



Meeting of the working group on euro risk-free rates

held in Frankfurt am Main on Friday, 10 May 2019, 9:00 to 13:00 CET

SUMMARY

1. Introductory remarks, approval of the agenda and obligations of working group members as regards competition law

Steven van Rijswijk (Chair) welcomed Generali to the working group on euro risk-free rates, as a new member with the status of an “invited institution”. Generali will co-chair subgroup 5 on cash and derivatives products and represent the buy-side in the respective discussions, in the person of Anna Kozhevnikova and her alternate, Bruno Servant.

Steven van Rijswijk (Chair) asked the members of the working group on euro risk-free rates to approve the agenda for the meeting and reminded them of their obligations under EU competition law, as described in the guidelines on compliance with EU competition law published on the ECB’s website.

2. Subgroup 3 to present the draft public consultation report on the EONIA legal action plan, including proposals for recommendations with regard to legacy and new contracts referencing EONIA

Adolfo Fraguas (BBVA) presented the draft public consultation prepared by subgroup 3 on contractual robustness. The draft had been submitted to the working group via written procedure and most of the comments of the working group members had been accommodated in the new version of the consultation.

The public consultation contains a set of draft recommendations to address the legal implications for new and legacy contracts referencing EONIA as a result of the proposed transition from EONIA to €STR. It is proposed that the working group recommends that new contracts referencing EONIA include robust fallback provisions and an acknowledgement that references to EONIA will be understood to be references to EONIA as modified after the change to its methodology on 2 October 2019. It is also proposed that the working group recommends that, after 2 October 2019, whenever operationally feasible, market participants should consider no longer entering into new contracts referencing EONIA, in particular new contracts maturing after 31 December 2021. For legacy contracts referencing EONIA and maturing after December 2021, market participants should consider replacing EONIA as a primary rate as soon as possible or embedding robust fallback clauses referencing the recommended fallback rate for EONIA. Additionally, the working group intends to recommend €STR plus a spread (the one-off computation of the difference between €STR and EONIA in the context of the proposed recalibrated EONIA methodology) as the EONIA fallback rate.

Some working group members expressed regret over the lack of legislative solutions originating from the public sector to support the transition from EONIA to €STR. The Chair recalled the working group’s understanding of the limitations of the public sector and asked the public authorities to reflect on possible ways to provide support. The public authorities participating in the working group on euro risk-free rates recalled the recent political agreement between the EU co-legislators to extend the BMR transitional period for critical benchmarks by two years and reiterated their willingness to support the private sector in other ways in finding solutions for a smooth transition from EONIA to €STR.

In reply to a question, **Randy Priem (FSMA)** indicated that the recalibration of the EONIA methodology was seen as a positive step towards the compliance of EONIA with the EU BMR requirements. He recalled, however, that the full assessment of EONIA’s compliance would have to be undertaken once the European Money Markets Institute (EMMI) files for authorisation for the EONIA benchmark. The FSMA also needs to consult the college of supervisors before its management committee can formally decide whether to grant the license or not.

Finally, **Alessandra Atripaldi (EU Commission)** shared some concerns that the consultation document could be seen as suggesting that it might be acceptable to continue referencing EONIA in new contracts entered into after €STR is published on 2 October 2019, as long as these contracts instead contain a fallback provision that addresses the discontinuation of EONIA at the end of 2021. The EU Commission indicated that, in its view, recourse to fallback provisions should be confined to situations where the use of EONIA is unavoidable and this

would hardly be the case for contracts concluded after 2 October 2019, given that market participants would be able to make direct reference to €STR. According to the EU Commission, the publication of the reformed EONIA after 2 October 2019 should be understood essentially as a service provided by EMMI for the duration of legacy contracts concluded before that date. In this regard, some working group members indicated that the transition from EONIA to €STR would probably be a gradual process after 2 October 2019, owing to the time needed for market participants to adapt their systems to the new benchmark.

3. Presentation of the reorganisation of Subgroup 2 on the term rates methodologies

3.1. Composition and approval updated Terms of Reference

David Gorans (BNP) presented the revised composition of subgroup 2 on term rates methodologies after a renewed call for interest in the context of the reorganisation of the working group.

Against this background, several working group members wondered about the policy addressing possible conflicts of interest, notably regarding upcoming work by subgroup 2B which is tasked with approaching administrators who would potentially publish €STR-based term rates. Subgroup 2 will liaise with the law firms participating in subgroup 3 on contractual robustness to ascertain whether they could advise on this competition law matter on a pro bono basis. On this basis, subgroup 2 would propose to the working group a procedure to address any possible conflicts of interest arising from the interactions with administrators who would potentially produce forward-looking term rates.

The working group endorsed the Terms of Reference of subgroup 2, which had been updated to reflect its new deliverables in the context of the reorganisation of the working group on euro risk-free rates. The new Terms of Reference will be published on the ECB's website. The new composition of subgroup 2 will be clarified in the light of the conflict of interest issues, before being published on the ECB's website.

3.2. Roadmap 2019

The governance of the reorganised subgroup 2 on term rates methodologies would remain broadly the same, with Dominique Le Masson (BNP) as Chair, and Alberto Covin (Unicredit), Carlos Infesta (Santander) and Neil McLeod (Erste) taking the lead of the new subgroups 2A and 2B. David Gorans (BNP) highlighted several linkages with the deliverables of subgroup 5 (with respect to the development of €STR-based derivative markets and with respect to the analysis of the use cases for forward and backward-looking methodologies as fallbacks for Euribor). A few working group members emphasised the need for international coordination with other currency areas on these deliverables.

3.3. Status update Subgroup 2A on overview of backward-looking methodologies and credit spread calculation methodologies

Subgroup 2A, led by Neil McLeod (Erste), would be tasked with the following deliverables: (i) analysing and making recommendations on how to deal with the spread difference between Euribor and an €STR-based term structure; and (ii) analysing possible backward-looking methodologies and conducting a technical analysis of their potential coexistence with the chosen forward-looking methodology. Both deliverables are expected to be completed ahead of the working group meeting scheduled in September 2019 and would serve as an input for the work of subgroup 5.

The working group discussed whether a public consultation would be necessary on the issue of the credit spread component, and, if so, whether this could or should be coordinated with other currency areas, with the support of the trade associations, such as the Loan Market Association. This would be dependent, in part, on the respective time frames. Subgroup 2A would first need to perform its initial analysis of the credit spread, taking into account the specificities of the euro area (notably usage in mortgages), before suggesting a way forward for subgroup 2 and the working group.

3.4. Status update Subgroup 2B on the way forward for the working group to support an administrator to publish €STR-based forward-looking term rates as possible Euribor fallbacks

Subgroup 2B, led by Alberto Covin (Unicredit) and Carlos Infesta (Santander), would be tasked with the following deliverables: (i) ensuring that a forward-looking term rate, based on the methodology recommended by the working group, can be calculated by an administrator on a daily basis (e.g. data collection/source), as a potential fallback for Euribor; and (ii) engaging with potential administrators of this new benchmark.

In the weeks to come, subgroup 2B would focus on the following priorities: (i) discussing with legal advisors from subgroup 3 on contract robustness the framework for the discussion with administrators, in order to avoid possible

conflicts of interest; (ii) launching a public call for information from interested administrators; and (iii) identifying Multilateral Trading Facilities (MTFs) and their characteristics. Once the interested administrators had been identified, subgroup 2B would try to understand their possible constraints in order to support them in the production of fallback rates for Euribor.

Cornelia Holthausen (ECB) cautioned that any call for information from benchmark administrators could be misunderstood if not placed in the broader context of the working group, and might be confusing as the use cases for forward-looking term rates were still to be analysed by subgroup 5, together with backward-looking methodologies. She argued that forward-looking rates should not be presented as “the only fallbacks for Euribor”, pointing to some recent misunderstandings by market participants of the results of the second public consultation on forward-looking term rates. In this context, a careful analysis and communication regarding the business cases for administrators to produce forward-looking term rates were necessary.

The working group clarified that the analysis of backward-looking methodologies, led by subgroup 2A, was aiming at supporting subgroup 5 on cash and derivative products in its analysis of appropriate backward and/or forward-looking fallbacks for each asset class.

4. Presentation of Subgroup 5 on market adoption for cash and derivatives

4.1 Composition

The working group had been informed of the composition of subgroup 5 and its Terms of Reference had been agreed by written procedure. Both documents will be published on the ECB’s website.

4.2 Table of content and priorities for EONIA to €STR transition

Christian Gau (Deutsche) and Anna Kozhevnikova (Generali) presented the priorities for subgroup 5 on cash and derivative products. They recalled the main deliverables of subgroup 5: (i) enabling market participants to transition from EONIA to €STR; and (ii) embedding €STR term structure-based fallbacks in Euribor contracts to avoid market disruption. These deliverables were detailed in the Terms of Reference of subgroup 5.

Considering the timing of the EONIA to €STR transition, the top priority of subgroup 5 will be, first, establishing a list of products, processes and models affected by the transition; and, second, agreeing on recommendations for the identified products, processes and models, with the aim of addressing individual transition issues for each of them. A working document drafted by subgroup 5 should be submitted for approval at the next working group meeting on 4 July, and would serve as a basis for the recommendations for each product, process and model affected by this transition. Given the very tight time frame, whether or not there was a need to launch a public consultation on these future recommendations was debated. It was agreed that the co-chairs of subgroup 5 should submit a proposal to the working group in the coming weeks on whether a full public consultation would be needed, or only a partial public consultation on particularly sensitive topics.

A question was raised regarding possible overlaps with the activities of the other subgroups, particularly subgroup 6, and it was clarified that subgroup 5 would focus on operational aspects and perform analysis at a more granular level compared with subgroup 6. Moreover, an efficient and regular exchange of information among the subgroups should be set up.

Finally, **Christian Gau (Deutsche) and Anna Kozhevnikova (Generali)** explained that after the summer of 2019 subgroup 5 would focus on the development of the derivative market based on €STR, as well as Euribor fallbacks.

4.3 Move of EONIA publication from T to T+1: potential issues based on SONIA experience

Joseph McQuade (Barclays, for subgroup 5) presented an indicative time frame and potential considerations as guidance to EONIA users in adapting to the change in the timing of the EONIA publication to T+1, owing to its new methodology. The identified milestones and considerations cover pre and post-trade issues as well as business readiness, and highlight the very short time frame for adaptation before the expected start date of 2 October 2019. In this context, a few working group members shared their concerns about the potential lack of awareness and preparation among users regarding the change of timing. The working group agreed that communication efforts should be increased in this regard vis-à-vis EONIA users.

5. Presentation of Subgroup 6 on financial accounting and risk management

5.1 Composition

The working group had been informed of the composition of subgroup 6 and its Terms of Reference had been agreed by written procedure. Both documents will be published on the ECB's website.

5.2 Roadmap and foreseen timeline 2019

Markus Schmidtchen (KfW) recalled the main deliverables of subgroup 6, which is tasked with analysing the impact on financial accounting (focusing on IFRS 9 and IAS 39 but considering other standards as well) and risk management (focusing on interest rate risk management but other risk categories could be considered as well) of: (i) the transition from EONIA to €STR; and (ii) the inclusion in contracts of fallbacks for Euribor based on a €STR-based term structure methodology and possible fallback triggers. As the publication of €STR will commence in October 2019, the impact analysis for the EONIA to €STR transition is considered the top priority.

In terms of organisation, subgroup 6 would utilise two “drafting teams” of members with expertise in risk management and hedge accounting issues. Regarding hedge accounting issues, the most urgent task would be to identify critical points which could trigger discontinuation of hedge accounting relationships, i.e., among other things, a change in documentation, substantial modification of the contract terms and highly effective test. The analysis should incorporate cash flow as well as fair value hedges. On risk management issues, subgroup 6 should first focus on the implications for interest rate risk and asset liability management, potential adjustments to risk management systems and valuation infrastructures, and historical data requirements.

The working group agreed to the proposal made by subgroup 6 that a formal letter be sent to the International Accounting Standards Board (IASB), highlighting the specific issues of the transition from EONIA to €STR. After further analysis, a final report will be produced at the end of October 2019 that will include recommendations regarding the possible impact of moving from Euribor to €STR-based term rates.

6. Presentation of Subgroup 7 on communication and education

Steven van Rijswijk (Chair) announced that Santander would take the lead on this important work stream. The composition and roadmap of this subgroup will be communicated to the working group on euro risk-free rates in the next few weeks.

7. Other business

7.1. Next meeting

The next meeting of the working group will take place at the ECB on 4 July 2019, from 11:00 to 16:00 CET.

List of meeting participants

Chair

ING Bank

Mr Steven van Rijswijk

Ms Marjolein de Jong-Knol

Voting members

Bank of Ireland

Mr Barry Moran

Barclays

Mr Joseph McQuade

Bayerische Landesbank

Mr Harald Endres

BBVA

Mr José Manuel Gonzalez-Páramo

BBVA

Mr Adolfo Fraguas Bachiller

BBVA

Mr José Carlos Pardo Labrador

BNP Paribas

Mr David Gorans

BNP Paribas

Mr Patrick Chauvet

BPCE/Natixis

Ms Sophie Asselot

BPCE/Natixis

Mr Olivier Hubert

CaixaBank, S.A.

Mr Juan Cebrián Torallas

CaixaBank, S.A.

Mr Sergio Castellá Quintana

Crédit Agricole

Ms Florence Mariotti

Crédit Agricole

Mr Olivier Coupard

Deutsche Bank

Mr Juergen Sklarczyk

Deutsche Bank

Mr Christian Gau

DZ Bank

Ms Cornelia Gericke

DZ Bank

Mr Michael Schneider

Erste Group Bank AG

Mr Neil McLeod

Eurobank - Ergasias SA

Mr Theodoros Stamatou

HSBC

Mr Pierre Jenft

HSBC

Mr Gay Guggenheim

ING Bank

Mr Jaap Kes

ING Bank

Ms Johanneke Weitjens

Intesa Sanpaolo

Ms Maria Cristina Lege

KfW Bankengruppe

Mr Markus Schmidtchen

KfW Bankengruppe

Mr Ingo Ostermann

Santander

Mr Carlos Fernandez Infesta

Santander

Mr Óscar García Maceiras

Société Générale

Mr Olivier Balpe

Société Générale

Mr Stéphane Cuny

UniCredit Bank

Mr Alberto Covin

Non-voting members

European Money Markets Institute
European Fund and Asset Management Association
International Capital Market Association
International Swaps and Derivatives Association

Mr Alberto López Martín
Ms Agathi Pafili
Mr David Hiscock
Mr Rick Sandilands

Invited institutions

European Investment Bank
Generali
Generali

Mr Thomas Schroeder
Ms Anna Kozhevnikova
Mr Bruno Servant

Observers

European Central Bank
European Central Bank
European Securities and Markets Authority
Financial Services and Markets Authority
European Commission

Ms Cornelia Holthausen
Mr Holger Neuhaus
Mr Michele Mazzoni
Mr Randy Priem
Ms Alessandra Atripaldi

Secretariat

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Ms Stephanie Broks
Mr Mikael Stenström
Ms Yasmina Santalla Perez
Mr Vladimir Tsonchev