FESE response to the European Commission consultation on the review of the EU Benchmark Regulation

Brussels, 23rd December 2019

Q1 - To what extent do you think it could be useful for a competent authority to have broader powers to require the administrator to change the methodology of a critical benchmark?

☒1 (not useful at all)

☐2

☐3

☐4

☐5 (very useful)

☐Don't know / no opinion / not relevant

Q1.1 – Please explain your reply to question 1

(2000 characters max)

The benchmark administrator is already required to have an oversight committee, and the competent authority already has sufficient powers in relation to the methodology of a benchmark. The methodology should remain a business decision of the administrator. In addition, there is already transparency on the methodology towards users.

FESE therefore does not consider that competent authorities should have broader powers regarding methodology modifications for critical benchmarks. On the contrary, we consider that this could create uncertainty for users regarding the continued provision of such benchmarks.

Q2 - Do you consider that such corrective powers should apply to critical benchmarks at all stages in their existence or should these powers be confined to:

a) situations when a contributor notifies its intention to cease contributions?

☐Yes

☐No

☒Don't know / no opinion / not relevant

b) situations in which mandatory administration and/or contributions of a critical benchmark are triggered?

☐Yes

☐No

☒Don't know / no opinion / not relevant

Q2.1 - Please explain your reply to question 2 a) and 2 b)

(2000 characters max)

The current framework and governance are appropriate

Q3 - Are there any other changes to Article 23(6)(d) BMR relative to the change of methodology for critical benchmarks that might be desirable to improve the robustness, reliability or representativeness of the benchmark?

☐Yes
☒No
☐Don't know / no opinion / not relevant

Q3.1 – Please explain your reply to question 3

(2000 characters max)

Please see answer to Q1

Q4 – To what extent do you think that benchmark cessation plans should be approved by national competent regulators?

☐1 (completely disagree)
☐2
☐3
☐4
☒5 (fully agree)
☐Don't know / no opinion / not relevant

Q4.1 – Please explain your reply to question 4

(2000 characters max)

We are asking NCAs to ensure that the cessation of a critical benchmark is conducted in an orderly fashion, without causing market disruptions and legal uncertainties. Approved cessation plans for critical benchmarks are therefore seen as an appropriate measure to ensure a reliable discontinuation process. For completeness we note that we do not propose that cessation plans should be approved in relation to any types of non-critical benchmark as we consider that this would be disproportionate (particularly given the requirement for administrators to consult in respect of proposals to cease providing a benchmark).

Q5 - Do you consider that supervised entities should draw up contingency plans to cover instances where a critical benchmark ceases to be representative of its underlying market?

☐Yes
☒No
☐Don't know / no opinion / not relevant

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Q5.1 – Please explain your reply to question 5

(2000 characters max)

Benchmark users consider the current supervisory and incentive structure of administrators of critical benchmarks as stipulated by the EU Benchmark Regulation as sufficient to ensure the representativeness of a critical benchmark of its underlying market.

Q6 - To what extent do you consider the system of supervision by colleges as currently existing appropriate for the supervision of critical benchmarks?

☐1 (not appropriate at all)
☐2
☐3
☐4
☐5 (very appropriate)
☒Don't know / no opinion / not relevant

Q6.1 – If you consider the system of supervision by colleges as currently existing not appropriate, what changes would you suggest?

(2000 characters max)

Q6.1 – Please explain your reply to question 6

(2000 characters max)

Q7 - Do you consider that it is currently unclear whether a competent authority has the powers to withdraw or suspend the authorisation or registration of an administrator in respect of one or more benchmarks only?

☐1 (very unclear)
☐2
☒3
☐4
☐5 (very clear)
☐Don't know / no opinion / not relevant

Q7.1 – Please explain your reply to question 7

(2000 characters max)

We believe the text is clear in the sense that an administrator can be suspended which will have an impact on all benchmarks provided by it. We believe the choice to suspend individual benchmarks will depend on the severity of the facts underlying the decision: if an overall governance issue has been detected which is considered severe enough to suspend the administrator, it will impact most or all of the benchmarks offered by the administrator. The question is whether policy makers wish to extend their supervisory powers to suspend individual benchmarks if they decide BMR is not complied with at that individual level. If there are no other means available to the NCA and if the NCA is of the opinion that users are impacted negatively, then this option could be considered. It may

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indeed be relevant to withdraw/suspend one or several specific benchmark(s) while allowing the administrator to continue the business in relation to other benchmarks. We would therefore support this proposal, but to ensure consistency in relation to any decisions to withdraw-suspend individual benchmarks are made consistently, the broad factors that will be considered in making these determinations should be set out in the BMR.

Q8 - Do you consider that the current powers of NCAs to allow the continued provision and use in existing contracts for a benchmark for which the authorisation has been suspended are sufficient?

☐1 (totally insufficient)
☐2
☒3
☐4
☐5 (totally sufficient)
☐Don't know / no opinion / not relevant

Q8.1 – Please explain your reply to question 8

(2000 characters max)

FESE believes the current powers for competent authorities are sufficient for authorised benchmark administrators. If a competent authority decides to withdraw an authorisation, one has to assume the reasons for the withdrawal has been considered serious enough to disallow the administrator to maintain its benchmark business.

We recommend that the Commission considers the addition of similar provisions when the recognition and endorsement of third country administrators in respectively Article 32 and Article 33 of the Benchmarks Regulation is suspended. For administrators it would be helpful to understand what conditions the regulator would consider applying in such situations, such as, what oversight, supervision or actions would be taken by the NCA when permitting the administrator to continue providing a benchmark for which authorization has been suspended.

Q9 - Do you consider that the power of competent authorities to permit continued use of a benchmark when cessation of that benchmark would result in contract frustration are appropriate?

☐1 (not appropriate at all)
☐2
☐3
☐4
☐5 (very appropriate)
☒Don't know / no opinion / not relevant

Q9.1 – Please explain your reply to question 9

(2000 characters max)

It is too early to have comments on this matter as it has not been possible to make such observations yet.

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Q10 - Do you consider that the regulatory framework applying to non-significant benchmarks is adequately calibrated?

☐1 (not well calibrated at all)
☒2
☐3
☐4
☐5 (completely adequately calibrated)
☐Don't know / no opinion / not relevant

Q10.1 – Which adjustments would you recommend? Please explain your reply to question 10.

(2000 characters max)

The calibrations as such are appropriate, but the overall compliance requirements are still disproportionate. For example, the requirement in article 26.3 to explain why one makes use of the calibrations seems unnecessary. The calibrated regime has been put in place after considerations of which requirements may not be necessary for non-significant benchmarks. Given such considerations have already been made, it seems disproportionate for each administrator to have to make such explanations again.

We believe that much of the governance and control requirements would not have to be applied to non-significant benchmarks, especially in cases where there are very little assets under management.

Q11 - Do you consider quantitative thresholds to be appropriate tools for the establishment of categories of benchmarks (non-significant, significant, critical benchmarks).

☐1 (not appropriate at all)
☐2
☐3
☐4
☒5 (completely appropriate)
☐Don't know / no opinion / not relevant

Q11.1 – Please explain your reply to question 11. If applicable, which alternative methodology or combination of methodologies would you favour?

(2000 characters max)

Q12 - Do you consider the calculation method used to determine the thresholds for significant and critical benchmarks remains appropriate?

☐1 (not appropriate at all)
☐2
☐3
☒4
☐5 (completely appropriate)
☐Don't know / no opinion / not relevant

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Q12.1 – Please explain your reply to question 12. If applicable, please explain why and which alternatives you would consider more appropriate?

(2000 characters max)

BMR categorises benchmarks as critical, significant or non-significant based on the value of instruments, contracts and or funds referencing it. This is specified in Delegated Regulation (EU) 2018/66 which outlines how the total value of financial instruments, financial contracts or investment funds referencing a benchmark should be determined. It outlines the methodology to be used for financial instruments, UCITS, derivatives and collective investment undertakings and a process to be used where amounts or values are not available or incomplete. However, it is only in the latter case where the administrator is using alternative amounts or data that the total amount can be calculated on "a best effort basis and to the best of its ability, based on the available data". FESE considers that the calculation should all be done on a best effort basis, regardless of the data sources i.e. this treatment should be provided for also for calculations according to Article 1-3, considering that calculation of thresholds is challenging even where mandatory data sources have been identified.

There are also issues for financial products like funds and structured products originating in third countries and available to EU investors as it is not possible to calculate the exact exposure in the EU, e.g. for structured products that have a primary listing in a third country but are redistributed by EU banks to their EU retail clients and where an index fund, has EU users although the asset manager does not market and distribute the fund in the EU. There is a lack of clarity whether the underlying indices can then be considered as benchmarks under BMR. A clarification in BMR or an RTS would be appreciated.

Q13 - Would you consider an alternative approach appropriate for certain types of benchmarks that are less prone to manipulation?

☐1 (not appropriate at all)
☐2
☐3
☐4
☒5 (completely appropriate)
☐Don't know / no opinion / not relevant

Q13.1 – If you would consider an alternative approach appropriate for certain types of benchmarks that are less prone to manipulation, please explain for which types.

(2000 characters max)

BMR applies to all benchmarks regardless of underlying market. But we believe different types of benchmarks pose different types of risks to the markets. From a global perspective – where many developments have taken place – IOSCO has recognised that benchmarks based on regulated data could be subject to a proportionate approach. BMR also acknowledged that regulated data benchmarks are less prone to manipulation. However, experience with its application has shown that the actual framework does not differ much from that of other types of benchmarks. There is also a lack of clarity regarding the definition of 'index' which we think has led to indices originally not intended to be in scope of BMR becoming regulated. 'Made available to the public' could therefore benefit from more guidance. Alternatively, the definition could be narrowed down, e.g. to refer to indices that are in widespread use within financial instruments / contracts. The definition of regulated data benchmarks could benefit from clarification related to third country regulated data. Currently, only data from EU trading venues and a limited

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number of commodity exchanges fall within the definition. There are exchanges in numerous jurisdictions which are not included. To clarify, the definition references equivalence decisions under Article 28(4) of MiFIR on the derivatives trading obligation and Article 2a of EMIR for OTC derivatives. It ignores equivalence decisions e.g. under Article 25(4) of MiFID II related to share trading obligations. This may be a reference error. By not recognising such exchanges as equivalent, a vast number of equity benchmarks cannot be classified as regulated data benchmarks. This may deprive EU investors from access to innovative indices and access to emerging markets. In addition, non-EU regulated data benchmarks may be deprived of the intended exemption from being deemed a 'critical' benchmark.

Q14 - To what extent are you satisfied with your overall experience with the ESMA register for benchmarks and administrators?

☐1 (not satisfied at all)
☐2
☐3
☒4
☐5 (completely satisfied)
☐Don't know / no opinion / not relevant

Q14.1 – Please explain your reply to question 14

(2000 characters max)

Users of benchmarks appreciate the efforts of ESMA to maintain a central register for benchmark administrators and third-country benchmarks. The overall experience has been satisfactory.

However, the register could become more user friendly (please see comments to Q15). We believe the link to the general website of administrators can be improved, in any case a link to the dedicated section on benchmarks would be useful.

Q14.1 – If you are not satisfied with your overall experience with the ESMA register for benchmarks and administrators, please explain how could the register be improved.

(2000 characters max)

Q15 - Do you consider that, for administrators authorised or registered in the EU, the register should list benchmarks instead of/in addition to administrators?

☐1 (completely disagree)
☐2
☐3
☐4
☒5 (fully agree)
☐Don't know / no opinion / not relevant

Q15.1 – Please explain your reply to question 15

(2000 characters max)

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We would support listing benchmarks instead of/in addition to administrators in terms of transparency. However, this should not impact the time to market for users of these benchmarks.

Currently, the information on benchmarks is available from ESMA on request, and we understand requests are indeed made frequently. FESE believes this information is valuable. Providing information on the benchmarks as a standard in the register would be more helpful, and we believe more efficient for all, than having to request it separately from ESMA's staff. We appreciate that this may result in large amounts of data on the ESMA register and to ensure that this is manageable, suggest that benchmarks could be listed at family level (where applicable) rather than individually.

We welcome the proposal to include the benchmarks of authorised and registered administrators in the ESMA register. Currently, it is not always entirely clear which registered/authorised administrator provides which benchmark. However, from the perspective of users of benchmarks, it is important to have a reliable source of information regarding benchmarks. As it is not always sufficient to only see the authorisation or registration status, an extension of the register with regards to the specific benchmarks of authorised and registered administrators would be beneficial for users of benchmarks. The extension of the register will be particularly valuable, if NCAs obtain the power to suspend or withdraw authorisation or registration of single benchmarks.

We would also flag that, owing to the obligation on supervised entities in article 29 of the BMR, it is important that the ESMA register lists EU benchmarks individually (at least at family level) to help these entities comply with their obligations.

Q16 - In your experience, how useful do you find the benchmark statement?

☐1 (not useful at all)
☒2
☐3
☐4
☐5 (very useful)
☐Don't know / no opinion / not relevant

Q16.1 – Please explain your reply to question 16

(2000 characters max)

There are currently overlapping requirements between information that should be included in the benchmarks statement and the provisions related to transparency of methodology. Clarification would be helpful to streamline procedures and simplify compliance with a view to assessing the need of the benchmark statement altogether as most information is already available via other means.

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Q17 – How could the format and the content of the benchmark statement be further improved?

(2000 characters max)

A template would be useful as it would help administrators better understand exactly which information is required and would allow users to better compare different statements.

Q18 - Do you consider that the option to publish the benchmark statement at benchmark level and at family level should be maintained?

☐1 (should definitely be removed)
☐2
☐3
☐4
☒5 (should definitely be maintained)
☐Don't know / no opinion / not relevant

Q18.1 – Please explain your reply to question 18

(2000 characters max)

We do not believe there is much added value in a separate benchmark statement. However, users often demand this information and therefore should the benchmark statement be maintained, we would support the approach to combine statements in a "family of benchmarks statements".

Q19 - Do you consider that competent authorities should have explicit powers to verify:

a) whether the chosen climate-related benchmark complies with the requirement of the Regulation?
☒1 (completely disagree)
☐2
☐3
☐4
☐5 (fully agree)
☐Don't know / no opinion / not relevant

b) whether the investment strategy referencing this index aligns with the chosen benchmark?
☒1 (completely disagree)
☐2
☐3
☐4
☐5 (fully agree)
☐Don't know / no opinion / not relevant

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Q19.1 - Please explain your reply to question 19 a) and 2 b)

(2000 characters max)

We strongly support the initiatives to incentivise sustainable investments and enabling the financial community to market these products in a comparable transparent fashion. However, we would caution against an approach that would introduce a control framework that could end up disincentivising sustainable investments considering that we are still in the early stages of moving capital towards a sustainable goal. Policymakers clearly recognised this, stating that the sustainable legislative framework should aim to incentivise investment. While we appreciate the need to create a level playing field and improve transparency whilst reducing possible abuse, we would see this as a staged approach. The new legislation that sets standards for low carbon benchmarks should be seen in this perspective.

We think it is important that investment managers are held to certain standards when designing new products so they meet the needs of customers, do not mislead customers and are transparent in what a climate-related benchmark tracks and how a product based on such a benchmark performs. If a benchmark offered by an authorized/registered administrator or endorsed/recognized third country administrator has been classed as a climate related benchmark, investors should be confident that the benchmark is compliant with EU regulation.

FESE's view is that the same approach to non-climate related benchmarks in investment products should be applied to the use of climate related benchmarks in investment products. It would discourage the development of products based on climate related benchmarks if investment managers and benchmark administrators were required to go through a verification process each time a new climate related product was requested by a client or launched by an investment manager.

Q20 - Do you consider that competent authorities should have explicit powers to prevent supervised entities from referencing a climate-related benchmark, if such benchmark does not respect the rules applicable to climate-related benchmarks or of the investment strategy referencing the climate-related benchmark is not aligned with the reference benchmark?

☒1 (completely disagree)
☐2
☐3
☐4
☐5 (fully agree)
☐Don't know / no opinion / not relevant

Q20.1 – Please explain your reply to question 20

(2000 characters max)

FESE does not agree with preventing supervised entities from referencing a climate related benchmark that does not meet the EU requirements for climate related benchmarks following from the Benchmarks Regulation. ESG related benchmarks are developed in line with the rules applicable in different jurisdictions and based on varying demand from customers around the world.

The usage of a benchmark that is not in line with EU rules for climate related benchmarks may be appropriate for the needs of a supervised entity and its customers. Restrictions on the usage of climate related benchmarks would reduce customer choice, and limit the offering of climate related benchmarks to EU customers.

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FESE, however, notes that there should not be any suggestion of customers being misled by information regarding a climate related benchmark or investment strategy referencing such benchmark, or not being advised in accordance with the applicable rules and regulations. In such cases, authorities have the powers to take action and using a climate related benchmark that does not meet the climate related benchmark rules and claiming that the investment strategy is aligned with EU rules on climate related benchmarks should be an offence.

Q21 - Do you consider the current conditions under which a commodity benchmark is subject to the requirements in Title II of the BMR are appropriate?

☐1 (not appropriate at all)
☒2
☐3
☐4
☐5 (completely appropriate)
☐Don't know / no opinion / not relevant

Q21.1 – Please explain your reply to question 21

(2000 characters max)

There is currently a lack of clarity between provisions for regulated data benchmarks and commodity benchmarks and how these overlap for benchmarks that fit into both frameworks.

FESE would see benefits in clarifying the provisions applicable for benchmarks which fit both in the category of commodities benchmarks, and the category of regulated data benchmarks (please also see comments to Q22 on the de minimis threshold).

Q22 - Do you consider that the compound de minimis threshold for commodity benchmarks is appropriately set?

☐1 (not appropriate at all)
☒2
☐3
☐4
☐5 (completely appropriate)
☐Don't know / no opinion / not relevant

Q22.1 – Please explain your reply to question 22

(2000 characters max)

The compound threshold for commodity benchmarks should at least be doubled. Especially in the commodities sector there are many niche benchmarks where these are used by a smaller number of users but for whom this benchmark is essential. Given the smaller circle of users, the business value is limited, and combined with BMR compliance costs, there is a risk that benchmark administrators will stop providing such benchmarks. There is also a risk that trading venues that are also administrators could find it challenging to launch new products going forward. This is because whilst liquidity in a product is developing, it is sometimes necessary for these venues to utilise data such as broker runs, which is potentially considered "contribution of input data". As a result, the indices produces in connection with these products would be subject to code of conduct obligations in the BMR. This in turn could have the unintended consequence of dis-incentivising the provision

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of input data, which in turn would add to the challenges of launching new products. FESE believes these would be unintended and negative consequences. The risks with the effects of raising the de minimis threshold are very limited, considering the smaller circles of use of these niche benchmarks.

Q23 - To what extent would the potential issues in relation to FX forwards affect you?

☐1 (not at all)
☐2
☐3
☐4
☒5 (very much)
☐Don't know / no opinion / not relevant

Q23.1 – If the potential issues in relation to FX forwards would affect you, how would you propose to address these potential issues?

(2000 characters max)

The existing FX derivatives at FESE exchanges are either physically delivered or based on an index that is already subject to the EU Benchmark Regulation. Market participants might, however, wish to have exposure to currency pairs, for which only non-deliverable forward in the form of cash-settled products can be set up. Many of these currency pairs have country, cultural or economic specifications that may only be covered by local benchmarks of third-country administrators. In order to be able to offer market participants non-deliverable FX forward contracts, exchanges would need access to the underlying FX spot rate as reference rate. Against this background, FESE would support sensible legislation which allows the use of FX spot rates for not fully convertible currencies as reference rates for non-deliverable forward contracts.

Q24 – What improvements in the above procedures do you recommend?

(3000 characters max)

We appreciate the different methods for how third country benchmark providers could bring their benchmarks into the EU. The reality shows that equivalence is not a real option and the recognition process sets up large hurdles due to the need for an establishment of a legal presence in the EU. The endorsement process would benefit, if the requirements could be described and defined in more details in BMR or via an RTS.

Additional information - Definitions

As benchmarks administrators, FESE members have encountered some issues in relation to the application of the BMR definitions. Considering that the review is taking place very early, we would appreciate the opportunity to provide detailed input regarding this at a later stage.

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