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Benchmarks Regulation

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Overview

The Benchmarks Regulation is intended to prohibit the use in the European Union of unauthorised benchmarks, including benchmarks prepared by unregistered non-EU administrators from non-equivalent jurisdictions and to enhance the single market by creating a common framework across Member States. By limiting the ability of national administrators to set benchmarks rates using their own discretion, it is hoped that conflicts of interests will be reduced and confidence will be restored in the accuracy and integrity of benchmarks.

The Regulation seeks to:

- improve governance and controls over the benchmark process, in particular to ensure that administrators avoid conflicts of interest, or at least manage them adequately
- improve the quality of input data and methodologies used by benchmark administrators
- ensure that contributors to benchmarks and the data they provide are subject to adequate controls, in particular to avoid conflicts of interest, and
- protect consumers and investors through greater transparency and adequate rights of redress.

The Regulation aims to address potential issues at each stage of the benchmark process and will apply in respect of:

- the provision of benchmarks
- the contribution of input data to a benchmark, and
- the use of a benchmark within the EU.

Benchmark categories

- The Regulation defines a "benchmark" as “any index by reference to which the amount payable under a financial instrument or a financial contract, or the value of financial instrument is determined or an index that is used to measure the performance of an investment fund.”

  The Regulation sets three main categories of benchmarks:

Critical benchmarks

- These are benchmarks used for financial instruments, contracts and performance of investment funds having a total value of at least €500bn, and meeting qualitative criteria such as location of contributors and importance of the benchmark in the country where a majority of contributors is located.
- Administrators of critical benchmarks have to comply with all requirements set out in the Regulation.

Significant benchmarks

- These are benchmarks used for financial instruments, contracts and performance of investment funds having a total value of at least €50bn over a period of six months, and meeting qualitative criteria such as the benchmark has no reliable substitute, and its absence would lead to market disorder.
- Administrators of significant benchmarks do not have the mandatory obligation to comply with all the rules related to governance, control of administrators and input data, but have to comply with the other provisions in the Regulation.

Non-significant benchmarks

- These are benchmarks that do not fulfill the conditions set for critical or significant benchmarks.
- Administrators of non-significant benchmarks are subject to a lighter regulatory regime based on a compliance statement - administrators are exempt from governance, control of administrators and input data, but have to comply with the code of conduct rules.

Administrator requirements

- An administrator is defined in the Regulation as a natural or legal person that has control over the provision of a benchmark, and in particular administers the arrangements for determining the benchmark, collects and analyses the input data, determines the benchmark, and either directly publishes or outsources the publication or the calculation of the benchmark to a third party.

  In order to ensure the integrity of benchmarks, administrators are subject to a number of requirements, including:

- implementation of adequate governance arrangements
- establishment of a permanent and effective oversight function
- outsourcing limitations

- adoption of a code of conduct specifying obligations of contributors in respect of input data, and in particular its reliability and consistency with the benchmark administrator's controls and methodology
- publication of benchmark statements providing key information to users in relation to the benchmarks measures and their vulnerabilities
- systems and controls to ensure integrity of data
- complaints handling mechanisms, and
- adequate record keeping requirements.

Administrators providing benchmarks must by authorised. Alternatively, when benchmarks are non-significant or provided by a supervised entity other than an administrator, they can apply for registration with a competent authority.

Input data

- To ensure that only sufficient and accurate data is used in determination of benchmarks, the Regulation sets out five requirements for benchmark administrators. They must:

- ensure that the input data accurately and reliably represents the market or economic reality that the benchmark measures
- obtain the input data from a reliable and representative panel or sample of contributors
- ensure that the input data is verifiable
- publish clear guidelines regarding the types of input data, the priority of their use and the exercise of expert judgement, and
- not use input data from contributors who do not adhere to the code of conduct.

Contributor requirements

- The Regulation imposes obligations on supervised contributors making them subject to adequate governance and controls requirements, specifically to avoid conflicts of interest.

Contributors are also required to adhere to a legally binding code of conduct adopted by administrators, and can be required by competent authorities to contribute to critical benchmarks to preserve their credibility.

Use of a benchmark

- The definition of "use of a benchmark" extends the scope of the Regulation to the following activities:

- issuance of a financial instrument which references an index or a combination of indices
- determination of the amount payable under a financial instrument or financial contract by referencing an index or combination of indices
- being party to a financial contract which references an index or combination of indices
- providing a borrowing rate calculated as a spread or mark-up over an index or a combination of indices and that is solely used as a reference for a financial contract, and
- determination of the performance of an investment fund through an index or combination of indices for the purpose of tracking the return of such index or combination of indices, of defining the asset allocation of a

portfolio or of computing the performance fees.

Third country regimes

- To ensure investor protection, the Regulation provides for the following mechanisms under which third country benchmarks can be used by supervised entities in the EU:

  - **Equivalence** - the Commission takes a positive decision on equivalence of a third country regime or specific rules/ requirements of a third country with respect to individual and specific benchmarks/ administrators. Co-operation arrangements with the relevant third country competent authorities must follow the equivalence decision.

  - **Recognition** - national competent authorities assess the application of IOSCO Principles by a third country administrator, and determine whether such application is equivalent to compliance with the requirements established in the Regulation. A third country administrator must also have a legal representative in the EU. Recognition is intended as a temporary measure until such time as an equivalence decision is adopted by the Commission.

  - **Endorsement** - administrators or supervised entities located in the EU can apply to their competent authority to endorse third country benchmarks.