



**EUROPEAN PARLIAMENT
COMMITTEE ON ECONOMIC AND MONETARY AFFAIRS**

- PUBLIC CONSULTATION -

Questionnaire for the public consultation on

**MARKET MANIPULATION: LESSONS AND REFORM
POST LIBOR/EURIBOR**

by ECON Vice President and Rapporteur – Arlene McCarthy MEP

This public consultation is organised in the context of the preparation of the ECON Committee reports by Arlene McCarthy MEP based on the Commission amended proposals of 25 July 2012 for a Regulation on insider dealing and market manipulation (market abuse) (COM(2012)421) and for a Directive on criminal sanctions for insider dealing and market manipulation (COM(2012)420).

Interested stakeholders are invited to respond to the questionnaire below. To facilitate the evaluation process, concise and informative responses are welcome.

Received contributions, together with the identity of the contributor, may be published on the European Parliament's website, unless contributors object to publication of their identity or parts of their responses. If contributors do not wish their identity or parts of their responses to be divulged, this should be clearly indicated and a non-confidential version should be submitted at the same time. In the absence of any indication of confidential elements, the ECON Secretariat will assume that the response contains none and that it can be published in its entirety.

Please send your answer to econ-secretariat@europarl.europa.eu by 17 September 2012 at 12.00.

IDENTITY OF THE CONTRIBUTOR

- **Name of the person and/or organisation responding to the questionnaire:**

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The Association of Corporate Treasurers

- **Description of the main activities of the organisation:**

The Association of Corporate Treasurers (ACT) is the leading professional body for international treasury providing the widest scope of benchmark qualifications for those working in treasury, risk and corporate finance. Membership is by examination. We define standards, promote best practice and support continuing professional development. We are the professional voice of corporate treasury, representing our members.

Our 4,200 members work widely in companies of all sizes through industry, commerce and professional service firms.

For further information visit www.treasurers.org

Please indicate whether you object to the publication of the identity of the contributor:

no, I do not object

If you object, an anonymous contribution may be published.

We note that certain of your questions could be interpreted very widely but we assume that the questions are being asked in the context of the recent problems with LIBOR and EURIBOR. We are therefore relating our responses to these indices and also to market indices more generally

TOPIC 1: TACKLING THE CULTURE OF MANIPULATION

Q1: How widespread is the problem? Are there other financial instruments, markets and/or benchmarks vulnerable to potential manipulation?

What action should be taken to ensure these forms of market abuse are tackled?

A1: We hope that manipulation is not widespread. However where the production of a reference rate or market index relies on some form of judgement it could be vulnerable to manipulation. However even where the index is produced from actual hard data this could be subject to manipulation through placing of abnormal trades at critical times or when market volumes are low. For example an equity index or share price at close could be distorted by trades placed in the very last few seconds of the day.

Abuse can be tackled though having good procedure and checks in compiling the index and with good governance structures supervising it. Assuming the index concerned is important or widely used then manipulating the index (whether by rate contributors or by compilers or others) should be treated as market abuse and be brought within provisions comparable to the existing directives and regulations on market abuse.

Q2: What action should be taken to ensure the integrity and quality of all benchmarks, financial instruments and markets?

We assume you are primarily interested in benchmarks. Actions to ensure integrity of instruments and markets is a very wide question and would need to consider all manner of regulations and market practices including all the aspects covered by the prospectus directive, the transparency directive, MiFID and so on.

- a. Do both benchmarks and those entities that input into the setting of the benchmark need to be regulated?

Answer: The entities involved do not themselves need to be regulated but they should be subject to market conduct rules. For example issuers of securities are not regulated but are subject to the conduct rules in the Market Abuse Directive. Likewise those entities inputting to benchmarks and compiling them need to come within provisions comparable to market abuse rules.

- b. Are traded rates as opposed to offered rates a better basis for input? Or should a 'hybrid' approach be adopted?

Answer: We assume this question is seeking to compare rates determined only by actual trades and rates based on some sort of observation of the markets supplemented by judgement. Any market index should be informed by actual market transactions as the starting point but it can be appropriate to use judgement to interpret those transactions and rates. LIBOR is based on the rates a contributor may fund itself but judgement is used to fill in gaps in the maturities where no trading took place or where trades were not typical for some reason, e.g. a particular counterparty is involved, the time of day of the last appropriate trade, the size. Euribor is based on an added degree of judgement in that the rates are the rates a contributor thinks that a

hypothetical good quality bank, not itself, may fund itself.

We therefore believe that a hybrid approach is acceptable. Such an approach including some judgement will help avoid additional variability not reflecting the changes the index should be following. For Euribor the desired variations in the rates contributed arise from changes in market conditions and the understood credit standing of the theoretical bank. For Libor, the last is replaced by changes in a bank's understanding of its own credit standing in the market. When actual transaction volumes are low there will often need to be more judgement and interpretation used. When there is market turmoil and probably there are fewest transactions, rates are most vulnerable to manipulation but yet that is just the time when indices are at their most important as indicators of what is happening. At these times particularly, supervision and checking is crucial.

- c. Should the posters of rates be granted anonymity? What would be the potential downside to such an approach? Would such a status add or diminish the integrity of prices?

Answer: In order to understand properly the nature of the index or rate, the firms contributing must be publicly known, but we accept that the contributors may have good reasons for their individual rate submissions to remain confidential to the public, at least for a period. A delay may be of systemic benefit too if it avoids needless alarm/panics about particular institutions, given the inter-connectedness, through the market, of large banks. Furthermore, a delay in publication is often used in anti-trust type rulings to impede the operation of rate-fixing rings. The party consolidating the data and regulators/supervisors should have access to the names and the quotes put in at all times so as to allow audit and checking.

- d. What kind of powers should regulators of the financial sector be given to set and introduce criminal sanctions for attempted or actual manipulation of benchmarks?

Answer: Setting criminal sanctions, or any regulatory sanctions for manipulation is a matter for legislation. The legislation can then give powers to local regulators to receive reports, to investigate and to apply any permitted sanctions

TOPIC 2: ESTABLISHING INTEGRITY AND TRUST POST LIBOR/EURIBOR

Q3: What specific measures should be taken at European/Global level to improve investor confidence? How can cooperation between global regulators be improved?

How can legislators ensure continuity between existing contracts which rely on Libor/Euribor (some \$500 trillion of contracts) and future contracts?

A3: Again we assume this question is about investor confidence in indices. In the ACT response to the Wheatley enquiry in the UK (<http://www.treasurers.org/node/8160>) the ACT recommended that the rate compilation should not be based solely on actual rates, which could easily be distorted by special circumstances, but should allow for the use of judgement by the contributors. Also the governance process should be improved.

It should not be assumed that LIBOR and EURIBOR need to be replaced. It is instead, we think, possible to refine the processes involved to improve the current system while leaving unchanged the broad principles these rates are based on. For example, a clear code to be followed by contributors, inclusion of the activity within market-abuse-type regulation and requirement by a bank's supervisors that contributors properly govern rate contributions with appropriate compliance arrangements can help confidence. For Libor, widening the definition to capture more, wider money-market transactions rather than merely inter-bank transactions so that contributions are informed by more data can help too. (A similar change is probably not needed for Euribor as that is not based off the individual bank's transactions and is entirely theoretical.)

Q4: What specific measures could be taken to enhance transparency and information quality in the financial sector?

A4: The ACT recommends that manipulation of LIBOR /EURIBOR be brought within the scope of provisions comparable to the Market Abuse Directive. We also think that institutions should be required to contribute to properly-regulated reference rates, if called upon so to do. Without that, voluntary contributions are likely to wither away, making reference rates impossible, as banks seek to avoid the compliance costs and reputational risk associated with rate contribution.

Q5: What future action could be taken to achieve better governance in order to prevent future manipulation and establish integrity, trust and fairness in the financial services industry?

A5: The rate setting process could be tightened up with a clear Code of Conduct for those involved, regular checks and supervision with a governance structure involving parties independent of the contributors and ideally involving the local financial conduct regulator. Given the reputational risk for banks, the prudential supervisor should require bona-fide contribution to reference rates by institutions they supervise.

THANK YOU FOR RESPONDING TO THIS QUESTIONNAIRE.