

Terms of reference for the Working Group on Euro Risk-Free Rates

1 Introduction

Major reference interest rates play a pivotal role in the global financial system because of their usage in a broad range of financial products and contracts. Due to potential litigation, compliance risks as well as increasing costs of compliance, banks have become more and more reluctant to participate voluntarily in benchmark panels. Together with the declining activity in the underlying market, this has undermined confidence in the reliability and robustness of the existing benchmarks. The resulting uncertainty about the integrity of reference rates represents a potentially serious source of vulnerability and systemic risk.

In 2013 the G20 asked the Financial Stability Board (FSB) to undertake a fundamental review of major interest rate benchmarks and plans for their reform. In July 2014 the FSB published its recommendations on interest rate benchmark reform¹, developed under the guidance of the Official Sector Steering Group (OSSG) and drawing on reviews of benchmark administrators by the International Organization of Securities Commissions (IOSCO) and the work of a Market Participants Group (MPG) that comprised senior financial executives with a wide range of expertise and market experience.

In order to ensure that benchmarks remain robust and are used appropriately by market participants, the FSB recommended a “multiple-rate approach” with two broad objectives:

- Strengthening existing interest rate benchmarks and other potential reference rates based on unsecured bank funding costs by underpinning them with transaction data as far as possible.
- Developing alternative, nearly risk-free, reference rates (RFRs).

¹ FSB (2014): [Reforming major interest rate benchmarks](#) .

In September 2017 the European Central Bank (ECB), the Financial Services and Markets Authority (FSMA), the European Securities and Markets Authority (ESMA) and the European Commission announced the launch of a new working group tasked with the identification and adoption of RFRs to serve as a basis for an alternative to the current benchmarks used in a variety of financial instruments and contracts in the euro area.

2 Current major euro area interest rate benchmarks

The most widely used interest rate benchmarks for financial contracts denominated in euro are the Euro Interbank Offered Rate (Euribor) and the Euro Overnight Index Average (EONIA). Both are based on the unsecured interbank market and administered by the European Money Markets Institute (EMMI). The Euribor is a quote-based interest rate benchmark, available for several tenors (one and two weeks, as well as one, two, three, six, nine and twelve months). The EONIA is the overnight reference rate for the euro computed on the basis of real transactions in the interbank market. Both benchmark rates are undergoing reforms led by their administrator. These reforms aim to bring both benchmarks into compliance with the new EU Regulation on Benchmarks², which was published in 2016 and will be applicable as of 1 January 2018. In the meantime, these two benchmarks have also been designated as critical by the European Commission, which makes them subject to specific provisions, notably regarding the modalities for their supervision.

3 Composition of the Working Group on Euro Risk-Free Rates

The working group will be an industry group chaired by a representative from the private sector. It will comprise senior officials from major credit institutions with relevant expertise. Firms will be granted membership of the working group only at the invitation of the four public institutions mentioned above, with individual working group members being appointed by member firms. The choice of private sector

² 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 and amending Directives 2008/48/EC and 2014/17/EU and Regulation (EU) No 596/2014 (OJ L 171, 29.6.2016, p. 1).

representatives will also be made so as to ensure broad geographical coverage of the euro area.

Representatives from the FSMA, ESMA, ECB and European Commission will participate in the working group as observers and the ECB will provide its Secretariat.

Given the current FSB mandate of the International Swaps and Derivatives Association (ISDA) to develop fallback arrangements in case interbank offered rates (IBORs) cease to exist at some point, ISDA will be invited to participate as a non-voting member.

EMMI will also be invited to participate in the working group as a non-voting member, in view of its role as an administrator of critical benchmarks.

The working group will also invite additional institutions to participate as non-voting members, such as clearing houses or market associations, if it is considered useful to do so.

In addition, the working group will establish sub-groups on specific aspects, which will report to the working group on their findings.

Finally, the working group is expected to reach out to and gather feedback from a wide range of stakeholder groups, including central counterparties, exchanges and end-users. The members of the public institutions involved will facilitate this outreach process by hosting roundtable meetings at the request of the working group.

4 Deliverables of the working group

The working group is expected to provide the following deliverables:

1. *Identify alternative euro RFRs.* The working group will consider alternative euro interest rates consistent with the IOSCO principles for financial benchmarks and compliant with the EU Regulation on Benchmarks. It will identify which RFRs should be used as best practice for certain new derivatives and other contracts, including mortgage contracts. Based on a decision by the working group, dedicated sub-groups may be set up to propose and examine various potential RFRs and, if appropriate, assess whether these proposed reference rates are compliant with the EU Regulation on Benchmarks (e.g. liquidity of the underlying market, representativeness, robustness, reliability, potential for input

- data to be manipulated, etc.). Such sub-groups could be chaired by private-sector rapporteurs assigned by the working group and would report to the working group on a regular basis.
2. *Identify best practices for contract robustness.* The working group will consider best practices for contract design that ensure that new contracts are robust and resilient to the possible cessation or material alteration of the underlying benchmark. Furthermore, the working group will consider the factors that could facilitate the adoption of the chosen RFRs or the adoption of best practices for contract robustness among a broad group of market participants, including end-users. The role of ISDA will be important here given the synergies with the work streams already ongoing in the derivatives community.
 3. *Develop an adoption plan, and if necessary the creation of a transition plan for legacy contracts referencing existing benchmarks.* The working group may create a transition plan and a timeline for the transition from current benchmarks, if at some point in the future this is deemed necessary. For retail contracts, given the consumer protection issues involved, ESMA will coordinate a dedicated sub-group and provide its Secretariat. This sub-group will be in charge of identifying appropriate alternatives for term structured benchmarks and developing a transition plan. It will be composed of private-sector representatives and report to the working group on a regular basis.

5 Indicative timeline

The Benchmarks Regulation provides for transitional provisions that would also apply to the current critical benchmarks the Euribor and the EONIA. The Benchmarks Regulation requires the administrator of the Euribor and the EONIA to seek authorisation before the end of 2019. After this transitional period it will no longer be possible for supervised entities in the Union to use these benchmarks unless the administrator has been authorised or its supervisor has granted an exemption. In view of this timeline, the working group's first deliverable, i.e. the selection of alternative reference rates for the euro, is expected by end-2018, while the second and third deliverables should run in parallel and be completed by the end of 2019. A more detailed work plan will be publicly available once agreed by the working group.

6 Governance of the working group

A call for expressions of interest is being launched for those firms that are interested in participating in the working group. This call is primarily aimed at credit institutions, but other, non-banking institutions or associations are also welcome to flag their

interest in actively contributing to the activities of the working group notably through its future substructures.

Membership of the working group will be granted only at the invitation of the four public institutions above, with individual working group members being appointed by member firms. Individual members of the working group are expected to represent their respective firms and draw on their firm's resources where appropriate. Participation in the working group or any substructure will not give rise to remuneration or other emoluments.

For voting and decision-making, each member firm will have one vote. Observers will not be eligible to vote. Decisions and recommendations of the working group should be reached by consensus, if possible, or otherwise by a two-thirds majority where necessary. Any sub-groups will need to report on a regular basis to the working group, will be purely advisory and will not be able to take formal decisions.

The working group's recommendations will not commit individual firms or public authorities to specific actions. The working group's recommendations and publications will represent the views of its private-sector members only and should not be taken as approved by, or even as representing, the views of the public authorities concerned.

The ECB will disclose these terms of reference, the institutional membership of the working group, meeting agendas and minutes, once approved, on its public website.

Any information disclosed or opinions expressed during working group or sub-group meetings will be treated as confidential unless and until the working group has authorised their public release. Working group and sub-group members may be exposed to sensitive and potentially material non-public information in the course of their work. It is understood that working group or sub-group members' staff may see some documents related to the working group or sub-group. Nonetheless any unnecessary involvement of third parties in handling this material is strongly discouraged. Whenever working group or sub-group documentation is seen by third parties, individual members will be held responsible for ensuring that those third parties are aware of and respect the confidentiality and sensitivity associated with the working group, its sub-groups and the documents in question.

7 Competition law

It is the responsibility of working group and sub-group members to ensure that they understand their responsibilities under all applicable competition laws, including EU competition law.