Commodity Markets Council - Europe

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18 December 2019

CMCE response to European Commission consultation on the review of the Benchmark Regulation

Section 2 – Critical benchmarks

IBOR reform

Q1: To what extent do you think it could be useful for a competent authority to have broader powers to require the administrator to change the methodology of a critical benchmark? Very useful –not useful at all (5 categories). Please explain.

CMCE members are concerned by the approach envisioned by the European Commission to grant competent authorities with new powers to change methodology of critical benchmarks. We believe that regulatory interference in methodologies should be minimised and that the oversight and transparency provisions built into the framework should be enough to ensure that authorised benchmark administration is robust.

Article 23(6)(d) of the Regulation, which empowers competent authorities to require a change to the methodology or to other rules of a critical benchmark when it risks becoming unrepresentative of its underlying market, is already a concern for CMCE members in this regard. Competent authorities already have sufficient well-established tools to ensure the adequate supervision of critical benchmarks which do not require NCAs to intervene in the methodology of a benchmark.

In addition, assessing commodity prices is an activity which requires staff who have been thoroughly trained in price assessment and the appropriate methodologies. Given the high degree of expertise necessary it is unclear whether any circumstances could arise in which it would be anything except damaging to markets for a competent authority to have the power to intervene in or change the methodology of a commodity benchmark.

Therefore, the assessment of commodity price benchmarks should stay in the remit of benchmark administrators. Competent authorities' powers to ask for a change in a benchmark's methodology should not be broadened beyond what already exists in article 23(6)(d). Indeed, we would welcome the deletion of this existing provision.

Q2: Do you consider that such corrective powers should apply to critical benchmarks at all stages in their existence or should these powers be confined to (1) situations when a contributor notifies its intention to cease contributions or (2) situations in which mandatory administration and/or contributions of a critical benchmark are triggered? Yes / no? Please explain.

Q3: Are there any other changes to Article 23(6)(d) BMR relative to the change of methodology for critical benchmarks that might be desirable to improve the robustness, reliability or representativeness of the benchmark? Yes / no? Please explain.

Orderly cessation of a critical benchmark

Q4: To what extent do you think that benchmark cessation plans should be approved by national competent regulators? Agree completely –not agree at all (5 categories) + explain

Q5: Do you consider that supervised entities should draw up contingency plans to cover instances where a critical benchmark ceases to be representative of its underlying market?

Colleges

Q6: To what extent do you consider the system of supervision by colleges as currently existing appropriate for the supervision of critical benchmarks? Very appropriate –not appropriate at all (5 categories). If not, what changes would you suggest?

Section 3 – Authorisation and registration

Authorisation, suspension and withdrawal

Q7: Do you consider that it is currently unclear whether a competent authority has the powers to withdraw or suspend the authorisation or registration of an administrator in respect of one or more benchmarks only? Very unclear –very clear (5 categories)

The Regulation does not provide for authorisation or registration at the level of the benchmark but rather at the level of the benchmark provider. It is currently unclear whether a competent authority has the power to withdraw or suspend one or more benchmarks. It may be prudent to consider whether competent authorities' ability to withdraw specific benchmarks could be clarified. The withdrawal of an entity's authorisation would be a significant and potentially disproportionate action and may not be appropriate in a case where a specific benchmark or family of benchmarks requires specific or temporary remedy. Therefore, CMCE considers it would be more appropriate for NCAs to be able to apply these powers at a more granular level – i.e. individual benchmarks.

However, this does introduce other issues with regard to the Benchmark Register. Currently, EU benchmarks are not listed individually on the register, only the administrator is listed. Therefore, the suspension/withdrawal of a single benchmark within an administrator portfolio would be unclear. This becomes even less clear where authorisation has been granted for a benchmark family.

Continued used of non-compliant benchmarks

Q8: Do you consider that the current powers of NCAs to allow the continued provision and use in existing contracts for a benchmark for which the authorisation has been suspended are sufficient? Totally sufficient –totally insufficient (5 categories). Please explain.

Q9: Do you consider that the powers of competent authorities to permit continued use of a benchmark when cessation of that benchmark would result in contract frustration are appropriate? Very appropriate –not appropriate at all (5 categories). Please explain

Whilst CMCE understands that to avoid market disruption, continued use of a benchmark, post cessation, for legacy/existing contracts could be beneficial, the practicalities of this are unclear. If cessation is due to the benchmark no longer being representative of the underlying market, then continued reference could itself be disruptive. Cessation implies the benchmark is no longer available. Would the administrator be required to continue calculation and publication based on insufficient data? If not, it is unclear how legacy/existing contracts would be dealt with.

Section 4 – Scope of the BMR

Q10: Do you consider that the regulatory framework applying to non-significant benchmarks is adequately calibrated? Which adjustments would you recommend? Completely adequately calibrated –not well calibrated at all (5 categories). Please explain.

Q11: Do you consider quantitative thresholds to be appropriate tools for the establishment of categories of benchmarks (non-significant, significant, critical benchmarks). If applicable, which alternative methodology or combination of methodologies would you favour? Completely appropriate –not appropriate at all (5 categories). Please explain.

Q12: Do you consider the calculation method used to determine the thresholds for significant and critical benchmarks remains appropriate? If applicable, please explain why and which alternatives you would consider more appropriate. Completely appropriate –not appropriate at all (5 categories). Please explain.

Q13: Would you consider an alternative approach appropriate for certain types of benchmarks that are less prone to manipulation. If so, please explain for which types. Completely appropriate –not appropriate at all (5 categories). Please explain.

CMCE members believe that the current provisions of BMR do not take account of the different risk profile of commodity benchmarks. The risk profile associated with physical commodity markets is different to that in financial markets and relates to variations in price over time resulting from the extraction, transportation and the delivery of physical commodities. Commodity derivatives are predominantly used to manage these risks along this supply chain. Commodity benchmarks are by essence less prone to distortion caused by financial flows. In addition, PRAs have been implementing the IOSCO PRA principles since 2012. Recital 34 of BMR says that "(…) *Certain commodity benchmarks are exempt from this Regulation but would need to nevertheless respect the relevant IOSCO principles*". The small commodity benchmark exemption is predicated on administrators adhering, in the case of Annex II administrators, to the IOSCO PRA principles. This resulted in these principles becoming an integral part of PRAs' management policies and operational processes.

Hence, CMCE members would ask for a higher de minimis threshold to EUR 5 billion, as explained in our response to question 22.

Section 5 – ESMA register of administrators and benchmarks

Q14: To what extent are you satisfied with your overall experience with the ESMA register for benchmarks and administrators? If not, how could the register be improved? Completely satisfied –not satisfied at all (5 categories). Please explain.

CMCE would like to raise the following issues to improve the ESMA register:

- Having separate threads and therefore search criteria for EU and third country benchmarks is not ideal;
- The "related third country benchmarks" column and associated link does not link to the related third country benchmarks;
- Benchmark families should be listed/searchable.

Q15: Do you consider that, for administrators authorised or registered in the EU, the register should list benchmarks instead of/in addition to administrators? Agree completely –do not agree at all. (5 categories)

Yes. CMCE considers the register should allow for the lowest level of granularity – individual benchmarks. The user should be able to drill down to the benchmark level from administrator, endorsing entity, benchmark family etc. or simply search by name of benchmark.

Section 6 – Benchmark statement

Q16: In your experience, how useful do you find the benchmark statement? Very useful –not useful at all (5 categories)

Q17: How could the format and the content of the benchmark statement be further improved?

Q18: Do you consider that the option to publish the benchmark statement at benchmark level and at family level should be maintained? Should definitely be maintained –should definitely be removed (5 categories). Please explain

Section 7 – Supervision of climate related benchmarks

Q19: Do you consider that competent authorities should have explicit powers to verify (1) whether the chosen climate-related benchmark complies with the requirement of the Regulation and (2) whether the investment strategy referencing this index aligns with the chosen benchmark? Agree completely –donot agree at all (5 categories). Please explain.

Q20: Do you consider that competent authorities should have explicit powers to prevent supervised entities from referencing a climate-related benchmark, if such benchmark does not respect the rules applicable to climate-related benchmark or of the investment strategy referencing the climate-related benchmark is not aligned with the reference benchmark? Agree completely – do not agree at all (5 categories). Please explain.

Section 8 – Commodity benchmarks

Q21: Do you consider the current conditions under which a commodity benchmark is subject to the requirements in Title II of the BMR are appropriate? Completely appropriate –completely inappropriate (5 categories). Please explain.

Recital 34 of BMR acknowledges the need to introduce specific requirements for commodity benchmarks that differ from the overall regime for financial benchmarks, given the unique characteristics of the physical commodity markets. Article 19 BMR sets out the distinct regime for commodity benchmarks by providing a tailored regime in Annex II instead of the requirements in Title II. However, there are exceptions for regulated-data benchmarks and benchmarks based on submissions by contributors the majority of which are supervised entities, or critical benchmarks with gold, silver or platinum as the underlying asset. We believe that the question of the majority threshold should be deleted.

Whether or not a benchmark should be supervised under Annex II or Title II should depend on the features of the benchmark, not the regulatory status of any contributors. The Annex II regime is actually the *only* appropriate regime under the current BMR to apply to PRA commodity price assessments, regardless of the identity of any contributors. It is an appropriate regime tailored to the features of commodity benchmark administration.

The specific nature of commodity benchmarks has been rightly recognised by the EU and by IOSCO. BMR indeed acknowledges "*the role of the IOSCO principles as a global standard for the provision of benchmarks*" (Recital 45). Annex II is modelled closely on IOSCO's Principles for Price Reporting Agencies which provided that PRAs and their contributors should operate in all cases according to IOSCO's PRA Principles. This position was reconfirmed in IOSCO's subsequent Principles for Financial Benchmarks which differentiated the approach necessary for commodity benchmarks. The threshold in Article 19 BMR which reclassifies the governance regime applicable to a commodity benchmark if a majority of contributors are supervised entities should be removed. Unlike many financial benchmarks the mix of contributors to a PRA benchmark can vary continuously. This means that at any one time there might be a minority of supervised contributors while on the next day there could be a majority. For example, consider a commodity benchmark subject to Annex II one of whose existing contributors subsequently becomes authorised as a MiFID II investment firm, tipping the balance over the majority threshold specified in Article 19. In this case, (a) the benchmark administrator and NCA would need to change the whole basis on which the administrator is supervised, (b) the administrator would need to engage with its contributors about those changes, seeking adherence to a code of conduct, initiating reporting protocols which are not suitable for commodity markets and so forth (which may deter some of those contributors from continuing) or (c) the administrator may want to exclude these contributors. Furthermore, if the mix of contributors were subsequently to change again, the process may have to be reversed.

None of these outcomes would have a positive impact on the integrity of the benchmark, in fact they are more likely to harm it by reducing the level of contribution. Similarly, for the same reason, administrators may be deterred from accepting contributions from supervised entities. In addition, an unintended consequence could be that the proportion of non-EU contributors increases as these would not be considered supervised entities.

Nothing in the nature of the population of contributors could amount to a good supervisory reason for switching regimes from Annex II to Title II. Title II was not designed with PRAs in mind and any requirements to apply Title II would be very damaging. Title II is not compatible with the PRA assessment methodology for physical commodity markets, commodity benchmarks could end up being subjected to an entirely different regime that is inherently ill-suited to such benchmarks. The requirements set out in Annex II remain relevant and appropriate regardless of the sources of information used by PRAs. We do not think this could have been intended under BMR given the care and consideration around maintaining

separate regimes for commodity benchmarks and financial benchmarks through the IOSCO process, and as subsequently enshrined in BMR.

Another anomaly is that the majority supervised entity threshold in Article 19 would place PRAs in jurisdictions outside the EU which are expected to comply with IOSCO's PRA Principles, in the impossible position of applying inconsistent standards to the same benchmarks.

There is no requirement for market participants in the physical commodity markets to provide information to PRAs. All information is submitted on a wholly voluntary basis. Any additional onerous obligations – such as the adherence to a code of conduct, or additional reporting – could have a chilling effect which would likely lead to them ceasing voluntary contributions to PRAs on the advice of their compliance and legal departments. Both IOSCO and energy regulators have issued specific warnings about this risk.

PRAs are not also always able to monitor the number of supervised entities providing information. The mix of contributors to a PRA benchmark is constantly changing. For example, global editorial teams in PRAs work collaboratively and teams covering market A (where the published price is used by an exchange as a 'benchmark' within BMR's scope) will interact with colleagues covering markets B, C and D (where the published prices are not 'benchmarks') because these are linked physical markets (different grades of gasoline for example). Professional market reporting, which is integral to price reporting, in the commodity space requires that these relationships between different commodities are understood and reported on in context. A constant monitoring exercise of supervised contributors over the full range of the editorial activities is not always possible or reasonable.

Q22: Do you consider that the compound de minimis threshold for commodity benchmarks is appropriately set? Completely appropriate –completely inappropriate (5 categories). Please explain.

We believe that the small commodity benchmark exemption in article 2(2)(g) should be reviewed. First, we believe the limitation of the exemption to benchmarks on "only one trading venue" should be amended to include the provision of a minimum trading volume for benchmarks traded in more than one trading venue. Secondly, we would ask for the €100mn threshold to be increased in a more proportionate way given the thresholds for significant and critical benchmarks, which are €50bn and €500bn respectively. Thirdly, the 'only one trading venue' exemption is anti-competitive without any apparent justification. The exemption provides an unhelpful incentive for Annex II benchmark administrators not to license benchmarks to more than one trading venue.

The exemption for small commodity benchmarks is so narrow that in reality, most commodity benchmarks will simply have a one size fits all approach applied, without taking into account scale and volume. We believe it should be possible to introduce more meaningful tiers or thresholds that take a more proportionate view of the risks BMR seeks to prevent. Hence, CMCE members would advocate for a threshold at EUR 5 billion. Concerning the methodology for calculating the notional value, the calculation should be based on publicly available data.

Section 9 – Non-EEA benchmarks

Q23: To what extent would the potential issues in relation to FX forwards affect you? Very much –not at all (5 categories). If so, how would you propose to address these potential issues?

Q24: What improvements in the above procedures do you recommend?