

24 January 2014

Response to IOSCO's request for public comment on implementation of PRA principles

ISDA supports the increased attention on the functioning and oversight of oil Price reporting Agencies (PRAs) and the IOSCO principles for oil PRAs that aim to enhance the reliability of oil price assessments that are referenced in derivatives contracts.

ISDA members welcome the opportunity to give their views on the implementation of these principles.

Questions

1. What changes have interested parties seen from the PRAs as they have implemented the Principles in the oil markets? Is there sufficient transparency regarding the changes made?

ISDA members have seen limited changes in relation to certain benchmarks in certain regions. We cannot though directly attribute these changes to the Principles.

We however note that the PRAs have made a significant effort to increase the transparency of the price determination process. Looking back at reports published in early 2012 and comparing them against reports in mid-May 2013 and on-going, one of the leading oil PRAs has significantly increased the commentary/ detail around its assessment mechanisms. Previously, commentary had been very limited accompanied by a simple summary of trades taken in to account.

One PRA ISDA members had significant engagement with in 2013 emphasised a recent increase in rigour around its assessment process. As well, the discussion of disagreements over derived prices or data used to derive prices has become more open. The PRAs all now appear to have a clear step-by-step complaints procedure that is documented on their websites. A greater effort is also being made to dialogue with market actors regarding modifications to the price determination methodologies.

The recent publication of external audits suggests that PRAs are making internal changes to ensure avoidance of conflicts of interest and compliance with training, methods and procedures.

Otherwise, no significant changes in the behaviour of PRAs towards market participants have been noticed.

Overall, ISDA members believe the PRA principles have been favourable for the functioning of oil markets.

2. How has behaviour by participants in the oil market changed over the last year, if at all, in the context of the greater focus on benchmarks and the perceived associated risks?

ISDA members have not observed material changes in behaviour or traded volumes by market participants in this period.

3. What further enhancements, if any, should be made to the PRA Principles to improve the reliability of price assessments in the oil market? If they were to be made applicable to other commodity markets what other changes should be made?

The PRA Principles have reinforced price assessment reliability while ensuring the continuing functioning of oil markets, notably by reinforcing the dialogue surrounding the changes in methodology which ensures that continuing improvements will occur in the price reporting process. It is important that the former was not attained at the cost of the latter. Consultation by PRAs with market participants and other stakeholders is key to ensuring the best methodologies and application of them. As such, ISDA members would like to see further efforts from the PRAs in this regard. Accordingly, the PRA Principles could be enhanced by giving further consideration to this matter and potentially providing for formalisation of arrangements.

Quality of price assessment and editorial staff is of the highest importance. Accordingly the PRA Principles could give this matter further consideration towards ensuring consistently high quality of these staff in the PRAs, including formalised training.

Another aspect that could augment the PRA principles relates to access of information. It is critical that market relevant information (including historical data) is made available by PRAs to market participants, at a reasonable cost.

Given the international nature of oil markets, ISDA encourages consistency of application of the PRA Principles by all IOSCO members so that any potential for regulatory arbitrage is minimised. In certain jurisdictions such as the EU, considerations are under discussion which may require equivalence to be based on adherence to IOSCO principles. Therefore, measures to consistently apply the principles would be extremely valuable.

Any changes to the price reporting process or to the relationship between the price reporting agency and the submitters of market data must not hinder the on-going voluntary reporting of information by market participants worldwide. In particular, it must avoid putting constraints or obligations on reporting entities that are so significant that they discourage participation. The PRA principles appear, so far, to have struck the right balance here.

Application of the Principles to other commodity markets should be carefully considered on a case by case basis and we would encourage thorough consultation with the users of those particular markets, as has been done for oil. Commodity markets also vary widely in terms of associated infrastructure, delivery points and as to whether they are traded regionally, nationally or internationally so bespoke of each consideration is essential.

In addition to these comments, ISDA notes that IOSCO will consider whether there is scope for closer alignment of PRA Principles with the IOSCO Principles for Financial Benchmarks and would like to express the following views:

As indicated in the “Summary of the Principles” to the IOSCO Principles for Financial Benchmarks, “The Principles provide a framework of standards that Administrators should implement according to the specificities of each Benchmark.” IOSCO has recognized the specificities of oil markets and adapted an approach to them under the PRA Principles. As indicated in Chapter 1 of the IOSCO Principles for Financial Benchmarks, “the PRA Principles were developed with due regard to the specifics of the oil markets, while these Principles for Financial Benchmarks focus on Benchmarks generally. As a result, while both sets of principles reflect similar high-level concerns, they differ in some specifics.” The PRA Principles expressed these specifics for the oil industry and must be preserved intact. Accordingly, ISDA members do not support the alignment of these principles with IOSCO Principles for Financial Benchmarks.

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About ISDA

Since 1985, ISDA has worked to make the global over-the-counter (OTC) derivatives markets safer and more efficient. Today, ISDA has over 800 member institutions from 62 countries. These members include a broad range of OTC derivatives market participants including corporations, investment managers, government and supranational entities, insurance companies, energy and commodities firms, and international and regional banks. In addition to market participants, members also include key components of the derivatives market infrastructure including exchanges, clearinghouses and repositories, as well as law firms, accounting firms and other service providers. Information about ISDA and its activities is available on the Association's web site: www.isda.org.