and therefore have no vested interest in making these points.

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[8] Ofgem, p14
[9] IOSCO FR06/12, p34

Appendix B

The PRA benchmark workstream

The price reporting agencies (PRAs) are actively engaged in implementing the *IOSCO Principles for Oil Price Reporting Agencies* in co-operation with IOSCO Committee 7 during an agreed 18-month evaluation period. The IOSCO Committee 7 Implementation Questionnaire of 21 March 2013 begins with a clear synopsis of the IOSCO PRA workstream, reproduced below in full.

> In October 2012 IOSCO published a final report *Principles for Oil Price Reporting Agencies* (Oil PRA Report), which detail a set of recommended practices for PRAs that produce assessments which are referenced by oil derivatives contracts.[1] That report is the IOSCO Board's response to the G20 Leaders' Cannes Summit Final Declaration (2011) for work relating to oil price reporting agencies (PRAs) for *"…Recognising the role of Price Reporting Agencies for the proper functioning of oil markets, we ask IOSCO, in collaboration with the International Energy Forum ("IEF"), International Energy Agency ("IEA"), Organisation of Petroleum Exporting Countries ("Opec") to prepare recommendations to improve their functioning and oversight to our Finance Ministers by mid-2012*", and the G20 Leaders' Los Cabos Declaration.[2]
>
> Although the PRA principles were developed in the context of PRAs and oil derivatives markets, PRAs were encouraged to implement the principles more generally to any commodity derivatives contract that references a PRA assessed price without regard to the nature of the underlying.
>
> The PRA principles establish a benchmark against which market authorities[3] can determine whether a PRA assessed price referenced or proposed to be referenced in an oil derivatives contract has been constructed under procedures that reflect the PRA principles.
>
> In its report, IOSCO adopted the following approach to implementation of the principles:
>
> 1. Voluntary adoption and implementation of the principles by PRAs in their internal policies and procedures and/or through industry codes; and/or
> 2. The use by a market authority of its rule approval and/or review authority over derivatives contracts, as appropriate, to refuse admission to exchange trading or central clearing of any oil derivatives contract that references a PRA-assessed price which, in the opinion of the market authority, has been developed under policies and procedures that do not reflect effective implementation of the PRA principles and call into question the reliability of an assessment.
>
> The Oil PRA Report provided that "IOSCO, in collaboration with the IEA, IEF and Opec, will review the extent of implementation over the next 18 months" (ie, since the October 5, 2012 publication date). Such a review will evaluate the degree to which the principles have been implemented by PRAs and the principles' impact. In assessing implementation, IOSCO will seek to obtain the input of market

[1] FR06/12 Principles for Oil Price Reporting Agencies, Report of the Board of IOSCO http://iosco.org/library/pubdocs/pdf/IOSCOPD391.pdf. Price reporting agencies were defined in the report as: "Publishers and information providers who report prices transacted in physical and some derivatives markets, and give an informed assessment of price levels at distinct points in time. PRAs also report news stories relevant to the commodity markets." The report focused on PRA assessments in oil.

[2] G20 Leaders' Cannes Summit Final Declaration (November 2011), ¶56
http://www.g20.org/images/stories/docs/eng/cannes.pdf;
G20 Leaders' Los Cabos Declaration (June 18-19) ¶62,
http://g20.org/images/stories/docs/g20/conclu/G20_Leaders_Declaration_2012_1.pdf
We also look forward to IOSCO's recommendations to improve the functioning and oversight of Price Reporting Agencies in November 2012, which will be produced in collaboration with other mandated organizations (IEF, IEA and Opec), and task Finance Ministers to take concrete measures in this area as necessary.

[3] "Market Authority" is defined as a governmental regulator, a self-regulatory organization, a regulated market or a clearing organization. See Appendix "A" Glossary of Common Terms attached (from the Oil PRA Report).

authorities, stakeholders, and PRAs on the degree to which the principles have been implemented, and may make further recommendations as appropriate at the end of the evaluation period.

At its Mexico City meeting in November 2012, the G20 welcomed the recommendations contained in the Oil PRA Report and asked IOSCO to liaise with the IEA, IEF and Opec to assess the impact of the principles on physical markets and report back.[4]

IOSCO intends to work co-operatively with PRAs to achieve implementation of the principles set out in this report.

[4] Communiqué of Meeting of the G20 Finance Ministers and Central Bank Governors, Mexico City, November 5, 2012 http://www.g20.org/load/780984360