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Directorate-General for Financial Stability, Financial Services and Capital Markets Union

FINANCIAL MARKETS
Securities markets

PUBLIC CONSULTATION DOCUMENT
REVIEW OF THE EU BENCHMARK REGULATION

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This document is a working document of the Commission services for consultation and does not prejudge the final form of any future decision to be taken by the Commission.

The views expressed in this document are indicative only and are not a final policy position nor do they constitute a formal proposal by the European Commission.

The responses to this consultation will provide important guidance to the Commission when preparing, if considered appropriate, a formal Commission proposal.

You are invited to comment on the issues raised in this consultation document through the **online questionnaire** available on the following webpage:

https://ec.europa.eu/info/publications/finance-consultations-2019-benchmark-review_en

Please note that in order to ensure a fair and transparent consultation process **only responses received through the online questionnaire will be taken into account and included in the report summarising the responses.**

In replying to these questions, please indicate the expected impact described in each section of this paper on your activities or the activities of firms in your jurisdiction, including estimates of administrative or compliance costs. Please also state reasons for your answers and provide, to the extent possible, evidence supporting your views.

If need be, files with additional information can be uploaded using the button at the end of the consultation page. In order to assist in the evaluation of your contribution, we would appreciate if you could maintain the structure of this questionnaire and indicate clearly the question you are responding to in any additional material you might want to provide.

This consultation follows the normal rules of the European Commission for public consultations. Responses will be published unless respondents indicate otherwise in the online questionnaire.

Responses authorised for publication will be published on the following webpage:
https://ec.europa.eu/info/publications/finance-consultations-2019-benchmark-review_en

Commission Services Consultation

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1. INTRODUCTION

The EU Benchmark Regulation (the ‘Regulation’, the ‘Benchmark Regulation’ or the ‘BMR’)¹ has been in application since 1 January 2018. Administrators of EU benchmarks have to apply for authorisation or registration by 1 January 2020. For administrators of critical benchmarks and third country benchmarks, the transitional period expires on 31 December 2021.

According to Article 54 of the Regulation the European Commission has to review and submit a report to the European Parliament and to the Council on the Regulation by 1 January 2020. The review must, in particular, cover the following topics:

- (a) the functioning and effectiveness of the rules applicable to critical benchmarks, the mandatory administration and mandatory contribution rules and the definition of a critical benchmark;
- (b) the effectiveness of the authorisation, registration and supervision regime applicable to benchmark administrators, the benchmark colleges as well as the appropriateness of supervision of certain benchmarks by a Union body;
- (c) the functioning and effectiveness of Article 19(2) on certain commodity benchmarks, in particular the scope of its application.

In addition, subsequent to the political agreement on climate-related benchmarks, the Commission will also be required to submit, by 1 April 2020, a report on the operation of third-country benchmarks in the Union, including on the recourse that third country benchmark administrators have had to endorsement, recognition or equivalence. That report will have to also analyse the consequences of the extension of the transitional period for critical and for third country benchmarks until 31 December 2021.

The Commission will also take into consideration the answers received in this consultation to feed into the reflections aimed at fostering the international role of the Euro².

This consultation seeks the views of stakeholders on the issues identified below.

2. CRITICAL BENCHMARKS

The Regulation introduces specific rules that only apply to critical benchmarks. Once the European Commission adds a benchmark to the list of critical benchmarks, the competent authority has increased powers to ensure the representativeness and continuity of the

¹ In this consultation, “the Regulation” or the “Benchmark Regulation” refers to Regulation (EU) 2016/1011 of the European Parliament and of the Council of 8 June 2016 on indices used as benchmarks in financial instruments and financial contracts or to measure the performance of investment funds and amending Directives 2008/48/EC and 2014/17/EU and Regulation (EU) No 596/2014

² https://ec.europa.eu/commission/publications/towards-stronger-international-role-euro-commission-contribution-european-council-13-14-december-2018_en

critical benchmark. This includes powers to require mandatory administration of a critical benchmark and/or mandatory contributions to a critical benchmark.

As part of the political agreement on the so-called “climate change” benchmarks, the co-legislators agreed to extend the time limit for mandatory administration of and contributions to critical benchmarks from 24 months to five years. The political agreement on the ESAs review³ entrusts ESMA, as of 1 January 2022, with the supervision of EU critical benchmarks. (EU critical benchmarks are defined in Article 20(1)(a) BMR).

The continued reform of critical benchmarks raises several issues:

IBOR reform

On the basis of current estimates, contracts will be referencing IBOR rates at least until 2050. Certain contracts referencing IBOR rates might be impossible to change (e.g. mortgages or bonds with a 100% noteholder agreement clause). Should a critical IBOR rate cease, there is a risk of disruption to parties whose contracts reference this IBOR rate.

Competent authorities might, however, be confronted with the situation that an IBOR rate no longer represents the market or economic reality it is intended to measure (e.g., due to one or several contributors’ plans to withdraw from an IBOR panel). In terms of Article 23 of the Regulation, the IBOR rate will then lose the “capability” to measure its underlying market.

In these circumstances, Article 23(6)(d) of the Regulation already empowers competent authorities to require a change to the methodology or to other rules of a critical benchmark when it risks becoming unrepresentative of its underlying market. As private sector benchmark administrators might prove reluctant to change benchmarks materially of their own volition (e.g., they might fear litigation by parties that would be disadvantaged by a change), regulatory powers to request the necessary changes might need to be strengthened.

Stakeholders are therefore invited to assess if competent authorities’ powers to require a change of methodology in a critical benchmark should be reinforced and, if so, in what way.

Furthermore, competent authorities might also wish to exercise the power to require a change of methodology in other circumstances, such as when an administrator intends to cease providing a critical benchmark.

Where, for instance, an administrator is aware that a benchmark is no longer representative, it has the option under Article 11(4) BMR to change the methodology (or the input data or contributors) to rectify any shortcomings. But the administrator is not obliged to do so and can, instead, opt to cease the provision of the benchmark altogether.

In certain circumstances the immediate cessation of a critical benchmark may not be the best option to preserve market stability. Therefore, alongside the power to compel the administrator of a critical benchmark to continue publication, it might be useful for the competent authority to have, also in these circumstances, the power to require the necessary changes to the benchmark’s methodology.

³ Publication of the Regulation in the OJ expected in Q4 2019.

Question 1: To what extent do you think it could be useful for a competent authority to have broader powers to require the administrator to change the methodology of a critical benchmark?

Very useful – not useful at all (5 categories). Please explain.

Question 2: Do you consider that such corrective powers should apply to critical benchmarks at all stages in their existence or should these powers be confined to (1) situations when a contributor notifies its intention to cease contributions or (2) situations in which mandatory administration and/or contributions of a critical benchmark are triggered? Yes / no? Please explain.

Question 3: Are there any other changes to Article 23(6)(d) BMR relative to the change of methodology for critical benchmarks that might be desirable to improve the robustness, reliability or representativeness of the benchmark? Yes / no? Please explain.

Orderly cessation of a critical benchmark

Article 28(1) BMR requires **benchmark administrators** to publish a procedure setting out how they will act in the event of changes to or cessation of one of their benchmarks. Such contingency plans should ensure that administrators plan ahead and share their planning with users. The aim is to avoid disruption to users and financial markets when benchmarks are materially changed or cease to be published.

Where feasible and appropriate, cessation plans need to designate appropriate alternatives. Such plans are particularly important for systemically important (critical) benchmarks. It might therefore be useful to further detail these requirements for critical benchmarks, e.g. by making them subject to approval of the national competent authority.

Article 28(2) BMR aims to ensure that **supervised entities other than benchmark administrators** are prepared for the cessation or material change of a benchmark. It might be necessary to expand on existing requirements for critical benchmarks, e.g. to cover the instance where an existing benchmark is found to be no longer representative of its underlying market, or to increase supervisory powers in such a case.

Question 4: To what extent do you think that benchmark cessation plans should be approved by national competent regulators? Agree completely – not agree at all (5 categories) + explain

Question 5: Do you consider that supervised entities should draw up contingency plans to cover instances where a critical benchmark ceases to be representative of its underlying market?

Colleges

Currently, three critical benchmarks are supervised by a college set up in accordance with Article 46 of the Regulation: Euribor, EONIA and LIBOR.

For Euribor and EONIA, both administered by the European Money Markets Institute (EMMI), there is a single college. These colleges, apart from the competent authority of the administrator and ESMA, comprise the competent authorities responsible for the

supervision of each of the members of the panel of the respective critical benchmark and of the competent authorities for the Member States for which the critical benchmark in question is of particular importance.

Question 6: To what extent do you consider the system of supervision by colleges as currently existing appropriate for the supervision of critical benchmarks? Very appropriate – not appropriate at all (5 categories). If not, what changes would you suggest?

3. AUTHORISATION AND REGISTRATION

Authorisation, suspension and withdrawal

Article 35 of the Regulation addresses the situation when it may become necessary to suspend or withdraw a benchmark administrator's authorisation or registration and thus prevent the use of its benchmarks, either permanently or for the duration of a suspension.

The provision to suspend or withdraw operates at administrator level – so exercising this power might result in preventing use of all benchmarks provided by the administrator except those to which Article 35(3) of the Regulation may be applied. It could prove disruptive to prevent the use of all benchmarks of a particular administrator when only one of them has become non-compliant. Given this, and the fact that Article 51(4) BMR only covers use of a non-authorized benchmark during a transitional period, it may necessary to clarify that a competent authority should have the option to suspend or withdraw authorisation or registration in respect of one or more individual benchmarks, without having to suspend the authorisation for the administrator itself. This would allow continued use of all other BMR-compliant benchmarks of that particular administrator.

Question 7: Do you consider that it is currently unclear whether a competent authority has the powers to withdraw or suspend the authorisation or registration of an administrator in respect of one or more benchmarks only? Very unclear – very clear (5 categories)

Continued use of non-compliant benchmarks

Article 35(3) of the Regulation provides for the possibility that immediate cessation of use of a benchmark in existing contracts may not be appropriate and makes provision for legacy use of individual benchmarks to continue where an administrator's authorisation has been suspended. In such a case, the competent authority may suspend the authorisation/registration of the administrators while allowing the provision of the benchmark and its use until the decision of suspension has been withdrawn.

During that period of time, the use of such a benchmark by supervised entities is permitted only for financial contracts, financial instruments and investment funds that already reference the non-compliant benchmark.

It might be useful for a competent authority also to have this possibility of allowing the continued provision and use of a non-compliant benchmarks for legacy contracts where the authorisation is withdrawn (and not only suspended).

Question 8: Do you consider that the current powers of NCAs to allow the continued provision and use in existing contracts for a benchmark for which the authorisation has

been suspended are sufficient? Totally sufficient – totally insufficient (5 categories). Please explain.

The Commission would also like to receive stakeholders' opinion on the powers of competent authorities to permit the continued use of non-compliant benchmarks under Article 35(3) and under Article 51(4).

Question 9: Do you consider that the powers of competent authorities to permit continued use of a benchmark when cessation of that benchmark would result in contract frustration are appropriate? Very appropriate – not appropriate at all (5 categories). Please explain.

4. SCOPE OF THE BMR

The impact assessment supporting the original proposal for the Benchmark Regulation⁴ did not delineate the scope of the Regulation to specific categories of benchmarks, such as critical benchmarks or to specific underlying markets which are particularly vulnerable to manipulation. To the contrary, the assessment at the time was that “*the vulnerability and importance of a benchmark varies over time. Defining the scope by reference to important or vulnerable indices would not address the risks that any benchmark may pose in the future*”⁵. This means that the Regulation is applicable to all types of benchmarks regardless of their underlying markets. As a consequence, as soon as an index is used in a way that responds to the definition of 'use of a benchmark', it becomes a benchmark and is therefore within the scope of the Regulation.

The Regulation introduces differentiation between benchmarks (e.g., commodity benchmarks and regulated data benchmarks are subject to a different set of rules than, e.g., critical benchmarks). Administrators of significant benchmarks (benchmarks fulfilling the conditions laid down in Article 24(1)) can opt-out from the application of a limited number of detailed requirements of the Regulation.⁶ Non-significant benchmarks (not fulfilling the conditions laid down in Articles 20(1) and 24(1)) are subject to a less detailed set of rules, whereby administrators are able to choose not to apply some requirements of the Regulation. In such a case, the administrator needs to explain why it is appropriate to do so by means of a compliance statement that is published and provided to the administrator's competent authority.⁷

The Commission is empowered to review, every two years, calculation methods that are used to determine the threshold for critical and significant benchmarks.

Over the course of the last years several jurisdictions have begun codifying the IOSCO principles by creating authorisation requirements for financial benchmarks. In the

⁴ Available at <https://eur-lex.europa.eu/legal-content/EN/TXT/?uri=CELEX:52013SC0336>.

⁵ Paragraph 7.1.4. “*Scoping: targeting critical or important benchmarks*”.

⁶ Recital 41 provides that “*Due to the existence of a large variety of types and sizes of benchmarks, it is important to introduce proportionality in this Regulation and to avoid putting an excessive administrative burden on administrators of benchmarks the cessation of which poses less threat to the wider financial system. Thus, in addition to the regime for critical benchmarks, two distinct regimes should be introduced: one for significant benchmarks and one for non-significant benchmarks*”.

⁷ Recital 42 clarifies that “*While non-significant benchmarks could still be vulnerable to manipulation, they are more easily substitutable, therefore transparency to users should be the main tool used for market participants to make informed choices about the benchmarks they consider appropriate for use. For that reason, the delegated acts in Title II should not apply to non-significant benchmark administrators*”.

exercise of assessing third-country jurisdictions with the aim of granting equivalence, the Commission's services note that such third countries have opted for an approach whereby regulation and supervision is limited to the most critical or systemic financial benchmarks administered in their respective jurisdictions. The decision as to whether a benchmark is critical or systemic rests with the relevant competent authority.

The Commission's services are now seeking feedback from stakeholders on how to deal with benchmarks that (i) are not significant in terms of their use in the Union or (ii) certain types of benchmarks that are less prone to manipulation e.g., regulated data benchmarks.

Question 10: Do you consider that the regulatory framework applying to non-significant benchmarks is adequately calibrated? Which adjustments would you recommend?

Completely adequately calibrated – not well calibrated at all (5 categories). Please explain.

Question 11: Do you consider quantitative thresholds to be appropriate tools for the establishment of categories of benchmarks (non-significant, significant, critical benchmarks). If applicable, which alternative methodology or combination of methodologies would you favour?

Completely appropriate – not appropriate at all (5 categories). Please explain.

Question 12: Do you consider the calculation method used to determine the thresholds for significant and critical benchmarks remains appropriate? If applicable, please explain why and which alternatives you would consider more appropriate.

Completely appropriate – not appropriate at all (5 categories). Please explain.

Question 13: Would you consider an alternative approach appropriate for certain types of benchmarks that are less prone to manipulation. If so, please explain for which types.

Completely appropriate – not appropriate at all (5 categories). Please explain.

5. ESMA REGISTER OF ADMINISTRATORS AND BENCHMARKS

In accordance with Article 36 of the Regulation, ESMA maintains a register listing benchmark administrators that have either been authorised or registered in the EU as well as benchmarks and administrators approved for use in the Union through equivalence, recognition or endorsement. According to comments received from benchmark users, the functioning of the register could be improved, e.g., the register currently does not list the benchmarks provided by EU-authorised or -registered administrators, yet several administrators that operate worldwide have only applied for authorisation / registration with respect to a subset of the benchmarks they provide. This means that identification of the benchmarks authorised or registered may prove difficult.

However, for large administrators whose portfolio of benchmarks is subject to frequent changes, maintaining an up-to-date list of benchmarks approved for use in the Union could be challenging. The Commission is therefore seeking views on the functioning of and potential improvements to the register.

Question 14: To what extent are you satisfied with your overall experience with the ESMA register for benchmarks and administrators? If not, how could the register be improved?

Completely satisfied – not satisfied at all (5 categories). Please explain.

Question 15: Do you consider that, for administrators authorised or registered in the EU, the register should list benchmarks instead of/in addition to administrators?

Agree completely – do not agree at all. (5 categories)

6. BENCHMARK STATEMENT

Article 27(1) BMR requires administrators to publish a benchmark statement for each benchmark or, where applicable, for each family of benchmarks. The aim is to enable users of benchmarks to choose appropriate benchmarks and to understand the economic reality that the benchmark or family of benchmark is intended to measure and the risks attached to the benchmarks. Benchmark statements should be of reasonable length but provide users with the key information in an easily accessible manner.

Different practices among administrators may however impede comparability among benchmark statements. While some administrators publish a benchmark statement for each benchmark, others publish it at family level, consolidating information thousands of benchmarks. In addition, the end objectives of the benchmark statement and its articulation with the benchmark's methodology are unclear. As a result, the benchmark statement overlaps to a certain extent with the information disclosed on a benchmark's methodology and may bring, in itself, little added-value.

The objectives of the benchmark statement were further specified in the regulation on climate-related benchmarks and ESG disclosures for all benchmarks. In particular, in order to enable market participants to make well-informed choices, Article 27(2a) of the Benchmark Regulation as amended will require the disclosure of ESG information for all benchmarks – except currency and interest rate benchmarks – in the benchmark statement. Furthermore, the format of the benchmark statement will be standardised for references to ESG factors.

Stakeholders are therefore invited to share their experience and use of the benchmark statement.

Question 16: In your experience, how useful do you find the benchmark statement?

Very useful – not useful at all (5 categories)

Question 17: How could the format and the content of the benchmark statement be further improved?

Question 18: Do you consider that the option to publish the benchmark statement at benchmark level and at family level should be maintained?

Should definitely be maintained – should definitely be removed (5 categories). Please explain.

7. SUPERVISION OF CLIMATE-RELATED BENCHMARKS

In February 2019, the co-legislators reached a political agreement resulting in the creation of two new types of ‘Climate-related Benchmarks’ (the EU Paris Aligned Benchmark and the EU Climate Transition Benchmark). The Regulation also aims to improve transparency regarding Environmental, Social and Governance (ESG) factors by requiring ESG disclosures for all investment benchmarks (excluding interest rates and currency benchmarks). The objectives of the new rules are to orient the choice of investors who wish to adopt a climate-conscious investment strategy, and to address the risk of greenwashing. The minimum standards as to the methodology of those two climate-related benchmarks and the content of ESG disclosures will be further detailed in delegated acts to be adopted by the Commission in early 2020. Benchmark administrators will be required to comply with those requirements by end-April 2020.

The Commission’s services consider that competent authorities should have adequate powers to ensure that a variety of benchmark administrators and investment managers that wish to use climate-related benchmarks to offer investment products based on climate-related benchmarks adhere to the requirements of the Regulation.

This requires that the Regulation empowers competent authorities to verify that any supervised entity mentioned in Article 3(1)(17) of the Regulation only refers to a climate-related benchmark once two conditions are met: (1) the administrator of the climate-related benchmark has received certification that the index is compliant with the Regulation and (2) the investment strategy represented by the supervised entity’s product is aligned with the appropriate climate-related benchmark.

This implies that the competent authority, when authorising an investment firm, UCITS management company or alternative fund manager to offer an investment product that references one of the two climate-related benchmarks, needs to verify (1) whether the chosen reference index complies with the requirements of the Regulation and (2) whether the investment strategy aligns with the chosen benchmark.

Competent authorities should be put in a position to exercise their surveillance over the climate-related benchmarks and have the power to prevent supervised entities from referencing a climate-related benchmark, if either (1) such benchmark does not respect the rules applicable to climate-related benchmarks or (2) the investment strategy referencing the climate-related benchmark is not aligned with the climate-related benchmark.

The Commission is seeking feedback from stakeholders on whether the above set of supervisory powers is sufficient to ensure an effective supervision of the new climate-related benchmarks.

Question 19: Do you consider that competent authorities should have explicit powers to verify (1) whether the chosen climate-related benchmark complies with the requirement of the Regulation and (2) whether the investment strategy referencing this index aligns with the chosen benchmark?

Agree completely – do not agree at all (5 categories). Please explain.

Question 20: Do you consider that competent authorities should have explicit powers to prevent supervised entities from referencing a climate-related benchmark, if such benchmark does not respect the rules applicable to climate-related benchmarks or of the

investment strategy referencing the climate-related benchmark is not aligned with the reference benchmark?

Agree completely – do not agree at all (5 categories). Please explain.

8. COMMODITY BENCHMARKS

Commodity benchmarks are subject to a specific set of rules under the Regulation, with requirements set out in Annex II to the Regulation replacing those in Title II. Annex II reflects the IOSCO Principles for Price Reporting Agencies (PRAs).

There are however certain instances when a commodity benchmark is subject to the 'normal' regime for benchmarks in Title II: if the benchmark is a regulated data benchmark or if the benchmark is based on submissions from contributors the majority of which are supervised entities. This second situation in particular has faced criticism from commodity benchmark providers.

In addition, Article 19(2) BMR sets out that commodity benchmarks are nevertheless subject to the requirements in Title II of the BMR if they meet the following two conditions:

- The commodity benchmark in question is a critical benchmark; and
- The underlying asset is gold, silver or platinum.

Currently, no commodity benchmark fulfils these criteria.

Finally, for commodity benchmarks, there is a *de minimis* threshold below which a benchmark is exempt from the Regulation. It operates on the two conditions that instruments referencing the benchmark can only be admitted to trading on a single trading venue *and* that the total notional amount of those instruments cannot exceed 100 million euro.

In respect of the quantitative element of this condition, commodity benchmark administrators have explained that seasonal effects may imply that a benchmark's usage may exceed the threshold at one point in time within the year and may stay below at another point in time within the same year.

Question 21: Do you consider the current conditions under which a commodity benchmark is subject to the requirements in Title II of the BMR are appropriate?

Completely appropriate – completely inappropriate (5 categories). Please explain.

Question 22: Do you consider that the compound *de minimis* threshold for commodity benchmarks is appropriately set?

Completely appropriate – completely inappropriate (5 categories). Please explain.

9. NON-EEA BENCHMARKS

The Benchmark Regulation stipulates that, from January 2022 onwards, EU supervised entities can only use benchmarks provided by administrators located in a third country if one of three conditions is met: (1) the European Commission has adopted an equivalence

decision; (2) the benchmark administrator has been recognised by an EU competent authority; or (3) the benchmark has been endorsed by an EU supervised entity.

The use of certain non-EEA benchmarks is widespread and economically important, especially for currency or interest rate hedging.

For example, the Benchmark Regulation covers foreign currency exchange (FX) spot rates when they are used in calculating the payments due for EEA listed non-deliverable forwards (NDFs) as long as these contracts are traded on an EEA trading venue. For most major currencies, FX spot rates that meet the criteria of the BMR are available. By contrast, once a currency is not fully convertible, the corresponding FX spot rates will reflect a variety of policy choices and would not be eligible for equivalence, recognition or endorsement.

FX spot rates for not fully convertible currencies may therefore no longer be eligible as a reference rate to calculate the payoff from an NDF once the extended BMR transitional period (31 December 2021) expires.

The question therefore arises whether the Regulation should cover the use of third-country benchmarks by supervised entities in non-deliverable FX forward contracts that are entered into in order to reduce risks directly relating to the commercial activity or treasury financing activity of non-financial counterparties.

Question 23: To what extent would the potential issues in relation to FX forwards affect you?

Very much – not at all (5 categories)

If so, how would you propose to address these potential issues?

Stakeholders argue that for many non EEA indices neither equivalence, recognition nor endorsement provide for legal certainty with regard to the continued use of third-country benchmarks.

Equivalence

The European Commission is currently assessing which non-EEA countries have an equivalent regulatory and supervisory regime in place, focusing on those countries that have either adopted IOSCO compliant benchmark rules or are in the process of preparing such rules in place before 1 January 2022.⁸ Should rules only cover part of the benchmark universe administered in those jurisdictions (i.e., systemic or critical benchmarks only), equivalence assessments will only comprise the benchmarks covered by the relevant rules. Equivalence might therefore not allow for a continued use of the majority of indices administered outside the Union.

Recognition and Endorsement

Recognition of a third-country benchmark administrators requires those administrators to have a legal representative in the Union. Stakeholders argue that, in order for recognition

⁸ On 29 July, the Commission adopted the first decisions stating that the administrators of certain interest rates and foreign exchange rates in Australia and Singapore are subject to legally binding requirements equivalent to the requirements set out under the Benchmark Regulation.

to become effective, tasks and responsibilities of the legal representative would need to be clarified further.

In the absence of licensing income from EU users, many third-country benchmark administrators might not have the incentive to seek either recognition or endorsement of their benchmarks for use in the Union. This would mean that many third-country benchmarks could no longer be used in the Union after the expiry of the (extended) transitional period, by the end of 2021.

<p><u>Question 24</u>: What improvements in the above procedures do you recommend?</p>
