

To: Solvency II Working Group
From: Prudential Team
cc:
Date: 16-06-2021
Reference: ECO-SLV-21-174

Subject: Call with EIOPA on IBOR transition

Summary

On Tuesday 15 June, the secretariat attended a call organised by EIOPA on the IBOR transition. The aim of the call was to collect any initial views from stakeholders on the ongoing consultation on IBOR (see [ECO-SLV-21-163](#)) before the end of the consultation period.

As an introduction, EIOPA briefly summarised the key points in the consultation and set out its expected timeline. There was a subsequent Q&A session where stakeholders were able to share their preliminary views to which EIOPA provided feedback.

Introduction by EIOPA

- EIOPA's objective is to update its process for producing risk-free rates (RFR) to incorporate any necessary changes arising from the discontinuation of the IBOR benchmarks without unnecessarily influencing the market. It aims to have a common approach for all currencies, but acknowledges the transitions are moving at different speeds.
- EIOPA proposes to make an instant switch from IBOR-based curves to overnight index swap (OIS) curves based on two preconditions:
 - 1) the IBOR and OIS rates are closely aligned for a period of time (proximity precondition)
 - 2) OIS swaps make up more than 50% of the total volume of traded swaps (liquidity precondition).
- EIOPA's view is that the credit risk adjustment (CRA), required by the Delegated Regulation, is no longer needed as OIS curves are essentially risk-free.
- For the JPY and CHF, it is likely that EIOPA will have to produce RFR curves based on government bonds once IBOR curves are withdrawn, as OIS swaps are not yet sufficiently liquid.
- EIOPA propose not to change the historical curves in the future calculation of the long-term average spread (LTAS). The LTAS is a parameter used in the calculation of the VA and MA.

Expected timeline

- 23 July: deadline for the consultation
- End-September: a proposal will be made to the Board of Supervisors for its decision on the way forward
- October 2021 onwards: implementation of agreed approach

Summary of Q&A discussion

Change of instrument and last liquid point

- Stakeholders raised concerns that the switch could lead to disruption and solvency volatility due to a change in instrument and/or LLP which would subsequently be reversed when liquidity in the OIS markets increased.
 - EIOPA acknowledged the point but noted that changes will need to be based on data. It recognised that the LLP should be kept as stable as possible.
 - From its current assessment of the liquidity of the OIS markets, EIOPA does not expect that a change to using government bond curves would be short-term.
- It was noted that EIOPA and the PRA have proposed different LLPs for the GBP.
 - EIOPA highlighted that the PRA uses a forward-looking approach. EIOPA does not yet see 40-50 years as liquid, whereas the PRA sees evidence they will be in the future and so uses an LLP of 50 years.
- Stakeholders asked if EIOPA had considered the impact of changing LLPs on ALM, risk management, hedging noting that changes in LLPs could become difficult to manage and hedge.
 - EIOPA's impact assessment only looks at the impact of changing the RFRs but EIOPA is monitoring liquidity on a daily basis.

Credit risk adjustment (CRA)

- Stakeholders enquired how EIOPA would ensure that the OIS curves did not need to apply the 10 basis point minimum CRA specified in the Delegated Regulation.
 - EIOPA highlighted that the CRA is required only for instruments that embed credit risk, therefore it is not needed for OIS.
- It was questioned whether the CRA should be applied to government bonds, as proposed for the Yen and Swiss franc.
 - EIOPA noted that it was bound by the Delegated Regulation which stipulated that the CRA should be applied to government bond curves as well.

Data sources

- Stakeholders requested information on the data sources EIOPA was using to assess liquidity and asked if it was possible for indicators to be published on a regular basis.
 - EIOPA noted it has access to data on all trades in the EU under EMIR (as well as in the UK due to agreement with the PRA) and so its available data is broader than publicly available information
 - It will consider how best to communicate its assessment of liquidity with the market.

Impact assessment

- It was queried why is EIOPA testing +/- 10bps for the euro in the impact assessment when the analysis suggests the observed difference is 5bps?
 - This was noted to refer to the expected maximum impact which would arise if the proximity precondition was met.