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 (Text with EEA relevance)

REGULATION (EU) 2016/1011 OF THE EUROPEAN PARLIAMENT AND OF THE COUNCIL

of 8 June 2016

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(Text with EEA relevance)

THE EUROPEAN PARLIAMENT AND THE COUNCIL OF THE EUROPEAN UNION,

Having regard to the Treaty on the Functioning of the European Union, and in particular Article 114 thereof,

Having regard to the proposal from the European Commission,

After transmission of the draft legislative act to the national parliaments,

Having regard to the opinion of the European Central Bank[(1)],

Having regard to the opinion of the European Economic and Social Committee[(2)],

Acting in accordance with the ordinary legislative procedure[(3)],

Whereas:

(1) The pricing of many financial instruments and financial contracts depends on the accuracy and integrity of benchmarks. Serious cases of manipulation of interest rate benchmarks such as LIBOR and EURIBOR, as well as allegations that energy, oil and foreign exchange benchmarks have been manipulated, demonstrate that benchmarks can be subject to conflicts of interest. The use of discretion, and weak governance regimes, increase the vulnerability of benchmarks to manipulation. Failures in, or doubts about, the accuracy and integrity of indices used as benchmarks can undermine market confidence, cause losses to consumers and investors and distort the real economy. It is therefore necessary to ensure the accuracy, robustness and integrity of benchmarks and of the benchmark determination process.

(2) Directive 2014/65/EU of the European Parliament and of the Council[(4)] contains certain requirements with respect to the reliability of benchmarks used to price a listed financial instrument. Directive 2003/71/EC of the European Parliament and of the Council[(5)] contains certain requirements on benchmarks used by issuers. Directive 2009/65/EC of the European Parliament and of the Council[(6)] contains certain requirements on the

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use of benchmarks by undertakings for collective investment in transferable securities (UCITS). Regulation (EU) No 1227/2011 of the European Parliament and of the Council[7] contains certain provisions which prohibit the manipulation of benchmarks that are used for wholesale energy products. However, those legislative acts only cover certain aspects of certain benchmarks and they neither address all the vulnerabilities in the provision of all benchmarks, nor do they cover all uses of financial benchmarks in the financial industry.

(3) Benchmarks are vital in pricing cross-border transactions, thereby facilitating the effective functioning of the internal market in a wide variety of financial instruments and services. Many benchmarks used as reference rates in financial contracts, in particular mortgages, are provided in one Member State but used by credit institutions and consumers in other Member States. In addition, such credit institutions often hedge their risks or obtain funding for granting those financial contracts in the cross-border interbank market. Only a few Member States have adopted national rules on benchmarks, but their respective legal frameworks on benchmarks already show divergences regarding aspects such as the scope of application. In addition, the International Organisation of Securities Commissions (IOSCO) agreed principles on financial benchmarks on 17 July 2013 (‘IOSCO principles for financial benchmarks’), Principles for Oil Price Reporting Agencies on 5 October 2012 (‘IOSCO principles for PRAs’) (together, ‘the IOSCO principles’), and since those principles provide a certain flexibility as to their exact scope and means of implementation, Member States are likely to adopt rules at national level which would implement such principles in a divergent manner.

(4) Those divergent approaches would result in fragmentation of the internal market since administrators and users of benchmarks would be subject to different rules in different Member States. Thus, benchmarks provided in one Member State could be prevented from being used in other Member States. In the absence of a harmonised framework to ensure the accuracy and integrity of benchmarks used in financial instruments and financial contracts, or in order to measure the performance of investment funds, in the Union it is therefore likely that differences in Member States' laws will create obstacles to the smooth functioning of the internal market for the provision of benchmarks.

(5) Union consumer protection rules do not cover the particular issue of adequate information on benchmarks in financial contracts. As a result of consumer complaints and litigation relating to the use of benchmarks in several Member States, it is likely that divergent measures, inspired by legitimate concerns of consumer protection, would be adopted at national level, which could result in fragmentation of the internal market due to the divergent conditions of competition attached to different levels of consumer protection.

(6) Therefore, in order to ensure the proper functioning of the internal market and improve the conditions of its functioning, in particular with regard to financial markets, and to ensure a high level of consumer and investor protection, it is appropriate to lay down a regulatory framework for benchmarks at Union level.

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(7) It is appropriate and necessary for that framework to take the form of a regulation in order to ensure that provisions directly imposing obligations on persons involved in the provision, contribution and use of benchmarks are applied in a uniform manner throughout the Union. Since a legal framework for the provision of benchmarks necessarily involves measures specifying precise requirements concerning aspects inherent to such provision of benchmarks, even small divergences on the approach taken regarding one of those aspects could lead to significant impediments in the cross-border provision of benchmarks. Therefore, the use of a regulation, which is directly applicable, should reduce the possibility of divergent measures being taken at national level, and should ensure a consistent approach and greater legal certainty, and prevent the appearance of significant impediments in the cross-border provision of benchmarks.

(8) The scope of this Regulation should be as broad as necessary to create a preventive regulatory framework. The provision of benchmarks involves discretion in their determination and is inherently subject to certain types of conflicts of interest, which implies the existence of opportunities and incentives to manipulate benchmarks. Such risk factors are common to all benchmarks and should be made subject to adequate governance and control requirements. The degree of risk, however, varies, and the approach adopted should therefore be tailored to the particular circumstances. Since the vulnerability and importance of a benchmark varies over time, restricting the scope by reference to indices that are currently important or vulnerable would not address the risks that any benchmark poses in the future. In particular, benchmarks that are currently not widely used could be used more in the future with the result that, in their regard, even a minor manipulation could have a significant impact.

(9) The critical determinant of the scope of this Regulation should be whether the output value of the benchmark determines the value of a financial instrument or a financial contract, or measures the performance of an investment fund. Therefore, the scope should not be dependent on the nature of the input data. Benchmarks calculated from economic input data, such as share prices and non-economic numbers, or values such as weather parameters should thus be included. The framework provided for in this Regulation should also acknowledge the existence of a large number of benchmarks and the different impact that they have on financial stability and the real economy. This Regulation should also provide for a proportionate response to the risks that different benchmarks pose. This Regulation should therefore cover benchmarks which are used to price financial instruments listed or traded on regulated venues.

(10) A large number of consumers are parties to financial contracts, in particular consumer credit agreements secured by mortgages, that reference benchmarks that are subject to the same risks. This Regulation should therefore cover credit agreements as defined in Directives 2008/48/EC[(8)] and 2014/17/EU of the European Parliament and of the Council[(9)].

(11) Many investment indices involve significant conflicts of interest and are used to measure the performance of a fund such as a UCITS fund. Some of those benchmarks are published and others are made available, for free or upon payment of a fee, to the public or a section of the public and their manipulation can adversely affect investors.

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This Regulation should therefore cover indices or reference rates that are used to measure the performance of an investment fund.

(12) All contributors of input data to benchmarks can exercise discretion and are potentially subject to conflicts of interest, and so risk being a source of manipulation. Contributing to a benchmark is a voluntary activity. If any initiative requires contributors to significantly change their business models, they could cease to contribute. However, for entities already subject to regulation and supervision, requiring good governance and control systems is not expected to lead to substantial costs or disproportionate administrative burden. Therefore this Regulation imposes certain obligations on supervised contributors. When a benchmark is determined on the basis of readily available data, the source of such data should not be considered to be a contributor.

(13) Financial benchmarks are not only used in the issuance and manufacturing of financial instruments and contracts. The financial industry also relies on benchmarks for measuring the performance of investment funds for the purpose of return tracking or of determining the asset allocation of a portfolio or of computing the performance fees. A given benchmark can be used either directly as a reference for financial instruments and financial contracts or to measure the performance of investment funds, or indirectly within a combination of benchmarks. In the latter case, the setting and review of the weights to be assigned to various indices within a combination for the purpose of determining the pay-out or the value of a financial instrument or a financial contract or measuring the performance of an investment fund also amounts to use as such an activity does not involve discretion, in contrast to the activity of provision of benchmarks. The holding of financial instruments referencing a certain benchmark is not considered to be use of the benchmark.

(14) Central banks already meet principles, standards and procedures which ensure that they exercise their activities with integrity and in an independent manner. It is therefore not necessary that central banks be subject to this Regulation. When central banks provide benchmarks, especially where those benchmarks are intended for transaction purposes, it is their responsibility to set appropriate internal procedures in order to ensure the accuracy, integrity, reliability and independence of those benchmarks, in particular with respect to transparency in governance and computation methodology.

(15) Furthermore, public authorities, including national statistics agencies, should not be subject to this Regulation where they contribute data to, provide or have control over the provision of, benchmarks for public policy purposes, including measures of employment, economic activity, and inflation.

(16) An administrator is the natural or legal person that has control over the provision of a benchmark and in particular administers the arrangements for determining the benchmark, collects and analyses the input data, determines the benchmark and publishes it. An administrator should be able to outsource to a third party one or more of those functions, including the calculation or publication of the benchmark, or other relevant services and activities in the provision of the benchmark. However, where a person merely publishes or refers to a benchmark as part of that person's journalistic

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activities but does not have control over the provision of that benchmark, that person should not be subject to the requirements imposed on administrators by this Regulation.

(17) An index is calculated using a formula or some other methodology on the basis of underlying values. There exists a degree of discretion in constructing the formula, performing the necessary calculation and determining the input data which creates a risk of manipulation. Therefore, all benchmarks sharing that characteristic of discretion should be covered by this Regulation.

(18) However, where a single price or value is used as a reference to a financial instrument, for example where the price of a single security is the reference price for an option or future, there is no calculation, input data or discretion. Therefore single price or single value reference prices should not be considered to be benchmarks for the purposes of this Regulation.

(19) Reference prices or settlement prices produced by central counterparties (CCPs) should not be considered to be benchmarks because they are used to determine settlement, margins and risk management and thus do not determine the amount payable under a financial instrument or the value of a financial instrument.

(20) The provision of borrowing rates by creditors should not be considered to be benchmark provision for the purposes of this Regulation. A borrowing rate provided by a creditor is either set by an internal decision or calculated as a spread or mark-up over an index (e.g. EURIBOR). In the first case, the creditor is exempt from this Regulation for activity concerning financial contracts entered into by that creditor with its own clients, while in the latter case the creditor is considered to be only a user of a benchmark.

(21) In order to ensure the integrity of benchmarks, benchmark administrators should be required to implement adequate governance arrangements to control conflicts of interest and to safeguard confidence in the integrity of benchmarks. Even where effectively managed, most administrators are subject to some conflicts of interest and could have to make judgements and decisions which affect a diverse group of stakeholders. It is therefore important that administrators have in place a function that operates with integrity to oversee the implementation and effectiveness of the governance arrangements that provide effective oversight.

(22) The manipulation or unreliability of benchmarks can cause damage to investors and consumers. Therefore, this Regulation should set out a framework for retention of records by administrators and contributors as well as for providing transparency about a benchmark's purpose and methodology which facilitates a more efficient and fairer resolution of potential claims in accordance with national or Union law.

(23) Auditing and the effective enforcement of this Regulation requires *ex post* analysis and evidence. This Regulation should therefore set out requirements for adequate record-keeping by benchmark administrators relating to the calculation of the benchmark for a sufficient period of time. The reality that a benchmark intends to measure and the environment in which it is measured are likely to change over time. Therefore it is necessary that the process and methodology of the provision of benchmarks are reviewed on a periodic basis to identify shortcomings and possible improvements.