

## Frequently Asked Questions About the Reference Rate (IBOR) Reform

### What is reference rate?

The interest rates used in financial product contracts can be set as fixed or variable, but reference interest rates are also commonly used. The London Interbank Offered Rate (LIBOR) is one of the most commonly used reference rates and is taken as reference in products such as derivatives, bonds and loans.

LIBOR is a reference rate published on every business day and administered by the ICE Benchmark Administration (IBA). LIBOR is based on the quotations given by 20 panel banks in five currencies (USD, EUR, CHF, GBP and JPY) for seven maturity ranges (overnight, weekly, 1,2,3,6 and 12-month).

Some countries used special reference rates for their own currencies. EURIBOR for EUR and TIBOR for JPY are examples of special reference rates used by countries for their own currencies.

### Why do reference rates change?

The decrease in interbank daily trading volume after the 2008 crisis caused liquidity depth to disappear and the potential for manipulation in the current reference rate IBORs to increase. It is aimed to set markets on a strong foundation by using alternative reference rates based on observable trades unlike IBORs.

### What is happening in financial markets?

After the G20 asked the Financial Stability Board (FSB) in 2013 to review important reference rates and recommend a reform on these rates, the FSB published its recommendations consisting of two bases in 2014;

- i. Make a reform in LIBOR (and its equivalents) to ensure that reference rates reflect the essential market conditions and remain as trade-based as possible,
- ii. Develop reference rates that include no loan or maturity item

The UK Financial Conduct Authority (FCA) announced that panel banks currently contributing to the calculation of LIBOR will not be required to submit an interest rate as of the end of 2021.<sup>1</sup>

Regulatory authorities throughout the world play an active role in encouraging the distancing from LIBOR rates and are continuing their efforts to develop alternative reference rates and new products to be used to price loans, securities, borrowings, derivatives and other financial instruments.

### What are the alternative reference rates to the current reference rates?

Alternative reference rates provide a very suitable, strong and reliable overnight reference rates for market needs and many other purposes.

Both cash and derivative markets are expected to start using alternative reference rates as their main reference rates.

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<sup>1</sup> Currently, there may be some rates that will continue to be published for some time.

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Currency	Current reference rate	Alternative reference rate	Transaction type
USD <sup>2</sup>	LIBOR	SOFR, Secured Overnight Financing Rate	Secured
EUR <sup>3</sup>	LIBOR, EURIBOR	€STR, Euro short-term rate	Unsecured
GBP	LIBOR	SONIA, Sterling overnight index average	Unsecured
JPY	LIBOR	TONAR, Tokyo overnight average rate	Unsecured
CHF	LIBOR	SARON, Swiss average rate overnight	Secured

### Where does the transition take place?

The transition process is ongoing in all major economics including the US, Europe and Asia. A similar process is followed in our country where Borsa Istanbul has been publishing the Turkish Lira reference rate (TLREF) and the TLREF index as of 2019 as an alternative to TRLIBOR.

### Which reference rates in the process of transition are commonly used?

All countries with their own currencies have their own reference rates used for the financial products in these currencies. The example of this in Turkey is TRLIBOR.

Many floating-rate financial products in the world take one of these five LIBOR rates as reference: Sterling, US Dollars, Japanese Yen, Euro and Swiss Franc LIBORs.

The European Union has three reference rates for the Euro: The Euro Overnight Index Average (EONIA), the EUR LIBOR and the Euro Interbank Offered Rate (EURIBOR).<sup>4</sup>

In the US, the USD LIBOR is under reform as part of this process.

<sup>2</sup> International regulatory authorities lean towards continuing to publish USD LIBOR's most commonly used overnight, 1-month, 3-month, 6-month and 12-month rates until June 2023. However, regulatory authorities do not advise new products to be established based on these products.

<sup>3</sup> The EURO short-term rate (€STR) will replace the EURO Overnight Index Average (EONIA) at the end of 2021. EURIBOR has no potential cessation date.

<sup>4</sup> Unlike the other reference rates, the EURIBOR is expected to remain in use after 2021 after it was restructured in September 2019 to comply with the EU Benchmark Regulation (BMR).

### **Will all reference rates be discontinued?**

The focus of the reference rate reform is the five main LIBORs (GBP, USD, EUR, JPY and CHF) for which publication is expected to be ceased. These reference rates will be considered in the scope of change as they will not be suitable for use pursuant to the regulation arranging interest rates in the European Union (EU-BMR) as of the end of 2021.

EURIBOR was subject to deep reforms in recent years to meet the EU-BMR requirements, strengthen the governance framework and develop a new hybrid model.

However, many regulatory authorities plan to replace the reference rates in the upcoming years or, as in the case of regulatory authorities in the Asian markets in particular, working on a multi-rate system in which the current and new reference rates can be used simultaneously.

### **Who will the transition affect?**

The transition will affect all market actors holding financial product(s) related to IBORs and who will identify an alternative reference rate for their own currency.

### **In which products are the IBOR reference rates used?**

Today, the IBOR reference rates are among the most significant parameters of floating-rate financial products. The replacement process of the reference rates will affect loans, securities, borrowings (Cash Products) and derivative products.

### **When will the transition take place?**

The publication of IBORs is expected to be ceased at the end of 2021. Therefore, the transition process needs to be completed before this date. Also, it is also important to update the fallback language of IBOR-referenced contracts before the end of 2021.

### **What is fallback language?**

Fallback language is provisions that activate upon a "trigger" event and describes the steps to be taken for transition to an alternative reference rate if the reference rate affecting the transition is no longer available.

In the context of the reference rates reform, fallback language may be triggered when IBORs cease being published or when the FCA announces that LIBOR is no longer representative of the market. However, the trigger event should be assessed separately in terms of each fallback language.

On the other hand, the fallback languages in many financial contracts seem to have been designed not with respect to the possibility of a reference rate ceasing permanently but becoming unavailable temporarily. Also, even if a fallback language legally represents a new rate, such rate may not be suitable or not commercially provide the intended purpose of the parties due to various reasons.

Fallback language should ideally be arranged against the cessation of IBORs in an effective and robust way, in a clear and practicable manner and individually by each market participant.

### **What changes will take place and when?**

Although the IBOR transition for all products is expected after the end of 2021, it may vary depending on the country.

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For example, in the United Kingdom, market participants are required to significantly reduce their inventory of IBOR-related products until the end of 2021 Q1.

Transition should be made in existing derivative contracts with maturities after the end of 2021 and the ISDA IBOR Fallback Language Protocol must be participated for implementation. (adherence).

### **Where can I find further information on the ISDA protocols?**

ISDA's website has detailed information on this matter.

- [Benchmark Reform and the transition from LIBOR](#)
- [ISDA Fallbacks Protocol](#)
- [ISDA Benchmarks Supplement & ISDA Benchmarks Supplement FAQs](#)
- [ISDA Benchmarks Supplement Protocol & Protocol FAQs](#)

ISDA Benchmarks Supplement [How to Adhere: Step-by-Step instructions](#)

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