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Feedback Statement

Q1 Are you or your company currently subscribers to the services of PRA(s)? If so, how would you rate the overall quality of the work being carried out by the PRA(s)?

A significant number of commenters subscribed to numerous PRAs or were otherwise familiar with the PRAs' publications. Many of these commenters described the work of the PRAs in positive terms, using language such as "the highest quality", "sound and ethical", and "commitment to integrity". One exchange noted that "the use of PRAs as transaction price determinants is voluntary and presumptively because market participants perceive the quality of the PRAs and their output to be of sufficiently high quality to satisfy that purpose". It found that "PRAs have a commitment to integrity in all aspects of price discovery and the related processes are strong and sound". Another exchange thought the overall quality of their work is good and one consultant responded that "over the last 39 years, the quality of reporting has increased...[and] PRAs publish price assessments of the highest quality". A trade association, whose members subscribe to PRA assessment services, understood the quality of work carried out by PRAs to be "sound and ethical" and an oil producer that subscribes to multiple PRAs felt that "the overall quality of the work performed is acceptable."

Several commenters commented positively on the quality and standards of the PRAs, but did so with reservations about certain aspects of the methodologies (such as in relation to judgment and the exclusion of trades) that could result in an inaccurate assessment or one that is susceptible to manipulation. For example, a trade association that subscribes to PRAs' assessment services believed that "PRAs have consistently applied their own devised methodologies, but these sometimes involve subjective judgment and exclusions of certain trade activities that could result in an assessment that does not necessarily reflect the true market. Illiquidity of many of the markets that the PRAs assess subjects these methodologies to a significant risk of manipulation." One consultant that does not subscribe to PRA services, but works for clients who are PRA subscribers, said that all three of the main publications (Platts, Argus and ICIS), "set high standards for themselves and by and large appear to uphold those standards." They identified problems with the scope of the assessments, such as the limited inclusion of deals, impact and power over contracting framework. One oil company that is a subscriber to the major PRAs' energy services said that the work they do can generally be considered to be "conscientious and professional" but that "the published prices do not always represent those of the market with the same degree of accuracy" and "the quality of reporting is not always consistent over time".

A minority of commenters expressed problems with quality, believing that the quality and accuracy of PRAs' models is impaired by a lack of effective external checks and the relatively limited scope of prices that are used in an assessment. A group of academics, some of whose participants are subscribers to PRAs, did not regard PRA assessments to be "absolutely reliable" and noted that Russian practice witnesses a small number of contracts. One individual, who was previously a subscriber, said that "the fixed price spot market is now almost completely notional and can no longer be 'reported'...It is now 'assessed' and that is not journalism." They contended that "the oil journals often turn over the responsibility of settling industry prices to inexperience[d] journalists with only a few weeks of training."

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Q2 *Please provide information on the impact of PRAs on physical oil and oil derivatives markets. Please support your comments with data on the volume and value of the related physical oil and oil derivatives business you are aware of, which is dependent on PRA benchmark prices (where possible broken down into the following categories: OTC; OTC cleared; or exchange-traded).*

A large number of commenters said that PRAs have a significant impact on physical oil and derivatives markets. They made comments that their influence in Asia is “pervasive”, they are “integrally involved” and “perform a critical function” in the market. However, only a few were able to provide data to support their comments and some acknowledged that these were only estimates. To demonstrate the widespread use of PRAs, one exchange highlighted that it has over “300 products based on price assessments provided by the most significant PRAs in that industry, including Platts, Argus, ICIS-LOR and PetroChemWire”. It further noted that PRAs “have assisted in providing structure to the underlying oil markets” and enable “market users to have sufficient information to adequately manage market risk”. One trade association commented that their OTC oil derivatives business which is dependent on PRA benchmark prices represents about 20% of global jet fuel consumption (40million tonnes) and noted that exchange trades are very limited (Dubai and CME) but “total traded volumes are estimated at 10 times consumption”. One individual commented that, in Asia, “almost everything is tied primarily to Platts and to a lesser extent to Argus, RIM and a few other oil journals. This is true of physical spot and term deals, OTC swaps and most exchange traded swaps”. One oil company said that 75%-80% of “oil market pricing links sales to representative price references”, whilst one trade association said that PRAs are “integrally involved in the physical and derivatives oil markets”. Another oil company felt that PRAs “perform a critical function in the price discovery process in physical oil markets”.

A few commenters said that their understanding of the impact was only based on estimates.

A group of academics said that Russian authorities closely examine PRA price estimates but that although “PRAs data is rather widely spread...its magnitude has not been properly estimated”. One consultant believed that “the vast majority of physical oil products moves under contracts that use PRA benchmarks as a reference point” and estimates that “perhaps ~60-70% of OTC swaps and options are priced or cash-settled by reference to PRA quotes.” They also said that “a significant proportion of exchange traded contracts use PRA prices for cash settlement at expiry.”

Only one commenter felt that PRAs do not have an impact on oil markets. The oil producer said that “PRAs should not have any impact on the physical oil market as PRAs do not play the role of trading houses.”

One PRA said it “understands that its price assessments are used by a wide range of market participants for a number of different purposes in the trading process, including to set bilateral contracts...as well as by downstream customers, governments, regulators and analysts.” It estimated that “90-95% of crude oil is sold through term contracts, with the balance sold on the spot market” and its price information is licensed to several derivatives exchanges for use as the basis for derivative contracts that are traded and/or cleared by the licensee. Another PRA said that PRAs “provide important transparency to oil markets that would otherwise remain opaque,”

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yet did acknowledge that “data on volume and value of related OTC, OTC cleared and exchange-traded contracts need to be provided” although suggested this should be provided by market participants, brokers, clearing houses and exchanges, rather than by a PRA.”

Q3 *What are the impacts of PRA processes on oil trading markets, physical and/or derivatives? In your answer please comment on the quality of PRA processes, their strengths, as well as the potential impacts of any perceived weaknesses.*

Nearly all commenters said that PRA processes have an impact on oil trading markets. A number of commenters felt that PRA processes are strong. One exchange said that PRAs “have brought a significant amount of transparency to the oil markets”, noting that they have “over 300 contracts” that reference PRA prices. A group of academics wrote, “[a]part from stating that this impact is substantial, it is not yet possible for our group to give its quantitative measurement”. One consultant reiterated that “PRAs publish price assessments of the highest quality”. A trade association said that there is “widespread reliance” on PRA reporting and “nearly all OTC forward and derivative deals are quoted as spreads from a PRA benchmark or a CME-NYMEX or ICE oil settlement”.

One oil producer commenter disagreed, responding that “PRAs should not have any ‘impact’ on markets other than to provide the transparency needed to allow companies to deal with the markets in an orderly fashion”.

Other commenters said that, while a number of processes are strong, there are areas of potential weakness that could be addressed. One trade association said that using a “Market on Close” methodology considers transactions within a “small trading window” which omits a number of trades which “can have an impact in some illiquid markets”. Although, conversely, one consultant said that one of the PRAs’ trading windows is strength because it results in “further standardization”. They also believed that one of the PRAs is “sincere in its objective of introducing changes to improve the market, but [suggested that] IOSCO and the industry may wish to...[see] whether a forum for other voices would be valuable”. One exchange noted that “the impact of PRA processes on oil trading markets is significant and broad-ranging”. It raised concern that “there are certain widely referenced PRA processes (e.g. the Dubai partials market), where limited volume and a narrow range of market participants means that the pricing process is highly susceptible to manipulation. In other cases, a complete absence of liquidity within such markets means that price reporting is based upon journalistic assessments rather than market driven price discovery”. One oil company said that market participants depend on PRAs, but “sometimes the criteria imposed by PRAs does [*sic*] not assure an accurate representation of the market”. Two trade associations said that methodologies used by PRAs “have an impact on the physical oil and oil derivative markets” and they worry that PRAs can “exclude trades from their price assessments” and “do not have to account for the basis on which they exercised their discretion”.

One individual commenter found the PRA processes to be significantly flawed, saying that “the overriding fundamental flaw that they all share is that the final price assessments they each make each day are heavily subjective, with lots of room for journalistic license”.

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One PRA recognized that “a publisher’s price discovery process - if well accepted by the marketplace - will result in its assessment being adopted as a reference price in the physical or the derivative market”, whilst another PRA also pointed out the PRAs’ role in standardization saying that “wide acceptance by the industry of the price assessment in physical contracts may lead to a requirement for hedging”.

Q4 Do you consider PRAs to have potential systemic impact on the financial system? Please give reasons for your answers.

While many commenters believed that PRAs are important to the oil markets, only a few said PRAs have potential systemic impact on the financial system. One individual said that PRAs “decide the market price each day for a very large percentage of the world’s crude oil and refined product sales”. One exchange responded that “participants have a large incentive to ‘influence’ the assessment made by Platts” in order to impact the physical oil and large swaps markets whose prices are relative to the assessment. They said that 14million barrels of physical crude, 10million barrels of Dubai swaps and the majority of the East of Suez refining margin are based on these prices. Two trade associations believed the fact that PRA prices “are used for physical, cash and derivatives contracts in financial and physical markets...across global markets all point to systemic impact”.

Many commenters believed that commodity markets that reference PRAs, while large, do not rise to the level of systemic impact on the financial system. One exchange and one consultant noted that most physical and derivative oil contracts have fallback clauses providing for another PRA’s assessment in the event that a PRA were to fail. One trade association and an oil company both used data to support their belief that the PRA-referenced OTC derivatives market could not have a systemic impact on the financial system. The trade association stated that all OTC “commodity derivatives account for less than 0.5% of...all outstanding OTC derivatives” and the oil company said that oil markets, at \$250billion in volume, are “considerably smaller than all other financial markets combined.” One consultant, an oil producer and another PRA said that it is market participants, not PRAs, which could potentially have a systemic impact.

One PRA distinguished their impact from credit rating agencies (“CRAs”), noting that whilst CRAs “make forecasts, Argus’ primary activity is reporting today’s prices”. Another PRA reiterate that there are fallback clauses in the event of one PRA’s failure.

Q5 What are your views regarding PRA price methodologies, including your ability to identify methodological errors? Do you consider that mechanisms or procedures exist to address any such concerns and are they adequate? Have PRAs demonstrated responsiveness in updating their methodologies to reflect market development?

Commenters appreciate that PRAs publish their methodologies. However, many felt that market participant complaints regarding PRA methodologies and comments to methodological amendments are not taken into account. One trade association said that “users have reported potential assessment errors to PRAs” but felt that PRAs have been “hermetic” to these concerns and “are not inclined to improve their assessment methodology”. They want the “mechanisms to address

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complaints...[to] be established/improved and an independent complaint committee...[to] be established”. One consultant commented that methodologies “should be auditable for methodological errors. However, in reality the amount of data produced on a daily basis and the exercise of subjective judgment by the PRAs when there is insufficient data makes this impractical”.

One individual commenter said that while PRAs are “somewhat responsive to suggestions in methodology improvements, overall they are more intent on defending their methodologies than improving them”. One exchange commented that for products in their market, the “methodology used promotes the trading of relatively small volumes of oil with the sole purpose of influencing pricing”. One oil company responded that where PRA methodologies are followed, the results are generally close to the market, but when PRA methodologies incorporate “judgment” inconsistencies can result. They also said that “generally, PRAs are not responsive to proposed changes to their methodologies from market players” and, whilst they seek input, “this input may not always be taken fully into consideration”. Two trade associations “see the need for a more objective and transparent forum than exists today for consultation on methodologies”. They commented that “there is not a formal complaints process, nor an adequate compliance function”. This seems particularly important given the complaint that “there have been instances where mathematical errors in the published prices were clearly evident to subscribers who can see the trades on the screen and calculate that the prices published are outside the range”. With regard to amendments to methodologies, “the PRAs may listen to subscribers’ proposals for amendments...however the evaluation of any proposed amendments is not always clear and transparent”.

A minority of other commenters stand by the PRAs’ methodologies and believed their efforts to amend methodologies and listen to complaints is appropriate. One consultant said that “all PRAs publish data on their crude value estimates...[T]he valuations provide clear obvious tests of the quality of the PRA estimates”. One oil producer said that methodologies used by PRAs to assess the physical markets reflect each PRAs’ “best efforts at capturing the market’s prices”.

One PRA said they maintain “constant alertness to both overall suitability of a methodology...as well as the day-to-day application of [a] methodology.” It said that it “actively consults the market whenever it is considering a material change to its methodology” but “acts with total editorial independence in respect of changes to its methodologies” and “does not change them to satisfy any particular constituency in the market, nor does it act on the basis of consensus among industry participants.” Another PRA said that it establishes “methodologies in consultation with market participants”, its “methodologies are transparent” and it has “clear complaints and compliance policies.”

Q6 *Does the voluntary reporting of transactions used in certain PRA assessments pose risks to the price assessment process? If so, how should these risks be mitigated? Would it be beneficial if reporting of transactions to PRAs were mandated (contractually or by legislation)?*

Nearly all commenters believed that it would be beneficial if more market transactions were submitted to be included in the PRA assessment. A majority of commenters

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acknowledged that there are risks to the voluntary reporting of transactions used in certain PRA assessments, but commenters were divided on whether some sort of mandate for reporting would be beneficial or detrimental. Those that supported a mandate felt that it would increase the number of transactions on which to base assessments and eliminate selective reporting by market participants. One trade association said that voluntary reporting allows market participants “to include or exclude trades according to what would work to their favor. It can cause a distortion of market prices”. They commented that mandating reporting is “desirable” because it would reduce the risk of “no-trade days” that leave price setting “at the PRAs['] editor’s discretion”. A group of academics commented that voluntary reporting “tends to be fraught with risks for the users” and that “regulation of this domain would be beneficial”. Two trade associations responded that “where a PRA is providing significant price reporting in a market, market participants should be required to report all concluded transactions to PRAs”. They said that “mandating reporting...would aid consistency and robustness in the price formation process” but “recognize that there may need to be a mechanism to protect confidentiality, price stability and liquidity for commercially large transactions”.

Other commenters worried that a mandate would be cumbersome and reduce the quality of the data reported. One consultant said that “selective reporting of deals leaves the price reporting system wide open to abuse” but was nevertheless worried that “a contractual or legal obligation to report all deals to PRAs would add more problems than it would solve”. One individual said that even if the PRAs had information on all deals done, “they would still have to subjectively assess the information to come up with numbers to publish as representing the market”. One exchange felt that voluntary reporting poses risks because market participants only report trades if they believe it is in their best interests, but, again, felt that the “mandatory reporting of transactions either contractually or by legislation would be arduous and cumbersome to control”. One oil company said that selective reporting could have an impact on prices published by PRAs, but was not concerned that “selective reporting by market participants is a serious risk to the integrity of these prices”. One oil producer commented that voluntary reporting always runs the risk of missing some transactions, but that regulating PRAs would amount to “regulating the wrong entities”.

One consultant commenter believed that “voluntary reporting does not pose a risk because PRAs have a strong incentive to provide accurate crude price estimates”.

One PRA commented that “more data is better than less data” but “the quality and transparency of the data...factored into its price assessments are of paramount importance”. They were concerned that “having a multitude of potentially irrelevant mandated disclosures could confuse and/or conceal price formation rather than improve transparency”. They currently attempt to mitigate the risks of using voluntarily reported transactions by “monitoring and assessing both the validity and integrity of the information provided”. Another PRA noted that “transparency rather than universality” is required for reliable prices and expressed its support for “any initiative by the authorities to encourage market participants to report more widely to PRAs on pre-trade and post-trade information in the interests of transparency”.

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Q7 *Do low numbers of transactions used in certain PRA assessments pose risks to the price assessment process? If so, what crude grades and markets do you see affected by this? What is considered to be a 'low' number? How should such risks be mitigated?*

A number of commenters said that low numbers of transactions could pose risks to the price assessment process. This is more likely to occur in certain, low volume products which reflect the heterogeneous nature of the oil market. One trade association commented that “jet fuel markets are significantly impacted” and suggested that transactions should be eligible for submission to PRAs to be used in their assessments at any point during the entire day, rather than during only a 30 minute window. One consultant said that “even if this situation is not currently being abused, the potential for abuse is obvious”. One individual said that although this risk exists, it is minor compared to the “fundamental subjectivity flaw” and that “the only way you can get fairly accurate and consistent results out of oil journal price assessments is by averaging several of them”. One exchange believed that “low transaction levels in the Dubai pricing assessment undermine the integrity of the price discovery process”. Two trade associations responded that “where there is limited liquidity in the underlying physical markets to form assessments, e.g. (Liquid Petroleum Gas) LPGs such as Butane and Propane, there is the possibility that the assessment process can lead to unrepresentative price formation”. They “are supportive of the differential method used, providing the methodology is subject to the balance and checks noted above but...not supportive of the ‘survey the market’ approach which lacks transparency and is subjective”.

Other market participants felt that the current PRA methodologies were designed to deal with the constraint and are the best way to deal with illiquid markets. One consultant said that refiners have used product markets for decades to determine the relative value of different crudes and that “PRAs replicate this process and thus can make sure the published relative values are correct”. One trade association thought PRAs ensure “the best outcomes” and found “it difficult to suggest a better methodology [than theirs]”.

One PRA respondent highlighted that it “has editorial protocols that filter out bids or offers that could result in price obscurity or illogical market behaviour. The rules on how and when bids and offers can be incrementally changed and allow evaluation of whether bids/offers are typical and repeatable market values, or outliers designed to mask or obfuscate the market level”. It looks at data in a specific market “while also evaluating the conditions in the overall market”, noting that “many markets may not have daily liquidity but, nevertheless, that commodities have an inherent value”. In this respect, it compares the valuation of illiquid markets to a valuer estimating the value of a house despite even if no transaction having occurred in the neighbourhood for weeks or even months. Another PRA questioned the premise that the price assessment process “should be based purely on transactional data as a matter of preference”. It noted that “price discovery in physical oil markets is the balance between tightly defining the assessment and increasing the number of pricing inputs. The precision of a benchmark must always be weighed against the volumetric liquidity behind it”.

Q8 *Taking account of existing PRA procedures to obtain information on which to base their assessment when no transactions have been submitted, are there any other approaches that may produce their benchmark prices in the absence of liquidity?*

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Most commenters felt that the current PRA procedures to obtain information on which to base their assessments in the absence of submitted transactions are adequate. However, a couple of commenters believe that other methodologies, such as keeping reported prices flat or looking to exchange-traded products, should be used. Among those commenters that felt another approach could be used, one trade association said that “if there are no trades reported within a window period then more precedence should be given to the possibility that the market actually remained “flat” rather than moved in sequence with a wide range of bid/offer spreads that were never filled”. One consultant said that “the use of regulated exchange prices to set the flat price benchmark at a series of given points in the day would do much to solve this problem...“rather than using devices, such as the Platts window, to recreate a questionable substitute for what already exists”. .

The other commenters who responded to this question said either that existing PRA procedures are the best approach or described a methodology that was similar to what is used by a number of PRAs. One individual said that “there are no accurate alternatives” and one exchange echoed this by saying that the Arabian Gulf has no alternatives. Three trade associations all felt that where no transactions have been submitted, the PRAs work to ensure the best outcome.

In terms of methodology, one PRA highlighted that their editors’ “experience and comprehensive market knowledge” are used on days where there are fewer trades or wider spreads. Another PRA noted that “the precision of a benchmark must always be weighed against the volumetric liquidity behind it. A benchmark may be so narrowly defined that it represents insufficient volume, whereas a high-volume index may be so vague that it is of little value to the market”.

Q9 *Are there any issues regarding PRAs that concern you from a public accountability perspective?*

A narrow majority of a broad range of commenters had issues relating to public accountability of PRAs. An issue, cited by one trade association and one consultant was the perceived forced use of restricted trading windows and trading platforms, particularly, as noted by the trade association, because they are unregulated. Two oil companies, one exchange, a group of academics and an investment bank all highlighted the lack of transparency in price assessments, whilst another trade association pointed out the confusion of business with editorial objectivity in either smaller scale PRAs or in PRAs in general. One exchange, one trade association, an investment bank and one oil company referred to a lack of independent price assessment dispute procedures, whilst another oil company and two other trade associations mentioned the lack of supervisory or regulatory oversight. One of those trade associations noted that PRAs “have no independent governance standards or oversight in respect of that function. Further, in so far as a PRA may also provide material trade execution services, to the extent that these are analogous to activities which in other markets attract regulation, they should be subject to equivalent regimes”.

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One neutral commenter, an oil producer, argued that if PRAs were regulated “this should ensure that price assessors are experienced.”

A minority of commenters had positive views. One exchange argued that if any correction were necessary, it should be proportionate, whilst one trade association commented that the relationship between a user and a PRA is that of a customer to a vendor which does not require wider and more public accountability. Another exchange commented that PRAs have a strong incentive to act properly, but sometimes have to make unpopular decisions to “ensure the ongoing integrity of the markets”.

The PRAs themselves either submitted extremely positive arguments for their current business profile, or declined to comment, but declared a general concern for good governance.

Q10 Do you consider the function performed by PRAs to require a form of public oversight of PRAs? If so, which PRA activities should be subject to a form of public oversight and why?

A large minority of respondents expressed concerns about the current lack of public oversight of PRAs. One trade association argued that PRAs should be subject to public oversight in relation to their “structure, governance, assessment methodology and complaint procedures” so that overall it “safeguard[s] all stakeholders from unilateral PRAs decision[s] that may compromise a fair price assessment”. Similar arguments were repeated, to a greater or lesser degree, by other respondents including a group of academics, three trade associations and an investment bank. The investment bank argued for some form of public oversight in relation to price methodology, dispute resolution and participation in PRA trading forums such as the Platts e-Window. One oil company shared concerns about the need for oversight of “pricing methodologies and dispute resolution” and thought that PRAs should be subject to “some degree of reasonable constraint to their ability to overcharge/terminate their services in a way that may be detrimental to the market”. A number of other respondents, including another trade association and a consultant, specifically reiterated the argument for regulatory oversight of the Platts e-Window as a trading system.

Neutral commenters, who were in small minority (the responses to this question were polarised), argued for proportionality in oversight following a cost/benefit analysis, particularly one exchange, whilst one consultant recommended that oversight be focused only on specific attributes of the system, such as the Platts e-Window.

A sizable minority of commenters argued strongly against any form of public oversight, including one trade association, two oil companies, an individual and one exchange ,

The PRA respondents argued that they are publishers and should remain unfettered, are already accountable and have robust controls in place with transparent operations. One said it has “nothing to hide” but acknowledged that issues relating to accuracy and representativeness of data should be subject to public scrutiny.

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Q11 Please detail any concerns you may have about current ownership of PRAs in particular with regard to possible conflicts of interest.

There were only a small number of clearly critical responses to this question. One critical by a group of academics commented that “legal initiatives should minimize or in some instances eliminate the existing conflicts of interest”, although they did not specify any current problems. Whilst one individual mentioned that conflicts of interest exist, but said they are unrelated to the question of ownership.

A significant minority of commenters gave neutral replies. Although there were concerns about oil industry market participants owning the PRAs, these were clearly intended as prescriptions for future regulation, rather than an analysis of the current situation. One consultant said they would be “uneasy if any large entity of any kind whose fortunes vary with the oil price were to take a significant ownership stake in a PRA”, whilst one trade association said that “participants in the market particularly banks, oil companies and trading houses, should be strictly banned from owning PRAs.” One oil company said “conflict of interest in ownership could be a concern that would be worth regulating” and another consultant commented that “market participants should not influence the [PRA] firms”.

A number of commenters, many of whom had been critical in their responses to related questions, expressed little or no concern here and a significant minority of submissions (just under a third of respondents) did not address this question at all. One oil company considered this issue to be of “lesser significance”, whilst one trade association commented that “if PRAs were to be required to have appropriate controls over conflicts of interest, dispute resolution and the giving and receiving of benefits and inducements, the issue of their ownership would be of far less significance”. Another oil company said “indeed conflict of interest in ownership could be a concern that would be worth regulating”.

One of the PRA respondents expressed concern that “a number of price-reporting organizations exists [*sic*] in the space which are owned or operated by brokerage services...[which]...[d]espite claims of impartiality,...are not independent observers of commodities markets, since they are ultimately dependent for their revenues on serving the interests of their largest clients”. Two other PRAs endorsed the current situation on the basis that either their holding company imposes the strictest of standards in corporate behaviour or their articles of association prevented market participants from taking ownership of them.

Q12 Do you have any concerns regarding the current corporate governance standards of PRAs? If so, what are the improvements that you believe are needed?

A significant minority of commenters did not address this question at all.

A sizable group of the remaining commenters expressed critical views in varying degrees, in particular in relation to transparency and accountability. One trade association commented that the “player-referee relationship is currently not in place”, whilst another trade association said that the PRAs “need to develop transparent procedures around disputes and

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complaints...[which] should be part of a robust corporate governance regime and independently overseen by a regulatory body”. One investment bank commented that there need to be improvements in PRA corporate governance standards, “including the need to develop transparency and accountability...with a level of independent oversight [which] would enhance confidence around the price discovery processes”, as did a third trade association that also cited “lack of transparency and external accountability” as their main concerns in relation to corporate governance.” One oil company highlighted the absence of board-level management of price assessment integrity and an empowered complaints officer. A group of academics commented that one of its major concerns is the lack of clarity surrounding PRA ownership.

Another oil company responded more neutrally, expressing that it was less concerned with corporate governance issues as they “expect such issues to be managed in line with corporate governance best practice and...high level systems and controls requirements such as those applicable to financial institutions” and suggested that external oversight would not be necessary if a voluntary code of conduct and self-attestation were applied.

Only three commenters clearly expressed no concerns with the status quo. One exchange proposed no changes to PRA corporate governance standards and one consultant indicated it had no concerns in this regard at all.

Two PRA commenters wholeheartedly endorsed their current profile, having asserted that they conform to the highest corporate standards. A third PRA, however, argued for improvement in corporate governance in current standards of inter-PRA competition which impacted the accuracy of data and allegedly restricted the size of the data pool; nevertheless, the handling of the relationship between a PRA and its ‘marketplace’ was not of concern here.

Q13 Do PRAs need to be subject to standards of corporate governance that are equivalent to the standards to which regulated financial entities are subject? Please elaborate.

A sizable minority of commenters agreed that the corporate governance standards of the PRAs need to follow, at least to some extent, those of regulated financial entities. Three respondents, including an exchange, said they would like to see a strict application of equivalent standards. One was a trade association which linked its reasoning to the “widespread impact that the work of the PRAs has on global businesses and economies”, whilst one oil company referred to the “prominent role of PRAs in ensuring price availability to markets” as a supporting argument. Other commenters made recommendations for PRAs to be subjected to corporate governance standards that are more tailored to the corporate structure of the PRAs, including two trade associations that said corporate governance principles should be applied “in a way that takes into account the size, structure and requirements of individual entities” and an investment bank that does “not support an equivalent regime to financial institutions, as this may be disproportionate with unnecessary costs on the PRAs and industry” but did endorse “drawing from these rules in addressing the key elements of specific corporate governance issues”. A group of academics commented that equivalent standards should only be applied when the PRAs were owned by financial institutions (failing which, media and standard commercial corporate

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governance standards would apply) and one consultant believed they should only apply “if a PRA undertakes a different line of business”, i.e. that of a trading platform.

A small number of other commenters completely opposed, either directly or indirectly, any application of the corporate governance standards of financial institutions. One oil company argued that “the mere fact that PRA benchmarks are reflected in the design or pricing of a commodity derivative instrument does not give rise to the same type of risks as credit maturity transformation activities performed by banks”. One exchange proposed no changes and one oil producer responded, “Absolutely not. Regulated financial entities actually handle other people’s money and control profits and losses. The PRAs are reporting agencies that may be subject to a different type of oversight based on a full understanding of their current methodologies and how such methodologies are applied”.

The PRA respondents argued against being subjected to such standards on the basis that they are already subject to the “highest possible standards” and because they are “media organization[s]”.

Q14: Do you have any concerns as to the robustness of the systems and controls in place at PRAs as they relate to the integrity of the processes used to construct price series or indices? Please explain.

A majority of commenters expressed concerns as to the robustness of the systems and controls in place at PRAs. One trade association said that “controls are not sufficiently tight leading to a high risk of manipulation on the price assessment” and one individual was concerned that the process is subjective with “no checks or balances” which allows PRAs to act as a “law unto themselves” and the price assessment process to be subject to regular manipulation and “journalistic license”. Two trade associations expressed concern in relation to the substantial amount of discretion and judgment employed by PRAs when applying their methodologies to price assessments.

Some respondents highlighted specific concerns. One consultant highlighted a particular process whereby the reduction of “the market” to a half hour period in the day, when a limited volume is transacted, could lead to the exclusion of key companies from the price formation process. One trade association raised a similar concern regarding trade exclusion and one exchange stated that the lack of regulatory oversight renders a lack of transparency around trades. Another two trade associations highlighted a key man dependency on the editors who derive the prices.

A minority of commenters did not have any concerns, including one consultant and an exchange.

One commenter was very complimentary of the transparency and robustness of the systems and controls employed by the PRAs. That exchange described the price assessment process as “highly professional” and noted that the PRAs are “highly committed to integrity”.

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The PRAs themselves provided detailed responses explaining the controls and systems they have in place, and one PRA evidenced that no complaints had been received in relation to the robustness of its systems and controls. Two of the PRAs provided details on their draft internal code of conduct and cited this as a robust control mechanism for their price construction process.

The remaining respondents, were either not familiar with the issue of systems and controls or did not respond to this question.

Q15: Which authority, if any, should establish a set of principles for the appropriate level of systems and controls within a PRA and in particular as they relate to PRA benchmark methodologies? Would this sufficiently address any concerns you may have and, if so, how?

The responses to these questions were evenly split between those commenters who were in favour of an authority being in place to establish principles and those respondents who were against any external regulation.

Those commenters who thought that an external authority should be responsible for establishing the set of principles were of the general opinion that, due to the structural importance of PRAs, they should be subject to regulation. One trade association commented that, given the global nature of the market, “there is merit in setting the underlying principles on systems and controls for PRAs at global level e.g. through G20 and IOSCO, and that these [should] then [be] interpreted at a national level by the appropriate oversight (e.g. government department, energy regulatory) [authority]”. This suggestion that principles be set by a global authority such as IOSCO was also supported by two other trade associations. An alternative of having individual jurisdictional regulators involved in the coordination of such oversight was also mentioned. One exchange said that individual markets regulators in each jurisdiction “should be involved in coordination of any such oversight” and a group of academics suggested that such an authority could be one “selected by the corresponding government if...one has not been appointed [through legislation]...” One consultant suggested that an oversight panel (made up of regulators, traders or retired traders, representatives of major independent producer, refiner and trading companies, regulated exchanges, NOCs, OPEC, fiscal authorities and potential PRA representatives) could be involved in establishing standards in systems and controls at PRAs and, similarly, another trade association suggested a group consisting of experienced stakeholders should establish these principles.

However, even some of those commentators in favour of an external authority setting principles or criteria showed caution in their responses. One consultant stated that PRAs are commercial independent companies who have the right to use the methodologies they deem appropriate, as long as they remain transparent and adhered to by the PRAs, whilst one oil company warned that financial market regulators already have oversight of the oil derivatives market and both they and the market operators should satisfy themselves that the methodology used to obtain benchmarks is sufficiently robust. An investment bank supported leaving the development of benchmark methodologies to PRAs, suggesting instead that an authority, such as IOSCO, could develop a set of specific criteria against which the suitability of PRA benchmarks should be assessed.

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A minority of commenters felt strongly about imposing external regulation. One trade association clearly stated that, due to the fact they believe PRAs not to be systemically important, “regulation of them by IOSCO entities is neither necessary nor appropriate...[and that] there is therefore no mandate for intervention by IOSCO or any of its members with respect to the activity of reporting prices”. One oil producer felt that “in the absence of clear evidence by IOSCO or others on specific concerns, it is unreasonable to speculate...[as the] suggestion of oversight is conditioned on a detailed analysis of the current practices which IOSCO is yet to provide”. One exchange stated that “PRAs are not exchanges” and therefore should not be subject to exchange-like governance, however they could develop “best practice standards which leading PRAs could adopt”.

The PRAs themselves were of the clear position that regulation of them is unjustified and would risk eliminating healthy competition in the sector. One stated that external controls would be “an unacceptable intrusion on its rights as a publisher” which would “undermine...[its] independence”. However, that PRA did offer the compromise of submitting periodic reviews and another PRA further suggested a voluntary code of practice be put in place.

Q16: Should PRAs as a general matter be subject to a specified external audit of individual operations or processes, the results of which could be published demonstrating standards of compliance with relevant rules? Would PRAs need to be held to account for such an audit and, if so, which organisations would be best placed to carry out such an audit? What are the benefits and risks?

The majority of the commenters agreed that some form of external audit should be conducted on the PRAs. Whereas some respondents, including one trade association, a group of academics and one consultant, simply provided a response in agreement to both external audit and publication of the results, others offered various modes and method suggestions. Due to concerns surrounding the technical nature of the market and the fact that, as one PRA suggested, “virtually all the global expertise in developing market-reporting methodologies lies within the price-reporting services themselves”, one oil company suggested that audit firms should “hire the needed talent to perform such audits”, whilst one consultant suggested that these audits “might be carried out by trading specialists that might be accredited for the purpose by IOSCO”. Another trade association suggested some form of apportionment of such responsibilities between internal audits by the PRAs and external audits, and that “there should be scope for PRAs to be subject to direct regulatory scrutiny on an appropriate basis e.g. failure to comply with governance principles”. There was general agreement with the publication of the results of audits, with the same oil company responding that to do so would enable market participants to assess PRAs for themselves. One consultant suggested that, rather than full audit results being published, only the “failure to satisfy such a technical audit should be made public” but with consequences attached such as potential regulatory actions or fines levied on the PRAs for failure.

A minority of commenters did not see any additional benefit of an external audit. Instead, one exchange suggested “self-certification standards” would be appropriate, whilst one trade

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association rejected this on the basis that they would “prefer to see the activities of PRAs...brought under the scope of authorisation and supervision specific to a price reporting agency”. One oil producer felt there was not enough clear evidence to warrant the imposition of external audit, whilst an individual commented that to impose such a control would be “a waste of time” because they believe PRAs “can’t be fixed”.

Two PRA commenters reiterated that there are sufficient controls in place, including independent audit functions and codes of conducts, with one saying they would be open to providing a published report summarising details of an annual audit.

Q17: Should PRAs be required to incorporate into their rules, if absent, a formal complaints procedure. If so, please explain what would be your preference in terms of procedure or process?

The vast majority of respondents provided affirmative responses and support a formal complaints procedure being incorporated into PRA rules. The key preferences suggested were around the timely resolution of a complaint of critical importance and the economic consequence of ongoing dispute resolution. One trade association suggested that a PRA should “respond to a complaint within 48 hours...[and that] if the matter is not resolved within a reasonable time frame, it should be referred to an independent committee”. One oil company also emphasized that “dispute resolutions should be undertaken rapidly” particularly because of the PRA practice of “putting market participants ‘in the box’ (excluding them from the price assessment process) as punishment for not following [a] PRA’s guidelines”. They highlighted that “excluding a major market participant from the price formation process for one or more days can have significant economic consequences both on the prices assessed in the market and on the company concerned”. Several respondents also voiced a preference for a person or committee to deal with the complaint altogether. Two trade associations even cited the process currently in place at the London Metal Exchange as a good example and suggested best practice for a complaints procedure. One exchange highlighted the need for “PRAs’ complaint procedures...[to] be transparent to the market”. However, one oil producer and one consultant confirmed that most PRA’s already have a complaints handling procedure in place and that “a clear understanding of current practices are a prerequisite to judge whether additional clarifications or modifications are required”. Another consultant described the absence of a third party for a subscriber or stakeholder to complain to as being “particularly frustrating for companies whose deals are excluded from the price information database by Platts”.

Only a single commenter was against the implementation of a formal complaints procedure. That individual stated that “it would not make any difference”, but rather that to introduce such a process would, in turn, introduce delays and “lots of retroactive adjustments” of prices that would be unhelpful and instead cause a situation where “the cure would be worse than the disease”.

Exchange operators expressed either no view, had no comment, or considered that complaints procedures “should be a matter for PRAs”.

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All the PRA commenters stated that complaints handling procedures are either already in place or desirable. One said that, at a minimum, such a process should include a log and document the handling of complaints. It also concluded that the open publication of a complaints log would not be useful because “many complaints against PRAs are motivated by commercial gain, or – in many cases – originate from traders who have lost money on a trading position”.

Q18: Should disputes be resolved by an appropriate third party as a matter of course? Please explain the benefits and risks.

The vast majority of commenters did not express the necessity for a third party to resolve disputes as a matter of course, rather some commenters saw the role of a third party to be that of oversight only. One reason provided both by a trade association and an investment bank was that they believed any such entity would be “unlikely to understand the specifics of the relevant market to which the complaint refers”. An individual said this would amount to a third party “subjectively determining if the subjective oil journal assessments were wrong” and that there is, therefore, “no way this could work in practice”. One consultant said this “would not be appropriate” given that they presumed that “a fair number of complaints are actually misunderstandings that can be resolved easily and cheaply by a quick phone call to the PRA concerned”. One exchange said that “complaints procedures should be a matter for PRAs”. An investment bank commented that it “do[es] not believe that it is necessary for complaints to be resolved by a third party as a matter of course”, rather that it considered a “third party’s role to be that of an oversight function, focused on the governance process surrounding the complaints procedure and the resolution mechanism” and instead suggested that “a practitioner’s panel or industry committee would be the preferred body to deal with issues such as complaints handling”. Likewise, another trade association also supported this argument.

A minority of respondents expressed a need for an escalation point to a third party. One trade association commented that a third party should be involved “but only if the complaint was not resolved at the PRA level and it does not cause a delay in the pricing report”.

One PRA commenter responded that external dispute resolution “creates the potential for long-running and market-damaging disputes” and would have a negative impact on the independence and authority of PRAs. Another said that it lacked confidence in “any third party’s competence to rule on matters that pertain to...[its] price reporting methodologies”.

Q19: Should such a formal complaints procedure necessitate greater transparency in the handling and resolution of complaints by PRAs, for example by requiring transparency of the complaints process and publication of decisions and the rationale for them?

Responses were balanced, with positive views proposing more disclosure, as opposed to negative views questioning the practicality of a more transparent formal complaints procedure. One trade association said that “the complaint and the response should be publicly displayed” and that “a decision by a PRA to exclude a transaction from the assessment process needs to be clearly explained to avoid price speculation on the decision”. Likewise one oil

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company supports greater transparency and commented that “the lodging of a complaint should be made public immediately...as should the deliberations, decision and rationale”.

Other commenters suggested that greater transparency surrounding complaints is not necessary. Two trade associations did not propose the publication of the specifics of individual complaints cases, but did express the view that complaints decisions should be published insofar as they can inform best PRA practices. One exchange considered that complaints procedures “should be a matter for PRAs”.

The PRA commenters were also varied in their responses. One stated that it is in strong support of transparency, including the publication of complaints, final decisions and the rationale for them. However, another PRA was cautious that “many ‘complaints’ are commercially motivated” and therefore “a requirement to publish details of all complaints may “inadvertently create a lobbying tool for market participants on one side of the market”.

Q20: Please describe concerns you may have relating to potential conflicts of interests affecting PRAs arising from revenue generation, media reporting, internal staff management or any other source. Has this had any impact on the price reporting function of PRAs and if so how?

Some commenters have concerns surrounding potential conflicts of interest in relation to the ownership of PRAs and their relationships with subscribers to whom they provide a service, but from whom they also receive fees and information. Two respondents expressed concerns in relation to the ownership of PRAs. One trade association commented that it would be “desirable to ban from PRAs ownership any bank, financial institution, oil company and any other organization who has an interest in the results of PRAs['] price assessments”. A group of academics also commented that if a PRA were even partially owned by those market traders whose price information is used in their assessments, and that fact were concealed, there would be a conflict of interest constituting a platform for information abuse. Another potential conflict of interest that was noted by another trade association occurs when “*PRAs engage in revenue generation, price reporting and news services on oil markets, as incentives may arise to favor those who pay greater subscriber fees or provide greater access to market information*”. A third trade association suggested that, where this is the case, PRAs “should be required to manage conflicts...through information barriers/Chinese walls to minimize contamination risk of information which could be considered inside or privileged”. One exchange responded that the current lack of regulatory oversight, of transparency surrounding the trades which form part of price assessment process, and of a forum for complaints or independent third party review of assessments and reports published creates “an opportunity for price anomalies to be introduced into the system and for price distortions to contaminate regulated environments globally”.

Two exchanges provided positive to neutral feedback. One “found the PRAs['] management of the price assessment process to be highly professional” and noted that the PRAs “have a commitment to integrity in all aspects of price discovery and the related processes are strong and sound”, whilst another exchange expressed “no concerns”.

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The PRA commenters all confirmed that they have policies and/or a code of conduct in place to identify, manage and mitigate any conflicts of interest that may arise in their business and by their staff, and, where applicable, these are enforceable on their employees. One stated that “no-one has ever made a complaint to...[it] relating to potential conflicts of interest and it is aware of no evidence that a specific complaint of this nature has ever been made about [it]”. Another said that “editorial decisions are taken independently and without regard to the commercial interests of the company, and reporting lines are separated from the sales, marketing and consulting functions...[and that it] derives no revenue that is linked to the value of the commodities it assesses”. A third PRA commented that it “has subscribers on both the buying and selling side” and has “no incentive to influence oil prices or their level of volatility [because] if assessments are not perceived as fair, independent and ultimately representative of market value,...[it] would lose business”.

Q21 Are there any undue obstacles that prevent market participants from adopting different sources for price references? Please explain.

Responses were divided, with just under half of commenters believing that there are no undue obstacles that prevent market participants from adopting or switching to different sources for price references. One oil producer commented that “no such obstacles exist. If the buyers and sellers agree, they can change from one marker to another or one benchmark to another”. One consultant echoed this sentiment, noting that if two parties agree to use an index “it is up to the parties to address their problems”. Three exchanges also responded that there are no such undue obstacles. One said that “many, if not all, contracts incorporating price assessments have the ability to substitute a particular price in the event a particular PRA were to fail”, whilst another said that the obstacles to switching “are not ‘undue obstacles’, they are simply switching costs of the kind that are common to many markets”. One trade association commented that it “does not see the existence of any undue obstacles other than the simple and plain truth that once a market finds a mode of operation, it rarely changes”.

The other commenters said they encounter considerable difficulties in adopting or switching to a different source for price references and provided examples of what they consider to be undue obstacles from the perspective of end-users and PRA subscribers. One trade association said that changing to a different source would “necessitate re-negotiation of contracts, one by one, and convincing reluctant fuel suppliers to agree to a new price reference”. One consultant said that “it is undoubtedly the case that there is rigidity in the system that prevents companies switching PRAs easily” and “to use a Platts’ risk management tool to hedge an Argus or ICIS based physical contract would be to introduce significant basis risk into a hedge, because it is less liquid”. Similarly, one oil company referred to the risk associated with switching price references, responding that “for a given price in the market, one simply cannot switch back and forth between Platts and Argus or another PRA without suffering a cost that reflects market liquidity for the alternative reference, and the risk posed by differing pricing methodologies”. Another two trade associations agreed that “where a firm’s clients are exposed to a PRA’s price benchmark, the firm is tied to the PRA and practically has limited influence or ability to negotiate”. One individual listed several obstacles including “[e]xaggerated basis risk of using a new standard when so many long term contracts use [an]

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existing one, and trader herd mentality and fear of using a standard that everyone else is not using”. Whilst a group of academics considered some obstacles described in the consultation report to be “far-fetched”, they were strongly of the view that “it is impossible to exaggerate the inviolability of binding to the benchmarks of any particular PRA”.

Of the PRA commenters, one responded that the primary obstacle preventing market participants from adopting different sources is their “own inertia”. Another PRA referred to the difficulty market participants experience in jointly and simultaneously agreeing to adopt a new price reference. Whilst a third PRA said there is ample evidence that benchmarks and other price references are not fixed over time. The PRAs also provided some examples of market participants switching from one index to another.

Q22 If so, does this constitute a competitive concern for either individual PRA benchmarks or the PRA sector as a whole? Where appropriate, please refer to specific benchmarks.

The majority of respondents did not comment on this question.

However, a few commenters believed that the existence of undue obstacles that prevent market participants from adopting different sources for price references does constitute a competitive concern. One oil company said the “existence of barriers to switching price references is a competitive concern because access to these prices is an ‘essential service’ within the oil industry” and that because “the leading PRA sets the pace on prices, the competing PRAs need only set their prices in-line with the former”. One individual commented that “the few [PRAs] that are entrenched have a huge competitive advantage because it is so difficult for the industry to change pricing mechanisms”. One trade association reiterated its concern, responding that “until 2 years ago fuel contract pricing for the airline industry was 95% linked to one PRA quotation” and that “changing to another PRA is costly and suppliers are reluctant to accept change”. A group of academics were of the view that the possibility of changing the traditional referencing scheme presents a competitive concern for PRAs, but that this is “a blessing for the clientele”.

One consultant, whilst it acknowledged that there are obstacles to adopting different sources for price references, did not have major competitive concerns based on the fact that large players continue to use Platts and are therefore “not so unhappy with Platts’ services that they would be prepared to take on basis risk to avoid using Platts”. Having said this, they noted that this “may also reflect the fact that the large players that are most vociferous in their condemnation of the Platts are broadly neutral to the impact of those shortcomings of the Platts services of which they complain: their physical contracts and their hedge contracts all use Platts so any price assessments they do not like are cancelled out. The concern, if there is one, is where this leaves small companies, NOCs and fiscal authorities that have no influence on prices and who have a short or long exposure to prices of which some large companies are critical.”

Another consultant was of the view simply that “this is none of IOSCO’s business.”

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Naturally, the PRAs said there is no competitive concern for either individual PRA benchmarks or the PRA sector as a whole. They reiterated their comments in response to Q21 that there is ample evidence that benchmarks and other price references are not fixed over time, and that market participants have switched to other index providers in the past. One said that “there is ample literature written, for example, on US benchmarking and switches that were made by market participants to either sour or alternative Brent pricing in the US crude market”, accordingly they “believe that the record suggests there are limited barriers to entry, exit or switch in the price reporting industry”. Another PRA said “questions about competitive concerns in PRA benchmarks or the PRA sector as a whole are better dealt with by companies that participate in oil markets than by addressing the functioning and oversight of PRAs. Companies have a choice over whether to stay with benchmarks that they find unsatisfactory, or to switch...for instance, APPI Tapis, Platts Dated Brent to ICE Bwave, Platts gasoline in northwest Europe, Platts WTI for sour crude delivered to the US, Platts US gasoline and middle distillates, and Platts liquefied petroleum gas...Market participants themselves have the answer to competitive concerns - the choices are available if they want to make them”. A third PRA considered “the principle obstacle to price-switching is the legacy issue, or ‘network effect’ issue, associated with long-standing use of benchmarks. The erroneously perceived ‘power’ of price reporting services is in effect a by-product of this issue, and not the result of deliberate behaviour on the part of the services involved”.

Q23 If you have concerns about competition relating either to individual PRAs or to the PRA sector or around individual benchmarks, please comment on how you think these could be addressed.

The majority of commenters suggested various options to increase competition in the PRA sector ranging from a comparative survey of methodologies, practices and resulting data from PRAs, an international meeting of experts, preference for benchmarks from regulated markets, oversight of market abuse and mandatory competition. A group of academics suggested a number of methods of addressing competitive concerns including carrying out “a detailed comparative survey of methodologies, practices and resulting data of various PRAs, a study of laws and procedures regulating PRAs activity and an international meeting of experts for the discussion of related topics (PRAs, price volatility and regulation, physical-financial markets linkage, OTC trading) and...development of relevant recommendations”. One consultant suggested that “where a regulated futures market exists the flat prices they generate for benchmark grades are the best source of price information for that benchmark”. One exchange expressed a similar view, commenting that “pricing through a regulated exchange...is a more preferable solution in so far as Arabian Gulf price transparency and fair value are concerned”. An individual responded that “a good start would be to disallow the use of oil journal pricing in regulated futures contracts, and not oil journal priced OTC instruments to be cleared by regulated clearing houses”. One oil company noted that “there is a need for oversight in controlling pricing practices to ensure that there is no abuse of a dominant position in the market and that price adjustments are in-line with the evolution of directly associated costs”. One trade association supported “competition and new entrants; however this should not be forced and it is more appropriate to ensure PRAs are appropriately regulated to manage conflicts of interest, fair practices, etc.” Another trade association suggested that one

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way to ensure there is “competition to drive improved services is to require all suppliers in the world to provide customers the choice of at least three PRAs for pricing of their contracts”.

A minority of commenters did not consider PRAs to be a cause for competitive concern because they believe the decision to switch is with market participants and does not involve the PRA. An individual commented that “buyers and sellers signing long-term contracts...are...fully knowledgeable regarding the behaviour of the participants”. One oil producer said that “buyers of the services can shift between PRAs as well as between exchanges...it is the choice of the buyers and sellers and their call to determine the payment basis”.

Whilst the PRAs respondents did not raise any competition concerns in response to Q22, they acknowledged that competition could increase as a result of new regulation, governmental support or by working with the industry to determine alternative pricing strategies. One defined the market, for the purposes of analyzing the extent of competition, as including “all entities that publish and/or disseminate prices in physical and derivative oil and other energy markets” and noted “a number of emerging competitors in providing price assessments, including among financial information providers and exchanges”. It suggested that competition “may become more intense as increasing volumes of derivative transactions are consummated on exchanges and cleared through centralized clearing houses under Dodd Frank and analogous local regulatory requirements”. Another PRA commented that “government authorities should encourage competition by broadening the number of PRAs used in the provision of price assessments for tax and royalty calculations, in production-sharing contracts, and in other such agreements” in a similar manner to the way in which the UK tax authorities “consider price assessments from several PRAs and drop any PRA for a period if that PRA’s methodology temporarily fails to reflect the market conditions required for tax assessment purposes”. They said that “G20 governments could further promote competition by encouraging state-controlled companies to increase the number of PRAs that are used to provide price benchmarks in their long-term contracts” and state-controlled oil companies to sell a greater proportion of their output in the spot market which it believes would enhance spot market price discovery by PRAs. A third PRA proposed a collaborative industry review of the options available for alternative pricing strategies in the in the Asian marketplace—in relation to Dubai-Oman pricing.

Q24 Is there a need for structural reforms that would provide a process or mechanism for increased stakeholder representation or input of views? Given the use of PRAs by the oil industry, what mechanism would be needed to alleviate concerns of collusion?

The majority of commenters provided recommendations for structural reforms, including direct regulatory oversight, the formation of a combined public and private advisory group and pricing through an open and regulated marketplace. A group of academics said that “in order to enhance the stakeholders’ influence on the PRAs some well-prepared measures (‘reforms’) seem obvious”. One trade association suggested that “government oversight of PRAs’ assessment methodology and procedures may be considered to ensure that a larger group of stakeholders are able to provide inputs and that the views of stakeholder groups other than the oil companies are given equitable relevancy”. One consultant recommended “oversight by a

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regulator, possibly IOSCO, using a panel of experts as its operative arm,...[which]...might be populated by traders”, industry experts and PRAs. Another two trade associations both hoped for “PRAs [to] have an objective and transparent framework...subject to...systems and controls and regulatory oversight”. One exchange suggested “an open and regulated market place for the fair pricing of oil based on actual trades”. One oil company did not directly address the need for increased stakeholder representation, but suggested that the use of independent third party auditors could be a way to satisfy the market operator and the regulator that the benchmark is sufficiently robust and does not create or incentivise “disorderly or abusive behaviour”.

A minority of commenters did not consider there to be a need for structural reform. One exchange commented that “the leading PRAs are constantly engaged with market participants” via “regular open forums and...public consultation[s] on changes to methodologies”. It said “it is important that PRAs are able to make unpopular changes where necessary and there is a risk that mechanisms designed to increase stakeholder representation end up making necessary change more difficult”. One oil producer agreed that the PRAs “already regularly solicit industry input, especially when they are considering methodology changes” so the question of “‘collusion’ may therefore be inappropriate”. One consultant said that “the competitive nature of the reporting process assures that stakeholder interests are heard as long as no firm is allowed to engage in specific anticompetitive actions”.

One individual commenter believed the PRA system is so “fundamentally flawed” that it cannot be fixed.

The PRAs express clear satisfaction with their existing processes for soliciting input from the industry. One described their editorial processes as “independent and impartial” and said they “are very interested in hearing and considering all views, and not just from a limited number of stakeholders”, hence why they “as a matter of course, hold[s] numerous forums and gatherings to engage the industry”. Another commented that “no-one [sic] has ever made a complaint...[to them]...regarding deficiencies in its consultation with stakeholders”. A third PRA commented that it believes its interactions with the industry are “effective”.

Q25 What should be included in the terms of reference or objectives of any such process? What are the benefits and risks?

The majority of commenters provided varied responses on the terms of references or objectives. One trade association said that “the main objective would be to ensure that no participant is able to influence or manipulate the price assessment by PRAs”. One consultant suggested that “the terms of reference of such a panel would be to host regular (quarterly/ half yearly?) industry meetings” to discuss relevant issues. However, that consultant did note that one potential risk to its panel model is the conflict of interest of experts on the panel, therefore panel members would need to act “in a neutral and objective manner” chaired, for example, by “a member of staff of the regulator”. One individual said that “carefully structured indices with direct industry input and proper oversight is the best alternative”, whilst one exchange proposed moving the process to the exchange space for “true price discovery accessible to all”.

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The minority of commenters did not believe there is a need for terms of reference. One consultant simply said that this is “not applicable”, whilst an oil producer said more explicitly that “there is no need for terms of reference or objectives”.

The PRA respondents were of the view that the process should be left to the oil industry to decide and that specific mechanisms should not be imposed on them. They reiterated that they already hold forums for industry participants and one PRA noted that the process of gathering information should be “broad and inclusive as any participant represents a different facet of the market”. Another PRA took a ‘don’t shoot the messenger’ view of the process, but did, however, indicate its willingness “to participate to the full in any discussion of the process for choosing benchmarks on a more objective basis”. A third PRA responded that the terms of reference for any forums that it organizes would be determined by itself, and that “the terms of reference and objectives related to oil industry forums are a question for the industry to consider independently, rather than specifically in respect of PRAs”. They commented that “imposing a specific process or mechanism to gather feedback would lead to “a narrower and less constructive dialogue”.

Q26 Who, if any one, should provide any oversight for such a process?

Not all commenters commented on this question. Of those that did, the majority proposed some form of regulatory oversight. One trade association suggested that “the anti-trust authorities” could provide oversight, whilst a group of academics commented that “in any given country the form of an oversight body must be tailored to particular circumstances” and suggested that several options could be considered, including oversight at “a purely governmental level”, as well as “a number of mixed formats, such as various partnerships”. One consultant supported “oversight by a regulator, possibly IOSCO, using a panel of experts as its operative arm” and one individual suggested that “it could be [the] exchanges”. One exchange responded that oversight should be provided by the “appropriate regulator for each exchange in each jurisdiction”. Two trade associations both supported “regulatory oversight”.

One oil producer commenter said that who or whether there should be oversight depends on “maybe nobody, maybe subscribers”. The commenter said that, “in order to assess the issue, IOSCO would need to provide the required understanding of PRAs and their methodologies and communicate such understanding to subscribers who will then be in a position to provide informed opinions to IOSCO”.

One consultant commenter responded by reiterating that “oversight is not needed if PRAs cannot engage in anticompetitive behaviour”.

The PRA commenters prefer no regulatory oversight, rather they prefer to be self-governed and favour “an industry-wide approach”. One said their “forum format is open and transparent” and that “anything that impedes the free flow of ideas and comments is potential counter-productive”. Another warned that “oversight by an external authority of such a process risks unintentionally reducing competition in oil price benchmarks... In the absence of clear evidence of manipulation, it would be inappropriate and potentially detrimental to the efficient functioning of the market for an external oversight authority to endorse the methodology of one particular index in preference to another or to select a methodology for all PRAs”. A third PRA said that “such a process can only succeed on the basis of a collaborative industry-wide approach”.

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Q27 If required, what would be appropriate models for oversight of PRAs, covering the options described above and potentially others you may consider appropriate? What are the potential benefits and risks, if any? What economic impact, if any, would there be?

A minority of commenters were against the most extreme level of oversight. One exchange said that “subjecting PRAs to regulation by financial regulators would be too ‘expensive’ and ‘cumbersome’” and highlighted that there already “exist across many jurisdictions rules and regulations which are designed to protect against fraud, manipulation and collusion in market pricing. One trade association commented that “because PRAs are not systemically important, regulation of them by IOSCO entities is neither necessary nor appropriate”. One consultant believed that “oversight would likely strengthen the monopoly power of some market participants, leading to higher consumer costs” and that “regulation would likely reduce competitive forces and allow producers with a large market share to boost prices”. One oil producer was quite adamantly against regulation, commenting that “regulating for the sake of regulation is neither acceptable nor ethical”. Another oil producer opposed regulatory oversight because “most jurisdictions do not have a physical oil market regulator...[and] it would not be appropriate to assign such responsibilities to national energy...regulators...or financial market regulators”.

The majority of commenters, believed that PRAs should be “subject to the effective oversight of an independent body”. In particular, one trade association described this as vital. An investment bank supported “independent regulatory oversight of PRAs”, but noted that this should be “focused on...[ensuring] transparent and accountable price discovery methodologies, governance and complaints handling procedures”. They also indicated their support for “proportionate regulation of PRA trading execution windows.” Similarly, another trade association supports regulatory oversight of PRAs in the situation when “they operate like trading venues”. One consultant proposed oversight by “a regulator, possibly IOSCO, using a panel of experts as its operative arm...populated by traders and/or by trading consultants...[as well as] representatives of major oil and independent producing/refining/trading companies, regulated exchanges, NOCs, OPEC and fiscal authorities”. An individual also suggested that “journalists could participate in the panels, along with traders and brokers” and that “what is needed is a large panel of inputters with a core of neutral participants, and a high percentage of discards at both the high and low ends, with a neutral authoritative overseer, such as an exchange”. A third trade association highlighted the MTF model in Europe and that of DTEF (Derivatives Transaction Execution Facility) in the US and stated that the lack of independent oversight over PRAs is an anomaly. One oil company cited ESMA as the appropriate authority.

The PRA commenters advocate “self-regulation through adoption of a Code of Conduct for independent price reporting agencies”, the three leading PRAs having collaborated in preparing a draft of such a code. One commented that “the criticisms of the PRA system are, we believe, anecdotal and we are not aware of any evidence that the current system is broken, or that the benefits of reforming the system would outweigh the costs”. Another commented that there is no “public policy justification for additional direct regulation of PRAs” and that PRAs are already captured under various laws that “amount to substantial public oversight”. A third PRA said “given the open-ended, global nature of the physical oil complex, it is unclear in practical terms

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how a regulatory body could be constituted with effective powers to regulate the market, and by extension to regulate the activities of price-reporting services”.

A few commenters cited the benefits and risks of oversight. One oil company cited the benefit as providing “an ultimate recourse in relation to complaints [which would]...ensure follow-up of audits and self-regulatory procedures...and assurance on pricing methodologies” but noted that the risks include the economic impact, which would be passed onto the industry, the potential knock-on effect of stifling competition and the “risk that an oversight body would make the PRAs more rigid and less responsive to change in the market”. One exchange urged IOSCO to review the cost-benefit impact of regulation and one consultant noted that the economic impact could be “significant. The PRA commenters support self-regulation partly on the basis of “low cost”. One PRA also said there is a potential risk of partial regulation in that it “could have the undesirable effect of creating a two-tier market place”. One trade association acknowledged that there is likely to be an “increase in cost for PRAs in meeting new standards which is likely to be passed on to the subscribers. However, this may be offset by the increased transparency and information in the market.”

Q28 Do you believe that a self-regulated PRA Code of Conduct could appropriately mitigate any risks or concerns you have about PRA governance? Please explain any concerns or identified risks and give reasons for your answer.

The majority of commenters did not support a self-regulated PRA Code of Conduct. One trade association expressed concern that such a code would “not offer sufficient guarantees that problems will be acknowledged on time and that appropriate corrective measures will be implemented. An example of such failure is the banking system”. One consultant did not support a code because they did not feel it would tackle their concerns surrounding “the power given by the industry to one PRA in particular, namely Platts”. They said it “would be of little use in addressing this situation”. An individual said “it would be meaningless” and one exchange said it was “not sure there would be any change from the current situation without a fully regulated solution”. Another trade association suggested that “the more appropriate route would be towards a regulatory framework at a regional level which adheres to a prescribed set of global principles”, and one oil producer believed the pre-existing “self-regulation currently practiced by the PRAs has served the industry [well]”. A third trade association commented that “for such standards to be meaningful there must be some form of independent assurance or regulatory backstop”, noting that the “trend over recent years has been to move away from self regulation to more formal regulation”. A fourth trade association noted that the risks of self-regulation are that “it is hard for third parties via a committee to have sufficient power to meaningfully modify behaviour inside PRAs without becoming shadow 12 directors”, and that it is difficult to structure those committees “so that they are not dominated by those with the most significant commercial interests”.

A minority of commenters were in favour of a code, although some had reservations as to whether, in practice, this would have the desired outcome. One exchange said that “A self-regulated PRA Code of Conduct would be a welcome initiative. It could help codify the best practices that currently exist amongst PRAs and provide a useful catalyst for industry dialogue

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about further enhancements”. Whilst a group of academics said that “all measures should be mobilized including the self-regulated PRA Code of Conduct”, they also noted that “as the current experience with a multitude of similar code[s] demonstrates, their practical outcomes finish soon after adoption”. Similarly, one oil company commented that they found it “hard to imagine the PRAs changing through a self-imposed Code of Conduct”.

All three PRA respondents were in favour of a Code. One noted that such a Code would cover the impact of oil PRA benchmark prices, methodologies, voluntary trade reporting, accountability, governance, competition, complains, annual audits, stakeholder representation and public accountability. Another PRA said that “under the proposed Independent Price Report Organization (IPRO) Code , which was drafted by three major price reporting organizations, verification of compliance with the Code will be through independent audit by an internationally recognised audit firm or independent internal audit group within the IPRO’s corporate organisation”.

Q29 Would your view of the application of a Code of Conduct change if the PRAs were held to account for its application by a public authority? Please explain and, if appropriate, state which authority or authorities would be best placed to hold the PRAs to account. What, if any, are the potential benefits and risks?

The majority of commenters’ views would not change, for reasons linked to a desire for greater or less oversight. A group of academics said their view of the code would not change if a public authority held the PRAs to account for its application because, regardless, “there is a drastic need for the establishment of concrete deeds for which the PRAs should be definitely accountable”. One individual responded “this would just add a layer of bureaucracy on top of the fundamentally flawed oil journal methodologies”. One exchange said they “do not believe that oversight by a public authority is necessary” and one consultant commented that this “would chill reporting and likely lead to higher prices”.

A minority of commenters changed their views at the prospect of PRAs being held accountable to a public authority for their application of a Code. An investment bank commented that “such a code...[would]...be appropriate if it meets the standards set by a regulatory oversight body”. Similarly, one oil company said “it is hard to imagine the PRAs changing through a self-imposed Code of Conduct unless they are fully held to account for its application”. They suggested that “within the PRAs, an officer at the corporate board level or the corporate executive level should be held accountable for the application of a Code of Conduct and for ensuring that the Code of Conduct meets the standards and expectations of the market. This officer should also be responsible for compliance with an annual external and public audit by the PRAs of their adherence to their Code of Conduct. Ultimately, it should be possible to escalate to an external arbiter (the regulator) a repeated breakdown in compliance by a PRA with its own a self-regulated Code of Conduct”. One trade association said any “Code of Conduct should be binding, reflect standards set by IOSCO and be subject to some appropriate oversight” and highlighted that because “the impact of PRAs spans both the physical and financial markets, we believe local financial and energy regulators will need to liaise closely regarding any oversight of PRA standards”. Another trade association said they “believe that

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self regulation carries risks” and that “supervision by energy authorities is needed to ensure the PRA performs its functions correctly”. A third trade association commented that “a code of conduct is necessary but not sufficient. More importantly, it is the oversight of a government body such as the Financial Services Authority that will guarantee the proper execution of a code of conduct”.

The PRA commenters did not change their views. One said it was unclear “whether any authority exists which could suitably ‘hold to account’ the full gamut of price-reporting organizations which exist in the world today”.

Q30 Should greater attention be focused by all market authorities, namely exchanges, their governmental regulators and relevant SROs, on the reliability of price series and indexes that are constructed by oil PRAs? If “yes”, please comment on the objectives of and mechanisms for such greater involvement by these market authorities. If possible, please provide examples of financial instruments that raise price series/index reliability concerns.

The majority of commenters did not support greater attention being focused by market authorities on the reliability of price series and indexes that are constructed by oil PRAs. One exchange commented that they “have found the PRAs management of the price assessment process to be highly professional”. One trade association said that “regulatory bodies currently possess the power necessary to ensure the reliability of indices and, therefore, no new additional regulations are needed.” Another trade association also believed the current amount of market authority scrutiny “does not need to be expanded or enhanced” and an oil producer suggested instead that attention “be focused on the exchanges and their participants with thorough analysis of the PRAs’ current practices as well as a critical evaluation and comparison between methodologies so as to understand every element that impacts the development of spot prices”. Two more trade associations commented that “if PRAs are subject to a regulatory framework...this would negate the need to set such criteria”.

A minority of commenters supported greater attention being focused by market authorities. One trade association commented that the “reliability of price series and indexes is a key issue. It is imperative that market authorities focus their attention on [this]”. A group of academics also supported this suggestion, but said “it must imply a scheme of productive interaction between market authorities...covering all the financial instruments currently in usage”. One consultant commented that “if a regulated exchange relies upon PRA data for cash-settlement at expiry, I believe the exchange should have a duty of care to ensure that the assessments used are truly representative of the market price and are not subject to manipulation”.

The three PRA commenters did not support the suggestion that greater attention be focused by all market authorities on the reliability of price series and indexes that are constructed by oil PRAs.

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Q31 *Should IOSCO and any other relevant authorities develop for regulated markets and other trading facilities which use PRA benchmark prices in their derivatives contracts a set of specific criteria against which the suitability of PRA benchmarks should be assessed? If so, which criteria do you think should be included.*

The majority of commenters did not support the development of a specific set of criteria, against which to assess PRA benchmarks. One individual said simply that PRAs “need to be replaced because they cannot be fixed”, whilst one consultant said “IOSCO should do nothing until it demonstrates competence. It clearly has no qualifications in this regard as yet”. One oil company commented that, “given the evolving nature of the oil markets, setting such criteria (even at a high level) risks ossifying the process of change and evolution in the PRA benchmarks”. A trade association commented that it prefers “the suitability of the use of PRA benchmark prices in other traded derivatives to be at the behest of market counterparties rather than by supervisory boards who should focus on the integrity of that which is being published on behalf of all wider stakeholders”. Another oil company responded that they “expect both the market operator and the regulator of that market to have satisfied themselves that the methodology used to obtain that benchmark is sufficiently robust and does not create or incentivise disorderly or abusive behaviour. This could be achieved by the use of independent third party auditors”. Two other trade associations “believe that if PRAs are subject to a regulatory framework...this would negate the need to set such criteria”. One exchange commented that they “do not believe that it is possible to develop a meaningful set of criteria against which the use of PRA benchmark prices can be assessed in the development of tradable derivative contracts, since PRAs have different methodologies and competition between such methodologies is valuable”. An investment bank commented that they “welcome a proportionate approach to legislation addressing PRA responsibility for self-regulating certain of their functions, subject to oversight by a regulatory authority”.

A minority of commenters supported the development of a specific set of criteria, against which to assess PRA benchmarks. One trade association recommended that the criteria should include “daily traded volumes, number of participants, transparency on the assessment methodology, responsiveness to complaints [and] an assessment of the pros and cons of the PRA’s methodology”. One consultant agreed that “it would provide considerable comfort to small companies who are not themselves active in the market but who rely on PRA prices in their contracts to be able to see a regulatory stamp of approval, equivalent to a kite market, attached to the PRA on which they rely”. One exchange supported this, commenting that it would “require a significant industry consultation, perhaps through a forum”.

The PRA commenters did not support or were dubious as to the need for the development of such criteria. One highlighted that “IOSCO has already addressed this issue in the recently adopted Principles for the Regulation and Supervision of Derivatives Market...[which]...establishes that the appropriate focus regarding PRA index suitability is on ‘principles’ rather than ‘specific criteria’”. Another PRA said it “believes in the expression of free markets” but that if “IOSCO were to construct specific criteria against which the suitability of PRA benchmarks...[it] would consider carrying such information in its publications with a

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proper identifier”. A third PRA commented that this seems “an eminently sensible step, though in essence it duplicates procedures for verification already put in place by regulated trading markets and exchanges”.