

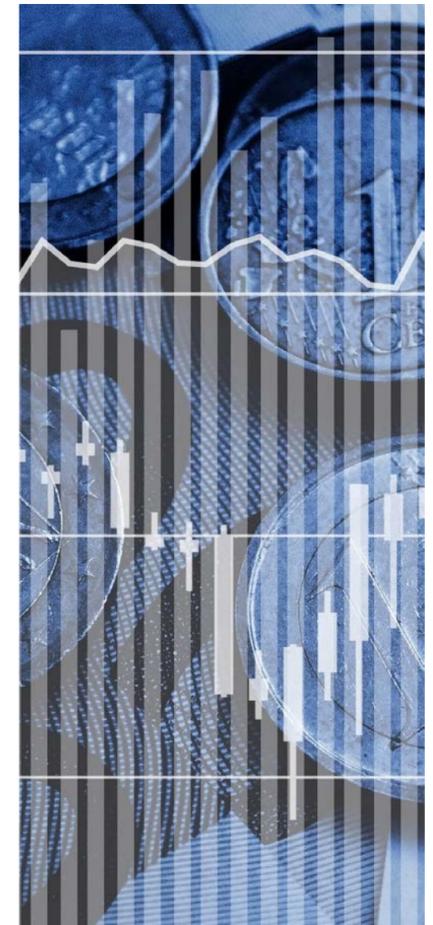
# EURIBOR fallback trigger events

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Chair of the subgroup on contractual robustness



# Background

**Why does the market need EURIBOR fallback provisions?**

# Critical benchmarks are undergoing significant reforms

- **Financial Stability Board recommendations on “[Reforming major interest rate benchmarks](#)”** in 2014:
  - strengthen existing benchmarks by underpinning them with transaction data to the greatest extent possible (EURIBOR in 2019);
  - develop alternative nearly risk-free reference rates (SOFR - NY FED, SONIA - Bank of England, and €STR - ECB) aimed at complementing/substituting existing interbank offered rates.
- These recommendations came in parallel to, or have resulted in the introduction of:
  - [IOSCO principles for financial benchmarks](#) in 2013 in terms of governance (administrators, third parties and oversight), quality of benchmark and methodology, and accountability.
  - [EU Benchmark Regulation \(BMR\)](#) in 2016 (came into force in January 2018). **The BMR requires that administrators of benchmarks such as EURIBOR be authorised or registered for supervised entities to continue using such benchmarks in contracts and financial instruments covered by BMR.**
- In addition, to cover for a scenario in which a benchmark permanently ceases or materially changes, **the BMR and IOSCO principles for financial benchmarks demand the introduction of robust fallbacks in contracts referencing financial benchmarks.**

# The need for a EURIBOR fallback provision

The BMR contains regulatory requirements in relation to fallback provisions

*The requirements for fallback provisions are laid out in BMR article 28(2)\**

Supervised entities are required to:

- **produce and maintain robust written plans** setting out the actions they would take in the event that a benchmark they are using materially changes or ceases to be provided. **This includes the nomination of alternative benchmark(s) that could be referenced to substitute the benchmark no longer provided, where feasible and appropriate;**
- **provide** their written plans, upon request, **to the relevant competent authority;**
- **reflect** the written plans **in their contractual relationships with clients.**

Robust fallback provisions reduce contract uncertainty and the risk of legal disputes in the event that the initially agreed upon benchmark rate is no longer available

\* ESMA has published a Q&A that provides guidance on the implementation of BMR article 28(2)

# Fallback provisions and their main elements

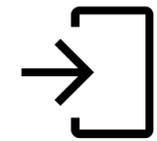
## What is a fallback provision?

- A fallback provision is contractual clause that determines what rate should apply to a relevant contract or financial instrument in the event that the initially agreed upon benchmark rate (such as EURIBOR) is not available.

 Without a fallback, contractual parties may be subject to legal uncertainty and disputes in relation to the execution of the contract due to the unavailability of the referenced benchmark rate.

## Key elements of a fallback provision:

- Fallback provisions are defined by three key elements which determine the application of, and the conditions applicable to, the provision:



Trigger event: defines events



Effective date: when the fallback rate will be applied on



Fallback rate: identifies the substitute reference rate



Spread adjustment: if the new fallback rate provides an economically different outcome to the original rate, a spread is included to avoid or minimise the transfer of value.

# Status of the EURIBOR reform

## What is the status of the EURIBOR reform?

- **EMMI has conducted an EURIBOR reforms over the last years to meet the BMR requirements by:**
  - strengthening its governance framework;
  - developing a hybrid methodology in order to ground the calculation of EURIBOR in euro money market transactions.
- **Authorization was granted on 2 July 2019** by the Financial Services Market Authority (FSMA) under BMR art. 34.
- This authorization **allows EU supervised entities to continue using EURIBOR.**
- Besides, BMR includes **precautionary measures and supervisory powers:** mandatory contribution, mandatory administration, requiring the administrator to change the methodology, etc.



**EURIBOR is not scheduled to be discontinued. However, EURIBOR fallback provisions are required in order to (1) provide legal certainty for a scenario in which the benchmark may permanently cease; and (2) comply with IOSCO principles and BMR article 28(2).**

# **Public consultation on EURIBOR fallback trigger events**

# Public consultation on EURIBOR fallback trigger events – objective/general considerations

## Objective

- **Identify a generic set of potential events that would trigger the activation of EURIBOR fallbacks** that market participants could consider including in their contracts and financial instruments referencing EURIBOR. Market participants are invited to provide feedback on the proposed EURIBOR fallback trigger events.

## General Considerations

- Trigger events should be drafted in **precise and objective terms**.
- Trigger events should be based on **events made public**.
- The **effectiveness date** should be:
  - ✓ The date of discontinuation, not the date of the public statement.
  - ✓ For the next period of interest.

# Public consultation on EURIBOR fallback trigger events – Scope / EU framework

## Scope

- Four main **considerations regarding the scope** of the public consultation on EURIBOR trigger events:
  - ✓ Covers all asset classes and proposes the use of the same trigger events for all to ensure as much consistency as possible
  - ✓ Covers the permanent discontinuation of EURIBOR, but does not cover any potential temporary unavailability of EURIBOR
  - ✓ Covers the permanent discontinuation of all EURIBOR tenors. The discontinuation of some tenors, but not all, is out of the scope of both consultations.
  - ✓ Acknowledges recommendations made by market associations (e.g. ISDA, LMA, AFME)

## EU legislative framework

- **The consultation paper is based on the current legislative framework in the EU.** It should be noted that on 24 July 2020, the European Commission published a proposal for a Regulation to amend the BMR including, among other topics, the designation of replacement benchmarks for certain benchmarks in cessation (LIBOR).

# Public consultation on EURIBOR fallback trigger events - proposals

#	Description of events	What	Who? Issuer		How? Decision			
		Public Statement	Supervisor	Admin	Cessation	Non-representative	Contingency	Illegality
1	A public statement or publication of information by or on behalf of the regulatory supervisor of the administrator of EURIBOR stating that the said administrator has ceased or will cease to provide EURIBOR permanently or indefinitely	✓	✓	—	✓	—	—	—
2	A public statement or publication of information by or on behalf of the administrator of EURIBOR stating that the said administrator has ceased or will cease to provide EURIBOR permanently or indefinitely	✓	—	✓	✓	—	—	—
3	A public statement by the supervisor of the EURIBOR administrator that, in its view, EURIBOR is no longer representative, or will no longer be representative	✓	✓	—	—	✓	—	—
4	The administrator of EURIBOR determines that EURIBOR should be calculated in accordance with its reduced submissions or other contingency or fallback policies	—	—	✓	—	—	✓	—
5	It has become, for any reason, unlawful under any applicable law and regulation for relevant parties to the agreement to use EURIBOR	—	—	—	—	—	—	✓
6	EURIBOR is permanently no longer published without a previous official announcement by the competent authority or the administrator	—	—	—	✓	—	—	—
7	Material change of EURIBOR methodology*	—	✓	✓	—	—	—	—

(\* ) Note that this event would not be understood as an automatic trigger event and, so it could cover either (i) an acknowledgment that EURIBOR may materially change and references to EURIBOR shall continue to be references to EURIBOR as changed; or ii) an option for parties to discuss whether to continue the contract with the materially changed EURIBOR or to fall back to the EURIBOR fallbacks included in the contract

# Public consultation on EURIBOR fallback trigger events – questions

#	Description of events	Question
1	<b>A public statement or publication of information by or on behalf of the regulatory supervisor of the administrator of EURIBOR</b> stating that the said administrator has ceased or will cease to provide EURIBOR permanently or indefinitely	Do you agree with the inclusion of “Event 1” as a trigger event in EURIBOR fallback provisions?
2	<b>A public statement or publication of information by or on behalf of the administrator of EURIBOR</b> stating that the said administrator has ceased or will cease to provide EURIBOR permanently or indefinitely	Do you agree with the inclusion of “Event 2” as a trigger event in EURIBOR fallback provisions? (yes / no / no opinion)
3	<b>A public statement by the supervisor of the EURIBOR administrator that, in its view, EURIBOR is no longer representative</b> , or will no longer be representative	Do you agree with the inclusion of “Event 3” as a trigger event in EURIBOR fallback provisions? (yes / no / no opinion)
4	The administrator of EURIBOR determines that EURIBOR should be calculated in accordance with its <b>reduced submissions or other contingency or fallback policies</b>	Do you agree with the proposal of <u>not</u> including “Event 4” as a trigger event in the EURIBOR fallback provisions? (yes / no / no opinion) Please elaborate.
5	It has become, for any reason, <b>unlawful</b> under any applicable law and regulation for relevant parties to the agreement to use EURIBOR	Do you agree with the inclusion of “Event 5” as a trigger event in EURIBOR fallback provisions? (yes / no / no opinion)
6	EURIBOR is <b>permanently no longer published</b> without a previous official announcement by the competent authority or the administrator	Do you agree with the inclusion of “Event 6” as a trigger event in EURIBOR fallback provisions? (yes / no / no opinion)
7	<b>Material change</b> of EURIBOR methodology	Do you agree that the inclusion of a material change in EURIBOR methodology (as defined by EMMI) should <u>not</u> result in an automatic trigger event and parties are free to agree when entering into the contract that either <b>(i) references in contracts to EURIBOR shall be understood to be references to EURIBOR as changed, or (ii) discuss between parties to continue the contract with the materially changed EURIBOR or to fall back to the EURIBOR fallback rates included in the contract?</b> (yes / no / no opinion)

# Q&A session

## Adolfo Fraguas

- BBVA
- Chair of the subgroup on contractual robustness

## Rick Sandilands

- International Swaps and Derivatives Association (ISDA)
- Member of the working group

## Kam Mahil

- Loan Market Association (LMA)
- Member of the working group

## Tilman Lueder

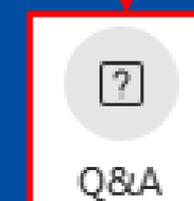
## Alessandra Atripaldi

- European Commission

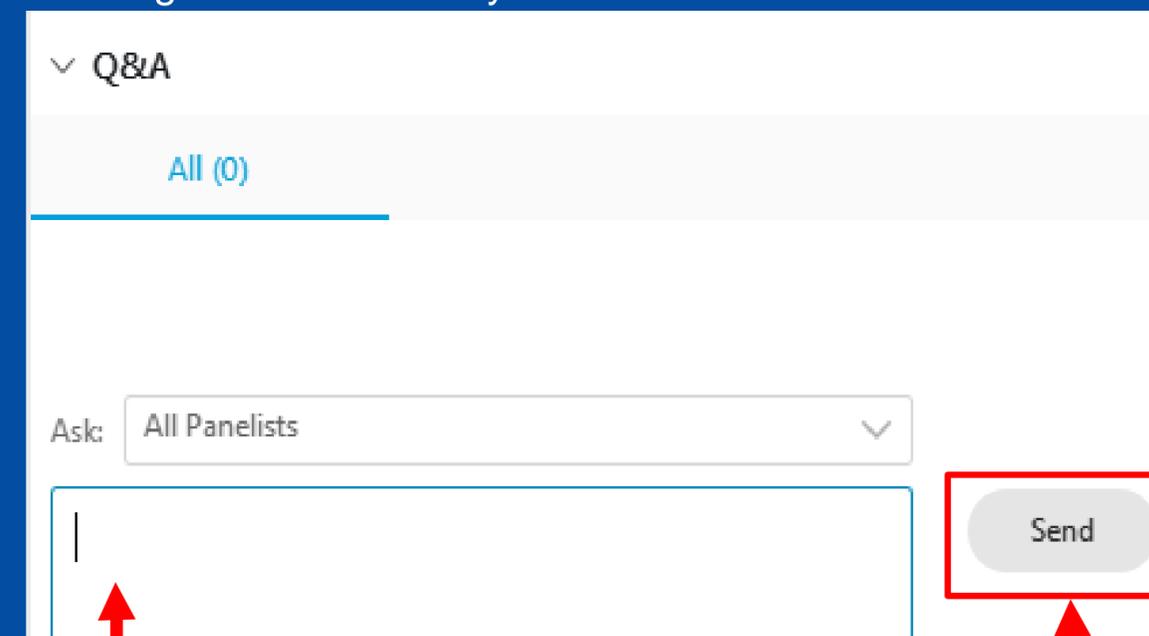
## Michele Mazzoni

- European Securities and Markets Authority (ESMA)

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send your question to:  
[Roundtable.EuroRFR@ecb.europa.eu](mailto:Roundtable.EuroRFR@ecb.europa.eu)

