

Implementation of the Principles for Oil Price Reporting Agencies

Report



IOICU-IOSCO

**The Board
OF THE
INTERNATIONAL ORGANIZATION OF SECURITIES COMMISSIONS**

FR05/2014

SEPTEMBER 2014

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I. Introduction

A. Background

On 5 October 2012, the Board of the International Organization of Securities Commissions (IOSCO) published its final report on *Principles for Oil Price Reporting Agencies* (PRA Principles),¹ which sets out Principles intended to enhance the reliability of oil price assessments that are referenced in derivative contracts subject to regulation by IOSCO members. These Principles were prepared in response to a request from the G20 Leaders at their Cannes Summit in November 2011² in relation to price reporting agencies (PRAs), that “IOSCO, in collaboration with the International Energy Association (IEA), International Energy Forum (IEF) and the Organization of Petroleum Exporting Countries (OPEC), prepare recommendations to improve their functioning and oversight....” This work was further encouraged by the G20 Leaders’ Los Cabos Declaration.³

The PRA Principles specify implementation within one year of publication, *i.e.*, by October 2013. IOSCO committed to a review of implementation eighteen months after publication. IOSCO stated that such a review will evaluate the degree to which the PRA Principles have been implemented by PRAs and their impacts. With respect to such impact analysis, the G20, in its Communiqué of 5 November 2012,⁴ specifically asked IOSCO to liaise with IEA, IEF, and OPEC to assess the impact of the PRA Principles on physical markets.

In the context of the broader initiative to strengthen financial market benchmarks, it should be noted that the PRA Principles were IOSCO’s first contribution to benchmark and reference pricing standards. In July 2013, IOSCO subsequently published its *Principles for Financial Benchmarks* (Financial Benchmarks Principles).⁵ In its development of the

¹ *Principles for Oil Price Reporting Agencies*, Final Report of the IOSCO Board (October 2012), available at <http://www.iosco.org/library/pubdocs/pdf/IOSCOPD391.pdf>

² G20 Leaders’ Cannes Summit Final Declaration, available at <http://www.g20.org/images/stories/docs/eng/cannes.pdf>

³ Los Cabos Declaration G20 Leaders’ Los Cabos Declaration (June 18-19) ¶62: “We also look forward to IOSCO’s recommendations to improve the functioning and oversight of Price Reporting Agencies in November 2012, which will be produced in collaboration with other mandated organizations (IEF, IEA and OPEC), and task Finance Ministers to take concrete measures in this area as necessary,” available at http://g20.org/images/stories/docs/g20/conclu/G20_Leaders_Declaration_2012_1.pdf.

⁴ Final Communiqué Meeting of Finance Ministers and Central Bank Governors Mexico City, 4-5 November 2012, available at <http://www.treasury.gov/resource-center/international/g7-g20/Documents/G20%20Ministerial%20Communique%20November%204-5-2012-Mexico%20City.pdf>.

See also Communiqué issued by Finance Ministers and Central Bank Governors, Moscow, February 2013, which, among other things, looked forward to IOSCO’s report, in cooperation with IEA, IEF, and OPEC, of the impact of the PRA Principles on physical markets, available at

https://www.g20.org/sites/default/files/g20_resources/library/Final_Communique_of_FM_and_CBG_Meeting_Moscow.pdf.

⁵ *Principles for Financial Benchmarks* Final Report of the IOSCO Board (July 2013), available at <http://www.iosco.org/library/pubdocs/pdf/IOSCOPD415.pdf>

Financial Benchmark Principles, IOSCO took into consideration the PRA Principles, so that both sets of Principles reflect similar high-level concerns.⁶ However, because the PRA Principles were developed with due regard to the specifics of the underlying physical oil markets (including stakeholder outreach with oil market participants), and the Financial Benchmark Principles developed with due regard for benchmarks more generally, they necessarily differ in some detail.

Nonetheless, in its July 2013 report on the Financial Benchmarks Principles, IOSCO stated that it would, in the context of its collaboration with IEA, IEF, and OPEC, consider the need in due course for any modification of the PRA Principles to align them more closely with the Financial Benchmarks Principles. In order to respect the circumstances under which these two sets of Principles were adopted, as well as the on-going evaluation process of the PRA Principles, IOSCO stated that it expected that the oil PRAs would continue to comply with and implement the PRA Principles.

As requested in the November 2012 Communiqué of the meeting of G20 Finance Ministers and Central Bank Governors in Mexico City, in October 2013, IOSCO provided a progress report to the G20 on implementation of the PRA Principles. In that report IOSCO informed the Ministers and Central Bank Governors of the G20 that, IOSCO, in collaboration with IEA, IEF, and OPEC, intended to submit a report on the state of implementation as of April 2014 to the IOSCO Board in June 2014; IOSCO will then report to the G20 later in the year.

For the meeting of the IOSCO Board in June 2014 IOSCO Committee 7 on Commodity Derivatives Markets (“Committee 7” or “C7”) provided an update summarizing the status of C7’s review of implementation of the PRA Principles and committed to submit the full report to the IOSCO Board thereafter. This report to the Board is intended to meet this commitment.

B. Overview of IOSCO’s Efforts, in Collaboration with the IEA, IEF, and OPEC

Since the publication of the PRA Principles, IOSCO has continued to work in constructive collaboration with the IEA, IEF, and OPEC. In doing so, the focus has been on three main areas:

- IOSCO has continued to liaise with the four PRAs⁷ identified as the most significant in the oil markets, to ensure that they were fully engaged in the process of implementing the PRA Principles.

⁶ The Principles for Financial Benchmarks modeled Principle 9 on transparency of benchmark determinations on PRA Principle 2.3. That PRA Principle requires a PRA to describe and publish with each assessment a concise explanation of how the assessment was developed and the extent to which expert judgment was used.

⁷ Whilst developing the PRA Principles, IOSCO undertook work to identify which PRAs were most relevant for our work and identified the four main PRAs deemed most relevant to the global crude oil market, namely Argus, ICIS, OPIS, and Platts. Going forward, IOSCO will consider whether there are other PRAs that should be brought under the PRA review work.

- IOSCO has been in dialogue with audit practitioners to provide clarification and guidance on the PRA Principles to assist in their development of guidance for assurance reports on benchmarks and indices that adequately considers the specifics of the PRA Principles.
- IOSCO has engaged with stakeholders to obtain their views on the impact of the PRA Principles, and whether there is sufficient justification to warrant modification or changes to its language. This also included consideration as to whether the PRA Principles should be aligned with IOSCO's Financial Benchmarks Principles.

The following sections provide further detail on the work IOSCO has taken against each of these three areas as part of our review of implementation of the PRA Principles.

Engaging with Oil PRAs to Encourage Implementation of the PRA Principles

Given that adherence by the PRAs to the PRA Principles is voluntary, IOSCO has not taken implementation for granted. Therefore, IOSCO has continued to liaise with the four main PRAs to ensure that they are fully engaged in the process of implementing the guidelines set forth in the PRA Principles. In this regard, the PRAs have shown consistently a willingness to engage with IOSCO and have stated clearly their intention to comply with the PRA Principles.

In January 2013, representatives from IOSCO, IEA, IEF, and OPEC met with representatives from the four main PRAs to discuss the PRAs' implementation plans; the meeting resulted in the publication of Frequently Asked Questions (FAQ) on the IOSCO Principles for Price Reporting Agencies report (PRA Report)⁸ on the IOSCO website to address areas of the PRA Principles for which the PRAs had sought greater clarity.

In May 2013, the four main PRAs were asked to complete a self-assessment questionnaire. The responses were analyzed by the Committee 7 and discussed with IEA, IEF, and OPEC. The timing of this request meant that the PRAs were describing processes undergoing development to conform to the Principles that were not due for full implementation until later in the year.

Accordingly, at that stage of IOSCO's review it was not possible for these PRAs to demonstrate full compliance of their written policies and procedures with the PRA Principles. Nevertheless, IOSCO concluded that the responses demonstrated that the PRAs had made progress in implementing the Principles and devoted material resources towards their implementation. However, IOSCO sought to provide feedback to the PRAs to assist with their full implementation.

In June 2013, C7 subsequently advised the PRAs collectively that more work was likely to be needed and outlined to them the most relevant Principles on which further progress was expected. These included evidencing the inputs used in the assessment process (particularly where assessments are based on inputs other than transactions, and where a

⁸ Frequently Asked Questions (FAQ) on IOSCO Principles for Price Reporting Agencies report (PRA Report) available at <http://www.iosco.org/library/pubdocs/pdf/IOSCOPD406.pdf>

significant degree of judgment is involved); enhancing transparency with regard to how assessments are concluded; demonstrating the integrity of the reporting process and the controls on inputs and the identification of suspicious and anomalous data; and providing greater clarity regarding the processes for the identification and management of conflicts of interest.

Over the course of July and August 2013, representatives from C7 met individually with each of the four main PRAs at their primary offices to provide the PRAs with the opportunity to seek further clarification on the feedback provided regarding their self-assessment questionnaires. These meetings were particularly valuable in that IOSCO representatives were able to learn from the PRAs what changes they had been making. The meetings also revealed a good level of engagement by the PRAs both at supervisory and executive level management. It was apparent from these on-site visits that each of the PRAs had made concrete actions and was allocating the necessary human and financial resources to start reforming and improving their supervisory, governance, and technical policies.

Finally, the report outlining the PRA Principles encourages the PRAs to implement the Principles more widely to other commodity price assessments referenced in derivative contracts.⁹ Subsequent to this, IOSCO's discussions with the four main PRAs indicated that they had applied or intended to apply the PRA Principles to the majority of their price assessments, which would include commodities other than oil. The exact degree to which each of the PRAs has applied or intends to apply the PRA Principles to these price assessments varies at the moment, according to the individual PRA.

Contributing to the Production of Rigorous Assurance Review Guidelines

IOSCO determined that a key element of evaluating implementation of the PRA Principles would be the requirement that PRAs' appoint independent external auditors to review and report on the PRA's adherence to the requirements of the PRA Principles. These external reviews were undertaken by the four main PRAs in 2013.¹⁰ The resulting first year assurance reports¹¹ represent independent and objective reviews of implementation.

In 2013, IOSCO entered into a dialogue with the Institute of Chartered Accountants in England and Wales (ICAEW). At that time, ICAEW was in the process of producing general guidance on providing external assurance¹² on benchmarks and indices in anticipation that

⁹ See *Principles for Oil Price Reporting Agencies*, IOSCO October 2012, supra fn 1, p. 7, available at <http://www.iosco.org/library/pubdocs/pdf/IOSCOPD391.pdf>

¹⁰ In view of the external review requirement, IOSCO determined that it would not make any compliance assessments of individual PRAs with the PRA Principles. IOSCO has focused on obtaining direct stakeholder input in this regard.

¹¹ Although the PRA Principles refers to an annual audit, as a point of clarification, the term audit is reserved for financial statements. As explained further below, the external reviews of implementation are referred to as assurance engagements and reports.

¹² An assurance is an engagement in which a practitioner expresses a conclusion designed to enhance the degree of confidence of intended users other than the responsible party about the outcome of the evaluation or measurement of a subject matter against criteria. See Glossary at page 76 in Technical Release TECH02/14FSF *Assurance Reports on Benchmarks and Indices*, <http://www.icaew.com/~media/Files/Technical/technical-releases/financial-services/tech02-14fsf-assurance-reports-on-benchmarks.pdf>.

market participants would demand such assurance to support confidence in important benchmarks. ICAEW met with regulators and policymakers, including IOSCO, to seek their views on the proposed guidance in order to help ICAEW ensure that the guidance would meet their needs and align with their expectations.¹³

IOSCO's discussions with ICAEW provided sufficient confirmation that the PRA Principles provide an adequate basis for an external review by independent auditors. ICAEW adopted its final guidance on assurance reports on benchmarks and indices in February 2014, which included a chapter devoted to assurance on the PRA Principles.¹⁴

The findings from the first round of external reviews were made available publicly at the end of 2013.¹⁵ As discussed below, the assurance reports reveal that the PRAs have taken concrete steps to undertake supervisory, governance, and technical reforms that are consistent with the PRA Principles.

Engaging in Stakeholder Outreach on the Impact of the PRA Principles

IOSCO further indicated to the G20 that in addition to drawing on evidence of implementation from the external reviews, IOSCO, IEA, IEF, and OPEC would seek to obtain further input from market authorities, market participants, other stakeholders, as well as the PRAs themselves. Stakeholder inputs along with the external assurance reports constitute the key components for evaluating the successful implementation of the PRA Principles.

In December 2013, IOSCO requested public comment from interested parties.¹⁶ The focus of that inquiry was to learn what changes commenters had seen from the PRAs, whether behavior by participants in the oil market had changed, whether further enhancements should be made to the PRA Principles to improve the reliability of oil price assessments referenced in derivative contracts, and whether the PRA Principles should be made applicable to other commodity markets.

To support the request for public comment, in February 2014, IOSCO, the IEA, IEF, and OPEC organized a stakeholder meeting, which was held under the Chatham House Rule in order to encourage frank discussion and sharing of views. Invited attendees included the four main PRAs, oil majors, national oil companies and other physical and financial market participants, trade associations such as International Air Transport Association (IATA), and

¹³ See the feedback statement that accompanied the adoption of the guidance by ICAEW in 2014. Available at <http://www.icaew.com/~media/Files/Technical/assurance-reports-on-benchmarks-feedback-statement.pdf>

¹⁴ ICAEW Technical Release TECH02/14FSF *Assurance Reports on Benchmarks and Indices*, <http://www.icaew.com/~media/Files/Technical/technical-releases/financial-services/tech02-14fsf-assurance-reports-on-benchmarks.pdf>.

See also <http://www.icaew.com/en/technical/financial-services/inspiring-confidence-in-financial-services/assurance-reports-on-benchmarks-and-indices>.

¹⁵ External reviews available at: Argus: <http://www.argusmedia.com/About-Argus/How-We-Work>; ICIS: <https://www.icis.com/compliance/documents/icis-audit-report-2013/>; OPIS: <http://notices.opisnet.com> (free access but registration required); and Platts: <http://www.platts.com/>.

¹⁶ IOSCO/MR/51/2013 *Public Release Requesting Comment on Implementation of PRA Principles* (December 18, 2013) <http://www.iosco.org/news/pdf/IOSCONEWS313.pdf>

the International Swaps and Derivatives Association (ISDA), other regulatory bodies such as Agency for Cooperation of Energy Regulators (ACER), and key derivatives exchanges such as CME Group and ICE, as well as expert industry consultants.

Engaging with stakeholders has been an invaluable part of IOSCO's review of implementation of the PRA Principles. In this context, IEA, IEF, and OPEC have developed a survey focusing specifically on the impact of the PRA Principles on the physical oil market, which will be circulated among oil market participants.

The remaining chapters in this report summarize the implementation efforts of the PRAs and representations made by stakeholders to IOSCO, before finally setting out our conclusions and next steps.

II. PRA Implementation Efforts and External Assurance Reports

A. PRA Implementation Efforts

IOSCO's discussions with the PRAs since the PRA Principles were adopted in July 2012 and the PRAs' responses to an IOSCO self-assessment questionnaire in May 2013 indicated that each of the PRAs had initiated internal reviews of their policies and practices against the PRA Principles, and had started to revise and, in some cases, develop new policies and procedures that were aligned with the PRA Principles.

Informal visits by C7 members to the offices of each of the PRAs in the summer of 2013 confirmed that the four main PRAs had made substantial progress in aligning their written policies and procedures with the PRA Principles, specifically in:

- the content of their methodologies and procedures for internal and external review of, and changes to, those methodologies;
- measures intended to ensure the quality and integrity of the price assessment process, including explicit criteria that define the market data that could be used to compose a price assessment and measures that are designed to ensure that transactions to be relied upon are bona fide, arm's length transactions;
- enhanced disclosure of the basis upon which individual price assessments were developed and the extent to which expert judgment was used;
- quality controls applicable to submitters of information;
- selection and training standards for assessors;
- internal supervision of the price assessment process;
- record keeping requirements that support the reconstruction of assessments (*i.e.*, audit trail);
- conflict of interest and complaints policies; and

- external auditing policies.

All of the PRAs indicated that the changes needed to adapt to the PRA Principles were highly beneficial from a business perspective insofar as they gave management better internal controls, assessors better guidance, and users' greater confidence in the accuracy of the assessments.

B. External Assurance Reports

The PRA Principles require that the PRAs' undertake annual reviews by appointing independent external auditors to review and report on the PRA's adherence to the requirements of the PRA Principles. Technically, these external reviews proceed under assurance standards as the term audit is reserved for the examination of financial statements.

The first external reviews were conducted in late 2013 by PricewaterhouseCoopers LLP (PwC) for Argus Media, ICIS, and OPIS, and by Ernst & Young LLP (EY) for Platts, in accordance with the *International Standard on Assurance Engagements 3000*, as issued by the International Auditing and Assurance Standards Board (IAASB). Based on the information we have gathered, C7 understands that the assurances undertaken also conformed with ICAEW's then-draft guidance for commodity benchmarks' assurance on PRA Principles.

The external reviews that were conducted corroborated IOSCO's view at the time that PRAs had policies and procedures in place that are consistent with the PRA Principles. The assurance reports also confirmed that all of the PRAs instituted rulebook and policy changes aligned with the PRA Principles, and instituted changes to supervisory lines of control, training standards for assessors, record keeping practices, and conflict of interest and complaints processes. The details of each of these findings can be viewed in the individual PRA assurance reports.

Because the external reviews were conducted under two different assurances: reasonable assurance and limited assurance,¹⁷ C7 has been particularly interested in understanding the differences in these types of assurances. C7 believes that this issue is highly relevant as C7 looks ahead to further external assurance reports later in 2014.

Assurance Reports

IOSCO's understanding of the differences between the assurances suggests that, while both reasonable and limited assurances provide assurance as to the adoption of policies and procedures that align with the PRA Principles and as to the likelihood that if those policies and procedures were followed they would give effect to the PRA Principles, a reasonable assurance is based on a larger evidentiary base and more testing than for a limited assurance.

Specifically:

¹⁷ A reasonable assurance review was conducted by EY for Platts. Limited assurance reviews were conducted by PwC for Argus Media, ICIS, and OPIS.

- A reasonable assurance results in a positive form of expression of the practitioner’s conclusion that: *“PRA’s control procedures are suitably designed such that there is reasonable but not absolute, assurance that the PRA’s Methodology Framework and the requirements of the PRA Principles will have been achieved if the described control procedures are complied with satisfactorily.”*
- A limited assurance results in a negative form of expression of the practitioner’s conclusion that: *“Based on the results of our procedures, nothing has come to our attention to indicate that the PRA’s response to the PRA Principles is not fairly stated, in all material respects.”*

At its meeting held in May 2014, C7 met with representatives of the ICAEW specifically EY, PwC, and Deloitte (collectively, the “practitioners”) in order to clarify the distinctions between the two forms of assurances as well as to learn the practitioners’ impressions of their external reviews.

The practitioners confirmed that under both forms of assurance, they collect evidence that maps the PRAs’ policies to the PRA Principles, and they examine whether the PRAs also have practices that are intended to carry out those policies. The practitioners explained that under both limited and reasonable assurances, they were able to report that there are policies and procedures consistent with the PRA Principles in place. They also clarified that a reasonable assurance gathers sufficient evidence to express a positive conclusion that there are policies and procedures in place that would give effect to the Principles if they were being followed and that as the limited assurance expresses a negative conclusion that does not require the same degree of evidence and testing.

Accordingly, the distinction between the two assurances is found in the evidentiary standards and testing procedures necessary to permit a practitioner to provide a conclusion.

The practitioners noted that the decision whether to proceed with a limited or reasonable assurance ultimately is made by the PRAs, based on the PRAs’ evaluation of the practitioners’ description of the extent of procedures required under the two assurances, as well as costs associated with each type of review. The cost of a reasonable assurance is generally greater than that of a limited assurance.

The practitioners agreed that as the PRAs gain more experience in applying their revised policies and procedures, the assurances conducted will provide a greater body of evidence available for review, which may allow a practitioner to make additional unconditional affirmative conclusions with respect to whether the PRA’s policies and procedures could give effect to the PRA Principles if followed. In this regard, one practitioner observed that it was not surprising for the majority of PRAs to undertake limited assurance reviews, because over the period these reviews were undertaken, PRAs were primarily engaged in revising their internal policies and procedures in response to the PRA Principles, as published in October 2012.

Notwithstanding such greater body of evidence, the practitioners noted that in fact they would not be able to provide the affirmative statement of implementation under a reasonable assurance with respect to certain of the PRA Principles having aspirational objectives (Principles that called for the PRAs to take measures encouraging actions by third

parties).¹⁸ The practitioners noted that they had no way to determine, for example, whether submitters were in fact submitting all of their data as called for under Principle 2.2(f).

IOSCO's understanding of the different assurances suggests that a reasonable assurance standard provides a more comprehensive basis for demonstrating adherence to the PRA Principles as it requires a larger evidentiary base and more testing than a limited assurance.

As noted above, the first year of implementation generally has been a developmental year in which the PRAs have put into place the overarching structure of policies and practices that are intended to align with the IOSCO PRA Principles. The second year review should have a greater body of evidence available regarding the degree to which implementation in fact has taken place.

Based on greater understanding of the two assurances, IOSCO concludes that second year reviews should be conducted under the reasonable assurance in order to provide the most benefit in terms of revealing actual implementation practices. At the same time, the limited assurance would remain appropriate for Principles 2.2(e), 2.2(f), and 2.4(c), which call for actions by third parties that are not under the control of the PRA and beyond the power of the practitioners to obtain information.

III. Stakeholder Input

In collaboration with IEA, IEF and OPEC, IOSCO sought input from market authorities, market participants, and other stakeholders, as well as the PRAs themselves by means of a press statement published on IOSCO's website on 18 December 2013¹⁹ and at its meeting on 6-7 February 2014 in Madrid.

The February 2014, IOSCO, the IEA, IEF, and OPEC organized stakeholder meeting, was held under the Chatham House Rule in order to encourage frank discussion and sharing of views. Discussions focused on the following areas: changes the parties have seen from the PRAs as they have implemented the PRA Principles; how behavior by participants in the physical oil market had changed over the last year, if at all, in the context of the greater focus on benchmarks and the perceived associated risks; what further revisions, if any, should be made to the PRA Principles to improve reliability of price assessments in the oil market; and should the PRA Principles be made applicable to other commodity markets, and if so, what other changes should be made.

The following sections summarize the representations made directly to IOSCO through these mechanisms. This summary does not reflect any views or conclusions on the part of IOSCO or the IEA, IEF and OPEC.

A. Implementation of Principles

¹⁸ See PRA Principles 2.2(e) (encourage parties that submit data to submit all of their data); 2.2(f) (employ a system of appropriate measures so that submitters comply with the PRA's applicable quality and integrity standards for market data); 2.4(c), requiring a PRA to, among other things, "Encourage submitters to submit transaction data from back office functions...."

¹⁹ *IOSCO Requests Public Comment on Implementation of PRA Principles* (18 December 2013), supra fn 16 at <http://www.iosco.org/news/pdf/IOSCONEWS313.pdf>

Transparency

Stakeholders considered that the PRAs had taken reasonable steps to improve the transparency of their price assessment methodologies. There was general consensus that the PRAs have acted to address the Principles with regard to the quality and integrity of their methodology descriptions and their application to price assessments. Stakeholders felt that the enhanced transparency now available to market participants had not compromised the ability of the PRAs to maintain their independence from data submitters.

Although stakeholders acknowledged that much effort has been made by the PRAs to improve transparency, there was still a desire to see more granularity in the descriptions of how methodologies were applied in individual assessments and to have greater consistency in these descriptions across PRAs.

Detail of methodologies

Stakeholders noted improvements in the level of detail within the PRA price assessment methodologies, but observed that there are still variations in the level of detail provided in the narrative explanations of changes and deviations from methodology. However, other stakeholders considered that it would be difficult to apply stricter guidelines to how PRAs should explain and set out such deviations, especially where adjustments had been applied to bids and offers where no trades had occurred and given the unique dynamics of some of the markets.

Complaints and query handling

The production of a more formalized complaints process in response to the implementation of the Principles was appreciated by stakeholders, although feedback suggested that, as distinct from queries, there had been little use of formal complaints procedures yet, and so this was relatively untested.

Stakeholders noted concerns about the varying length of time that PRAs took to respond to market participant queries relating to individual price assessments. While some responses were quick, others were slow. Such queries ranged from questions on the consistency in the use of parameters, to clarifications sought on deviations between PRA and market participant views on price assessment results. Stakeholders suggested that further clarity and transparency on the PRA process for responding to queries might assist in this regard and it was further suggested that some form of published statistic examining the speed and quality of PRA query response might also be desirable.

Overall, stakeholders acknowledged that the external reviews undertaken by each PRA attested to their adherence to the PRA Principles.

B. Impact on market participant behavior

Feedback from some stakeholders suggested that the composition of participation in the price submission process had altered somewhat, but overall the general volume of submissions and the quality of resulting price assessments themselves remained unchanged.

Stakeholder views indicated that for some price assessments, market participants have been scaling back their price submissions. In this context, some stakeholders noted the increased role of compliance departments in the submission process in response to increased regulatory interest, and expressed concern that this might impact the readiness to make submissions to PRAs, as well as the speed with which they are made. Stakeholders considered that in view of the fact that price submissions are voluntary, IOSCO should give thought to what can be done to help manage potential compliance and liability risk for data submitters.

However, there was general consensus that the pool of available data to PRAs for their assessments had not been reduced, because, where some types of price submissions had been scaled back (*e.g.* concluded trades), other types of data (*e.g.* bids and offers) were being submitted as an alternative. Feedback also suggested that there were some changes to the profile of market participants in this regard, with some stakeholders noting the broad market trend of reduced participation in the commodity markets from investment banks. For some survey markets that are less liquid and therefore rely more on expert judgment, stakeholders noted that the ability to have useful discussions with market participants had in some cases been reduced.

In considering potential solutions to this issue, suggestions ranged from requests to an international body such as IOSCO for statements encouraging submissions, or for non-mandated general guidance provisions for data submitters, or for even a form of Code of Conduct for data submitters. Particularly for the latter, stakeholders warned that in considering such an option IOSCO should be conscious of the importance of data submitter independence, as market participants, from PRAs. In further discussions on the role of data submitters, it was noted that a significant proportion of the data submitters were already regulated in various forms and in different jurisdictions, and there was a preexisting culture that was aware of issues such as market abuse and this should be considered in any further discussion.

Stakeholders discussed whether there was sufficient transparency in the changes PRAs had made to their price assessments and whether this process provided sufficient opportunity for stakeholders to engage and influence the outcome in a productive and transparent manner.

However, stakeholders also noted a counterbalancing fear of anti-trust issues arising when proposed changes to price assessments are discussed with PRAs, in the context of both open and closed meetings, although the PRAs themselves discounted this. These stakeholders considered that this was particularly important where changes impacted derivative markets, because given the potential effect on financial markets they thought it particularly important to be able to share views and ideas without such risk arising.

C. Impact on derivative markets

In considering the potential impacts of the PRA Principles on how derivative exchanges operate their markets, stakeholder feedback confirmed that the most substantive impact was seen from exchanges requiring assurance that PRA assessments used in pricing their derivative contracts complied with the PRA Principles.

With regard to whether IOSCO should seek to identify whether there are additional PRAs that should adopt the PRA Principles, some feedback suggested that IOSCO should continue to endeavor to treat all relevant PRAs equally.

D. Potential amendments to the PRA Principles

Stakeholders expressed mixed but not strongly-held views on whether it was appropriate to formally widen the application of the PRA Principles to other commodities but there was general consensus that the PRA Principles required more time to become embedded before further consideration should be given to their wider application. Some stakeholders were of the opinion that the PRA Principles had been developed specifically for the oil market and the identified inefficiencies in their related price reporting activities. It might therefore be inappropriate to extend them to other commodities that have not been identified as exhibiting similar inefficiencies without a similar assessment process.

An opposing point was expressed that the PRA Principles were by their nature general, and it would be both possible and valuable to roll them out to other products. Here some stakeholders noted that broader application of the PRA Principles to other commodities had already been carried out by some PRAs.

Some stakeholders referred to potential key person risks relating to the authorship of price assessments as possible areas warranting examination by IOSCO. Such risks stemmed from relying on the expertise, knowledge, and contacts of a small pool of editors and reporters, or even from relying on the expert judgment of one individual.

E. Potential application of IOSCO Principles for Financial Benchmarks

The majority of stakeholders held the view that attempts to extend the Financial Benchmark Principles to the oil markets would be disruptive. It was noted that, given these initiatives were prompted by specific examination of non-commodity financial benchmarks (*e.g.*, LIBOR), it would be inappropriate to apply the Financial Benchmark Principles more broadly to oil and other commodities. However, some stakeholders noted that there were some aspects of the PRA Principles that could be brought into line with the Financial Benchmark Principles, such as the Financial Benchmark Principles guidance to data submitters. The overall consensus was that this was not sufficient to require their adoption.

IV. Conclusions

A. Implementation of the PRA Principles

IOSCO's framework for reviewing the implementation of the PRA Principles has involved ongoing collaboration with IEA, IEF, and OPEC, as well as ongoing engagement with the four main PRAs, input from stakeholders, and in the case of the external assurance reviews, audit practitioners.

Overall, IOSCO has concluded that during the first year of implementation the four PRAs have made good progress with regard to the PRA Principles. They have made changes to align their policies and procedures with the PRA Principles and invested considerable time and resources in doing so. The responses to a self-assessment questionnaire last year

demonstrated that the PRAs have updated their policies and procedures to implement the PRA Principles and instituted new ones.

Discussions held with the four main PRAs made clear that the implementation of the PRA Principles had support across the PRAs' business activities, from data collection supervision through to executive level management. The PRAs also have either broadened their application of the PRA Principles beyond crude oil products or have plans to do so.

The external review process has been undertaken in accordance with professional assurance standard practices and supports the conclusion that the PRAs have put in place, policies and procedures that are aligned with the PRA Principles. The first year assurance reports validate assertions made by the PRA that they have made changes to their assessment frameworks and methodology descriptions, record keeping, conflicts of interest management, and complaints process.

C7 notes that stakeholders have indicated that they are broadly content with how the PRAs have implemented the PRA Principles. C7 believes, however, that implementation is still ongoing and there are aspects of the implementation that require more time before a full assessment can be carried out and thus before any judgment can be made as to whether any modification of the PRA Principles is warranted.

C7's engagement with stakeholders indicated that some questions remain about the submission process, both from the perspective of the volume and type of data submitted, and in the context of ensuring the accuracy and reliability of submitted data used in the assessment process. Some stakeholders have requested further granularity regarding changes and deviations from PRA methodologies. In addition, there has been little use of the reformed complaints processes, so this area has been relatively untested.

Taken together, C7's review suggests that the implementation of the PRA Principles remains an on-going process. The preliminary nature of these conclusions reflects that this has been the first year of a continuing process of implementation and of evolution of policies and procedures by the PRAs.

IOSCO sought clarification from audit practitioners to interpret the results of the external assurance reports. Here, IOSCO has been particularly interested in understanding the differences in the types of assurances available (limited versus reasonable), and the implications for an understanding of the degree to which the PRAs have implemented the PRA Principles, and how the PRA Principles will take effect over time.

From this, IOSCO's understanding of the different types of assurances revealed that the application of the reasonable assurance in the second year assurances reports is a more comprehensive basis for demonstrating adherence to the PRA Principles. However, as noted above, it is appropriate to recognize that a limited assurance is appropriate for certain, aspirational Principles, particularly those dealing with the submission of data.

IOSCO's evaluation of stakeholder feedback also confirms its overarching conclusion that the initial efforts by the PRAs have brought about significant changes to their policies and procedures. Stakeholders also confirmed that they have perceived improvements in the enhanced transparency that PRAs have given to their price assessment methodologies. A more formalised complaints process was also highlighted by stakeholders as an improvement

particularly worthy of note, although there were residual concerns regarding the way the PRAs manage queries relating to their price assessments and the level of granularity in the descriptions of how the methodologies are applied. IOSCO intends to examine such residual concerns more closely as it examines how the PRA Principles take effect over the remainder of 2014 and into 2015.

With regard to oil derivatives available for trading on markets within the jurisdiction of IOSCO members, IOSCO has seen further evidence of implementation of the PRA Principles. In its publication of the PRA Principles, IOSCO noted that a market authority having due regard for IOSCO's PRA Principles would want to determine that a PRA assessed price that is referenced by the terms of a derivatives contract is sufficient and accurately reflects transactions in that market. Therefore, IOSCO was reassured to learn that regulated markets actively seek assurance that the price assessments utilised in their derivative contracts adhere to the PRA Principles.

These developments do not mean, however, that the vulnerabilities identified by IOSCO in the final PRA Principles' report have been eliminated entirely. The vulnerabilities IOSCO had identified at that time resulted from the following factors:²⁰

Selective reporting: The data that are provided by some physical oil market participants to PRAs are submitted on a purely voluntary basis. Of those participants who choose to submit data, there is no requirement that they submit all of their data.

Opacity and variations in assessment methodologies: The methodologies used by PRAs to assess oil prices show considerable variation both across PRAs and within a single PRA. The methodologies vary according to the extent to which they are based on actual transactions, bids, offers, and other relevant market information. The time periods (windows) in which data are collected, the relative importance assigned to each type of data, and the extent to which other market information is considered will vary based on the PRA's methodology. The methodologies also require the application of judgment, particularly when data are extrapolated or when there is a paucity of reported transactions.

As further noted in the final PRA Principles' report, these factors result from the realities and complexities of the physical market for oil, which are nonstandard and diverse. The PRA Principles were designed to address the aforementioned vulnerabilities and to do so within the context of the global physical oil market. In developing the PRA Principles IOSCO did not make judgments about specific PRA assessment methodologies.

The conclusions drawn from the multiple strands of IOSCO's review to date reflect that the PRA Principles have been the catalyst for meaningful change by the PRAs. Moreover, the practices put into place by the PRAs, particularly with respect to transparency of methodologies, explanations of how assessments are constructed, and complaints processes provide a mechanism by which stakeholders can engage with the PRAs.

²⁰ See *Principles for Oil Price Reporting Agencies*, IOSCO, October 2012., supra fn 1, pp. 6-7 available at <http://www.iosco.org/library/pubdocs/pdf/IOSCOPD391.pdf>

IOSCO expects that the continued efforts by the PRAs, annual assurance reviews, feedback to the PRAs by stakeholders, and IOSCO's further monitoring will all operate together to improve the assessment process.

B. Potential changes to the PRA Principles and market implications

IOSCO also considered whether there is any need to modify the PRA Principles or change the language of the final report that adopted the PRA Principles, particularly with regard to its closer alignment with the IOSCO Financial Benchmarks Principles.

Modification of PRA Principles

IOSCO notes that stakeholders have indicated that they are broadly content with how the PRAs have implemented the PRA Principles. However, implementation is on-going and there are aspects of the implementation that require more time before full assessment can be carried out and thus before any judgement can be made whether they are sufficiently material to warrant a modification of the PRA Principles.

IOSCO is conscious that the PRAs have been subject to only one external review and the four main PRAs are in the process of agreeing the scope and nature of their second year reviews for 2014. IOSCO believes that there is scope for the reviews to develop further and provide additional insights in the near term to help guide its thinking on whether the PRA Principles are achieving the desired outcomes. IOSCO also considers that as the four main PRAs are in the process of agreeing the scope and nature of their 2014 reviews, any modifications or changes made now to the language of the PRA Principles could disrupt this process and compromise the effectiveness of these reviews.

IOSCO notes that in considering the potential evolution of the PRA Principles its review of the implementation of these Principles brought to light what could be residual operational inefficiencies that warrant further examination. For example, stakeholder feedback suggests that there may be a need for a more formal query management process to assist in providing a framework in which PRAs can respond to queries on a more consistent basis than currently the case. Such a process could align with that which the PRAs have already implemented for complaints handling. However, it could potentially be disruptive, to propose changes to the PRA Principles before they have had sufficient time to be applied across more PRA processes, and before IOSCO and the market have had the opportunity to assess fully the materiality of such residual concerns.

With regard to the aspects of the implementation that require further evidence and analysis, IOSCO believes that the potential impact of the PRA Principles on the nature of data submissions may warrant further examination. Information IOSCO has gathered suggests that data submitters are adapting to a changing regulatory environment that is affecting both their engagement with the PRAs and the type of data they submit for PRA price assessments.

The PRAs and stakeholders are conscious of increasing risks around the quality and quantity of submitted data used in price assessments. Consequently, IOSCO has concluded that this is a particularly important development to analyse, given the voluntary nature of the PRA Principles and the potential for data submitters to regard submission to PRAs as representing a significant regulatory risk. However, since stakeholders do not generally

consider there to have been a change in the total volume of data submissions to PRAs, IOSCO believes it would be premature to seek to modify the PRA Principles or change its language at this time, to address this perceived risk until further work is undertaken later in 2014-2015.

Overall, IOSCO believes that there is an insufficient basis to support changes to the wording of the PRA Principles at this time but will set a clear timeframe in which to monitor further how the PRA Principles take effect and will examine closely identified residual concerns.

Alignment of PRA Principles with Financial Benchmark Principles

IOSCO considered whether there would be any scope for aligning the PRA Principles with the Financial Benchmarks Principles. IOSCO's review of this issue, which included obtaining stakeholder input, did not suggest that further alignment of PRA Principles with those for Financial Benchmarks Principles is warranted and so has determined not to undertake any further work in this regard.

In considering the merits of this, IOSCO has had due regard for the genesis of the Financial Benchmarks Principles and the PRA Principles. IOSCO notes that the Financial Benchmarks Principles were developed in response to a specific examination of the risks relating to non-commodity financial benchmarks (*e.g.*, LIBOR), while the PRA Principles were developed to improve the functioning and oversight of the oil markets.

IOSCO supports the views expressed by those stakeholders that considered that, while there are financial benchmarks that reference oil, it is important to keep the PRA Principles separate from the Financial Benchmarks Principles so as to ensure that the PRA Principles continue to target effectively the vulnerabilities arising from the specific nature and dynamics of price assessments in the oil market.

Furthermore, IOSCO notes that the PRA Principles preceded the Financial Benchmark Principles and came into effect in October 2012 after a comprehensive two-year period of stakeholder engagement and analysis, while the Financial Benchmark Principles were published a year later in July 2013. Therefore, in developing the Financial Benchmark Principles, IOSCO already sought to align those Principles with the PRA Principles, giving due regard to the specific nature of financial benchmarks and to price assessments in the crude oil market.²¹

Given that work to align the two sets of Principles already took place and that IOSCO's review of implementation of the PRA Principles did not suggest that further alignment of PRA Principles with those for Financial Benchmarks is warranted, IOSCO does not believe that further alignment of PRA Principles with those for Financial Benchmarks Principles is justified.

Impact of the PRA Principles on physical markets

²¹ Page 6 of the Financial Benchmark Principles notes that “*IOSCO took into consideration the PRA Principles during the development of these Principles for Financial Benchmarks.*”

The G20, in its Communiqué of 5 November 2012, asked IOSCO to liaise with IEA, IEF, and OPEC to assess the impact of the PRA Principles on physical oil markets. IEA, IEF, and OPEC are liaising with IOSCO to engage with market participants to identify changes in the physical oil market that may be attributable to the PRA Principles and intend to provide an assessment of any potential impact in a report to the G20 at its Summit in Brisbane in November 2014.

V. Next Steps

A. Continued monitoring by IOSCO

The preliminary nature of our conclusions reflects that this has been the first year of a continuing process of implementation and evolution of policies and practices by the PRAs.

Accordingly, IOSCO in collaboration with IEA, IEF and OPEC will undertake further examination and monitoring in this regard, including outreach to stakeholders, and will report back on PRA implementation efforts in 2015.

B. The PRAs under review

IOSCO notes that when it published the PRA Principles, it called for the voluntary adoption and implementation of the PRA Principles by PRAs without distinction as to the identity, size, or market impact of particular PRAs. In addition to the express adoption and implementation by a PRA of the PRA Principles, IOSCO identified the selective use by a market authority of its rule approval and/or review authority over derivatives contracts as a means to effect implementation and review of the Principles.²²

To date, IOSCO's implementation review has focused on the four main PRAs that voluntarily adopted and implemented the PRA Principles. IOSCO has determined, however, that it should examine, first, the extent to which entities other than those four main agencies, which also perform PRA activities, produce assessments that are referenced by oil derivatives contracts, and, second, whether it is appropriate to bring these other entities within the scope of IOSCO's review of implementation of the PRA Principles.

C. Report to the G20

IOSCO, in collaboration with IEA, IEF and OPEC, will submit its report to the G20 at the Summit in Brisbane in November 2014 and highlight its intention to further examine the following areas:

- The external review process as it develops over the course of 2014-2015.
- The PRAs' progress in addressing the identified operational issues.
- Monitoring of the risks relating to the quality and quantity of information to which PRAs have access for their prices assessments.
- The results of IEA, IEF, and OPEC's review, in co-operation with IOSCO, of the impact of the PRA Principles on the physical oil markets.

²²

Id.

- Further stakeholder input, particularly with respect to the adequacy of the PRAs' explanation of how a particular assessment has been derived and the effectiveness of PRAs' complaints processes.
- Whether there are other PRAs that should be brought into the scope of the PRA review.