

BME SPANISH EXCHANGES COMMENTS ON ESMA CONSULTATION PAPER ON PRINCIPLES FOR BENCHMARK-SETTING PROCESSES IN THE EU (ESMA 2013/12)

February 15th, 2013

Bolsas y Mercados Españoles (BME) integrates the companies that operate the securities markets and the financial market infrastructures in Spain. Amongst others, it brings together, under a single activity, decision-making and coordination unit, the Spanish equity, fixed income and derivative markets and their clearing and settlement systems.

We welcome the ESMA Consultation paper on Principles for benchmarks-setting processes in the EU (ESMA 2013/12). We would like to thank ESMA for the opportunity to participate in this public consultation process.

Q1: Definition of the activities of benchmark setting

Do you agree with the definitions provided in this section? Is this list of activities complete and accurate?

The wide description provided with in the definitions contained in the Consultation Paper defines benchmarks, entities and activities related is suitable to the purpose of the document.

Precisely because of such deliberated wideness, it could be appropriate considering if it is exact to refer to these principles as “Benchmarks-Setting Processes”, as long as the Principles are not only applied to the process of setting and definition of benchmarks but they also refer to many other activities such as benchmark dissemination and the use of the benchmarks to promoting and marketing financial instruments. For these reasons, it might be desirable to read “Principles for Benchmarks Processes” whether in the title or in several paragraphs of the Consultation Paper (e.g., the heading of paragraph 26 and the title in General Framework, in page 8.)

In a general view, the Principles should focus, on the one hand, on the substantial differences that exist between benchmarks based on real market transactions and those based on another type of data or contributions and, on the other, on the relevancy that volumes in transactions and contributions used for calculating benchmarks have.

Q2: Principles for benchmarks

Would you consider a set of principles a useful framework for guiding benchmark setting activities until a possible formal regulatory and supervisory framework has been established in the EU?

This question relates to the aim to introduce the, so-called, soft law, that is, recommendations, criteria or guidelines not legally binding.

In fact, it is frequent to wonder whether recommendations or principles are a good way to deal with the problems or questions detected or whether, on the contrary, it is desirable to set legal binding regulations.

This Consultation paper claims the usefulness of the Principles until the European Union sets a formal regulatory and supervisory framework.

Establishing criteria and draft principles and recommendations for all entities which carry out activities with benchmarks has been positively evaluated, as it is the way to reach a common framework for all of them.

On the other hand, it does not seem to be possible that those criteria and recommendations set down on the Consultation Paper can be used by national competent authorities as part of their market supervisory practices in financial markets (para. 9 of the Consultation Paper). In fact, the Consultation Paper reflects reservations about this possibility when exposing the question again, as it reads that the principles will be implemented in supervisory practices “where relevant and possible” (para. 26). It does not seem that the processes carried out by market participants in financial markets can involve undefined requests or uncertainties about the obligations and requirements demanded by the national competent authorities.

As a result, it is desirable that, with regard to those authorities, the proposed principles can be enounced as a first step and a common framework of understanding, necessary while preparing eventual necessary regulations.

Q3: General principles for benchmarks

Do you agree with the principles cited in this section? Would you add or change any of the principles?

This general principles - included in the title “General framework for Benchmarks setting” (Section A of the principles, page 8)- seem to be suitable for the purpose of the Consultation Paper and they match the suggestion made above about the use of the Principles by competent authorities.

Q4: Principles for firms involved in benchmark data submissions

Do you agree with the principles cited in this section? Would you add or change any of the principles?

Section B of the principles (page 9 and 10) is also suitable.

Paragraph B.10 declares zero tolerance policy for non-compliance with internal policies, including clear internal sanctions, and it seems to be justified. Nonetheless, it appears to be disproportionate that this zero tolerance policy requires a credible whistle-blowing policy. That is a specification that depends on the internal mechanisms of control implemented in each company and thus it is desirable that the Principles do not establish such a concrete measure.

Q5: Principles for benchmark administrators

Do you agree with the principles cited in this section? Would you add or change any of the principles?

Section C of the Principles (pages 10, 11 and 12) is properly formulated.

Paragraph C.2 deals with the responsibility in determining the methodologies for the calculation of the benchmark and provides that the compliance and governance functions should count on independent members - being ‘independent’ those that do not contribute with data for the calculation of the benchmark. It would be preferable the Principles to set a clear separation of

functions between data submitters and those responsible for the methodologies for the calculation of the benchmarks.

Paragraph C.6 sets the general rule for the full disclosure of the methodology for the calculation of the benchmarks and it adds that, where this is not possible, the relevant information such as weightings and prices of the components of the benchmark should be disclosed prior to any rebalancing of the benchmark. The Consultation Paper is not very precise with regard to when it will not be possible to fully disclose, and therefore a general obligation results in a vague situation. Furthermore, the wide range of benchmarks requires the paragraph C.6 to be modified in order to have a fully disclosed methodology, properly registered and available for the legally involved parts.

In relation with internal control policies (paragraph C.13), please see the observation made above in question B.10, when connected with a whistleblowing mechanism.

Q6: Principles for benchmark calculation agents

Do you agree with the principles cited in this section? Would you add or change any of the principles?

Principles for benchmark calculations are set in Section D (page 12) with no comments except those already made for internal policies with a whistleblowing mechanism.

Q7: Principles for benchmark publishers

Do you agree with the principles cited in this section? Would you add or change any of the principles?

With regards to the Section E, the wording in paragraph E.3 should be revised to make clear that the obligation for the benchmark publishers to obtain a confirmation from the benchmark administrators that the procedures for the validation of the submissions and calculations can be made under a publication agreement between the parties (periodically reviewed) and that this rule is not referring to each data, element or specific point in time.

Q8: Principles for users of benchmarks

Do you agree with the principles cited in this section? Would you add or change any of the principles?

Section F (pages 13 and 14) describes Principles for users of benchmarks, being affordable the obligation of the users of verifying that the benchmark used is appropriate, suitable and relevant (paragraph F.4). Once this Principle is clear, it seems exaggerated paragraph F.2 setting that the users must assure that benchmark administrators and benchmark calculation agents comply with the Principles by checking the user their confirmations of compliance publicly disclosed by administrators and calculation agents. It is a wide and imprecise principle, close to impossible to verify.

In a similar line, it seems reasonable that paragraph F.3 asks users to develop robust contingencies for the unavailability of a benchmark or any disruptive events leading to the benchmark not being calculated or published. However, it is not reasonable that these provisions also have to apply to those cases where the benchmarks are not being reliable as this word contains a subjective judgment, with the subsequent imprecisely and vagueness.

Question 9: Practical application of the principles

Are there any areas of benchmarks for which the above principles would be inadequate? If so, please provide details on the relevant benchmarks and the reasons of inadequacy.

The most important aspects related to this question have been already answered in the previous questions.

Question 10: Continuity of benchmarks

Which principles/criteria would you consider necessary to be established for the continuity of benchmarks in case of a change to the framework?

The problems derived from changes in benchmarks (methodologies of calculation and procedures) are already mentioned in the Principles (it is the case in paragraph F.3 for benchmark users) and, where it is not the case, they should be included in the rest of Sections, including the need of a suitable time in advance for the disclosure of the changes and offering a reasonable deadline for all stakeholders, allowing them a response to the modifications (rights exercise, switching the contract to another benchmark, finishing the contract, etc.).