



56, Avenue des Arts

B- 1000 Brussels

T. +32 (0)2 508 37 11 – F. +32 (0)2 511 23 28

info@euribor-ebf.eu - www.euribor-ebf.eu

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D2695B-2013

16.05.2013

Euribor-EBF Public Comment on OICV-IOSCO Consultation on Principles for Benchmarks

Introduction:

Euribor-EBF is an international non-profit making association under Belgian law founded in 1999 with the launch of the Euro and based in Brussels (56, avenue des Arts, 1000 Brussels). Its members are national banking associations in the Member States of the European Union which are involved in the Eurozone and the Euro-system¹.

Euribor-EBF has a mission of informing its members, other organizations, the European authorities and the national regulatory authorities on issues relating to the interbank rates. It develops and supports activities related to the Euribor (Euro Interbank Offered Rate), the USD Euribor, the Eonia (Euro OverNight Index Average), the Eurepo (benchmark rate of the large Euro repo market) and the Eonia Swap Index (derivatives market reference rate for the Euro).

It also supports other practical initiatives, fostering the further integration of the European financial market. These initiatives include the improvement of the liquidity and transparency of the short term commercial paper markets, by means of a harmonized framework for short-term European paper 'STEP', in collaboration with the European Central Bank.

Background documentation:

Euribor Code of conduct: http://www.euribor-ebf.eu/assets/files/Euribor_code_conduct.pdf

Euribor Technical Features: http://www.euribor-ebf.eu/assets/files/Euribor_tech_features.pdf

Euribor Panel Composition: <http://www.euribor-ebf.eu/euribor-org/panel-banks.html>

Frequently Asked Questions about Euribor:

<http://www.euribor-ebf.eu/assets/files/Euribor%20FAQs%20Final.pdf>

Euribor-EBF website: www.euribor-ebf.eu

¹ The list of Euribor-EBF National Members Associations is available at <http://www.euribor-ebf.eu/assets/files/euribor-ebf-members.pdf>

General Comments:

- Euribor-EBF welcomes the opportunity to answer the OICV/IOSCO consultation on financial benchmarks. Euribor-EBF's response will mainly refer to the Euribor benchmark, from an administrator's perspective.
- Euribor EBF wishes to emphasize that this response purports to discuss the possible evolution of the benchmark production and use but is in no way meant to express any comment on the current benchmark production process and the various parties who currently participate in it as well as the parties using such benchmarks.
- Euribor-EBF considers that the benchmark-setting process must rely on a robust Code of Conduct, setting out, *inter alia*, a clear definition of the benchmark and transactions to be taken into account (where applicable), clear contributions process guidelines, and sufficient safeguards at contributors' level and calculator agent's level. It should also have in place appropriate and independent oversight functions to enable the benchmark operating effectively and ensuring its quality.
- Euribor-EBF believes it is appropriate to have a common set of core principles for benchmarks governance but stresses the need to allow enough flexibility to adapt to each benchmark's features. An element of proportionality may help to bring the large variety of benchmarks and indices better into compliance with the principles.
- Euribor-EBF underlines the importance to coordinate benchmarks' reforms at European and global level to ensure consistency and a level-playing field.
- Euribor-EBF is currently analysing the technical feasibility of setting, along with the large majority of Euribor panel banks and in addition to Euribor, a transactions-based benchmark. A real-transactions calculation test is currently being set up with the collaboration of the European Central Bank.

Response to Consultation Questions:

2. Additional measures to address risks resulting from Submission-based Benchmarks or control structures: Additional measures have been specified within certain principles to address specific risks arising from a reliance on Submissions (principles 4, 10, 13 and 17) and/or from ownership or control structures (Principles 2, 5 and 16).

- a. **Should these additional requirements apply to Submitters and Administrators of all submission-based Benchmarks or Benchmarks with the specified ownership/control structures?**
- b. **If not, please explain why all or some submission-based Benchmarks or Benchmarks with the specified ownership/control structures should be exempt.**

Euribor-EBF generally agrees with the additional requirements specified to address risks derived from submission-based Benchmarks (principles 4, 10, 13 and 17) as well as those aimed at Benchmarks with specified ownership/control structures (principles 2, 5 and 16).

More specifically, Euribor-EBF would like to comment on the following principles:

- **Principle 2: Oversight Of Third Parties**

Euribor-EBF agrees that when activities relating to the benchmark determination process are undertaken by third parties (i.e. calculation agent), the Administrator should maintain appropriate oversight of such third parties.

Euribor-EBF would like to point out that, while the Administrator should define its expectations regarding procedures and controls being applied by the calculation agent and retain adequate control on the activities of the calculation agent, the calculation agent must also have a responsibility to ensure that it has in place robust safeguards and controls in order to prevent from any irregularities in the benchmark's computation. In this respect, the calculation agent should have its own Code of Conduct and disclose all information relevant to the computation's process. In addition a Service Level Agreement (SLA) should be established by both the calculation agent and the Administrator.

Euribor-EBF also agrees that the calculation agent should perform internal audits. Moreover the Administrator should perform a yearly audit on the calculation agent.

Additionally Euribor-EBF believes that **substantive back-testing** of the quoted rates must be performed by the calculator agent and the Administrator, with report to the Steering Committee. It is important to note that, Euribor being an estimation of the market by the

panel banks, the back-testing cannot be based on real-transactions (panel banks do not quote their own position) but should rather be based on contribution criteria/deviation safeguards.

Finally, Euribor-EBF believes that a “four-eye” principle (cross-checking by different parties) on the calculation process should be performed by the Administrator and the EU supervisor before publishing benchmark data.

- **Principle 4: Control Framework For Administrators**

Euribor-EBF agrees that the Administrator should implement an appropriate control framework reviewed periodically for the process of determining and distributing the Benchmark.

First, the benchmark-setting process must rely on a **robust Code of Conduct**, setting out, *inter alia*, a clear definition of the benchmark and transactions to be taken into account (where applicable), clear contributions process guidelines including sufficient safeguards at contributors’ level and calculator agent’s level.

In addition, Euribor-EBF introduced a **Euribor Management Annual Certification Form** in July 2012, whereby panel banks must certify that (1) all internal procedures are set up to ensure a **robust process for the submission of contributions, excluding any internal and external influences**, (2) that all submitted contributions are the **bank’s appreciation of the evolution of the interbank market in the Eurozone according to the Euribor definition** and (3) that the **Euribor Code of Conduct** is fully respected when contributing to the fixing.

Likewise, Euribor-EBF believes that a **strong contribution process** must be defined by the Administrator and implemented by the submitters. Euribor-EBF is currently developing written guidelines on the contribution process and general responsibilities, including *ex-ante* and *ex-post* controls and organizational and administrative arrangements with a view to avoid potential conflicts of interests, as further detailed under principle 13. These guidelines also provide that contributing staff should receive appropriate training and confirm understanding of rules and policies.

Moreover, Euribor-EBF believes that a whistleblowing mechanism must be applied at different stages: (1) at the contributors’ level, with extensive *pre-* and *post-*controls; (2) at the calculator agent’s level, with robust and automatic controls and safeguards with regard to the individual submissions; (3) at the Administrator’s level, with substantive back-testing and report to the Steering Committee and (4) at Supervisory authority level, which Euribor-EBF believes it should apply ‘four-eye principle’ (cross checking by different parties) on the calculation process run by the calculator agent should be performed by the European Supervisor.

Separately, Euribor-EBF stresses that the composition of submitting panels must be as large and representative as possible in order to preserve the credibility, the representativeness and accuracy of a benchmark, in particular when it is based on submissions.

Euribor being a European benchmark, we believe it is important to ensure that the panel is large enough to reflect faithfully the geographic diversity of the still segmented money market in the euro zone. Meanwhile, this criterion must be well balanced with market standards in order to maintain the credibility of the index.

With the recent events, contributing to an index may be considered as an additional burden, given the costs and resources that additional compliance and governance measures will generate, as well as a potential source of reputational risk. While making the contribution to the benchmarks compulsory might be a solution in order to preserve their accuracy and representativeness, Euribor-EBF recommends that the regulators envisage the possibility of introducing incentive measures in order to encourage panel banks to continue participating in setting these benchmarks.

Finally, with regard to the monitoring of submissions, Euribor-EBF believes that in addition to the *pre* and *post* submission controls further detailed in the contribution guidelines (confer principle 13), a regular review of the submissions must be held on a regular basis by the Steering Committee. In this context, the calculator agent provides Euribor-EBF with regular statistical reports on panel banks contributions, which are discussed at each Steering Committee meeting. Those reports include statistics on the highest and lowest 15% contributions excluded from the final calculation, on the banks which missed contributing on some days, and on the number of times the calculator agent called some panel banks to remind them to contribute or to validate their submission.

Euribor-EBF would also like to point out that generally a benchmark administrator cannot have the authority to ultimately ensure that principles are implemented within the entity of a contributing firm. This is and should be the task of the competent supervisors. Similarly, Euribor-EBF believes that principles relating to internal sanctions and remuneration policies should remain the responsibility of the contributing firms. Meanwhile, Euribor-EBF may suspend or exclude a bank from the panel in case an entity does not comply with those principles.

- **Principle 5: Internal Oversight**

Euribor-EBF agrees that the benchmark-setting process should have in place an appropriate and independent committee in charge of the oversight functions in order to enable the benchmark operating effectively an ensuring its quality.

Euribor-EBF is currently reviewing the **composition of the Euribor Steering Committee** by reducing the number of members from panel banks to a minority and including other

classes of stakeholders in order to further develop its independence and diversity. According to the Euribor Code of Conduct, “All the members must be independent and not subject to instructions from the companies or organisations to which they belong”.

The tasks and obligations of the Euribor Steering Committee as well as the nomination and replacement process are defined in the Euribor Code of Conduct.

At every meeting, Euribor Steering Committee members review the level and use of the index and how it reflects market conditions; the composition of the panel and the compliance of panel banks with their obligations under the Code of Conduct.

Amongst these items the Euribor Steering Committee members discuss whether the index definition and features are in line with the market, whether the panel is large and representative enough, and review the individual submissions of panel banks (top/bottom 15% contributions; any missing contribution). In case of a panel bank’s failure to fulfill its obligations under the Code of Conduct, warnings, suspension and/or exclusion sanctions may be applied by the Steering Committee.

The frequency of Steering Committee meetings has been increased to bi-monthly meetings in order to reinforce the monitoring of contributions and of the level of the fixing. In addition, *ad hoc* conference calls are set up on a regular basis (i.e. seven conference calls have been held since February 2013). Similarly, with a view to further enhance transparency, minutes of the Steering Committee will be published promptly after the meetings, once approved by the Chair and Committee members.

While the Steering Committee is responsible for the benchmark’s governance and technical changes, market participants must be directly informed, in a reasonable timeframe, and, when possible, consulted about any change in the Code of Conduct and technical features of the benchmark. As an example, in the context of the Euribor reform Euribor-EBF has been consulting the panel and other stakeholders on their views on the clarifications of the Euribor definition, contributions process guidelines and reduced number of maturities.

Indeed, Euribor-EBF strongly believes that market participants’ expertise is crucial in order to ensure that the measures taken at Euribor-EBF and/or regulatory/supervisory fit the market’s needs. **Decisions or choices taken not considering market practitioners’ opinion may be disruptive for the community.**

Finally, in addition to the above-mentioned Steering Committee, Euribor-EBF is in favour of the creation of an **independent body responsible for identifying and managing potential conflicts of interests**. While the composition of such committee is still to be determined, Euribor-EBF believes that it should be independent from the banking sector and include

audit, compliance and/or legal experts. This Committee should have regular meetings and transparent procedures regarding its membership, processes and decisions.

- **Principle 10: Content Of The Methodology**

Euribor-EBF agrees that the benchmark criteria, processes and governance must be clearly defined and transparent to market participants, regulatory authorities and others on a fair and non-discriminatory basis.

Euribor-EBF publishes, on a free basis, delayed daily rates (90mn after the fixing time) and individual submissions. All the criteria and procedures for determining the benchmark, including fallback provisions in case of insufficient submissions, are published in the Euribor Code of Conduct and in the Euribor Technical Features available on www.euribor-ebf.eu.

In this context, as previously mentioned, Euribor-EBF is currently developing written guidelines on the contribution process and general responsibilities, including *ex-ante* and *ex-post* controls and organizational and administrative arrangements, as further detailed on principle 13. These contribution guidelines will be included in the Euribor Code of Conduct.

The Euribor Code of Conduct also defines clear criteria to apply for and stay on the panel, as well as the procedure followed by the Steering Committee to review new applications. The Steering Committee reviews the panel composition at each meeting (bi-monthly).

Any change in the panel composition is promptly notified to the Steering Committee, the respective panels of banks, and the calculation agent. The Euribor-EBF website is also updated accordingly.

Similarly, the benchmark's Code of Conduct or the technical features of the benchmarks must define clear **re-fix rules, contribution window and fallback provisions** contemplating the minimum data needed to determine a Benchmark.

- **Principle 13: Submitter Code Of Conduct**

Euribor-EBF agrees that the Administrator must provide standards and procedures for Submitters in a Code of Conduct, including clear contribution guidelines and rules to address potential conflicts of interest.

In this context, Euribor-EBF believes that a **strong and harmonized contribution process with *pre* and *post* submission controls** must be established in order to ensure sufficient safeguards and integrity of the data. In this perspective, Euribor-EBF has been working on written guidelines on the contribution process and general responsibilities, including *ex-ante* and *ex-post* controls.

With a view to illustrate the recommended principles, the above-mentioned Euribor contribution process guidelines are detailed hereunder:

Determination of the Euribor contribution:

- There should be a clear **definition of roles** in the contribution process and segregation of duties of the contribution team in order to prevent conflicts of interests. This means that, in any case, conflicts of interests between the employees responsible for the quotes (e.g. Treasury or Money Market Desk) and the Derivatives Traders must be avoided.
- In addition, **contributing staff should receive appropriate training** and confirm understanding of rules and policies. **Panel banks should appoint at least two persons and two deputies responsible for the contribution.** Only the appointed persons will be allowed to input the bank's submissions into the calculation agent's system.
- **Four-eye principle and pre-submission control:** The **level of the contribution** should be subject to supervisory review by and responsibility of the senior management (e.g. Treasury senior management) taking into account evolution of interest rate level, market criteria, ECB rates with appropriate levels of alerts (thresholds).
- In case the senior management has any issues or concerns with the respective panel Bank's contributions, the panel bank should implement a well-documented escalation process within its organisation. The panel bank should implement an internal information and communication process. Any communication or exchange of views during the pre-submission control process should be well documented on a daily basis.
- The panel bank should ensure through specific and detailed guidelines and policies that the processes for the Euribor submission, in general, and for determining the Euribor contributions, in particular, are transparent and well documented, that is, information, comments, and data used for determining the contribution rates should be stored according to the respective archiving requirements.

Submission of the Euribor contribution:

- The contribution team, under the supervision of the senior management, should be responsible for inputting the rates into the calculator agent's system.
- A 'four-eye' principle, or automation of the submissions when possible, should also be applied when inputting the rates, in order to avoid any mistyping mistakes.
- Panel bank must also ensure the correct and timely submission of its contribution rates to the calculation agent by implementing processes and procedures. (An automatic reminder procedure is already in place on the calculator agent's side.)
- Panel banks must communicate the names of the contributing persons and senior management responsible to Euribor-EBF and the calculator agent. (Already in place though a contact form to be returned to Euribor-EBF on an annual basis). Any change in

the contact list must be communicated without delay to Euribor-EBF and the calculator agent.

- Recordkeeping of contributors' names, internal communications and data related to the process for a period of five years after the date of each submission, in particular when there are different opinions on the rate, must be ensured.
- The system(s) used for the submission process must meet minimum security standards in order to avoid unwanted, uncontrolled changes and amendments to the contribution rates (e.g. personal logins, passwords, etc.)

Post-submission controls

- A neutral group within the bank should review and analyze the bank's contributions over a wider time horizon (e.g. one calendar month) in close cooperation with other stakeholders within the bank on a regular basis (e.g. monthly review meeting).
- The **Compliance Department** or another independent department, depending on the banks' internal organisation, should actively review **the internal contribution processes and respect of the Code of Conduct** and escalate breaches to the senior management of the bank, supervisors and Euribor-EBF. This independent department should be able to review the process on real-time basis.

Internal audit

- Each panel bank should ensure that the internal audit department regularly reviews, checks, and validates all processes and procedures relating to the Euribor submission every 6 months.

External audit

- Each panel banks should request an independent, third-party auditor to conduct a yearly audit of the bank's processes and procedures relating to the Euribor submission as part of the annual review. Written reports should be transmitted promptly after the internal audits to the Administrator who will keep records of these reports.

These **contributions guidelines will be included in the Euribor Code of Conduct, to which panel banks must subject themselves unconditionally.** In addition, submitters should be required to detail their processes to the Administrator.

With regard to the above-mentioned common contributions guidelines, Euribor-EBF acknowledges that banks' internal structures may differ significantly from one to another and that some adjustments might be necessary.

In addition, as mentioned previously in principle 4, Euribor-EBF introduced a **Euribor Management Annual Certification Form** in July 2012, whereby panel banks must certify that (1) all internal procedures are set up to ensure a **robust process for the submission of contributions, excluding any internal and external influences**, (2) that all submitted contributions are the **bank's appreciation of the evolution of the interbank market in the Eurozone according to the Euribor definition** and (3) that the **Euribor Code of Conduct** is fully respected when contributing to the fixing.

Currently, Euribor panel banks are requested by the Secretariat to return a contact form with the contact details of 2 persons: one in the Executive Team and one as a contributor. The revised Code of Conduct should include a requirement to designate two persons responsible for the Euribor contribution and two back-up persons within each panel bank.

- **Principle 16: Audit Controls**

Euribor-EBF agrees that the Administrators' processes and governance structure should be subject to both internal and external audits, followed by public disclosure of the results. Internal and external audits should be performed once a year.

- **Principle 17: Audit Trail**

Euribor-EBF believes that written records of contributors' names, internal communications, and data related to the process, should be retained by the Administrator and the Submitters for five years as detailed in the Audit Trail principle. Such requirement will be included in the contribution guidelines for submitters.

Additionally, Euribor-EBF believes that the benchmark calculation agent should also have a responsibility in the record-keeping of submission data, daily rates, outliers, controls and communications with the benchmark administrator/submitters.

3. Notice Concerning Use of Expert Judgement: Should Administrators be required to briefly describe and publish with each benchmark assessment:

- a. a concise explanation, sufficient to facilitate a User's or Market Authority's ability to understand how the assessment was developed, terms referring to the pricing methodology should be included (e.g. *spread-based, interpolated/extrapolated or estimate-based*); and**
- b. a concise explanation of the extent to which and the basis upon which judgment (i.e. exclusions of data which otherwise conformed to the requirements of the relevant methodology for that assessment, basing assessment on spreads, interpolation/extrapolation or estimates, or weighting**

bids or offers higher than concluded transactions etc.) if any, was used in establishing an assessment.

Euribor-EBF agrees that the benchmark criteria, and methodologies must be clearly defined and transparent.

The Code of Conduct and the technical features of the benchmarks, setting out the governance, the collection and calculation methodology (*estimate-based* in the case of Euribor), including fallback provisions in case insufficient data is available are publicly available.

In addition, Euribor-EBF is currently working on clarifying the key terminology of the Euribor benchmark, by explaining the “**prime bank**” and “**interbank transactions**” wording in the definition in order to provide contributing firms with further guidance. Separately, with a view to clearly differentiate the “prime bank” and “panel bank” terminology it is also working on the **clarification of “panel bank” terminology**. The above-mentioned clarifications of the Euribor definition and the contributions guidelines detailed under principle 13 will be included in the Euribor Code of Conduct.

It is important to note that, with a view to preserve the continuity of the index, these clarifications are not aimed at changing the current Euribor definition.

Euribor-EBF believes that the Euribor, with its current definition, should remain an estimation of the market price levels by a panel bank, as it was originally conceived, while strengthening the contribution guidelines, controls and overall governance of the index. It relies on an expert judgment of the market, by the market, which also contributes to reduce market disruptions in periods of illiquidity and in a fragmented market environment.

Euribor-EBF would like to point out that, when a market becomes illiquid or with very few transactions for some maturities, it might be difficult to justify the experts’ estimations only on transactions based or verifiable data. Likewise, in an illiquid market, sparse transactions may produce extreme volatility of an index, thus mining its credibility and causing damages to the retail and corporate sector. A rate calculated in sparse markets may also be more subject to manipulation which could hardly be detected. In addition, for the specific case of Euribor, panel banks do not quote a price reflecting their own position in the market, but the rate that each panel bank believes one prime bank is quoting to another prime bank for interbank term deposits within the Euro zone. It relies on an expert judgment of the market, by the market. Consequently transaction-based verification is currently not feasible. A plausibility check, to the extent possible should be called for in this context.

4. Revisions to the principles: Please provide any suggested changes to specific principles or key definitions set out in Annex A, including drafting proposals and rationales.

Are there any other principles needed: Should principles to address any additional issues, risks or conflicts of interest be developed? Please provide a summary of the issue and drafting for the proposed principle.

Euribor-EBF generally agrees with the cited principles and with the terminology defined in Annex A of this consultation paper.

Against this background, **Euribor-EBF believes it is appropriate to have a common set of core principles for benchmarks governance but stresses the need to allow enough flexibility to adapt to each benchmark's features. An element of proportionality may help to bring the large variety of benchmarks and indices better into compliance with the principles. Euribor-EBF also supports the introduction of European public supervision on benchmarks.**

Finally, Euribor-EBF underlines the importance to coordinate benchmarks' reforms at European and global level to ensure consistency and a level-playing field. In this context, there is a need for a harmonized supervisory framework and improved coordination between supervisors at both national and European level.

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