

The new EU benchmarks regulation: What you need to know

The new EU Regulation on financial benchmarks has been published in the Official Journal and has now entered into force. The Regulation imposes new requirements on firms that provide, contribute to or use a wide range of interest rate, currency, securities, commodity and other indices and reference prices. Most of the new rules will not apply until 1 January 2018 but some provisions relating to critical benchmarks are already in effect and the Commission has already designated the first critical benchmark under the Regulation. Consultations have begun on the “Level 2” measures to be adopted under the Regulation. The new rules present a significant implementation challenge, particularly where EU firms reference non-EU benchmarks in securities or derivatives or use them in the management of investment funds.

Objectives

The new Regulation is a key part of the EU’s response to the LIBOR scandal and the allegations of manipulation of foreign exchange and commodity benchmarks. It aims to reduce the risk of manipulation of benchmarks by addressing conflicts of interest, governance controls and the use of discretion in the benchmark-setting process. It requires EU administrators of a broad class of benchmarks to be authorised or registered by a national regulator and to implement governance systems and other controls to ensure the integrity and reliability of their benchmarks. These build on – but go beyond – the 2013 Principles for Financial Benchmarks and the 2012 Principles for Oil Price Reporting Agencies adopted by the International Organisation of Securities Commissions (IOSCO).

Supervised entities under EU legislation, including banks, investment firms, insurance companies, UCITS and pension funds, fund managers and consumer lenders, will also be subject to restrictions on using benchmarks unless they are produced by an EU administrator authorised or registered

under the Regulation or are non-EU benchmarks that have been qualified for use in the EU under the Regulation’s third country regime. EU administrators must require all contributors to their benchmarks to comply with a code of conduct and the Regulation will directly require supervised entities that contribute to EU benchmarks to maintain systems and controls to ensure the integrity and reliability of their input data.

The new EU regime will replace the current UK framework regulating the administrators of LIBOR and other specified benchmarks. It takes a very different approach from those jurisdictions, such as Japan and Singapore, that – like the UK – have so far chosen to regulate a limited range of critical benchmarks and those jurisdictions, such as the US, that are relying on self-regulation and robust enforcement action to achieve the objectives of the IOSCO Principles. The Regulation provides three routes allowing the use of non-EU benchmarks in the EU. However, non-EU administrators may not be willing or able to qualify their benchmarks for use in the EU under this regime.

Key issues

New EU regime regulating producers, contributors to and users of benchmarks

Covers interest rate, FX, securities, commodity and other benchmarks used in financial transactions

Most provisions of the Regulation apply from 1 January 2018

EU benchmark administrators must be authorised or registered and implement new systems and controls

New rules for firms contributing input data to EU benchmarks

Supervised entities must not use unregulated benchmarks in the EU in securities or derivatives traded on a venue or via a systematic internaliser, certain consumer loans or investment funds

Non-EU benchmarks can only be used in the EU if the benchmark is qualified under the third country regime

Transitional provisions do not specifically address new benchmarks launched after 30 June 2016

Risk that some benchmarks may be discontinued and some non-EU benchmarks may not qualify under the third country regime.

Timing and transitional arrangements

The Regulation entered into force on 30 June 2016. The provisions relating to the mandatory administration of and mandatory contribution to critical benchmarks came into effect immediately and the Commission has already adopted an implementing act designating Euribor as a critical benchmark for the purposes of the Regulation. The early application of these provisions on critical benchmarks is intended to prevent critical benchmarks from being undermined by an exodus of contributors. The rest of the Regulation will apply from 1 January 2018.

EU benchmark administrators providing benchmarks on 30 June 2016 will have until 1 January 2020 to apply for authorisation or registration. Transitional provisions will allow these administrators to

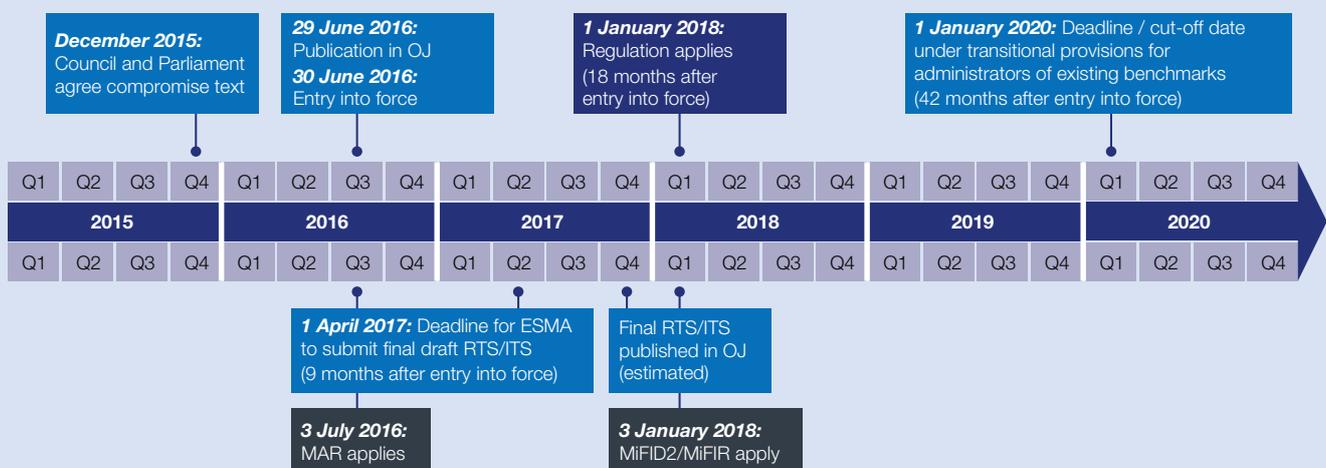
continue to provide those existing benchmarks (and for supervised entities to continue to use those benchmarks) until 1 January 2020 or, if an administrator applies for authorisation or registration before that date, until their application is refused. However, the Regulation does not provide supervised entities with a means of identifying whether an application has been or when it has been refused. In addition, the Regulation does not contain provisions stating that administrators applying for authorisation or registration after 1 January 2018 can delay compliance with the other requirements of the Regulation.

After 1 January 2020 national regulators will be able to permit the continued use of an existing benchmark provided by an EU administrator that does not comply with the Regulation if cessation or change to the benchmark would cause a force majeure event, frustrate or breach the

terms of a financial instrument, financial contract or rules of an investment fund that references that benchmark. No financial instruments, financial contracts or measurements of the performance of an investment fund will be able to add a reference to the existing EU benchmark after 1 January 2020 but no specific provisions allow for the continued production of the benchmark after that date.

Where a benchmark provided by a non-EU administrator is already used in the EU on 30 June 2016 and has not yet been qualified for use in the EU under the Regulation's third country regime, then its use in the EU will only be permitted in a financial instrument or financial contract, or for measuring the performance of an investment fund, that already references the benchmark or adds a reference to the benchmark before 1 January 2020.

EU Benchmarks Regulation – timeline



Note: The Regulation does not prescribe a timetable for the adoption of the Commission's delegated and implementing acts or ESMA's guidelines under the Regulation.

The Regulation does not appear to allow the continued use in the EU after 1 January 2018 of benchmarks provided by an EU administrator for the first time after 30 June 2016 or of benchmarks provided by a non-EU administrator that are used in the EU for the first time after 30 June 2016, unless and until the EU administrator is authorised or registered under the Regulation or the non-EU benchmark is qualified for use in the EU under the third country regime. However, this could create a hiatus during which use of these benchmarks in the EU must cease from 1 January 2018 until the administrator has achieved authorisation or registration or qualification of the benchmark for use in the EU.

The new Regulation requires the European Securities and Markets Authority (ESMA) to draft regulatory and implementing technical standards (RTS/ITS) specifying the detail of many of the requirements. The Regulation requires ESMA to deliver final drafts to the Commission by 1 April 2017. The Commission may choose to amend those standards and the Parliament and the Council must be given a period in which to object to any RTS. The Regulation also envisages that ESMA will issue guidelines and that the Commission will adopt delegated acts further defining other aspects of the Regulation. These may also only be available at a late stage before the date of application. Thus, the full set of final requirements may only be available shortly before the Regulation begins to apply, complicating implementation planning for firms.

On 15 February 2016, ESMA issued a discussion paper consulting on its initial proposals for the technical standards and

its technical advice to the European Commission on its delegated acts. On 27 May 2016, ESMA issued a consultation paper on its draft technical advice. The comment periods for these papers have now closed. ESMA is expected to issue a further consultation paper on its draft technical standards before the end of 2016.

The Regulation will apply in the UK before the likely earliest date on which the UK could withdraw from the EU. UK regulators have made clear that UK firms should continue to implement existing and new EU legislation notwithstanding the UK's planned exit from the EU.

The start date of 1 January 2018 also means that the Regulation takes effect shortly before the revised effective date (3 January 2018) of the new Markets in Financial Instruments Directive and Regulation (MiFID2/MiFIR) even though the new Regulation relies on several concepts used in MiFID2/MiFIR. However, the gap is very short and may not significantly add to the larger practical issue of identifying what instruments are traded on venues within the scope of MiFID2/MiFIR and thus potentially within the scope of the Regulation.

What benchmarks will be regulated?

The new Regulation is designed to cover a very wide range of indices including indices linked to interest rates, currencies, securities, commodities and even factors such as the weather. An index will be regulated as a "benchmark" where it determines amounts payable under or sets the value of financial instruments or financial contracts or is used in investment funds.

The aim is to cover indices used in securities or derivatives traded on a regulated trading venue under MiFID2/MiFIR, including securities and derivatives traded outside a venue via an investment firm that is a "systematic internaliser" under MiFID2/MiFIR. The Regulation also covers indices used to set interest rates under certain consumer loans and consumer mortgages as well as the indices used in index tracking and some other funds.

This is the case regardless of the volume or systemic relevance of the usage of the index. A key test will be whether the index is considered to be published or made available to the public. ESMA's Consultation Paper proposes that an index should be considered as "made available to the public" if the index is accessible by a large or potentially indeterminate number of recipients or is provided or is accessible to one or more supervised entities to allow the "use" of the index within the meaning of the Regulation and, through that use, the index becomes accessible to an indeterminate number of people. Thus, the regulation could apply to customised proprietary indices provided by investment banks for specific financial instruments as well as the well-known indices widely used in the financial sector. However, the Regulation aims to provide a more proportionate and flexible regime for administrators of benchmarks that are not regarded as being of critical importance.

The Regulation exempts certain kinds of providers and indices from the scope of the Regulation. In particular, there are exemptions for central banks and public authorities (both EU and non-EU) that provide indices for public policy purposes. There is also an important

What is a benchmark?	
Benchmark	Any index by reference to which the amount payable under a financial instrument or financial contract , or the value of a financial instrument is determined or ... an index that is used to measure the performance of an investment fund with the purpose of: <ul style="list-style-type: none"> ■ tracking the return of such index or ■ defining the asset allocation of a portfolio or ■ computing the performance fees.
Index	Any figure: <ul style="list-style-type: none"> ■ that is published or made available to the public; ■ that is regularly determined, entirely or partially, by the application of a formula or any other method of calculation, or by an assessment; and ■ on the basis of the value of one or more underlying assets or prices, including estimated prices, actual or estimated interest rates, quotes and committed quotes or other values or surveys.
Financial instrument	Any of the instruments listed in Section C of Annex I of MiFID2: <ul style="list-style-type: none"> ■ for which a request for admission to trading on a trading venue (as defined in MiFID2) has been made or ■ which are traded on a trading venue or via a systematic internaliser (as defined in MiFID2)
Financial contract	Any credit agreement covered by the Consumer Credit Directive or the Mortgage Credit Directive
Investment fund	Any UCITS or alternative investment fund (AIF)

exemption for single reference prices for an individual security or derivative, but this does not cover single reference prices for commodities. Although not expressly stated, it seems likely that the Regulation will not prevent supervised entities using indices produced by a person that is exempted from the scope of the Regulation.

Restrictions on use

From 1 January 2018 (and subject to the transitional arrangements discussed above) supervised entities will be prohibited from “using” indices as a benchmark in the EU unless they are produced by an EU administrator included on ESMA’s register of administrators authorised or registered

under the Regulation or are non-EU benchmarks that are included on ESMA’s register because they have been qualified for use in the EU under the Regulation’s third country regime.

This prohibition will not cover every use of other indices. For example, it will not prevent supervised entities making corporate loans or holding or trading a security referencing other indices. It should also not prevent counterparties referencing other indices in an OTC derivative executed outside a regulated EU trading venue if none of the counterparties is a “systematic internaliser” in relation to that derivative. ESMA’s proposed technical advice would suggest that a counterparty to an OTC derivative contract should not be regarded as using a benchmark by “issuing” a financial instrument” referencing an index by entering into such a contract. ESMA proposes that a person should only be regarded as “issuing a financial instrument” for these purposes where the financial instrument takes the form of a transferable security, money market instrument or unit in a collective investment undertaking. Managers of investment funds will need to focus on the precise use they are making of other indices as the restrictions do not only apply to index-tracking or similar funds.

The Regulation does not further define what will amount to use “in the EU”. Nor does it specify whether the definition of supervised entities will cover entities that fall within the definitions of a credit institution or investment firm but that would benefit from exemptions under the relevant legislation or entities that are established outside the EU (or how the regime applies where supervised entities act through non-EU branches).

What exemptions will apply under the Regulation?	
Exemption for:	Additional conditions
Central banks	None
Public authorities	Where they contribute data to, provide, or have control over the provision of, benchmarks for public policy purposes, including measures of employment, economic activity, and inflation
Central counterparties	Where they provide reference prices or settlement prices used for CCP risk-management purposes and settlement
Single reference prices	Where the single reference price is for an instrument listed in Section C of Annex I of MiFID2
Press, media, journalists	Where they merely publish or refer to a benchmark as part of their journalistic activities with no control over the provision of that benchmark
Any person (consumer and mortgage credit)	Where it grants or promises to grant credit in the course of its trade, business or profession, only in so far as that person publishes or makes available to the public its own variable or fixed borrowing rates set by internal decisions and applicable only to credit agreements covered by the Consumer Credit Directive or the Mortgage Credit Directive entered into by that person or a company within the same group with their respective clients
Commodity benchmarks	Where: <ul style="list-style-type: none"> ■ the benchmark is based on submissions by contributors which are in majority non-supervised entities; ■ the benchmark is referenced by financial instruments for which a request for admission to trading has been made on only one trading venue (as defined in MiFID2), or which are traded on one such trading venue; and ■ the total notional value of financial instruments referencing the benchmark does not exceed €100 million See above for definition of 'financial instrument'
'Involuntary' index providers	Where the index provider of an index is unaware and could not reasonably have been aware that the index is used for the purposes set out in the definition of a 'benchmark' under the Regulation

Supervised entities that use benchmarks are also required to maintain robust written contingency plans addressing the actions that they would take if a benchmark used by them materially changes or ceases to be produced. Where feasible and appropriate, the

plans must nominate one or more alternative benchmarks that might be referenced in substitution for discontinued benchmarks. In addition, supervised entities must reflect these plans in the contractual relationship with their clients. For example, ISDA

derivatives documentation provides a framework to address changes to or the discontinuance of indices. The Regulation does not clarify whether it has retroactive effect in relation to existing contracts.

Authorisation or registration of EU administrators

Every person located in the EU that has control over the provision of a benchmark will be required to be authorised or registered by a national regulator, unless an exemption applies. However, in some cases, it may be difficult to determine whether a person is a user of a benchmark or a provider of a benchmark requiring authorisation or registration as an administrator. The recitals to the Regulation suggest that weighting indices within a combination of indices to determine the pay-out or the value of a financial instrument or a financial contract or measure the performance of an investment fund will be regarded as the use of an index rather than the provision of a new index. The Regulation also contains provisions indicating that a lender in a consumer loan or mortgage loan will be regarded as a user rather than a provider of a benchmark if it provides a borrowing rate calculated as a mark-up or spread over an index in contracts to which it is a party. However, it does not make clear that other similar determinations of an interest rate based on a mark-up to a benchmark (for example, for the purposes of a listed floating rate note) are treated in the same way.

A person that provides an index will not require authorisation or registration if the provider is not aware and could not reasonably have been aware that its index is being used as a benchmark. However, EU providers may require authorisation or registration if they

What 'use' of benchmarks will be restricted by the Regulation?

Financial instruments

- The issuance of a financial instrument which references an index or a combination of indices
- The determination of the amount payable under a financial instrument by referencing an index or a combination of indices

Financial contracts

- The determination of the amount payable under a financial contract by referencing an index or a combination of indices
- Being party to a financial contract which references an index or a combination of indices
- Providing an interest rate (expressed as fixed or variable percentage applied on an annual basis to the amount of credit drawn down) calculated as a spread or mark-up over an index or a combination of indices and that is solely used as a reference in a financial contract to which the creditor is a party

Investment funds

- Measuring of the performance of an investment fund through an index or a 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

See above for definitions of 'index', 'financial instrument', 'financial contract' and 'investment fund'

become aware that data they publish are being used as a benchmark, even if this use is without their consent.

Regulation of EU administrators

The obligations that apply to EU benchmark administrators mainly depend on the type and category of their benchmarks. There are four broad types of benchmark, depending on their underlying asset or factor: interest rate benchmarks, commodity benchmarks, regulated-data benchmarks and other (non-commodity) benchmarks. In addition, there are three different categories of benchmark: critical, significant and non-significant. This creates a highly differentiated regime

where different rules apply to benchmarks with different characteristics.

EU administrators that are supervised entities must be registered under the Regulation, unless they provide a critical benchmark, when they must be authorised. EU administrators that are not supervised entities must be authorised under the Regulation, unless they provide a non-significant benchmark, when they must be registered (but there is a transitional period during which administrators of non-widely used significant benchmarks may be registered instead of authorised). The intention is that registration should be a faster and less burdensome procedure than authorisation, but registered and authorised administrators are subject to

the same compliance obligations according to the type and category of their benchmarks.

Compliance obligations of EU administrators

When authorised or registered, administrators will have to publish a "benchmark statement" describing the key features of each regulated benchmark or family of benchmarks that they provide as well as the methodology and input data used to calculate the benchmark.

In addition, the Regulation imposes a wide-ranging set of requirements on benchmark administrators regulating governance and conflicts of interest, internal oversight, control and accountability frameworks, input data and benchmark methodologies. In particular, national regulators are given powers to require certain benchmark administrators to establish an independent oversight function (with balanced stakeholder representation) if conflicts of interest cannot be adequately mitigated and ultimately to direct full ownership separation or cessation of the publication of a benchmark if conflicts cannot be adequately managed.

Interest rate benchmarks

The Regulation imposes distinct requirements on interest rate benchmarks. In particular, administrators are required to give priority to input data from actual transactions in the underlying market over observations of third party transactions, committed quotes or indicative quotes or expert judgment. Administrators of interest rate benchmarks are also required to establish an independent oversight committee tasked with regular scrutiny of calculation methodology, input data and wider governance arrangements. Specific and comprehensive systems and controls

requirements also apply to firms contributing to interest rate benchmarks. All interest rate benchmarks are subject to a biennial independent external compliance audit.

Commodity benchmarks

The administration of certain commodity benchmarks is subject to a separate set of requirements. Administrators of these commodity benchmarks are required to specify the criteria that define the physical commodity that is the subject of a particular benchmark. They must give priority to input data based on concluded and reported transactions as well as data relating to bids and offers, in order to present an accurate picture of the market. There are also special rules relating to the role of assessors and a requirement for an annual independent external compliance audit.

Commodity benchmarks cannot benefit from the relief for significant or non-significant benchmarks but they may be subject to the more onerous rules applicable to critical benchmarks. However, if a commodity benchmark is critical and its underlying is gold, silver or platinum then it is subject to the general rules for financial benchmarks rather than the special commodities rules. Similarly, if the majority of contributors to a commodity benchmark are supervised entities, the benchmark is subject to the general rules for financial benchmarks.

Regulated-data benchmarks

Administrators of regulated-data benchmarks are not required to comply with certain of the governance and control requirements regulating the contribution of input data. Regulated-data benchmarks are benchmarks determined by the application of a formula from input data contributed entirely and directly from trading venues, approved publication arrangements, approved reporting

mechanisms and certain commodity exchanges. The Regulation now allows benchmarks based on input data from certain equivalent non-EU trading venues to benefit from these rules.

Regulated-data benchmarks are not subject to the additional requirements applicable to critical benchmarks. However, regulated-data benchmarks that are not commodity benchmarks may benefit from the less onerous rules applicable to significant or non-significant benchmarks if the regulated-data benchmark underpins business valued at up to €500 billion.

Critical benchmarks

The Commission has to designate a list of critical EU benchmarks at least every two years on the basis of the following:

- the benchmark underpins business valued at €500bn or more;
- the benchmark has a majority of supervised contributors in one Member State and is recognised as critical in that Member State by its national regulator; or
- the benchmark underpins business valued at €400bn or more and has no or very few appropriate market-led substitutes and cessation of or data failures relating to the benchmark would result in significant and adverse impacts on market integrity, financial stability, consumers, the real economy or the financing of households or corporations in one or more Member States (and national regulators can determine that this condition is satisfied, including waiving the quantitative thresholds).

In practice, this gives national regulators considerable discretion to determine that benchmarks produced by their administrators should be designated as critical benchmarks. Critical benchmarks

are subject to additional requirements, including the following:

- a mandatory annual external audit of compliance;
- regulators' powers to delay the discontinuance of the benchmark by requiring the administrator temporarily to continue the provision of the benchmark;
- a requirement for the administrator to provide licences of, and information on, the benchmark to all users on a fair, reasonable, transparent and non-discriminatory basis;
- regulators may require supervised entities temporarily to contribute input data to the benchmark (although they cannot be required to enter into transactions for this purpose);
- the administrator's home state regulator must establish a college of supervisors to oversee the benchmark, including regulators from other Member States where the benchmark is significant.

The rules on mandatory administration and contribution to benchmarks took effect on 30 June 2016. As noted above, the Commission has already adopted an implementing act designating Euribor as a critical benchmark for the purposes of the Regulation.

Significant and non-significant benchmarks

Non-critical financial benchmarks will be treated as significant benchmarks if:

- the benchmark underpins business valued at €50bn or more; or
- the benchmark has no or very few appropriate market-led substitutes and cessation of or data failures relating to the benchmark would result in significant and adverse impacts on market integrity, financial

stability, consumers, the real economy or the financing of households or corporations in one or more Member States.

Other benchmarks are treated as non-significant. However, it may be difficult for the administrator of a benchmark to establish whether the benchmark should be treated as non-significant, particularly where the administrator has no direct information on the volume of business underpinned by the benchmark.

The administrator of a significant benchmark has the option to “comply or explain” in relation to some compliance obligations, in particular as regards the operational separation of benchmark activities from other business activities. However, national regulators have the discretion to override this option taking into account the nature or impact of the benchmark or the size of the administrator.

The administrator of a non-significant benchmark can make greater use of “comply or explain” (without a regulatory override). Such administrators are also exempt from some of the detailed technical standards made under the new Regulation, although ESMA may issue guidelines for these administrators.

Contributors

Where a benchmark is based on input data from contributors, the administrator must develop a code of conduct for contributors and ensure that contributors adhere to the code. The administrator must also monitor input data and contributors so as to be able to report suspected market abuse to its national regulator.

The Regulation imposes obligations on supervised entities that contribute input data to benchmarks provided by EU administrators to ensure that the data is

not affected by conflicts of interest, that any discretion is independently and honestly exercised based on relevant information in accordance with the code of conduct and to have a control framework and effective systems and controls to ensure the integrity, accuracy and reliability of input data and compliance with the code of conduct.

These rules on contribution of input data do not apply to contribution of input data to benchmarks subject to the separate rules on commodity benchmarks, which impose more limited obligations on the administrator as regards input data.

Non-EU benchmarks

There are three routes through which non-EU administrators can qualify their benchmarks for use in the EU under the Regulation: equivalence, recognition and endorsement. However, all three routes present practical challenges and some non-EU administrators may not be willing or able to qualify their benchmarks for use in the EU under the third country regime. Non-EU administrators may have limited incentives to do this, particularly where their benchmark is made available free of charge or they derive relatively low licence revenues from the EU.

All three routes do allow EU regulators to rely on an administrator’s compliance with the IOSCO Principles, at least if compliance is equivalent to the requirements of the Regulation. However, some of the requirements of the Regulation appear to go beyond the requirements of the IOSCO Principles and it is not clear how these types of inconsistency might affect equivalence decisions.

Equivalence

ESMA will be able to register a benchmark provided by a non-EU

administrator as qualified for use in the EU if:

- the Commission has adopted an equivalence decision;
- the administrator is authorised or registered, and is supervised, in the non-EU state;
- the administrator has notified ESMA of its consent to the use of its benchmarks in the EU by supervised entities (and of a list of the benchmarks and of the relevant non-EU regulator); and
- cooperation arrangements between ESMA and the non-EU authority are operational.

The Commission will be able to adopt an equivalence decision with respect to a non-EU state if administrators authorised or registered in that state comply with binding requirements that are equivalent to the Regulation. Alternatively, the Commission will be able to adopt an equivalence decision if there are binding requirements in the non-EU state equivalent to the Regulation with respect to a specific non-EU administrator or benchmark or benchmark family. This provides some flexibility as it will allow the Commission to make equivalence decisions for non-EU benchmarks in those cases where a non-EU state only regulates a limited category of critical benchmarks on an equivalent basis. At present, relatively few non-EU states could qualify for an equivalence determination for any benchmarks.

In either case, the non-EU requirements must be subject to effective on-going oversight and enforcement in the non-EU state. In determining equivalence, the Commission can take into account if the legal framework and supervisory practice

in the non-EU state ensures compliance with the IOSCO Principles.

Recognition

Pending a Commission equivalence determination, ESMA will be able to register a benchmark provided by a non-EU administrator as qualified for use in the EU if the administrator has been recognised by the national regulator in its EU Member State of reference and maintains a legal representative in that Member State.

The non-EU administrator will have to comply with most of the obligations applicable to EU administrators. It will be allowed to fulfil that compliance obligation by applying the IOSCO Principles but only if the national regulator determines that their application is equivalent to compliance with the requirements established in the Regulation.

The relevant national regulator will be able to rely on an auditor's or supervisor's certification as to IOSCO compliance, but even where this can be provided, it is not clear how often it will need to be updated or the circumstances in which national regulators could choose to look behind the certification.

Non-EU administrators will also have to identify their Member State of reference applying rules that take into account the location of affiliated supervised entities, the location of trading venues for financial instruments referencing their benchmarks and the location of supervised entities using their benchmarks. In some cases, it may be difficult for non-EU administrators to identify the Member State of reference because they do not have the required information on the location of trading or use of its benchmarks.

The non-EU administrator will also have to ensure that the legal representative can perform an oversight function in relation to the benchmark together with the administrator and the legal representative will be accountable to the national regulator in this respect. It may be difficult to agree appropriate arrangements with the legal representative.

If the administrator is subject to supervision, regulatory cooperation agreements must be in place with ESMA. In addition, local law, regulation or administrative practices must not prevent the national regulator from exercising supervision over the non-EU administrator.

Endorsement

ESMA will also be able to register a benchmark provided by a non-EU administrator as qualified for use in the EU if an administrator or other supervised entity in the EU has been authorised by its national regulator to endorse the benchmark. The endorsing entity will have to have a "clear and well defined role within the control or accountability framework of the third country administrator" that allows it "to effectively monitor the provision of the benchmark". This may not be straightforward, especially if the endorsing entity is not in the same group as the administrator.

The endorsing entity is responsible for compliance with the Regulation and will have to satisfy its national regulator that the provision of the third country benchmark fulfils mandatory or voluntary requirements in the non-EU country that are "at least as stringent" as those under the Regulation. Again, the national regulator is allowed to take into account compliance with the IOSCO Principles if this is equivalent to compliance with the requirements established in the Regulation.

The national regulator must refuse authorisation unless there is an objective reason to provide the benchmark outside the EU and endorse it in the EU.

Supervisory and enforcement powers

National regulators will have a wide range of supervisory and investigatory powers to access data, require information, conduct on-site inspections and request the freezing or sequestration of assets. Member States must also give national regulators powers to take administrative measures and impose sanctions, including cease and desist orders, profit disgorgement, warnings, suspension and withdrawal of authorisation, limitations on natural persons performing management functions as well as financial penalties on both natural and legal persons (of up to at least €500,000 or equivalent for natural persons and in certain cases of up to at least 10% of turnover for legal persons). Some Member States may choose to apply criminal penalties to contraventions.

The Regulation gives Member States until 1 January 2018 to adopt national rules on penalties and other sanctions for contravention of the Regulation and notify these to the Commission.

National courts may also be able to impose civil liability on persons that contravene the requirements of the Regulation under the general principles applicable to EU regulations.

Other legislation and review

The Regulation requires trading venues to include details of the relevant benchmarks and their administrators when they notify their national regulator under the Market Abuse Regulation (MAR) of financial instruments traded on their systems that reference a

benchmark. This will provide some transparency as to the financial instruments that are within the scope of the Regulation.

The Regulation requires prospectuses for securities and UCITS referencing a benchmark to contain clear and prominent information stating whether the benchmark is provided by an administrator included in the ESMA register of administrators.

The Regulation amends the Consumer Credit Directive and the Mortgage Credit Directive so as to require lenders making loans regulated by those Directives which reference a benchmark to disclose to consumers the name of the benchmark and its administrator and the implications of the use of the benchmark for the consumer. The Regulation gives Member States until 1 July 2018 to adopt the necessary implementing rules under those Directives and to bring them into force.

The Regulation has also amended MAR to provide relief to persons discharging managerial responsibility in an issuer (and persons closely connected with them) from the requirement to disclose transactions in financial instruments linked to securities of the issuer, in particular where those securities do not exceed 20% of the relevant exposure or underlying investments.

There is also other existing EU legislation on benchmarks. MAR already specifically regulates the manipulation of financial benchmarks and the manipulation of

power and gas benchmarks may also be covered by the Regulation on Energy Market Integrity and Transparency (REMIT). MiFID2/MiFIR will introduce rules giving CCPs and trading venues rights of non-discriminatory access to benchmarks.

The Commission is required to carry out a review of the Regulation by 1 January 2020.

Impact and implementation

EU entities will need to identify all indices produced or controlled by them that may qualify as regulated benchmarks under the new Regulation (including proprietary or customised indices) and consider how to be authorised or registered under the Regulation. They will also need to overhaul their internal procedures in order to meet the new standards for the provision of benchmarks, even if they already implement the IOSCO Principles.

Similarly, firms will need to identify where they contribute input data to benchmarks administered by EU entities. Where relevant, they will need to review their willingness to adhere to the administrator's code of conduct and, if they are supervised entities, to comply with the direct obligations imposed by the Regulation on supervised contributors. An administrator may ask calculation agents and other service providers to comply with additional requirements to ensure its compliance with the Regulation.

Administrators that are located outside the EU will need to assess whether they

are willing and able to qualify their benchmarks in the EU under the third country regime.

Supervised entities need to identify which of their business lines are engaged in activities that may constitute the "use" of a benchmark in the EU (for example, when issuing securities or entering into derivatives contracts, making consumer loans or managing a fund). They will need to identify whether the administrators of relevant benchmarks will continue providing the benchmarks and the administrators' plans for complying with the new regime (in particular, in the case of non-EU administrators). They will also need to prepare contingency plans, contract remediation programmes and prospectus and consumer disclosures, as appropriate.

Conclusion

The new Regulation imposes broad-ranging and exacting requirements on a wide range of market participants. It may reinforce the trend to discontinue benchmarks and reference prices and may result in some non-EU benchmarks becoming unavailable for use in the EU, restricting the range of hedging and investment products available in the EU. Market participants will need to create implementation plans to prepare for full compliance with the Regulation's requirements by 1 January 2018.

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Financial Markets Toolkit

Topic Guides | Financial Markets Resources | Our Financial Markets Experience | Presentations

Back to previous

In this section

- Alternative financing (shadow banking)
- Alternative Investment Fund Managers Directive (AIFMD)
- Bank finance – TLAC and MREL
- Bank Recovery and Resolution Directive (BRRD)
- Bank resolution in the Asia-Pacific region
- Banking Union
- Benchmark reform and regulation**
- Brexit
- China: market liberalisation
- Covered bonds
- Credit rating agencies
- Cross border insolvency
- EU legislative process explained
- European Market Infrastructure Regulation (EMIR)
- Euro area crisis and financial stability measures
- Execution: A guide to English law execution
- Fintech
- Margin for uncleared derivatives
- Market Abuse Regulation
- MIFID2 and MiFIR
- Prospectus Directive and Transparency Directive
- Sanctions

Benchmark reform and regulation

Topic Guides

Since the LIBOR scandal broke in 2012, interest rate, FX, energy and other financial benchmarks have remained in the regulatory spotlight. This Topic Guide looks at the UK reform of LIBOR and other benchmarks and examines proposals for further reform at the EU and international level, including the EU Benchmarks Regulation.

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Inside this Topic Guide

- Topic overview
- Clifford Chance contacts
- Key developments
- UK benchmark reform and administration
- EU benchmark reform and administration
- International benchmark reform and administration
- Other jurisdictions
- Clifford Chance briefings
- Clifford Chance presentations

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