

27 November 2020

The EU Benchmarks Regulation ('BMR'): Public Consultations by the Working Group on Euro Risk-Free Rates

This circular is being addressed to market participants falling within the scope of BMR, particularly administrators of benchmarks¹, contributors of benchmarks² and users of benchmarks³.

1.0 Background

The working group on euro risk free rates (the 'Group') was primarily established in order to identify and recommend risk-free rates which could provide for an alternative to benchmarks which are currently used in several financial contracts and instruments within the euro area, including the euro interbank offered rate ('EURIBOR') and the euro overnight index average ('EONIA'). This Group is composed of representatives from the private sector.

On 13 September 2018, the Group recommended that the Euro short-term rate ('€STR') should be used as the Euro area's risk-free rate. Accordingly, the Group is now providing the market with the necessary support for the transition to the €STR.

In this respect, on 2 October 2019, the ECB published for the first time the €STR reflecting the trading activity which took place on 1 October 2019.

Further information relating to the Group's key milestones, past meetings, the €STR and related information may be accessed through the following [link](#).

2.0 Public Consultations Issued by the Group

The Authority would like to inform market participants that the Group has on 23 November 2020 published two public consultations relating to fallback rates to EURIBOR. Fallback rates are rates that can be relied upon in case of an unavailability of the main rate. Whereas both consultation documents

¹ In terms of Article 3(1)(5) of BMR, provision of a benchmark means: (a) administering the arrangements for determining a benchmark; (b) collecting, analysing or processing input data for the purpose of determining a benchmark; and (c) determining a benchmark through the application of a formula or other method of calculation or by an assessment of input data provided for that purpose.

² Pursuant to Article 3(1)(8) of BMR, contribution of input data refers to providing any input data not readily available to an administrator, or to another person for the purposes of passing to an administrator, that is required in connection with the determination of a benchmark, and is provided for that purpose.

³ Article 3(1)(7) of BMR defines use of a benchmark as: (a) issuance of a financial instrument which references an index or a combination of indices; (b) determination of the amount payable under a financial instrument or a financial contract by referencing an index or a combination of indices; (c) being a party to a financial contract which references an index or a combination of indices; (d) providing a borrowing rate as defined in point (j) of Article 3 of Directive 2008/48/EC calculated as a spread or mark-up over an index or a combination of indices and that is solely used as a reference in a financial contract to which the creditor is a party; and (e) measuring the performance of an investment fund through an index or a combination of indices for the purpose of tracking the return of such index or combination of indices, of defining the asset allocation of a portfolio, or of computing the performance fees.

are available on the ECB's website, the following sections provide a brief overview of the two consultation documents.

2.1 Consultation on EURIBOR fallback trigger events

Fallback measures are intended to reduce the risk related with the temporary or permanent cessation of a benchmark rate. With respect to EURIBOR, the inclusion of an alternative benchmark rate ensures that parties to a financial instruments or contracts referencing EURIBOR cannot dispute the contract and any action taken thereafter as a result of the unavailability of the referenced benchmark rate. Following a high-level recommendation put forward by the Group in November 2019, any new contracts and financial instruments which reference EURIBOR should also include provisions which cover fallback trigger events in case of both temporary and permanent cessation.

The Group has in this [consultation paper](#), identified a number of events which may potentially lead to a permanent EURIBOR fallback trigger and that market participants may consider including in fallback provisions in their contracts and financial instruments referencing EURIBOR. In this respect, market participants are invited to provide feedback on the proposed EURIBOR fallback trigger events.

2.2 Consultation on €STR-based EURIBOR fallback rates

The Group considered two types of €STR fallback rates, namely the (i) Forward-looking rates⁴; and (ii) Backward-looking rates⁵ The objective of this consultation paper is to survey market participants, organisations representing market participants and any other interested stakeholders with respect to the most appropriate EURIBOR fallback provisions for cash products. This [consultation paper](#) therefore covers:-

- The most adequate EURIBOR fallback rate which is based on (a) a €STR-based term structure methodology for each financial product examined against a list of key factors, and (b) a spread adjustment methodology which is used to avoid potential value transfer in the eventuality that a fallback is triggered; and
- The market conventions which should be used to calculate the compound term rate based on the €STR.

2.3 Way Forward

The two consultation papers are open for feedback until 15 January 2021. The Group invites all stakeholders to provide feedback on the consultation papers via e-mail to eurorfr@ecb.europa.eu. Thereafter, the ECB and the European Commission will evaluate all the feedback received and prepare an anonymized summary of the feedback. The summary will be published on the ECB's website and will be considered by the Group at its meeting on 18 February 2021. Final recommendation on the EURIBOR fallback measures are expected shortly after.

⁴Based on the derivatives markets referencing the €STR and which reflect market expectations of the evolution of the €STR. These rates are known at the start of the interest rate period

⁵Based on simple mathematical calculations of the value of past realised daily fixings of the €STR over a given period of time. These rates are known and available at the end of the interest rate period.

On a final note, the Authority would like to inform market participants that a virtual roundtable event, including Q&A sessions dedicated to the two public consultations will take place on 14 December 2020 between 14:30hrs and 18:00hrs. For those market participants who are interested in participating, the registration link will be published on the ECB's website in the coming days.

Contacts

Should you have any queries relating to the above kindly contact the Authority on bmr@mfsa.mt.