February 8, 2013

Comments on the International Organization of Securities Commissions'
Consultative Report on Financial Benchmarks

Japanese Bankers Association

We, the Japanese Bankers Association ("JBA"), would like to express our gratitude for this opportunity to comment on the *Consultative Report on Financial Benchmarks*, released on January 11, 2013 by the International Organization of Securities Commissions ("IOSCO").

We hope that our comments below will be of assistance as you work towards finalizing the Report.

<General comment>

In light of the policy objectives set in response to the attempted manipulation of interest rate benchmarks, in particular involving LIBOR, which aim to enhance the credibility and transparency of financial benchmarks (Benchmarks) and to ensure clear governance and accountability arrangements, recommendations on Benchmarks provided in the Consultation Report would contribute to the enhancement of credibility and transparency of Benchmarks in many aspects, and are important drivers for increasing transparency of not only Benchmarks but also the financial services that use such Benchmarks.

The discussion on the role of Benchmarks and their appropriate supervision requires a renewed understanding/clarification of the role Benchmarks play in financial markets. Various Benchmarks have been created to improve the usefulness of financial markets to accommodate needs of wider-ranging market participants, including financial institutions as well as borrowers and investors. Of these Benchmarks, those which fit into users' needs have been selected and employed through a trial use and survived competition, these have contributed to the extensive development of the financial markets. In view of this Benchmark development, our candid opinion is that most of the discussions on the role of Benchmarks and appropriate supervision in the Consultation Report should be made taking into account various aspects of the Benchmarks. We therefore fully support the perspective "that a one-size-fits-all approach may not be appropriate for the universe of Benchmarks", as noted in the Consultation Report.

A point which deserves particular attention is that the Consultation Report discusses some issues within the same framework for Benchmarks complied in markets for exchange-traded transactions or where the mechanism of quoted announcement is well developed, and those complied in markets for off-exchange over-the-counter transactions. However, differences in an environment in which respective Benchmarks are operating, such as differences in monetary policies and economic environment and the legal system in each jurisdiction, should also be taken into account in such discussions. Furthermore, there are concerns that standardised regulations and excessive intervention by authorities may inhibit innovation in the financial markets, including the creation of new Benchmarks, as well as that standardised regulations may increase the

cost of Benchmark calculation.

Also, if expert judgment is reasonably justified under adequate mechanisms, submitted rates based on such expert judgment could be deemed as a “bona-fide” rate.

While Benchmarks vary depending on their nature and stage of development, it is requested to fully publicize the purpose of announcing Benchmarks, their characteristics, and limitations under certain conditions, to ensure common understating among Administrators, Submitters and users of the Benchmarks.

<Specific comments>

(Q1) Agreed.

(Q2) Agreed.

(Q3) The approach requiring Submitters to comply with the code of conduct developed by Administrators, and to monitor the compliance is considered to be more realistic than to require Administrators to verify the integrity of all information and data used in the submission process.

If Benchmarks are based on market rates, a process should be developed that enables Submitters to subsequently justify their submitted rates (prices). In addition, although an increase in the number of Submitters should be considered as one measure to increase the credibility of Benchmarks, the vulnerability may still be difficult to reduce in certain cases. At any rate, it is considered desirable to maintain the number of Submitters at a level which is appropriate for the market size.

(Q4) Our opinion is that Submitters should develop a framework that enables them to subsequently justify their submitted rates (prices) to ensure the integrity of information/data provided to Administrators. Such a framework should comply with the code of conduct set by Administrators.

Further, Submitters may, in some cases, need to present other relevant data as necessary at the request of Administrators.

(Q5) The required level of transparency with regard to Benchmarks would vary depending on who the users are and the intended use. In general, Benchmarks are publicly announced and neither Submitters nor Administrators can completely identify who use Benchmarks or for what purpose. As such, it is considered necessary for Administrator to extensively disclose the code of conduct for both Submitters and Administrators in order for wide-ranging users to understand the governance framework and Benchmark calculation process in place.

(Q6) In terms of publishing Benchmarks, Administrators should specify cases where Benchmarks will not be published, for example due to the setting of the minimum required number of data points

and unexpected disruption in the financial markets.

On the other hand, there may also be a situation where certain factors on the Administrators' side may preclude a public announcement. To address such an issue, it is considered advisable for users to make other arrangements by way of those set forth, for example, in the ISDA Master Agreement.

However, how Benchmarks are published may depend on their definition and usage, uniform discussions on this issue may not be appropriate.

(Q7) With respect to procedures pertaining to a definition change, we believe that Administrators and other relevant parties should first discuss such changes, and then certain actions should be undertaken, for example inviting public comments from market participants such as users and Submitters. Also a transition period should be set.

(Q8) Our basic position on the definition change is that such a change should be avoided as much as possible, given that Administrators cannot fully identify users or the object of the use, and the definition change may have an extensive impact on the markets. However, if in a certain circumstance, for example where the market on which Benchmarks rely changes significantly, a definition change may need to be considered

On the other hand a periodic review of Benchmark submission procedures is considered to be appropriate as this would contribute to an improvement in the credibility and the usefulness of Benchmarks, for example the strengthening of a governance framework, while giving consideration to the burden such a change may impose on Submitters. In conducting such a review, it is desirable to undertake a thorough analysis of whether there is any impact on users, and the magnitude of such impact, if any.

(Q9) No comment provided.

(Q10) The establishment of the Administrator's oversight committee is considered to be effective for improving the governance of Administrators and ensuring the transparency of Benchmarks, but the necessity of establishing such a committee should be determined considering the stage of development of each Benchmark and the intended use of the Benchmark. As such, the introduction of a standardised requirement should be avoided so as not to impair financial innovation, for example the creation of new Benchmarks.

Also, the level of independent authority on the oversight committee or other body should not be defined uniformly, and it is desirable for each entity that publishes a Benchmark to set such authority based on the characteristics of the relevant Benchmarks.

Careful attention needs to be paid to ensure that recommendations made by the oversight committee or other body will not lead submitted rates (prices) to converge to a certain level.

(Q11) We agree that they should establish accountability procedures to assess their compliance with operational standards and scrutiny of Benchmark submissions.

(Q12) The measures discussed in the Consultation Report are considered to be sufficient, given that Submitters are subject to regulatory supervision by local supervisors even if Benchmarks are not regulated.

In terms of the discussion on introducing the requirement for an external audit, we are of the opinion that further discussions need to be had on: (1) the balance between the benefit arising from an increase in the credibility that would come from a check by an independent third party and the challenge associated with selecting a party to conduct such an independent audit; and (2) the need for agreement to be reached between Administrators and Submitters on costs and cost sharing.

(Q13) The frequency, audit scope, and granularity of internal audit should be determined on a risk basis, instead of uniformly discussing “frequency” only. An audit should be conducted within the scope and at the frequency that Administrators consider appropriate for each Benchmark to verify the appropriateness of the rate-submission-related framework/processes and their operating effectiveness.

Furthermore, rather than selecting to conduct either an internal or external audit, an appropriate combination of internal and external audits, as well as appropriate methodologies, should be determined, considering the stage of development of a Benchmark and the intended use of the Benchmark.

Internal audit is conducted by personnel familiar with Benchmark-related practice, while external audit is performed by an independent external party, and hence these audits mutually serve as a complementary function. In light of such understanding, an issue that the required level of external audit may depend on an environment under which Benchmarks are operating should be assessed in considering the introduction of external audit.

(Q14) The measures discussed in the Consultation Report are considered to be sufficiently effective.

(Q15) The frequency, audit scope, and granularity of internal audit should be determined on a risk basis, instead of uniformly discussing “frequency” only. An audit should be conducted within the scope and at the frequency that Administrators consider appropriate for each Benchmark to verify the appropriateness of the rate-submission-related framework/processes and their operating effectiveness.

In terms of the discussion on introducing the requirement for an external audit, we are of the opinion that further discussions need to be had on: (1) the balance between the benefit arising from an increase in the credibility that would come from a check by an independent third party and the challenge associated with selecting a party to conduct such an independent audit; and (2) the need for agreement to be reached between Administrators and Submitters on costs and cost sharing.

(Q16) It is considered that public self-certification would be sufficiently effective if an industry standard recognized by a third party is set.

(Q17) We consider that the measures discussed are effective. However, it is not appropriate to uniformly apply these measures to all Benchmarks. The selection of the measures provided for each Benchmark should be left to each Submitter.

(Q18) It is considered that transactions, committed quotes and expert judgment are merely a difference in the definition, and do not directly affect the level of creditability. The selection of input types may also be dependent on which Benchmarks Administrators intends to publicly announce, and how users understand the Benchmark.

The code of conduct is based on the definition of such Benchmarks, and is intended to ensure an appropriate rate submission. The code of conduct would not necessarily be different even if the reference data for Submitters differs (for example, transactions, committed quotes, and expert judgment).

Regardless of the type of input, retention of evidence is considered to be crucial to enable subsequent review.

(Q19) The advantage is the increased creditability of Benchmarks from improved governance and the strengthening of enforcement, while the disadvantage includes increased costs for addressing the regulations and a reduction in the number of Submitters.

(Q20) The advantage is the increased creditability of Benchmarks from improved governance and the strengthening of enforcement, while the disadvantages include a loss of adequate price discovery due to the increased cost of addressing the regulations, and reducing financial market innovation.

(Q21) We agree on the distinction between Benchmarks which have an extensive impact on domestic and foreign markets and those only having a limited impact.

(Q22) No comments provided.

(Q23) No comments provided.

(Q24) No comments provided.

(Q25) No comments provided.

(Q26) We have no particular comments on the type of code of conduct (whether a voluntary code of conduct, an industry code of conduct submitted to and approved by a relevant Regulatory Authority, a code of conduct developed by IOSCO etc). However, the determination of which code of conduct to apply should be made on a benchmark-by-benchmark basis.

(Q27) We consider that the discussion on the creation of a Self-Regulatory Organisation needs to factor in circumstances specific to each jurisdiction, and the necessity of such an organisation should be

considered based on this assessment.

We do not think that the creation of a Self-Regulatory Organization is the only approach to solve all issues, although it is understood that this would strengthen certain aspects of Benchmark governance. External environmental factors, such as the role of Benchmarks and initiatives to enhance the creditability of Benchmarks, varies across jurisdictions, and therefore the assessment of whether costs are reasonable and identifying alternative risk mitigants, etc. would need to be made on a benchmark-by-benchmark basis.

(Q28) Submitters' compliance with a code of conduct is crucial for Administrators. However, whether such a compliance obligation should be imposed only based on the authorities of the supervisors should be determined on a case-by-case basis, taking into account the nature and materiality of Benchmarks.

(Q29) First, who are the users need to be defined. As users are not necessarily "bona-fide", the qualification of users needs to be verified to some extent.

After defining the "users", the consideration on whether users who do not benefit from an excessive performance-fee based program should participate in discussions on how to increase the quality of Benchmarks, along with Administrators, is considered to be beneficial. In that case, it is preferred to discuss with Submitters and Administrators the Benchmark-setting and governance approaches they deem appropriate.

(Q30) Although it is understood that observable transactions provide one of significant evidences of submitted rates, it is considered important that the extent of use and approaches to be applied be determined by fully factoring in the definition, nature, development status and intended use of Benchmarks, rather than be uniformly determined.

With respect to the treatment of Benchmarks not anchored by actual observable transactions under market stress, an approach whereby Administrators provide certain criteria, and each Submitter retains evidence of rate submissions in accordance with such criteria, is considered to be appropriate.

(Q31) In OTC markets, "observable transactional data" is limited, and could not be deemed as "only criterion". The treatment of "observable transactional data" should also consider the definition of the Benchmarks, etc. The key consideration is whether a benchmark is accepted and used by market participants. Hence, if a Benchmark is accepted and used, such a benchmark could be construed as having certain value in the market.

(Q32) The existence of Benchmarks may contribute to the maintenance and increase of market liquidity in a developing market or a market with a temporary reduction in liquidity, and hence the intended use and significance would vary by benchmark.

(Q33) As a result of comparing between a market with high liquidity and a market with low liquidity, or between a developed market and a developing market, the weight of information contained in one actual transaction should not be considered the same. Under a market stress, some transactions may be executed at an exceptional price due to unusual reasons (e.g. loss-cut) attributable to a minority of participants. A number of participants do not deem such a price as prevailing. In such a case, actual transactions should not be deemed as only information representative of a prevailing market.

We have no objection to the opinion that an actual transaction is one of the critical elements used for justifying submitted rates (prices). However, it is presumed that certain monetary policies, such as quantitative easing policies, may lead to an evaporation of a "surface" liquidity, which is representative of actual transactions, within the markets over time. Under such a situation, information other than actual transactions will become more remarkable. Should the governance over the rates (prices) be provided and the submissions process effectively function, information other than actual transactions data (e.g. committed quotes and expert judgment based on market inputs) could be used as "bona-fide" information.

(Q34) No comments provided.

(Q35) Although Benchmarks vary in their definition (such as, actual transactions, committed quotes, and expert judgment based on market inputs), taking into account that Benchmarks are representative of actual market conditions, Administrators, Submitters and users should assume that Benchmarks have the same characteristics of being prone to a deterioration in their function or a sharp rise in their variability (in particular, in cases of actual transactions) under market stress. Particularly, it is considered desirable for users to make specific arrangements in order to address market stress.

(Q36) When a "living will" is set, measures to eliminate participants that would benefit from triggering the "living will" and ensure a minimal impact on existing Benchmark users should be considered.

(Q37) This would need to be primarily discussed by users. In light of varying needs of jurisdictions, fair and open discussions on alternate benchmarks with the existing Administrators, Administrator candidates for alternate Benchmarks, and Submitters need to be made.

(Q38) We have no particular comment. However, as Benchmarks are diverse, prioritisation reflecting the characteristics of each benchmark identified would need to be considered.

(Q39) It is understood that the transition between market Benchmarks will be generally carried out at the discretion of each party. Based on this, it is considered necessary to set a sufficient period to notify all stakeholders of legacy Benchmarks (such as holders of relevant financial instruments and relevant exchanges).

(Q40) We have no particular comments on the transition between Benchmarks as it is understood that the transition will generally be carried out at the discretion of each party.

However, we strongly request the existing Benchmark Administrators to take the following two actions: (a) fully notify potentiality of profit/loss volatility that may incur on holders of legacy Benchmark linked financial instruments; and (b) include the clause regarding a settlement method in cases where Benchmarks are not calculated.

(Q41) We have no particular comment as situations would differ depending on the characteristics of Benchmarks. However, as a general point, any of the options is believed to be significant, but the determination on the timeframe would need to be made in consideration of any legal risk, such as the risk of a lawsuit filed by an existing contractor.