

Upcoming EU interbank offered rates (€IBORs) transition



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The European Central Bank's ("ECB") working group on euro risk-free rates published earlier this week its final recommendations regarding the EONIA to €STR Legal Action Plan subsequent to the third public consultation issued in this respect. The EONIA to €STR Action Plan covers legacy and new agreements referencing EONIA in different contexts (in particular derivative transactions, collateral agreements and cash products) and was developed by the ECB working group in coordination with some of the major market participants. The main aim of the Action Plan and the related communications made by the ECB is to support the market in the implementation of the transition away from EONIA. As such, application of any of the ECB's 33 recommendations is at the full discretion of market participants.

The key recommendations are as follows:

- as from 2 October 2019, avoiding entering into any new contracts referencing EONIA, in particular where these contracts have a maturity date after 31 December 2021;
- for legacy contracts maturing after 31 December 2021 and referencing EONIA, replacing EONIA as primary rate as soon as possible or ensuring the implementation of robust fallback clauses referring to a fallback rate;
- designating €STR plus a spread as the fallback rate to be chosen in replacement of EONIA, irrespective of the type of product or purpose involved.

This ECB initiative took place as part of a broader shift in the EU IBORs framework, resulting in a global transition from the use of IBORs to the use of alternative benchmarks, mainly consisting of risk-free rates ("RFRs"). A large number of market participants have become accustomed to using IBORs for multiple financial products since the 1980s. Nevertheless, IBORs' vulnerability to misconducts and conflicts of interest has in particular been illustrated in the difficulties

encountered by the administrators of such benchmarks when facing the new requirements established by Regulation (EU) 2016/1011 of the European Parliament and of the Council of 8 June 2016 on indices used as benchmarks in financial instruments and financial contracts or to measure the performance of investment funds.

As a response to the challenges set-out by the new EU regulatory framework, a transition from some of the main IBORs to new benchmarks is under way. In this context, the following IBORs will evolve and/or be discontinued and replaced:

- as described above, EONIA will be replaced by €STR, a new benchmark to be issued by the ECB as from 2 October 2019;
- EURIBOR will be replaced by the HYBRID EURIBOR, still issued by the European Money Market Institute and in respect of which a transition is envisaged before the end of 2019;
- GBP LIBOR will be replaced by the Sterling Overnight Interbank Average Rate (SONIA), a benchmark already issued by the Bank of England and which should completely replace GBP LIBOR by the end of 2021 at the latest;
- USD LIBOR will be replaced by the Secured Overnight Financing Rate (SOFR), a benchmark issued by the Federal Reserve Bank of New York since 2 April 2018 and to which a transition is in progress and should again be completed by the end of 2021 at the latest.

Regulators and policymakers are currently focusing their efforts on a way to smoothen the transition from IBORs to RFRs or other alternatives, so as to minimise any market disruption or value transfer and ensure financial stability.

In light of the potential impact of such transition on the market, each stakeholder should closely monitor developments and take actions to already have a clear understanding of which of its products and/or transactions will be affected and what its transition plan will be.