

Benchmark Regulation and its Impact on Funds

Introduction

In June 2016, the EU published the Benchmark Regulation (the “Regulation”) as a reaction to allegations of manipulation of LIBOR, EURIBOR and other benchmarks. The aim of the Regulation is to reduce the risk of manipulation of benchmarks, reduce the use of discretion in the benchmark-setting process and to govern the provision of, contribution to and use of benchmarks.

The Regulation applies from 1 January 2018 but there are transitional arrangements meaning that certain elements of the Regulation apply later.

What is a Benchmark?

A benchmark is an index that is used for specific purposes such as:

- To determine the amount payable under a financial instrument or a financial contract or to determine the value of a financial instrument.
- To measure the performance of an investment fund with the purpose of tracking the return of an index.
- To define the asset allocation of a portfolio.
- To compute the performance fees payable by a fund.

Who is impacted by the Regulation?

The Regulation applies to the following:

- An entity providing the benchmark – the administrator. The administrator determines the benchmark, collects input data and analyses the data.
- An entity contributing input data to a benchmark – the contributor.
- An entity using a benchmark – the user. UCITS, UCITS management companies and AIFMs are users.

Impact on Users - UCITS, UCITS management companies and AIFMs

One of the key aspects of the Regulation is the new authorisation and supervision regime for administrators of benchmarks for which a final deadline of 1 January 2020 applies. Users will need to ensure the benchmark is provided by an administrator which is authorised and registered within the EU by ESMA. For non-EU administrators, certain equivalence and recognition procedures need to be complied with.

Another key obligation is the need for users to draft and maintain a “robust written” contingency plan which outlines a course of action in case the benchmark materially changes or ceases to be provided. This applies from 1 January 2018 and the contingency arrangements should be included in contracts with clients. ESMA issued a Q&A in September 2018 in which it provided guidance on what it considers to be robust written contingency plans.

A third obligation specifically targets UCITS not AIFs. UCITS will need to make disclosures in their prospectuses about whether the administrators of the benchmarks used are listed in the register of administrators and benchmarks maintained by ESMA. This update to the prospectus has to be made at the latest by 1 January 2019. The name of the benchmark administrator is not required to be disclosed.

KB Associates’ Services

KB Associates offers a range of services to investment funds and management companies including:

- The provision of UCITS/AIF management company services.
- The provision of designated persons to perform UCITS business plan and AIFMD programme of activity managerial functions.

If you would like to discuss any issues raised in this article or related to KB Associates’ services in general, please feel free to contact Mike Kirby (+353 1 667 1980), Peter Northcott (+44 203 170 8813) or Mike Parton (+1 345 946 4224).