esma European Securities and Markets Authority

EBA European Banking Authority

# Final Report

ESMA-EBA Principles for Benchmark-Setting Processes in the EU

6 June 2013 | 2013/658

Date: 6 June 2013
ESMA/2013/658

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# List of acronyms

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| EBA | European Banking Authority |
| ESMA | European Securities and Markets Authority |
| IOSCO | International Organization of Securities Commissions |
| MiFID | Markets in Financial Instruments Directive |
| PRA | Price Reporting Agency |
| UCITS | Undertakings for Collective Investment in Transferable Securities |

## I. Executive Summary

### Reasons for publication

On 11 January 2013 ESMA and EBA published a consultation paper on Principles for Benchmark-Setting Processes in the EU (ESMA/2013/12). This Final Report sets out the final text of the Principles for Benchmark-Setting Processes in the EU (the "Principles").

ESMA and EBA have developed these Principles to address the problems in the area of benchmarks in the period until a potential formal regulatory and supervisory framework for benchmarks has been devised for the EU.

Although the provisions will be without binding legal effect they provide benchmark users, benchmark administrators, calculation agents and publishers and firms involved in benchmark data submissions with a common framework to work together and provide a transition path toward potential future legal obligations.

At the international level, IOSCO is in the process of establishing principles for benchmarks. EBA and ESMA worked towards an alignment of the international and EU-level principles.

### Contents

Section II sets out the feedback statement to the Consultation Paper (ESMA/2013/12) published by ESMA and EBA on 11 January 2013.

Annex I includes the opinion of the Securities and Markets Stakeholder Group on the Consultation Paper of 26 February 2013.

Annex II contains the full text of the final Principles.

### Next steps

ESMA and EBA plan to conduct a review of the application of the principles eighteen months after their publication, but may alter that timeframe should they deem it to be appropriate or necessary.

ESMA and EBA may revise the Principles in light of potential future EU regulations, material changes in market practices or the agreement of international standards pertaining to benchmarks.

## II. Feedback Statement

### Background

*Concerns of ESMA and EBA*

1. Financial market reference rates and their calculation procedures have come under close public scrutiny in recent years. Starting in 2009, authorities in jurisdictions such as the EU, the US, Japan, and others have investigated cases of alleged misconduct around the rate-setting of LIBOR, Euribor, and other reference rates. More recently, the first outcomes of the investigations at national levels, legal settlements between charged institutions and their supervisory authorities, as well as a mounting number of cases of private litigation have highlighted the scope and scale of potential manipulation of reference rate-setting mechanisms. A number of initiatives to reform reference rate-setting mechanisms have been launched across wide parts of the regulatory and supervisory communities as well as the financial markets.

2. ESMA and EBA are concerned about and take an immediate interest in this issue. First, the on-going investigations may point at serious flaws in the way inter-bank interest rate benchmarks are being set in the EU. Second, the use of these benchmarks is widespread in securities and other financial markets, and any abuse can have serious implications for market integrity and the credibility of reference rates in the future, with significant negative consequences for financial flows and activities in the EU and globally. Finally, and as a result, the outcomes of the on-going investigations may provide additional evidence supporting the need for legislative reforms regarding reference rate setting in the EU, and in their regulatory and supervisory capacities ESMA and EBA are ready to contribute to these reforms. A consistent and coordinated response is clearly desirable, and ESMA and EBA have worked closely with IOSCO and the European Commission to ensure that the Principles are closely aligned.

3. In that context, in order to fully understand the Euribor-EBF rate-setting process and its susceptibility to the risk of manipulation, EBA and ESMA also agreed to undertake a review of the Euribor-EBF process. The findings of the review are set out in the EBA-ESMA report (ESMA/2013/BS/2) which includes recommendations to the EBF related to the administration and management of Euribor. This review has contributed to the development of the draft principles proposed in this consultation paper.

*Other relevant workstreams*

4. ESMA and EBA have coordinated and aligned their work with the other work streams on financial benchmarks as undertaken at the European and international level. This consultation is not aimed at prejudging the outcomes of either of these work-streams.

5. At international level, IOSCO is in the process of establishing principles for benchmarks through the work undertaken by the Board Level Task Force on Financial Market Benchmarks constituted in September 2012 to identify relevant benchmark-related policy issues and develop global policy guidance and principles for benchmark-related activities of particular relevance to market regulators.[1] IOSCO published Consultation Reports on financial benchmarks in January and April 2013, and is expected to publish a set of principles[2]. IOSCO published principles for Oil Price Reporting Agencies based on the work undertaken by IOSCO Committee 7 on Commodity Futures Markets[3]. EBA and ESMA worked towards an alignment of the international and EU-level principles.

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[1] See the press release available at: http://www.iosco.org/news/pdf/IOSCONEWS250.pdf.

[2] See the Consultation Report available at http://www.iosco.org/library/pubdocs/pdf/IOSCOPD399.pdf and www.iosco.org/library/pubdocs/pdf/IOSCOPD409.pdf.

[3] See the Principles for Oil Price Reporting Agencies available at http://www.iosco.org/library/pubdocs/pdf/IOSCOPD391.pdf.

6. ESMA and EBA are also aware of the Bank for International Settlements' report entitled "Towards better reference rate practices: a central bank perspective – A report by a Working Group established by the BIS Economic Consultative Committee (ECC)" of 18 March 2013[4].

7. At the EU level, in July 2012 the European Commission put forward proposals to amend its proposals for a Regulation on market abuse[5] and for a Directive on criminal sanctions for market abuse[6] to ensure that any manipulation of benchmarks is clearly and unequivocally illegal.

8. On 5 September 2012 the European Commission published a Consultation Document on the Regulation of Indices ("A Possible Framework for the Regulation of the Production and Use of Indices serving as Benchmarks in Financial and other Contracts")[7] aimed at assessing how to improve the production and governance of benchmarks and verifying the need for any necessary changes to the legal framework in relation to benchmarks.

9. Finally, the European legislation on UCITS[8] contains provisions on the use of a subset of benchmarks, i.e. financial indices to which UCITS funds take an exposure. These rules have been complemented by the guidelines on Exchange-Traded Funds (ETFs) and other UCITS issues recently published by ESMA[9] which, among others, provide guidance on financial indices.

*General considerations on benchmarks*

10. The existence of a large number and spectrum of different benchmarks is broadly recognised. Benchmarks are used not only as a reference for financial instruments and transactions, but also to price a variety of non-financial transactions such as commercial contracts.

11. The range of benchmarks that are based on different asset classes is very broad and includes:

    — interbank lending and borrowing rates,
    — overnight index rate and borrowing indices,
    — swap indices,
    — credit benchmarks,
    — commodity indices,
    — currency benchmarks,
    — bond and equity indices,
    — strategy and investment indices, and
    — others, including but not limited to hedge fund strategies or financial parameters, such as volatility or correlation indices.

12. The range of inputs used to calculate the different benchmarks is diverse. The types of data used include actual prices or transaction values, bids and offers, surveys, auction price systems, quotes, market reports, and judgements. Some of these methods may naturally give wider discretion in the calculation of the benchmark to either the contributor of the data or the calculation agent or the administrator. Whenever transaction data are used, such data should be considered to be more objective and easily verifiable. Rate-setting mechanisms using estimated rather than transaction-based data may require more discretion and the estimate is more likely be more susceptible to conflicts of

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4 Bank for International Settlements, "Towards better reference rate practices: a central bank perspective – A report by a Working Group established by the BIS Economic Consultative Committee (ECC) and chaired by Hiroshi Nakaso, Assistant Governor, Bank of Japan", 18 March 2013, available at http://www.bis.org.

5 Available at: http://ec.europa.eu/internal_market/securities/docs/abuse/20120725_regulation_proposal_en.pdf.

6 Available at: http://ec.europa.eu/internal_market/securities/docs/abuse/20120725_directive_proposal_en.pdf.

7 Available at: http://ec.europa.eu/internal_market/consultations/docs/2012/benchmarks/consultation-document_en.pdf.

8 Directive 2009/65/EC.

9 ESMA/2012/474, available at: http://www.esma.europa.eu/system/files/2012-474.pdf.

interest and manipulation. The range of submissions is likely to have an impact on the level of representativeness of the benchmark.

13. The number of Benchmark Submitters contributing data to survey-based or panel-based benchmarks may vary considerably. This phenomenon is also common to transaction-based benchmarks, which may receive submissions from a limited number of market participants or from a broad number of submitters. Moreover, market liquidity itself (i.e. the number of executed transactions) may vary over time and by type of instrument and tenor.

14. Benchmarks include a variety of interest-rate benchmarks, but also market indices such as stock, bond, derivative market indices, or commodity market benchmarks, including raw material and oil markets. Especially in the case of market indices and commodity market benchmarks, methods of data collection and calculation are highly heterogeneous and vary widely. In addition, for a large number of these benchmarks the underlying data are obtained or the benchmark is calculated outside the EU, even if their use by market participants in the EU may be widespread.

**Responses received**

15. ESMA received 70 responses on the Consultation Paper (CP) on Principles for Financial Benchmarks published by EBA and ESMA on 11 January 2013. Responses were received from banks and banking associations (31%), index providers (24%, including Regulated Markets), asset managers (18%), and other types of market participants (27%).

*Definitions*

***Question 1: Do you agree with the definitions provided in this section? Is this list of activities complete and accurate?***

*Scope*

16. Whilst an initiative on benchmarks is broadly supported for interbank lending benchmarks, there were mixed opinions on whether other types of benchmarks, such as commodity, equity and proprietary benchmarks, should be covered by the Principles.

17. The main argument for this position is that for some of these benchmarks self-regulation is sufficient and that, whilst all benchmarks share some characteristics, there are also many features which differentiate them and make them more or less susceptible to manipulation. Some of the differentiating features stated are the nature of the underlying data (ranging from actual transaction data to subjective estimates), the origin of underlying data (ranging from prices publicly available on exchanges to voluntary contributions in over-the-counter (OTC) markets), whether the contributing data are already regulated (as for trade used for equity indices), the transparency of their methodologies and the degree of discretion applied in their calculation and the existence of inherent conflicts of interest in their provision.

18. While some respondents agreed with the definitions, most respondents indicated that the definition of benchmarks was too broad. Some respondents indicated that some indices should be excluded such as bespoke indices or equity and bond indices.

    **EBA and ESMA response:** The Principles should apply to all benchmarks that are covered by our definition with a view to ensuring a level-playing field among benchmarks and to ensure uniform protection of investors and consumers.

*Definition of Benchmarks*

19. Regarding the specific definition of benchmarks, some respondents claimed that international consistency on the definition is key and further alignment with IOSCO was needed. Some respondents also suggested that further clarification on the definition was needed.

**EBA and ESMA response:** The definition of Benchmarks has been modified to provide further clarity and has been aligned with existing definitions, such as the one put forward by IOSCO in its Consultation Report on Principles for Financials Benchmarks.

Definition of Benchmark Submitters

20. A few respondents argued that clarity should be provided on the definition of submitters and only firms that contribute data exclusively for the calculation of the benchmark should be considered. One respondent stated that more guidance should be provided on the criteria to qualify as a submitter.

**EBA and ESMAs response:** The definition of Benchmark Submitters has been modified by indicating that Benchmarks Submitters provide submissions that are used exclusively for the calculation of the Benchmark.

*Administration and administrator*

21. A few respondents called for the inclusion of a definition of a 'sponsor' which would be the entity that owns the Intellectual Property Rights of the benchmark and could be different from the administrator. A few indicated that 'person' should be replaced by 'legal person' or 'entity'. One respondent suggested that the definition of administration should also encompass the creation of the benchmark and its design. A few respondents argued that the definition of administrator was not fit for Price Reporting Agencies (PRAs) as it does not include editorial media functions.

**EBA and ESMA response:** The reference to legal person or entity and the design stage have been included in the definitions of Benchmark Administrator or Benchmark Administration. The definition of 'sponsor' as well as further amendments related to the specific features of some Benchmarks such as those produced by PRAs were not added as it was EBA's and ESMA's view that it would add a layer of complexity and would not be consistent with the definitions envisaged by other institutions such as IOSCO.

*Benchmark User*

22. Most respondents agree with the definition of users. However, for a few the definition was too narrow and considered it should include secondary users or refer to asset allocation instead of transaction, while others stated that the definition should only apply to professional users and not include market participants that use indices for reporting purposes. Another set of respondents claimed that users should not be subject to the principles.

**EBA and ESMA response:** The definition of Benchmark Users has been modified to focus on professional clients within the meaning of Annex II to Directive 2004/39/EC. The definition of Stakeholder has been added in order to ensure sufficient transparency by the Benchmark Administrator towards Benchmarks Users and Stakeholders (Principles A2, A4 and B8).

*Principles of good conduct for benchmark-setting*

***Question 2. Principles for benchmarks: Would you consider a set of principles a useful framework for guiding benchmark setting activities until a possible formal regulatory and supervisory framework has been established in the EU?***

23. A large majority of respondents indicated that they considered the set of principles necessary, useful or appropriate. Only a few participants indicated that they were against these principles, suggesting that

there was no need to "anticipate" any potential measures on the part of IOSCO or the EU Commission. A couple of other participants also expressed their belief that a formal framework was absolutely necessary to properly regulate benchmarks given the difficulty to regulate based on principles.

24. Among the supporters of the principles, a significant number of participants indicated their belief that early response and guidelines would help re-establish confidence in benchmark indices or address existing concerns. Some participants indicated that guidelines would be a useful interim or transitional regime to help "bridge the gap" until a formal legal framework is put in place; a few others seemed to favour a principle-based approach as a long-term solution, rather than a formal Framework. A couple of participants highlighted that benchmarks need to be resilient in times of crisis. The approaches suggested include creating new robust benchmarks even when liquidity dries up. Two respondents indicated that EBA and ESMA were correct in their mentioning that national supervisory authorities may not be able to exercise their activities based on simple principles, and that those principles should therefore be a means to achieve a harmonized framework.

25. A very large number of participants raised concerns over the principles, irrespective of whether they agreed with their establishment or not. These concerns can be regrouped under the following categories:

    a. Coordination with international standards: Many respondents expressed concern that interim principles could significantly differ from the shape of a final legal framework. Some of them urged EBA and ESMA to coordinate with the European Commission in order to provide continuity and consistency between the interim principles and the final framework; others called EBA and ESMA to follow the discussions on international standards at the IOSCO-level sometimes with the aim of reducing regulatory fragmentation. A couple of participants feared that the principles might result in increased compliance costs or risk duplication of market participants' efforts if were too different from the final framework, especially if the principles are binding. One respondent suggested that regional statutory requirements inconsistent with global standards could result in costs so high that some Benchmark Administrators may simply stop producing their Benchmark.

    b. Differentiation of benchmarks: In many answers, participants indicated that the current scope of principles was either too vague or too broad. Specifically, there seems to be consensus on the need to regulate, or at least reform, panel-based benchmarks such as EURIBOR and LIBOR, and two participants said that regulators should prioritise these. Several others highlighted the difference between panel-based and "market" or "commercial" indices, which do not suffer from the same inherent conflict of interest but rather need to remain transparent and reliable in order to remain competitive. The regulatory answer should therefore be calibrated proportionally to the risk posed by various categories of benchmarks, with some requiring direct supervision and others less burdening regulation. A few others highlighted that UCITS were unfairly burdened with heavy transparency requirements regarding the use of benchmarks that other benchmark users' were not subjected to. One respondent added that a level-playing field should be created by subjecting all benchmark-users to the same requirements rather than targeting a specific category of users.

**EBA and ESMA response:** Consistency with existing or emerging standards at international level is an important objective, and therefore ESMA and EBA have worked in close coordination with IOSCO. On the issue of differentiation, given the scope of the Principles it was decided not to design specific Principles that would be aimed at a particular category of Benchmarks. However, some differentiation has been achieved by restricting the definition of Benchmark Submitters to legal persons or entities that provide submissions that are used exclusively for the calculation of the Benchmark.

*A. General Principles for Benchmarks*

***Question 3: General Principles for benchmarks: Do you agree with the principles cited in this section? Would you add or change any of the principles?***

26. Overall, a large majority of respondents seemed to broadly agree with the 5 principles set out by ESMA. However, almost all the answers included some comments, either general or on specific principles.

27. Regarding general comments, the main points raised concern over 1) the scope of benchmarks to be affected by the principles, sometimes to highlight that the principles were not aligned with IOSCO's work on PRAs, and 2) the proportionality of new regulatory requirements, and the risk of burden for Benchmarks Users.

*Methodology*

28. There was a rich variety of comments on principle A1. Related to methodology. First, a majority of participants indicated their preference for "transaction-based" (or "market-based") prices where and when (i.e., depending on markets and frequency/availability of transactions) possible, rather than submissions by a panel of contributors. Many participants also added, however, that this principle was not applicable to all benchmarks due to the illiquid nature of some specific markets (e.g., high-yield bonds) and the associated volatility or capacity of single transactions to influence price fixture. In addition, several respondents highlighted the vagueness of the expression "sufficiently liquid"; they recommend keeping necessary "expert judgments" and/or algorithms (i.e., submissions) to complement transaction data.

    **EBA and ESMA response:** The Principle states that, where appropriate, actual market transactions should be used for Benchmark Calculations. The reference to sufficient liquidity has been replaced by a statement that the Benchmark should represent adequately the market, strategy or interest it seeks to measure.

*Governance*

29. Many submissions mentioned the fundamental problems posed by conflicts of interests; some indicated that these conflicts arise from the position of Benchmark Submitters as equally important market participants, and stressed the importance of submitters' ability to make discretionary decisions. Others highlighted the need to address conflicts of interest and a small number of answers acknowledged that it was not necessarily an easy task given the importance of having some experts with deep knowledge of the markets contribute to the benchmark-setting process; in specific cases, conflicts of interest could be tolerated provided that they are adequately controlled. The scope of benchmark regulation came to the fore once again as several respondents indicated that market, commercial and financial indices were not subject to such conflicts of interest; on the contrary, transparency, reliability and good governance are deemed necessary for these indices to remain competitive in the market. Governance requirements should therefore be proportionate, and based on the potential systemic importance of a benchmark. For those benchmarks that urgently require changes (i.e., panel-based Benchmark), codes of conduct, an independent administrator or an oversight committee were the solutions mentioned the most frequently. The definition of "independent" was deemed unclear by a few participants, with aspects such as remuneration or composition of the administrator/committee having the potential to create new issues and conflicts of interest if not carefully predefined.

    **EBA and ESMA response:** The principle has been amended to indicate that the benchmark setting process should be governed by independent procedures and governing processes should be established to reduce conflict of interest as much as possible. Where unavoidable, conflicts should be identified, disclosed and monitored.

*Supervision and oversight*

30. Reactions to the supervision principle were limited. Several respondents cautioned that regulation may overburden benchmark-setting, potentially disrupting or hampering market development, and that supervision was inadequate or unnecessary for certain categories of benchmarks that had not suffered reputational damage. Some participants also indicated that some benchmark users or benchmark underlyings were already under an existing regulation (e.g. UCITS or MAD/MAR) and there was no need to duplicate efforts in those sectors. Self-regulation was often mentioned as a reliable alternative. On the other hand, several respondents indicated their support for public supervision, especially for panel-based benchmark.

    **EBA and ESMA response:** The principle was maintained and a reference to existing EU legislation on Market Abuse was added.

*Transparency*

31. Concerns about the protection of Intellectual Property Rights were repeatedly mentioned, with warnings about the potential consequence of rights infringement on competition, trading strategies and the risk of stifling innovation. A number of participants also supported the need for clear methodology definition and transparency along with the importance of informing stakeholders of methodology changes, with some indicating their preference for an advance notice when such changes are made in order to allow for smoother Benchmark-User transition or adaptation. Publication of historical data and track record could also help to improve transparency. Finally, several responses suggested that a modest time lag in the publication of submissions could be justified in order to mitigate the impact on markets, especially under stress conditions.

    **EBA and ESMA response:** In order to support confidence in benchmarks, transparency is needed, especially on the rules governing the administration of the benchmark. Therefore, the Principles put strong emphasis on transparency. Transparency may be limited only in exceptional circumstances based on legal provisions safeguarding confidentiality and intellectual property rights.

*B. Benchmark Submitters*

***Question 4: Do you agree with the principles cited in this section? Would you add or change any of the principles?***

32. In general most respondents supported the principles and many stressed the importance of strong governance. While the principles are broadly supported especially for panel-based benchmarks, many respondents raised concerns over proportionate application and disproportionate costs of implementation which could discourage firms from contributing data. Some respondents suggested developing incentives for participation. Some respondents asked for recognition of different data processes since not all data are collected by active data submissions.

    **EBA and ESMA response:** While the Principles apply to all types of benchmarks the definition of Benchmark Submitter has been revised to include only submissions which are used exclusively for computing a Benchmark. To address concerns on adequate level of participating Benchmark Submitters ESMA and EBA inserted a principle for Benchmark Administrators to develop policies to discourage withdrawals from panels and surveys.

*Sharing data with the Benchmark Administrator*

33. Some respondents suggested including a requirement for submitting firms to provide the relevant underlying data of their submissions to the administrator if so requested by the administrator. It should be recognised, though, that submitting firms may not always be in a position to provide all data

due to confidentiality reasons but should comply with all reasonable requests to facilitate investigation of post-submission irregularities.

**EBA and ESMA response:** A Benchmark Administrator has the overall responsibility for quality and reliability. To enable the Administrator to exercise these controls, the principles were revised to include a requirement to share relevant data with the Benchmark Administrator to conduct post-submission controls.

*Conflicts of interests and submission controls*

34. Some respondents suggested following MiFID threefold approach to conflicts of interests (avoid, manage, disclose). Others noted that the principles should recognise that in some circumstances the most appropriate person to act as submitter may not be entirely free from a risk of conflict of interest. Some stressed segregation of duties and coverage also of manipulation of corroborative data that might subsequently be used to justify a false submission. One respondent supported more principle-based policies as a set of rules on collusion may be more difficult to enforce while it may be clearer whether or not a principles and ethos has been followed.

35. Several respondents noted that actual transactions are not always available and suggested to complement the principle to cover these situations. It was suggested to add a requirement on verifiable documentation of qualitative assessments for scrutiny by oversight functions.

**EBA and ESMA response:** While conflicts of interests should, as a priority, be avoided the principles now also cover management of conflicts of interests where they are unavoidable. The principles were assessed as being adequately high level and were not revised to be more principle based. Submission controls should be undertaken based on actual transactions, but, to cover situations where actual transactions data are not available, the relevant principle was revised to describe a process for controls based on verifiable information. The principle on submission controls was revised to cover situations where actual transactions data are not available.

*Confirmation of compliance*

36. Many respondents expressed concerns over legal liabilities towards general public on public confirmation of compliance and suggested deleting the principle or providing the confirmation to the relevant supervisory authority.

**EBA and ESMA response:** Benchmark Submitters should confirm their compliance to the Benchmark Administrator which should publicly disclose those confirmations.

*Clarifications, contingencies, whistle-blowing mechanisms*

37. Some respondents suggested covering data sourcing and transparent methodologies also for submitting firms.

38. Some respondents asked for clarification on some terms used (e.g. normal requirements, appropriate training, reverse transactions).

39. One respondent suggested supplementing the principle with a requirement to have in place a robust contingency provision for unavailability of the required delivery systems.

40. Some respondents assessed the principle on whistle-blowing policies to be disproportionate for small firms.

**EBA and ESMA response:** The principle on calculation criteria has been revised to cover data sourcing by Benchmark Administrators. In response to the feedback the used terminology has been

clarified in the Principles. Contingency provisions were added for all entities involved in the Benchmark setting process to ensure contingency through the process. The Principles should be applied in a proportionate way and a separate section on proportionality was included in the Principles.

*C. Benchmark Administrators*

***Question 5: Do you agree with the principles cited in this section? Would you add or change any of the principles?***

41. The majority of respondents supports the Principles and the focus on adequate transparency and independent governance arrangements. Many respondents object to the Principles and suggest focusing on panel based benchmarks and promoting industry code of conducts. Some respondents asked for differentiation among different kinds of benchmarks and especially ones based on actual transactions. Some respondents supported wide coverage of different kinds of benchmarks.

42. Some respondents stress the importance of a Benchmark Administrator being responsible for the whole Benchmark setting process. Some respondents were concerned over the cost impact of new regulatory requirements.

**EBA and ESMA response:** As stated above, the Principles cover all types of benchmarks. The definition of Benchmark Submitters has been reviewed to include legal persons or entities that provide submission that are used exclusively for the calculation of the Benchmark. The overall responsibility of a Benchmark Administrator on the quality and reliability of the Benchmark has been strengthened in the Principles.

*Independent governance*

43. Respondents in general supported increasing independence of oversight functions but some expressed concerns on availability of independent members for all small benchmarks and finding a balance between independency and adequate expertise of oversight function members. Some respondents suggested using "non-contributing" instead of independent. Some members questioned the need for disclosing names of members in governing bodies to wide public and suggested to provide them to relevant stakeholders.

**EBA and ESMA response:** Definition of independent members was clarified and emphasis was given to non-contributing members. For increased transparency the details of the oversight functions membership should be made available to the public.

*Methodology, transparency*

44. Some respondents raised concern that some benchmarks require a certain degree of judgement and that judgement should be limited only to the extent possible. Some noted that the focus should be on manipulation and conflicts of interests and not judgement itself. Some suggested including a hierarchy of contribution methods starting from actual transactions to judgement/expertise.

45. Several respondents expressed concerns about the requirement to fully disclose methodologies and proposed clarification that only for widely used benchmarks weightings and prices of components should be disclosed to the public. For other benchmarks it should be adequate to disclose to the relevant stakeholders. Some expressed concerns over different interpretations of "where this is not possible" creating a non-level playing field.

**EBA and ESMA response:** The methodology should include well-defined calculation criteria to limit judgement, qualitative assessments and other discretionary decision making. The principle on methodology has been reviewed to further clarify use of judgement and the related criteria where these are necessary for calculating a Benchmark. The general Principles and Principles for Benchmark

Administrators have been revised to provide more clarity on transparency and level of details that should be disclosed.

*Oversight and controls*

46. Some respondents stated that the oversight and control role over submissions does not fit for all different kind of entities acting as Benchmark Administrators. Respondents also argued that oversight of submissions is not relevant for benchmarks based on actual transactions.

47. Some respondents expressed concerns on possibilities of a Benchmark Administrator to ensure implementation of principles by Benchmark Submitters. Some expressed concerns on granting access to data to Benchmark Administrators. While overall responsibility of the Benchmark Administrator was supported, it was stressed that Benchmark Submitters also have responsibility for the quality of their submissions.

48. Some respondents asked for clarification for minimum record keeping period and posting of meeting minutes.

49. Several respondents noted that transactions data may not always be available and for these cases a requirement for plausibility checks should be included. One respondent suggested including a four-eye principle and one respondent a requirement for tightly and clearly defined and codified consistency checks agreed by the oversight body.

**EBA and ESMA response:** Requirements for Benchmark Submitters on record keeping and sharing relevant data with the Benchmark Administrator were strengthened to enable Benchmark Administrators to monitor quality of submissions. Minimum record keeping periods was clarified to be 5 years. Relevant minutes are required to be kept available for supervisory authorities upon request. The Principles now cover consistency and plausibility checks on the basis of actual transactions or other verifiable data where available.

*Review of benchmarks, outsourcing, whistle-blowing mechanism*

50. Respondents had different views on the necessity of regular reviews of benchmark products. One respondent asked to clarify “range of products” as sometimes a single benchmark can serve a single market.

51. Some respondents noted that outsourcing should be done via appropriate contractual and service level arrangements and that there should be predefined criteria for choosing the third party. One respondent noted that a Benchmark Administrator may not always have the instruments or the authority to audit a Benchmark Calculation Agent.

52. Several respondents assessed the requirement for a whistle-blowing mechanism as disproportionate and suggested to use for non-systemic benchmarks a complaints procedure. One respondent supported comprehensive arrangements for whistle-blowing at all stages of the Benchmark setting process.

**EBA and ESMA response:** The principles on outsourcing were revised to provide more details on access to data and contractual arrangements. The principles now also cover complaints procedures.

*Confirmation of compliance*

53. Several respondents were against public disclosure of compliance and raised concerns on legal character of such confirmation. Some respondents suggested providing confirmation to Benchmark Users upon request.

**EBA and ESMA response:** A Benchmark Administrator should disclose publicly confirmation of compliance with the Principles.

*D. Benchmark Calculation Agent*

***Question 6: Do you agree with the principles cited in this section? Would you add or change any of the principles?***

54. Most respondents support the principles and many stress the importance of a clear calculation method and administrator's control over the calculation agent. Some respondents notes that the processes and interactions with both the submitting parties (if any) and the administrator shall be duly documented and recorded so as to easily identify anomalies if required or needed by authorities. Those respondents objecting the principles argue that any future regulation should not be anticipated and that relations between administrators and calculation agents should be established by contracts or service level agreements.

55. One respondent asks for clarification if the Benchmark Calculation Agent should be a regulated entity while others note that several Calculation agents already are under supervision. One respondent suggested that an independent entity, private or public, be entrusted with the task of benchmarks' calculation agent.

**EBA and ESMA response:** The Principles are applicable to all entities independent of whether they are regulated or not.

*Controls and contact between Administrators and Submitters*

56. Some respondents question how a Benchmark Calculation Agent could perform any control pre-submission and some suggest applying proportionality and requiring pre-submission controls based on a benchmark's susceptibility to conflicts of interest and how widely it is used by market participants. One respondent stressed the importance of robust safeguards and controls in order to prevent any irregularities in the benchmark's computation.

57. One respondent suggests to further assess the possibility for an external oversight committee which would complement individual benchmark administrators in identifying, mitigating and managing potential conflicts of interests.

58. Two respondents suggested requiring record keeping of all relevant data related to computation and communication with Benchmark Submitters and Benchmark Administrators.

59. Two respondents stressed the need to include an overarching principle requiring the administrator to have the full and ultimate responsibility of the process even if it relies on outside parties for different functions.

60. One respondent suggested adding a requirement for active dialogue by providing feedback on the quality or any problems in submissions to the administrator and suggested improvements in the methodology of the calculation. A respondent also suggested naming individuals for communication with other parties.

**EBA and ESMA response:** The Principles were revised to cover robust pre- and post-computation controls to cover all controls before submitting a Benchmark fixing to a Benchmark Publisher. A Benchmark Administrator has the overall responsibility for the Benchmark setting process and that appropriate controls are implemented. The Principles now cover dialogue between Benchmark Submitters and Benchmark Administrators.

*Confirmation of compliance*

61. Many respondents expressed concerns over legal liabilities towards the general public on public confirmation of compliance and suggested deleting the principle or providing the confirmation to the relevant supervisory authority.

    **EBA and ESMA response:** Benchmark Calculation Agents should confirm their compliance to the Benchmark Administrator which should publicly disclose those confirmations.

*E. Benchmark Publisher*

***Question 7: Do you agree with the principles cited in this section? Would you add or change any of the principles?***

62. Most respondents support the principles. Some respondents objecting to the principles support tackling the issue by contractual arrangements with the Benchmark Administrator.

63. Two respondents suggested differentiating between primary (the source of the benchmark and can only be one for each benchmark) and secondary publisher (onward distribution) and that there should be arrangements that the primary publication should at least for the systemically important benchmarks be on a fair and non-discriminatory basis.

64. One respondent argued that where a benchmark is based on observable market transactions and transparent methodologies, there is no need to obtain confirmation from the administrator. Some others suggested that the administrator should confirm that procedures have been followed rather than the publisher actively seeking for confirmation for each publication. Some respondents suggested that confirmation should be done under a public agreement not requiring verification of each data, element or specific point in time.

65. One respondent suggested supplementing the principle with a requirement to have in place a robust contingency provision for unavailability of the required delivery systems.

    **EBA and ESMA response:** A Benchmark Administrator has the responsibility of quality and reliability of each published Benchmark and it should provide confirmation for published benchmark data. Contingency provisions were added for all entities involved in the benchmark setting process to ensure contingency through the process.

*F. Principles for users of benchmarks*

***Question 8: Do you agree with the principles cited in this section? Would you add or change any of the principles?***

66. Several respondents agreed with the proposed principles. One of these respondents encouraged considering not only immediate users of the benchmarks, but also the ultimate end users who buy benchmark-referenced financial products.

67. A benchmark calculation agent welcomed the inclusion of principles for benchmark users arguing that controls on the activities of submitters and administrators should not extend to prescribing the use to which benchmarks should be put.

68. A bank agreed with the principles, but asked introducing a proportionality element and clarifying that the principles apply to benchmarks used by a wide range of market participants, on which a wide range of products are based or that are prepared based on multiple contributions.

69. Two associations of financial market participants did not support the proposal that "users" should be among the participants covered by the proposed principles and argued that the principles should apply to those entities that participate in the production or distribution of benchmarks with overall the responsibility for any benchmark process (including integrity, transparency and governance) ultimately resting with the sponsor.

70. Several bank associations were of the opinion that the principles imposed on users were excessive and that benchmark users (in particular, according to some of these respondents, smaller players such as small and medium-sized credit institutions) are not in a position to comply with these principles.

71. A price reporting agency agreed that it could be appropriate to produce principles that guide regulated financial services firms on their use of benchmarks in financial markets, but recommended full alignment with the IOSCO PRA Principles for commodity markets. Two other respondents mentioned that market participants are typically well positioned to decide which benchmark best suits their needs.

*General principles – F.1*

72. Several respondents agreed that benchmark users should regularly assess the benchmarks they use and verify that they are appropriate, suitable and relevant relative to their targeted market. An academic body stressed that this requirement presupposes that index providers be required, on a complimentary basis, to clearly disclose the objectives of each of their indices along with the detailed metrics that allow for assessing the achievement of these objectives and the historical track record of these indices with respect to achievement of these goals. A bank association was of the view that administrators should clearly disclose changes to the methodology for rebalancing in order to allow users to assess the continued suitability and representativeness of each benchmark they use. Some investors' associations also mentioned that investors currently have extreme difficulties if they try to verify the quality of a benchmark (in terms of benchmark description, methodology and past performance).

73. Some respondents mentioned that the main responsibility for developing, calculating and dissemination of a benchmark should remain on the contributors, administrators and calculators of the data. A stakeholder argued that users should act with due diligence when making the decision to use a benchmark, but they shall not become responsible for any irregularity that the benchmark could experience over time, even though it could be proven that the irregularity already existed when the decision about its use was taken. Furthermore, several respondents argued that for futures or options that have benchmark underlyings, asset managers should be able to rely on the procedures of the market infrastructure that listed those instruments.

74. A respondent strongly objected to the requirement for a user to notify any potential irregularities to the administrator or the competent authorities.

*Supporting principles – F.2*

75. An academic body considered that regulators should ensure that enough information is provided to the market for users and other participants to conduct by themselves the mandated due diligence on the integrity of benchmarks.

76. An association of investment professionals considered the principle in F.2 inappropriate and unnecessary since it might imply an outsourcing of a third-party audit or verification function to users. This respondent argued that placing an additional requirement on users to check compliance is unnecessary and would do little to further strengthen the integrity of the benchmark. Similarly, some respondents considered the requirement impossible to comply with for benchmark users and argued that it should be the responsibility of regulators to verify that the benchmark administrator and the benchmark calculation agent comply with the applicable principles. Other respondents mentioned that it should be sufficient for users to rely on the confirmation, preferably in conjunction with a supervisor's certification.

77. A consultative committee of a public authority mentioned that in view of the principle under F.4, the principle in F.2 establishes an excessive requirement for users.

78. A respondent argued that it is doubtful if a benchmark user can ensure that the administrator complies with the principles and this is likely to cause an administrative burden on the administrator to issue confirmations to an unknown number of benchmark users. Another respondent was of the opinion that the responsibility for whether the benchmark is functioning properly should lie with the administrator.

79. An asset manager was of the opinion that the mere existence of a confirmation of compliance might just be counterproductive as it suggests transforming a diversified analysis into an administrative review of the existence of formal declarations.

80. An asset managers' association mentioned that when the benchmark administrator or calculation agent is located outside the EU it would be difficult (or impossible) for the user to comply with this principle.

81. Some respondents argued that the different roles of the end investor, the direct user and the index provider should be taken into account. These respondents mentioned that in several cases it would be the end users who would make the choice of the indices of the portfolios asset managers manage and, therefore, any review decision regarding benchmarks can only be taken by the end users or in coordination with them, but not by the asset managers alone.

82. An asset managers' association suggested rephrasing the principle in order to make it more proportionate. Another respondent equally suggested to replace the word "ensure" with "reasonable due diligence" in order to achieve similar results.

*Supporting principles – F.3*

83. A respondent agreed that benchmark users should develop contingencies for the unavailability of a benchmark within contracts referencing it. An asset managers' association was of the opinion that developing robust contingencies in the case a benchmark becomes unavailable is a preventive task that users are in the position to carry out, but it asked for clear guidance in this respect. Another asset managers' association argued that users who use an index for pricing a financial instrument need to implement robust contingency plans while those using the index in order to, for instance, benchmark performance of portfolios that they manage, would have less, or no, need to do so.

84. A consultative committee of a public authority agreed with the requirement to have contingency plans, but considered excessive that the plans should be applied in cases where benchmarks are not reliable, since this is a subjective matter and leads to a lack of precision as well as ambiguity.

85. An accountants' representative was of the view that contingency plans may be very difficult for benchmarks like LIBOR, which does not really have an equivalent replacement, and also if contracts referencing the benchmark do not allow for replacement.

86. Some bank associations mentioned that the principle proposed in F.3 is very far-reaching and would require a material assessment of the events which should be undertaken by a central body (ideally the administrator, possibly in consultation with supervisors), not by each individual user.

87. A stakeholder considered that the contingency's requirement would not be in the investors best interest if contingency plans need to include reference to contracts of contingency providers since the costs thereof ultimately will be borne by the investors.

*Supporting principles – F.4*

88. Some respondents considered the principle appropriate and suitable.

89. An academic body mentioned that sufficient transparency should be provided to the market to allow for independent replication of benchmarks by market participants with a view to controlling benchmark integrity and assessing the extent of discretion exercised by the index provider.

90. An association of investment professionals mentioned that the principles under F.4 was redundant with the general principle and could therefore be deleted.

91. A banks' association argued that any use of a benchmark should be considered thoroughly when the user establishes a contract or derivative based on that benchmark, but once the contract is concluded, the benchmark user cannot change the use of benchmark.

**EBA and ESMA response:** Given the support received from the respondents to this question, EBA and ESMA decided not to introduce any substantial amendment to the relevant principles. As for the request to introduce a proportionality element, EBA and ESMA recall that a reference to proportionality has been introduced in the principles (see also the answer to Q9 below) and this applies to all the Supporting Principles in the different sections of Annex II, including the principles for benchmark users. As for the request of increasing the level of transparency vis-à-vis the users of benchmarks, EBA and ESMA increased such transparency with the provisions under Principle A.4 in Annex II. Principle F.2 in Annex II was modified in order to provide that users should use sufficient due diligence to ascertain whether the benchmark administrator and calculation agent comply with the principles and should not be required to ensure that the benchmark administrator and calculation agent comply with the principles. A clarification was introduced under Principle F.3 in Annex II on the requirement applying to benchmark users using a benchmark as a reference for financial transactions or contracts to be entered into by its clients, or by itself on behalf of its clients.

*Adequacy of the principles to any benchmark-setting process*

***Question 9: Are there any areas of benchmarks for which the above principles would be inadequate? If so, please provide details on the relevant benchmarks and the reasons of inadequacy.***

92. Several respondents mentioned that there are no areas for which the principles would be inadequate.

93. An association of financial markets participants made the following comments for the enhancement of the principles: (i) the principles should be adapted to a benchmark's circumstances, including prioritization of application of the principles to more significant, widespread benchmarks, rather than the entire universe of benchmarks, and (ii) the goal of compliance with the principles could be alternatively be achieved through a number of means other than the key benchmark participants certifying their compliance with the principles. Several respondents similarly mentioned that the proposed principles could not be adequate for all of the wide range of benchmarks currently existing and that, therefore, some proportionality should be introduced.

94. A respondent noted that the proposed principles are largely focused on the issues relating to the LIBOR and in many instances are inapplicable and contrary to the way equity benchmarks are calculated. Furthermore, this respondent expressed a specific concern relating to the provisions on the fair and open access to benchmark information since this challenge national intellectual property rights laws and conventions.

95. An investors' association was of the view that when a benchmark is the performance of a single instrument or a composite of few instruments, many of the described principles are not accurate or easily implemented.

96. A bank association mentioned that the proposed principles will raise considerably the cost of quoting reference rates.

97. An asset managers' association argued that only market or strategy indices which are created for a large number of users should be in the scope of the principles.

98. A respondent argued that there are only very few products for which liquid markets exist and was of the opinion that moving to a mandatory transaction-based system would create greater reliance on market models which would most certainly be more systemically and morally hazardous. Two other respondents argued that basing future benchmarks on actual transactions could be problematic since unforeseeable events may lead to transactions no longer occurring for an extended period of time or being too little to serve as a reliable basis for the benchmark.

99. Two banks' associations mentioned that the requirements applying to publishers and users are inadequate and unjustified by the past experience.

100. An asset managers' association and an asset manager recommended coming to a common view at an international level on many questions that have been raised and discussed by IOSCO.

101. As for commodity market benchmarks, a price reporting agency stressed that the proposed principles would be inappropriate and recommended not to take any step that could disrupt the IOSCO PRA Principles process. Another respondent considered that a self-regulated code of conduct, in line with the provisions of principles, such as those defined by IOSCO, supported with an annual external audit, provides the appropriate degree of oversight for this kind of benchmarks.

**EBA and ESMA response:** EBA and ESMA saw merit in introducing a reference to proportionality with reference to all the Supporting Principles in the different sections of Annex II, in the understanding that the general principles (i.e. those under Section A and the headings General Principles in Annex II) should apply to all benchmarks in the same manner.

The Principles are – as far as possible at this stage – aligned with the principles that IOSCO is in the process of developing. ESMA and EBA may revise the principles in light of, inter alia, the agreement of international standards pertaining to benchmarks. Furthermore, EBA and ESMA saw merit in clarifying that the principles are without prejudice of the IOSCO Principles for Oil Price Reporting Agencies – Final Report.

*Legal continuity*

***Question 10: Which principles/criteria would you consider necessary to be established for the continuity of benchmarks in case of a change to the framework?***

102. The large majority of respondents considered that, in order to minimise market disruptions, sufficient time should be allowed for the implementation of any change to the framework.

103. A European public authority mentioned that, should EBA and ESMA decide to foster extensive changes to the reference rate production methodologies, they should also design a robust transition regime that would mitigate the operational and legal risks and protect the rights of affected contractual parties in a transparent and predictable manner. The same respondent recognised that specific legislation may be needed at both the EU and national level to define such transitional arrangements and safeguard continuity of contractual parties' rights and obligations under existing contracts.

104. Two respondents were of the opinion that any transition process must be smooth and implemented in such a way as to minimise the impact, including the legal and financial implications, to all classes of market participants, including benchmark users.

105. A banks' association asked to apply the principles in the CP to new benchmarks only. Another respondent similarly mentioned that for the indices currently in use, an effort should be made to

maintain their original definition and the characteristics of the market they are expected to represent and old indices should remain available until no contract, product or instrument is any longer referenced to the old indices.

106. Some respondents argued that to procure a legally binding and enforceable replacement of an existing benchmark or a materially altered benchmark would require the identification and subsequent amendment of all agreements and/or replacement of financial instruments containing the (direct or indirect) reference to the benchmarks in question. A stakeholder also mentioned that identifying all legacy contract participants will present a significant practical challenge. Therefore, several respondents mentioned that any replacement or amendment would require an extended transition period during which it will be necessary to ensure the continuation of any existing benchmark.

107. A bank association mentioned that the continuity issue goes beyond the ability of single market participants to ensure and suggested to establish a standing panel for each benchmark that would have the right to decide on the succeeding benchmark with subsequent universal application.

108. Some respondents mentioned that in case of changes or transition particular attention should be paid to ensuring minimum disruptions and time flexibility for market participants to reshape contractual arrangements.

109. Some stakeholders were of the opinion that to facilitate continuity, in case of changes to the methodologies and procedures of an index/benchmark, all stakeholders should be involved in a consultation process before any changes are implemented. Similarly, another respondent argued that any changes to the calculation methodology should be debated and agreed through the benchmark's oversight committee and, if the committee so recommends, further input should be sought via user consultation.

110. A bank association mentioned that if the basic benchmark framework is changed fundamentally, many derivatives and other contracts will lose their legal basis and will have to be terminated or renegotiated.

111. A respondent considered that a distinction should be made between cases of the transfer of an existing benchmark to a new benchmark administrator and the transfer to a different benchmark that is provided by a competing benchmark administrator.

112. An asset manager suggested taking into consideration whether rate benchmarks are used as a purely indicative or explicit rates to calibrate the performance of a fund and it warned that in case of benchmarks used as explicit reference rate, a move away would be more problematic as there would be significant economic impacts in connection with any contractual shift.

113. Two associations of financial markets participants recommended minimising the impact of the proposals to already issued financial instruments, particularly benchmarks that are extensively used.

114. A bank mentioned that continuity requirements should only apply to those benchmarks on which a wide range of products and users depend.

115. A benchmark calculation agent mentioned that for existing contracts in derivative markets the onus is on users and their representatives first, to ensure that the use to which a benchmark is put is appropriate, and second that, if that changes, contracts are sufficiently flexible to accommodate transition to whatever alternative the parties to the contract consider most appropriate.

116. Two respondents highlighted the importance to ensure that sufficient time is allocated to adjust, migrate away from, or terminate an existing benchmark in order to avoid market disruptive consequences and undue burden for market participants.

117. A price reporting agency mentioned the competitive environment within which price reporting agencies operate and recalled that it is usual for a range of alternative price assessment series to be available from different price reporting agencies for any particular commodity.

118. A couple of respondents mentioned that a change of index and transition to a substitute index should be authorised, but not imposed by the regulator. These respondents argued that it may be appropriate to include a clause in the documentation whereby counterparties agree to either close the contract or change reference if necessary or simply suitable to both.

119. An index provider was of the opinion that both a significant early announcement and – in the case of larger adjustments – a staggered execution are good means to implement larger changes with minimal distortion. Another index provider argued that a change in the framework as foreseen in the CP could cause significant market disruption in that investors may not have robust information available to them, or the underlying interest in financial products could become uncertain.

120. A respondent argued that since there is a wide range of different interest rate benchmarks which is available to the market, appropriate standards and requirements for all interest rate benchmarks should be set, but it should be left to the market to decide which benchmarks to use in practice.

121. A banks' association mentioned that the continuity of a benchmark could be threatened if a sufficient number of submitters are no longer willing to contribute to the benchmark setting process.

**EBA and ESMA response:** To the extent that the Principles in Annex II are by their nature "principles", EBA and ESMA did not consider necessary to introduce any transitory measure for the application of their principles. The provisions to follow in case of contingency by the different actors involved in the benchmark-setting process were streamlined in the new Section G of Annex II.

# Annex I – Opinion of the Securities and Markets Stakeholder Group

## ADVICE TO ESMA

### Benchmarks/Indices

#### I. Executive summary

Indices are fundamental because they may underpin an investment strategy, serve as underlyings or even reflect the state of an economy. The competitive environment in which index providers operate means that indices have been refined over time to take advantage of improvements and offer better choice for users. Nevertheless, these should be underpinned by universally agreed principles of good governance, sound methodology and transparency, in order to provide investors with the adequate level of protection and to limit risks of conflicts of interests and manipulation.

To this end, the members of the Securities and Markets Stakeholder Group (hereafter referred to as "the Group") welcome ESMA and EBA's Principles, which will provide for the "interim" regulatory framework needed prior to the application of more binding requirements through, notably, the revised Market Abuse Directive and the forthcoming Benchmark Regulation. In addition, the Group members believe that the proper enforcement of existing product regulations, which indirectly provide a framework for indices and benchmarks used in certain financial instruments (such as the Prospectus Directive and UCITS) at national levels should be encouraged.

In terms of scope, the majority of the Group believes that, contrary to ESMA and EBA's suggestions, the Principles should apply both to widely used benchmarks and indices and to strategy and proprietary indices. To this end, a "one-size-fits-all" approach should be avoided. The Principles should leave indices and benchmarks providers with the ability to choose between two main approaches: (i) a governance-based approach (where the processes in respect to the setting and calculating of indices and benchmarks should be supervised by independent third parties) or (ii) a transparency-based approach (where firms would have to disclose to regulators and their clients clear information about the methodology and data used to calculate the index or benchmark). Whichever approach is adopted, it should be made public.

In terms of information source, the Group members believe that the Principles should draw a clear hierarchy between the different sources of data (transaction prices, quotes, surveys), and should encourage particular care to be given to the liquidity of the markets on which indices and benchmarks are based, in order to limit distortions and manipulations.

The Group members consider that user information should be encouraged. In particular, access to indices' and benchmarks' past performance should be made easily and freely available to individual investors and borrowers. However, a proper balance should be maintained between, on the one hand, the need for a sufficient level of transparency, and, on the other hand, the need to protect intellectual property (IP) rights. In order to protect IP rights, which are crucial to the economic value of indices and benchmarks, and to ensure that these Principles do not put EU index provider at a competitive disadvantage in

comparison to other providers operating on a global level, ESMA and EBA should attempt at further coordinating with other national regulators, at the international level.

The Group members believe that in the near future direct supervision of indices and benchmarks by EU regulatory authorities should be encouraged, notably in respect to the governance arrangements in place at the level of the index provider, as well as in respect to the data and methodology used to calculate the indices.

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## II. Summary of ESMA SMSG discussions on benchmarks

1. The Group members decided that given the short deadlines, it would be preferable to concentrate on giving high-level advice rather than responding to ESMA/EBA consultation. The questions from ESMA focus on the following issues: scope, who should be captured, what activities should be subject to regulation and/or oversight, how would this impact the users and the continuity of indices.

2. Based on the discussions in the Group, the SMSG advice is structured as follows:

### Scope and definition

3. The original purpose of indices was to be a barometer of stock market performance. The compilation of information is useful for price information as it reduces the cost by allowing parties to share research. Indices are compiled from different sources including:

   - Censuses – e.g. GDP, retail price index
   - Traded prices on exchanges – e.g. FTSE 100, Euro STOXX 50, CAC40
   - Off-exchange real-time tradable prices – e.g. EuroMTS government Bond Index
   - Estimates and quotes – e.g. EURIBOR, LIBOR

4. Typically, an "index" is an aggregation of market data of financial instruments or acquirable assets which are used either as a basis for financial products ("underlying") or to evaluate financial investments ("benchmark"). Although provision of information was the primary reason for establishing the first indices, today's prominent and well-known indices usually fulfill three main purposes often simultaneously, namely:

   (i) as a benchmark for the risk and performance assessment,

   (ii) as an underlying for tradable investment products and

   (iii) as aggregated information to the public and investors.

5. The Group members believe that ESMA and EBA, for the purpose of the proposed Principles, should ensure that the definition of indices and benchmarks used is consistent with other regulations. To this end, the Group members encourage ESMA and EBA to adopt the same definition as the one recommended by the European Commission in its September 2012 Consultation Paper, according to which a "benchmark" means "*any commercial index or published figure calculated by the application of a formula to the value of one or more underlying assets or prices, including estimated prices, interest rates and other values, or surveys by reference to which the amount payable under a financial instrument is determined*".

6. Such definition would enable to exclude pure macroeconomic indicators describing the state of an economy, as these are not directly tied to any financial instrument, and are usually only used to achieve a clearer picture of the current economic environment. However, it would be comprehensive enough to include the two main existing types of indices and benchmarks:

    (i) *Widely used "public" benchmarks and indices*. These include indices that are broadly recognised and used, such as the ones produced by exchanges, but also interbank interest rates such as LIBOR and EURIBOR.

    (ii) *"Proprietary" and "strategy" indices*. Characteristically the purpose of these indices is to reflect individual trading strategies of the index provider. They therefore tend to be much more bespoke than widely used "public" benchmarks and indices.

7. In fact, whilst certain Group members consider that " proprietary" or "strategy" indices should not fall under the scope of these Principles, the majority of the Group members agrees that these indices, similarly to benchmarks, should be covered by high standards in terms of governance, transparency, and methodology for calculation, and therefore fall under the scope of the Principles. This is because even the most bespoke proprietary indices can be used in retail products such as mortgages for instance.

**Two alternative approaches: governance-based approach and transparency-based approach**

8. In order to improve investor and user confidence, the Group members believe that the adoption of Principles in terms of governance and/ or transparency is key. In fact, the setting of benchmarks and indices, as demonstrated by the recent LIBOR and EURIBOR cases, may give rise to important risks of conflicts of interests. These conflicts may materialize when the same entity undertakes the calculation of indices / benchmarks while, simultaneously, creating products based on the benchmark and index and holding trading positions in these products, thereby rendering it directly interested in the evolution of the benchmark or index. Risks of conflicts of interests may also arise when entities combine different activities, such as exchanges. However, exchanges, as some of the Group members pointed out, appear to be more neutral entities in respect to index provision, as they do not take any position or enter into risk hedging activities in respect to the indices they create.

9. Therefore, the majority of the Group members agrees that all indices and benchmarks should be covered by the Principles. However these Principles should be flexible enough to meet the particular constraints faced by benchmarks and indices providers and avoid resulting in disproportionate costs. To this end, the majority of the Group members believes that indices and benchmarks providers should be given the ability to choose between two alternative regulatory approaches in the Principles.

    (i) *Governance-based approach*. This approach would require indices and benchmarks providers to have in place sound governance mechanisms for the setting and calculation of benchmarks and indices, notably via the monitoring of the related processes by independent third parties. This would be ensured by requiring an independent committee to oversee the production of indices and benchmarks. The composition of such committee should be set in such a way to avoid one constituency to be favoured over another, by, for instance, requiring representatives of issuers and investors to be included as members. Independent committees should ensure that rules and due processes are followed including dialogue with clients, stakeholders and regulators. They should be responsible for approving and vetting the rules governing the processes for benchmarks and indices setting, and oversee these processes on the basis of sound principles and subject to an audit trail. If these fundamental principles are not guaranteed, the index should not be

allowed to be linked to contracts such as mortgages, ETFs, UCITS, etc. In addition, and notably in the case of indices created by exchange, third parties should ensure that decisions on the composition of the index are made in accordance with a process giving the companies part of the index or which could be expelled from the index the possibility to be heard. Ideally there should be regulatory oversight of these principles. In the case of indices based on quotes rather than trade information, the role of this independent committee would be particularly important to ensure that a framework is in place for the submitting entities.

(ii) *Transparency-based approach*. Under this approach, indices and benchmarks providers would be required to disclose to regulators and the providers' clients the methodology used for the calculation of benchmarks and indices as well as the sources of data used, in order to enable the external monitoring of the setting of those indices and benchmarks. This approach would meet the constraints faced by some indices and benchmarks providers, who do not necessarily have the internal resources needed for the intervention of the third-parties mentioned in alternative (i), and avoid disproportionately increasing their cost-base (which would ultimately be passed on to end-users in the form of higher fees) while still ensuring that these providers are subject to external monitoring.

10. In order to ensure that regulators and users are made aware of the regulatory approach chosen by the index / benchmark provider, the Group members believe it is necessary for the Principles to encourage the indices and benchmarks providers to publicly disclose the approach chosen. This could be achieved by adding a flag to the indices and benchmarks corresponding to the approach retained. This would enable users and regulators to identify the indices and benchmarks for which no third-party is involved, and therefore encourage them to monitor with particular care the disclosure made by the related providers.

**Information sources**

11. Regarding information sources, the Group members expressed divergent views on the use of quotes versus trade data. However, generally the Group members were of the opinion that it is preferable to base an index on real prices and real liquidity as otherwise, the index was more prone to manipulation. However, although anchoring a benchmark by observable transactions is ideal, it is not always possible. There was also a problem for submitting entities to quote prices when there was no information available on transactions.

12. The proposed MiFID review, which is currently being discussed at EU level, may improve the trade data available for non-equities, in particular for fixed income products. However, certain indices and benchmarks may require the use of other data. In fact, three different types of data sources are usually differentiated (as it is the case in IOSCO January 2013 Consultation Report). The Group members generally believed that these data should be classified in accordance with the following hierarchy:

(i) *Publicly available transaction and trade data*. Traded prices or firm quotes sourced from a liquid and regulated market. Traded prices from a regulated market do not require explicit explanations. A relevant example would be equity indices like the EURO STOXX 50, CAC 40 or the DAX being calculated with the traded prices from the leading locally regulated exchanges in Europe. Firm quotes from regulated markets are defined as being executable at all times. An example of the usage of firm quotes is the process for including new components in the eb.rexx fixed income indices, where binding ask prices from the regulated Eurex Bonds platform are used.

(ii) *Any other indicative pricing which could be non-firm quotes or estimates obtained systematically or randomly*. An example would be the LIBOR. However, indices for market segments currently dominated by off-exchange trading resulting in non-transparent pricings also fall into this category. One prominent example would be many fixed income indices (if they are not based on traded prices).

(iii) *Any other data may also be used as a basis for the other informational instruments*. Those figures might be obtained by surveys, statistical census or individual measurements. Examples here are unemployment rates, inflation rates or consumer sentiment data. In principle, there is no limitation for any such figures.

13. Where surveys are used, such as in the case of interbank interest rates, the Group believes that ESMA and EBA Principles should be consistent with CFTC's guidelines10 which set the following hierarchy:

(i) Bank's borrowing or lending transactions observed by the submitter

- Transactions in the market;
- Transactions in other markets (unsecured funds);
- Transactions in related markets (foreign current forwards, repo, etc.).

(ii) 3rd party transactions observed by bank's submitter

- Transactions in the market;
- Transactions in other markets (unsecured funds);
- Transactions in related markets (foreign current forwards, repo, etc.).

(iii) 3rd party offers observed by bank's submitter

- Transactions in the market;
- Transactions in other markets (unsecured funds);
- Transactions in related markets (foreign current forwards, repo, etc.).

14. In addition, the Group members encourage ESMA and EBA's Principles to highlight that not only the source of the data should be considered as important but also the quality of those data. As a general rule indices and benchmarks should, as much as possible, be based on liquid products, in order to limit the scope for distortions or manipulations. Providers should therefore be required to give due consideration to the liquidity of the underlying when creating indices / benchmarks.

15. Furthermore, whilst data originating from electronic transactions duly published raise little risks in terms of conflicts of interests, on the contrary data originating from surveys or OTC transactions, not necessarily subject to a strict regulatory framework in respect to disclosures and publications, may be more prone to risks of conflicts of interests and manipulation, as demonstrated by the recent LIBOR and EURIBOR cases. As such, the Group members believe that the Principles should include appropriate rules requiring entities to manage the risks of conflicts of interests that may arise when calculating indices or benchmarks on the basis of data collected through surveys or OTC transactions.

**Users and access to past performance**

16. The Group members understand that the "Users" section of the Consultation Paper does not target end investors and borrowers but only financial professionals. The Group members believe that ESMA

[10] http://www.cftc.gov/ucm/groups/public/@lrenforcementactions/documents/legalpleading/enfrbsorder020613.pdf

and EBA should spell out the definition they use of "users of benchmarks", and enlarge its scope, as end investors and borrowers are indeed users of benchmarks and indices, and their needs and protection must be taken into account when designing rules, guidelines and principles on benchmarks-design.

17. In fact, indices are used across many applications both by the buy side and the sell side for investment and trading purposes. Consumers are directly and indirectly impacted by benchmarks as retail investors and as borrowers. For instance over 90% of mortgages in several EU Member-states are referenced on LIBOR or EURIBOR. In that context, the Group members pointed to the fact that the further development and improvement of LIBOR was a politically sensitive issue. It was also pointed out that it is important to take into account the fact that LIBOR in particular is widely used outside of Europe. 50% of assets are quoted and monitored out of the USA primarily by asset managers. The Group members pointed out that there was an increasing 'retailisation' of the use of indices.

18. Consumer representatives Group members stated that it is necessary for investors to have the ability to access the information on the past performance of the index. Whilst in general the Group members believe that all types of users should be given the means to understand indices and benchmarks, some Group members believe it is necessary to highlight that there is very little access of retail investors to retail products benchmark's past performance. Retail investor associations found examples of indexed UCITS - reported to the national supervisor and to the European Commission11 – where the index's past performance is either missing or wrong. The issue is compounded by the fact that it is often impossible for the retail client to verify the accuracy of many major index/benchmark's past performances as they are not published and freely accessible to retail clients, especially by the index providers themselves (including world leading equity and fixed income index providers). Besides, there is no mention or ineffective mention of where to find such data in the KIID.

19. The Group members agreed that the Principles should require benchmark provider's clients to be granted access to data on past performance as well as to the methodology used to calculate these indices and benchmarks.

**Intellectual property rights**

20. The publication of an index is a complex process which implies the collection and selection of data, the calculation, the checking of information and the distribution of data. In fact, indices are the result of significant investments in the making and maintenance of the underlying database. Index providers continuously invest significant financial and operational resources and know-how in the creation and maintenance of their indices, obtaining and cleansing the raw financial data, periodic reviews according to the applicable criteria, provision of real-time calculation IT infrastructure and monitoring.

21. Intellectual property rights allow the producers of indices to extract economic value from putting indices together. Indeed, indices are subject to multiple intellectual property rights, including, but not limited to copyrights, data base protection rights, trademark rights, trade secrets etc.. Such rights are, inter alia, enshrined in Article 17(2) of the Charter of Fundamental Rights of the European Union. The intellectual property rights guarantee that index providers can autonomously decide which data will be published and which is restricted or only available under licenses.

22. The majority of the Group members believes that the transparency requirements as currently described in the Consultation Paper could be too far reaching. Such requirements should avoid depriving independent index providers of their IP rights and their investments by requiring them to

[11] see for example EuroFinUse reply to the EC consultation on the regulation of indices

disclose virtually all information in connection with the constitution of their indices. From a political perspective such clauses would contravene longstanding ambitions of the EU to provide for an efficient protection of IP rights as a source of innovation, growth and economic dynamics in Europe. There is, in addition, a significant risk for ill-defined transparency requirements to result in an un-level playing field between, on the one hand, EU entities falling under the scope of such requirements and, on the other hand, other entities not covered by the same transparency rules which would have the ability to use the information disclosed by the former to replicate their indices and benchmarks.

23. Therefore, whilst the Group members acknowledge that transparency is a crucial policy goal and that protection of IP should not in any circumstances serve as an excuse to prevent users from getting crucial information, a balanced solution between the need for increased disclosures in respect to indices and benchmarks and the protection of IP rights is required.

24. Such a solution could be achieved through greater coordination between ESMA and EBA and other regulators, at the international level, in order to ensure that all index and benchmark providers are covered by similar transparency requirements across the world.

25. The recognition of those rights should not prohibit investigations by regulators regarding the implementation and enforcement of the Principles.

**Continuity of indices**

26. Once an index is created and is embedded in existing contracts, there is a long-term interest in the continuation of the index from a user perspective. The Group members agree that there is therefore a strong interest in the continuation of the current indices, both for borrowers and investors, both at the index level but also at the benchmarked product level (e.g. when the fund managers switches from one index to another).

**Regulation**

27. Some Group members consider that indices and benchmarks are already indirectly regulated through product regulation such as the Prospectus Directive, UCITS Directive and ESMA's Principles for UCITS. However, other members pointed at the fact that indices regulation through product regulation greatly varies in the EU. Certain countries, such as France, monitor closely the indices used as underlying for certain financial instruments, but this practice is not necessarily widespread across member states. The Group members agree that proper enforcement of existing product regulation should be encouraged in the EU. Notably, correlation between product stocks and indices disclosed as underlying or as serving as a benchmark for performance should be ascertained and controlled by regulators.

28. However, relying only on product regulation does not appear as sufficient to ensure that indices and benchmarks are subject to an appropriate framework. The majority of the Group members believe that the adoption of additional Principles addressing indices and benchmarks specifically should be encouraged. In fact, today, many players in the industry are not regulated. Whilst the revised Market Abuse Directive and the potential Benchmark Regulation may put an end to this situation in the near future, a proper framework should be adopted and implemented in the meantime. However, the Group members acknowledge that the binding character of such "interim" regulation may be problematic. In order to encourage the broad acceptance and application of these principles, ESMA and EBA should put a particular emphasis on self-regulation and coordinate with industry representatives, such as Global Financial Markets Association, as well as with other standard setting bodies such as IOSCO. It was suggested that for instance producers could declare publicly that they were in compliance with the Principles.

29. Furthermore, whilst the Group acknowledges that such an approach may not be applicable in the absence of any binding regulation, the Group members believe that in the near future direct supervision of indices and benchmarks by EU regulatory authorities should be encouraged, notably in respect to the governance arrangements in place at the level of the index provider, as well as in respect to the data and methodology used to calculate the indices. Some Group members pointed at the need for those indices used in retail products to be supervised by ESMA (in terms of design, production and use) when:

    - no national supervisor is in charge;
    - the index is widely used by end investors and/or borrowers; and
    - the index is not based on publicly available trade prices based on real liquidity, or other objective data

30. Some Group members believe that indices such as LIBOR and EURIBOR should also be supervised at the European level.

This advice will be published on the Securities and Markets Stakeholder Group section of ESMA's website.

Adopted on 26 February 2013

Guillaume Prache

Chair

Securities and Markets Stakeholder Group

# Annex II – Principles for Benchmark-Setting Processes in the EU

## Definitions

For the purpose of these Principles, the following definitions apply:

i. **Benchmark**: A price, rate, index or other value which is

   a) made available to users, whether free of charge or for payment; and

   b) calculated through the application of a formula to the value of one or more underlying assets or prices, including estimated prices, interest rates or other values, or surveys; and

   c) by reference to which

      i. the amount payable under a financial instrument or the value of the financial instrument is determined; or

      ii. the performance of a financial instrument is measured.

   For clarity, this definition does not include credit ratings as defined in Art. 3(1)(a) of the Regulation (EC) No 1060/2009 of the European Parliament and of the Council of 16 September 2009 on credit rating agencies.

ii. **Benchmark Administration**: Includes all the stages and processes involved in the establishment, design, production and dissemination of a Benchmark from the gathering of the input data and the calculation of the Benchmark based on the input data to the dissemination of the Benchmark to users including any review, adjustment and modification of this process.

iii. **Benchmark Administrator**: The legal person or entity responsible for Benchmark Administration as defined above, irrespective of whether the legal person or entity owns the intellectual property relating to the Benchmark.

iv. **Benchmark Calculation**: The activity of performing the calculation of the Benchmark based on the methodology provided by a Benchmark Administrator and the data collected by the entity performing the calculation or the Benchmark Administrator or submitted by Benchmark Submitters.

v. **Benchmark Calculation Agent**: A legal person or entity performing Benchmark Calculation activities.

vi. **Benchmark Publication**: The activity of publishing Benchmark values, which includes making available such values on the internet or by any other means, whether free of charge or not.

vii. **Benchmark Publisher**: A legal person or entity performing Benchmark Publication activities.

viii. **Benchmark Submitter**: A legal person or entity contributing to Benchmark data submissions to a Benchmark Administrator or Calculation Agent which are used exclusively for the calculation of the Benchmark.[12]

ix. **Benchmark User**: A professional client within the meaning of Annex II to Directive 2004/39/EC that uses a Benchmark in one of the following manners:

— as a reference for a financial transaction or contract that the legal person or entity sells or places, or for financial instruments that it structures; or

— as a reference for a financial transaction or contract to be entered into by the legal person's or entity's clients, or by itself on behalf of its clients, in the context of its individual or collective portfolio management activities.

x. **Methodology**: The written rules and procedures according to which the data are collected and the Benchmark is calculated.

xi. **Stakeholder**: A Benchmark User or a legal person or entity that purchases the Benchmark determination services, or other legal persons or entities who own contracts or financial instruments that reference a Benchmark.

xii. **Supervisory Authority**: A regulator or a supervisor that has responsibility for the relevant actors, markets or instruments involved in Benchmark setting.

The Benchmark Administration, Calculation and Publication activities may be performed by distinct legal entities, or may be grouped together such that one entity performs more than one.

[12] Legal persons or entities performing market transactions (e.g. equity trading) may indirectly be involved in benchmark setting but are not be considered Benchmark Submitters.

ESMA and EBA have adopted the Principles for Benchmark-Setting Processes ("Principles"). These Principles aim to mitigate governance and incentive issues pertaining to Benchmarks provided by private sector Benchmark Administrators. They may also serve as a useful yardstick for public-sector entities providing relevant Benchmarks or involved in their provision.

ESMA and EBA consider important that these Principles are implemented not only by all market participants, with the aim of reinforcing the robustness of the procedures, ensuring a minimal level of transparency to the public and creating a level-playing field, but also by Supervisory Authorities in their supervisory practices, where relevant and possible.

Market participants and Supervisory Authorities should apply the "Supporting principles" under sections B. (Principles for Benchmark Administrators), C. (Principles for firms involved in Benchmark data submissions), D. (Principles for Benchmark Calculation Agents), E. (Principles for Benchmark Publishers), F. (Principles for Benchmark Users) and G. (Principles for the continuity of Benchmarks) below in a way that is appropriate to the size, nature and complexity of any specific Benchmark. Proportionality should operate both ways: for some Benchmarks, more sophisticated policies or practices will need to be applied in fulfilling the requirements; for other Benchmarks, the requirements of the "Supporting Principles" may be met in a simpler or less burdensome way.

The Principles cover all stages of the Benchmark process:

— Benchmark Data Submission,
— Benchmark Administration,
— Benchmark Calculation,
— Benchmark Publication,
— the use of Benchmarks, and
— the continuity of Benchmarks.

The Principles are not intended to and do not replace any existing EU or national regulations in relevant areas. They are also without prejudice to the IOSCO Principles for Oil Price Reporting Agencies[13] and of the specific provisions on financial indices in the ESMA Guidelines on Exchange-Traded Funds (ETFs) and other UCITS[14].

A framework for any Benchmark setting process should include at least the following Principles in order to instil confidence in financial markets and market participants, and guarantee the necessary accuracy and integrity of the Benchmark formation process:

**A. General framework for Benchmark setting**

A.1 **Methodology**: The methodologies for the calculation of a Benchmark, including information on the way in which contributions are determined and corroborated, should be documented and be subject to regular scrutiny and controls to verify their reliability. The definition of a specific Benchmark should be precise in order to avoid subjective interpretation of key concepts. A Benchmark should represent adequately the market, strategy or interest to which it refers, and measure the performance of a representative group of underlyings in a relevant and appropriate way. Where appropriate, actual market transactions should be used as a basis for a Benchmark Calculation.

A.2 **Governance structure**: The process of setting a Benchmark needs to be governed by clear and independent procedures, with detailed information on the process made available publicly, in

[13] http://www.iosco.org/library/pubdocs/pdf/IOSCOPD391.pdf.
[14] ESMA/2012/474, available at: http://www.esma.europa.eu/system/files/2012-474.pdf.

order to avoid and manage conflicts of interest and limit its susceptibility to manipulation, discretionary decision making or price distortion. Governing processes should include clear rules on the allocation of responsibilities for the Benchmark Administration. Benchmark structures should be established and managed in a way so as to reduce conflicts of interest as much as possible. Conflicts of interest may arise where Benchmark Submitters have discretion regarding the submitted data, while at the same time they or their clients have an exposure against the Benchmark. Where conflicts of interest are unavoidable, they should be identified, disclosed to the public and monitored so as to be transparent and acceptable to Stakeholders and to maintain confidence in the Benchmark setting process.

A.3 **Supervision and oversight**: Confidence in a Benchmark is enhanced through regulation and oversight and an appropriate sanctioning regime that allows sanctions for improper conduct, as it will be the case in accordance with future EU legislation on market abuse. In the EU, outside of proposals for market abuse, a formal regulatory regime for Benchmarks does not exist so far. For any existing applicable regimes and rules and for the application of these Principles, Benchmark Submitters, Benchmark Administrators, Benchmark Calculation Agents, Benchmark Publishers and Benchmark Users should co-operate closely with the relevant Supervisory Authorities.

A.4 **Transparency**: A Benchmark should be transparent and accessible to the public, with fair and open access to the rules governing its establishment and operation, calculation, and publication; the fact that a Benchmark is (or may be) published first to certain Stakeholders before it is to others should be disclosed. A high degree of transparency on the process determining a Benchmark, or any modification thereof, will enhance confidence in its integrity, which would also help foster understanding of the Benchmark in the market place. Transparency may be limited in exceptional circumstances only, based on contractual provisions safeguarding confidentiality and intellectual property rights. The full Methodology along with historical records[15] should be disclosed to the public wherever possible in order to make it fully replicable. Where this is not possible based on contractual provisions, the relevant information, such as weightings and prices of components, should be disclosed to the public prior to any changes in the composition of the Benchmark, with sufficient notice so as to allow a proper reassessment by Stakeholders.

[15] Historical records should include the data relating to the historical composition, past performances and Methodology of a Benchmark including its past and current weightings, historical panel composition – if any – past and current Methodology, data on past submissions by Benchmark Submitters, and when possible benchmark data, i.e. the data disclosed by the Benchmark Publisher.

## B.Principles for Benchmark Administrators

**General principles**

B.1 A Benchmark Administrator should ensure the existence of robust methodologies for the calculation of the Benchmark and appropriately oversee its operations and ensure that there is an appropriate level of transparency to the public regarding the rules governing the Benchmark.

**Supporting principles**

- **Methodology**

  - Calculation criteria

B.2 A Benchmark Administrator should establish methodologies with well-defined criteria for the calculation of the Benchmark, so that judgement and qualitative assessments or other opportunities for discretionary decision making are limited and confined to well-defined stages of the Benchmark setting process or specific situations, such as cases of market disruption or operational contingencies. *Inter alia*, such criteria should address the composition of panels where applicable, the algorithm for the calculation of the Benchmark, the definition and sourcing of the data used in the calculation, and provisions regarding operational continuity.

B.3 The methodologies established by the Benchmark Administrator should be rigorous, systematic and continuous. Any amendment to an established methodology should be made according to a transparent and determined process, and be published by the Benchmark Administrator beforehand.

  - Calculation errors

B.4 Benchmark Administrators should have clear policies for communicating errors in the Benchmark (whatever the reason for the error), and any subsequent re-fixing.

  - Withdrawals

B.5 Without prejudice of the principles under Section G. below, a Benchmark Administrator should encourage Benchmark Submitters not to withdraw from surveys or panels.

  - Representativeness and liquidity

B.6 A Benchmark Administrator should regularly review the Benchmarks or the range of Benchmarks provided (such as, for example, asset classes, currencies and tenors). It should ensure that any Benchmark reflects the market or interest it seeks to represent.

B.7 The data used to construct a Benchmark determination should be sufficient to represent accurately and reliably the underlying assets or prices, interest rates or other values measured by the Benchmark. These data should be anchored by observable transactions entered into at arm's length between buyers and sellers in the market for the underlying assets or prices, interest rates or other values the Benchmark measures in order for it to function as a credible indicator of prices, rates, indices or values.

Administrators may rely on non-transactional data such as offers and bids and adjustments based on expert judgment for purposes of constructing an individual Benchmark determination, but such data should only be used as an adjunct or supplement to transactional

data. The principle does not prohibit the use of non-transactional data for indices that are not designed to represent transactions and where the nature of the index is such that non-transactional data is used to reflect what the index is designed to measure.

- Disclosure of the Methodology

B.8 A Benchmark Administrator should fully disclose the Methodology to the public. Where this is not possible for legal reasons, the relevant information, such as weightings and prices of components, should be disclosed to the public prior to any changes in the composition of the Benchmark, with sufficient notice so as to allow for a proper reassessment by Stakeholders.

➢ **Governance structure**

B.9 A Benchmark Administrator should have governance and compliance functions and processes to enable it to operate effectively and ensure the quality of the Benchmark. A Benchmark Administrator should provide well-defined criteria and procedures to select members of the governance and compliance functions that participate in the determination of the methodologies for the calculation of the Benchmark. Governance bodies of Benchmark Administrators should include members who are independent and appointed from outside those that through ownership or other linkages could face conflicts of interest, in particular those representing members contributing to the Benchmark. Members of governing bodies should be present and fully involved in ensuring that Benchmark Administration respects internal rules and procedures. Details of the membership of the relevant governance and compliance functions should be disclosed to the public, along with any declarations of conflicts of interests and the processes for appointment to and removal from the governance and compliance functions.

➢ **Oversight and control**

- Submission controls

B.10 A Benchmark Administrator should have procedures to enable its oversight functions to report to their respective Supervisory Authorities, if any, any irregularities, unusual submissions or misconduct by the Benchmark Submitters of which the Administrator becomes aware.

- Supervision

B.11 A Benchmark Administrator should comply with any query from its Supervisory Authority or, when it is not under the responsibility of a Supervisory Authority, is encouraged to co-operate with the Supervisory Authorities responsible for the other actors, markets and instruments involved in the setting of the Benchmark to which it contributes.

- Record-keeping requirements

B.12 A Benchmark Administrator should record minutes of relevant meetings of its oversight functions along with details of all interactions between the Benchmark Administrator and Benchmark Submitters, Benchmark Calculation Agents and Benchmark Publishers. Meeting minutes should be kept for a minimum of five years and be made available to Supervisory Authorities upon request. A Benchmark Administrator should keep audit records of all data used by Benchmark Calculation Agents and Benchmark Submitters in the process of calculating the Benchmark as well as of all the Methodologies used to calculate the Benchmark.

- Internal control mechanisms

B.13 The governance and compliance functions of a Benchmark Administrator should seek to ensure that Principles applying to Benchmark Submitters, Benchmark Calculation Agents and Benchmark Publishers are implemented. In particular, the Benchmark Administrator should require Benchmark Submitters, where they are part of the Benchmark setting process, Benchmark Calculation Agents and Benchmark Publishers to publically and periodically confirm adherence to these Principles.

B.14 A Benchmark Administrator should establish an effective whistleblowing mechanism as well as complaints procedures in order to facilitate early awareness of any misconduct or other irregularities that may arise.

B.15 A Benchmark Administrator should establish, implement and maintain adequate internal control mechanisms on the data contributed. This should include consistency and plausibility checks on the basis of transaction-based or other verifiable data where available.

- Oversight of outsourced activities

B.16 A Benchmark Administrator, when outsourcing Benchmark Calculations to a third party, should retain adequate access to and control over the activities of the third party. A Benchmark Administrator should have formal selection criteria as well as contractual and service level arrangements in place when outsourcing Benchmark Calculations to a third party, and periodically audit the services performed by the Benchmark Calculation agent. In particular, a Benchmark Administrator should retain adequate access to and control over the activities of the Benchmark Calculation agent, including a proper functioning of its Benchmark computation process, and the ability to check its compliance with the Methodology of the Benchmark.

➢ **Transparency**

B.17 A Benchmark Administrator should publicly disclose a confirmation by its management of compliance with the above principles as well as the confirmation received from the Benchmark Submitters, the Benchmark Calculation Agent and Benchmark Publisher.

## C. Principles for Benchmark Submitters

### General principles

C.1 A Benchmark Submitter should have in place internal policies covering the submission process, governance, systems, training, record keeping, compliance, internal controls, audit and disciplinary procedures, including complaints management and escalation processes.

C.2 A Benchmark Submitter should maintain and operate effective organisational and administrative arrangements with a view to avoid and manage conflicts of interests from affecting the Benchmark data submitted.

### Supporting principles

- **Governance structure**

  - Conflicts of interest policy

C.3 A Benchmark Submitter should establish, implement and maintain an effective conflicts of interest policy to enable it to identify, with reference to the activities related to Benchmark data submissions, conflicts of interest that may arise, along with the procedures to be followed and measures to be adopted, in order to manage such conflicts.

C.4 The conflicts of interest policy should include:

— effective procedures to prevent or control the exchange of information between staff engaged in activities involving a risk of a conflict of interest where the exchange of that information may affect the Benchmark data submitted;

— contingency provisions in case of absence of control of the flow of information;

— rules to avoid collusion between Benchmark Submitters and between Benchmark Submitters and Benchmark Administrators;

— measures to prevent any person from exercising inappropriate influence over the way in which staff involved in Benchmark data submission carry out activities;

— the removal of any direct link between the remuneration of staff involved in Benchmark data submissions and the remuneration of, or revenues generated by, different staff principally engaged in another activity, where a conflict of interest may arise in relation to those activities.

  - Record-keeping requirements

C.5 Record keeping should mean for a Benchmark Submitter to arrange for records of all relevant aspects of the submission process to be kept for a period of at least five years in line with the requirements on record keeping in MiFID. These records should cover but not be limited to:

— procedures and methodologies governing submissions and the underlying data;

— names and role of the individuals responsible for submission and submission oversight;

— relevant communication of submitting parties with the Benchmark Administrator and

the Benchmark Calculation Agent;

— substantial exposures of individual traders or trading desks to Benchmark related instruments;

— any transaction reversing positions subsequent to a submission; and

— findings of external or internal audits related to Benchmark submission, remedial actions and progress in their implementation.

Records should be retained in a medium that allows the storage of information in a way accessible for future reference, and in such a form and manner that it must not be possible for the records to be manipulated or altered.

- Governance policy

C.6 A Benchmark Submitter's governance policy should ensure that:

— clearly accountable, named individuals, at the appropriate level of seniority within the firm, are responsible for Benchmark data submissions;

— staff involved in Benchmark data submissions are aware of the procedures which must be followed for the proper discharge of their responsibilities.

C.7 A Benchmark Submitter should ensure that staff involved in Benchmark data submissions have the skills, knowledge and expertise necessary for the discharge of the responsibilities allocated to them. Staff involved in Benchmark data submissions should undergo appropriate training and development programmes.

➢ **Oversight and control**

C.8 A Benchmark Submitter should establish, implement and maintain adequate internal control mechanisms designed to secure compliance with decisions and procedures at all levels of the firm. Internal procedures should stipulate, for example, periodic internal and, where appropriate, external audit of submissions and procedures. Controls performed on the data submitted should be appropriate to the nature of the Benchmark. Controls should include comparisons with actual, transaction-based, verifiable data. Where actual data is not available, documentation by the submitter of a verifiable basis for their qualitative assessment should be required and scrutinised for appropriateness by oversight functions. The Benchmark Submitter should record transactions which may form the basis of the submission to verify that they represent arm's length commercial transactions, and are not transacted solely for the purpose of Benchmark submission. Compliance reports containing explanations of the compliance function's findings should be submitted to senior management and any oversight function on a regular basis. This, as well as any relevant data for submission controls based on a reasoned request by the Benchmark Administrator, should be made available to the Benchmark Administrator on request.

C.9 A Benchmark Submitter should comply with any reasonable query from its Supervisory Authority, where relevant, and is encouraged to co-operate with the Supervisory Authorities responsible for the other actors, markets or instruments involved in the setting of the Benchmark to which it contributes.

C.10 A Benchmark Submitter should establish a zero-tolerance policy, including disciplinary measures, for non-compliance with internal policies, with an effective whistle-blowing policy.

- **Transparency**

C.11 A Benchmark Submitter should submit to the Benchmark Administrator a confirmation by its management of compliance with the above principles which should be published by the Benchmark Administrator in line with Principles B.13 and B.17.

## D. Principles for Benchmark Calculation Agents

### General principles

D.1 A Benchmark Calculation Agent should ensure a robust calculation of the Benchmark and ensure the existence of appropriate internal controls over the Benchmark Calculations it makes.

### Supporting principles

- **Record keeping**

D.2 A Benchmark Calculation Agent should duly document and keep records of all interactions with submitting parties, if any, so as to easily identify anomalies, and make these available to Supervisory Authorities upon request. A Benchmark Calculation Agent should keep audit records of all data used in the process of calculating the Benchmark as well as of all contributions by Benchmark Submitters.

D.3 A Benchmark Calculation Agent should keep records of contacts with the Benchmark Administrator (where Benchmark Administration and Benchmark Calculation activities are not exercised by the same legal entity or person), and make these available to Supervisory Authorities upon request.

- **Governance structure**

D.4 A Benchmark Calculation Agent should have clearly accountable, named individuals, at the appropriate level of seniority within the entity, responsible for Benchmark computation.

D.5 A Benchmark Calculation Agent should implement and maintain systems for pre- and post-calculation control that are adequate to ensure consistent and timely Benchmark computation.

- **Oversight and control**

D.6 A Benchmark Calculation Agent should establish an effective whistleblowing mechanism in order to facilitate early awareness of any misconduct or other irregularities that may arise.

D.7 A Benchmark Calculation Agent should have clear policies in place on how to publicise any errors in calculation due to any reason and communicate clearly any new Benchmark fixing or determination.

- **Transparency**

D.8 A Benchmark Calculation Agent should submit to the Benchmark Administrator a confirmation by its management of compliance with the above Principles which should be published by the Benchmark Administrator in line with Principles B.13 and B.17.

## E. Principles for Benchmark Publishers

### General principles

E.1 A Benchmark Publisher should ensure reliable publication of the Benchmark it has agreed to publish.

### Supporting principles

- **Governance structure**

E.2 A Benchmark Publisher should have clearly accountable, named individuals, at the appropriate level of seniority within the entity, responsible for Benchmark publication.

E.3 A Benchmark Publisher should implement and maintain systems for pre- and post-publication control that are adequate to ensure consistent and timely Benchmark Publication.

- **Oversight and control**

E.4 Before publishing Benchmark data, the Benchmark Publisher should obtain a confirmation from the Benchmark Administrator that the procedures for the validation of the submissions and calculations have been followed.

E.5 A Benchmark Publisher should have clear policies in place on how to publicise any errors in calculation due to any reason; and communicate clearly any new Benchmark fixing or determination.

- **Transparency**

E.6 A Benchmark Publisher should publish any changes to the Benchmark composition, Benchmark Submitters or any other feature of the Benchmarks.

E.7 A Benchmark Publisher should submit to the Benchmark Administrator a confirmation by its management of compliance with the above Principles which should be published by the Benchmark Administrator in line with Principles B.13 and B.17.

## F. Principles for Benchmark Users

### General principles

F.1 Benchmark Users should regularly assess the benchmarks they use in financial products or transactions, and verify that the Benchmark used is appropriate, suitable and relevant for the targeted market. Any potential irregularities observed in a Benchmark should be notified to the Benchmark Administrator or the relevant Supervisory Authorities if appropriate.

### Supporting principles

- **Due diligence**

F.2 A Benchmark User should use sufficient due diligence to ascertain whether the relevant Benchmark Administrator and Benchmark Calculation Agent comply with the Principles applying to Benchmark Administrators and Benchmark Calculation Agents. In order to comply with this requirement, the Benchmark User may rely, among other sources, on the confirmation of compliance publicly disclosed by the Benchmark Administrator.

F.3 A Benchmark User should regularly assess the appropriateness, suitability, and relevance of the use of a Benchmark, both when it acts as a principal and when it acts as an agent for any third party. When the Benchmark User uses the Benchmark as a reference for financial transactions or contracts to be entered into by its clients, or by itself on behalf of its clients, the extent of the assessment done by the Benchmark User may be limited by the contractual relationship with its clients, but this is without prejudice of the requirement for the Benchmark User to at least inform its clients about the continued appropriateness, suitability, and relevance of the use of a Benchmark for their needs.

## G. Principles for the continuity of Benchmarks

### General principles

G.1 All those participating in the Benchmark setting process and, where relevant, Benchmark Users should put in place robust and credible contingency provisions for cases in which there is a risk to the continuity of the provision of a Benchmark due to, for example, a drying-up of market liquidity, an operational failure, a lack of submissions, transactions or quotes or the unavailability of the Benchmark.

### Supporting principles

- **Benchmark Administrators**

G.2 The contingency provisions put in place by Benchmark Administrators should be transparent and ideally written into contract, so as to reflect the needs of contracting parties. The range of possible solutions may include the use of alternative data sources, including derivatives, or proxies such as algorithms or expert judgments to complement market transactions; increasing the time window for Benchmark submissions; lowering minimum threshold amounts for Benchmark submissions; or the use of a substitute rate based on comparable underlying data. Benchmark Administrators should disclose to the public any temporary switch – due to a contingency situation – from a transaction-based system to an expert judgment-based system and provide evidence for such a switch.

- **Benchmark Submitters**

G.3 A Benchmark Submitter should implement and maintain systems that are adequate to ensure consistent and timely delivery of submissions, including during adverse events.

- **Benchmark Calculation Agents**

G.4 A Benchmark Calculation Agent should have appropriate technical and procedural contingency plans in case of technical failure.

- **Benchmark Publishers**

G.5 A Benchmark Publisher should have robust contingency provisions for unavailability of the systems required to ensure consistent and timely Benchmark Publication.

- **Benchmark Users**

G.6 The contingency provisions put in place by Benchmark Users, where relevant, should be transparent and ideally written into contract, so as to reflect the needs of contracting parties.

G.7 A Benchmark User should develop robust contingencies for the unavailability of a Benchmark within contracts referenced to it. The contingency provisions should be used in the event of interruptions in the provision of a Benchmark, or other market disruptive events which lead to the Benchmark not being calculated or published in the usual manner.

## Legal continuity, revision and review

Without prejudice of the above Principles, ESMA and EBA are conscious that any change to a benchmark framework (calculation methodologies and procedures) should be managed so as to ensure that any disruption to existing benchmark-referenced contracts are proportionate and minimised.

ESMA and EBA may revise the above Principles in light of potential future EU regulations, material changes in market practices or the agreement of international standards pertaining to benchmarks.

ESMA and EBA plan to conduct a review of the application of the above Principles eighteen months after their publication, but may alter that timeframe should they deem it to be appropriate or necessary.