

Where are we on benchmark reforms?

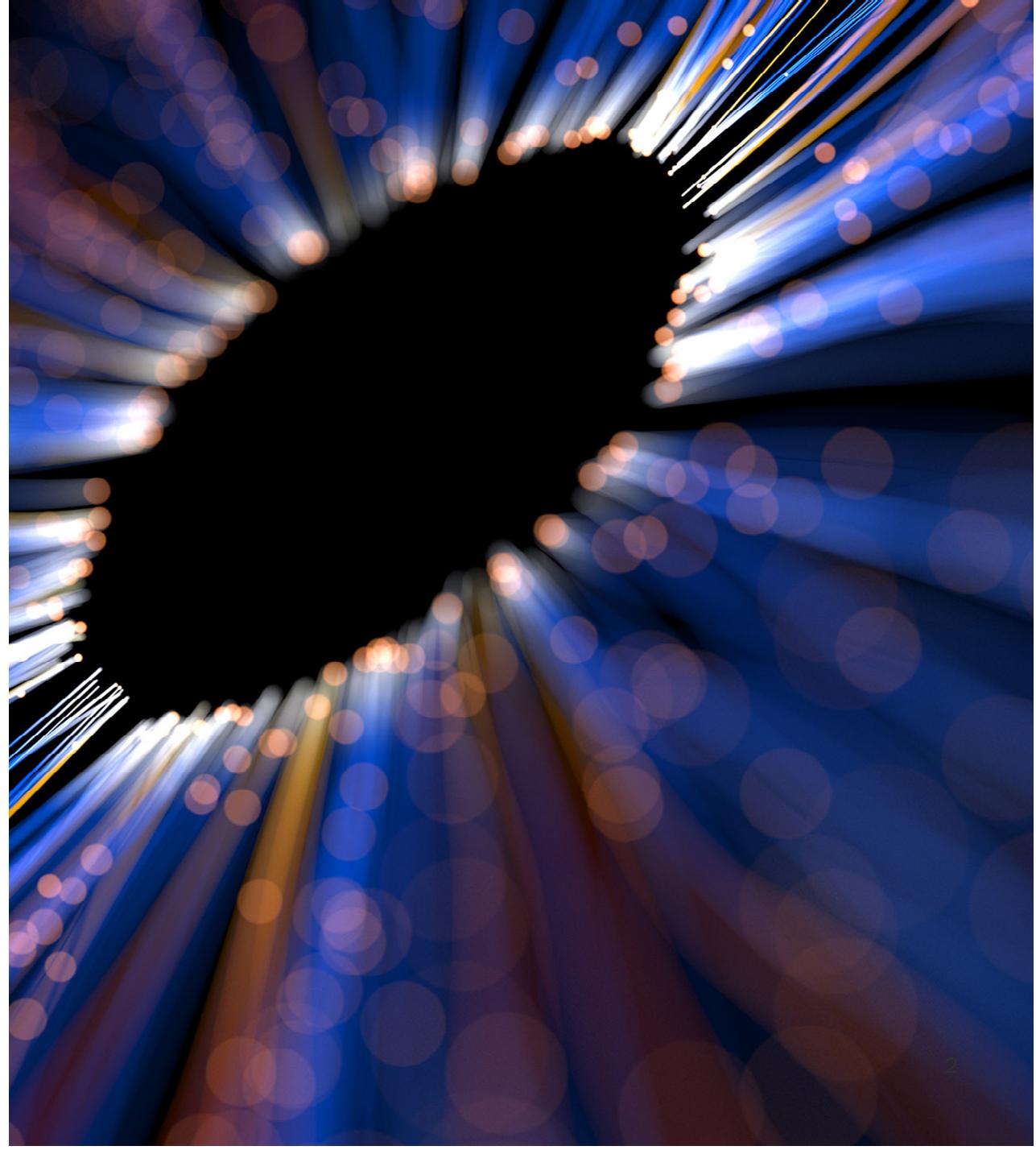
Financial Markets Legal
Update – the webinar series

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Agenda

- 1 Introduction
- 2 EURIBOR, EONIA, LIBOR
- 3 Fall-backs
- 4 Remediation
- 5 Q&A / Quiz questions



1. Introduction



Background to benchmark reform

Benchmark scandals:

- Barclays: Since 2005: misleading quoting of LIBOR (quotes were too high to increase bank revenues and, during the financial crisis, too low to help the bank). At Barclays, management knew of the manipulation.
- Rabobank: 2005-2011: 30 employees involved in misleading LIBOR and EURIBOR quotations. Settlement for USD 1 billion (€774 million). 30 employees dismissed, warned or de-moted. Bonusses worth EUR 4.2 million clawed back. CEO stepped down. Bank ignored signals from its own audit/internal control function.
- UBS: USD 1.5 billion fine.
- Deutsche Bank: paid USD 220 million to 45 US states to avoid criminal prosecution.
- RBS: reached a USD 612 million settlement with the UK's Financial Services Authority, the US Commodity Futures Trading Commission, and the US Department of Justice.

QUIZ TEST QUESTION: what is the longest jail term handed out for benchmark manipulation?



1. Introduction

Benchmark reform

- 01 January 2018: EU Benchmark Regulation (BMR) in effect
- December 2019: BMR under review: governance arrangements, benchmark methodology requirements, reporting of infringements, mandatory administration of a critical benchmark and non-significant benchmarks
- Ongoing: benchmark reform across the financial markets

2. EURIBOR and EONIA



Current status:

- 13 September 2018: WG on Euro RFR recommend that €STR be used as RFR to replace euro overnight index average (EONIA) and the euro interbank offered rate (EURIBOR).
- 02 October 2019: ECB published €STR for the first time.
- 28 November 2019: EMMI successfully completed phase-in of all panel banks; implementation of **EURIBOR hybrid methodology** complete.
- 01 January 2020: FIs may **only use authorised benchmarks in new contracts**. Transitional periods under BMR expired. Extension of transitional period for critical and third country benchmarks until 31 December 2021.
- 19 February 2020: WG recommendations to support smooth transfer of **EONIA's liquidity to €STR** in cash and derivatives products: EONIA-linked contracts with maturities beyond 3 January 2022 entail significant risks. Recommendation that market participants replace EONIA products with €STR products and reduce their EONIA-linked legacy exposures as soon as possible.
- 17 April 2020: LCH, Eurex and the European Association of CCP Clearing Houses (EACH) announced a 5 week delay (namely until **27 July 2020**) for move from **EONIA to €STR** discounting for cleared trades (due to concerns over operational risks from COVID-19).

€STR

Rate -0.555

Reference date 30-06-2020

Volume (EUR millions) 42421

Number of active banks 28

Number of transactions 496

Share of volume of the five largest active banks 48%

Rate at 25th percentile of volume -0.60

Rate at 75th percentile of volume -0.53

Publication type standard

Calculation method normal

last update: 01 July 2020 08:00

2. EURIBOR and EONIA (continued)

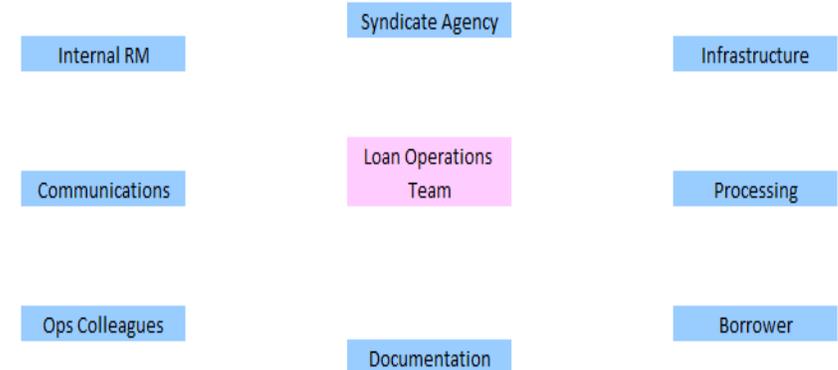


Developments:

- 27 February 2020: ICMA published quick guide to transition to RFR in bond market. Key issues include (i) floating rate notes, (ii) covered bonds, (iii) capital securities, (iv) securitisations and (v) structured bonds.
- Industry standards: LMA, ICMA, ISDA etc.

Challenges:

- April 2020: IASB published Exposure Draft on Interest Rate Benchmark Reform Phase 2: proposed amendments affecting financial reporting after the reform of benchmark.
- Keeping up to speed with legal and regulatory initiatives.
- Ongoing: impact of RFR transition on operations.



2. LIBOR



Current status:

- May 2020, WG on Sterling RFR published paper on identification of tough legacy issues (i.e. no robust fallbacks and unable to be amended ahead of LIBOR discontinuation)
- 29 April 2020: WG on Sterling RFR:
 - changes to near term targets for the Sterling LIBOR loan market due to the impact of COVID-19;
 - transition to SONIA in the bond market largely completed;
 - WG and BoFE recognise that it will not be feasible to complete transition away from LIBOR across all new sterling linked loans by the end Q3-2020 target.

Developments:

- ISDA expects to publish amendments to the 2006 ISDA Definitions to incorporate the fallbacks for new trades in July. A protocol will simultaneously be launched to allow participants to incorporate the revisions into legacy trades if they choose to.



3. Fall-backs



Debt capital markets:

- 25 April 2019: ARRC publishes recommendations regarding USD LIBOR FRNs.
- 06 November 2019: WG on Euro RFR published recommendations for fallback provisions in contracts for cash products and derivatives transactions referencing EURIBOR.
- 12 November 2019: WG on Euro RFR published report on €STR fallback arrangements.

Loan markets:

- 20 March 2020: LMA published revised facility agreements. LMA incorporated replacement of benchmark wording in facility agreements. The main purpose of the clause is to provide parties with greater flexibility to include a replacement benchmark in the Facility Agreement if a Screen Rate Replacement Event occurs.

Derivatives:

- ISDA expects to publish amendments to the 2006 ISDA Definitions to incorporate the fallbacks for new trades in July

Discussion points throughout the last year:

- Adjustment spreads, regional variations and regulatory constraints (BMR), pre-cessation triggers.

4. Remediation Planning

LIBOR death and its many friends

- Is 'do nothing' an option?
 - Regulatory initiatives in the UK & the US for “tough legacy”
 - “the market must continue actively transitioning away from LIBOR” (Rishi Sunak, 23 June)
- Can I rely on fallbacks?
 - A legally and commercially certain outcome that is economically acceptable?
 - Regulatory change termination events?
 - “Two step” amendment processes
 - LIBOR cessation triggers: risk of congestion
- Proactive or Reactive?
 - Different answer for different products and exposures
 - “snooze or lose” clauses; mixing up transition with other amendments; who pays?
 - At what point does failure to remediate a contract become your problem?
- Factors affecting remediation planning include
 - Due diligence – LIBOR exposure: LIBOR terms, maturity > 2021, fallbacks
 - Due diligence – remediation:
 - out of scope / in scope : high, medium or low priority
 - currency, agency roles, third party consents, commercially linked contracts, hedged v. unhedged exposures
 - Available market standard solution v. bespoke solution first to market risk
 - Systems readiness - controls the timing of changes becoming effective



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*Current
comprehensive IBOR
news and thought
leadership from our
global capital
markets, structured
products, derivatives,
banking and
regulatory practice.*

4. Is there an “off the shelf” tech solution?



- Data cleaning
- Data Security, database management, eDiscovery, text extraction and AI analysis?
- Project management & management information
- Autodrafting
- Manual drafting
- eSignatures
- Integration with in house document management, risk and transaction management software?

*Simmons & Simmons
IBOR team*

*IBOR remediation is a
requirement, not a
choice – let us be the
law firm to guide you
through the LIBOR
transition process.*

5. Q&A / Quiz questions



1

Do you believe IBOR reform remains a top 3 priority for the financial markets for the next year?

A. Yes.

B. No, there are other priorities (Brexit, Corona, economic crisis, other).

2

Are you personally engaged (or have you been asked by your employer to engage) in repapering/addressing issues in legacy contracts?

C. Yes, and I know exactly what to do.

D. Yes, but I do not fully understand what I am doing and why.

E. No.

3

Do you worry about financial, economic and accounting consequences of IBOR reform (pricing of loans, bonds, derivatives etc.)?

F. Yes.

G. No.

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