15th November, 2021

Letter from the Chairman of the EUR Risk Free Rates Working Group to the European Commission

Dear Mr Lueder,

I am writing to you on behalf of the Euro Risk Free Rates Working Group ("RFRWG") with regards to discussions on the potential designation of statutory replacement rates for GBP LIBOR and JPY LIBOR.

An agreed action in the WG meeting held on 1 July 2021 was to convene a task force to consider solutions for GBP and JPY LIBOR contracts referencing the 1, 3, and 6 months tenors of the mentioned rates for which active transition or updating contractual language to include robust fallbacks will not be possible by the end of 2021 ("tough legacy"). UK authorities have announced that they will mandate IBA to continue publishing GBP LIBOR and JPY LIBOR beyond the end of 2021 under a revised (synthetic) methodology, but have stated that the rates will no longer be representative of their underlying interest, and have limited publication to one year, with an annual review for synthetic GBP LIBOR for up to ten years. As a result, market participants and clients would face uncertainty on the future performance of their contracts. This may lead to confusion, the need for parties to implement divergent operational solutions, and legal uncertainty.

The outcome of the Task Force discussion and the proposal supported by the RFR WG is to align the approach taken for tough legacy contracts under EU law with that adopted by the UK, which is the use of a synthetic LIBOR for GBP and JPY LIBOR referencing contracts and the adoption of specific legislation providing legal certainty to contracts linked to synthetic LIBOR. The alignment of the EU's approach with that of the UK will provide a consistent approach for all tough legacy contracts. However, such alignment creates certain challenges within the legal framework of the EU Benchmark Regulation (BMR), compared to the legislative solution pursued in the UK.

The RFR WG and Task Force are of the view that within the remit of the EU BMR, full legal certainty can only be achieved with the designation of a statutory replacement rate. To ensure alignment with the UK approach, several options to designate a replacement rate have been identified and discussed in the Task Force and the RFR WG, including referring to the methodology/components underlying the synthetic LIBOR (i.e. term RFR plus ISDA spread). There was agreement that all of the foregoing options create certain challenges in terms of either full alignment with the UK approach or operational aspects (including the fact there is no certainty whether synthetic LIBOR will continue to be published after the end of 2022).

We are open to further discussion on the most appropriate approach under these circumstances.

The RFR WG recognises that the primary objective of market participants should be the active transition from GBP and JPY LIBOR to SONIA and TONA (or TORF) respectively. Any decision made by the Commission to designate statutory replacement rates should not impede the progress of market participants to actively transition to the risk-free rates. Furthermore, the RFR WG is cognisant of the importance of statutory replacement rates to not displace bilateral amendments or suitable fallback provisions agreed between parties governed under EU law, as outlined in Article 23b(3) of the revised Benchmarks Regulation. In combination with ongoing industry initiatives, this designation will maintain the ongoing market integrity in the EEA when both GBP and JPY LIBOR cease to be representative of the underlying interest after this year and further discontinued in the short/medium term, and also mitigate the specific risks and potential contingencies highlighted in the recitals of the revised Benchmark Regulation in relation to the LIBOR cessation.

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On behalf of the RFRWG, I would like to highlight the importance of having certainty about relevant action **as soon as practicable,** so market participants can focus on the deliverables required to achieve a successful transition away from GBP and JPY LIBOR. I look forward to your consideration of our proposal and would welcome further discussion in due course.

Yours Sincerely
James von Moltke
Chairman of the EUR Risk Free Rates