19 December 2019

EU BENCHMARKS REGULATION - EUROPEAN COMMISSION CONSULTATION
ICMA RESPONSE

The following responses were submitted to the European Commission's consultation on its review of the EU Benchmarks Regulation (the **BMR**) using the European Commission's online questionnaire. In addition, a supporting document was uploaded, the text of which is set out in the Annex to this document.

CRITICAL BENCHMARKS / IBOR REFORM

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.

ICMA response: Useful.

Broader powers for competent authorities to require the administrator to change the methodology of a critical benchmark would be positive because it could help to ensure continuation of critical benchmarks and avoid market disruption which could occur in financial markets upon the cessation of a critical benchmark such as LIBOR or EURIBOR.

However, it will be very important that competent authorities and administrators are mindful of the need to support contractual continuity as far as possible if the methodology of a benchmark is modified.

We also note that competent authorities have the power to compel an administrator to continue publishing the benchmark for a maximum period of five years, pursuant to Article 21(3) of the BMR as amended by Regulation 2019/2089. Noting the Commission's assessment of the importance of continued publication of critical benchmarks for market stability and the fact that many financial instruments referencing critical benchmarks have long maturities or are perpetual, it may be prudent to consider whether competent authorities' powers for mandatory administration should extend to a point in time in which a benchmark is no longer critical, rather than for a specific time period such as five years. Extending authorities' power in this way would be complementary to a broader power to require changes to the benchmark methodology, by strengthening the tools available to authorities to avoid the potentially significant market disruption that could be caused by permanent cessation of a critical benchmark.

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.

ICMA response: These powers should be confined to situations in which mandatory administration of and/or mandatory contributions to a critical benchmark are triggered. It would be difficult to justify applying these powers any earlier, because it would not be clear that a critical benchmark itself, or its representativeness, is at risk at an earlier stage.

CRITICAL BENCHMARKS / ORDERLY CESSATION

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?

ICMA response: Article 28(2) requires supervised entities to "reflect [their contingency plans] in the contractual relationship with clients". Therefore requiring supervised entities to draw up contingency plans to cover instances where a critical benchmark ceases to be representative of its underlying market, and requiring those supervised entities to reflect that in their contracts for bonds and other in-scope financial instruments would seem to result in it being mandatory for new bonds and other in-scope financial instruments to include a "pre-cessation" trigger in fallback provisions.

Many bonds being issued now will contain such a pre-cessation trigger, and this approach has been suggested by the ARRC in the context of bonds referencing USD LIBOR. In addition, the FSB recently called upon ISDA to add pre-cessation triggers into contracts for derivatives; and bond market participants will seek to ensure consistency in fallbacks across bonds and related derivatives. Therefore we query whether it is necessary to mandate this in the BMR.

If this were to be mandated, we assume that any such requirement would not have a retroactive effect i.e. it would only impact upon new contracts and not legacy contracts. This is particularly important in the context of the bond market, where legacy contracts are difficult to change. It would also be very important that any "pre-cessation trigger" envisaged in the BMR was drafted in a clear and objective way.

AUTHORISATION AND REGISTRATION / AUTHORISATION, SUSPENSION AND WITHDRAWAL

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)

ICMA response: Unclear.

Currently, it is not expressly clear in Article 35 that a competent authority can withdraw or suspend the authorisation or registration of an administrator in respect of individual benchmarks. A drafting change to allow this flexibility would be welcome.

AUTHORISATION AND REGISTRATION / CONTINUED USE OF NON-COMPLIANT BENCHMARKS

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.

ICMA response: The powers contained in Article 35(3), which relate to circumstances in which the authorisation or registration of a benchmark administrator has been suspended, appear to be sufficient (save that, as identified in Q7, it would be beneficial if it were clear that these powers can be applied in respect of individual benchmarks rather than in respect of the administrator). However, these powers should also be available when the authorisation or registration of an administrator (or one or more individual benchmarks) has been withdrawn.

This could be achieved by amending Article 35(4) so that a relevant competent authority could allow continued publication and use of a benchmark when the authorisation or registration of an administrator has been withdrawn in the same circumstances in which it can do so when the authorisation or registration of an administrator has been suspended under Article 35(3). In addition, the change suggested in Q7 (i.e. clarifying that competent authorities have the power to withdraw or suspend the authorisation or registration of an administrator in respect of individual benchmarks) should be reflected in both Article 35(3) and an amended version of Article 35(4).

See further the supporting document submitted with this response.

ESMA REGISTER OF ADMINISTRATORS AND BENCHMARKS

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)

ICMA response: Agree.

It would be helpful if the ESMA register were to list authorised benchmarks as well as administrators. This will be particularly important if Article 35 is amended to allow a competent authority to withdraw or suspend the authorisation or registration of an administrator in respect of individual benchmarks.

NON-EEA BENCHMARKS

<u>Question 24</u>: What improvements in the above procedures [*the third country benchmark regime*] do you recommend?

<u>ICMA response</u>: On 10 January 2019, ICMA published an article "*The Impact of the EU BMR on the Use of Third Country Benchmarks*" highlighting the issues surrounding the third country benchmark regime. Those issues remain and it is still unclear how third country benchmarks will be able to be used by supervised entities in the EU after the transition period. Examples of why this is problematic include the need for EU entities to use third country FX benchmarks when hedging foreign currency bond exposures and EU investors wishing to hold bonds linked to third country benchmarks.

The article explains why the current regime is problematic for third country benchmark administrators. At that time, this was evidenced by the lack of a single third country benchmark on ESMA's register. Currently just eight administrators appear on the ESMA register, with only one use of equivalence and one endorsement. While this progress is encouraging, continued efforts to provide timely equivalence rulings, clear guidance and proportionate application of requirements can all contribute positively to assuaging the concerns. Consideration should also be given to expanding the definition of 'public authority' to include third country administrators of FX spot rates in non-convertible and pegged currencies.

Also, it will be crucial that EU27 supervised entities are able to continue using LIBOR under the EU BMR if LIBOR becomes a third country benchmark from an EU27 perspective. Provided the Commission issues a positive equivalence assessment for the UK in respect of the post-Brexit UK regime, UK-based administrators will be able to be included in the ESMA register. Conversely, it will also be important that the other EU critical benchmarks continue to be available for use by supervised entities under a post-Brexit UK regime, which will become possible if the UK issues a positive equivalence assessment for the EU27.

ANNEX
SUPPORTING DOCUMENT UPLOADED WITH THE ICMA RESPONSE

European Commission
Directorate-General for Financial Stability, Financial Services and Capital Markets Union
(Submitted via an online questionnaire)

19 December 2019

Dear Sirs

Response to European Commission Public Consultation Document: Review of the EU Benchmarks Regulation

The International Capital Market Association (ICMA) has provided comments on certain of the issues raised in the European Commission Public Consultation Document: Review of the EU Benchmarks Regulation via the European Commission's online questionnaire.

This document sets out further information in response to Question 8 of the public consultation document.

ICMA is a not-for-profit membership association, headquartered in Switzerland, that serves the needs of its wide range of member firms in global capital markets. As at October 2019 it has more than 580 members in 62 countries. Among its members are private and public sector issuers, banks and securities houses, asset managers and other investors, capital market infrastructure providers, central banks, law firms and others. Its European transparency register number is 0223480577-59. See: www.icmagroup.org.

Additional information in response to 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?

1. It appears that Article 35(3) would operate so that a relevant competent authority could allow the continued publication of a benchmark when the authorisation of the administrator has been suspended if the cessation of the benchmark would result in a force majeure event, frustrate or otherwise breach the terms of *ANY* financial contract or financial instrument, or the rules of *ANY* investment fund, which references that benchmark.

2. While the cessation of a benchmark may not constitute a force majeure event, frustrate or otherwise breach the terms of most outstanding bonds (because contractual fallbacks would apply), we anticipate that there will be other types of financial contracts, financial instruments or rules of investment funds for which cessation of EURIBOR or LIBOR (the key benchmarks referenced in bonds) would result in a force majeure event, frustration or other breach; and so it is highly likely that the

relevant competent authority could allow continued publication and use of EURIBOR or LIBOR under Article 35(3).

3. This is important because we agree with the Commission's assessment in the consultation paper that cessation of a critical benchmark such as EURIBOR or LIBOR would present challenges for market stability. The issues surrounding IBOR cessation are well known to authorities. In the bond market, many fallback provisions that would be triggered by IBOR cessation were not drafted at a time when cessation was envisaged. Typical fallback provisions in legacy bonds are likely to result in many legacy floating rate bonds becoming fixed rate bonds for the remaining life of the bond (due to the typical drafting of fallback provisions in legacy bonds). This may be commercially unacceptable for both issuer and investors. From an investor perspective, such issues may become illiquid and may cease to perform the commercial purpose investors intended for them. In addition, if rates are low at the time that the benchmark ceases to be available (and therefore that low rate is fixed for the remaining life of the bond), there could be a negative mark to market impact for investors. From an issuer perspective, those that aim to match liabilities via other instruments may be adversely affected.

4. In light of this, it would also be helpful to allow continued provision and use of a non-compliant benchmark in legacy contracts where authorisation has been withdrawn (and not only suspended) by amending Article 35(4) so that a relevant competent authority could allow continued publication and use of a benchmark in the same manner as envisaged in Article 35(3). This would help to avoid any question surrounding whether this is possible under Article 51(4) due to its placement in the "Transitional provisions" section of the BMR.

5. In addition, it is not currently clear from the provisions of the BMR whether an administrator would be able to continue publishing a benchmark after its authorisation or registration had been withdrawn. A change to Article 35(4) to make it clear that a relevant competent authority could allow continued publication of a benchmark in the same circumstances as envisaged in Article 35(3) would be useful to rectify this uncertainty.

6. The suggested change would also make it clear that supervised entities could continue to use the benchmark in financial instruments that already reference the benchmark (eg legacy bonds). This would be useful to avoid any uncertainty as to whether a supervised entity bond issuer could continue to make payments under its legacy floating rate bonds in a situation in which the benchmark continues to be published but its administrator is not authorised or registered.

7. In the light of the uncertainties noted above and the potentially significant negative effects of a disorderly cessation or LIBOR or EURIBOR, it would be very helpful if Article 35(4) were to be amended so that a relevant competent authority could allow continued publication and use of a benchmark in the same manner as envisaged in Article 35(3). In addition, the change suggested in Q7 (i.e. clarifying that competent authorities have the power to withdraw or suspend the authorisation or registration of an administrator in respect of individual benchmarks) should be reflected in both Article 35(3) and an amended version of Article 35(4).

Yours faithfully,

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