IOSCO
Public Consultation on
Financial Benchmarks

Reply from NASDAQ OMX

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General comments

NASDAQ OMX welcomes the report produced by IOSCO. This report takes a broad approach and includes relevant aspects for consideration.

The benchmark industry benefits from a high level of integrity and credibility, as the market demands accuracy and reliability. As an index provider, NASDAQ OMX contributes with neutrality, transparency and accuracy as indexed based on data in the form of actual transactions provides an accurate reflection of the underlying.

Below we provide a few general comments for the way forward and also a few comments to the consultation questions.

Competitive environment

As a first comment, we wish to underline the importance of ensuring a competitive environment in the business of indices and benchmarks. On the European side, the European Commission’s proposal for a revision of the Markets in Financial Instruments Directive (MiFID) includes provisions to ensure non-discriminatory access between trading venues and clearing houses, to ensure access to relevant price and data feeds and information on the composition, methodology and pricing of a benchmark, and to licenses on a reasonable and commercial basis. These provisions must be defended in order to ensure a competitive environment and the efficient functioning of index and benchmark businesses.

Global market

The index and benchmark business is global. IOSCO should discourage regulatory intervention taken on regional levels which distort the functioning of this global market.

Regulatory measures should be carefully targeted

The world of indices and benchmarks is very broad. Not every corner of this broad world may benefit from regulatory intervention. Especially, a one size fits all approach would be detrimental.

Ensure same regulatory conditions for all market participants

Different regulatory conditions should not be a competitive factor. As an index provider, NASDAQ OMX is in competition with other index provider. Innovation is ever ongoing. Some index providers are financial institutions and as such regulated and under supervision from authorities.

Relevant target

We especially agree with IOSCO’s analysis of the retail context. The retail aspect is the one where regulatory intervention may be most motivated.

Integrity is a business case

A useful and successful index or benchmark business needs to provide assurance to its users that it is as reliable as it can be. This is why the industry continuously develops ways to ensure neutrality, transparency, representativeness, etc. Regulators should recognise that there is an inherent drive in the industry to develop such self-regulation.
Chapter 1

Scope

1. Do you agree with the scope of the report and intended audience? Are there other Benchmarks or stakeholders that have idiosyncrasies that should place them outside of the scope of the report? Please describe each Benchmark or stakeholder and the idiosyncrasies that you identify and the reasons why in your view the Benchmark or stakeholder should be placed outside of the scope of the report.

NASDAQ OMX does not object to the scope of the report, which is broad. It is necessary to recognize that the benchmark world is indeed both broad and diverse.

NASDAQ OMX specifically agrees with the approach taken by IOSCO to analyse the users perspective, in particular the impact of benchmarks in a retail context. In wholesale contexts, users are generally professional and as such better informed. This may not be the case in the retail context. The risks related to the retail context are the ones that should be the primary target for analysis and considerations of possible regulatory intervention.

Chapter 2

Benchmark design

2. Do you agree that the design of a Benchmark should clearly reflect the key characteristics of the underlying interest it seeks to measure?

The usefulness of a benchmark is relative to its accuracy, so it is inherent in the benchmark business to develop benchmarks that as clearly as possible reflect the key characteristics of its underlying interest. The demand for accuracy and integrity drives such a development.

Quality and integrity of Methodologies

3. What measures should Administrators take to ensure the integrity of information used in Benchmarking-setting and that the data is bona fide? Please highlight any additional measures required where Benchmarks are survey based. Please also comment on each of the factors identified in the discussion on the ‘vulnerability of data inputs’ such as voluntary submission, discretion exercised by Administrators. Are these measures adequately reflected in the discussion of roles and responsibilities of the Administrator discussed in section E?

4. What measures should Submitters implement to ensure the integrity of information provided to Administrators? Are these measures adequately reflected in the discussion of a code of conduct for Submitters discussed in section E? In particular, should Submitters submit all input data and not a selection of such data so as to maximise the representation of the underlying market? Please comment on any practical issues that compliance with such an approach may give rise to.

A few comments on the points brought forward in the report:

Quality and integrity: Benchmarks based on actual transactions and trade data are the most reliable ones as there is the least, if any, room for conflicts of interests in the process.

Voluntary submission: It is relevant to develop procedures and policies governing submission discipline and frequency of contribution. However, there must be room to adapt the principles to
each specific area, as in some areas it may not be possible to produce input. For instance, in the fish 
business, if there is no catch, there is nothing to report.

**Administrator discretion:** Transparency on the composition procedure is the best means to 
counterbalance any discretion on the administrator side.

**Composition of Submitting Panels:** What is most important is to have a representative participation. 
The risks arising from potential conflicts of interest are real, which makes this aspect one of the 
relevant targets for possible regulatory intervention. As much transparency and neutrality as possible 
in the procedure mitigates problems.

**Verifications of submissions:** Regarding communication with relevant regulatory authorities, we 
underline the importance of ensuring that all players in the competitive benchmark business must be 
able to operate under the same conditions, including the same regulatory conditions. Regulatory 
restrictions must be targeted at all players equally.

**Bona Fide:** This is indeed one of the changes that are being developed in the aftermath of the LIBOR 
scare and it is a relevant development.

### Transparency of Benchmark methodologies

| 5. What level of granularity with regard to the transparency of Methodologies would enable users to assess the credibility, representativeness, relevance and suitability of a Benchmark on an ongoing basis and its limitations with respect to their intended use? Relevant factors could include: criteria and procedures used to develop the Methodology, type of data used, how data is collected, relative weighting of data used, how and when judgement is used, contingency measures (e.g., methods when transaction data is unavailable etc), publication of information supporting each Benchmark determination, etc. Please provide examples where you consider there are currently significant gaps in the provision of this information. |

Transparency of methodologies is fundamental. It allows users to evaluate and make informed decisions of whether or not to use e benchmark and to understand what is actually being used. A relevant level of transparency is naturally driven by the need and demand for products that are in reality useful. Too much granularity does not serve this purpose, so a certain margin and judgment is needed in each case.

### Transparency of contingency provisions for episodes of market disruption, illiquidity or other issues

| 6. What steps should an Administrator take to disclose to Market Participants and other stakeholders the contingency measures it intends to use in conditions of market disruption, illiquidity or other stresses? |

Publication on website is the most appropriate and efficient.

### Transparency over changes to the Methodology

| 7. What steps should an Administrator take to notify Market Participants of material changes to a Benchmark Methodology (including to Benchmark components) and to take their feedback into account? |
| 8. How often should the Administrator review the design and definition of the Benchmark to ensure that it remains representative? |
These are typically issues where one and the same routine may not be relevant for all benchmarks. Review and related communication and consultation must be done in accordance with what is the most relevant and efficient for each market. This may depend on the type of underlying, the number and type of market participants and the production of the benchmark.

**Governance**

9. The Consultation Report discusses a number of potential conflicts of interest that may arise at the level of the Submitters, between Submitters at different entities, and between Submitters, Administrators and other third parties. Are there other types of conflicts of interest that have not been mentioned that you consider may arise? If so, how best should these conflicts of interest be addressed? Are the measures discussed in the Consultation Report sufficient to address potential conflicts of interests at the level of the Submitters, between Submitters at different entities, and between Submitters, Administrators and other third parties?

10. Do you agree that the Administrator should establish an oversight committee or other body to provide independent scrutiny of all relevant activities and management of conflicts of interest? Please comment if and why any different approaches might be appropriate for different kinds of Benchmarks. What is the minimum level of independent representation this committee or body should include?

Governance becomes most important where there are potential conflicts of interest that risk damaging market participants that need to be protected, such as typically retail clients. In the case of LIBOR and other similar “IBORs”, it is especially relevant to ensure proper management of conflicts of interests, as “IBORs” are often used as references in retail contexts, such as mortgages. We note that in the LIBOR debacle, conflicts of interests is indeed one aspect which has been the subject of investigation by the relevant authorities. This is relevant and appropriate and we underline the importance of enforcement of legislation where such a framework is already in place.

The establishing of an oversight committee for each and every benchmark, may not be feasible. For benchmarks in smaller markets, such a requirement may be a burden that risks discontinuing the benchmark, which in certain cases may anyway be the best available and extremely useful for this market.

**Accountability**

11. Should the Submitters establish accountability procedures to assess their compliance with operational standards and scrutiny of Benchmark submissions?

Yes.

12. Are the measures discussed in the Consultation Report (e.g. Audit Trail, external audits and requirement for regulatory cooperation) sufficient to ensure the accountability of Submitters? Should additional mechanisms be considered?

Yes.

13. How frequently should Submitters be subject to audits? Should these be internal or external audits?

This may vary depending on the size of the market and how widely a benchmark is used. As already underlined, where there is an aspect of protection of retail clients, the need for proper control is more relevant.
14. Are the measures discussed in the Consultation Report (e.g., complaints process, Audit Trail, external audits and requirement for regulatory cooperation) sufficient to ensure accountability of the Administrator? Should additional mechanisms be considered?

15. If recommended, how frequently should Administrators be subject to audits? Should these be internal or external audits?

16. Is public self-certification of compliance with industry standards or an industry code another useful measure to support accountability? This approach might also contemplate explanation of why compliance may not have occurred. If so, what self-certification requirements would make this approach most reliable and useful to support market integrity.

This may vary depending on the size of the market, how widely a benchmark is used and which are the end users. As already underlined, where there is an aspect of protection of retail clients, the need for proper control is more relevant. For instance, some structured products may use self-indexing, which cannot be described as neutral, and which may entail certain risks from a retail perspective.

**Code of conduct for Submitters**

17. The Consultation Report discusses elements of a code of conduct for Submitters. Are the measures discussed (e.g., adequate policies to verify submissions, record management policies that allow the Submitter to evidence how a particular submission was given, etc.) sufficient to address potential conflicts of interest identified or do you believe that other control framework principles should be added?

18. What would be the key differences in the code of conduct for Benchmarks based on different input types, for example transactions, committed quotes and/or expert judgement?

A Code of Conduct may be a relevant measure, as it would allow for flexibility to adjust to what is relevant for each benchmark and market. Again, where there is an aspect of protection of retail clients, the need for proper control is more relevant, which may motivate stronger measures, especially in relation to conflicts of interests where such rules are not already in place.

**Chapter 3**

**Approaches to enhanced oversight**

19. What are the advantages and disadvantages of making Benchmark submissions a regulated activity?

20. What are the advantages and disadvantages of making Benchmark Administration a regulated activity?

21. Do you agree with the factors identified for drawing regulatory distinctions? What other factors should be considered in determining the appropriate degree of oversight of Benchmark activities (discussed in Chapter 3)? Please provide specific recommendations as to how the distinctions discussed in Chapter 3 should inform oversight mechanisms.

As already noted, the benchmark industry is a very broad and diverse industry. As the report suggests, a one-size-fits-all approach is not relevant. As already stated, one factor that should motivate regulatory intervention is where there is a retail context.
22. What distinctions, if any, should be made with regard to Benchmarks created by third parties and those created by regulated exchanges?

As regulated exchanges and other players compete on the same market, no distinctions should be made. This is crucial as differences in the regulatory treatment would distort the playing field between these competitors. Regulatory differences should not be a competitive factor.

23. Assuming that some form of enhanced regulatory oversight will be applied to an asset class Benchmark, should such enhanced oversight be applied to the Submitters of data as well as the Administrator?

24. What are the considerations that should be taken into account if the Submitters to a Benchmark operate in an otherwise unregulated market (e.g., physical oil, gold or agricultural commodity markets) and are not otherwise under any obligation to submit data to an Administrator?

We again underline that all players in one business must be subject to the same regulatory framework. Some of the commodity markets are indeed unregulated in the sense that the underlying products are not traded on regulated trading venues. Other commodities markets are however both regulated and quite ‘financial’ as they are traded in the form of futures. A common feature of commodities markets are however that they are global. Another common feature seems to be that these markets are essentially wholesale and professional, i.e. with no retail participation. This suggests that the commodities part of the benchmark world should not be a priority for regulatory intervention.

25. Do you believe that a code of conduct, either on its own or in conjunction with other measures outlined within the report, would provide sufficient oversight to mitigate the risks that have been identified in Chapter 2? What measures should be established in conjunction with a code of conduct? For which Benchmarks is this approach suitable?

26. What other measures outlined in the report, if any, should apply in addition to a code of conduct? If you believe a code of conduct, either on its own or in conjunction with other measures outlined within the report, would provide sufficient oversight to mitigate the risks that have been identified in Chapter 2, what type of code of conduct should apply (e.g., a voluntary code of conduct, an industry code of conduct submitted to and approved by the relevant Regulatory Authority, a code of conduct developed by IOSCO, etc.)?

27. Do you believe that the creation of a Self-Regulatory Organisation (e.g., one that exercises delegated governmental powers) and itself subject to governmental oversight, whether or not in conjunction with industry codes is a viable alternative for sufficient oversight and enforcement to mitigate the risks that have been identified in Chapter 2? For which Benchmarks is this approach suitable? What if any complementary arrangements might be necessary, such as new statutory obligations or offences for Administrators and/or Submitters?

28. Do you believe that, for some Benchmarks, reliance upon the power of securities and derivatives regulators to evaluate products that reference a Benchmark or exercise their market abuse or false reporting powers creates sufficient incentives for the Administrator to ensure sure that Submitters comply with a code of conduct?

As a general comment, self-regulatory development is inherent in the benchmark business, as its success depends on trust and reliability. This would suggest that in general, self-regulation would be
a sufficient and appropriate solution. Further regulatory intervention and thus supervisory oversight should be considered where it is specifically motivated, such as where there are retail aspects.

29. Do you believe that users of a Benchmark, specifically, the users who are regulated or under the supervision of a national competent authority should have a role in enhancing the quality of Benchmarks? Which form should this role take: on a voluntary basis (e.g. the user being issued a statement that will only use Benchmarks that follow IOSCO principles), or on a compulsory basis (e.g., the competent authority could request that users who are registered under their jurisdiction should only use Benchmarks that fulfil IOSCO principles)?

Where use of benchmark involves any type of repackaging of or referencing to benchmarks to retail clients, such “re-use” could be specifically targeted with regulatory measures to the extent such activities are not already regulated. Where there is a retail context, a compulsory basis is motivated.

Chapter 4

Data sufficiency

30. Do you agree that a Benchmark should be anchored by observable transactions entered into at arm’s length between buyers and sellers in order for it to function as a credible indicator of prices, rates or index values? How should Benchmarks that are otherwise anchored by bona-fide transactions deal with periods of illiquidity due to market stress or long-term disruption?

31. Are there specific Benchmarks for which you consider that observable transactional data is not an appropriate criterion or the sole criterion? If so, please provide a description of such Benchmarks and what value you think such Benchmarks provide?

32. What do you consider the limitations or value in Benchmarks referencing asset classes and underlying interests where there is limited liquidity? Please describe the uses and value of such Benchmarks in the financial markets.

33. Do you agree that the greatest weight should be given to transactions in the construction of a Benchmark and that non-transactional information should be used as an adjunct (e.r., as a supplement) to transactions?

34. What factors and how often should Administrators (or others) consider in determining whether the market for a current Benchmark’s underlying interest is no longer sufficiently robust? What effective methods of review could aid in determining the insufficiency of trading activity within the market for a Benchmark’s underlying interest?

The preferred case would be to always anchor benchmarks in observable transactions. This is indeed the strength of indices and benchmarks produced by exchanges. However, for all benchmarks in the broad and diverse benchmark business, transactions may not always be available. The best way to deal with illiquidity and long-term stress may vary depending on the market and type of benchmark.

Transition

35. What precautions by Benchmark Administrators, Submitters, and users can aid Benchmark resiliency during periods of market stress, mitigating the potential need for market transition?

36. What elements of a Benchmark “living will,” drafted by a Benchmark Administrator, should be prioritised?
37. By what process, and in consultation with what bodies, should alternatives be determined for Benchmark replacement?

38. What characteristics should be considered when determining an appropriate alternate Benchmark? (Examples below) Should any of these factors be prioritised?

- Level and Type of Market Activity
- Diversity/Number of Benchmark Submitters
- Length of historical price series for the Benchmark alternative
- Benchmark Methodology
- Existing regulatory oversight
- Existing enforcement authority
- Volume, tenors and contract structure of the legacy trades

39. What conditions are necessary to ensure a smooth transition between market Benchmarks?

40. What considerations should be made for legacy contracts which reference a Benchmark in transition? To what extent does a substantive legacy book preclude transition away from a Benchmark? What provisions can be included in [new and existing] contract specifications which would mitigate concerns if and when a Benchmark transitions occurs?

41. How should a timeframe be determined for market movement between a Benchmark and its replacement? What considerations should be made for:

- Altered regulatory oversight?
- Infrastructure development/modification?
- Revisions to currently established contracts referencing the previous Benchmark?
- Revisions to the Benchmark Administrator?
- Risk to contract frustration

No comments.