

IBOR Transition FAQs

Objective

The purpose of this document is to provide the customers and counterparties of Emirates Islamic Bank (P.J.S.C) (EIB) with an overview of the discontinuation of the London Interbank Offered Rate (LIBOR). This document is provided for information purposes only. EIB is not providing any recommendation, nor any legal nor regulatory advice, in this document. You should, together with your own independent, professional advisors, conduct your own analysis on the potential impact of benchmark rate reform, including LIBOR discontinuation, on your business.

Background of IBOR transition

What is Benchmark Reform about?

A lack of liquidity in the unsecured wholesale lending market following the financial crisis of – 2007 2008 resulted in reduced transaction-based inputs to support LIBOR. In 2012, **a number of banks were fined by the UK Financial Conduct Authority (FCA) for having manipulated interbank offer rates (IBOR) which they had submitted during the financial crisis¹**. It was observed by regulators that manipulation of IBORs was relatively easy (due to the methodology construct and reliance on ‘expert judgement’) which posed a systemic risk.

In the wake of the LIBOR manipulation and the declining transactions in the LIBOR market, the **FCA transferred supervision of the index to the Intercontinental Exchange Benchmark Administration (IBA)**.

In July 2017, **the FCA announced that panel banks would no longer be compelled to contribute LIBOR for the determination of LIBOR after 2021**. If panel banks cease to contribute the data required to compile LIBOR, LIBOR may become more volatile and less liquid. Therefore, LIBOR is to be discontinued. Regulators and public and private sector working groups in several jurisdictions have been discussing a transition to alternative reference rates (ARRs) to replace LIBOR.

Several other interbank offered rates (IBORs) and benchmarks are being reformed or, in some cases, discontinued. For some currencies, the relevant IBOR will continue alongside the ARR. For other currencies, the relevant IBOR will likely cease to be provided and so the principal benchmark will be the ARR.

A number of ARR working groups have been set up across a range of countries and the ARR which has been chosen by those working groups for each LIBOR currency is shown below:

¹Sources: [FCA fine enforcements](#)

IBORs and corresponding ARR

IBOR	ARRs
USD LIBOR	Secured Overnight Financing Rate (SOFR)
GBP LIBOR	Sterling Overnight Index Average (SONIA)
EUR LIBOR	European Short-term Euro Rate (€STR)
CHF LIBOR	Swiss Average Rate Overnight (SARON)
JPY LIBOR / JPY / EuroYen TIBOR	Tokyo Overnight Average Rate (TONAR)
SIBOR / SOR	Singapore Overnight Rate Average (SORA)

What are the differences between LIBORs and ARR

ARRs are structurally different to IBORs. IBORs are calculated by reference to forward-looking rates applicable to a future tenor and include a risk element for interbank lending (for example, term bank credit risk or liquidity premium for longer term exposure). ARR, on the other hand, are overnight rates calculated on a compounded or weighted-average basis (so-called 'risk-free' rates (**RFRs**)), are backward-looking and do not take account of interbank lending risk.

IBOR	ARRs
Forward Looking rate with the defined Term Structure (7 tenors)	Overnight only (at this stage), backward looking rates with limited forward term structure
Based on expectations/speculations ; quotes submitted by panel banks	Based on actual transactions; calculated volume-weighted median
Includes a built-in Credit Risk and Liquidity Spread across the tenors	Nearly risk free rates
Centrally calculated in the Interbank Market	Each country has its own rate calculation mechanism
Responsive to risk free rate, liquidity and credit pricing (especially in the event of stress)	Only responsive to change in risk free rates

When will IBORs be discontinued?

There are two key triggers expected to follow in connection with the discontinuation of IBORs and the application of ARR: a **Pre-Cessation Event** and a **Cessation Event**.

A **Pre-Cessation Event** occurs when the regulatory supervisor for the administrator of an IBOR (currently, the FCA in respect of LIBOR) announces publicly that the IBOR is non-representative or is otherwise no longer a reliable benchmark as of a specific date even though publication of the IBOR benchmark will yet to have ceased.

A **Cessation Event** occurs when the regulatory supervisor for the administrator of an IBOR announces publicly that it has ceased, or will cease, to provide the relevant IBOR permanently or indefinitely, provided that, at that time, there is no successor administrator that will continue to provide the relevant IBOR.

A Pre-Cessation Event occurred on 5 March 2021 when the FCA announced that the following LIBORs will either cease to be provided or will no longer be representative immediately after the following Cessation Dates:

- 31 December 2021: (i) in respect of Sterling, Euro, Swiss Franc and Japanese yen, all LIBOR tenors; and (ii) in respect of United States dollars (USD), for one week (USD LIBOR 1w) and for two months (USD LIBOR 2m); and
- 30 June 2023, in the case of USD, all remaining LIBOR tenors.

What happens to my existing LIBOR referencing financing arrangements?

Financing Arrangement	Financing Maturity	Action
Existing non-USD LIBOR referencing contracts	On or before 31 December 2021	No action required
Existing USD LIBOR 1w and USD LIBOR 2m referencing contracts	On or before 31 December 2021	No action required
Existing USD LIBOR referencing contracts (except USD LIBOR 1w and USD LIBOR 2m tenors)	On or before 30 June 2023	No action required
Existing non-USD LIBOR referencing contracts	After 31 December 2021	Amend current LIBOR referencing contracts to ARR referencing contracts
Existing USD LIBOR 1w and USD LIBOR 2m referencing contracts	After 31 December 2021	Amend current LIBOR referencing contracts to ARR referencing contracts
Existing USD LIBOR referencing contracts (except USD LIBOR 1w and USD LIBOR 2m tenors)	After 30 June 2023	Amend current LIBOR referencing contracts to ARR referencing contracts

What will happen to new floating rate financing arrangements?

Financing Arrangement	Financing Maturity	Action
New GBP floating rate contracts	After 31 December 2021	The FCA and the Bank of England have recommended that, from 1 April 2021, any new floating rate GBP Financing and linear derivatives expiring after 31 December 2021 be documented by reference to SONIA and not to GBP LIBOR.
New floating rate contracts denominated in Euro, Japanese yen and/or Swiss Francs	After 31 December 2021	The European Union (EU) in respect of Euro, the Bank of Japan in respect of Japanese yen, and the Swiss National Bank in respect of Swiss Francs, have each recommended that, from 1 July 2021, any new floating rate financing arrangements and linear derivatives denominated in those currencies, respectively, and expiring after 31 December 2021 be documented by reference to the relevant ARRs and not to LIBOR.
New USD floating rate contracts	After 30 June 2023	The FCA and the US Federal Reserve have recommended that, as soon as possible but no later than 31 December 2021, new USD floating rate financing arrangements expiring after 30 June 2023 be documented by reference to ARRs and not IBORs.

What is happening to the Emirates Interbank Offered Rate ('EIBOR')?

EIBOR is regulated by the Central Bank of the United Arab Emirates and it is the benchmark profit rate, stated in UAE Dirhams, for financing between banks within the UAE market. At present, we are not aware of any current plans for discontinuation of EIBOR. As the UAE Dirham is not a LIBOR currency, we do not expect EIBOR to be directly affected by the discontinuation of LIBOR. However, the Central Bank of the United Arab Emirates may, in future, mandate reforms to EIBOR.

What is happening to the European benchmark rates, EURIBOR and EONIA?

EURIBOR is the interbank offer rate for Euro between European banks and EONIA is the Euro overnight index average. While EONIA will be discontinued on 3 January 2022 and replaced by the €STR (being an overnight wholesale funding rate that is published by the ECB), EURIBOR (having undergone reform in 2019 and been authorized by the competent authority as being compliant with the EU benchmark regulations) can continue to be used for new and legacy contracts after the Cessation Date for EONIA. We continue to monitor announcements for any change to the availability and use of EURIBOR.

What is fallback language?

Terms and conditions of financial products typically contain fallback provisions, which identify how a successor or substitute will be selected if LIBOR, EURIBOR, EONIA or a similar benchmark is not published. There is a risk that fallback terms do not adequately cater for the circumstances in which they need to be used. For example, fallbacks which rely on a poll of banks are dependent on the co-operation of third parties, which may not be provided.

Fallback language in the context of LIBOR is the contractual language contingent on the cessation trigger and/or the pre-cessation trigger that will initiate the switch to the ARR. Links to various regulatory working groups are set out below, detailing their respective recommendations on fallbacks.

What is Credit Adjustment Spread (CAS)?

LIBORs and ARRs are economically different, as demonstrated by the different composition of the two.

Given this difference, a credit adjustment spread (CAS) may be required when transitioning a LIBOR referencing financing to an ARR referencing financing to eliminate or minimize any transfer of value.

$$\text{LIBOR} + \text{Margin} \approx \text{ARR} + \text{Margin} + \text{CAS}$$

One of the methods for determining the CAS is the 'ISDA Median Spread'. The International Swaps and Derivatives Association (ISDA) provided for the calculation of the ISDA Median Spread. It is equivalent to the median difference over a historic five year period (ending no later than two business days before the relevant IBOR Pre-Cessation Date) between the relevant IBOR being replaced and the corresponding ARR compounded in arrears for the term equivalent to the tenor of the IBOR it replaces.

The ISDA Median Spread was determined and fixed on 5 March 2021. This establishes a benchmark for the application of a credit adjustment spread in moving LIBOR referenced financing arrangements to ARR referencing finance arrangements.

While the ISDA Median Spread may be applied in whole or used as a benchmark, ultimately it is a commercial agreement to be made between the parties and so, banks are likely to adopt alternate methodologies to compute applicable credit adjustment spread.

Is there any guidance for Islamic financing and Islamic derivatives?

Concrete regulatory guidance, and corresponding industry consensus, on IBOR referencing Islamic financing and derivative products are yet to emerge.

What are the fallbacks being developed in the Derivatives markets?

The IIFM guidance is awaited for fallback protocol regarding derivatives.

Does the transition affect accounting treatment?

In September 2019, the International Accounting Standards Board (**IASB**) amended some of the requirements for hedge accounting. The amendments modify some specific hedge accounting requirements to provide relief from potential effects of the uncertainty caused by the IBOR reform. The amendments came into effect on 1 January 2020.

These changes provide temporary relief for so-called 'hedge relationships' prior to LIBOR's discontinuance ('Phase 1'), further guidance relating to the actual adoption of ARR and the discontinuance of LIBOR ('Phase 2') was provided in 2020.

In March 2020, the Financial Accounting Standards Board (**FASB**) also approved an Accounting Standards Update (ASU) to provide 'temporary, optional guidance to ease the potential burden in accounting for reference rate reform'.

In August 2020, the IASB published the Phase 2 Amendments to the IBOR reforms, to provide guidance on replacement of existing contracts with new ARRs and the implications for market valuations and the effectiveness of existing hedges, and tax and accounting changes if any. It is recommended to seek professional advice for accounting implications.

Next Steps

- Given that LIBOR is widely used, its discontinuation may impact, amongst other things, the payments under and/or the value of the products you currently have or that you may obtain in the future, your systems and processes, hedging arrangements and tax and accounting treatment. The implications of LIBOR discontinuation will differ depending on the product and/or service that you use. When entering into transactions with EIB, you should consider the risks and benefits of using a particular benchmark and understand the consequences if such a benchmark is changed or discontinued. You should consider whether you have suitable contingency plans in place should any of the events described above happen. You should consider, and keep under review (on your own behalf or through independent professional advice), the potential impact and risks of any future changes to the relevant benchmark rates under the financial contracts and financial instruments that you have (or may in the future enter into) with EIB. We recommend that you keep up to date with the latest industry developments in relation to the upcoming changes and the potential alternative benchmark rates that may be relevant to you. For any queries relating to the discontinuation of LIBOR, please contact your Relationship Manager.
- EIB plans to be operational to transact new ARR products in line with regulatory guidance and market developments.
- EIB will communicate with its clients at the relevant time for the purposes of amending existing LIBOR referencing contracts.

Where can I find more information on ARRs/RFRs?

Each of the central bank led RFR working groups that were set up at the recommendation of the FSB have established specific websites to provide market participants with information regarding key transition topics and steps, meeting minutes, feedback on consultations, and other relevant data.

Working Groups

Currency	Working Group Links
GBP	https://www.bankofengland.co.uk/markets/transition-to-sterling-risk-free-rates-from-libor
EUR	https://www.ecb.europa.eu/paym/initiatives/interest_rate_benchmarks/WG_euro_risk-free_rates/html/index.en.html
USD	https://www.newyorkfed.org/arrc
JPY	https://www.boj.or.jp/en/paym/market/jpy_cmte/index.htm/
CHF	https://www.snb.ch/en/ifor/finmkt/fnmkt_benchn/id/finmkt_reformrates
SGD	https://www.abs.org.sg/benchmark-rates/about-sora
HKD	https://www.hkma.gov.hk/eng/news-and-media/insight/2019/05/20190502/

IBOR	ARRs
ISDA International Swaps and Derivatives Association	https://www.isda.org/ https://www.isda.org/category/legal/benchmarks/
ICMA - International Capital Market Association	https://www.icmagroup.org/Regulatory-Policy-and-Market-Practice/benchmark-reform/
LMA - Loan Market Association	https://www.lma.eu.com/libor
LSTA - Loan Syndications and Trading Association	https://www.lsta.org/
APLMA - Asia Pacific Loan Market Association	https://www.aplma.com/
ACT - Association of Corporate Treasurers	https://www.treasurers.org/

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