



## Eurex Response

To the ESMA & EBA Consultation Paper on  
*'Principles for Benchmarks-Setting Processes in the EU'*

Frankfurt/ Main, February 15<sup>th</sup>, 2013

## I. Background

Eurex welcomes the opportunity to respond to the ESMA & EBA consultation paper on 'Principles for Benchmarks-Setting Processes in the EU'. The response to this questionnaire is focused on the regulated market Eurex Deutschland administered and operated by Eurex Frankfurt AG ('Eurex'). In order to provide a comprehensive picture of Eurex and its affiliates ('Eurex Group'), please see a description below.

Eurex is one of the world's leading derivatives exchange organizations and is owned by Deutsche Börse AG. Eurex offers a broad range of international derivatives benchmark products and operates the most liquid fixed income markets in the world, featuring open and low-cost electronic access. With a global distribution network connecting more than 400 institutions from 24 countries, with more than 8,600 admitted traders, trading volume at Eurex exceeds 1.5 billion contracts a year.

Aside from operating a fully electronic trading platform, Eurex Group provides an automated and integrated joint Clearing House. Eurex Clearing is Europe's largest central counterparty clearing house, processing gross risks valued at almost EUR 10 trillion every month, with fully-automated, straight-through post-trade services. And it is the world's only major clearing provider to control risk continuously by recalculating position risk in real-time.

Since its inception in 1998, Eurex has continually set a proven track record in electronic trading and clearing and is providing highly efficient liquidity pools. The deep market liquidity of Eurex products and the diversity of trading participants ensure fair, transparent and competitive pricing.

Neutrality to the markets, a clear and binding regulatory framework and the supervision through the responsible authorities is key, especially in volatile market conditions. We have three levels of oversight: federal, state and internal regulatory measures.

## II. Introduction

Financial Indices are an aggregation of market data of financial instruments or acquirable assets which are used for three different purposes, either as a) a basis for financial products ("underlying") or b) to evaluate financial investments ("benchmark") or c) for information purposes. Besides their obvious function as underlying for various financial products, indices fulfill other important roles in the overall macro-economic environment.

Against the background of the recent alleged misconduct around LIBOR / EURIBOR, **Eurex supports initiatives that address concerns about panel-based indices** and also welcomes policy orientations for this specific class of indices ahead of any formal legislative framework which may follow in the future.

Any risks of manipulation arising from potential inherent conflicts of interest linked to production and governance as well as use of benchmarks needs to be analyzed in order to derive potential necessary steps accordingly. However, **only a small number of indices or indicators are created and operated in a non-transparent way, nor are usually conflicts of interest involved** as in the cases of the LIBOR, EURIBOR and TIBOR manipulation.

To the contrary, there are several Neutral Index Providers operating on a global scale who compete with each other and who in fact use high quality data to calculate their benchmarks. In doing so they operate alongside clear and transparent rules, and have no conflicts of interest tied to the production of those benchmarks, indices or indicators. **Neutral Index Providers in fact serve the entire market in an unbiased and transparent way. Reliability as well as transparency is not only in the Neutral Index Providers' pure self-interest, but is also a fundamental requirement of regulated markets as their major customers and users of benchmarks who need high quality and transparent indices as underlying for their openly and transparently traded derivatives products.** Eurex is the market operator of a derivatives exchange/ regulated market, neutrally organizing trading in such derivatives. Eurex is highly concerned with the suitability and reliability of indices on which derivatives are designed to be traded on exchange. These products must be designed to not only suffice the requirements for multilateral and transparent derivatives trading, but also need to adhere to the requirements set by the law and regulation as well as by the competent supervisory authorities. **An index-based derivative will serve the market well only if the derivative contract is approved by the relevant competent authority and its underlying index is trusted by market participants.**

Regulating those financial service providers, like Neutral Index Providers and indirectly regulated markets, and their products in the same way as those banks involved in the creation of LIBOR, EURIBOR and TIBOR would clearly result in excessive regulation, which could lead to regulatory arbitrage if not applied on a global scale. It is essential to **draw clear distinctions between indices, which are created and operated by a person or unit with a conflict of interest on the one hand and indices provided by Neutral Index Providers on the other hand.** Thus, fully rule-based objective indices do not require any further governance arrangements.

Moreover, it should be avoided that any guidelines or principles addressing indices other than panel-based ones potentially prejudge the outcome of the legislative process initiated by the European Commission in late 2012, where Eurex already contributed through the Deutsche Börse Group statement.<sup>1</sup>

### **III. General Remarks**

Eurex, a regulated market under MiFID, has licenced a variety of benchmarks/indices from different index and benchmark providers.

**Eurex designs derivatives contracts based on these indices and in this respect can be seen as user of indices. As a regulated market, however, Eurex does not make use of any of its listed derivatives products , but organises open and transparent markets for the participants of its market.** For example, Eurex uses indices to create derivatives that address the needs of various derivatives users either with the purpose of directional trading (exposure), hedging or cash management.

As a provider of listed derivatives, Eurex constantly seeks to offer products from various asset classes for its customers. **Together with market participants and also Neutral**

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<sup>1</sup> [http://ec.europa.eu/internal\\_market/consultations/2012/benchmarks/registered-organisations/deutsche-boerse-ag\\_en.pdf](http://ec.europa.eu/internal_market/consultations/2012/benchmarks/registered-organisations/deutsche-boerse-ag_en.pdf)

**Index Providers, the suitability and reliability of indices as underlying is discussed. Derivatives products designed for trading need to be approved by the competent authority, as described before.**

Eurex is constantly and closely monitoring its product portfolio. **As such derivatives on potential benchmark indices as underlying can be added to the product portfolio or discontinued, if an index is not utilized by the market place anymore.**

Further aspects that need to be considered are market structure and liquidity that might have an impact on the factors to determine a reliable benchmark. While for equity indices high liquidity and transparency are main factors, for less liquid and rather intransparent markets the use of the benchmark, its rulebook, and its governance has a major impact on the selection of the benchmark.

#### **IV. Detailed Comments**

***Question 1: Definition of the activities of benchmark setting***

***Do you agree with the definitions provided in this section? Is this list of activities complete and accurate?***

The proposed definition does not fully include index based derivatives contracts listed on regulated markets like Eurex. Eurex does not offer structured products, but designs derivatives on indices which are approved by the competent exchange supervisory authority and listed on a regulated market for open and transparent derivatives trading. Hence, this is an aspect that differentiates the regulated market as a user from other uses described in this consultation paper.

***Question 2: Principles for benchmarks***

***Would you consider a set of principles a useful framework for guiding benchmark setting activities until a possible formal regulatory and supervisory framework has been established in the EU?***

At this point, it is important to emphasize the difference between benchmarks based on regulated market transactions and panel-based indices (OTC data polls), where an inherent conflict of interest exists between the data contributor and the benchmark user. Against the background of the recent alleged misconduct around LIBOR / EURIBOR, Eurex supports initiatives that address concerns about panel-based indices.

***Question 3: General principles for benchmarks***

***Do you agree with the principles cited in this section? Would you add or change any of the principles?***

Although Eurex is mainly a user of indices, certain elementary aspects are clarified:

- Clearly, the Neutral Index Provider, as described above, or regulated markets offering index-based products for transparent and organized trading serve the entire market in an unbiased and transparent way.

- As such, regulated markets lean towards transparency in methodology and composition of indices. The information should be made fully transparent to regulators and license users. However, not all elements should be published to the general public, due to IP rights.
- In regards to the methodology we motivate to extend the wording that the underlying not only should be 'liquid', as proposed in the consultation, but 'should be representative and sufficiently liquid for the respective market'.

**Question 8: Principles for users of benchmarks**

**Do you agree with the principles cited in this section? Would you add or change any of the principles?**

As a provider of listed derivatives, Eurex constantly seeks to offer products from various asset classes for its customers. Together with market participants and Neutral Index Providers, the methodology, suitability and reliability of indices, which are already used as underlying or are considered for listing, is discussed in an ongoing dialogue. Derivatives products based on indices and designed for trading at regulated markets need to be approved by the competent authority, before listing these on the regulated market.

Moreover, along with derivatives listing, there are also contingency plans and fallback scenarios for Eurex and its clearing house Eurex Clearing to have alternative price determination in place, in case index unavailability is prevalent. Regulated markets are obliged to offer fair and orderly markets and therefore this aspect is a key element.

**Question 10: Continuity of benchmarks**

**Which principles/criteria would you consider necessary to be established for the continuity of benchmarks in case of a change to the framework?**

Changes to benchmarks can have significant impact on the value of financial products based on the benchmark and practical and risk implications. Therefore, any change of the framework should be communicated and discussed with the benchmark users such as a regulated market, if possible. For a regulated derivatives market it is important to have sufficient lead-time to react to changes due to the longer-term nature of derivatives contracts of currently up to 10 years. Therefore, derivatives exchanges and CCPs clearing derivatives might need to continue the old calculation method longer due to outstanding positions. If the benchmark should not be continued, these types of users should be granted a right to use the former index methodology until the last position is closed, given the underlying market is still tradable and accessible.

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