

# **Powers in relation to LIBOR contributions**

**Consultation Paper**

CP17/15\*\*

June 2017

## How to respond

We are asking for comments on this Consultation Paper (CP) by 12 August 2017.

You can send them to us using the form on our website at: [www.fca.org.uk/cp17-15-response-form](http://www.fca.org.uk/cp17-15-response-form).

Or in writing to:  
Richard Grafen  
Markets Policy Department  
Financial Conduct Authority  
25 The North Colonnade  
Canary Wharf  
London E14 5HS

**Telephone:**  
020 7066 7018

**Email:**  
[cp17-15@fca.org.uk](mailto:cp17-15@fca.org.uk)

### How to navigate this document onscreen



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takes you to helpful abbreviations

## Contents

<b>1</b>	Summary	3
<b>2</b>	LIBOR and the FCA's approach	6
<b>3</b>	Defining the market	8
<b>4</b>	Establishing a list of candidate banks	10
<b>5</b>	Compulsion under existing UK law	14
<b>6</b>	Critical benchmarks under the EU Benchmarks Regulation	15
<b>Annex 1</b>		
	List of questions	17
<b>Annex 2</b>		
	Cost benefit analysis	18
<b>Annex 3</b>		
	Compatibility statement	21
<b>Annex 4</b>		
	Abbreviations used in this paper	24
<b>Appendix 1</b>		
	Draft Handbook text	25

# 1 Summary

## Introduction

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- 1.1** The London Interbank Offered Rate (LIBOR) is a systemically important benchmark underpinning transactions in many different markets worldwide, with an aggregate outstanding nominal amount estimated by the Financial Stability Board in 2014 as US\$220 trillion.<sup>1</sup> Its reliability and accuracy are very important to market integrity, in the UK and globally.
- 1.2** LIBOR is based on input data that is contributed by banks. We have power to require banks to contribute, if necessary, under the Financial Services and Markets Act 2000 (FSMA), and will have new powers to require contributions under the EU Benchmarks Regulation (BMR)<sup>2</sup> when the European Commission (the Commission) designates LIBOR as a 'critical' benchmark, potentially later this year, or when the BMR applies in full in 2018.
- 1.3** We are therefore reviewing the way in which we would use our compulsion powers should that be necessary, and this Consultation Paper (CP) sets out our proposed approach and seeks your views on it.

## Who does this consultation affect?

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- 1.4** This consultation most directly affects banks that are current or potential submitters to LIBOR, and the administrator of LIBOR, ICE Benchmark Administration Limited (IBA). You may also be indirectly affected if you use LIBOR, for example, in hedging products or loan agreements.

## Is this of interest to consumers?

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- 1.5** The procedures discussed in this CP will not directly involve retail consumers, but LIBOR is used in many financial products including, for example, loan agreements and investment funds. Retail consumers may, therefore, have an interest in the quality of LIBOR as a benchmark.

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1 'Reforming Major Interest Rate Benchmarks', Financial Stability Board, 22 July 2014, [www.fsb.org/wp-content/uploads/r\\_140722.pdf](http://www.fsb.org/wp-content/uploads/r_140722.pdf)  
2 'Regulation (EU) 2016/1011 of the European Parliament and of the Council of 8 June 2016' (OJ L171, 29.06.16, p.1 [eur-lex.europa.eu/legal-content/en/TXT/?uri=CELEX:32016R1011](http://eur-lex.europa.eu/legal-content/en/TXT/?uri=CELEX:32016R1011))



## Context

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- 1.6** The Financial Services Authority (FSA) consulted on the regulation and supervision of benchmarks in December 2012.<sup>3</sup> This included a discussion of compulsion powers. We have powers to compel contributions to LIBOR under FSMA through our own initiative powers in s.55L, or by making a rule under s.137A and s.137F.
- 1.7** Our compulsion powers will however, change when the Commission designates LIBOR as critical under the BMR. The FSMA power will at that point be replaced by the BMR power in Article 23 in relation to contributors to which the BMR applies. The BMR power is subject to specific requirements, and so we are reviewing the way in which we would identify the banks to compel if that proved necessary. Our policy would be to use the FSMA power, if necessary, in a way that takes into account the BMR power.
- 1.8** The European Securities and Markets Authority (ESMA) published a methodological framework on 2 June to promote convergence in relation to the selection of which firms should be required to contribute to critical benchmarks.<sup>4</sup> That framework constitutes guidance that is not legally binding. In line with paragraph 10 of the framework, our proposals are intended to represent an application of this framework, adapted where necessary to reflect the particular nature and circumstances of LIBOR. If we were to use our compulsion powers under the BMR, we would have to select the appropriate contributors with the close cooperation of their competent authorities, and we would have to make any decision to compel in consultation with the LIBOR 'college' – a group of regulators defined in Article 46 of the BMR, including ESMA and at least the national regulators of all the banks contributing to LIBOR. In addition to Article 23, the proposals in this CP also take account of other BMR requirements where relevant, including Annex 1 to the BMR.
- 1.9** Under the BMR power, one of the tests for compulsion is a firm's 'actual and potential participation in the market that [LIBOR] intends to measure.'

## Purpose of consultation

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- 1.10** The purpose of this consultation is to explain and to seek views on a proposed way in which we would require banks to contribute to LIBOR, should it prove necessary to do so, that is compatible with the changes that will occur once LIBOR becomes a Critical Benchmark under the BMR.
- 1.11** In particular, we are seeking views on:
- our general approach to the use of powers to require contributions, should that prove necessary
  - proposals for the way we would establish the population of banks to compel, including:
    - defining the market for this purpose
    - specifics of transaction types, participants, funding centres

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3 'CP12/36: The regulation and supervision of benchmarks', Financial Services Authority, December 2012, [www.fca.org.uk/publication/consultation/cp12-36.pdf](http://www.fca.org.uk/publication/consultation/cp12-36.pdf)

4 'Methodological framework: Selection of supervised entities for mandatory contribution under Article 23(7) BMR', ESMA, 2 June 2017, [www.esma.europa.eu/sites/default/files/library/esma70-143-5\\_methodological\\_framework\\_bmr.pdf](http://www.esma.europa.eu/sites/default/files/library/esma70-143-5_methodological_framework_bmr.pdf)

- relevant data other than transaction data
- a draft rule that we could use if we needed to compel banks under domestic UK law

**1.12** The proposals are not intended to deal with what we would do if we saw a need to take urgent action, before the BMR applies, to compel a bank that is currently a member of the LIBOR panel to continue contributing. In these circumstances, we can also use our own initiative powers to compel continued submission under s.55L of FSMA. See Chapter 5 for further detail.

**1.13** We are aware that IBA is currently implementing reforms to LIBOR. As explained in Chapter 2, the current proposals take LIBOR as it will be when the current first phase of reforms are complete as its starting point. If any further changes to LIBOR were introduced before the date on which we needed to use our compulsion powers we would use an approach similar to the one set out here, but adapted it to take account of the changes.

## Equality and diversity considerations

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**1.14** We have considered the equality and diversity issues that may arise from the proposals in this CP.

**1.15** Overall, we do not consider that the proposals in this CP adversely impact any of the groups with protected characteristics, i.e. age, disability, sex, marriage or civil partnership, pregnancy and maternity, race, religion and belief, sexual orientation and gender reassignment.

**1.16** We will continue to consider the equality and diversity implications of the proposals during the consultation period, and will revisit them when publishing the final rules.

**1.17** In the meantime, we welcome any input to this consultation on such matters.

## Next steps

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**1.18** We want to know what you think of our proposals. We ask questions throughout this CP which are also collated in Annex 1. Please send us your comments by 12 August using the online response form on our website or by writing to us at the address on page 2.

**1.19** We will consider your feedback and aim to publish a summary of responses and a Policy Statement in September 2017. We may include a revised version of the draft rule, but we do not plan to make the rule except in circumstances where we think it is necessary to do so.

**1.20** In parallel with this consultation, we are gathering the data proposed in Chapter 4 that will improve our knowledge of the market and the participants in it, and that could be used to inform compulsion decisions. We may undertake a further data-gathering exercise if the criteria in this CP change significantly following the consultation.

**1.21** We will be consulting separately, in the next few months, on changes to the Handbook that will be required before the BMR applies in full on 1 January 2018.



## 2 LIBOR and the FCA's approach

- 2.1** IBA publishes LIBOR rates daily in five currencies (pounds (GBP), US dollars (USD), Euro (EUR), Japanese yen (JPY) and Swiss Franc (CHF)) and seven tenors, from overnight to 12-month. LIBOR is calculated by IBA on the basis of submissions provided by a panel of banks that submit rates each day. These submissions are currently based on a mixture of transactional and market data and expert judgement by the banks.
- 2.2** IBA has published plans to develop LIBOR to improve its robustness and stability<sup>5</sup>, which it has grouped into two phases. IBA and the panel banks are currently preparing for the transition to phase 1. Our detailed proposals below are based on the phase 1 definition and methodology for LIBOR. If, at the time we use our powers, there have been other developments in the way LIBOR is composed, we would adapt our approach to compulsion in an appropriate manner while using a similar overall approach.
- 2.3** We have been regulating IBA since it took over as LIBOR administrator in January 2014 and the panel banks as submitters since April 2013.
- 2.4** We currently have powers to compel banks to contribute to LIBOR either through requirements imposed under the use of our own initiative powers under s.55L of FSMA or through our rule-making powers under s.137A and s.137F of FSMA.
- 2.5** When LIBOR is designated as a critical benchmark under the BMR, by the Commission, the BMR will apply in respect of LIBOR and in some respects replace the UK's existing legislation. The power to require supervised entities to contribute input data to LIBOR will apply in relation to firms which are subject to the BMR. The remainder of the provisions in the BMR will apply to the IBA and LIBOR, as to other administrators and benchmarks, from 1 January 2018.

### Our approach to using compulsion powers

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- 2.6** We will intervene by using compulsion powers to protect the representativeness of LIBOR if it is necessary for market integrity or consumer protection, and in accordance with the BMR where applicable. We recognise the potential costs associated with contributing to LIBOR and would, therefore, seek to use compulsion powers only where it would be appropriate to ensure market integrity or consumer protection. We would not envisage supporting LIBOR by using compulsion powers indefinitely.
- 2.7** A key consideration in whether and for how long the continuation of LIBOR is essential for market integrity will be the availability of credible alternative interest rate benchmarks, particularly the risk-free rates on which work is under way in relation to many currencies in response to the recommendations in the Financial Stability Board's report.<sup>6</sup>

<sup>5</sup> 'Summary of ICE LIBOR evolution', ICE Benchmark Administration, 24 January 2017, [www.theice.com/publicdocs/LIBOR\\_evo\\_summary.pdf](http://www.theice.com/publicdocs/LIBOR_evo_summary.pdf), contains links to previous position statements and papers

<sup>6</sup> See footnote 1

- 2.8** We would not expect to use compulsion powers to increase the number of contributors significantly above its current level. We would also consider limiting compulsion to fewer than all seven of the tenors.
- 2.9** Any bank that was required to contribute to a currency panel for the first time would need to invest in its capacity to make contributions in accordance with the LIBOR code of conduct and the applicable law. We are interested in your views about the time and costs that would be necessary to establish a unit capable of contributing LIBOR submissions based on transactions, and submissions based on expert judgement, including on any difference in the time and costs required.
- Q1:** **What time and costs do you think would be required for a new bank to prepare itself for contributing to LIBOR for transactions-based submissions and for expert judgement based submissions?**
- Q2:** **Do you have any comments on our general approach to the use of compulsion powers in relation to LIBOR?**



## 3 Defining the market

- 3.1** Under the UK powers, there are no prescribed criteria for who can be compelled to contribute, but we are proposing that we should identify the appropriate banks to compel in a way that should, so far as possible, take account of the regime that will apply once LIBOR is designated as a critical benchmark. Under the BMR, compulsion of contributors to a critical benchmark must be based upon their actual and potential participation in the market that the benchmark intends to measure.
- 3.2** For the participation test, therefore, we need to start by measuring the relevant market. We have taken the description of the benchmark given by its administrator, IBA, as our starting point for that. As explained in Chapter 2, we are using IBA's phase 1 description.
- 3.3** IBA published a 'Roadmap for ICE LIBOR' in March 2016.<sup>7</sup> This discussed existing approaches to defining LIBOR and proposed replacing them with the ICE LIBOR 'Output Statement'. They published a summary of the evolution process on 24 January 2017.<sup>8</sup> The Output Statement describes the benchmark as 'a wholesale funding rate anchored in LIBOR panel banks' unsecured wholesale transactions to the greatest extent possible...' It then outlines a 'waterfall' approach to submissions to enable the rate to be published in all market circumstances. This starts with a 'volume weighted average price (VWAP) of transactions in unsecured deposits and primary issuances of commercial paper and certificates of deposit since the previous submission, with a higher weighting for transactions booked closer to 11:00 London time.'
- 3.4** Any bank has the capacity to raise unsecured wholesale funding, and to that extent all banks are potential participants in the wholesale funding market. However, the extent to which banks are active in this market differs, and in order to ensure a proportionate approach is taken, we have further defined the population of banks from which contributors could be chosen. It is an important characteristic of LIBOR that it is based on contributions from banks of a particular quality, specifically the quality of the existing panel banks. We cannot limit potential contributors to those existing banks, but we need to define the population of banks from which contributors could be drawn that would maintain the nature of LIBOR.
- 3.5** We recognise that a significant proportion of wholesale loan transactions in non-EU LIBOR currencies is likely to take place in the relevant jurisdictions (i.e. US dollar transactions in the United States, yen transactions in Japan, and Swiss franc transactions in Switzerland). Neither the BMR nor FSMA provides a power to compel legal entities that have no presence in the EU to make LIBOR contributions. Where, however, an entity with a presence in the EU also conducts relevant transactions outside the EU but in one of the funding centres currently eligible under IBA's rules, this activity is potentially part of the relevant market. Even if the activity is conducted by another group entity, the inclusion of these transactions is likely to increase the robustness of the benchmark.

<sup>7</sup> 'Roadmap for ICE LIBOR', ICE Benchmark Administration, 18 March 2016, [www.theice.com/publicdocs/ICE\\_LIBOR\\_Roadmap0316.pdf](http://www.theice.com/publicdocs/ICE_LIBOR_Roadmap0316.pdf)

<sup>8</sup> See footnote 5



- 3.6** To avoid changing the nature of LIBOR, we think we should select banks of a similar quality to the existing panel banks. Therefore, we propose to include, within the scope of the participation test, only those banks that are of similar size and credit quality to the existing panel banks, and that have a presence in the United Kingdom.
- 3.7** We, therefore, propose to define our market for the purpose of the participation test as 'the interbank and corporate unsecured wholesale funding market for GBP, USD, EUR, CHF and JPY involving large banks that have good credit quality and a presence in the United Kingdom'.
- 3.8** The next chapter sets out the specific data we think would best enable us to identify these banks and to apply the participation test.

**Q3: Do you have any comments on the description of the market we would propose to use for the BMR participation test in relation to LIBOR?**



## 4 Establishing a list of candidate banks

- 4.1** In order to apply the participation test, we would need to measure actual and potential participation in the interbank and corporate unsecured wholesale funding market for GBP, USD, EUR, CHF and JPY involving large banks that have good credit quality and a presence in the United Kingdom.
- 4.2** This involves preselecting the banks that fit the three limbs of the description, and using measures of actual and potential participation. The pre-selection criteria definitions and the participation measures we propose to use are explained below.
- 4.3** Three pre-selection criteria will determine the population of banks from whom we seek further data. We will then need to use the data measuring actual and potential participation to produce a ranking of the most appropriate banks to be on the panel.
- 4.4** If there are sufficient transactions in the defined market for one or more of the currencies, it might be possible to construct a panel based only on actual transactions. On the basis of the number of transactions that the existing panel banks have, however, we think that there will be at least some currencies where we will need also to use data showing evidence of potential participation.
- 4.5** We are not, at present, in a position to reach final decisions on the most appropriate methodology. In the light of the CP responses, we will reach final decisions on the pre-selection criteria and on the proposed measures of actual and potential participation. And we should be able to form a better view of the market and its participants once we have assessed the data quality and gained a more accurate picture of transaction volumes. Once we have completed those processes, we will be able to reach final decisions on the most appropriate methodology for combining the data we receive.
- 4.6** We would expect to use a 'scorecard' method, normalising the scores against each measure of actual or potential participation, weighting them and then combining them to produce an overall score for each bank.

### Pre-selection criteria

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- 4.7** The three criteria we propose to use are:
- **Presence in the United Kingdom** – we will use the Bank of England's list<sup>9</sup> of banks and building societies that have a deposit-taking permission.
  - **Credit quality** – we will look at various publicly available indicators of short-term credit quality and include only those banks comparable with the existing panel banks, meaning that their issued debt should be investment grade.

<sup>9</sup> 'Banks and Building Societies Lists', Bank of England, Prudential Regulation Authority, [www.bankofengland.co.uk/pru/Pages/authorisations/banksbuildingsocietieslist.aspx](http://www.bankofengland.co.uk/pru/Pages/authorisations/banksbuildingsocietieslist.aspx)

- **Size** – measured by group-wide total assets. We will include only banks that are of similar size to the existing panel banks.

## Measuring actual participation

**4.8** Actual participation will be measured by the number and value of transactions in the market.

**4.9** For the detailed types of transactions, eligible funding centres and counterparty types, we propose to start from the criteria currently used by IBA for collecting data for LIBOR. We are using the set of transactions to which IBA and the panel banks are transitioning under phase 1 as the basis of a consistent approach across all panel banks, as set out in the following table. We propose to use transactions of all sizes, as these are part of participation in the relevant market, and we also propose to ask banks to separate out transactions greater than the thresholds currently used by IBA (USD 10m, GBP 10m, JPY 1,000m, CHF 10m, EUR 10m).

### Transactions to be included

Transaction types	Eligible funding centres	Counterparty types
<ul style="list-style-type: none"> <li>• unsecured deposits</li> <li>• commercial paper</li> <li>• certificates of deposit</li> </ul>	<ul style="list-style-type: none"> <li>• Australia</li> <li>• Canada</li> <li>• European Free Trade Association</li> <li>• EU</li> <li>• Hong Kong</li> <li>• Japan</li> <li>• Singapore</li> <li>• USA</li> </ul>	<ul style="list-style-type: none"> <li>• banks</li> <li>• central banks</li> <li>• government entities</li> <li>• financial institutions</li> <li>• sovereign wealth funds</li> <li>• supranational corporations</li> <li>• corporates – only transactions with maturities greater than 35 days</li> </ul>

**4.10** To avoid seasonal distortion, we propose to use data relating to the latest available 12-month period.

## Measuring potential participation

**4.11** We propose to use the following measures of potential participation:

- size of banking groups' assets
- participation in related markets
- lending and borrowing activity
- presence in the main jurisdiction of a currency



- 4.12** The size of banks will already have been used in the pre-selection to exclude small banks, but we think it should be included as a measure of actual and potential participation for two reasons: first, larger banks are more likely to have the potential to participate at scale in the market from existing resources; and second the burden of being required to contribute to LIBOR could impose a disproportionate cost on smaller banks.
- 4.13** Active participation in markets which are related to the wholesale money market may be a good indicator of a bank's potential ability to participate in that market. For example, a bank may not be active in the unsecured money market but, when making funding decisions, it would likely be assessing the costs and benefits of choosing a repo transaction over a deposit.
- 4.14** The related markets we propose to look at for each currency are the ones that are included by IBA in its phase 1 listing of information that can be used to inform expert judgement when there are not sufficient transactions. These are interest rate futures, forward rate agreements, interest rate swaps, floating rate notes, floating rate Certificates of Deposit, foreign exchange forwards and swaps, and repos.
- 4.15** The scale of a bank's lending and borrowing will give an indication of its knowledge and visibility of related lending markets, which will contribute to an assessment of its potential participation. For lending and borrowing, we propose to use the following measures: total debt, syndicated loans and business loans. The first two were used for this purpose in the FSA's consultation on LIBOR in 2012.
- 4.16** A bank that has a significant presence in the home jurisdiction of a currency is likely to have more knowledge of conditions in the currency's domestic market.

**Q4: Do you agree with the criteria we propose to use to identify banks to include in our population and the measures we propose to assess actual and potential participation in the market LIBOR intends to measure? Are there other criteria or measures that you would recommend using?**

## Data gathering

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- 4.17** It is difficult to decide on an appropriate weighting and ranking approach without a better understanding of the market and the indicators, so in parallel with this consultation we are gathering the data described above, as well as data on banks' exposure to LIBOR. We are writing to around 50 banks matching our pre-selection criteria. If we conclude from the responses to this CP that more data are needed to measure actual and potential participation, then we will seek further data. We may also undertake a further data-gathering exercise if the criteria in this CP change significantly following the consultation.

- 4.18** Collecting the data now will give us the opportunity to test our proposed approach with actual data. It would also reduce or eliminate the need for urgent requests for data that we would otherwise have to impose on banks if we had to use compulsion powers.
- 4.19** As well as ensuring that we would be prepared for the contingency of compelling banks under the BMR or by a FSMA rule, the data we gather will enable us to develop an improved understanding of the market underlying LIBOR, and the representativeness of the current panel banks.



## 5 Compulsion under existing UK law

- 5.1** If we find it necessary to compel banks to contribute to LIBOR before LIBOR is designated as a critical benchmark, we have the option of using our own initiative powers under s.55L of FSMA, or making a rule under s.137A or s.137F of FSMA.
- 5.2** Own initiative requirements are individually addressed to each firm affected and do not require consultation. Each case would be judged on its individual merits but this can be used to take urgent action where appropriate against one or more individual banks that wanted to stop contributing to LIBOR.
- 5.3** A rule would apply to a group or class of firms and generally requires prior consultation. An appropriately formulated rule would operate in a way more obviously similar to the BMR powers. The appendix to this CP, therefore, contains a draft rule for this purpose, on which we would be interested in your comments.
- 5.4** The approach taken is to create an obligation to provide benchmark submissions to LIBOR that applies to a set of banks specified in the rule. The rule specifies which currency rates each listed bank should contribute to and the date from which they should contribute.
- 5.5** The rule would come into effect as soon as it was made, though for any bank that was required to contribute for the first time, we would specify a date by which it must start contributing allowing time for it to develop the necessary systems. We would take responses to Question 1 into account in setting this period.
- 5.6** The obligation is further specified in terms of compliance with IBA's Code of Conduct for LIBOR. This should allow more flexibility for adaptation of requirements over time, than if the obligations were specified in detail in the rule itself.
- 5.7** We are consulting on a form of a rule in this CP, and if we were to use it we would select the banks to apply it to using the criteria developed through this CP. We would aim to give those banks an opportunity to make representations if we decided to make a rule. This might be through a further public consultation or by bilateral engagement with the banks affected.

**Q5: Do you have any comments on the draft rule in the appendix?**

## 6 Critical benchmarks under the EU Benchmarks Regulation

- 6.1** The BMR was published in the Official Journal on 29 June 2016 and took effect on the following day. Most of its provisions will apply from 1 January 2018, and we plan to consult separately, in the next few months, on the changes that are required to the Handbook.
- 6.2** A number of provisions of the BMR applied from 30 June 2016, including some of those on critical benchmarks. These enable the Commission to designate certain benchmarks as 'critical benchmarks' including any benchmark that is used as a reference for financial instruments or contracts or measuring the performance of investment funds, having a total value of at least €500 billion (under Article 20(1)(a) of the BMR). The BMR provisions that already apply also confer the power for a national competent authority to require administrators of critical benchmarks to continue issuing the rate and the power to require 'supervised entities' to contribute input data to a critical benchmark (Articles 21 and 23 of the BMR). Those powers may be exercised from the date on which the relevant benchmark is designated as critical.
- 6.3** So far, the only benchmark that the Commission has designated is Euribor. The Commission is expected to designate LIBOR as critical in due course. From the point at which the Commission designates LIBOR (or any UK benchmark) as critical, the compulsion powers under the BMR will apply to that benchmark (where that benchmark has contributors the majority of which are supervised entities).
- 6.4** For the purpose of this CP, the key change is that, for firms which fall within the scope of the BMR, our ability to require banks to contribute to LIBOR under FSMA will be replaced by the power under Article 23 of the BMR to require supervised entities to contribute input data to a critical benchmark.
- 6.5** The BMR is not explicit as to whether branches in the European Union (EU) of firms based outside the EU fall within the scope of the compulsion power in Article 23. We are considering that issue. To the extent that third country branches in the UK fall outside the scope of that power, then we consider that our existing domestic powers (to impose requirements on firms and to make rules) under FSMA could be used to require such branches to contribute to a critical benchmark (where appropriate).
- 6.6** Article 23 of the BMR provides that if a contributor that is a 'supervised entity' (i.e. a MiFID investment firm, bank or credit institution, or one of various other firms defined in sectoral EU legislation) notifies its benchmark administrator that it intends to cease contributing input data, the administrator and its competent authority should assess the implications for the capability of the benchmark to measure the underlying market or economic reality. In the meantime, the competent authority can require the contributor or contributors to keep contributing for up to four weeks.



**6.7** If, following the competent authority's assessment, it considers that 'the representativeness of the critical benchmark is put at risk', it has the power to require supervised entities to contribute for up to 12 months. That requirement can be extended by a further period of up to 12 months. For each compulsion decision, the competent authority of the administrator has to consult a college – a body composed of that competent authority, ESMA and at least the competent authorities of supervised entities that contribute to the benchmark.

**6.8** As noted in paragraph 3.1, the way in which the competent authority must choose the supervised entities that are to be compelled is defined in Article 23(7) of the BMR:

*'...on the basis of the size of the supervised entity's actual and potential participation in the market that the benchmark intends to measure.'*

And we have described above the way in which we should apply this to LIBOR, taking into account the ESMA methodological framework referred to in paragraph 1.8 above.

**6.9** In the event that we needed to compel under the BMR because one or more panel banks had notified us of their decision to stop contributing, we would be able to require those banks to keep contributing for four weeks in the first instance. If we thought it would be necessary to require any banks to continue contributing beyond four weeks, we would need to select banks for compulsion on the basis of their 'actual or potential participation in the market'.

**6.10** Applying this participation test is likely to require data that we do not currently have about banks, including banks that are not currently panel members. It would be challenging to collect the necessary data, to consult the college and to make compulsion decisions within four weeks. As explained in paragraph 4.17, we are, therefore, gathering data now in parallel to this consultation and may gather further data in the future. This should make it easier for us to carry out the relevant assessments, to select banks in a way compliant with the BMR, and to act within the timescales which apply to compulsion decisions under the BMR should the need arise.

**Q6: Do you have any comments on our proposal to use the approach described above if necessary to require firms specifically under the BMR powers?**



## Annex 1

### List of questions

- Q1:** What time and costs do you think would be required for a new bank to prepare itself for contributing to LIBOR for transactions-based submissions and for expert judgement based submissions?
- Q2:** Do you have any comments on our general approach to use of compulsion powers in relation to LIBOR?
- Q3:** Do you have any comments on the description of the market we would propose to use for the BMR participation test in relation to LIBOR?
- Q4:** Do you agree with the criteria we propose to use to identify banks to include in our population and the measures we propose to assess actual and potential participation in the market LIBOR intends to measure? Are there other criteria or measures that you would recommend using?
- Q5:** Do you have any comments on the draft Rule in the appendix?
- Q6:** Do you have any comments on our proposal to use the approach described above if necessary to require firms specifically under the BMR powers?



## Annex 2

# Cost benefit analysis

### Introduction

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1. S.138I of the FSMA requires us to perform a cost benefit analysis before consulting on rules and to publish the result, unless we consider the proposal will not give rise to any cost or to an increase in cost of minimal significance.
2. If used, the draft rule in Appendix 1 would require a number of banks to contribute to LIBOR. We would do this only if we considered that it was appropriate in order to ensure market integrity or consumer protection. We would decide at the time of using it which and how many banks should be included. This would impose costs on the banks affected, and we have estimated those below.
3. Overall, although the benefits of maintaining LIBOR for a period are difficult to quantify, given its global importance we believe that the benefits would outweigh the costs.
4. Most of the CP is about developing the way in which we propose to identify the banks to compel. This does not involve any changes to our rules or guidance, and so we are not required to carry out a cost benefit analysis under FSMA. We have, however, set out below what the main costs and benefits appear to be.

### Draft rule

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#### Costs

5. We have estimated the cost to a bank of contributing to LIBOR assuming that it contributes to all five currencies and all seven tenors using the current methodology. To the extent that a bank contributed to fewer currencies or fewer tenors, the cost would be reduced though not fully proportionately.
6. Table 1 shows our estimates of the costs for a LIBOR contributor. We estimate that ongoing staff costs for providing contributions would be around £1.8m a year, and this includes the individuals who make the submissions but also compliance staff, management oversight, internal audit and monitoring and surveillance. On top of that we estimate that there will be around £600k each year for IT and infrastructure. This gives a total ongoing cost of around £2.4m a year. The initial one-off cost to set up the IT and infrastructure we estimate at £3.5m, around half of which is for development, with smaller amounts for subject matter experts, business analysts, testing and project management.
7. These estimates are substantially higher than those contained in the Financial Services Authority's 2012 CP.<sup>10</sup> Our new estimates benefit from our experience since 2013 of supervising banks that are contributors to LIBOR.

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10 See footnote 3

8. We have asked in Question 1 of the CP for your estimates of the time and cost it would take to become a contributor to LIBOR.
9. The total cost imposed by a rule would depend upon the number of banks that we decided to compel, the number of currency rates to which each bank had to contribute, and how many of the banks were new contributors to LIBOR. It would also depend on the degree to which submissions based on expert judgement rather than transactions were required. We accept that expert judgement might require higher staff costs than transaction-based submissions.

**Table 1: Compliance costs for a LIBOR contributor**

Data unit	One-off costs	FTE	Ongoing costs
Submitters		4	700,000
Compliance		0.5	100,000
Management oversight		0.5	125,000
Internal Audit		1	200,000
Monitoring and surveillance		1	200,000
External Audit			500,000
IT & infrastructure			
Subject Matter Expert	281,250		
Business Analysis	187,500	0.5	125,000
Development	1,750,000		
Testing	750,000		
Support & Maintenance		2	250,000
Project Management	500,000	0.5	125,000
Market Data			100,000
<b>Total</b>	<b>3,468,750</b>		<b>2,425,000</b>

FCA estimates

## Benefits

10. As noted in paragraph 1.1 of the CP, the Financial Stability Board estimated the value of transactions linked to LIBOR in 2014 at US\$220 trillion. If there was a disorderly cessation of the rate or a sudden loss of market confidence in it, this would cause uncertainty about the pricing of an enormous quantity of financial assets held by banks. This in turn could generate uncertainty about the valuation of banks, and there could be concerns about potential losses. This would at the very least lead to higher costs of capital for banks, which would feed back into higher LIBOR rates. This would increase the costs of loans to firms and households.
11. Using the rule to ensure continuation of a representative rate would therefore avoid very significant economic disruption. It would allow some time for the development of and transition to alternative rates, and it would at least allow counterparties, if necessary, to renegotiate contracts in a more orderly way.



## Proposed method of identifying banks

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12. The proposed method for deciding which banks to compel is to gather data from the banks themselves, and, where available, central banks, about commercial banks' actual or potential participation in the relevant market, and other data, and to use the data to identify those that have the greatest actual and potential participation.
13. If we did not gather data in this way, we would have to select banks in a less structured way using data that was already available.

## Benefits

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14. The benefits of using the proposed method would be:
  - a. LIBOR being a more representative benchmark, compared with using other data, as contributors will be those with actual and potential participation in the market.
  - b. It would treat all banks equally based on their role in the market.

## Costs

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15. The added costs for FCA of the proposals would lie in managing the collection and analysis of new data, which will incur staff costs that will be greater than if we used other readily available data.
16. The additional external cost will be for the banks, which will have to provide the data.

## Annex 3

# Compatibility statement

1. This Annex records the FCA's compliance with a number of legal requirements applicable to the proposals in this consultation, including an explanation of the FCA's reasons for concluding that our proposals in this consultation are compatible with certain requirements under the Financial Services and Markets Act 2000 (FSMA).
2. When consulting on new rules, the FCA is required by section 138I(2)(d) of FSMA to include an explanation of why it believes making the proposed rules is (a) compatible with its general duty, under s.1B(1) of FSMA, so far as reasonably possible, to act in a way which is compatible with its strategic objective and advances one or more of its operational objectives, and (b) its general duty under s.1B(5)(a) of FSMA to have regard to the regulatory principles in s.3B of FSMA. The FCA is also required by s.138K(2) of FSMA to state its opinion on whether the proposed rules will have a significantly different impact on mutual societies as opposed to other authorised persons.
3. This Annex follows the requirements set out in s.138I of FSMA. When consulting on new rules, we are required by that section to include an explanation of why we consider the proposed rules are compatible with our strategic objective, advance one or more of our operational objectives, and have regard to the regulatory principles in s.3B of FSMA. We are also required by section s.138K(2) of FSMA to state our opinion on whether the proposed rules will have a significantly different impact on mutual societies as opposed to other authorised persons.
4. This Annex includes our assessment of the equality and diversity implications of these proposals.
5. Under the Legislative and Regulatory Reform Act 2006 (LRRRA) the FCA is subject to requirements to have regard to a number of high-level 'Principles' in the exercise of some of our regulatory functions and to have regard to a 'Regulators' Code' when determining general policies and principles and giving general guidance (but not when exercising other legislative functions like making rules). This Annex sets out how we have complied with requirements under the LRRRA.

### **The FCA's objectives and regulatory principles: Compatibility statement**

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6. The proposals set out in this consultation are primarily intended to advance the FCA's strategic objective of ensuring that relevant markets function well. They are also relevant for the FCA's consumer protection and integrity objectives.
7. We consider that the proposals in this CP are compatible with our strategic objective of ensuring that the relevant markets (set out in s.1F of FSMA) function well. This is because they are designed to clarify the way in which we would use powers in the directly applicable BMR, which seeks to ensure the accuracy and integrity of indices used as benchmarks and so to avoid failures in, or doubts about, benchmarks undermining market confidence. The proposals are, therefore, also intended to advance our operational objective of ensuring market integrity, by protecting and enhancing the soundness, stability and resilience of the UK's financial system, and the orderly operation of the financial markets.



8. Any disorderly cessation or loss of confidence in LIBOR would have an impact on consumers of the many financial products that use LIBOR. The approach proposed here would improve our ability to intervene in support of LIBOR, if that should prove necessary, and thereby advance our operational objective to secure an appropriate degree of protection for consumers.
9. We consider we are acting consistently with our duty under s.1B(4) of FSMA to, so far as compatible with the consumer protection objective or integrity objective, discharge our functions in a way which promotes effective competition in the interests of consumers.
10. In preparing the proposals set out in this consultation, the FCA has had regard to the regulatory principles set out in s.3B of FSMA. We explain that briefly below.  
**(a) The need to use the resources of each regulator in the most efficient and economic way:**
11. Given the systemic importance of LIBOR, we consider that it is appropriate to use FCA resources to develop proposals in this area. As is explained below, we would only seek to use our compulsion powers where it would be appropriate to ensure market integrity or consumer protection and in accordance with the BMR (where applicable).  
**(b) The principle that a burden or restriction should be proportionate to the benefits:**
12. We recognise the potential costs associated with contributing to LIBOR and would, therefore, seek to use compulsion powers only where it would be appropriate to ensure market integrity or consumer protection and in accordance with the BMR (where applicable). We would not envisage supporting LIBOR by using compulsion powers indefinitely.  
**(c) the desirability of sustainable growth in the economy of the United Kingdom in the medium or long term:**
13. LIBOR is a systemically important benchmark. The proposals should help promote sustainable growth in the in the economy of the United Kingdom in the medium or long term.  
**(d) the general principle that consumers should take responsibility for their decisions:**
14. Given the systemic importance of LIBOR, we do not consider that the proposals are inconsistent with this principle.  
**(e) the responsibilities of the senior management of persons subject to requirements imposed by or under FSMA, including those affecting consumers, in relation to compliance with those requirements:**
15. Aside from their existing obligations in relation to regulatory requirements, the proposals do not specifically affect the responsibilities of senior management.  
**(f) the desirability where appropriate of each regulator exercising its functions in a way that recognises differences in the nature of, and objectives of, businesses carried on by different persons (including different kinds of person such as mutual societies and other kinds of business organisation) subject to requirements imposed by or under FSMA:**
16. The proposed criteria are designed to take account of the differences between different types of firm.

**(g) the desirability in appropriate cases of each regulator publishing information relating to persons on whom requirements are imposed by or under FSMA, or requiring such persons to publish information, as a means of contributing to the advancement by each regulator of its objectives:**

17. As currently drafted, the draft rule, if made, would include a list of the firms subject to the rule.

**(h) the principle that the regulators should exercise their functions as transparently as possible:**

18. This consultation seeks to enhance the transparency of any exercise of our compulsion power by consulting on a proposed way in which we would require banks to contribute to LIBOR.

### **Expected effect on mutual societies**

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19. The FCA does not expect the proposals in this paper to have a significantly different impact on mutual societies.

### **Compatibility with the duty to promote effective competition in the interests of consumers**

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20. In preparing the proposals as set out in this consultation, we have had regard to the FCA's duty to promote effective competition in the interests of consumers.

### **Equality and diversity**

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21. We are required under the Equality Act 2010 to 'have due regard' to the need to eliminate discrimination and to promote equality of opportunity in carrying out our policies, services and functions. As part of this, we conduct an equality impact assessment to ensure that the equality and diversity implications of any new policy proposals are considered.
22. The outcome of the assessment in this case is stated in paragraphs 1.14 – 1.17 of the Consultation Paper.

### **Legislative and Regulatory Reform Act 2006 (LRR)**

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23. We have had regard to the principles in the LRR and the Regulators' Code for the parts of the proposals that consist of general policies, principles or guidance. In particular:
- by consulting we are developing the proposals in a way which is transparent and accountable;
  - the proposed criteria are intended to ensure firms would be selected in a proportionate and consistent way;
  - the proposals are intended to target action only where it is needed taking account of the level of risk and the importance of LIBOR.

## Annex 4

### Abbreviations used in this paper

<b>BMR</b>	Benchmarks Regulation (Regulation EU 2016/1011)
<b>CHF</b>	Swiss Franc
<b>CP</b>	Consultation Paper
<b>ESMA</b>	European Securities and Markets Authority
<b>EU</b>	European Union
<b>EUR</b>	Euro
<b>FSA</b>	Financial Services Authority
<b>FSMA</b>	Financial Services and Markets Act 2000
<b>GBP</b>	Pound Sterling
<b>IBA</b>	ICE Benchmark Administration Limited
<b>JPY</b>	Japanese Yen
<b>LIBOR</b>	London Interbank Offered Rate
<b>USD</b>	US Dollar

We have developed the policy in this Consultation Paper in the context of the existing UK and EU regulatory framework. The Government has made clear that it will continue to implement and apply EU law until the UK has left the EU. We will keep the proposals under review to assess whether any amendments may be required in the event of changes in the UK regulatory framework in the future.

We make all responses to formal consultation available for public inspection unless the respondent requests otherwise. We will not regard a standard confidentiality statement in an email message as a request for non-disclosure.

Despite this, we may be asked to disclose a confidential response under the Freedom of Information Act 2000. We may consult you if we receive such a request. Any decision we make not to disclose the response is reviewable by the Information Commissioner and the Information Rights Tribunal.

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# Appendix 1

## Draft Handbook text

## LIBOR BENCHMARK INSTRUMENT 2017

### Powers exercised

- A. The Financial Conduct Authority makes this instrument in the exercise of the following powers and related provisions in the Financial Services and Markets Act 2000 (“the Act”):
- (1) Section 137A (FCA’s general rules);
  - (2) Section 137F (Rules requiring participation in benchmark);
  - (3) Section 137T (General supplementary powers); and
  - (4) Section 139A (Power of the FCA to give guidance).
- B. The rule-making powers listed above are specified for the purpose of section 138G(2) (Rule-making instruments) of the Act.

### Commencement

- C. This instrument comes into force immediately.

### Amendments to the FCA Handbook

- D. The Glossary of definitions is amended in accordance with Annex A to this instrument, and the Market Conduct sourcebook (MAR) is amended in accordance with Annex B.

### Notes

- E. In Annex B to this instrument, the note (indicated by “**Note:**”) is included for the convenience of readers but does not form part of the legislative text.

### Citation

- F. This instrument may be cited as the LIBOR Benchmark Instrument 2017.

By order of the Board  
[date]

**Annex A****Amendments to the Glossary**

Insert the following definitions in the appropriate alphabetical position. The text is new and is not underlined.

<i>LIBOR</i>	the <i>specified benchmark</i> which is specified in paragraph 1 of Schedule 5 to the <i>Regulated Activities Order</i> , namely, the London Interbank Offered Rate, also known as LIBOR.
<i>LIBOR administrator</i>	the <i>benchmark administrator</i> in relation to <i>LIBOR</i> .
<i>LIBOR Code of Conduct</i>	the code of conduct (as amended from time to time) published by the <i>LIBOR administrator</i> which sets out the responsibilities of <i>benchmark submitters</i> in relation to <i>LIBOR</i> .

## Annex B

### Amendments to the Market Conduct sourcebook (MAR)

Amend MAR 8.1 (Application and purpose) as shown. New text is underlined.

## 8 Benchmarks

### 8.1 Application and purpose

Application

- 8.1.1 R (1) ~~This chapter applies~~ MAR 8.1 to MAR 8.3 apply to every *firm* which is a *benchmark submitter* or a *benchmark administrator*.
- (2) MAR 8.4 applies in accordance with the application provisions set out in that section.

...

Insert the following new chapter after MAR 8.3 (Requirements for benchmark administrators). The text is not underlined.

### 8.4 Requirement to provide benchmark submissions in relation to LIBOR

- 8.4.1 R (1) This section applies to each *firm* (a “specified *firm*”) specified in column (1) of the table in (2).
- (2) Table: specified *firms* which are required to provide *benchmark submissions* under MAR 8.4.2R(1).

(1) Name of <i>firm</i>	(2) CHF	(3) EUR	(4) GBP	(5) JPY	(6) USD
[Firm A]	[Specified from XXX]				
[Firm B]					
<b>Note:</b> in the table above, “N/A” means “not applicable”.					

- 8.4.2 R (1) A specified *firm* must provide *benchmark submissions* to the *LIBOR administrator* in relation to each *LIBOR* tenor for each specified rate.

- (2) A specified *firm* which is required to provide *benchmark submissions* under (1) must do so:
- (a) from the date specified in relation to the specified rate in the table in *MAR 8.4.1R(2)*; and
  - (b) in accordance with:
    - (i) *MAR 8.2*; and
    - (ii) the version of the *LIBOR Code of Conduct* (including the provisions regarding the timing and frequency of *benchmark submissions*) which applies to the specified *firm* at the time when it provides the *benchmark submission* under this *rule*.
- (3) For the purpose of this *rule*:
- (a) “*LIBOR* currency rate” means the *LIBOR* rate which is determined for each of the following currencies:
    - (i) CHF (Swiss franc);
    - (ii) EUR (euro);
    - (iii) GBP (pound sterling);
    - (iv) JPY (Japanese yen); and
    - (v) USD (US dollar);
  - (b) “*LIBOR* tenor” means the *LIBOR* currency rate which is calculated for each of the following maturity periods:
    - (i) overnight or spot next (as applicable);
    - (ii) one week;
    - (iii) one month;
    - (iv) two months;
    - (v) three months;
    - (vi) six months;
    - (vii) twelve months;
  - (c) “specified *firm*” means a *firm* specified in column (1) of the table in *MAR 8.4.1R(2)*; and

- (d) “specified rate” means the *LIBOR* currency rate specified in columns (2) to (6) of the table in *MAR 8.4.1R(2)* in respect of each *firm* specified in column (1).
- 8.4.3 G (1) The *rule* in *MAR 8.4.2R(1)* requires specified *firms* to provide *benchmark submissions* to the *LIBOR administrator*.
- (2) In accordance with *MAR 8.4.2R(1)*, a specified *firm* is required to provide *benchmark submissions*:
- (a) in relation to each *LIBOR* tenor for the *LIBOR* currency rates specified for that *firm* in *MAR 8.4.1R(2)*; and
- (b) from the date specified for those rates in *MAR 8.4.1R(2)*.
- (3) *MAR 8.4.2R(1)* does not prevent a specified *firm* from providing *benchmark submissions* from an earlier date if it wishes to do so.



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25 The North Colonnade Canary Wharf London E14 5HS  
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