ICE BENCHMARK ADMINISTRATION LIMITED

LBMA GOLD PRICE CONSULTATION – FEEDBACK STATEMENT

1. Introduction

On 14 April 2015, ICE Benchmark Administration Limited (IBA) launched a consultation on the following three aspects of the gold auction process operated by IBA:

- the approach for handling an auction should the minimum number of participants not be present
- the market convention of adding a Seller's Premium, and
- the usage of the prices in currencies other than USD (i.e. in EUR and GBP).

We are grateful for the feedback we received in response to the consultation and we provide a summary below together with IBA's proposed way forward on each of the above key aspects of the auction.

2. Auction without minimum number of participants

Rule 5.3 in IBA's Rule Book for the gold auction provides for minimum participation in a particular auction, as follows:

"(a) IBA shall, from time to time and after consultation with Participants, set a minimum number of Direct Participants for the Auction. Such minimum number shall be made public by IBA in the IBA Gold Auction Specification Document.

(b) If the minimum number of Direct Participants for an Auction is not satisfied, IBA will not conduct that Auction but will declare the Auction closed at the Opening Price.

(c) If there is no buying and selling interest for an Auction in the first Round, IBA will declare the Auction closed at the Opening Price."

In the consultation, IBA sought views as to whether it would be preferable, instead of declaring the auction closed at the Opening Price if the minimum number of Direct Participants for an auction is not present, to declare a No Publication (NP).

The clear feedback from the consultation was that users require a daily benchmark price for contractual certainty - even if the minimum number of Direct Participants for an auction are not present. Accordingly, if fewer than three Direct Participants are logged on at the commencement of an auction, IBA will not run an auction but, as the benchmark administrator, will still publish a price for the LBMA Gold Price benchmark.

3. Seller's Premium

The Seller's Premium is a long-standing market convention by which a USD 15 cents premium per ounce is added to the benchmark price so that all trades settle at a higher price than the published benchmark.

Direct Participants settle amongst themselves at the auction price plus the Seller's Premium (ie at the LBMA Gold Price plus USD 15 cents).

Direct Participants and their clients then settle at a spread around this new value of the benchmark price plus the Seller's Premium. Direct Participants each set a spread at which they will buy from clients and sell to clients. That spread is bilaterally agreed between each Direct Participant and its clients. For example, if the benchmark price is $1,200.00 and the client spread is 10 cents then transactions between direct participants settle at $1,200.15, selling clients receive $1,200.05 and buying clients pay $1,200.25.

The Seller's Premium is thought to have been introduced in order to allow some scope for enhanced profitability for producers who bring their product to market via the London auction. As the supply chain has grown in complexity, this aspect of the Seller's Premium has diminished in relevance but the Seller's Premium has remained an integral part of the process and is now reflected across the industry.

The consultation paper asked whether the Seller's Premium should still remain as a market convention for gold.

Of the respondents who expressed an opinion on this, views were mixed and no consensus emerged. Generally, producers would cease the convention. Views from both refiners and end users were mixed, with half preferring retention and half preferring cessation.

Those in favour of retaining the Premium cited reasons as follows:

- It encourages Direct Participants to be active in the auction
- The mid-market premium permits Direct Participants to apply commission to client order execution at a spread around the mid-market premium rate,
- It is a long-standing convention and its removal could lead to lower volumes going through the auction, and
- There would be significant work involved for Direct Participants if the Seller's Premium ceased because it would change their pricing structures.

Those in favour of ceasing the Premium as a convention expressed views that:

- The Gold price should not be restricted by market convention, rather it should allow market forces to dictate where prices move
- The Premium has implications on pricing for both end clients and Direct Participants

- It would be fair to buyers and sellers to have no Premium
- The Premium is an anachronism. Its removal would ameliorate the tracking error for financially settled derivatives and expand the usage and liquidity of swaps
- It is an obsolete convention. Bid offers should just move from +10 / +20 cents to -5 / + 5 cents
- It is an outdated concept that punishes buyers, and
- What is most important to investors is a deep, liquid market for gold with a competitive bid/offer spread. Removing the Seller's Premium would take away a frictional cost in the benchmark price and therefore should lower the transaction cost to investors, thus improving pricing and liquidity for all.

On the notice period that would be needed for ceasing the Seller's Premium, some respondents suggested several months.

The consultation also asked whether any changes should be made to the value of the Seller's Premium if it were kept. No respondent favoured changing the value of the Seller's Premium if it were kept.

Having considered the feedback, IBA has concluded (through the Oversight Committee) that the Seller's Premium should cease to be a market convention for the gold auction from 1 January 2016. All trades in the auction will settle at the benchmark price, though clients and direct participants are free to bilaterally agree the charging structure for their services (spreads, fees, etc.). This lead time will give Direct Participants enough time in which to inform their clients and put in place new pricing structures and documentation as necessary.

If there is sufficient interest, IBA will host an open forum to discuss the practical implementation steps. If you would like to attend such a forum, please let us know at IBA@theice.com.

4. Non-USD Prices (i.e. EUR and GBP)

The price discovery in the Gold auction is in USD. At the end of the auction, the price for Gold in USD is converted into EUR and GBP and these non-USD prices are published as indicative settlement prices at the end of the auction, or as benchmarks for reference in derivative contracts.

In the consultation, IBA asked about the usage of the non-USD gold prices (EUR and GBP), the impact of discontinuation of these prices and the notice that would be required of such a discontinuation.

Although very few respondents use the non-USD gold prices, either for settlement price purposes or as a benchmark in contracts, they value the availability of the EUR and GBP prices.

IBA intends to continue to publish the EUR and GBP prices but will keep the matter subject to periodic review.

5. Summary of actions

The following is a summary of the actions resulting from the consultation:

1. If fewer than three Direct Participants are logged on at the commencement of an auction, IBA will not run an auction but will still publish prices for the LBMA Gold Price benchmark.

2. The Seller's Premium will cease to be a market convention for the Gold auction from 1 January 2016, and

3. IBA will continue to publish the EUR and GBP prices.
