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REPORT FROM THE COMMISSION TO THE EUROPEAN PARLIAMENT AND THE COUNCIL

on the scope of Regulation (EU) 2016/1011, in particular with respect to the continued use by supervised entities of third-country benchmarks and on potential shortcomings of the current framework

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1. INTRODUCTION

A benchmark is an index ([1]) that is used as a reference to determine the price of a financial instrument or a financial contract. A wide variety of benchmarks are currently produced, including interest rate benchmarks such as EURIBOR, equity benchmarks and commodity benchmarks, e.g. energy benchmarks such as West Texas Intermediate (WTI) or Brent. Benchmarks differ in terms of the underlying data used, how the underlying data is collected, how the benchmark is calculated and how it is disseminated to the final user.

Financial markets are global markets, and benchmarks are produced and used internationally. European banks, investment funds and other benchmark users ([2]) reference EU and non-EU benchmarks for a variety of purposes, from hedging their own risks, including interest, credit, and foreign exchange risks, and offering products to hedge the risk of their clients, to establishing an investment portfolio using the benchmark either as an investment template or performance benchmark. Most benchmarks (more than 3.6 million) are produced by administrators outside the EU ([3]). The rules in Regulation (EU) 2016/1011 (Benchmark Regulation / BMR) on the use of non-EU benchmarks are therefore of great importance ([4]).

This report delivers on the mandate in Article 54(6) of the BMR, which calls for a report on the scope of this Regulation, in particular with respect to the continued use by supervised entities of third-country benchmarks and on potential shortcomings of the current framework. This report and its conclusion also fulfil the condition for the adoption of a delegated act pursuant Article 54(7) of the BMR, to extend the transitional period before the rules for the use of non-EU benchmarks start to apply.

2. POLITICAL AND LEGAL CONTEXT

The provision and use of benchmarks have been regulated activities under the BMR since 2016. All benchmark administrators in the EU are under national ([5]) or EU ([6]) supervision and must comply with organisational rules and rules on the conduct of business.

The BMR essentially implements the Principles for Financial Benchmarks of the International Organization of Securities Commissions (the IOSCO Principles), or, where applicable the Principles for Oil Price Reporting Agencies (IOSCO PRA Principles). These two sets of principles were developed at international level in 2012-2013 in response to various revelations about benchmark manipulation and continue to serve as an important focal point for systems of benchmark regulations worldwide. The principles are adhered to by most professional benchmark administrators, albeit mostly on a self-certification basis.

([1]) An index is a statistical measure, typically of a price or quantity, calculated or determined from a representative set of underlying data.

([2]) Supervised entities are defined in Art. 3(1)(17) of the BMR.

([3]) According to information received from ESMA, which is based on data from Rimes Technologies - Data Management for Financial Services (www.rimes.com).

([4]) Notably Art. 29(1) *in fine* and Artt. 30-33 of the BMR.

([5]) For all benchmarks except EU critical benchmarks.

([6]) EU critical benchmarks are supervised by ESMA.

Scope of the BMR

The BMR is binding on all EU benchmark administrators, with infringements punishable by fines of up to 10 % of the infringing party's annual turnover. In contrast with legal regimes for benchmarks in other jurisdictions, the BMR has a broad scope, based on the premise that all financial benchmarks and all administrators are potentially subject to conflicts of interest. Therefore, the BMR not only covers benchmarks with systemic relevance and benchmarks that are especially susceptible to conflicts of interest, but also less-used benchmarks and benchmarks where conflicts of interest are unlikely to arise. For this reason, significant elements of proportionality were built into the BMR based on differences between benchmarks in terms of characteristics and vulnerabilities ([7]). Finally, to mitigate any risk of regulatory arbitrage, the use of non-EU benchmarks was prohibited, except where they are subject to equivalent local regulation and supervision, or where a benchmark's administrator voluntarily complies with the BMR and seeks access to the EU market through recognition or endorsement.

The BMR entered into application on 1 January 2018, with a transitional period for existing benchmarks and non-EU benchmarks until 31 December 2019. That deadline was later postponed twice and is now 31 December 2023 ([8]).

The proposal for what would become the 2020 BMR review examined the effects of the third country rules provided for in the BMR on the availability of certain foreign exchange (FX) benchmarks to EU market participants, as market participants have signalled that Art. 29(1) BMR would restrict access to many of these benchmarks if the third country chapter entered into application. ([9]) A particular challenge for these benchmarks in securing access to the EU market lies in the fact that they are generally not produced for commercial purposes and are often published by semi-public entities or are under the control of governments that use them as a policy tool. As they are published on a non-commercial basis, their administrators lack an economic incentive to seek compliance with the BMR. Recognising the risk that EU supervised entities might be left without access to FX benchmarks needed to hedge business activities in the third countries concerned, the co-legislators granted the Commission powers to allow the use of specific FX benchmarks.

More broadly, the co-legislators understood that the entry into application of the rules on third country benchmarks would potentially affect the availability of third-country benchmarks for EU benchmark users beyond the very specific subset of FX benchmarks. It was also in the course of this negotiation process that the co-legislators included the review mandate at the origin of this report. ([10])

([7]) E.g., there is a graduation between critical, significant, and non-significant benchmarks on the basis of the volume of financial contracts and financial instruments referencing a benchmark, with administrators of the latter two categories having the option of disapplying certain requirements on a comply-or-explain basis (see Artt. 25 and 26 BMR). In addition, benchmarks using input data regulated at source (so-called regulated data benchmarks) are subject to less stringent rules on controls of input data (see Art. 17 BMR).

([8]) By Regulation (EU) 2019/2089 and Regulation (EU) 2021/168.

([9]) See the Impact Assessment Report at: https://eur-lex.europa.eu/legal-content/EN/TXT/?uri=CELEX%3A52020SC0142

([10]) Articles 54(6) and 54(7) BMR.

Rules for the use of non-EU benchmarks ([11])

Under the current third-country rules non-EU benchmarks can be used in the EU provided they obtain access via one of three routes specified in the BMR.

The first route is **equivalence (Article 30 BMR)**, which takes the form of an implementing decision stating that the regulatory framework in a third country imposes binding requirements equivalent to those of the BMR, and that those requirements are subject to effective supervision and enforcement. Two variants of such a decision are available, either covering the entire scope of a third country jurisdiction's benchmark regulation or covering only specific administrators, specific benchmarks or families of benchmarks. Once an equivalence decision is taken, the European Securities and Markets Authority (ESMA) contacts the third country supervisor and draws up cooperation arrangements covering the exchange of information and prompt notification should a third country competent authority find an administrator in breach of its legal obligations. Benchmarks covered by an equivalence decision are included in ESMA's register of third country benchmarks that are available for use in the EU. Only Australia and Singapore have been granted partial equivalence, with a handful of other jurisdictions having expressed interest.

Whereas equivalence depends on a third country legislator and / or supervisor taking the initiative to contact the European Commission, the two access routes below can be used on the initiative of benchmark administrators alone, or benchmark administrators active in a jurisdiction where they are not subject to binding regulation.

The second access route is **endorsement (Article 33 BMR)**, in which an EU supervised entity (which may be a benchmark administrator or another type of entity subject to supervision by an EU national competent authority) assumes regulatory responsibility for a non-EU benchmark. The BMR sets out that the endorsing entity should have a 'clear and well-defined role within the control or accountability framework of a third country administrator' and is able to 'monitor effectively the provision of a benchmark'. Among other conditions, the BMR requires an objective reason why the benchmark is produced outside the EU. Endorsed benchmarks or families of benchmarks are included in the ESMA register of third country benchmarks.

The third access route for non-EU benchmarks is **recognition (Article 32 BMR)**. Under this scheme, a third country administrator needs to have a legal representative, i.e., a natural or legal person located in the EU and expressly appointed by that administrator to act on its behalf with regard to its obligations under the BMR. The administrator needs to demonstrate compliance with the main requirements of the BMR to ESMA, which can conclude a cooperation arrangement with the administrator's domestic supervisor where applicable.

Both recognition and endorsement can be initiated by a non-EU administrator wishing to market its benchmarks to EU supervised entities. However, obtaining access via either of these routes requires that an administrator has an economic interest in doing so. If there is none, a non-EU administrator will not make the effort of setting up and remunerating the required presence in the Union, and EU users will be deprived of the benchmarks concerned.

([11]) Notably Art. 29(1) *in fine* and Artt. 30-33 of the BMR.

A picture of the EU market for benchmarks

72 EU benchmark administrators are currently listed in the ESMA register. Of the benchmarks currently in use in the EU, one (EURIBOR) is a critical benchmark under ESMA supervision ([12]). Three - the Stockholm Interbank Offered Rate (STIBOR), the Norway Interbank Offered Rate (NIBOR) and the Warsaw Interbank Offered Rate (WIBOR) are critical benchmarks under national supervision ([13]). All these critical benchmarks are interest rate benchmarks, and each of them is administered by a different EU administrator. An informal survey of national supervisors by ESMA revealed that in September 2022, six benchmark administrators under European supervision (three EU and three non-EU ([14])) offer a total of 50 significant benchmarks ([15]). Further, as of March 2023, there is a total of 12 administrators providing EU climate benchmarks, half of which are subject to European supervision under BMR: five supervised by national authorities and one supervised by ESMA under the recognition regime.

The ESMA register also lists 14 non-EU administrators, who choose varying access routes. The **equivalence** decisions for Australia and Singapore cover two administrators and a total of seven benchmarks. Two benchmark administrators (S&P Dow Jones Indices LLC and SIX Index AG) have chosen the **endorsement** route for a total of 4,597 benchmarks. Via the **recognition** route, 10 administrators ([16]) have been included in the ESMA register, with a total of 15,245 benchmarks covered.

Table 2: Overview of the number of EU and non-EU benchmark administrators

Benchmark administrators	**Total**	**EU**	**Non-EU**
Total number	345	72	273
Available in the EU ([17])	86	72	14

In addition, 259 third-country administrators currently not registered in the EU benefit from the transitional period provided for in Article 51(5) of the BMR. ([18]) The top 10 among these 259, in terms of number of benchmarks offered, are based either in the UK or

([12]) Article 20(1)(a) BMR, which requires that a benchmark is referenced by a total amount of financial contracts and financial instruments of at least EUR 500 billion.

([13]) Article 20(1)(b) BMR.

([14]) Having obtained access to the EU market via recognition or endorsement. This is in addition to an unknown number of non-EU administrators offering significant benchmarks in the EU under the transitional provisions.

([15]) i.e., benchmarks referenced by a total amount of financial contracts and financial instruments in excess of EUR 50 billion, or [which have] no or very few appropriate market-led substitutes and [could cause] a significant and adverse impact on market integrity, financial stability, consumers, the real economy or the financing of households or businesses in one or more Member States.

([16]) Hedge Fund Research, Inc. (USA), ICAP information Services Limited (UK), Invesco Indexing LLC (USA), JPX Market Innovation & Research, Inc. (Japan), Leonteq Securities AG (Switzerland), LPX AG (Switzerland), Nikkei Inc. (Japan), Scientific Infra Pte Ltd (Singapore), STOXX Ltd. (Switzerland), WisdomTree, Inc. (USA).

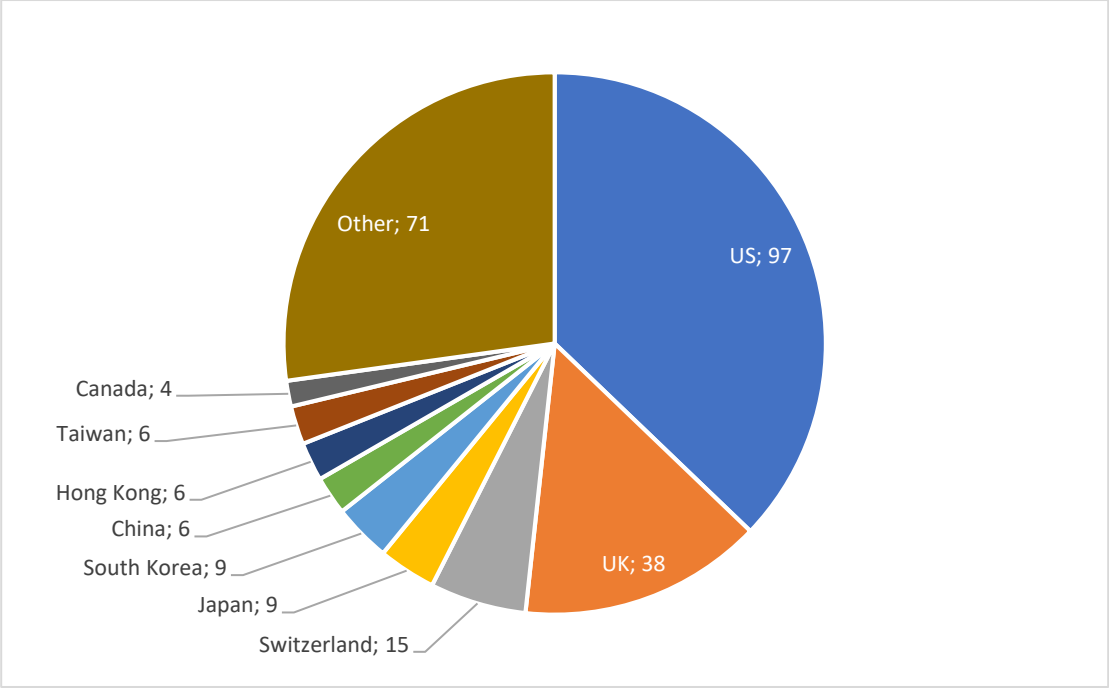
([17]) Once the third country rules start to apply.

([18]) Reported by ESMA on the basis of a commercial database.

the US. Figure 1 gives an overview of the number of benchmark administrators in each country and presents the overall distribution of benchmark administrators worldwide. In addition, the top 10 third-country benchmark administrators account for 98% of the total third-country benchmarks provided. By comparison: the largest third country administrator currently registered (by endorsement or recognition) in the EU would not rank among the top 10 benchmark administrators globally by number of benchmarks provided.

The above shows that only 5 percent of the non-EU benchmark administrators whose benchmarks are currently available for use on the EU market have obtained a status that will ensure their benchmarks remain available once the third country rules become mandatory.

Figure 1: Number of benchmark administrators per country worldwide (excluding those already registered) ([19])



3. APPRAISAL

BMR was designed to apply to all benchmarks, all benchmark administrators and all use of benchmarks by EU supervised entities. EU supervised entities are only allowed to use benchmarks that comply with the BMR. For benchmark administrators located in the EU, compliance with the BMR is mandatory and results in the availability of all their benchmarks for use in the Union. For non-EU benchmarks, a number of access routes for non-EU administrators were provided. Still, non-EU benchmark administrators - apart from those whose benchmarks are covered by an equivalence decision – need to take a

([19]) The category "Other" includes: Chile, India, New Zealand, the Russian Federation, Singapore and South Africa (with three administrators each); the United Arab Emirates, Argentina, Australia, Bahrain, Brazil, Egypt, Indonesia, Israel, Namibia, Nigeria, Philippines, Thailand, Turkiye and Vietnam (with two administrators each) and Colombia, Guernsey, Jamaica, Jordan, Kenya, Kuwait, Kazakhstan, Sri Lanka, Morocco, Montenegro, Mauritius, Mexico, Malaysia, Oman, Panama, Pakistan, Qatar, Serbia, Saudi Arabia, Tunisia, Trinidad and Tobago, Ukraine, Uganda, Zambia and Zimbabwe (with one administrator each).

positive decision to seek compliance with the BMR through recognition or endorsement. That decision depends on the economic interest the EU market represents to them.

It was assumed that over time non-EU jurisdictions would develop comparably comprehensive rules for financial benchmarks. This would have allowed the Commission to recognise those regulatory systems as equivalent or would have enabled third country benchmark administrators to seek access to the EU market via the routes of recognition or endorsement with no or lower additional compliance efforts. However, this has not been the case. Of the non-EU systems of benchmark regulation, none except the UK BMR operate on the basis of an equally broad scope.

This situation affects EU benchmark users, as the application of the current third country rules under the BMR could dramatically reduce the number and variety of benchmarks that EU supervised entities can use. Among other things, this would be problematic for the asset management sector, as it would restrict the number and variety of benchmarks available for investment funds to replicate the performance of a benchmark or to compare an investment fund's performance to a benchmark, both of which are considered as use of that benchmark under the BMR. This might destabilise the EU's asset management sector, and could reduce derivatives users' ability to hedge their activities. This destabilisation of the Union's asset management sector, in addition to the reduced ability for derivatives users to rely on a broad range of options to hedge their activities due to the reduced capacity of those derivatives to reference third-country benchmarks, could imply financial stability concerns in the Union. Lastly, a smaller market with fewer players offering benchmarks is likely to be less competitive.

EU benchmark users and end-users rely significantly on benchmarks administered outside the EU. A targeted consultation held in the summer of 2022 ([20]) pointed out the following:

- Of the **benchmark users** who responded to the questionnaire, none responded that their activities did **not** rely on non-EU benchmarks at all – though there may be selection bias at play (16 out of 20 users reported that their activities were moderately, strongly or exclusively reliant on non-EU benchmarks)

- The reasons cited for using a non-EU benchmark instead of an EU alternative include:
    - **habit**: the use of a particular benchmark is an established practice, or the user has a long-standing or broad business relationship with the benchmark administrator;
    - **unavailability of EU-based alternative**, e.g., in certain niche markets that are intrinsically linked to a specific non-EU benchmark, such as the dry bulk freight market which relies on benchmarks produced by the Baltic Exchange, based in London;
    - **client demand or market power of certain benchmark administrators:** clients sometimes seek exposure to a specific (often brand name) non-EU benchmark, and certain non-EU benchmarks are also perceived to be leaders in their specific market segment (e.g. MSCI World index family).

- Although several benchmark users report mainly or exclusively using benchmarks that currently already satisfy the criteria of the BMR third country rules, or report

([20]) See https://finance.ec.europa.eu/regulation-and-supervision/consultations/finance-2022-benchmarks-third-country_en for a synopsis report of the responses to this consultation.

that they are confident the administrators of benchmarks they use will take the required steps in time, there continues to be significant uncertainty on the future availability of many non-EU benchmarks. In many cases (58%; 11 out of 19), administrators whose benchmarks are not yet BMR-compliant have not yet systematically informed their EU users of their intentions to comply.

Where the use of non-EU benchmarks is a response to specific demands from end-users or specific exposure or hedging characteristics sought by end-users that cannot be met by EU benchmarks, restricting their use by EU supervised entities might displace the demand for financial products and services referencing these benchmarks to financial service providers outside the EU. Indeed, where an investor's or a business' demand cannot be met by an EU bank or investment fund (due to the inability to reference a non-EU benchmark), demand might shift to providers in jurisdictions that do not restrict access to these benchmarks.

4. NEXT STEPS

The current number of benchmarks administered in third countries that are used in the EU in accordance with the access routes of equivalence, recognition, and endorsement of the BMR is low compared to the total number of benchmarks available worldwide. Should the rules applicable to third country benchmarks enter into application on 31 December 2023, the continued use in the Union of such third-country benchmarks by supervised entities would be significantly impaired or would pose a risk to financial stability. Therefore, the Commission has decided to make use of the empowerment in Article 54(7) to adopt a delegated act postponing the entry into application of the rules governing the use of non-EU benchmarks until 31 December 2025. Noting the differences between the EU regime and other jurisdictions, the Commission continues monitoring the application of the BMR in the EU and the related financial stability risks to inform a possible review of the legal regime in the future.