Cost-benefit Analysis on Draft Technical Standards relating to the Benchmarks Regulation: Final Report

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1 Executive Summary

This report analyses the costs and benefits of ESMA’s draft Technical Standards related to the application of the Benchmarks Regulation (BMR). The Technical Standards assessed relate to:

- oversight function;
- input data;
- transparency of methodology;
- code of conduct;
- governance and control requirements for supervised contributors;
- criteria for significant benchmarks;
- compliance statement;
- benchmark statement;
- authorisation and registration of an administrator; and
- recognition of an administrator located in a third country.

The report has considered both the direct compliance costs to market participants, in both qualitative and, where possible, quantitative terms, as well as undertaking a qualitative analysis of the potential benefits and other — what can be termed ‘indirect’ — costs. Our primary focus is upon those impacts attributable to ESMA’s Technical Standards that are over and above those associable with the BMR itself. The evidence for this analysis comes from in-depth interviews with a range of different market participants including administrators, contributors, and users.

On the following pages, we present the key findings of our analysis for each of the ten areas assessed.
Table 1.1: Analysis of the Technical Standards on Oversight function requirements

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<thead>
<tr>
<th>Oversight function requirements</th>
<th>Qualitative description</th>
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<tr>
<td><strong>Timing</strong></td>
<td>The overarching benefit of the Benchmarks Regulation is in improving the reliability,</td>
<td>Not assessed.</td>
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<td>integrity and quality of benchmarks. ESMA’s RTS reinforce this by setting out composition</td>
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<td>requirements which ensure oversight committees have more balanced representation across</td>
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<td>different stakeholder groups. While providing additional guidance on the composition of</td>
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<td>the oversight function, the RTS retain sufficient flexibility for administrators to tailor</td>
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<td>them to their own specific requirements. This should promote benefits to integrity and</td>
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<td>reduce the costs to national competent authorities who the oversight functions must report</td>
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<td>to. In the case of contributor membership of the oversight committee, the presence of</td>
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<td>contributors should be beneficial, as they have extensive knowledge of the market and</td>
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<td>technical expertise. However, contributors may face conflicts of interest and may be</td>
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<td>best placed to exploit these where the contributors are also the users of the benchmarks;</td>
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<td>and/or the contributors are the sole providers of specialist knowledge. Allowing for the</td>
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<td>presence of persons involved in the provision of relevant benchmarks on oversight</td>
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<td>committees in a non-voting capacity should help to improve the expertise of the oversight</td>
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<td>committee, while not jeopardising its integrity by introducing potential conflicts of</td>
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<td>interest. By allowing for a single overarching oversight function across multiple</td>
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<td>benchmarks, administrators should be able to avoid unnecessary duplication of costs and</td>
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<td>save on secretarial costs for the administrator. An overarching oversight function could</td>
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<td>also improve the effectiveness of oversight. It may create cost incentives to apply higher</td>
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<td>standards of oversight across all benchmarks, rather than to just the more complex</td>
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<td>benchmarks. Furthermore, the oversight function’s ability to act independently of the</td>
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<td>administrator should help ensure that the oversight function is able to report relevant</td>
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<td>cases of misconduct to their competent authority, especially misconduct of the</td>
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<td>administrator itself. Direct costs will accrue almost exclusively to administrators. These</td>
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<td>would involve initial set-up costs in establishing oversight committees or adapting existing</td>
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<td>committees to be compliant with the legislation. This would include the costs of</td>
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<td>identifying and recruiting appropriate members, who meet relevant criteria. It would also</td>
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<td>include the costs of putting in place the procedures, such as the oversight functions</td>
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<td>terms of reference and developing the list of criteria for member selection. This</td>
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<td>encompasses both the costs of staff time involved in developing and implementing these</td>
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<td>various procedures, as well as the costs of staff time in documenting these new</td>
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<td>procedures and making relevant persons aware of them. The scale of the direct costs</td>
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<td>would depend on a number of factors: on the number of oversight committees the</td>
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<td>administrator is required to adopt and their structure; on the size of the administrator</td>
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<td>(with administrators of a large number of benchmarks bearing much lower incremental costs</td>
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<td>per benchmark); on the extent to which administrators are already compliant with the</td>
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<td>requirements (e.g. by applying IOSCO Principles). Our fieldwork indicated that for a</td>
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<td>majority of administrators the need to purely establish an oversight function would not</td>
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<td>require any changes to be made to their existing practices, with a small number of</td>
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<td>respondents suggesting some minor changes. The majority believed that no changes would</td>
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<td>have to be made to the way in which they manage conflicts of interest of the oversight</td>
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<td>function. However, with regard to ensuring the independence of the oversight function, the</td>
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|                                | majority believe...
### Oversight function requirements

<table>
<thead>
<tr>
<th>Timing</th>
<th>Qualitative description</th>
<th>Quantitative description</th>
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that at least minor changes would be required.

**Compliance costs (cont.)**

**Ongoing**

Costs of ensuring that all procedures required of the oversight function continue to be met on an ongoing basis. The oversight function is also required to report all other recommendations on benchmark oversight to the management body and record any instances when the management body acted (or is expected to act) contrary to the recommendations of the oversight committee. This would impose incremental ongoing costs of staff time involved in recording and reporting. Given the restrictions on composition administrators may need to hire more staff members (and also pay staff members more favourably), in order to compensate their expertise, resource commitments and their liability exposure. The administrators would also face costs of providing secretarial services to these committees, which would largely be the cost of staff time in arranging meetings for the oversight committee.

The scale of the ongoing costs would depend on similar factors as the one-off costs.

<table>
<thead>
<tr>
<th>Total annual costs across all administrators with significant and critical benchmarks: €0.4–0.8 million.</th>
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</table>

**Other costs**

The increased presence of external parties, in order to meet the composition requirements, could — contrary to the intentions of the regulation — increase scope for conflicts of interest and jeopardise independence.

There is some potential for ‘undue’ regulatory burden due to: proportionality issues; and issues of regulatory overlaps or inconsistencies. In terms of regulatory overlap, standards inconsistent with IOSCO could mean that administrators align their practices with the internationally agreed IOSCO Principles outside the EU, but the Benchmarks Regulation and ESMA’s RTS within the EU. This may introduce inefficiencies and could mean that ESMA’s RTS are less effective than they would be if they complied with the IOSCO Principles that guide good practice more internationally.

In terms of the potential implications of having oversight committees which oversee multiple benchmarks, there is likely a trade-off between efficacy and cost here. However, oversight committees for families of benchmarks could be counter-productive if drawn too widely.

There may also be detrimental impacts on benchmark users. If the compliance costs incurred by administrators are largely passed through to users as higher fees, users may look at alternate measures. If costs are relatively greater for smaller administrators, then this could drive sector consolidation either of administrators, or of benchmarks, or of both. This could result in efficiency gains, on the one hand, but could also act, as a knock-on effect, to increase the number of significant and critical benchmarks. Another knock-on effect of this could be a move away from well-formulated benchmark products to less well-formulated versions in order for benchmark users to reduce costs.

Not assessed.
### Executive Summary

**Table 1.2: Analysis of the Technical Standards on Input data**

<table>
<thead>
<tr>
<th>Input data</th>
<th>Qualitative description</th>
<th>Quantitative description</th>
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<tbody>
<tr>
<td><strong>Timing</strong></td>
<td>The requirements regarding the appropriateness of data should lead to the creation of a consistent control framework that would increase the quality of critical and significant benchmarks. Specifying the requirements means that less discretion is left to administrators. Market participants view this RTS to be of significant benefit to market confidence. Due to the ongoing nature of the data scrutiny requirements the quality of the benchmark would be consistent throughout its life cycle. Increased accuracy — resulting from improved quality controls of the data — might improve efficiency of the use of the benchmark. Oversight controls and conflicts of interest mitigation would reduce the probability of errors (intentional or unintentional). This would improve quality and accuracy of the input data, potentially increasing its credibility among users. For contributors and administrators that might mean additional sales or sales recovery. Trainings for front office staff involved in input data contribution would reduce the probability of future penalties for contributors for not complying with the regulation.</td>
<td><strong>Benefits</strong></td>
</tr>
<tr>
<td><strong>Compliance costs</strong></td>
<td>In terms of data appropriateness and verifiability, administrators would incur one-off set up costs. However, it should be kept in mind that the data requirements for the administrators of critical benchmarks and those administrators of significant benchmarks who comply with Article 8 BMR, do not go beyond requirements in the BMR. The costs are likely to be less significant for administrators of regulated data benchmarks (as they may choose not to apply the validation procedures). The views of the interviewed market participants on the impacts on processes around appropriateness and verifiability of data were mixed, with one quarter of respondents indicating that major changes would be required. Of those who suggested no changes required as a result of these RTS, some attributed this to the fact that the data they are using is mostly regulated/transaction based data and, as such, it is easier to comply with the requirements, or else that their national regulator already paid close attention to breaches in input data procedures. In terms of front office contributions, contributors could incur costs related to training, developing internal oversight procedures in line with the three lines of defence and conflicts of interest policies. Incremental costs related to internal oversight are likely to be low as three lines of defence architecture seems to be already implemented by a significant number of contributors, and the internal oversight requirements could be less onerous for some contributors. Our fieldwork indicated that administrators expected little to no changes with regard to the monitoring and oversight of front office contributions.</td>
<td><strong>Compliance costs</strong></td>
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Not assessed.
## Input data

<table>
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<tr>
<th>Timing</th>
<th>Qualitative description</th>
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<tr>
<td>Compliance costs</td>
<td>Administrators would incur ongoing costs of transmission and storage of data. As in the case of one-off costs, data requirements for the administrators of critical benchmarks and those administrators of significant benchmarks who comply with Article 8 BMR do not go beyond requirements in the BMR. Certain costs might nevertheless be incurred to ensure compliance against the final formulation of the RTS.</td>
<td></td>
</tr>
<tr>
<td>Ongoing</td>
<td>In terms of front office contributions, contributors could incur costs related to training. Incremental costs related to internal oversight are likely to be low as three lines of defense architecture seems to be already implemented by a significant number of contributors, and the internal oversight requirements could be less onerous for some contributors.</td>
<td>Not assessed.</td>
</tr>
<tr>
<td></td>
<td>Our fieldwork indicated that administrators expected little to no changes with regard to the monitoring and oversight of front office contributions.</td>
<td></td>
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<tr>
<td>Other costs</td>
<td>If the requirements are too onerous — either in terms of data requirements or rules around front office contributions — contributors could be discouraged from providing data to administrators. This would lead to a deterioration of benchmarks quality and representativeness. This would be less likely to happen in the case of supervised/small contributors which may be allowed by administrators of significant benchmarks to maintain the existing internal/simplified oversight structures.</td>
<td>Not assessed.</td>
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<td>During our fieldwork, concern was voiced that the administrator of a benchmark to which one is contributing would be able to view some of their highly sensitive exposure data, in order to verify the input data the administrator is receiving, which would be even more problematic where the administrator is also a direct competitor of that contributor. It was further suggested that this was a significant enough issue to review whether a contributor wishes to continue contributing. If contributors withdraw from the market this could have implications for data costs and innovation moving forward. Even if contributors became comfortable with these issues, sharing of these types of data would require the establishment of new internal data links within the contributing firm.</td>
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### Table 1.3: Analysis of the Technical Standards on Transparency of methodology

**Transparency of methodology**

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<th><strong>Timing</strong></th>
<th><strong>Qualitative description</strong></th>
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<tr>
<td><strong>Benefits</strong></td>
<td>The transparency of the key elements of the methodology as well as procedures governing reviews and approvals of the methodology might discourage administrators from data manipulation and other kinds of abuse. The RTS might also promote investor confidence as they would be able to verify that the benchmark they use is suitable for them (e.g. users would be able to compare different benchmarks which could create a more effective competitive environment. As such, not only investor would be equipped in tools allowing them to make better decisions but also, due to increased comparability of benchmarks, competition between administrators could induce them to improve their methodologies and internal monitoring of their appropriateness. Furthermore, the RTS might support competent authorities in their supervisory roles, which in turn could improve investors’ protection. Publishing the procedure used for internal review of methodology would keep the administrators accountable in following the same process consistently over time. In case of administrators of critical benchmarks and those administrators of significant benchmarks who would not opt out, publishing the panel composition and eligibility criteria for becoming a member of the methodology panel, as well as disclosing the bodies/functions of those involved in the methodology review would reduce the likelihood of conflicts of interest. Publishing the proposed changes in the methodology and following a consultation procedure eases the transition between methodologies for users. This might reduce volatility of the instruments relying on benchmarks.</td>
<td>Not assessed.</td>
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<tr>
<td><strong>Compliance costs</strong></td>
<td>While some one-off costs might in theory arise due to the Transparency of methodology requirements, we do not expect any incremental costs that could be attributed to this RTS. Our fieldwork suggested that administrators anticipate making minor to no changes in relation to this RTS.</td>
<td>No significant incremental costs.</td>
</tr>
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<td><strong>Compliance costs (cont.)</strong></td>
<td>Direct ongoing costs might include: preparing and publishing the methodology explanation to be disclosed, (additional) staff required to conduct regular internal reviews and consultations in case of methodology changes. Initially, these costs could be higher (in order to prepare the relevant documents and design the control procedures) and then decline over time, when the methodology would only require updates and monitoring. Our fieldwork suggested that administrators anticipate making minor to no changes in relation to this RTS. Changes to internal review processes were seen as, marginally, the most significant. Furthermore, none of the benchmark users who responded to the survey said that they would review their use of the benchmark given its methodology, although some administrators indicated that there would be some minor changes in this respect.</td>
<td>Total ongoing annual costs across all administrators of significant and critical benchmarks: €0.1–€0.3 million.</td>
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Executive Summary

Transparency of methodology

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<th>Timing</th>
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<td>There is a trade-off between intellectual property rights and transparency. Too much information might enable front-running. In that respect, publishing too detailed methodology could have particularly negative consequences when input data is broadly available (as in the case of regulated data benchmarks). This risk might also be higher for benchmarks of relatively illiquid securities where the methodology is disclosed in sufficient detail to allow third parties to profit — at the end investor’s expense — from the anticipated liquidity demand arising from a forthcoming benchmark rebalance. Failing to protect intellectual rights might discourage innovation and contributors’ participation as well as impact competition. To the extent that the key elements of the methodology to be disclosed are sufficiently high-level to avoid violation of intellectual rights, this costs would be small or non-existent.</td>
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<tr>
<td>Other costs</td>
<td>Not assessed.</td>
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Table 1.4: Analysis of the Technical Standards on Code of conduct

Code of conduct

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<td>The code of conduct RTS should help improve transparency and clarity of the contributions made, and their consistency over time. Moreover, it is the only part of ESMA’s RTS that places specific provisions on contributors who are non-EU entities. By imposing a clearer framework for contributions and detailing some of the underlying policies and processes that contributors should have in place, the RTS should also help to provide a clearer audit trail and thus improve accountability. The requirements for submitters should ensure that only those individuals with the necessary skills, knowledge, training and experience are able to submit input data, thus improving administrator confidence in the data provided by contributors. The requirement for the contributor to report suspicious transactions to the relevant competent authorities means that the latter should be aware of any infringements and provide them with the information necessary to undertake legal and supervisory duties.</td>
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<tr>
<td>Benefits</td>
<td>Not assessed.</td>
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The code of conduct could impose compliance costs on both administrators of critical interest-rate and commodity benchmarks and contributors that contribute to these benchmarks (including contributors who are non-EU entities, but contribute to administrators within the scope of the regulation).

In terms of the costs to administrators, they are likely to incur human resource costs in developing the various elements required in the code of conduct — and embedding this code into its organisation (e.g. through training, as required by the RTS). The materiality of these costs would depend on the extent to which such documentation is already produced, and on the extent to which the administrator has to adapt the code of conduct for different benchmarks. That said, it is likely that the code of conduct would share a lot of common elements across different benchmarks (despite some variations) and, therefore, these one-off costs are likely to be less significant on a per benchmark basis for those administrators operating a large number of benchmarks.

Our fieldwork suggested that, while a majority of administrators have some form of code of conduct in place with their contributors, they also anticipate that they will need to make minor tweaks to become compliant with the new code of conduct requirements.

Contributors could also face costs as a result of the code of conduct RTS. They are likely to incur people costs in understanding the new requirements, which could be exacerbated if the contributor contributes to several different benchmarks, and/or several different administrators, each of which has a slightly different code of conduct. Especially for contributors contributing to multiple (critical) benchmarks, it may impose higher resource costs, if the contributor has to read across the requirements of the various codes of conduct in order to develop practices and procedures that are simultaneously compliant with all the codes of conduct.

The record-keeping requirements may require the contributors to develop databases to sort and find the information when requested by the administrator. The materiality would, in part, depend on the extent to which such records are already kept in accordance with other requirements or guidance on market practices.

The requirements concerning conflicts of interest may be particularly burdensome for contributors as it could have implications for contributors’ IT systems, corporate policies and remuneration structures, including the possible need for Chinese walls, physical separation of staff and more thorough remuneration policies for submitters, although contributors may already have made many such changes in order to adhere to the IOSCO principles.

Our fieldwork suggested that the impact of these revised codes of conduct on contributors is more material than the costs to the administrators of actually producing these revised codes of conduct.

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<th>Code of conduct</th>
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<td><strong>Timing</strong></td>
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**Total cost to affected administrators:** €90,000 – €160,000.

**Total cost to contributors:** €0.8 – €4.8 million.
### Code of conduct

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<tr>
<th>Compliance costs (cont.)</th>
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<tbody>
<tr>
<td>Ongoing</td>
<td></td>
<td>In terms of ongoing costs, administrators would face the periodic costs of updating the code of conduct documentation as appropriate to reflect changes in the benchmark itself or its underlying methodology. The administrator is also required to specify as part of the code of conduct the frequency for reviews of the framework for the contributors’ contribution process, which will lead to ongoing review costs for the administrator. Contributors might face costs of additional human resource necessary to comply with the requirements related to reporting, due diligence, record-keeping, monitoring or training. They may also incur additional ongoing costs on a lumpier basis, determined by when the administrator makes changes to the benchmarks and/or their underlying methodologies. The magnitude of these costs would depend on the extent to which the contributors already have these procedures in place and whether, and if so to what extent, they would need to be adjusted to become compliant.</td>
<td>Not assessed.</td>
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### Other costs

There may be concern that the additional requirements imposed on contributors could discourage them from contributing data, especially if the administrator’s code of conduct is seen to overly constrain contributors’ own corporate governance decisions. This may be particularly true where contributions are made voluntarily, where the contributors are not supervised entities in the EU and/or where the input data is used for other purposes aside from constructing the benchmark.

One survey respondent noted that there could be broader consequences as a result of the impact on contributors, as contributors may require higher fees in order to recover the costs of the regulation or may move away from the business altogether, which would be detrimental to innovation.

The requirements may be seen as particularly burdensome for contributors based outside the EU, who contribute to EU-based administrators’ benchmarks.
Table 1.5: Analysis of the Technical Standards on Governance and control requirements for supervised contributors

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<tr>
<th>Governance and control requirements for supervised contributors</th>
<th>Qualitative description</th>
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<tbody>
<tr>
<td><strong>Benefits</strong></td>
<td>General systems and controls might restore transparency and users’ confidence. This could lead to increased sales or sales recovery. The governance and control requirements are seen as significant for improving regulatory oversight and market confidence. Identifying submitters as well as alternates in case a submitter becomes unavailable should ensure continuity of the data provided to administrators. A clear procedure governing sign-offs could reduce the risk of errors and/or manipulation by a single actor. Moreover, the risk of manipulation might be further reduced by minimising the interaction between supervised contributors and front office staff. Laying out the framework for expert judgement encourages consistency in developing the benchmark, as well as leaving less room for manipulation in situations where manipulation is most likely to occur. The requirement to periodically review the process of contributing data could help ensuring high quality of submitted data in a consistent way. Developing conflicts of interest procedures maintains transparency and improves investor confidence. Record keeping requirements are likely to facilitate the supervisory role of competent authorities.</td>
<td>Not assessed.</td>
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<tr>
<td><strong>Compliance costs</strong></td>
<td>Interviewed contributors’ were consistent in expecting only minor changes as being necessary as a result of the Technical Standards, including staff training, measures around avoiding conflicts of interest, record-keeping and other systems and controls.</td>
<td>Total cost to supervised contributors: €1.2–€6.4 million.</td>
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<tr>
<td><strong>Compliance costs (cont.)</strong></td>
<td>Ongoing costs might include: additional costs for upgraded data monitoring systems (operational and IT costs), staff training, and external audits could be incurred by contributors. These potential costs were not confirmed in our fieldwork, and thus we assume them to be negligible.</td>
<td>Ongoing costs would be negligible.</td>
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<tr>
<td><strong>Other costs</strong></td>
<td>If the systems and controls requirements are too burdensome, then the contributor could be deterred from providing information, hurting the quality and representativeness of the benchmark. Excessive sign-off procedures could cause delays when submitting information, which could be particularly damaging to the benefits created by developing automated processes. This cost would be partly mitigated by ESMA acknowledging that in certain circumstances, where a full sign-off procedure is not proportionate, other measures can be implemented instead.</td>
<td>Not assessed.</td>
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Table 1.6: Analysis of the Technical Standards on Criteria for significant benchmarks

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<th>Criteria for significant benchmarks</th>
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<td><strong>Timing</strong></td>
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<td>Benefits</td>
</tr>
<tr>
<td>Compliance costs</td>
</tr>
<tr>
<td>Compliance costs (cont.)</td>
</tr>
<tr>
<td>Other costs</td>
</tr>
</tbody>
</table>

Table 1.7: Analysis of the Technical Standards on Compliance statement

<table>
<thead>
<tr>
<th>Compliance statement</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Timing</strong></td>
</tr>
<tr>
<td>Benefits</td>
</tr>
</tbody>
</table>
## Compliance statement

<table>
<thead>
<tr>
<th>Timing</th>
<th>Qualitative description</th>
<th>Quantitative description</th>
</tr>
</thead>
<tbody>
<tr>
<td>Compliance costs</td>
<td>The incremental direct compliance costs are not likely to be substantial, and largely limited to reporting costs. This outcome is also likely to be facilitated by the requirement of submitting only one compliance statement for all benchmarks exempted from certain BMR requirements.</td>
<td>Incremental compliance costs are expected to be negligible.</td>
</tr>
<tr>
<td></td>
<td>Significant compliance costs could be generated where the listings of individual benchmarks issued by an administrator change frequently.</td>
<td></td>
</tr>
<tr>
<td>Compliance costs (cont.)</td>
<td>The incremental direct compliance costs are not likely to be substantial, and largely limited to reporting costs. This outcome is also likely to be facilitated by the requirement of submitting only one compliance statement for all benchmarks exempted from certain BMR requirements.</td>
<td>Incremental compliance costs are expected to be negligible.</td>
</tr>
<tr>
<td></td>
<td>Significant compliance costs could be generated, however, where the listings of individual benchmarks issued by an administrator change frequently.</td>
<td></td>
</tr>
<tr>
<td>Other costs</td>
<td>The requirement to update the compliance statement in response to a change in methodological inputs that implies a change in the &quot;exemption&quot; situation of the benchmark may dissuade administrators from changing the relevant methodologies as often as they would deem optimal. If the frequency of methodological updates is limited, then this could reduce the representativeness of the economic reality that is meant to be measured by a given benchmark and, thus, expose users to unanticipated outcomes when including the relevant instruments in their investment strategies.</td>
<td>Not assessed.</td>
</tr>
</tbody>
</table>

### Table 1.8: Analysis of the Technical Standards on Benchmark statement

<table>
<thead>
<tr>
<th>Timing</th>
<th>Qualitative description</th>
<th>Quantitative description</th>
</tr>
</thead>
<tbody>
<tr>
<td>Benefits</td>
<td>By increasing the clarity of the documents published, and improving the comparability of benchmark statements produced by different administrators, the RTS should increase transparency in the benchmarks landscape and heighten user caution, thus improving regulatory oversight and increasing user confidence.</td>
<td>Not assessed.</td>
</tr>
<tr>
<td></td>
<td>Users of benchmarks will likely benefit most, as they would be provided with information on what a given benchmark intends to measure and its susceptibility to manipulation. Administrators are also likely to benefit as there would be less room for errors in the application of the requirement and less scope for legal uncertainty.</td>
<td></td>
</tr>
<tr>
<td>Compliance costs</td>
<td>The draft RTS distinguishes between different types of benchmarks, and incremental reporting costs are likely to be higher for administrators of interest rate and commodity benchmarks — and administrators of critical benchmarks.</td>
<td>Total cost borne jointly by administrators and contributors associated with repapering agreements: €1.3–€5.3 million.</td>
</tr>
<tr>
<td></td>
<td>Providing an indication of the size of some markets in which a benchmark is referenced, even at a very high level, may be difficult (or even impractical), thus creating additional direct costs for administrators (e.g. one-off IT investments, ongoing human resources employed)</td>
<td></td>
</tr>
<tr>
<td></td>
<td>Outlining the professional profiles of the contributors to commodities benchmarks increases compliance costs for them and the administrators as additional information would need to be obtained and included in the benchmark statement. Such information could also be subject to confidentiality arrangements, thus creating additional costs in respect of any re-papering of any data licensing agreements.</td>
<td></td>
</tr>
</tbody>
</table>
### Benchmark statement

<table>
<thead>
<tr>
<th>Compliance costs (cont.)</th>
<th>Timing</th>
<th>Qualitative description</th>
<th>Quantitative description</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>Ongoing</td>
<td>With regards to information reflecting the application of discretion administrators could incur additional direct costs in terms of making sure the explanations offered are adequate and concise, verification checks and peer reviews either by other members of staff or external resources, and other reporting costs.</td>
<td>No material incremental costs.</td>
</tr>
</tbody>
</table>

**Other costs**

No other costs identified.

n/a

---

#### Table 1.9: Analysis of the Technical Standards on Authorisation and registration of administrator

**Authorisation and registration of administrator**

<table>
<thead>
<tr>
<th>Compliance costs</th>
<th>Timing</th>
<th>Qualitative description</th>
<th>Quantitative description</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>One-off</td>
<td>The RTS should help in ensuring more robust oversight of benchmark administrators and a more consistent approach across the EU.</td>
<td>Not assessed.</td>
</tr>
<tr>
<td></td>
<td></td>
<td>The additional information should help national competent authorities to evaluate the sufficiency of administrators’ policies and procedures relating to benchmark provision.</td>
<td></td>
</tr>
<tr>
<td></td>
<td></td>
<td>Documentation of procedures, systems and resourcing structures should also help to improve accountability and transparency within the administrator.</td>
<td></td>
</tr>
<tr>
<td></td>
<td></td>
<td>These changes should ultimately promote higher quality and more robust benchmarks and thus improve the integrity of benchmarks amongst users. This could in turn encourage users to increasingly look at the benchmarks produced by administrators outside their own jurisdictions, thus improving market competition.</td>
<td></td>
</tr>
<tr>
<td></td>
<td>One-off</td>
<td>The RTS are likely to impose one-off compliance costs in the form of additional documentation and reporting costs on benchmark administrators and publishers of relevant indexes. This will require staff resources, largely from the compliance team. In cases where new drafting of documentation is required, staff resourcing requirements are likely to be more material, especially as this may require staff from a number of different departments liaising with each other in producing finalised versions of required documentation.</td>
<td></td>
</tr>
<tr>
<td></td>
<td></td>
<td>Compliance costs could be limited by the fact that information can be submitted for families of benchmarks provided none of the benchmarks are critical. This could reduce the costs of compliance per benchmark. Compliance costs are also limited by the fact that, where there is duplication of information requirements across RTS, the information can be provided to satisfy both requirements in order to reduce the duplication of costs.</td>
<td></td>
</tr>
<tr>
<td></td>
<td></td>
<td>Our fieldwork suggests that administrators saw the systems and controls costs to be a more major cost driver than human resource costs.</td>
<td>Total costs to administrators: €0.7–€2.0 million.</td>
</tr>
<tr>
<td></td>
<td></td>
<td>The above compliance costs would be less material for administrators of non-significant benchmarks and those non-administrator entities providing indexes for use as benchmarks who are already supervised entities.</td>
<td></td>
</tr>
</tbody>
</table>
Authorisation and registration of administrator

<table>
<thead>
<tr>
<th>Compliance costs (cont.)</th>
<th>Timing</th>
<th>Qualitative description</th>
<th>Quantitative description</th>
</tr>
</thead>
<tbody>
<tr>
<td>Ongoing</td>
<td></td>
<td>Additional documentation and reporting might, in theory, require administrators to increase staff resources. That said, our fieldwork suggests that administrators did not see human resource costs to be a major cost driver.</td>
<td>Ongoing incremental costs should be negligible.</td>
</tr>
</tbody>
</table>

Other costs

A potential consequence of this would be raised barriers to entry to administration activity. This, in conjunction with the impact of the other Technical Standards / the BMR itself raising the cost of undertaking benchmark administration activity, may reduce the pace of innovation and also drive consolidation. A more concentrated benchmark market could also impact on the pricing of benchmark access.

In our fieldwork, it was suggested that the BMR is the strictest regulation so far globally, and that this could have detrimental impact on EU benchmark administrators who are competing with non-EU benchmark administrators on a global scale.

Table 1.10: Analysis of the Technical Standards on Recognition of an administrator located in a third country

<table>
<thead>
<tr>
<th>Timing</th>
<th>Qualitative description</th>
<th>Quantitative description</th>
</tr>
</thead>
<tbody>
<tr>
<td>Benefits</td>
<td>The RTS should contribute to building a European supervisory culture that ensures consistent approaches across NCAs. In this case, NCAs would possess a pre-defined well-structured framework, based on which they should more easily and rapidly be able to conduct their assessments. Such an outcome is also likely to limit legal uncertainty as well as incentives to engage in jurisdiction shopping by providers. An additional benefit is the externality (in terms of enhanced protection) for investors and consumers in other countries as the benchmarks provided both in the EU and the third-country would be scrutinised on the basis of a consistent information set.</td>
<td>Not assessed.</td>
</tr>
<tr>
<td>Compliance costs</td>
<td>Several elements of the requirements may be more onerous for small third-country administrators. Specifically, during the application process, third-country administrators would need to indicate the nature and characteristics of the benchmarks provided, as well as an indication of the relevant underlying market or economic reality. A critical assumption here is the number of non-EU administrators that would be expected to seek this route. This is complicated by the potential for additional cost burdens and regulatory risk to deter some current benchmark providers from continuing with serving the EU market.</td>
<td>Total cost to non-EU administrators: €0.3–€1.3 million.</td>
</tr>
<tr>
<td>Ongoing</td>
<td>There is a substantive ongoing information-provision requirement to fulfil by non-EU administrators</td>
<td>Total annual cost to non-EU administrators: €0.2–0.8 million.</td>
</tr>
</tbody>
</table>
Recognition of an administrator located in a third country

<table>
<thead>
<tr>
<th><strong>Timing</strong></th>
<th><strong>Qualitative description</strong></th>
<th><strong>Quantitative description</strong></th>
</tr>
</thead>
<tbody>
<tr>
<td>Other costs</td>
<td>In case the costs of obtaining recognition in the EU are considerable, small third-country benchmark providers may choose not to apply for recognition in Europe in the first place. This was seen as a material risk by various market participants, particularly those based in Asia. An indirect cost that may arise in this respect is the opportunity cost of sub-optimal investment behaviour. Users that provide financial products in Europe referencing such benchmarks could be particularly harmed if administrators remove them from the market. This would expose the designer of the financial instrument referencing the benchmark in question to additional costs involved in altering the product so as to include a new, and possibly even inferior benchmark. In the latter case, the end-user would not only face potentially higher costs, but obtain inferior use.</td>
<td>Not assessed.</td>
</tr>
</tbody>
</table>
2 Introduction

This report was commissioned from Europe Economics by the European Securities and Markets Authority (ESMA) to prepare robust cost-benefit analysis of ten draft Technical Standards related to the implementation of the Regulation (EU) 2016/1011 Benchmarks Regulation (BMR), under contract PROC/2016/02.

2.1 ESMA’s Technical Standards

The scope of our work covers the following aspects of the BMR.

- **Oversight function requirements.** ESMA is to develop Regulatory Technical Standards to determine the procedures regarding the oversight function and its characteristics, including its composition and its positioning within the organisational structure of the administrator, so as to ensure the integrity of the function and the absence of conflicts of interest.

- **Input data.** ESMA is to develop Regulatory Technical Standards to specify further how to ensure that input data is appropriate and verifiable, as well as the internal oversight and verification procedures of a contributor that the administrator has to ensure are in place in order to ensure the integrity and accuracy of input data.

- **Transparency of methodology.** ESMA is to develop Regulatory Technical Standards to specify further the information to be provided by an administrator, taking into account: the need to disclose those elements of the methodology in sufficient detail to allow users to understand how a benchmark is provided and to assess its representativeness, its relevance to particular users and its appropriateness as a reference for financial instruments and contracts.

- **Code of conduct.** ESMA is to develop Regulatory Technical Standards to further specify the elements of the code of conduct for different types of benchmarks, and in order to take account of developments in benchmarks and financial markets.

- **Governance and control requirements for supervised contributors.** ESMA is to develop Regulatory Technical Standards to specify further the requirements concerning governance, systems and controls, and policies, taking into account (among other things) the different characteristics of benchmarks and supervised contributors, and the risks of manipulation of the input data and the nature of the activities carried out by the supervised contributors.

- **Criteria for significant benchmarks.** ESMA is to develop Regulatory Technical Standards to further specify the criteria to be used by a competent authority in the context of over-riding the opt-out by an administrator of one or more of the requirements of BMR Articles 4(2), points (c), (d) and (e) of Article 4(7), point (b) of Article 11(3) and Article 15(2).

- **Compliance statement.** ESMA is to develop implementing Technical Standards setting a template for the compliance statement.

- **Benchmark statement.** ESMA is to develop Regulatory Technical Standards to further specify the contents of the benchmark statement and the cases in which an update of such statement is required, distinguishing for different types of benchmarks and sectors as set in the BMR.

- **Authorisation and registration of an administrator.** ESMA is to develop Regulatory Technical Standards to further specify what information to be provided in the application for authorisation and for registration, taking into account that authorisation and registration are distinct processes.
• Recognition of third country administrators. ESMA is to develop Regulatory Technical Standards to determine the form and content of the application by an administrator located in a third country for recognition with the competent authority of its Member State of reference.

2.2 Structure of this report

This report describes the tasks carried out and our findings. The remainder of this report is structured as follows.

• Section 3 provides an overview of the approach of the current benchmark landscape based on our findings.
• Section 4 sets out the results of our research into the likely impacts of ESMA’s draft Technical Standards in the form of qualitative and quantitative cost-benefit analysis.
• Finally, the Appendix (Section 5) summarises the primary data gathering that we have conducted.
An important task in the study is to elaborate on the current benchmark landscape in Europe. This is of course important in providing context and background information. However, the role of this task for the purpose of this study is more nuanced.

- First, it identified different types of stakeholders that could be affected by the BMR and ESMA’s Technical Standards.
- Second, it provided a useful means of identifying potential candidates for the stakeholder engagement programme.
- Third, and perhaps most importantly, it provides an indication of the relevant scalars for any impacts estimated through the primary data gathering, i.e. the likely magnitude of effects given the approximate number of benchmarks available.

In this section, we summarise our approach and findings.

3.1 Approach to identifying benchmarks

3.1.1 What information would ideally be collected?

The BMR distinguishes between certain types of benchmarks, namely: interest rate, commodity and regulated data benchmarks; and critical, significant and non-significant benchmarks. This typology, though likely to be a subset of all possible types of benchmarks, provides a natural framework for the purpose of this study since we are concerned with estimating the impacts of ESMA’s draft Technical Standards which also follow this typology.

Therefore, in an ideal scenario we would seek to populate the following table:

**Figure 3.1: Benchmark typology**

<table>
<thead>
<tr>
<th></th>
<th>Interest</th>
<th>Commodities</th>
<th>Regulated data</th>
<th>Total</th>
</tr>
</thead>
<tbody>
<tr>
<td>Critical</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Significant</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Non-significant</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Total</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
</tbody>
</table>

Source: Europe Economics.

However, our ability to establish this information is limited by the data that are available. An important restriction here is the ability (or inability) of administrators to distinguish critical, significant and other benchmarks.

3.1.2 Identification of critical and significant benchmarks

The visibility amongst administrators of the economic value associated with the benchmarks that they administer is often low. Where a benchmark is used elsewhere in the business then such knowledge is normally better. Various market participants develop a ‘benchmark’ that is bespoke to a given client and circumstance. In these cases, knowledge over the value of transactions is perfect — but such bespoke
benchmarks would not have sufficient value of transactions linked to them to qualify as significant, let alone critical.

Those benchmarks with multiple users are another case. The administrators of such benchmarks do not currently have access to information that would enable them to make a robust assessment or quantification of the full value of activity associated with a benchmark. These administrators tended to fall into two camps: those who considered it infeasible to make such a determination, and those who considered the exercise feasible but only at high expense (through disruptive change in terms of fully identifying the usage of a given benchmark, finding data sources and evaluating these). Even in the latter case, there was concern that customers would consider the relevant information to be commercially sensitive and so accessing such information on a regular basis could be difficult.

3.1.3 Our approach

From our desk research and from discussions with ESMA, we have established that there are no data sources that comprehensively detail the universe of benchmarks (either at a high level, i.e. the total number of benchmarks available, or at a more granular level, i.e. the different types of benchmarks offered). We have therefore examined a range of sources to try and identify as many possible benchmarks as possible. It is worth noting here again that the purpose of this task is not to establish definitively or precisely the number of benchmarks that are available; rather, we are seeking to understand the likely scale of the benchmark universe to help determine the magnitude of any identified impacts associated with ESMA’s Technical Standards.

The different sources of information that we have examined as part of our desk-based research are as follows.

- We analysed data from Bloomberg on the indices underlying securities and commodities traded in the EU. For example, we searched for all ETF and other packaged investment products listed on Bloomberg and then, from within the descriptions of these, identified the reference benchmarks.
- In addition, we reviewed the responses to the European Commission’s consultation on the BMR and responses to ESMA’s discussion paper to identify benchmark administrators. We then reviewed the websites of each of these administrators to investigate how many benchmarks each offered.
- We also reviewed the websites of all the markets listed on ESMA’s register of regulated markets to see how many benchmarks are available.
- Finally, we compared the responses received from administrators participating in our fieldwork to the information collected from the other sources.

We summarise our findings below.

3.2 Outline of the current landscape

The desk-top research identified about 100 administrators, about half of which were regulated markets (and several others were stock exchanges based outside the EU). Given the insight that some benchmark development is for very limited use (i.e. just one client) and so unlikely to reach the public domain, this total could underestimate the true number of administrators. On the other hand, this bespoke development is largely understood by us to be undertaken by the larger investment banks — most of whom were picked up by our analysis, i.e. we do not expect this source of under-estimation to be very significant.

There are about twenty non-EU administrators (or at least lacking an established presence in the EU) within this total, particularly from the USA, but also from elsewhere (e.g. Japan, Korea, Hong Kong etc.)
The number of non-EU administrators is likely under-estimated since some index or reference rate is likely linked to at least some products in the EU.

The desk-top research identified over 80,000 benchmarks. Our fieldwork indicated that this is an underestimate. The underestimation comes from two main sources.

- First, certain large benchmark administrators did not disclose a complete picture of their activities on their websites, and it was not fully accessible through our other desk-top research strands. On the other hand, such administrators are limited in number — as such we believe that what we have learnt through the fieldwork is possibly in itself a reasonable estimate of the additional benchmarks. Overall, we believe that this identifies a further 35–50,000 benchmarks.

- Second, bespoke ‘benchmarks’ developed for specific client purposes are understandably underrepresented. Our information on these is piecemeal, but suggests that a large bank could have 1–3,000 such additional benchmarks in play. (Market participants consider these to be within scope of the BMR). If we say that there are 10–15 such banks (including the two-three disclosing this information to us), then this indicates a further 12–43,000 benchmarks.

Overall then, accounting for just these factors, this indicates at least 127–173,000 benchmarks currently being deployed in the EU. Given the absence of better data, it is not implausible to consider the upper limit to be still be an underestimate. On the other hand, participants did find it difficult to reconcile precisely what they did with the definitions within the BMR — because this exercise remained a work-in-progress at their firms — and it could be that this creates a material upward bias in this number.

The vast majority of these are using regulated data. Others are designed for ‘single’ client use.\(^1\) The number of interest rate and commodity benchmarks look to both number below 100.

3.3 Agreements between administrators and contributors

We also investigated through our stakeholder engagement (the scope of which is described at the Appendix at Section 5) how administrators acquired data from contributors, specifically:

- whether any agreements were in place with contributors;
- the nature of any agreements in place with contributors, e.g. which might protect the contributed data from being published or used for purposes other than calculating benchmark; and
- whether any such licensing agreements involve payments to contributors.

Many administrators use only transactional data — as such they do not have contributors per se but either use their own data (e.g. in the case of a trading venue) or else acquire the market data from 3rd party data providers. Other administrators (e.g. in interest rate and commodity benchmarks) offered a mixed picture, with such contributor agreements only identified as being in place for certain commodity benchmarks. Payment was even less of a market feature, but was viewed as being increasingly part of the dialogue with contributors. Again, this evidence was limited to administration of commodity benchmarks.

The contributors that we engaged with tended not to have formal agreements in place with the administrators with which they had relationships (and also confirmed that they did not receive any payment in recompense for their contributions).

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\(^1\) ESMA is to provide technical advice to the European Commission on what is meant by “published or made available to the public” in the context of defining an index. This will determine the applicability of the BMR to such single-use benchmarks.
4 Qualitative and Quantitative Cost-Benefit Analysis

The first step in assessing the impacts of ESMA’s draft Technical Standards relating to the BMR is to map out the economic logic connecting the Technical Standards to different costs and benefits, and other market impacts. We call such a map the “mechanisms of effect”.

At a high level, the draft Technical Standards we assess relate to:

- oversight function;
- input data;
- transparency of methodology;
- code of conduct;
- governance and control requirements for supervised contributors;
- criteria for significant benchmarks;
- compliance statement;
- benchmark statement;
- authorisation and registration of an administrator; and
- recognition of an administrator located in a third country.

For each of these categories of Technical Standards, ESMA has defined the aspects of the Technical Standards that we investigate. We discuss each Technical Standard category below. In developing the qualitative cost-benefit analysis, we have drawn upon responses to the EC’s consultation on the BMR as well as responses to ESMA’s discussion paper on the draft Technical Standards.

4.1 Oversight function requirements

4.1.1 What does the Benchmarks Regulation say?

Article 5 requires benchmark administrators to establish an oversight function to provide oversight of all aspects of its benchmarks provision. The oversight function is to be carried out by a separate committee or by means of another appropriate governance arrangement.

Administrators of all benchmarks (whether critical, significant or non-significant) are required to establish an oversight function, but only critical and/or significant benchmark administrators must comply with ESMA’s RTS.

Article 5 of the Benchmarks Regulation specifies the following.

ESMA shall develop draft Regulatory Technical Standards to specify the procedures regarding the oversight function and the characteristics of the oversight function including its composition as well as its positioning within the organisational structure of the administrator, so as to ensure the integrity of the function and the absence of conflicts of interest. In particular, ESMA shall develop a non-exhaustive list of appropriate governance arrangements as laid down in paragraph 4.
ESMA shall distinguish between the different types of benchmarks and sectors as set out in this Regulation and shall take into consideration the differences in the ownership and control structure of administrators, the nature, scale and complexity of the provision of the benchmark, and the risk and impact of the benchmark, also in light of international convergence of supervisory practice in relation to governance requirements of benchmarks. However, the ESMA draft Regulatory Technical Standards shall not cover or apply to administrators of non-significant benchmarks.

The key components of this, as detailed in the first sub-paragraph, are that ESMA’s RTS shall specify:

- procedures regarding, and characteristics of, the oversight function;
- the positioning of the oversight function within the administrator’s organisational structure; and
- a non-exhaustive list of appropriate governance arrangements.

In doing so, ESMA’s RTS should distinguish between different types of benchmarks (e.g. nature, scale, complexity, risk and impact), sectors and administrator ownership and control structures. Therefore, it is up to ESMA to apply a proportional approach in determining (through its RTS) whether different oversight functions are required for the different types and sectors of benchmarks, as well as different administrator ownership and control structures, given their different underlying characteristics.

4.1.2 What do the ESMA draft Technical Standards say?

There are four components of ESMA’s RTS:

- composition of the oversight function;
- positioning within the organisational structure of the administrator;
- procedures governing the oversight function; and
- conflicts of interest management procedures.

We discuss each in turn.

Composition of the oversight function.

ESMA specifies the following with regard to the composition of the oversight function.

- That the structure and composition of the ownership function should be appropriate to the ownership and control of the administrator and the nature of the benchmark. Non-exhaustive examples are provided of possible governance arrangements in Annex I to the RTS.
- The oversight function should be composed of members with appropriate knowledge and skills. There are specific requirements dependent on the nature of the benchmark. Representatives of parties (such as trading venues) contributing to regulated-data benchmarks could be considered for appointment to the oversight function. Where contributors are appointed to the oversight function, administrators should consider the scope for conflicts (particularly vested interests in moving the level of the benchmark), and members with scope for a conflict of interest should not be in the majority. At least two independent members would be required for a critical benchmark.
- Observers are permitted to join the oversight function.
- Where staff of the administrator who are directly involved in the provision of the benchmarks are members of the oversight function, the administrator shall ensure that they do not adversely affect its integrity. Representatives of the management body may be invited to attend meetings by the oversight function but shall not be permanent members of the oversight function. Participation by individuals employed by the administrator in the oversight function is subject to further restrictions for critical benchmarks and regulated-data benchmarks of equivalent economic importance.
- Individuals convicted of financial services-related offences are precluded from membership.
Positioning within the organisational structure of the administrator

ESMA specifies that the positioning of the oversight function should allow it to provide effective scrutiny of benchmark provision. Specifically, the oversight function should be embedded within the administrator’s organisational structure, with separation from the management body and other governance functions of the benchmark administrator.

The oversight function is to act independently of the administrator and shall assess and challenge the decisions of the administrator’s management body. It is required to report all other recommendations on benchmark oversight to the management body and record any instances where the management body acted, or intends to act, contrary to recommendations resulting from a decision of the oversight function.

Procedures governing the oversight function

Administrators of benchmarks that require an oversight function are asked to establish a set of procedures to ensure the proper functioning of this oversight function.

ESMA specifies the following procedures:

- the terms of reference for the oversight function;
- the criteria for selecting oversight function members based on their expertise;
- the disclosure to users and potential users, to the relevant competent authority and, where relevant, to contributors, of procedures regarding the management of conflicts of interest;
- the processes for election, nomination or removal and replacement of committee members;
- the rules for participation of staff on the oversight function who are directly involved in the provision of benchmarks to be overseen;
- the criteria for determining which responsibilities are delegated;
- the criteria for selecting the person or committee within the oversight function to act as the contact point for the competent authority and the management body of the administrator;
- the mechanism for managing disputes arising in the oversight function;
- the processes governing the measures that are to be carried out in the case of code of conduct breaches;
- the procedures to notify the competent authority of expected contributor or administrator misconduct, as well as any suspicious or anomalous input data;
- the frequency of, and approach to, interaction with other administrator functions, especially the management body; and
- the arrangements to prevent improper disclosure of confidential or sensitive information received, produced or discussed by the oversight function.

Conflicts of interest management procedures

ESMA has also developed a specific list of procedures that oversight functions must introduce in order to manage the conflicts of interest that may arise due to the competing interest of different types of members. These procedures are:

- requiring members to disclose conflicts ahead of each agenda item;
- prohibiting staff directly involved in benchmark provisions from voting on oversight function decisions;
- prohibiting members voting on decisions that would directly impact the business they represent;
- excluding members from specific discussions that would cause them to become conflicted; and
- restricting membership of the oversight function to persons not already sat on another administrator’s oversight function.

Only the first bullet point would apply where the oversight function is a natural person. This natural person shall not be directly involved in the provision of the benchmark, and where the natural person represents another organisation it shall not make decisions that will have a direct business impact on that organisation.
Where it is not possible to manage conflicts of interest in this way, the RTS require administrators to alter the oversight function’s structure and, if necessary, replace conflicting members.

4.1.3 Expected impacts

Figure 4.1: Expected impacts of the RTS on characteristics and procedures of the Oversight Function

<table>
<thead>
<tr>
<th>Goals</th>
<th>Topics</th>
<th>Affected stakeholders</th>
<th>Costs</th>
<th>Benefits</th>
</tr>
</thead>
<tbody>
<tr>
<td>Provide oversight of all aspects of benchmark provision</td>
<td>Composition of the oversight function</td>
<td>Administrators of critical and/or significant benchmarks</td>
<td>One-off: Initial set-up costs of establishing oversight committees or adapting existing committees, including identifying and recruiting members.</td>
<td>Sufficient flexibility in the RTS for administrators to adapt to their own specific requirements. Maintaining expertise of oversight committees, while reducing likelihood of conflicts of interest.</td>
</tr>
<tr>
<td>Improve the reliability, integrity and quality of benchmarks</td>
<td>Positioning of the oversight function</td>
<td></td>
<td>Ongoing: Costs of staff time in operating oversight functions (including secretariat support), maintaining relevant procedures and reporting recommendations on benchmark oversight to the management body.</td>
<td>Direct compliance costs to administrators passed onto benchmark users as higher fees, which may cause benchmark users to switch to using cheaper, less well-formulated benchmarks to reduce costs.</td>
</tr>
<tr>
<td></td>
<td>Procedures governing the oversight function</td>
<td>Benchmark users (non-contributing)</td>
<td>Restrictions on composition may require administrators to hire more staff and/or pay staff more favourably to compensate their expertise, resource commitments and liability exposure.</td>
<td>Improved regulatory oversight and confidence amongst benchmark users, including more balanced representation and less opportunity for conflicts of interest to arise; and improved transparency and accountability.</td>
</tr>
<tr>
<td></td>
<td></td>
<td>Competent authorities</td>
<td>Increased presence of external parties could increase conflicts of interest. There is also a risk of lack of harmonisation with the IOSCO principles.</td>
<td>Costs of understanding the new regulation and what administrators are required to report to them. Small ongoing costs of keeping items that administrators are required to report to them up-to-date.</td>
</tr>
</tbody>
</table>

Source: Europe Economics.

**Costs**

Direct costs will accrue almost exclusively to administrators, although there should also be some costs to national competent authorities in understanding the new regulation and what administrators are required to report to them, e.g. their procedures regarding the management of conflicts of interest. Competent authorities are also likely to face (small) ongoing costs associated with keeping the relevant items that administrators are required to report to them up-to-date.

Most costs will be borne by administrators. In terms of the direct costs of ESMA’s RTS on the oversight function, there are likely to be initial set-up costs of establishing oversight committees where relevant, or adapting existing committees to be compliant with the legislation. This would include the costs of identifying and recruiting appropriate members, which meet relevant criteria, e.g. expertise, independence and so on. It would also include the costs of putting in place the procedures required by the RTS, such as the oversight functions terms of reference and developing the list of criteria for member selection. This encompasses both the costs of staff time involved in developing and implementing these various
Qualitative and Quantitative Cost-Benefit Analysis

procedures, as well as the costs of staff time in documenting these new procedures and making relevant persons aware of them.

As well as these initial set-up costs, there would also be the ongoing costs of operating these oversight functions, including the costs of ensuring that all procedures required of the oversight function continue to be met on an ongoing basis and are updated as, and when, appropriate. The oversight function is also required, as part of the RTS on positioning, to report all other recommendations on benchmark oversight to the management body and record any instances when the management body acted (or is expected to act) contrary to the recommendations of the oversight committee. This would impose ongoing costs of staff time involved in recording and reporting.

Given the restrictions on composition, in part imposed by the BMR, but further specified by ESMA’s RTS, administrators may need to hire more staff members (and also pay staff members more favourably), in order to compensate their expertise, resource commitments and their liability exposure. The administrators would also face costs of providing secretarial services to these committees, which would largely be the cost of staff time in arranging meetings (location, attendees, agenda etc.) for the oversight committee.

The scale of the direct costs would depend, in part, on the number of oversight committees the administrator is required to adopt and their structure. If administrators are able to set up oversight committees to cover an entire family of benchmarks, rather than each individual benchmark, then there are likely to be significant opportunities for cost savings. By a similar logic, administrators of a large number of benchmarks are likely to bear much lower incremental costs per benchmark than administrators with a small number of benchmarks. The ability, in some cases, to have a natural person as the oversight function, instead of an entire committee could also mitigate some of the effects of such cost scaling. However, an oversight function composed of a single natural person is not viable for administrators of critical benchmarks or regulated data benchmarks with a reference value in excess of €500 billion and, therefore, these administrators may incur relatively higher costs.

Our fieldwork indicated that the need to purely establish an oversight function would not require any changes to be made to their existing practices, with a small number of respondents suggesting some minor changes and only one respondent specifying that it would require major changes, i.e. the majority of administrators already have such oversight functions in place. Likewise, the majority of respondents also said that no changes would have to be made to the way in which they manage conflicts of interest of the oversight function.

However, with regard to ensuring the independence of the oversight function, the majority believe that at least minor changes would be required. There was a concern about accessing sufficiently expert individuals to make such boards properly independent (i.e. too many administrators might be chasing a select group of people). Evidence on whether any changes to the positioning of the oversight function was more mixed, with roughly half specifying no changes and the other half specifying minor changes. Overall, therefore, the costs appear relatively light touch for administrators, with the need to making the oversight function independent the largest break from existing practices, but still only requiring minor changes in order to be compliant.

Of course, the extent to which the above costs are incrementally realised for individual administrators, would depend on to which administrators are already compliant with the requirements of the RTS. The specificity of the RTS (e.g. setting the correct organisational positioning and procedures in place) may limit this. When asked what the key driver of their existing relevant procedures and practices is, the most common response was the IOSCO principles followed by existing regulatory requirements.

Administrators participating in our stakeholder engagement had oversight committees but believed that some additional change would be required in order to make these fully independent in the sense of the
Technical Standards. In part, this reflects concerns around potential scarcity of suitable individuals with the expertise to contribute — and yet had some distance from the process. This obligation would be applicable only to a subset of administrators (i.e. those with some significant or critical benchmarks, perhaps 15–20 in total). Reorganising these committees (by recruiting new individuals) could incur one-off and ongoing costs. If we accept the point that relevant people could be somewhat scarce, this implies some uplift in cost (even if there is a straight-forward substitution of people). We estimate both one-off and ongoing incremental costs incurred by administrators to be €0.4–0.8 million.

Overall, it is important to consider direct costs, not just from an administrator standpoint, but also because these direct costs could ultimately be passed onto benchmark users. This is discussed in more detail as part of the indirect costs later.

**Indirect costs** are the costs that arise not as a result of direct compliance with the regulation, but rather can be considered as secondary, undesirable effects which may arise due to, for example, changes in firm behaviour, or interactions with existing market or regulatory structures. We consider below the potential indirect costs of these RTS.

There are potential indirect costs that may arise as a result of perceived restrictions on the composition of the oversight committees. ESMA provides a non-exhaustive list of governance arrangements. In many cases, this should help mitigate costs, at least where a participant’s procedures are closely-aligned to the list. On the other hand, some stakeholders may be uncertain as to what other arrangements (i.e. those not on the non-exhaustive list) would be considered appropriate and may decide to adapt existing arrangements to avoid the risk of non-compliance. Restrictions on composition may be of particular concern in the case of more complex benchmarks, as such benchmarks may demand more expertise and knowledge, which the composition requirements may restrict.

A more significant concern may be that the increased presence of external parties, in order to meet the composition requirements, could in fact, contrary to the intentions of the regulation, increase conflicts of interest and jeopardise independence. Users, for example, may have the incentive to promote their own interests rather than the interests of the wider market because, as issuers of financial products based on the benchmarks, they can stand to gain from particular changes to those benchmarks. This may be of particular concern for widely used benchmarks, where the potential rewards are greater. To clarify, the Benchmarks Regulation itself does not stipulate that external parties must be present, but the ESMA RTS does by requiring, in some cases, an ‘independent’ committee, which they define as “a committee that includes natural persons who are not otherwise directly affiliated with the administrator”.

Another important issue to consider in the context of indirect costs is the potential for ‘undue’ regulatory burden due to: proportionality issues; and issues of regulatory overlaps or inconsistencies. We consider each in turn.

In terms of regulatory overlap, it is necessary to consider the standards set out by the IOSCO Principles for Financial Benchmarks. The more closely aligned ESMA’s RTS are with the IOSCO Principles, the less cost intensive ESMA’s RTS are likely to be. This is because administrators would already have the precedent of complying with the IOSCO Principles and may therefore be able to benefit from some cost efficiencies in complying with ESMA’s RTS. However, the IOSCO Principles say that benchmarks should be grouped on the basis of what they have in common rather than whether they are critical, significant etc., which is to some degree inconsistent with the Benchmarks Regulation and ESMA’s RTS, as only administrators of significant or critical benchmarks need to comply with ESMA’s RTS. Inconsistent standards could mean that administrators align their practices with the internationally agreed IOSCO Principles outside the EU, but the Benchmarks Regulation and ESMA’s RTS within the EU. This may introduce inefficiencies and could mean that ESMA’s RTS are less effective than they would be if they complied with the IOSCO Principles that guide good practice more internationally.
Next, we consider the potential implications of having oversight committees which oversee multiple benchmarks, i.e. a family of benchmarks. There is likely some trade-off between efficacy and cost here. This should be to a large extent beneficial in promoting efficient and effective benchmark oversight, and we will come on to discuss such benefits shortly. However, it should be recognised that oversight committees for families of benchmarks could be counter-productive if drawn too widely. Oversight committees require the necessary knowledge and expertise to cover specific benchmarks, and hence the wider the coverage of a given oversight committee, the less focussed the knowledge and expertise will become. Administrators may, however, have the incentive to adopt broader oversight committees in order to cut compliance costs, especially those administrators with a significant number of benchmarks, as they could stand to gain the most. Given the definition of ‘family of benchmarks’ provided in Article 3(1)(4) of the Benchmarks Regulation would have “input data of the same nature” and relate to “the same or similar market or economic reality” this concern looks to be marginal, if not negligible. A more significant concern is that, for an oversight committee encompassing multiple benchmarks, if conflicts of interest are realised, then it would affect a larger population of benchmarks and thus, potentially, a larger population of benchmark users. As well as the impacts on administrators, there may also be detrimental impacts on benchmark users. If the compliance costs incurred by administrators are largely passed through to users as higher fees, users may look at alternate measures. If costs are greater for smaller administrators, then this could drive sector consolidation (e.g. some market participants have already exited benchmark administration, at least partially, or are considering doing so). This would result in fewer administrators or fewer benchmarks or both. This could result in efficiency gains, on the one hand, but could also act, as a knock-on effect, to increase the number of significant and critical benchmarks (by concentrating activity around these). A, perhaps, more concerning knock-on effect of this could be a move away from more well-formulated benchmark products to less well-formulated versions in order for benchmark users to reduce costs. **Benefits** On the benefits side, it is more difficult to disentangle the benefits of ESMA’s RTS from the benefits of the underlying Benchmarks Regulation. In many cases, ESMA’s RTS are reinforcing the intended benefits of the Benchmarks Regulation, by providing practical guidance on how to implement Article 5 of the BMR (e.g. by providing a non-exhaustive list of possible oversight function structures). However, where possible, we will draw out specific benefits of ESMA’s RTS in the discussion that follows. The overarching benefit of ESMA’s RTS and the Benchmarks Regulation is in improving the reliability, integrity and quality of benchmarks. It can be noted at this point that improved benchmark reliability and integrity was ranked as the single most important benefit across all Technical Standards. This will be to the benefit ultimately of the investors and consumers who use these benchmarks. ESMA’s RTS reinforce this by setting out composition requirements which ensure oversight committees have more balanced representation across different stakeholder groups. This, in turn, helps to ensure that the interests of any one party are not promoted at the expense of the interests of the wider industry and wider public. It reduces the likelihood of conflicts of interest arising and should ensure that no particular stakeholder group has undue veto power on the committee’s decision making. In addition, the need under ESMA’s RTS to develop various procedures, such as the terms of reference and member selection criteria, should promote further transparency and accountability of the oversight function, which in turn should reinforce benchmark integrity. The RTS regarding positioning should mean that the oversight function is able to provide close up scrutiny of the administrator, while remaining independent. While providing additional guidance on the composition of the oversight function, the RTS retain sufficient flexibility for administrators to adapt to their own specific requirements. This is important given the varying nature of benchmarks provided by different administrators (in terms of size, underlying products, means of contribution, and so on). ESMA’s concept is that providing a non-exhaustive list of potential compositions,
this should be sufficient to (a) provide useful guidance to administrators, and (b) facilitate a greater degree
of alignment than would otherwise hold in terms of the administrator’s interpretation of the BMR’s Article
5. This should promote benefits to integrity and reduce the costs to national competent authorities who
the oversight functions must report to. This approach is mirrored in the RTS regarding procedures
required by the oversight function, as ESMA’s RTS only set out minimum requirements, which
administrators can build on where relevant.

In the case of contributor membership, the composition requirements provide a practical solution that
recognises the benefits that contributors bring to the oversight function, while also limiting the extent of
their membership in recognition of the potential detriments they can create. The presence of contributors
should be beneficial, as they have extensive knowledge of the market and technical expertise, which is
crucial when, for example, considering methodological changes to benchmark calculation, so as to ensure
any changes are consistent with market reality and operationally viable for relevant stakeholders. However,
contributors may face conflicts of interest and may be best placed to exploit these where:

- the contributors are also the users of the benchmarks;
- the contributors dominate the oversight committee; and/or
- the contributors are the sole providers of specialist knowledge.

ESMA’s RTS on benchmark composition help to prevent the second scenario (i.e. contributors dominate
the oversight committee) and thus ensure that contributors are not in a position to exploit these potential
conflicts of interest, while at the same time ensuring that the benefits contributors provide to oversight
functions are still realised. It is unclear how ESMA’s RTS on benchmark composition treat the first scenario
(i.e. where contributors are also users of the same benchmarks) and this would therefore require further
clarity to understand the potential costs and benefits. However, there is nothing in the Benchmarks
Regulation or ESMA’s RTS which specifically addresses the third scenario (i.e. where the contributors are
the sole providers of specialist knowledge).

ESMA’s RTS on composition also allow for the presence of persons involved in the provision of relevant
benchmarks on oversight committees, but only in a non-voting capacity. Again, this should help to improve
the expertise of the oversight committee, while not jeopardising its integrity by introducing potential
conflicts of interest.

Another key benefit of ESMA’s RTS is that they allow for the establishment of an overarching oversight
function across multiple benchmarks, with sub-functions reporting to it. This is key to ensuring
proportionality, as it would not be practicable for an administrator with, say, 100,000 benchmarks to set-up
an oversight committee for each one. By allowing for a single overarching oversight function, administrators
should be able to avoid unnecessary duplication of costs, as many identical, or at least very similar, tasks
that would otherwise have needed to be carried out by each separate oversight function can all be carried
out by one central oversight function. It should also save on secretarial costs for the administrator. As well
as these improvements in efficiency (cost savings), an overarching oversight function could also improve the
effectiveness of oversight: firstly, as it would be better placed to leverage on the technical input and market
expertise of members from different sub-functions; secondly, because it would have a complete, high-level
overview of the market to allow for greater consistency of judgement and consistency in monitoring and
supervision; and, thirdly, because it would help establish clearer accountability, especially within firms
operating a large number of benchmarks.

A further benefit of a single, overarching function is that it may create cost incentives to apply higher
standards of oversight across all benchmarks, rather than to just the more complex benchmarks. It may
also limit the number of additional personnel that an administrator needs to hire, which may be particularly
important in smaller EU countries where there may only be a limited number of persons with the correct
experience to serve on a benchmark oversight function.
This regulatory approach allows administrators to establish sub-functions along the lines of benchmarks’ characteristics (input data, methodology, market etc.), which is generally considered a more effective way of grouping benchmark oversight functions than by benchmark criticality. A potential knock-on effect of this arrangement is that non-significant benchmarks may be grouped with significant and/or critical benchmarks with similar underlying characteristics. Therefore, although non-significant benchmarks are outside the scope of the regulation, they may nevertheless benefit from increased scrutiny by virtue of being under the remit of an oversight function that is also responsible for several significant and/or critical benchmarks.

The positioning of the oversight function as being embedded within the organisation of the administrator should also help to facilitate effective challenge of the administrator. Furthermore, the oversight function’s ability to act independently of the administrator should help ensure that the oversight function is able to report relevant cases of misconduct to their competent authority, especially misconduct of the administrator itself. Indeed, survey respondents indicated that the oversight function requirements would have some incremental benefit to regulatory oversight, with the analysis of responses finding this to be the third most important set of Technical Standards in this regard (behind governance and control requirements for supervised contributors and recognition of third country administrators). However, allowing members of the management body to attend oversight function meetings (while maintaining separation of the two), should allow the oversight function to leverage the expertise of members of the management body while not losing the necessary independence.

4.2 Input data

4.2.1 What does the Benchmarks Regulation say?

The Directive requires input data, first, to represent accurately and reliably the market or economic reality that any given benchmark are intended to measure, and, second, to be verifiable by the administrator. The administrator is also required to publish clear guidelines regarding the types of data used, the priority of use of the different data types, and the way expert judgement is applied. Where possible and appropriate transaction data should be used. Where data from contributors is used, the administrator should ensure the data are reliable and representative of the market or economic reality the benchmark is intended to measure by obtaining the data from a reliable and representative panel/sample of contributors (where appropriate). The contributed data should not be used if the administrator has any indication that the contributor does not comply with the code of conduct — in which case, publicly available data should be used instead.

Administrators should have appropriate controls in respect of input data including:

- criteria that determine who may contribute data and how to select contributors;
- a process for evaluating contributor’s data and preventing the contributor from providing further data, where appropriate; and
- a process for validating input data, including against other indicators or data, to ensure its integrity and accuracy.

Where the data is contributed from a front office function the administrator should corroborate that data by comparing it with other data sources, and ensure that contributors have adequate internal oversight and verification procedures.

Where the administrator considers the data are not representative of the relevant market or economic reality, that administrator should (in a reasonable time frame) change the data, the contributors or the methodology, or stop providing the benchmark.
In this context, ESMA is tasked with developing draft RTS to specify how to ensure that the data is appropriate and verifiable, as well as the internal oversight and verification procedures of contributors. The draft RTS shall not cover administrators of non-significant benchmarks. ESMA shall take into account the different types of benchmarks and sectors, the nature of input data, the characteristics of the underlying market or economic reality, and the principle of proportionality, the vulnerability of the benchmark to manipulation and the international convergence of supervisory practice in relation to benchmarks.

4.2.2 What do the ESMA draft Technical Standards say?

Appropriateness and verifiability of input data

Administrators shall specify requirements to ensure that in view of methodology the input data obtained is appropriate and represents the market or economic reality that the benchmark is intended to measure. The requirements shall cover at least:

- Relevant threshold for quantity and quality of input data.
- Hierarchy of input data types.
- Justification required for use of other than the primary types of input data.
- Justification required for the exercise of any discretion or expert judgement in the contribution of input data.

Appropriateness shall be monitored on an ongoing bases through evaluation and validation.

Data is verifiable when it can be checked to be accurate or to stem from a reliable source. To demonstrate verifiability administrators shall ensure that all information necessary to conduct evaluation and validation checks is available.

Evaluation consists of at least the following formal checks on each individual input data contribution:

- whether the input data is contributed by an authorised submitter;
- whether input data is provided on time;
- whether input data is provided in the format specified; and
- whether input data fulfils the quantitative threshold set in the methodology, in any.

Validation, conducted after publication of the benchmark, makes use of the following techniques, where applicable:

- comparison within contributions from different contributors;
- comparison against previous contributions;
- comparison against related market indicators;
- comparison against historic series of data from underlying or related market/economic realities;
- for non-transaction data: back testing to corroborate input data when transaction data become available;
- checking coherence of the contribution with relevant contribution metadata recorded by the contributor, which may include:
  - policies and procedures governing the contributions and relevant changes therein;
  - substantial exposures of individual traders or trading desks to benchmark-related instruments as well as changes therein;
  - a record of disciplinary actions taken against any contributor’s staff in respect of benchmark-related activities;
  - a list of submitters and approvers (if applicable), including their names and general roles, with the dates when submission-related roles where authorised and exited;
  - with reference to each specific contribution to be validated:
data and time of the contribution;
- data inputs considered, data excluded and any other exercise of discretion;
- communication between the contributors and the administrator;
- relevant communication between the submitter and approvers within the contributor (if applicable);
- records of input data queries and their respective outcomes;
- recording of telephone conversations;
- electronic communications;
- data traffic records; and
- whistleblowing disclosures.

Administrators of regulated data benchmark would not be required to carry out validation.

Internal oversight and verification procedures in case of front office contributions

Upon receiving the input data submission, the administrator shall require information allowing the verification that the submitter has been permitted to submit input data on behalf of the contributor. Where input data is contributed from a front office function, the administrator shall ensure that the contributor has the following oversight and verification procedures in place.

- Contributors’ internal oversight is structured along three lines of defence and operates in accordance with written procedure describing the respective roles of these three lines of defence as well as the method of cooperation and flow of information between these functions, and operations of internal oversight functions are subject to regular reporting to senior management and that all internal oversight and verification procedures are communication to them upon request.
- The first line of defence comprises front office staff which are aware of the procedure for input data contribution as well as of clear behavioural expectations.
  - Elaborating training programmes tailored to the specific responsibilities of from office staff concerning at least:
    - the code of conduct;
    - the applicable laws and regulations;
    - the contributor's internal control framework;
    - the contributor's internal conflicts of interest procedure;
    - ethical standards;
    - the whistleblowing procedure; and
    - disciplinary actions.

The trainings should be conducted periodically or as necessary if there are material changes to the policies, procedures or in response to specific events.

- Performing effective checking processes of input data contributions such as a four-eyes process. Administrators shall ensure that contributions are prepared by an authorised submitter and reviewed for reasonableness, accuracy and completeness prior to contribution. Administrators of significant benchmarks may decide not to require contributors to implement a four-eyes process, if they demonstrate that alternative safeguards are in place.
- Excluding the access of contributions to persons not involved in the submission process, except under circumstances such as audit or investigations for suspicious inputs or errors.
- Setting up contingency measures or fall-back arrangements to ensure the provision of input data in the event of a disruption to the process of the provision of input data such as market stress.
The second line of defence comprises at least risk and compliance functions:

- performing a second level and independent control in relation to the reasonableness, accuracy and completeness of the contributions;
- maintaining a whistleblowing procedure to assist internal oversight functions in detecting activities affecting the integrity of the benchmark;
- maintaining procedures to notify the administrator immediately when they become aware of any attempted or actual manipulation or failure to comply with benchmark-related policies and procedures;
- maintaining a physical presence in the front office where applicable;
- monitoring communications within the front office and between the front office and other internal functions;
- monitoring communications between the front office and external bodies;
- performing regular checks for suspicious communication;
- establishing and maintaining a conflicts of interest policy that is appropriate to the context of front office contributions, covering:
  - disclosure to the administrator of actual or potential conflicts of interest of the contributor and of the contributor’s front office staff members who are involved in the contribution;
  - identification and reporting of conflicts of interest;
  - avoiding the existence of any direct link between the remuneration of staff involved in input data contribution and the remuneration of or revenue generated by other contributor staff principally engaged in another activity, where a conflict of interest may arise in relation to those activities;
  - clear segmentation of duties between front office staff involved in contributing input data and other front office staff; administrators of significant benchmarks may choose not to require contributors to implement this measure when not appropriate (based on the nature, scale and complexity of contributor’s activities and whether the contribution activity is part of the core business or an ancillary activity), if the contributor demonstrates sound principles and procedures to manage conflicts of interest;
  - physical separation between front office staff involved in contributing input data and other front office staff; as above — administrators of significant benchmarks may choose not to require contributors to implement this measure when not appropriate (based on the nature, scale and complexity of contributor’s activities and whether the contribution activity is part of the core business or an ancillary activity), if the contributor demonstrates sound principles and procedures to manage conflicts of interest;
  - effective procedures to prevent or control the exchange of information between front office staff and other contributor’s staff, where the exchange of that information may affect the input data contributed;
  - measures to prevent any person from exercising inappropriate influence over the way in which front office staff involved in contributing input data carry out activities; and
  - contingency provisions in case of temporary inefficiency of the controls of the flow of information.

The third line of defence comprises at least the internal audit function performing independent checks on a regular basis on the control exercised by the two lines of defence which may include, depending on the type of data contributed, techniques such as:

- comparison against previous contributions;
- comparison against related market indicators, where available;
- for non-transaction data: back testing to corroborate input data when transaction data become available.
For supervised contributors, administrators of significant benchmarks may allow that the required internal oversight procedure be aligned to pre-existing internal oversight structures rather than the three lines of defence.

Administrators of significant benchmarks may allow a simplified internal oversight architecture for smaller contributors whose organisation does not allow the establishment of three separate lines of defence.

4.2.3 Expected impacts

Figure 4.2: Expected impacts of the RTS on Input Data

### Costs

**Appropriateness and verifiability (evaluation and validation)**

Administrators would incur one-off set up costs and ongoing costs of transmission and storage of data. However, it should be kept in mind that the data requirements for the administrators of critical benchmarks and those administrators of significant benchmarks who comply with Article 8 BMR, do not go beyond requirements in the BMR. These costs might be passed on users. Alternatively administrators might have less of incentive to innovate. The costs are likely to be less significant for administrators of regulated data benchmarks (as they may choose not to apply the validation procedures).
If the requirements are too onerous — either in terms of data requirements or rules around front office contributions (which will be further analysed in the next section) — contributors could be discouraged to provide data to administrators. This would lead to a deterioration of benchmarks quality and representativeness. This would be less likely to happen in the case of supervised/small contributors which may be allowed by administrators of significant benchmarks to maintain the existing internal/simplified oversight structures. Similarly, if the fixed costs of contributing to an index increase (e.g. because the data transfers are more demanding than before which requires more sophisticated IT systems or better internal procedures) then a barrier to entry for new benchmark providers may be created. This could have an impact on competition in the market, and subsequently on the price and/or quality of benchmarks available to users.

Some data relevant for benchmarks and owned by contributors are confidential and sensitive. Sharing these with administrators might have “competitive implications if the administrator sits within a wider financial services firm”. However, given some flexibility in what kind of data are to be required by administrators to assess the appropriateness and verifiability of input data might mitigate this problem.

To the extent that procedures regulating the use of judgment in calculating the benchmark are too burdensome, administrators might be discouraged from providing the benchmarks where judgement is crucial. However, if — due to overly relying on own judgement — these benchmarks were not accurate and reliable, then eliminating them from the market might be actually beneficial for users who previously perceived these benchmarks as a good representation of the underlying market conditions. As currently formulated, the regulation related to the use of judgement in the draft RTS do not seem to be imposing requirements significantly beyond the BMR.

Being too prescriptive about the data scrutiny process (e.g. the frequency of data transfers, the timing of data validation or the kind of checks that should be done to ensure appropriateness) could prevent administrators from implementing more efficient measures to control the quality of input data. In cases, where it would be efficient to reduce the frequency of data transfers or skip the appropriateness checks which are irrelevant for a particular benchmark, imposing strict regulation would create cost for administrators which would not be justified by the associated benefit. As currently formulated, the proposed data evaluation and validation checks do not prescribe a specific timeframe or frequency of the data scrutiny process (except for stressing that verifiability of input data should be ensured on an ongoing basis). While they do provide a list of checks each individual input data should pass, the particular validation checks should be used only where applicable. Moreover, the concern regarding the irrelevance of the requirements for some benchmarks is partly mitigated in the RTS by allowing administrators of regulated data benchmarks to opt out of validation procedures. As such, those administrators would only have to comply with the more basic appropriateness and evaluation checks.

To the extent that RTS requirements do not align with IOSCO requirements, the cost of complying with the RTS requirements might be outweighing the benefits. Administrators that already comply with IOSCO principles have presumably better quality controls than those that do not. Imposing additional data quality controls which are not compatible (in the sense of adding compliance burden rather than being

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2 Confidential response to ESMA consultation question Q19: Do you agree with the list of records to be kept by the administrator for input data verification? If not, please specify which information is superfluous / which additional information is needed and why.

3 BMR Article 11(1)(c): “the administrator shall draw up and publish clear guidelines regarding the types of input data, the priority of use of the different types of input data and the exercise of expert judgement, to ensure compliance with point (a) and the methodology”; RTS Article 1: “Administrators shall specify and monitor requirements to ensure that the input data obtained is appropriate in view of the methodology and that it represents the market or economic reality that the benchmark is intended to measure. The requirements shall cover at least, as applicable to the relevant type of input data and benchmark: […] (d) justification for the exercise of any discretion or expert judgement in the contribution of input data”. [Emphasis — EE]
contradictory) with IOSCO requirements (i.e. administrators would have to spend similar amount of time complying with the RTS requirements as if they did not have IOSCO requirements already implemented) creates little additional benefits while still imposing some cost. On the other hand, it is also possible that firms complying with IOSCO principle will find it easier to comply with the RTS as their systems and processes would only require relatively minor adjustments (if any). The extent to which IOSCO principles actually hinder or facilitate compliance with the RTS requirements would be informed by the stakeholders’ responses to our survey.

Administrators might not have access to all the data required by the regulation. For example, "records of substantial exposures of individual traders or trading desks to benchmark related instruments" is not something administrators always know. Those benchmarks would either struggle to comply with the regulation or comply but the benefits would be limited (i.e. costs might outweigh the benefits). As currently formulated, the draft RTS defines a list of potential validation checks administrator may employ where applicable, without a strict requirement to employ all of them in each case. Therefore, any cases where data is simply not available to administrators are unlikely to be interpreted as lack of compliance.

Our fieldwork indicated that the key driver of current systems and business practices in this area are existing regulatory requirements, with anticipation of the BMR coming into application and response to changing market dynamics playing limited role in this respect. In terms of the type of impacts, survey respondents expected little to no changes with regard to the monitoring and oversight of front office contributions. The views on the impacts on processes around appropriateness and verifiability of data were however more mixed, with 25 per cent of respondents indicating that major changes would be required. Of those respondents who suggested no changes required as a result of these Technical Standards, some attributed this to the fact that the data they are using is mostly regulated/transaction based data and, as such, it is easier to comply with the requirements, or else that their national regulator already paid close attention to breaches in input data procedures and, therefore, did not expect the incremental impacts to be material.

Some respondents had more significant concerns about the wider market impacts of these Technical Standards beyond cost matters. Concern was voiced that the administrator of a benchmark to which one is contributing would be able to view some of their highly sensitive exposure data, in order to verify the input data the administrator is receiving, which would be even more problematic where the administrator is also a direct competitor of that contributor. It was further suggested that this was a significant enough issue to review whether a contributor wishes to continue contributing. If contributors withdraw from the market this could have implications for data costs and innovation moving forward. Even if contributors became comfortable with these issues, sharing of these types of data would require the establishment of new internal data links within the contributing firm.

Another problem was raised regarding the treatment of regulated input data sourced from Third Country Regulated Markets. As equivalence requirements are not expected to be concluded in the near future, a situation could develop whereby EU market participants can only use regulated data benchmarks with a scope internal to the EU. However, as the definition of the regulated data is out of scope of the RTS, this is more closely attributed to the Level 1 Regulation rather than ESMA’s Technical Standards.

**Front office contributions**

Direct costs to contributors related to training, developing internal oversight procedures in line with the three lines of defence and conflicts of interest policies.

Incremental costs related to internal oversight are likely to be low as three lines of defence architecture seems to be already implemented by a significant number of contributors (in particular, those complying with IOSCO Principles for Financial Benchmarks). Moreover, the internal oversight requirements could be
less onerous for some contributors. Specifically, contributors submitting data to significant benchmarks may not be required to implement the four-eyes process (as part of the first line of defence).

Furthermore, supervised contributors submitting data to significant benchmarks may not be required by the administrators to develop internal oversight along the three lines of defence and rely on existing oversight structures instead. Small contributors submitting data to significant benchmarks may only be required to ensure a simplified internal oversight architecture.

Contributors to significant benchmarks may also incur relatively lower costs associated with developing conflicts of interest policies as the administrators are not obliged to require all the elements of the relevant article in the draft RTS (Article 7, paragraph 2). In addition, contributors that are already authorised as investment firms (likely the vast majority) should have comprehensive prior experience with such conflicts policies.

Administrators of significant benchmarks have discretion regarding the segregation of duties and physical separation between front office staff involved in contributing input data and other front office staff. This exemption could avoid inefficiencies that would arise if a stricter formulation was adopted as for some contributors being a submitter/approver is not a full-time job and thus introducing organisational and physical separation would lead to high compliance costs for those contributors.

Overall, estimation of incremental compliance costs for these Technical Standards is particularly challenging. Contributors are largely operating with the necessary processes and procedures in place, in response to past regulatory action and adherence to the IOSCO principles. This implies that the incremental cost impact should be low. Whilst there could be some review of these against the final form of the standard, the number of significant and critical benchmarks is not well-established at present (see Section 3.1.2) and whilst the number is likely not large, the number of affected contributors is similarly not well-established — although it is likely focused upon the largest banks, brokers and commodity houses. This makes quantification a particularly hazardous exercise here. In any event, the application of verifiability of data looks to be more of a concern in wider impact terms more than simply one-off cost, i.e. it could affect the appetite of a contributor to continue as such.

**Benefits**

**Appropriateness and verifiability (evaluation and validation)**

The requirements regarding the appropriateness of data should lead to the creation of a consistent control framework that would increase the quality of critical and significant benchmarks. Specifying requirements regarding the input data, the process of evaluating and validating the data would mean that less discretion is left to administrators. This implies less room for data manipulation, which could encourage users to trust and rely on the benchmark more. For contributors and administrators that might mean additional sales or sales recovery. Market participants view the Technical Standards on Input data to be of significant benefit to market confidence, although they believe the impact in terms of improved regulatory oversight would be more minor.

The fact that the requirements regarding data scrutiny (evaluation and validation) are ongoing would ensure that the quality of the benchmark is consistent throughout its life cycle and not only at the inception. This would increase its credibility and promote trust among users. For contributors and administrators that

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4 NB appropriateness and verifiability of data, as high level concepts, were included in the BMR, Article 11(1)(a)-(b) (“The provision of a benchmark shall be governed by the following requirements in respect of its input data: (a) the input data shall be sufficient to represent accurately and reliably the market or economic reality that the benchmark is intended to measure. The input data shall be transaction data, if available and appropriate. If transaction data is not sufficient or is not appropriate to represent accurately and reliably the market or economic reality that the benchmark is intended to measure, input data which is not transaction data may be used, including estimated prices, quotes and committed quotes, or other values; (b) the input data referred to in point (a) shall be verifiable;”)
might mean additional sales or sales recovery. Furthermore, increased accuracy — resulting from improved quality controls of the data — might lead to more efficient use of the benchmark as there would less uncertainty what the benchmark is capturing.

Clear specification of the requirements regarding the type of checks that should comprise the process of evaluation and validation could increase regulatory clarity to administrators. This could help them avoid future penalties for not complying with the regulation.

The minimum requirements regarding the information necessary to ensure the verifiability of the input data in accordance with the draft RTS (Article 2) are exactly the same as specified in BMR Article 8. This implies that there would be no additional regulatory burden in that respect. If the kind of information specified in Article 8 are insufficient to demonstrate the verifiability of input data administrators are obliged to obtain from contributors any additional information that would allow them to do so (Article 2(4) of the RTS). To the extent that this RTS induced administrators to obtain more information (as per Article 2(4) of the RTS), the benefits associated with Article 8 would widen. For instance, the RTS could help the relevant authorities in their supervisory role. The benefits are likely to be greater for non-regulated data than regulated data as there already exist quality controls regarding the latter.

Internal oversight and verification procedures in case of front office contributions

Oversight controls and conflicts of interest mitigation would reduce the probability of errors (either intentional or resulting from negligence). This would improve quality and accuracy of the input data, and thus could increase its credibility and promote trust among users. For contributors and administrators that might mean additional sales or sales recovery.

Training for front office staff involved in input data contribution (as part of the first line of defence) will ensure that they possess all knowledge of applicable laws and regulations, and implications of illegal behaviour. This would reduce the probability of future penalties for contributors for not complying with the regulation.

4.3 Transparency of methodology

4.3.1 What does the Benchmarks Regulation say?

Administrators should ensure that the way their benchmark is developed, operated and administered, as well as its methodology, is transparent. In particular, administrators should publish or make available:

- The key elements of the methodology for each benchmark or, when applicable, for each family of benchmarks.
- Details of the internal review and approval of the methodology, and the frequency of such reviews.
- The consultation procedures for making any material change in the administrator’s methodology and the rationale for such changes, including a definition of “material change” and the circumstances in which the administrator is to notify users of any such changes.

The consultation procedures should include advance notice allowing the stakeholders to analyse and comment upon the impact of the proposed material change. Any such comments, along with the administrator’s response, should be made accessible after any consultation (except where confidentiality has been requested).

In this context, ESMA has been charged with developing draft RTS to specify the information to be provided by an administrator in compliance with the above requirements, distinguishing for different types of benchmarks and sectors. ESMA is take into account the need to disclose those elements of the methodology that provide for sufficient detail to allow users to understand how a benchmark is provided.
Qualitative and Quantitative Cost-Benefit Analysis

and to assess its representativeness, its relevant to particular users and its appropriateness as a reference for financial instruments and contracts and the principle of proportionality. The ESMA draft RTS shall not cover administrators of non-significant benchmarks.

4.3.2 What do the ESMA draft Technical Standards say?

Key elements of the methodology to be disclosed

The RTS lists the following key elements of the methodology administrators shall disclose as applicable to the relevant benchmarks and input data used:

- definition of the benchmark and of the market or economic reality it intends to represent;
- estimate of the size of the underlying market;
- unit of measurement of the benchmark;
- criteria for selecting input data;
- type(s) of input data used and the priority given to different types of input data;
- minimum, required quantity and/or quality of input data;
- minimum liquidity requirements for the constituents of the benchmark;
- rules identifying how and when discretion may be exercised in the determination of the benchmark;
- a description of the constituents of a benchmark and the criteria used for selecting the constituents and for assigning weights to these;
- whether the benchmark’s methodology required periodic changes to remain representative and, in such case:
  - criteria for and/or frequency of changes;
  - the interval and/or triggers for rebalancing the components of the benchmark;
- if the benchmark takes into account the reinvestment of the dividends and coupons paid by the constituents;
- panel composition and eligibility criteria for panel membership;
- limitations of the methodology, including — but not limited to — in illiquid markets;
- the means for tracing and verifying the methodology of calculation of the benchmark including — but not limited to — the use of secured algorithm in order to perform the calculation;
- error management procedures; contingency measures during conditions of market stress or when thresholds for minimum quantity and quality of input data are not met;
- triggers for the application of the measures and procedures related to (1) the means for tracing and verifying the methodology of calculation of the benchmark, and (2) error management procedures; administrators of significant benchmarks may choose not to disclose this;
- clearly defined roles of third parties in data collection, computation or dissemination; administrators of significant benchmarks may choose not to disclose this; and
- method used for the extrapolation and interpolation of data; administrators of significant benchmarks may choose not to disclose this.

Elements of the internal review of methodology to be disclosed

The administrator shall publish the following information regarding the procedure of internal review of methodology:

- a detailed description of the procedure of internal review and approval of the methodology, including
  - the frequency of internal review,
  - the bodies or functions involved in reviewing and approving methodology,
  - the roles performed by the persons involved in reviewing and approving the methodology (administrators of significant benchmarks may choose not to disclose this),
• a general description of the procedure for nomination and removal of the persons involved in reviewing and approving methodology (administrators of significant benchmarks may choose not to disclose this);

• a definition of what constitutes a material change of methodology; and

• a description of the procedure for consulting on any proposed material change in the methodology.

**Procedure for consultation on material changes to the methodology**

Whenever a benchmark administrator judges a change in methodology to be material in nature, an adequate consultation procedure should be followed.\(^5\) When consulting on a material change in the methodology, an administrator shall:

• ensure that stakeholders are at a minimum informed of the key elements of the proposed future methodology;

• inform stakeholders of the reasoning behind qualifying a proposed change as a material change, and — if possible — explain what the expected impact on the benchmark determination will be; and

• publish or make available the rationale behind a proposed material change.

**Publication of comments**

The administrator shall make accessible in full the comments received in consulting on a proposed material changes as well as the administrator's response to those comments (except when respondents requested confidentiality).

Administrators of significant benchmarks may publish their response to the comments in a form of a feedback statement, which shall include:

• the feedback of the administrator on the responses received in relation to the proposed changes;

• the list of the respondents to the consultation (excluding confidential responses); and

• the outcome of the consultation.

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\(^5\) It should be noted that this requirement on a slightly more general level was included in the BMR, Recital (65): “It could become necessary to change the methodology to ensure the continued accuracy of the benchmark, but any changes in the methodology have an impact on users and stakeholders of the benchmark. It is therefore necessary to specify the procedures to be followed when changing the benchmark methodology, including the need for consultation, so that users and stakeholders can take the necessary action in light of those changes or notify the administrator if they have concerns about those changes.”, and BMR, Article 13, paragraph 1: “An administrator shall develop, operate and administer the benchmark and methodology transparently. To that end, the administrator shall publish or make available the following information: […] (c) the procedures for consulting on any proposed material change in the administrator's methodology and the rationale for such changes, including a definition of what constitutes a material change and the circumstances in which the administrator is to notify users of any such changes.”
4.3.3 Expected impacts

**Figure 4.3: Expected impacts of the RTS on Transparency of Methodology**

<table>
<thead>
<tr>
<th>Goals</th>
<th>Topics</th>
<th>Affected stakeholders</th>
<th>Costs</th>
<th>Benefits</th>
</tr>
</thead>
<tbody>
<tr>
<td>Allow users to understand how a benchmark is made</td>
<td>Key elements of the methodology to be disclosed</td>
<td>Benchmark users (non-contributing)</td>
<td>Added cost (both ongoing and one-off) and delays to the benchmark production process could be passed through to the users if administrators have sufficient bargaining power.</td>
<td></td>
</tr>
<tr>
<td>Allow users to assess representativeness of index</td>
<td>Disclosure of information regarding internal review and approval of methodology</td>
<td>Benchmark administrators of critical and significant benchmarks</td>
<td>Ongoing and Indirect costs</td>
<td></td>
</tr>
<tr>
<td>Allow users to assess relevance to their needs</td>
<td>Reporting regarding material changes to methodology</td>
<td>Competent authority</td>
<td>Avoid / reduce due diligence costs of understanding index methodology before using it.</td>
<td></td>
</tr>
<tr>
<td>Allow users to assess appropriateness as a reference for financial instruments and contracts</td>
<td></td>
<td></td>
<td>Increased information content in indices / benchmarks may affect risk and returns on linked investments.</td>
<td></td>
</tr>
</tbody>
</table>

Source: Europe Economics.

**Costs**

Direct ongoing costs could include: preparing and publishing the methodology explanation to be disclosed, (additional) staff required to conduct regular internal reviews and consultations in case of methodology changes. Initially, these costs could be higher (in order to prepare the relevant documents and design the control procedures) and then decline over time, when the methodology would only require updates and monitoring. The Commission in their impact assessment stated that “the costs of providing this information would be small. Firms already have internal guidance on methodology and collate the input data. Publishing this data would not therefore involve significant costs.” Moreover, if some administrators in anticipation of implementing the BMR began disclosing their methodology, the overall costs for the industry could be lower.

As noted in ESMA’s Discussion Paper — there is a trade-off between intellectual rights and transparency. Too much information might enable front-running. In that respect, publishing too detailed methodology could have particularly negative consequences when input data is broadly available (as in the case of regulated data benchmarks). This risk might also be higher for benchmarks of relatively illiquid securities where the methodology is disclosed in sufficient detail to allow third parties to profit — at the end investor’s expense — from the anticipated liquidity demand arising from a forthcoming benchmark.

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6 EC, Impact Assessment, p35.
rebalance. However, as specified in the draft RTS (and recital 27 of the BMR\textsuperscript{8}), the key elements of the methodology to be disclosed do not include details on how the benchmarks are calculated. As such, the risk of violating intellectual rights and front running is likely to be mitigated.

Failing to protect intellectual rights might discourage innovation and contributors’ participation as well as impact competition. To the extent that the key elements of the methodology to be disclosed are sufficiently high-level to avoid violation of intellectual rights, this cost would be small or non-existent.

A very prescriptive requirement to have a consultation process would slow down the process of making any changes. This could be particularly inefficient when changes need to be made quickly. The draft RTS cannot and does not create any exemptions from the prescribed procedure (the Level I text only allows distinctions drawn on the type of the benchmark) and as such there is a risk that some inefficiencies would arise — although these may be attributable mostly or wholly to the BMR. The extent to which this would affect benchmark administrators is likely to be related to how “material change” is defined and how frequently such material changes need to be made urgently by administrators. The definition of “material change” is at the discretion of the administrators and should be published as part of the procedure for internal review of methodology.

Some responses to ESMA’s discussion paper suggested that publishing changes in methodology could be costlier for less significant benchmarks. While the requirement of the publication of administrators’ responses for administrators of significant benchmarks are slightly less extensive than for critical benchmarks, administrators of both categories of benchmarks are equally obliged to follow the same rules regarding the procedure for consultation on material changes to the methodology.

The key drivers of administrators’ current systems and business practices are existing regulatory requirements (where relevant, e.g. in the UK), followed by the IOSCO principles and pre-existing business practice. ESMA’s ‘Guidelines on ETFs and other UCITS issues’ were also mentioned as a driver of existing practice. Users often already expect a consultation process for methodological changes and, as such, material change as a result of the new regime is not widely expected.

In all aspects of the Technical Standards (including details of the methodology’s description, internal review processes, and processes around material changes in methodology), administrators anticipate making minor to no changes. Changes to internal review processes were seen as, marginally, the most significant. Furthermore, none of the benchmark users who responded to the survey said that they would review their use of the benchmark given its methodology, although some administrators indicated that there would be some minor changes in this respect.

Overall, we estimate ongoing annual costs across all administrators of significant and critical benchmarks to be in the region of €0.1–€0.3 million. This estimate is based on the methodology of a given benchmark being revised, on average, once per year. Based on the survey responses of administrators, who suggested minor to no changes required to existing practices, we estimate the number of incremental man days required per change in benchmark methodology to be in the region of 20-30 man days.

\footnote{LSEG — FTSE Russell response to ESMA consultation.}

\footnote{Recital 27 of the BMR: “The accuracy and reliability of a benchmark in measuring the economic reality it is intended to measure depends on the methodology and input data used. It is therefore necessary to adopt a transparent methodology that ensures the benchmark’s reliability and accuracy. Such transparency does not mean the publication of the formula applied for the determination of a given benchmark, but rather the disclosure of elements sufficient to allow stakeholders to understand how the benchmark is derived and to assess its representativeness, relevance and appropriateness for its intended use.”}
Benefits

The transparency of the key elements of the methodology as well as procedures governing reviews and approvals of the methodology, similarly to the requirements for input data itself, might have the following impacts:

- Discourage administrators from data manipulation and other kinds of abuse. The clearer and more transparent the rules are the less vulnerable the benchmark would be to manipulation.
- Promote investor confidence as they would be able to verify that the benchmark they use is suitable for them. According to survey respondents, transparency of methodology will be of significant benefit to market confidence, ranking as the second most significant driver of market confidence across the ten areas of Technical Standards. It would also provide a clear and consistent framework against which investors could compare the quality of a benchmark. In particular, they would be able to compare different benchmarks which could create a more effective competitive environment. As such, not only investor would be equipped in tools allowing them to make better decisions but also, due to increased comparability of benchmarks, competition between administrators could induce them to improve their methodologies and internal monitoring of their appropriateness.
- Support competent authorities in their supervisory roles. This could improve investors’ protection.

Publishing the procedure used for internal review of methodology would keep the administrators accountable in following the same process consistently over time. As a result, users would benefit from clarity and increased protection, which might mean that less individual investors’ due diligence is necessary.

Giving administrators discretion to determine the frequency of internal reviews, might allow them to conduct reviews in a cost efficient way. Assuming that they have an incentive to provide high quality products, they would conduct sufficiently many reviews to reflect the changing market environment and availability of data (with at least one review per year as required in the Directive in Article 5 on the oversight function requirements).

In case of administrators of critical benchmarks and those administrators of significant benchmarks who would not opt out, publishing the panel composition and eligibility criteria for becoming a member of the methodology panel, as well as disclosing the bodies/functions of those involved in the methodology review would reduce the likelihood of conflicts of interest. To the extent conflicts of interest are currently present in the industry, the integrity and quality of the benchmark would increase. Publishing the proposed changes in the methodology and following a consultation procedure eases the transition between methodologies for users. This might reduce volatility of the instruments relying on benchmarks.

Enabling significant benchmark administrators to opt out of some of the requirements could ensure that the compliance costs they would have to incur are not excessive.9

4.4 Code of conduct

4.4.1 What does the Benchmarks Regulation say?

The Benchmarks Regulation requires administrators to adopt a code of conduct, which specifies the responsibilities of their contributors in the provision of any given benchmark or benchmark family. According to Article 15 of the Benchmarks Regulation, the code of conduct is to cover issues pertaining to conflict management requirements, input data and reporting of suspicious input data, and record keeping.

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9 They can choose not to disclose a few of the elements of the methodology, some elements of the procedure regarding internal review of methodology, and may publish their response to the consultation responses in a form of a feedback statement.
According to Article 15, administrators are to ensure compliance of contributors to the code on at least an annual basis, and administrators should not use input data from those contributors who fail to adhere to the code. Administrators can issue a single code to cover all benchmarks within a family.

The Benchmarks Regulation stipulates that the code of conduct must include:

- description of input data to be provided and input data provision requirements (in accordance with Articles 11 and 14);
- details of who may contribute input data and procedures for evaluating the identity of contributors and submitters (and the latter’s authorisation) contributing on behalf of a contributor;
- policies to ensure all relevant input data are provided by the contributor;
- systems and controls to be put in place by the contributor.

Scope — this regulation excludes regulated data benchmarks (exempt under Article 17 of the Benchmarks Regulation). In addition, an administrator may choose not to apply Article 15(2) regarding in the case of its significant benchmarks (as stated in Article 25 of the Benchmarks Regulation) and its non-significant benchmarks (as stated in Article 26 of the Benchmarks Regulation).

It should be noted that the codes of conduct are also applicable to benchmark contributors who are not EU supervised entities.

Article 15 of the Benchmarks Regulation specifies the following.

ESMA shall develop draft Regulatory Technical Standards to further specify the elements of the code of conduct referred to in paragraph 2 for different types of benchmarks, and in order to take account of developments in benchmarks and financial markets.

ESMA shall take into account the different characteristics of benchmarks and contributors, notably in terms of differences in input data and methodologies, the risks of input data being manipulated and international convergence of supervisory practices in relation to benchmarks.

ESMA’s role is, therefore, to build on the code of conduct requirements set out in the Benchmarks Regulation to account for different types of benchmarks and potential developments, while taking into account the conditioning factors in the second paragraph quoted above.

4.4.2 What do the ESMA draft Technical Standards say?

ESMA provides that a benchmark administrator can establish a standard code of conduct across all benchmarks, that should then be adapted based on benchmark criticality, underlyings and methodology, as well as dependent on the supervised nature of contributors.

ESMA’s RTS identifies the following areas that the conduct of conduct is required to deal with.

- **Input data** (Article 1 of the RTS). For example, the code of conduct should include procedures for adjustment to, and standardisation of, contributions.
- **Submitters** (Article 2). For example, the code should set out how contributors need to ensure that submitters have the necessary skills, knowledge, training and experience to do this.
- **Policies to ensure that a contributor provides all relevant input data** (Article 3). For example, the code should include policies on what data should be included or excluded, and how to ensure secure data transfer.
• **Consistency of the process of contribution of input data** (Article 4). For example, the code is to specify the requirements expected throughout the contribution process regarding the quantity, quality and accuracy of data input, etc.

• **Validation of input data** (Article 5). For example, the code of conduct shall state that contributors need to have in place effective systems and controls to monitor input data, including suitable pre- and post-contribution checks for suspicious input data.

• **Record keeping policies** (Article 6). The code of conduct shall require contributors to keep specified records for at least five years in an easily accessible form, with adequate safeguards against tampering. These records would be made available to the administrator upon request.

• **Reporting of suspicious input data** (Article 7). The code needs to require contributors to have in place documented procedures to report suspicious input data to the contributor’s compliance function, the administrator and relevant competent authorities.

• **Conflicts of interest** (Article 8). The code needs to include policies, procedures and controls to ensure comprehensive management of conflicts of interest, for example addressing the remuneration policies of the contributor’s staff.

• **Training** (Article 9). The staff involved in the contribution process need to be trained on all elements of the code and other material matters.
4.4.3 Expected impacts

**Figure 4.4: Expected impacts of the RTS on Code of Conduct for contributors**

<table>
<thead>
<tr>
<th>Goals</th>
<th>Topics</th>
<th>Affected stakeholders</th>
<th>Costs</th>
<th>Benefits</th>
</tr>
</thead>
<tbody>
<tr>
<td>Clearly specify the responsibilities of contributors in the provision of benchmarks</td>
<td>Description of input data to be provided</td>
<td>Administrators of critical interest rate and commodity benchmarks (and significant benchmarks if stipulated by the competent authority)</td>
<td>One-off: Human resource costs in developing the various elements of the code of conduct.</td>
<td>A more standardised contribution process improves the clarity and robustness of future submissions.</td>
</tr>
<tr>
<td></td>
<td>Details of who may contribute input data</td>
<td></td>
<td>Ongoing: periodic costs of updating the code of conduct to reflect changes in benchmarks or their underlying methodologies, and of reviewing the framework for the contribution process.</td>
<td>Only those individuals with the necessary skills, knowledge, training and experience are able to submit input data, thus improving administrator confidence in data contributions.</td>
</tr>
<tr>
<td>Improve the reliability, integrity and quality of benchmarks</td>
<td>Policies to ensure all relevant input data are provided</td>
<td>Contributors to the above administrators</td>
<td>One-off: Human resource costs in understanding the requirements that the code(s) of conduct places on them, which may be exacerbated if code of conduct requirements differ significantly across different benchmarks and/or administrators. Costs of compiling relevant information and adapting existing, or developing new, practices and procedures to ensure compliance (e.g. periodic training).</td>
<td>Ongoing: the costs of undertaking the aforementioned procedures, including reporting, due diligence, record-keeping, monitoring and training.</td>
</tr>
<tr>
<td></td>
<td>Systems and controls to be put in place by the contributor</td>
<td>Competent authorities</td>
<td>The requirement for physical operational separation between submitters imposing one-off restructuring costs and introduce some ongoing inefficiencies, e.g. due to the prevention of information sharing.</td>
<td>May deter contributors if the administrator’s code of conduct overly constrains the contributor’s corporate governance, particularly if voluntary, outside the EU and/or the input data is used for purposes other than constructing the benchmark.</td>
</tr>
</tbody>
</table>

Source: Europe Economics.

**Costs**

The code of conduct could impose compliance costs on both administrators and contributors. Given the issues of scope raised in section 4.4.1, these costs would be incurred by the administrators of critical interest-rate and commodity benchmarks (with regulated data benchmarks exempt under Article 17 of the Benchmarks Regulation). These costs would not be incurred by administrators with respect to their significant and non-significant benchmarks (as stated in Article 25(1) and 26(1) of the Benchmarks
Regulation respectively), unless, in the case of significant benchmarks, a competent authority decides that the administrator must comply (as allowed for by Article 25(3)). Such costs would also be incurred by the contributors to these benchmarks, including contributors who are non-EU entities, but contribute to administrators within scope of the regulation.

In terms of the costs to administrators, they are likely to incur human resource costs in developing the various elements required in the code of conduct — and embedding this code into its organisation (e.g. through training). Of course, the materiality of these costs would depend on the extent to which such documentation is already produced. Where this is not the case, drafting new pieces of documentation could likely involve the input of, and liaison between, various different departments (legal, IT, compliance etc.). The materiality of costs would also depend on the extent to which the administrator has to adapt the code of conduct for different benchmarks. That said, it is likely that the code of conduct would share a lot of common elements across different benchmarks (despite some variations) and, therefore, these one-off costs are likely to be less significant on a per benchmark basis for those administrators operating a large number of benchmarks.

In terms of ongoing costs, administrators would face the periodic costs of updating the code of conduct documentation as appropriate to reflect changes in the benchmark itself or its underlying methodology. The administrator is also required to specify as part of the code of conduct the frequency for reviews of the framework for the contributors’ contribution process, which will lead to ongoing review costs for the administrator. However, despite the one-off costs of developing the code of conduct for contributors, administrators may stand to benefit on an ongoing basis to the extent that a more standardised contribution process improves the clarity and robustness of future submissions, as this may reduce the resources administrators need to dedicate to processing incoming contributions.

As with several of the other Technical Standards, the key drivers of current systems and business practices, according to the administrators surveyed, are existing regulatory practices (where applicable) and the IOSCO principles. For most, responding to changing market dynamics and anticipating the BMR coming into effect were not major determinants of their current practice.

Regarding the changes that administrators would need to make, the balance of views was that at most only minor changes would be required. More administrators were of the view that they would have to make minor changes to the content of code of conduct relative to the number of administrators who said that they would have to make minor changes regarding the actual existence of the code of conduct. This suggests that while a majority of administrators have some form of code of conduct in place with their contributors, they also anticipate that they will need to make minor tweaks to become compliant with the new code of conduct requirements.

Contributors could also face costs as a result of the code of conduct RTS. They are likely to incur people costs in understanding the new requirements that the administrator codes of conduct place on them. This could be exacerbated if the contributor contributes to several different benchmarks, and/or several different administrators, each of which has a slightly different code of conduct. This could lead to duplication (or worse) of costs on the part of the contributor. It may also impose higher resource costs on a one-off basis, if the contributor has to read across the requirements of the various codes of conduct in order to develop practices and procedures that are simultaneously compliant with all the codes of conduct. This will be particularly difficult if there are marked differences in some of the requirements established by administrators, or where the same team within the contributor is contributing to multiple (critical) benchmarks. That said, contributors’ compliance costs may be curtailed to some extent if an administrator adopts a common code of conduct across each family of benchmarks. The process of ensuring compliance with all codes of conduct is likely to require overall oversight from compliance personnel to ensure that, for each benchmark they contribute to, they are fulfilling of all aspects of the corresponding code of conduct.
Contributors would face costs in compiling relevant information and adapting existing, or developing new, practices and procedures in order to be compliant with the requirements of the code of conduct. Notably, this includes:

- a due diligence process for submitters, including identity and qualification checks and references;
- systems and controls to monitor input data both pre- and post-contribution, including recording of the checks that are undertaken;
- keeping records on a range of relevant information relating to contributions in an easily-accessible and secure form for a period of at least five years;
- reporting of suspicious input data both internally and externally to the administrator and the relevant competent authorities (i.e. the competent authority of the contributor and the competent authority of the administrator if it is different);
- maintenance of an up-to-date conflicts of interest register, providing evidence of the conflicts of interest that have arisen and the management measures adopted in response; and
- periodic training of staff involved in the contribution process about the code of conduct.

These requirements are likely to impose additional human resource costs on both a one-off and ongoing basis: the one-off costs in developing and implementing the new procedures and the ongoing costs of undertaking these procedures — whether that be ongoing reporting, due diligence, record-keeping, monitoring or training. They may also impose an additional ongoing costs on a lumpier basis, determined by when the administrator makes changes to the benchmarks and/or their underlying methodologies. The magnitude of these costs would depend on the extent to which the contributors already have these procedures in place and whether, and if so to what extent, they would need to be adjusted to become compliant.

The record-keeping requirements may also impose additional information storage costs for contributors, as well as the costs of developing a database to sort and find the information when requested by the administrator. The materiality would, in part, depend on the extent to which such records are already kept in accordance with other requirements or guidance on market practices, e.g. in accordance with existing IOSCO principles. Furthermore, where administrators permit the use of automated systems for the purpose of providing the benchmark submission, contributors are required to perform software update checks for these automated systems prior to them contributing input data. This could lead to further upfront IT costs, if the software currently in place is not up-to-date.

As with administrators, the materiality of costs faced by contributors would depend on the extent to which their administrators opt out of the requirements of Article 15 of the Benchmarks Regulation for their significant and non-significant benchmarks (and, on the flip side, the extent to which national competent authorities mandate that the code of conduct requirements must be met for significant benchmarks).

The requirements concerning conflicts of interest may be particularly burdensome for contributors as it could have implications for contributors’ IT systems, corporate policies and remuneration structures, including the possible need for Chinese walls, physical separation of staff and more thorough remuneration policies for submitters, although contributors may already have made many such changes in order to adhere to the IOSCO principles. Where such changes have not yet been made, there could be human and IT costs incurred during the actual migration process, in some cases resulting in ongoing inefficiencies, e.g. due to the prevention of previous information sharing between staff. This is only required by ESMA’s RTS where “reasonably practicable”, so significant one-off costs or ongoing costs are unlikely to materialise as otherwise this would imply that the separation was not “reasonably practicable” to impose.

Our fieldwork suggested that the impact of these revised codes of conduct on contributors is more material than the costs to the administrators of actually producing these revised codes of conduct. In terms of the provision and validation of input data and additional training, all respondents said that at least minor changes would be required, with 40 per cent in each cases anticipating major changes on the part of
Qualitative and Quantitative Cost-Benefit Analysis

contributors. The impact on record-keeping garnered more mixed views, with some administrators indicating that their contributors would need to make major changes while others reported that no changes would be required.

In terms of wider costs, there may be concern that the additional requirements imposed on contributors could discourage them from contributing data, especially if the administrator’s code of conduct is seen to overly constrain contributors’ own corporate governance decisions. This may be particularly true where contributions are made voluntarily, where the contributors are not supervised entities in the EU and/or where the input data is used for other purposes aside from constructing the benchmark. The extent to which this RTS in isolation could motivate a market participant to consider the cessation or even cease making contributions is unclear, but it seems unlikely to be a material driver in the context of the BMR as a whole. That said, one survey respondent noted that there could be broader consequences as a result of the impact on contributors, as contributors may require higher fees in order to recover the costs of the regulation or may move away from the business altogether, which would be detrimental to innovation.

The requirements may be seen as likely particularly burdensome for contributors outside the EU to EU-based administrators’ benchmarks (e.g. data from non-EU trading venues). This could lead to a degradation in the quality of submissions — and ultimately impact upon the viability of administration of such benchmarks within the EU.

When administrators were asked whether they anticipated any impacts on the users of benchmarks in terms of them reviewing their use of benchmarks given the new code of conduct, they said that they expected only minor or no changes to occur. This suggests that wider market impacts are unlikely to arise as a result of these Technical Standards, unless the higher fees (noted above) are sufficiently passed-through to benchmark users.

Overall, while the majority of administrators suggested that a code of conduct was already in place, they nevertheless need to make minor changes to their existing codes of conduct to be compliant with ESMA’s RTS. This is estimated to be in the region of a month full-time equivalent, i.e. 20 man days. This is estimated to give a total one-off cost to affected administrators of between €90,000 and €160,000, where the affected administrators are those involved in the provision of commodity or interest-rate benchmarks that are significant or critical (but not those involved only in the provision of regulated data benchmarks).

As aforementioned, in addition to the impact on administrators, there are also the costs to contributors in becoming compliant with these codes of conduct, particularly in terms of the provision and validation of input data and additional staff training. This applies to all firms who contribute to administrators of commodity or interest-rate benchmarks that are significant or critical, which is estimated to be in the region of 100 to 300 contributors. Given that the review and update of contributor’s internal operations to become compliant with the new codes of conduct is expected to take in the region of 20-30 man days, this equates to a total cost to contributors in the region of €0.8million to €4.8million. It can be seen that this is significantly higher than the costs imposed on the administrators, given a total industry cost in the range of €0.9million to €5million.

Benefits

In terms of wider benefits, the code of conduct RTS should help improve transparency and clarity of the contributions made, and their consistency over time. Another benefit is that, given the scope of the Benchmarks Regulation, it is the only part of ESMA’s RTS that place specific provisions on contributors who are non-EU entities.

Furthermore, by imposing a clearer framework for contributions and detailing some of the underlying policies and processes that contributors should have in place, the RTS should also help to provide a clearer audit trail and thus improve accountability. The requirements for submitters should ensure that only those
individuals with the necessary skills, knowledge, training and experience are able to submit input data, thus improving administrator confidence in the data provided by contributors.

The requirement for the contributor to report suspicious transactions to the relevant competent authorities means that the latter should be aware of any actual, or suspected, infringements and provide them with the information they require to undertake their legal and supervisory duties. The role of the competent authorities is also likely to be supported by a clearer distinction in responsibilities between administrators and contributors. By supporting more effective supervision by the competent authorities in this way, this requirement should help promote integrity of the benchmarks amongst users.

4.5 Governance and control requirements for supervised contributors

4.5.1 What does the Benchmarks Regulation say?

The Regulation requires supervised contributors to:

- ensure that the provision of input data is not affected by any conflicts of interest, and that — where discretion is required — it is independently and honestly exercised based on relevant information in accordance with the code of conduct; and
- have in place a control framework that ensures the integrity, accuracy and reliability of input data, and that it is provided in accordance with the BMR and the code of conduct.

Supervised contributors should have effective systems and controls to ensure the integrity and reliability of all contributions of data to the administrator, including:

- controls regarding who may submit input data (where proportionate, this should include a sign-off process by a natural person);
- appropriate training for submitters;
- measures for management of conflicts of interest, including organisational separation of employees where appropriate and consideration of how to remove incentives, created by remuneration policies, to manipulate a benchmark;
- record-keeping, for an appropriate period of time, of:
  - communications in relation to provision of input data,
  - all information used to enable the contributor to make each submission, and
  - all existing or potential conflicts of interest (including, the contributor’s exposure to financial instruments which use a benchmarks as a reference); and
- record-keeping related to internal and external audits.

Where input data relies on expert judgment, supervised contributors should, in addition to the above systems and controls, establish policies regarding the use of judgement or discretion, and should retain records of the rationale for it. Where proportionate, supervised contributors should take into account the nature of the benchmark and its input data.

Supervised contributors should fully cooperate with the administrator and the relevant competent authorities in the auditing and supervision of the provision of a benchmark and make available the information specified above.

ESMA has been charged with developing draft RTS to specify the requirements concerning governance, systems and controls. ESMA shall take into account the different characteristics of benchmarks and supervised contributors, the risk of manipulation of the input data and the nature of the activities carried out by the supervised contributors, and the developments in benchmarks and financial markets in light of
international convergence of supervisory practices. ESMA’s draft RTS shall not cover supervised contributors of non-significant benchmarks.

4.5.2 What do the ESMA draft Technical Standards say?

Governance, systems and controls

A supervised contributor shall have in place at least the following systems and controls to ensure the integrity, accuracy and reliability of all contributions:

- a process for identification of submitters, and procedures for making contributions when a submitter is unexpectedly unavailable, including the identification of alternates;
- policies, procedures and systems for monitoring the data used for contributions, and the contributions, which should
  - where it is proportionate for the controls to include a process for sign-off by a natural person senior to the submitter, include clear rules about the timing of the sign-off, and if this includes the possibility of a sign-off after submission, the circumstances in which this is permitted and the deadlines for sign-off should be stated; applicable only to contributions to critical benchmarks,
  - where it is not proportionate to include a process for such sign-off, provide for effective checks of the contribution to be carried out by staff other than the submitter who have sufficient knowledge, understanding and status to be able to challenge contributions; the frequency and timing of these checks should be specified taking into account the frequency of submission, the level of discretion involved in the process, and the nature, scale and complexity of the contributor’s activities; applicable only to contributions to critical benchmarks,
  - be capable of producing alerts in line with predefined parameters in order to allow for future analysis to be conducted.

The systems and controls shall include:

- periodic review of the process for contributing data;
- effective oversight of the process;
- policy and procedures for management of conflict of interest (including maintenance of a conflicts of interest register); and
- a policy on whistleblowing (including safeguards).

The systems and controls shall contain a procedure for detecting and managing breaches of the BMR and of code of conduct required by Article 15 BMR.

Process of contribution of input data

The systems and controls shall include processes and policies to ensure that each submitter has adequate knowledge and experience, and received adequate training on the firm’s conflict of interest policy and on the code of conduct. At least once a year all submitters’ understanding and knowledge should be reassessed. This requirement does not apply to contributors to significant benchmarks or to commodity benchmarks which are not critical.

The management of conflict of interest should include:

- physical separation of submitters from other employees working in other business units, where reasonably practicable, taking into account the nature, scale and complexity of the contributor’s activities and whether the contribution activity is based on the core business or on ancillary activities;
- internal oversight and verification procedures; where there is no organisation or physical separation of employees, the oversight and verification shall aim at controlling the interaction of submitters with front office employees.
The remuneration policy should ensure that the remuneration of a submitter is not linked to the benchmark nor to the submissions made, and is independent of the performance of any other contributor’s business unit that is likely to be significantly affected by the benchmark.

**Expert judgement**

Where input data relies on expert judgement, the policies shall include at least the following:

- the framework for ensuring consistency between different submitters and over time;
- identification of the information that could be used to support the use of expert judgement, and information that must not be taken into account; and
- procedures for systematic retrospective reviews of the application of expert judgement.

**Record keeping**

In keeping records of communications, the supervised contributor shall include the contributions made and the names of the submitters.

In keeping records of the contributor’s exposure to financial instruments which use a benchmark as a reference, the supervised contributor shall include information on whether the holding of the instruments is part of the core activity or is the result of treasury financing activity.

In keeping records of internal and external audits, the supervised contributor shall include, where applicable, the audit brief, the audit report, and a record of actions taken in response to each audit.
4.5.3 Expected impacts

Figure 4.5: Expected impacts of the RTS on Governance and Control Requirements for Supervised Contributors

<table>
<thead>
<tr>
<th>Goals</th>
<th>Topics</th>
<th>Affected stakeholders</th>
<th>Costs</th>
</tr>
</thead>
<tbody>
<tr>
<td>Improving governance and controls over the benchmark process</td>
<td>Governance, systems and controls</td>
<td>Benchmark users (non-contributing)</td>
<td>Increased fixed costs might reduce contributor’s willingness to provide data to administrators, which would in turn hurt benchmark’s quality and representativeness. Alternatively, contributors might aim to recover higher costs by increasing costs for their customers (not necessarily benchmark users).</td>
</tr>
<tr>
<td>Ensuring that contributors to benchmarks and the data they provide are subject to adequate controls, in particular to avoid conflicts of interest</td>
<td>Process of contribution</td>
<td>Benchmark administrators of critical and significant benchmarks</td>
<td>Minimising the interaction between supervised contributors and front office staff will reduce risk of data manipulation and thus improve the quality of benchmarks, One-off • Set up costs of processes compliant with systems and controls requirements Ongoing • Staff and IT costs (record keeping and maintenance). • External audits.</td>
</tr>
<tr>
<td></td>
<td>Expert judgement</td>
<td>Supervised contributing firm</td>
<td>Developing conflicts of interest procedures maintains transparency and improves investor confidence. This may lead to additional sales / sales recovery.</td>
</tr>
<tr>
<td></td>
<td>Record keeping</td>
<td>Competent authority</td>
<td>Facilitated supervisory role for competent authorities as they would benefit from a common control framework for supervised contributors.</td>
</tr>
</tbody>
</table>

Source: Europe Economics.

Costs

Direct one-off costs might include staff training and adjusting internal control and governance systems to comply with the RTS. On an ongoing basis additional costs for upgraded data monitoring systems (operational and IT costs), staff training, and external audits could be incurred by contributors. Our fieldwork indicated that a model whereby contributors were paid is not unheard of, at least in the commodity sector — but this is certainly not a market norm even there as yet. Therefore, passing on such costs to the administrator (if such a model exists) — which may in turn be passed onto the users — may not be possible. (Although one can imagine an additional cost burden triggering such a desire for recompense). Alternatively, contributors may choose to absorb these costs — or pass them on to someone else (i.e. the contributor could effectively cross-subsidise an increase in costs by seeking to recoup additional revenues elsewhere). The direct costs could be relatively high for those contributors submitting non-regulated data.

If the systems and controls requirements are too burdensome, then the contributor could be deterred from providing information, hurting the quality and representativeness of the benchmark. This was partly supported by our fieldwork with some contributors suggesting that governance and control requirements would have a minor effect on reducing the choice of benchmarks available to users. The same respondents
stated that this RTS will have a significant effect on increasing the licensing cost of benchmarks to market participants. Moreover, in general all contributors strongly agreed with the statement that the RTS as a whole would reduce the contributors' willingness to contribute data to administrators. Ultimately, they will strike a trade-off between the regulatory risks that could arise from the contribution process and the potential reputational damage that could accrue from discontinuing. Cost was not a critical decision-variable for the contributors we engaged with.

Excessive sign-off procedures could cause delays when submitting information, which could be particularly damaging to the benefits created by developing automated processes. This cost would be partly mitigated by ESMA acknowledging that in certain circumstances, where a full sign-off procedure is not proportionate, other measures can be implemented instead. The sign-off requirements would strictly apply only to critical benchmarks, which means that the costs borne by the administrators of significant benchmarks and commodity benchmarks which are not classified as critical could be relatively lower.

There is a trade-off between very rigorous requirements and efficiency in using judgement or discretion by contributors. The more restrictive the requirements are, the less room for actual discretion is left to contributors. This could limit the possibility of errors and manipulation. However, this could also become inefficient in situations where methods other than those specified in the policies need to be adopted and/or where decisions have to be made quickly. In order to balance these two possibilities, the draft RTS listed what kind of procedures should be developed at minimum but left the exact specification of these procedures to supervised contributors.

Contributors’ were consistent in expecting only minor changes as being necessary as a result of the Technical Standards, including staff training, measures around avoiding conflicts of interest, record-keeping and other systems and controls.

Overall, the one-off training and transitional costs faced by supervised contributors are expected to be in the region of 20-30 man days. When multiplied by the estimated number of contributors to critical and significant benchmarks (in the region of 135 to 400), this equates to a total one-off cost to supervised contributors of €1.2–€6.4million.

Benefits

As indicated in the ESMA consultation paper, it could be beneficial to create a control framework for supervised contributors that would be consistently applied across the EU. Otherwise, each national competent authority would have to create its own criteria and procedures for judging compliance.

General systems and controls might restore transparency and users’ confidence. This, similarly to other measures regarding input data and transparency of methodology, could lead to increased sales / sales recovery. The governance and control requirements are seen as significant for improving regulatory oversight and market confidence, ranking first, in both cases, when compared with the significance of impact of the other Technical Standards. Improved regulatory oversight was rated as the second most important benefit of ESMA’s Technical Standards.

Identifying submitters as well as alternates in case a submitter becomes unavailable could ensure continuity of the data provided to administrators. A clear procedure governing sign-offs could reduce the risk of errors and/or manipulation by a single actor. This might increase the extent to which administrators can rely on data provided by contributors, and thus promote the quality of benchmarks. As a result, users’ confidence and sales might increase.

An ex post sign-off procedure (which would be appropriate if the sign off cannot be done before submission) ensures that data is still checked and not overlooked. As such, any errors or deliberate data manipulations can be identified and rectified in a timely manner. Clear rules regarding when ex post sign off is appropriate should ensure that this procedure is not overused by supervised contributors, which would otherwise generate additional costs.
The RTS requires that, when sign-off procedure is not proportionate, appropriate checks are performed by sufficiently qualified staff other than the submitter. This ensures that even when a formal sign-off procedure is not implemented, the quality of the data is less likely to be compromised. The requirement to periodically review the process of contributing data could help ensuring high quality of submitted data in a consistent way. Minimising the interaction between supervised contributors and front office staff will reduce risk of data manipulation.

Developing conflicts of interest procedures maintains transparency and improves investor confidence. This could make the use of contributed data more efficient as it would indicate which data can be assumed to be safe to use.

Laying out the framework for expert judgement encourages consistency in developing the benchmark, as well as leaves less room for manipulation in situations where manipulation is most likely to occur. The resulting stability might promote confidence among users and reduce volatility in the market.

The record keeping requirements are likely to facilitate the supervisory role of competent authorities.

### 4.6 Criteria for significant benchmarks

#### 4.6.1 What does the Benchmarks Regulation say?

A competent authority may decide that the administrator of a significant benchmark should apply some of the requirements of Article 4 (Governance and conflict of interest requirements), Article 11 (Input data), and Article 15 (Code of conduct) of the Directive, if it considers it appropriate given the nature or impact of the benchmark, or the size of the administrator. To assess the appropriateness, the competent authority should, based on the information provided by the administrator, take into account:

- the vulnerability of the benchmark to manipulation,
- the nature of the input data,
- the level of conflicts of interest,
- the degree of discretion of the administrator,
- the impact of the benchmark on markets,
- the nature, scale and complexity of the provision of the benchmark,
- the value of financial instruments, financial contracts or investment funds that reference the benchmark,
- the importance of the benchmark to financial stability, and
- the administrator’s size, organisation form or structure.

ESMA has been charged with developing draft RTS to further specify the above criteria.

#### 4.6.2 What do the ESMA draft Technical Standards say?

The RTS specifies the following elements the competent authority should take into account for each of the general criteria specified in the BMR respectively.

**In relation to the vulnerability of the benchmark to manipulation**, the administrator should assess:

- whether the benchmark is based on transaction data, whether contributors are supervised, or whether any other robustness measures in place;
- whether the administrator’s organisation structure prevents manipulation incentives, and whether the administrator has a financial interest in products referencing the benchmark;
- whether there are proven cases of manipulation of the same benchmark or of a benchmark with similar methodology provided by an administrator of similar size and organisational structure;
- whether a third party has specific incentives to manipulate the benchmark.
In relation to the nature of the input data, the administrator should assess:

- when the input data is transaction data, whether the administrator is a participant in the market;
- the economic reality the benchmark intends to measure;
- when the input data is provided by contributors, whether the contributors hold positions in financial instruments referencing the benchmark;
- when the input data is sourced from third country exchanges or trading systems, whether the latter are supervised to ensure the integrity of the input data; and
- when the input data consists of quotes, whether these are committed or indicative, as well as whether they are prone to manipulation.

In relation to the level of conflicts of interest, the administrator should assess:

- whether the administrator has a financial interest in products referencing the benchmark;
- where the benchmark is based on contributions, whether the administrator’s relations with contributors are governed by adequate control mechanisms; and
- whether the administrator has controls or measures effectively mitigating conflicts of interest.

In relation to the degree of discretion applied by the administrator, the administrator should assess:

- where the benchmark methodology allows for expert judgement, whether its exercise is sufficiently transparent; and
- where the benchmark is based on quotes, whether the internal control measures applied are effective.

In relation to the impact of the benchmark on markets, the administrator should assess:

- where the benchmark is particularly relevant for a specific market(s), whether the unreliability of the benchmark would have a disruptive effect on the market(s), and whether there are adequate substitutes for that benchmark;
- when the benchmark is significant, the quantitative relation between the instruments referencing the benchmark and the total value of the respective instruments in a Member State.

In relation to the nature, scale and complexity of the provision of the benchmark, the administrator should assess:

- the degree to which input data is based on contributions, or whether the data is transaction data, and how this is reflected in the administrator’s control mechanisms;
- the amount of data, the number of data sources and whether the administrator has sufficient technical means to process the data;
- whether the calculation method gives rise to operational risks when processing data;
- the extent to which the administrator relies on external contributors.

In relation to the importance of the benchmark to financial stability, the administrator should assess the quantitative relation between the total value of the products referencing the benchmark and the total assets of the financial and banking sector in a Member State (where known to the competent authority).

In relation to the value of financial instruments, financial contracts or investment funds that reference the benchmark, the administrator should assess:

- the total value of all products referencing the benchmark across of all maturities or tenors (where known to the competent authority);
- whether the benchmark’s use is concentrated in individual categories of products (financial instruments, financial contracts, investment funds);
- when a benchmark is significant and where known to the competent authority, the proximity of the total value of referencing products to the thresholds for critical benchmarks.
In relation to the administrator's size, organisational form, or structure, the administrator should assess:

- when the provision of benchmarks is not the administrator’s principal business activity, whether the provision of the benchmark is organisationally separate and whether there are other means to avoid conflicts of interest; and
- when the administrator is part of a group and where some entities within this group are actual or potential users of the benchmark, whether the entity providing the benchmark is acting independently and how appropriate other measures applied by the administrator are to avoid conflicts of interest.

4.6.3 Expected impacts

**Figure 4.6: Expected impacts of the RTS on Criteria for Significant Benchmarks**

<table>
<thead>
<tr>
<th>Goals</th>
<th>Topics</th>
<th>Affected stakeholders</th>
<th>Costs</th>
<th>Benefits</th>
</tr>
</thead>
<tbody>
<tr>
<td>Applying the principle of proportionality regarding the requirements of significant benchmark administrators</td>
<td>Administrators may choose to opt-out from one or more BMR provisions</td>
<td>Benchmark Administrators of non-critical benchmarks</td>
<td>Ongoing: To the extent that administrators are required to organise information to the competent authorities some reporting costs could potentially be borne</td>
<td>The administrator’s own assessment should reflect upon the same information set as the competent authority and, hence, any costs should be de minimis.</td>
</tr>
<tr>
<td>Ensuring that the benchmark is robust, not prone to manipulation and not exposed to conflicts of interest</td>
<td>NCAs would assess the explanations offered by the administrator and may instruct the inclusion of the missing provisions</td>
<td>Benchmark users</td>
<td>Administrators may also benefit from increased legal certainty (i.e. if they appropriately mimic these criteria in their own determination, the likelihood of a successful subsequent challenge by the relevant NCA should be much reduced).</td>
<td>Greater comparability across Europe should enhance the efficiency of the new regime (ultimately to the benefit of users).</td>
</tr>
<tr>
<td></td>
<td></td>
<td>Competent authority</td>
<td>Indirect Cost: Benchmarks close to the lower and upper bound of the significant benchmark definition may impact adversely market confidence and choice</td>
<td>Ongoing: NCAs would bear the costs associated with the conduct of the assessment. The nature of any such costs would likely relate to reporting and collating data, i.e. largely speaking people time costs.</td>
</tr>
<tr>
<td></td>
<td></td>
<td></td>
<td></td>
<td>NCAs would possess a well-defined framework within which to develop their assessment, thus leading to greater ease and speed in decision-making (i.e. reducing costs).</td>
</tr>
<tr>
<td></td>
<td></td>
<td></td>
<td></td>
<td>facilitated supervisory role and improved oversight for competent authorities as they would benefit from a common control framework for supervised contributors.</td>
</tr>
</tbody>
</table>

Source: Europe Economics.

Administrators of significant benchmarks can choose not to apply certain provisions of the BMR (around organisational separation, control mechanisms for certain types of input data, contributor’s code of conduct). In turn, NCAs may partly or fully over-ride this choice, i.e. obliging the administrator to apply these provisions. ESMA’s Technical Standards provide guidance on how NCAs are to make such an assessment.

**Direct compliance costs**

Any compliance costs associated with the conduct of the assessment would be borne by the NCAs themselves. The nature of any such costs would likely relate to reporting and collating data, i.e. largely speaking people time costs.
Some minor one-off costs could be borne by administrators, to the extent that the latter are required to set up and organise information to be communicated to the competent authorities. However, the administrator’s own assessment should reflect upon this same information set, hence any such costs should be assumed de minimis. In this respect, as administrators’ ongoing costs should also be minimal.

This suggests that the total compliance costs associated with the criteria for significant benchmarks are low. Indeed, it is not clear these are quantifiable, as it is still very unclear at this stage the extent to which administrators will exercise their right not to apply certain aspects of the BMR.

**Indirect Costs**

There might be some frictions for benchmarks close to the lower and upper bound of the significant benchmark definition, which may impose an indirect negative effect on market confidence. In particular, investors may be sceptical over benchmarks that are below, yet close to, the lower bound and disqualify them from their investment strategies as they are not regulated.

Conversely, for benchmarks on the upper end of the range, the definition would fail to capture benchmarks which are locally significant but not necessarily associated with large value of transactions. In this case, reduced investor confidence in those benchmarks may have adverse effects on choice.

**Benefits**

The further specification of the Level 1 criteria should significantly reduce the risk of different competent authorities applying them differentially by providing NCAs with a well-defined framework within which to develop their assessment. This should lead to greater ease and speed in decision-making by NCAs (i.e. reducing costs), while also improving oversight.

By providing additional clarity on the criteria to be applied, administrators may also benefit from increased legal certainty (i.e. if they appropriately mimic these criteria in their own determination, the likelihood of a successful subsequent challenge by the relevant NCA should be much reduced).

In addition, and more importantly, this should create greater comparability across Europe, reducing the scope for jurisdiction shopping and promoting a level-playing field between participants. This should enhance the efficiency of the new regime (ultimately to the benefit of users). However, few respondents noted that there would be significant improvements in efficiency as a result of the Technical Standards (ranking as the second lowest benefit, only ahead of increased competition).

### 4.7 Compliance statement

#### 4.7.1 What does the Benchmarks Regulation say?

An administrator of a significant benchmark can choose not to comply with some of the requirements of Article 4 (Governance and conflict of interest requirements), Article 11 (Input data), and Article 15 (Code of conduct), provided it publishes and maintains a compliance statement that clearly states why it is appropriate not to comply with those requirements.

Similarly the administrator of a non-significant benchmark can choose not to apply some of the requirements of Article 4 (Governance and conflict of interest requirements), Article 5 (Oversight function requirements), Article 6 (Control framework requirements), Article 7 (Accountability framework requirements), Article 11 (Input data), Article 13 (Transparency of methodology), Article 14 (Reporting of infringements), Article 15 (Code of conduct), and Article 16 (Governance and control requirements for supervised contributors), it should publish a compliance statement clearly stating why it is appropriate not to comply with those requirements. The administrator should provide the compliance statement to the competent authority.
The relevant competent authority should review the compliance statement provided by the administrator of a non-significant benchmark. It may request additional information from the administrator (as specified in Article 41, Powers of competent authorities) as well as changes to ensure compliance with the Directive.

ESMA shall develop draft ITS to develop one compliance statement template for administrators with significant benchmarks and one for administrators with non-significant benchmarks.

4.7.2 What do the ESMA draft Technical Standards say?

Administrators of significant benchmarks

The administrator of a significant benchmark should use the following template for the production of a compliance statement.

<table>
<thead>
<tr>
<th>Item</th>
<th>Text field</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>A. General Information</strong></td>
<td></td>
</tr>
</tbody>
</table>
| 1. Date of creation of the compliance statement and of the latest update | 1. Created: [dd/mm/yy]  
Last updated: [dd/mm/yy] |
| 2. Identity of the administrator | 2. [As it appears in the “Register of administrators and benchmarks” published by ESMA] |
| 3. Relevant National Competent Authority | 3. [The NCA who has authorised the administrator] |

The following section(s) includes:
- which provisions the administrator has chosen not to apply,
- explanations on the appropriateness of this choice in relation to each provision not applied, and
- an indication to which significant benchmarks these provisions do not apply.

Such a section shall cover each group of significant benchmarks provided by the administrator for which:
- the same provisions are not complied with, and
- the same explanations for non-compliance apply.

**B. [Insert name of the administrator as in field 2] chooses not to apply the following provisions of Regulation (EU) No 2016/1011 with respect to its significant benchmarks listed below**

<table>
<thead>
<tr>
<th>Item</th>
<th>Text field</th>
</tr>
</thead>
<tbody>
<tr>
<td>4. Identification of significant benchmarks for which this section is relevant</td>
<td>4. [List of all the single benchmarks/ families of benchmarks, including, where available, single identifiers]</td>
</tr>
<tr>
<td>5. Indication to where the benchmark statements of the benchmarks referred to in section have been published</td>
<td>5. [e.g. webpage link]</td>
</tr>
</tbody>
</table>
| 6. (i) clear identification of each single provision;  
(ii) for each provision listed under point (i), a dedicated, detailed and clear explanation of the reasons why the administrator considers it appropriate not to comply with that specific provision | 6(i). [Number of the Article and paragraph of Regulation (EU) No 2016/1011 and full text of each single provision]  
6(ii). [Explanation on the appropriateness of the non-compliance for each specific provision] |

Administrators of significant benchmarks should amend the compliance statement immediately whenever any of the information is no longer up to date. After each amendment, the administrator should publish and provide to its competent authority the updated statement.
Administrators of non-significant benchmarks

The administrator of a non-significant benchmark should use the following template for the production of a compliance statement.

<table>
<thead>
<tr>
<th>Item</th>
<th>Text field</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>A. General Information</strong></td>
<td></td>
</tr>
</tbody>
</table>
| 1. Date of creation of the compliance statement and of the latest update | 1. Created: [dd/mm/yy]  
Last updated: [dd/mm/yy] |
| 2. Identity of the administrator | 2. [As it appears in the “Register of administrators and benchmarks” published by ESMA] |

The following section(s) includes:
- which provisions the administrator has chosen not to apply,
- explanations on the appropriateness of this choice in relation to each provision not applied, and
- an indication to which non-significant benchmarks these provisions do not apply.

This type of section shall be repeated for each group of non-significant benchmarks provided by the administrator for which:
- the same provisions are not complied with, and
- the same explanations for non-compliance apply.

| B. [Insert name of the administrator as in field 1] chooses to not apply the following provisions of Regulation (EU) No 2016/1011 with respect to its non-significant benchmarks listed below | |
| 3. Identification of non-significant benchmarks for which this section is relevant | 3. [List of all the single benchmarks / families of benchmarks, including, where available, single identifiers] |
| 4. (i) clear identification of each single provision;  
(ii) for each provision listed under point (i), a dedicated, detailed and clear explanation of the reasons why the administrator considers it appropriate not to comply with that specific provision | 4(i). Number of the Article and paragraph of Regulation (EU) No 2016/1011 and full text of each single provision  
4(ii). Explanation on the appropriateness of the non-compliance for each specific provision |

Administrators of non-significant benchmarks should amend the compliance statement immediately whenever any of the information is no longer up to date. After each amendment, the administrator should publish and provide to its competent authority the updated statement.
4.7.3 Expected impacts

Figure 4.7: Expected impacts of the RTS on Compliance Statements

Direct compliance costs

Given that the issuance of a compliance statement is part of the BMR and ESMA’s ITS only specifies its template, the incremental direct compliance costs associated with the latter are not likely to be substantial, and largely limited to reporting costs. This outcome is also likely to be facilitated by the requirement of submitting only one compliance statement for all benchmarks exempted from certain BMR requirements.

Significant compliance costs could be generated where the listings of individual benchmarks issued by an administrator change frequently. For instance, particularly for larger administrators, benchmark listings may change on a weekly, or even daily, basis. Such changes would necessitate the issuance of an updated statement, in cases where the administrator decides to apply the “exemption” to the new benchmarks.

Notwithstanding the smaller set of criteria for those administrators of non-significant benchmarks could result in the above costs being disproportionately incurred by small administrators of non-significant benchmarks. It is not yet clear the extent to which the associated costs might be passed onto the benchmark users.

Overall, we find that the provision of a template by ESMA adds no material costs on top of that already incurred as a result of the Level 1 BMR Regulation, i.e. the incremental compliance costs due to the Technical Standards are negligible.
Indirect costs and market impacts

The template compliance statement for non-significant benchmarks does not include a section indicating where the relevant benchmark statements can be accessed. This may reduce the transparency of non-significant benchmarks leading to increased searching costs for users, as they would have to identify the relevant benchmark statements themselves when deciding whether to use any given benchmark.

The requirement to update the compliance statement in response to a change in methodological inputs that implies a change in the "exemption" situation of the benchmark may dissuade administrators from changing the relevant methodologies as often as they would deem optimal. If the costs involved in producing or updating a compliance statement (particularly for those benchmarks whose methodological inputs change frequently) outweigh the associated benefits, administrators may be inclined to stop issuing the benchmark, thus reducing investor choice. If the frequency of methodological updates is limited, then this could reduce the representativeness of the economic reality that is meant to be measured by a given benchmark and, thus, expose users to unanticipated outcomes when including the relevant instruments in their investment strategies.

Benefits

Overall, the template compliance statement aims at ensuring consistency and clarity in the explanations offered for the non-application of BMR provisions, thus improving regulatory oversight and increasing confidence among investors. Overall, it should lead to:

- greater clarity with regards to the documents issued by different administrators — the use of a common template is likely to facilitate the examination of compliance statements by NCAs, users and other interested parties; and
- greater transparency in the explanations offered for the non-application of BMR requirements — the template is organised into specific sections that allow the reader to easily understand:
  - which requirements have not been applied by the administrator;
  - for which benchmarks these requirements have not been applied; and
  - the reasons why such decisions were taken.

The broad similarities in the template for significant and non-significant benchmarks ensure ease and consistency for both NCAs and administrators. This is particularly important as the value of some benchmarks may fluctuate between significant and non-significant during a short period of time.

In addition, the openness of the detailed explanation for non-application may allow the administrator to re-use reporting material used in the IOSCO compliance statement for the BMR compliance statement. This should restrict duplication of effort for international administrators.

4.8 Benchmark statement

4.8.1 What does the Benchmarks Regulation say?

Within two weeks of registration the administrator should publish a benchmark statement for each benchmark (or for each family of benchmarks) administered. Where the administrator begins providing a new benchmark (or a family of benchmarks) a similar statement should be published by the administrator. The administrator should review at least biannually and update the statements in the event of any changes to the information specified below.
The benchmark statement should:

- define the market or economic reality measured by the benchmark and the circumstances under which the benchmark may become unreliable;
- lay down technical specifications that identify the elements of the calculation of the benchmark in relation to which discretion may be exercised, the criteria applicable to the exercise of such discretion, the position of the persons that can exercise discretion, and how such discretion is evaluated;
- provide notice of the possibility that under certain circumstances the benchmark may need to change or be discontinued; and
- advise users that changes to, or the cessation of, the benchmark may have an impact upon the products referencing the benchmark.

The benchmark statement should contain at least:

- the definition for all key terms relating to the benchmark;
- the rationale behind the benchmark methodology and procedures for the review of the methodology;
- the criteria and procedures used to determine the benchmark (including the input data, the priority given to different types of input data, the minimum data needed to determine a benchmark, the extrapolation models/methods and any procedures for rebalancing the constituents of a benchmark’s index);
- the controls and rules governing the consistency of the use of judgement or discretion by the administrator or the contributors;
- the procedures governing the determination of the benchmark in periods of stress or where transaction data sources may be insufficient, inaccurate or unreliable, and the potential limitations of the benchmark in such periods;
- the procedures for dealing with errors in input data or in the determination of the benchmark (including when a re-determination of the benchmark is required); and
- the identification of potential limitations of the benchmark, including its performance in illiquid or fragmented markets, and the possible concentration of inputs.

ESMA has been tasked with the development of draft RTS to further specify the contents of the benchmark statement and the cases in which an update of such statement is required, distinguishing for different types of benchmarks and sectors as set in the Directive and taking into account the principle of proportionality.

4.8.2 What do the ESMA draft Technical Standards say?

Disclosure requirements

For the purpose of defining the market or economic reality measured by the benchmark the statement should contain:

- a general description of the measured market or economic reality;
- the geographical boundaries of the measured market or economic reality;
- any other relevant information, including among others:
  - information on participants of the measured market;
  - barriers to market access; and
  - an indication of the size of the market or economic reality.
For the purpose of defining the circumstances in which the benchmark might not be a reliable measure of the relevant market or economic reality, the administrator should take into account the following (while considering the methodology for the specific benchmark):

- the minimum size of the measured market or economic reality, and circumstances in which the administrator would lack sufficient data to determine the benchmark according to the methodology;
- the degree of liquidity of the underlying market necessary to ensure the integrity and reliability of the benchmark; and
- any other relevant information, e.g. exceptional market events (not applicable to significant benchmarks).

In relation to the exercise of discretion, the benchmark statement should:

- identify each element of the benchmark calculation process where discretion is or has to be exercised; and under which conditions discretion may or may not be used in accordance with the methodology;
- indicate the position of each function or body who may exercise discretion; and
- outline each step of the ex-post evaluation process for the use of discretion.

In relation to the process of changing or discontinuing a benchmark, the benchmark statement should:

- indicate the method and the means by which users are informed of a change to or a cessation of the benchmark;
- refer to the process for public consultation on the material changes to the methodology (where appropriate); and
- to the extent known, indicate any expected impacts of changes to or the cessation of the benchmark upon the products referencing the benchmark.

If a benchmark falls in more than one type of benchmarks, this should be outlined in the statement. Several of the above requirements should not apply (fully) to non-significant benchmarks.

**Regulated-data benchmarks**

In respect of a regulated-data benchmark, the benchmark statement should:

- indicate the benchmark’s qualification as a regulated-data benchmark;
- include, where available, the single identifier of the benchmark; and
- state the sources of the input data used and sectoral disciplines applying to such sources.

Where appropriate and without prejudice to transparency and easy access to information, the benchmark statement may be limited to indicating relevant sources documents, including when and where these have been disclosed to the public.

**Interest rate benchmarks**

In respect of an interest rate benchmark, the benchmark statement should:

- indicate the benchmark’s qualification as an interest rate benchmark;
- include, where available, the single identifier of the benchmark;
- refer to the enhanced regulatory regime applicable to interest rate benchmarks and specify which increased oversight mechanisms are applicable; and
- include details on applicable time limits (delays in publication of the benchmark and its re-determination) and provisions for the notification of users in such circumstances.

For any other relevant information and without prejudice to transparency and easy access to information, references to other sources of information may be included (in particular, to the external audit report and administrator’s website).
Commodity benchmarks

In respect of a commodity benchmark, the benchmark statement should:

- indicate the benchmark’s qualification as a commodity benchmark;
- include, where available, the single identifier of the benchmark;
- indicate whether the benchmark falls under the regime of Benchmark integrity and reliability (Title II of the BMR) or Commodity benchmarks (Annex II of the BMR);
- include a concise description of the criteria that define the relevant underlying physical commodity;
- indicate where the explanations for each benchmark’s calculations are published by the administrator;
- outline the professional profiles of the contributors to the benchmark and explain (where applicable) why the benchmark is predominantly based on contributions by non-supervised entities.

Critical benchmarks

In respect of a critical benchmark, the benchmark statement should:

- indicate the benchmark’s qualification as a critical benchmark;
- include, where available, the single identifier of the benchmark;
- refer to the enhanced regulatory regime applicable to critical benchmarks and specify which increased oversight mechanisms are in place;
- contain information (if available) on the most relevant types of financial products that reference the benchmark;
- contain information (if available) on the degree of use of the benchmark in one or more Member States and on the total reference value in respect of the critical benchmark;
- explain that the benchmark is subject to mandatory administration, contribution and supervision;
- contain a list of the contributors (including their name, principal activity and location);
- in the event of planned cessation, provide details of how the users can contact the administrator or competent authority to provide further information on potential adverse impacts; and
- include details on applicable time limits (delays in the publication of the benchmark and re-determination) and provisions on notification of users of such circumstances.

Significant benchmarks

In respect of a significant benchmark, the benchmark statement should:

- indicate the benchmark’s qualification as a significant benchmark; and
- include, where available, the single identifier of the benchmark.

Non-significant benchmarks

In respect of a non-significant benchmark, the benchmark statement should:

- indicate the benchmark’s qualification as a non-significant benchmark; and
- include, where available, the single identifier of the benchmark.

Updates

The administrator should review and update the benchmark statement whenever the included information is no longer correct or sufficiently precise.

An update is required in particular if:

- the benchmark is no longer reliable to accurately measure the underlying market or economic reality;
- the type of the benchmark changes;
- there is a significant change in the benchmark or its methodology; and
Qualitative and Quantitative Cost-Benefit Analysis

- fair and easy access to information is impaired as a consequence of a change in the information incorporated in the benchmark statement by reference.

In case a change occurred prior to the publication of the amendment to the benchmark statement, a clear indication of the relevant time period should be included in the update.

4.8.3 Expected impacts

Figure 4.8: Expected impacts of the RTS on Benchmark Statements

<table>
<thead>
<tr>
<th>Goals</th>
<th>Topics</th>
<th>Affected stakeholders</th>
<th>Costs</th>
<th>Benefits</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td></td>
<td>Distinguishing between different types of benchmarks</td>
<td></td>
<td></td>
</tr>
<tr>
<td></td>
<td></td>
<td>Definition of the economic reality measured by a given benchmark</td>
<td></td>
<td></td>
</tr>
<tr>
<td></td>
<td></td>
<td>Providing comprehensive information reflecting the application of discretion</td>
<td></td>
<td></td>
</tr>
<tr>
<td></td>
<td></td>
<td>Providing clear information to the public over what a benchmark is intended to measure</td>
<td></td>
<td></td>
</tr>
<tr>
<td></td>
<td></td>
<td>Providing clear information to the public over a benchmark’s susceptibility to manipulation</td>
<td></td>
<td></td>
</tr>
<tr>
<td></td>
<td></td>
<td>Benchmark administrators of interest rate, commodity and critical benchmarks irrespective of type</td>
<td></td>
<td></td>
</tr>
<tr>
<td></td>
<td></td>
<td>Benchmark administrators of critical, significant and non-significant benchmarks</td>
<td></td>
<td></td>
</tr>
<tr>
<td></td>
<td></td>
<td>Contributors to commodity benchmarks</td>
<td></td>
<td></td>
</tr>
<tr>
<td></td>
<td></td>
<td>Benchmark users (non-contributing)</td>
<td></td>
<td></td>
</tr>
</tbody>
</table>

Source: Europe Economics.

Direct compliance costs

Similar to the compliance statement (see section 4.7.3), the requirement to publish a benchmark statement, including the general characteristics of its content, forms part of the BMR (Article 27). The RTS does not include additional elements pertaining to the benchmark statement, but rather specifies how the elements in Article 27 would be incorporated in practice, i.e. it “fleshes out” the BMR.

The draft RTS distinguishes between different types of benchmarks, and incremental reporting costs are likely to be higher for administrators of interest rate and commodity benchmarks — and administrators of critical benchmarks (also when covered within the previous two categories).

An important aspect of this RTS is the definition of the economic reality measured by a given benchmark. The aim of this provision is to allow a more accurate placement of a benchmark within the overall economic landscape, thus creating a safer context for benchmarks usage. Nevertheless, providing an
indication of the size of some markets in which a benchmark is referenced, even at a very high level, may be difficult (or even impractical), thus creating additional direct costs for administrators (e.g. one-off IT investments, ongoing human resources employed). Apart from the limitations implied in the calculation of the benchmark exposure itself, there is limited transparency on market size, e.g. in commodities markets where a significant proportion of market players do not publish transaction volumes as they tend to be active for hedging purposes and so do not need to. In this regard, different administrators of similar benchmarks may provide divergent indications of market size and, thus, create confusion among benchmark users.

In addition, outlining the professional profiles of the contributors to commodities benchmarks increases compliance costs for them and the administrators, as additional information would need to be obtained and included in the benchmark statement. Such information could also be subject to confidentiality arrangements, thus creating additional costs in respect of any re-papering of any data licensing agreements. As we note at 3.3 above, such licensing agreements are in use but certainly not universal at present in the production of benchmarks related to commodity markets.

Similarly, for certain interest rate benchmarks, it may be particularly challenging to obtain an indication of the overall trading volumes of the market. With the exception of studies/surveys published by Central Banks or other private/bodies which mainly allow for an understanding of trends (and may also be accessed in return for a fee), data available in these cases is limited. Moreover, administrators of interest rate benchmarks will be additionally burdened by demonstrating the measures taken to address the requirements of Annex I.

With regards to information reflecting the application of discretion, as above, administrators could incur additional direct costs in terms of making sure the explanations offered are adequate and concise, verification checks and peer reviews either by other members of staff or external resources (e.g. attestation and audit costs from consultancy firms specialising on regulatory compliance) and other reporting costs (e.g. writing, editing, printing, etc.). Given that discretion is not applied to all benchmarks, introducing such a requirement in the benchmark statement may result in additional reporting costs for certain administrators, particularly small providers of benchmarks, which could have been avoided.

Overall, as with the compliance statement, we find that the template that ESMA specifies should impose no material costs on administrators, in addition to those already incurred as a result of the Level 1 BMR Regulation. That said, there are expected to be one-off costs associated with the repapering of existing agreements with contributors, as discussed in more detail above. The time involved in this repapering is expected to be fairly minor, involving total of 5–10 man days across both the administrator and contributor for each affected benchmark. The regulation on benchmark statements applies to all critical, commodity and interest rate benchmarks, of which there are approximately 100. Taking the above estimates, with the additional estimate that there are, on average, 5–10 contributors per benchmark, implies that

10 Although an indication of the size of the market is optional for the purpose of the definition of the market or economic reality measured by the benchmark, an approximation of the size of the market is mandatory for the purpose of defining the circumstances in which the measurement of the relevant market or economic reality may become unreliable. See Article 1 on disclosure requirements of the benchmark statement RTS.

11 Contributors may be reluctant to provide data to benchmark administrators so as to avoid disclosing sensitive commercial data or information which could damage them. See for example European Commission (2013) “Impact assessment accompanying the document Proposal for a Regulation of the European Parliament and of the Council on indices used as benchmarks in financial instruments and financial contracts”.


13 In our stakeholder engagement, indicative attestation and audit costs of £20,000–£50,000 were identified.
administrators and contributors would jointly incur a total cost associated with repapering agreements in the region of €1.3–€5.3 million.

Benefits
Overall, the key objective of the benchmark statement RTS is to increase transparency in the benchmarks landscape and heighten user caution, thus improving regulatory oversight and increasing user confidence. The RTS contributes towards securing these benefits by increasing:

- the clarity of the documents published; and
- the comparability of benchmark statements produced by different administrators.

Users of benchmarks will likely benefit most, as they would be provided with information on what a given benchmark intends to measure and its susceptibility to manipulation. This should facilitate user understanding of the risk profiles of different benchmarks and the selection of the most appropriate benchmark, among alternative ones.

Administrators are also likely to benefit from the RTS. More specifically, there could be less room for errors in the application of the requirement and less scope for legal uncertainty.

4.9 Authorisation and registration of administrator

4.9.1 What does the Benchmarks Regulation say?

The Benchmarks Regulation requires that an administrator must apply for authorisation to provide benchmarks if they are used, or intended to be used, to reference financial instruments, financial contracts or the performance of an investment fund. Registration is required for those administrators that are supervised entities providing significant or non-significant benchmarks, as well as for those administrators that are non-supervised entities providing non-significant benchmarks.

Article 34 of the Benchmarks Regulation also stipulates the authorisation to the relevant competent authority of a natural or legal person in the EU who intends to act as an administrator.

Article 34 further specifies that administrators of non-significant benchmarks and persons who are supervised entities are to be registered by the relevant competent authority. Supervised entities are only eligible for registration if:

- the legal framework concerning the entity does not prevent it acting as an administrator; and
- the entity does not plan to act as an administrator of critical benchmarks.

For both authorisation and registration, the regulation requires the applicant to provide all information needed by the relevant competent authority to conclude that the administrator has in place necessary arrangements to meet the requirements of the Benchmarks Regulation.

The regulation also states, however, that authorisation is to provide a more extensive assessment of the administrator application than registration. Administrators of non-significant benchmarks are subject to this less extensive assessment due to the nature of benchmarks they cover, while supervised entities qualify for registration as the relevant competent authorities are already aware of, and supervise, their activities.

Article 34 of the Benchmarks Regulation specifies the following.

ESMA shall develop draft Regulatory Technical Standards to further specify information to be provided in the application for authorisation and in the application for registration, taking into account that authorisation and registration are distinct processes where authorisation requires a more extensive assessment of the
administrator’s application, the principle of proportionality, the nature of the supervised entities applying for registration under paragraph 1(iii) and the costs to the applicants and competent authorities.

ESMA’s role is, therefore, to set out in detail the information that should be contained within applications for authorisation and registration, again taking into account the conditioning factors in the quote above.

4.9.2 What do the ESMA draft Technical Standards say?

ESMA’s RTS set out specific requirements on the information to be provided in authorisation applications in nine key areas. We set these out in turn below.

- **General information** — this includes details of name, address, legal status and contact details of a relevant contact person. It should also include details of the operations of the applicant in the EU that are potentially relevant for the activity of provision of benchmarks, including where these activities are conducted. Where the applicant is a supervised entity, it should include information about its current authorisation status, including the primary business for which it is authorised and its relevant competent authority in its home Member State. It should also include any deed of incorporation, articles of association or other constitutional documents. Where the applicant is part of a group, it should detail its group structure and provide an ownership chart showing the links between the parent undertaking and subsidiaries. Finally, applicants should include a self-declaration of good repute with details of any disciplinary proceedings, and any refusal or withdrawal of authorisation or registration by a financial authority.

- **Financial information** — this includes information on the applicant’s ownership structure, including shareholders and their holdings. Applicants must submit financial statements for the most recent three years, or if the applicant has not yet produced financial statements, a description of how it plans to raise financial resources, including a business plan, for the first three accounting years. It should also include forecasting information for at least one year ahead. In the case of supervised entities, information on the applicant’s compliance with its capital requirements should also be provided.

- **Organisational structure and governance** — this requires details of the internal organisation structure including the board of directors, senior management committees, oversight function and any other internal bodies with significant management functions. For members of the senior management, applicants are to provide CVs, a recent criminal record file, a self-declaration of good repute and details on their other activities within and outside the applicant. Applicants must also specify the number of employees along with senior managers per function/department, as well as the number of employees involved specifically in benchmark activities.

- **Conflicts of interest** — applicants are to provide details on: (i) how conflicts of interest which have the potential to arise will be identified, recorded, managed, mitigated, prevented, disclosed and remedied; (ii) the controls in place including any other parts of the conflicts of interest management framework; and (iii) particular circumstances in which conflicts could most likely arise. For each critical benchmark, applicants must provide an up-to-date log of actual and potential conflicts of interest and mitigative measures. Applicants must also provide the remuneration policy, which shall include details of the criteria used to determine the remuneration of those involved in benchmark provision.

- **Internal control structure, oversight and accountability framework** — applicants will be required to submit details on the policies and procedures for monitoring the activities of benchmark provision including those associated with: IT systems and controls; incident and risk management; adherence to code of conduct; the constitution, role and functioning of the oversight function and control framework; and the accountability framework. The applicant must all provide details on fall-back systems and arrangements and procedures for internal reporting of infringements.
• **Description of benchmarks provided** — applicants must include a description of benchmarks provided or those intended to be provided, including their type, categories and a description of the underlying market or economic reality (as well as an indication of the sources used to provide each of these information); a description of the contributors (and for critical benchmarks their identity); the measures to deal with corrections; the actions to be taken in the event of changes to, or cessation of, the benchmark; and information on the means of publication of a benchmark’s determinations. There are also specific additional requirements for interest-rate and commodity benchmarks, to demonstrate their compliance with Annex I and Annex II of Regulation No 2016/2011 respectively.

• **Input data and methodology** — applicants should include, with respect to input data: the description of the type of input data used, the priority of used and exercise of expert judgement; processes for ensuring input data is appropriate, verifiable and sufficient to represent the underlying market or economic reality; and processes for selecting and evaluating contributors and the input data they provide. With respect to the methodology, applicants should provide: a description; the measures to provide validation and review; and a description of the consultation process on any proposed material change in methodology.

• **Outsourcing** — for any activity relating to benchmark provision that is outsourced, applicants would need to include: the identity of the service provider; details of outsourced functions; the relevant contracts which demonstrate oversight; and policy and procedures regarding the oversight of the outsourced activities.

• **Others** — this is any additional information that the applicant deems relevant to its application, and shall provide requisite information in a manner and form determined by the competent authority.

For registration applications, ESMA’s RTS make certain omissions from the list above. The extent of omissions depends on the type of benchmarks provided. For supervised and non-supervised entities providing only non-significant benchmarks, the omissions are more significant. These administrators are, for example, only required to provide a synthetic description of the ‘conflicts of interest’ and ‘internal control structure, oversight and accountability framework’, rather than precise details on each of the requirements, as in the case of the application for authorisation. There are only a limited number of omissions for supervised entities who provide at least one significant benchmark and supervised entities providing only commodity benchmarks. In the cases where the applicant is a natural person, there are some omissions to the general and financial information requirements.

ESMA stipulates that the applicant may provide information at the level of a family of benchmarks, provided the benchmarks in question comply with the definition set out in Article 3(1)(4) of Regulation No 2016/1011 and provided none of the benchmarks in question are critical.

The applicant is also required to provide an explanation, as part of the application, for any requirement of the regulation that is not applicable to the applicant or to the benchmarks it provides.
4.9.3 Expected impacts

**Figure 4.9: Expected impacts of the RTS on Authorisation and Registration of an Administrator**

<table>
<thead>
<tr>
<th>Goals</th>
<th>Topics</th>
<th>Affected stakeholders</th>
<th>Costs</th>
<th>Benefits</th>
</tr>
</thead>
<tbody>
<tr>
<td>Improve the reliability, integrity and quality of benchmarks</td>
<td>General information</td>
<td>Administrators</td>
<td>One-off: Human resource costs in producing additional documentation and reporting, including compliance staff and potentially other departments. Investment in secure ways of storing and sending commercially sensitive information.</td>
<td>More material costs for administrators of critical benchmarks, e.g. due to the requirement to provide an inventory of conflicts of interest, and because information cannot be submitted for families of benchmarks in cases where one, or more, of the benchmarks are critical.</td>
</tr>
<tr>
<td></td>
<td>Financial information</td>
<td></td>
<td>However, where there is a duplication of requirements across RTS, e.g. between this application and the compliance statement, then the information need not be provided again in this application to reduce the costs of duplicating such work.</td>
<td></td>
</tr>
<tr>
<td></td>
<td>Organisational structure and governance</td>
<td>Administrators</td>
<td>Less material compliance costs for administrators of non-significant benchmarks and administrators who are already supervised entities, as they are only required to apply for registration, which contains certain omissions and is less granular than the application for authorisation.</td>
<td>Due to the increased oversight of competent authorities, administrators may experience beneficial behavioural change, in the form of more internal monitoring and accountability.</td>
</tr>
<tr>
<td></td>
<td>Conflicts of interest</td>
<td>Administrators</td>
<td>Proportionality is maintained by imposing reduced requirements on those applying for registration, particularly if they only provide non-significant benchmarks. This will not only reduce burden on administrators but also on competent authorities having to collect and process this information.</td>
<td></td>
</tr>
<tr>
<td></td>
<td>Internal control structure, oversight and accountability framework</td>
<td>Competent authorities</td>
<td>One-off: Human resource costs in processing the incoming information from administrators and following up with them where there are gaps in the information provided. Investment in secure ways of receiving and storing commercially sensitive information from administrators.</td>
<td>The common application process across administrators should make processing applications more cost efficient.</td>
</tr>
<tr>
<td></td>
<td>Description of benchmarks provided</td>
<td>Competent authorities</td>
<td></td>
<td>More robust oversight of administrators and a more consistent approach across the EU’s national competent authorities. Due to the greater accountability and transparency, authorities will be able to more readily assess the sufficiency of administrators’ policies and procedures for benchmark provision, help identify conflicts of interest before they materialise and speed up investigatory processes were they to arise.</td>
</tr>
<tr>
<td></td>
<td>Input data and methodology</td>
<td>Users</td>
<td></td>
<td>Common authorisation and registration throughout the EU will improve the integrity of benchmarks amongst users, as users will know that any benchmark provided by an authorised or registered administrator anywhere in the EU have met those same standards. This could lead to benchmark users increasingly looking to benchmarks produced by administrators outside their own national jurisdictions, thus improving market competition.</td>
</tr>
</tbody>
</table>

Source: Europe Economics.
Costs

The RTS are likely to impose one-off compliance costs in the form of additional documentation and reporting costs on benchmark administrators. This will require staff resources, largely from the compliance team, in order to compile the relevant information for the application. In many cases, e.g. names, addresses and CVs, this information is likely to already be stored by the administrator and thus it would simply be a case of a small amount of staff resourcing to compile the relevant information together for submission. However, other reporting requirements could prove more onerous, requiring drafting of new documentation. In cases where new drafting of documentation is required, staff resourcing requirements are likely to be more material, especially as this may require staff from a number of different departments, including finance, legal, compliance and IT, liaising with each other in producing finalised versions of required documentation.

Given that the additional information requirements include data which may be deemed commercially sensitive (e.g. input data and methodologies), administrators and the relevant national competent authorities may need to invest in secure ways of sending, storing and receiving this information. National competent authorities would also incur staff resource costs in processing all the additional incoming information and following up with administrators where there are gaps in the information provided.

Compliance costs could, however, be limited by the fact that information can be submitted for families of benchmarks provided the benchmarks meet the applicable definition in the regulation and provided none of the benchmarks are critical. This could lead to economies of scale for administrators who produce several benchmarks in the same family, thus reducing the costs of compliance per benchmark it administrates. Compliance costs are also limited by the fact that, where there is duplication of information requirements across RTS, e.g. between the application for authorisation/registration and the compliance statement, the information can be provided to satisfy both requirements in order to reduce the duplication of costs.

The key drivers of existing practices, according to the survey respondents, are the IOSCO principles and the existing regulatory practices (including regulation at the national level, where applicable) — although a minority of administrators in our fieldwork had done work in anticipation of the BMR coming into practice as guiding their existing practices. Administrator noted that authorisation under national level regulation had been costly and, therefore, advocated the use of a grandfathering approach for those already authorised under a national level regulation.

In terms of the types of costs incurred in becoming compliant the evidence was mixed. On balance, administrators saw the systems and controls costs to be a more major cost driver than human resource costs, with respondents indicating either minor or major changes with regard to the former. In terms of human resource costs, the majority of respondents said that no, or only minor, changes would be required to ensure compliance.

The above compliance costs would be less material for certain types of firm that provide or intend to provide indexes for use as benchmarks. This includes administrators of non-significant benchmarks and also those market participants who are already supervised entities (but are not administrators) and that do not plan to publish indexes that would be used as critical benchmarks. The latter group are only required to apply for registration, in accordance of BMR Article 34(1)(b), the application for which is shorter and less detailed than the application for authorisation. The compliance costs would also be slightly less material for natural persons, due to the exclusion of certain information requirements. That said, although the RTS are likely to be less material in pure monetary terms for these types of administrator participant, the RTS may nevertheless lead to relatively more incremental cost for them (e.g. as a proportion of total benchmark operating costs). Application costs are also likely to be more material for administrators of critical benchmarks, e.g. due to the need to provide an inventory of actual and potential conflicts of interest, in contrast to significant and non-significant benchmarks where only the conflicts of interest most likely to arise are included.
Overall, a key assumption is the division of administrators between those who will require authorisation and those that can opt for the registration process (e.g. those administrators with an existing authorisation, such as with the UK’s FCA). As we note at 3.1.2, the current evidence base for critical and significant benchmarks is extremely weak. We assume that the majority of participants would be able to register, and that perhaps only 10–15 would require the authorisation process. If a typical participant would need to spend 1–2 months on the registration process but 1.5–3 months on authorisation then we estimate the incremental one-off impact due to these Technical Standards on administrators at €0.7–€2.0 million. Ongoing incremental costs should be negligible.

A further corollary of this would be raised barriers to entry to administration activity. This, in conjunction with the impact of the other Technical Standards / the BMR itself raising the cost of undertaking benchmark administration activity, is likely to reduce the pace of innovation and also drive consolidation — i.e. in the future there would be fewer administrators (and potentially fewer benchmarks). This would be further compounded by concerns amongst non-specialist administrators at the potential regulatory risk of this activity. A more concentrated benchmark market could also impact on the pricing of benchmark access.

Benefits

In terms of benefits, the applications for registration and authorisation should help in ensuring more robust oversight of benchmark administrators and a more consistent approach across the EU. Without the granularity of requirements set out in ESMA’s RTS, national competent authorities could adopt very disparate information requirements which would hinder benefits associated with greater consistency. Of course, it is very difficult to untangle the extent to which any such benefit would be attributable to the Benchmarks Regulation, on the one hand, and ESMA’s RTS, on the other. Rather, ESMA’s RTS should help increase the likelihood of the Benchmarks Regulation’s intended benefits being delivered.

The additional information should help national competent authorities to evaluate the sufficiency of administrators’ policies and procedures relating to benchmark provision. The information could help competent authorities to identify potential areas for conflicts of interest before they materialise and should serve to speed up any investigatory processes were they to arise, as the competent authorities would already have a significant amount of relevant information with which to conduct the investigation.

Documentation of procedures, systems and resourcing structures should also help to improve accountability and transparency within the administrator. The RTS also provide clear indication upfront of the information that is required as part of the application, and thereby limit the scope for interpretation and ultimately the additional costs this can entail. In addition, the very fact that administrators are required to submit this various information about internal policies, procedures and so forth could help to incentivise beneficial behavioural change, by means of encouraging more thorough internal monitoring and accountability. The inclusion of remuneration policies, for example, should help ensure that there is no link between the remuneration a person receives and the level of the benchmark provided.

These changes should ultimately promote higher quality and more robust benchmarks and thus improve the integrity of benchmarks amongst users, as users would know that benchmarks provided by an authorised or registered administrator anywhere in the EU have met these same application requirements. This could in turn encourage users to increasingly look at the benchmarks produced by administrators outside their own jurisdictions, thus improving market competition. Survey evidence was highly mixed on the extent to which these Technical Standards would improve market confidence, with equal proportions of respondents indicating ‘no effect’ and ‘significant effect’. That said, no respondents indicated that there would be any significant increase in competition between benchmarks as a result of this regulation, with increased competition ranking lowest among the suggested benefits, and one respondent even suggesting that competition would decline (although not specifying a reason for this). Moreover, it was suggested that the BMR is the strictest regulation so far when considered globally, and that this could have detrimental
impact on EU benchmark administrators who are competing with non-EU benchmark administrators on a global scale.

The RTS also maintain a degree of proportionality, by imposing reduced requirements on those applying for registration, particularly if they only provide non-significant benchmarks. Not only will this not overly burden the administrators of these benchmarks, but it also ensures that national competent authorities are not overly burdened with information from these administrators, and thus can concentrate more resources on the applications received from administrators of significant and/or critical benchmarks.

4.10 Recognition of an administrator located in a third country

4.10.1 What does the Benchmarks Regulation say?

An administrator located in a third country, intending to obtain prior recognition, should apply for recognition to the competent authority of the reference Member State. The administrator should provide all information necessary to prove that it has established all the necessary arrangements to meet the requirements of the Directive (excluding Article 11(4) and Articles 16, 20, 21 and 23) and should provide the list of its actual and prospective benchmarks which may be used in the EU. The administrator should also, where applicable, indicate the competent authority responsible for its supervision in the third country.

Within 90 working days of receipt of the application, the competent authority should verify that the necessary conditions are fulfilled.

ESMA has been charged with developing draft RTS to determine the form and content of the application for recognition and the presentation of the information.

4.10.2 What do the ESMA draft Technical Standards say?

General requirements

An application of recognition should be addressed to the competent authority of the reference Member State. The applicant should provide information that covers, but may not be limited to, the following items (as specified in Annex I of the RTS).

Section A — Information on the providing person and its legal representative in the EU

- **General information**: full name, address, legal status, website, authorisation status and the name and address of the competent authority of the third country (where applicable), description of the operations of the applicant in the EEA and/or third countries that are relevant for benchmark provision, its group structure (where applicable) and a self-declaration of good repute (e.g. proceedings of disciplinary nature, refusal for authorisation/registration from a financial authority, withdrawal of authorisation/registration from a financial authority);

- **Legal representative in the Member State of reference**: evidence for the choice of the Member State of reference, and information regarding the legal representative (including its name, title or legal status, constitutional documents and a clarification on whether it is supervised, address, e-mail address, telephone number, written confirmation of the authority of the legal representative to act on behalf of the applicant, details of the involvement of the legal representative in the oversight function relating to the provision of benchmarks that may be used in the EU, contact details of the legal representative);

- **Financial information**: the applicant ownership structure (shareholders and their holdings), financial statements (balance sheet, income statement, cash flow and audit reports for the three most recent years) or (if the applicant has not yet produced financial statements) a description of how the applicant plans to raise financial resources, and financial forecasts for at least one year ahead;
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- **Organisational structure and governance:** internal organisation structure (number of members, terms of reference and adherence to any governance codes) with respect to board of directors, senior management committees, oversight function and any other significant management functions.
  - With respect to the members of senior management:
    - curriculum vitae,
    - a recent criminal record file,
    - a self-declaration of good repute,
    - detail on their other activities within and outside the applicant (or the group of which the applicant is part).
  - With respect to the resource:
    - the number of employees per function/department,
    - the number of employees involved in the benchmark activities.

- **Conflicts of interest:** policies and procedures (how conflicts of interest are identified, recorded, managed, mitigated, prevented and remedied; the controls put in place; particular circumstances in which the conflicts could most likely arise), and the structure of the remuneration policy;

- **Internal control structure, oversight and accountability framework:** policies and procedures for monitoring the activities of the provision of a benchmark (including IT systems and controls, incident management, risk management, checking and monitoring contributors’ adherence to the code of conduct, oversight function, control framework, accountability framework), fall-back systems and arrangements, and procedures for the internal reporting of infringements of the Directive.

- **Input data and methodology**
  - With respect to input data
    - a description of the type of input data used, their priority of use and the exercise of expert judgement,
    - the process for ensuring appropriateness and verifiability of the data,
    - an explanation of how the applicant is satisfied that there is sufficient input data to represent the market or economic reality the benchmark is intended to measure,
    - the selection and evaluation process of the contributors,
    - the evaluation of the contributor’s input data and process of data validation.
  - With respect to methodology
    - a description of the methodology,
    - the measures taken to validate and review the methodology (including any trials and back-testing),
    - a description of the consultation process on any proposed material methodological changes.

- **Outsourcing:** the identity of the service provider, details of the outsourced functions, the relevant contracts demonstrating compliance with the relevant article of the Directive or IOSCO Principles, policy and procedures regarding the oversight of the outsources activities;

- **Others:**
  - any additional information which is relevant to the application,
  - the information should be provided in the manner and form requested by the competent authority.

**Section B — Information on the benchmarks provided**

- **Description of the actual or prospective benchmarks (or the families of benchmarks) that may be used in the EU:**
  - a description of the benchmarks which are already provided in the EU,
  - a description of the benchmarks that are intended to be marketed in the EU,
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- a description of the underlying market or economic reality the benchmarks are intended to measure,
- a description of the contributors to each benchmark,
- evidence that a benchmark may be considered regulated-data benchmark,
- evidence that a benchmark may be considered commodity benchmark, and that it is not based on submissions by contributors the majority of which are supervised entities, along with evidence of the implementation of the special regime requirements,
- evidence that a benchmark may be considered interest-rate benchmark, along with evidence of the implementation of the special regime requirements,
- evidence on the qualification of the benchmark as either a significant or non-significant,
- the rationale behind the application of any of the exemptions (presented to the extent possible in the format established in the ESMA’s RTS related to the compliance statement),
- information on measures to deal with corrections to a benchmark determination or publication,
- information on the procedures and actions to be taken if the benchmark is changed or discontinued,
- information on the means of publication in the EU of a benchmark’s determination there are used or intended to be used.

The application should include an explanation of any requirements of the Directive that do not apply to an applicant or its benchmarks that are intended for use in the EU.

The applicant should not be required to provide the information specified above (Annex I of the RTS) to the extent that an independent auditor or the competent authority of the third country where the applicant is located has verified this information as part of the IOSCO Principles compliance assessment.

Format of the application

An application and all connected documents and information should be submitted in English or in the official language of the Member State of reference. Conditionally on the agreement between the applicant and the Member State of reference, an application and all connected documents and information may be submitted in another language.

An application should be submitted in paper form or (if accepted by the relevant authority) by electronic means. Those electronic means should ensure completeness, integrity and confidentiality of the information during the transmission.

An application should give a unique reference number to each document it submits. The applicant should ensure that each document specifies to which requirement of the Directive it refers.

Policies and procedures

Policies and procedures established for fulfilling the requirements of the Directive should contain or be accompanied by:

- An indication of who is responsible for the approval and maintenance of the policies and procedures.
- A description of how compliance with the policies and procedures is enforced and monitored, as well as who is responsible for this.
- A description of the measures to be undertaken in the event of a breach of the policies and procedures.
4.10.3 Expected impacts

**Figure 4.10: Expected impacts of the RTS on Third Country Recognition**

**Compliance costs**

Several elements of the requirements may be more onerous for small third-country administrators. Specifically, during the application process, third-country administrators would need to indicate the nature and characteristics of the benchmarks provided, as well as of the relevant underlying market or economic reality. This requirement implies the likely exposure of third-country administrators to the costs involved in the development of the benchmark statement (see section 4.8.3).

A critical assumption here is the number of non-EU administrators that would be expected to seek this route. This is complicated by the potential for additional cost burdens and regulatory risk to deter some current benchmark providers from continuing with serving the EU market. We take a broad range of 20–50 such administrators as at least providing some plausible parameters on this. We would expect the process for an individual non-EU administrator to sit somewhere between that of registration and authorisation described above at 4.9.3. On this basis, we estimate the incremental one-off cost imposed on non-EU administrators due to these Technical Standards at €0.3–€1.3 million. Ongoing incremental costs are likely non-negligible. There is a substantive ongoing information-provision requirement to fulfil by non-EU administrators, estimated at €0.2–0.8 million.
Indirect costs and market impacts

In case the costs of obtaining recognition in the EU are considerable, small third-country benchmark providers may choose not to apply for recognition in Europe in the first place. This was seen as a material risk by various market participants, specifically with respect to Asia-based market participants.

An indirect cost that may arise in this respect is the opportunity cost of sub-optimal investment behaviour. More specifically, a reduction in the number of benchmarks available in Europe limits the available instruments that can be used to diversify a given portfolio, thus exposing investors to the opportunity cost of being poorly diversified.14

Users that provide financial products in Europe referencing such benchmarks could be particularly harmed if the administrators remove them from the market. This would expose the designer of the financial instrument referencing the benchmark in question to additional costs (i.e. desk research, data collection, verification checks) involved in altering the product so as to include a new, and possibly inferior benchmark. In the latter case, the end-user would not only face potentially higher costs, but obtain inferior use (e.g. risks could be less well hedged).

Benefits

Overall, the proposed requirements for the recognition of third country administrators and benchmarks aims to build a European supervisory culture that ensures consistent approaches across NCAs. In this case, NCAs would possess a pre-defined well-structured framework, based on which they should more easily and rapidly be able to conduct their assessments. Such an outcome is also likely to limit legal uncertainty as well as incentives to engage in forum shopping by providers.

In addition, the requirements should ensure that an EU administrator does not avoid application of the BMR by providing the benchmark in a third country under more lenient regulatory provisions. Rather, the current BMR requirements provide an incentive to third country administrators to abide, at least at a minimum, to the IOSCO principles, thus increasing investor protection. This incremental benefit would only apply to benchmarks originating from countries that have not yet ratified — and applied — the IOSCO Principles.

An additional benefit is the externality (in terms of enhanced protection) for investors and consumers in other countries as the benchmarks provided both in the EU and recognised third-country administrators would be scrutinised on the basis of a consistent information set.

Appendix
Appendix: Methodology and Fieldwork

5.1 Overview of approach

As explained at the start of Chapter 4, this cost-benefit analysis was undertaken as a two stage process. The first stage made use of desk-based research, as well as responses to the EC’s consultation on the BMR and to ESMA’s discussion paper on the draft Technical Standards, in order to map out the economic logic connecting the Technical Standards to different expected costs and benefits. The second stage then involved analysing, both qualitatively and quantitatively, the findings of the stakeholder engagement programme, to determine to what extent stakeholder evidence supports and/or contradicts the expected costs and benefits set out in the first stage of the analysis. This appendix describes the stakeholder engagement programme undertaken.

5.2 Stakeholder engagement programme

As set out in our proposal, we need data to refine the qualitative cost analysis and to provide the information and parameters to populate our cost models (described below) and generally to provide a quantification of the cost analysis — this would be primary data-gathering, bespoke for this study.

In particular, we proposed to undertake a series of structured interviews with administrators, contributors, and users, and this would be supplemented by a focused surveys to broaden the reach of the stakeholder engagement on particular topics.

5.2.1 Interviews and survey

We contacted relevant stakeholders with a view to setting up interviews to take place in October–December, i.e. to allow for participants to digest the contents of ESMA’s published consultation on the draft Technical Standards, which is due out at the end of September.

We also contacted industry associations to access their overall views on the BMR, and specifically ESMA’s draft Technical Standards, and also to distribute the online version of the questionnaire to their members to generate further responses for use in our analysis. The template for this will be the same as that sent to interview participants ahead of interviews. (However, additional questions may be asked in the interviews, in addition to the opportunity to drill down and challenge any answers obtained).

We had originally proposed to target: five-seven benchmark administrators, six-seven benchmark contributors, and six-seven benchmark users, i.e. 17–21 interviewees. We have conducted fifteen interviews, i.e. short of this target. However, various participants were ‘hybrids’, i.e. they are complex organisations with business units that qualified as more than one of the categories identified in the BMR. Not all such hybrids contributed across all relevant categories (e.g. a large bank could qualify as an administrator, contributor and user — but focused only on the impacts on one or two of these). Overall we accessed the views of eight administrators, eight users and four contributors. Geographically, these came from Estonia, France, Germany, Ireland, Italy, Luxembourg and the UK.
5.3 Modelling

The results of the fieldwork were combined with our pre-existing qualitative analysis of the mechanisms of effect and our desk-top research to produce quantitative estimates of compliance estimates and to assess any wider impacts (such as indirect, market effects) and any benefits. This is described in more detail in the sections relating to the individual Technical Standards.