Minutes of the Working Group on Sterling Risk-Free Reference Rates

26 January 2021

Virtual meeting

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7. Bond Market Transition
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Standing items

1. The Chair welcomed attendees and noted remaining work on LIBOR transition ahead of end-2021, building on the good progress that the market has made.
2. The Working Group's competition law counsel gave a competition law reminder. The Chair noted that the minutes of the previous meeting had been approved via written procedure and were available on the Working Group's webpage.

Review of Progress

Update on RFRWG Publications

3. The Chair outlined a number of publications from the Working Group in December and January. Most notably, the Working Group's Roadmap reiterated its recommended timeline for new business and legacy exposures to shift away from LIBOR. After end-Q1 2021, the recommended milestone was for new cash products that expire beyond the end of 2021 to no longer reference GBP LIBOR. To support this, a number of Working Group publications have sought to remove remaining barriers to cash market transition.
4. Alastair Hughes (Bank of England) highlighted that the Working Group Roadmap had the support of the official sector. The FCA and the Bank of England will work with industry to overcome remaining obstacles to transition. In particular, supervisors of regulated firms will continue to expect transition plans to be executed in line with industry-recommended timelines. In the context of ongoing benchmark reform, the Bank of England intended to issue a consultation on clearing obligations for SONIA swaps with maturities longer than 3 year. In addition, the Prudential Regulation Authority was consulting on Solvency II Technical Information until 31 March 2021.

Update on ISDA Protocol

5. ISDA provided an update on its IBOR Fallbacks Protocol, which came into effect on 25 January 2021. Approximately 12,700 entities from 80 jurisdictions had adhered to the protocol, which acts to insert robust fallbacks into over-the-counter derivatives, which reference an interbank offered rates such as LIBOR. Firms would still be able to adhere to the protocol, or amend contracts bilaterally with their counterparty, where appropriate. The authorities and the Working Group also continued to encourage the active transition of LIBOR-linked derivatives.
6. Toby Williams highlighted FCA data, which showed that 460 UK entities had adhered to the protocol, covering around 85% of non-cleared GBP LIBOR transactions. Accounting for cleared derivatives, it was estimated that 97% of GBP LIBOR-linked derivatives had fallbacks.

Update on FCA Consultations

7. Edwin Schooling-Latter noted that the FCA's consultations on its potential powers under two

of the new articles (Articles 23A and 23D) that the Financial Services Bill proposed to incorporate into the UK Benchmarks Regulation closed for comment on 18 January. The FCA would publish its finalised Statements of Policy as soon as practicable. Any decision to exercise the FCA's potential new powers under Article 23D in respect of LIBOR would be subject to a separate consultation, including on the composition of a synthetic rate. Any final decision could only be made once the Financial Services Bill was on the statute book and would only come into effect once panel bank LIBOR ends.

8. Edwin Schooling-Latter also outlined the FCA's plans to consult on the permitted use of any synthetic LIBOR rate. This rate would not be intended for use in new contracts, but instead aims to assist with tough legacy contracts. The FCA would consult on its plans for legacy use of any synthetic LIBOR and potential restrictions on new use of any LIBOR settings which remain representative but are ceasing. Working Group members would be invited to discuss the matter further in a series of industry roundtables ahead of the formal consultation. At present, LIBOR exposures vary from those which could be easily converted (e.g. cleared contracts) to those which are clearly tough legacy (e.g. certain bonds or mortgages with non-responsive counterparties).

Term SONIA Reference Rates

Disbanding the Term Rate Sub-Group and Use Case Task Force

9. The Chair noted that both the Term Rate Sub-Group and the Term Rate Use Case Task Force had completed their objectives, with two Term SONIA Reference Rate (TSRR) administrators now providing their rates for use in financial contracts.
10. The RFR Secretariat asked Working Group members for any objections to disbanding the Term Rate Sub-Group and Use Case Task Force. No objections were raised.

FMSB code of conduct for term SONIA reference rates (TSRRs)

11. Following discussions at the December Working Group meeting, the Chair noted the work of the FICC Markets Standards Board (FMSB) to produce a standard for the use of TSRRs. The Working Group understood that the FMSB's intention was to keep its standard aligned with existing Working Group materials, in particular with the Use Cases of Benchmark Rates paper, and remained engaged with members of the Working Group.
12. Members had been invited to comment on the latest draft of the FMSB's standard and discussed what further feedback could be offered from the Working Group as a whole.
13. Appropriate benchmarks for use in syndicated multi-currency loans in particular had generated quite a lot of focus in the FMSB's discussions, due to the somewhat different timelines and approaches to term rates across jurisdictions. It was noted that the Working Group's Use Case paper did not make any case for use of term rates in these products, which typically involved larger amounts and more sophisticated participants and were more likely to be capable of using compounded rates.

14. Members discussed the current draft and the extent of consistency with the existing position taken by the Working Group. One member expressed the view that apart from the proposed exception for multicurrency lending, the Standard was broadly consistent with the Working Group's Use Case paper. Another member added that further work was needed internationally to encourage a consistent use of term RFRs, which could reduce divergence within multicurrency facilities.
15. One member felt that the multicurrency lending exemption was not a significant divergence from the Working Group's objectives. However, another member queried whether expanding use of TSRRs could undermine liquidity in markets using overnight SONIA compounded in arrears.
16. Edwin Schooling-Latter reiterated the need for GBP markets to be based on overnight SONIA, compounded in arrears, where possible. This included areas such as multicurrency loans. Overall, however, the draft standard appeared to be consistent with the Working Group's Use Case paper.
17. The transparency draft of the FMSB standard was expected to be released for public comment in February, at which point the Working Group would consider issuing a statement to help highlight the work and encourage market engagement.
18. The Chair's Office also outlined some further pieces of work from the FMSB. These would examine conduct in the transition of legacy LIBOR exposures and more general considerations of LIBOR in the structured products market.

Update from the Communications Sub-Group

19. Phil Lloyd (Co-Chair, Communications Sub-Group) commented that the Working Group's communication through its website, newsletter, and LinkedIn was well-established. Going forward, the Working Group would seek further support from trade associations to deliver messages to targeted groups, including through any virtual events.
20. In line with the Working Group's Roadmap, another messaging priority would be the active transition of LIBOR exposures wherever possible. The work of the Infrastructure sub-group regarding fallback operationalisation was likely to underscore the role of active transition in ensuring smooth operational transition away from LIBOR.
21. A further priority for communications would be encouraging borrower readiness for transition away from LIBOR in the loan market. The sub-group was considering a borrower survey to inform its engagement initiatives. One focus was likely to be providing content to advisory firms, to support that they are confident to advise on SONIA lending facilities and robust switch language in lending contracts.
22. There was broad agreement that the Working Group should remain focused on communicating its outputs effectively, with the Communications Sub-Group playing a role in making the technical content accessible to all market participants.

Derivative Market Transition

Linear derivatives – Paper on Q1 timeline & risk management exceptions

23. Chirag Dave (Co-Chair, Pension Funds, Insurance Company and Asset Manager Sub-Group) outlined that a discussion group of Working Group members had been looking to provide further clarity around the exception for “risk management of existing positions” in the Working Group’s recommended milestones for ceasing initiation of new LIBOR-linked derivatives.
24. The general ethos of these was that the use of LIBOR should only be for risk reducing activity. It was proposed that interdealer outright swaps move entirely to SONIA, with single currency basis swaps traded as necessary to manage risk. This approach, in combination with exemptions for client activity, was intended to enable market participants to continue to efficiently actively transition away from LIBOR.
25. Arif Merali (Bank of England) noted that, according to the Working Group’s proposed statement, the exceptions would be strictly limited and aimed to prevent any unintended consequences of a total cessation of new linear LIBOR derivatives, including a potential impact on other benchmarks such as swap rate fixings and to facilitate active transition. Although the Working Group recognised that firms cannot necessarily assess clients’ intentions when making LIBOR trades, supervisors would be engaging with firms to understand any LIBOR trading which took place after the relevant Working Group milestone. Regarding futures, Arif Merali noted that it was broadly accepted that work would be required beyond the Q1 milestone to shift new business from LIBOR to SONIA.
26. LCH highlighted that in the event of a change in liquidity of LIBOR versus SONIA, LCH could conduct a liquidity survey to inform updates to its risk model parameters.
27. The Chair requested that members provide comments on the draft statement by 5 February 2021.

Non-Linear Derivatives

28. Bob Goodfellow (Co-Chair, Non-Linear Derivatives Task Force) provided commentary on the position of the SONIA non-linear derivatives market. Although new business activity and price discovery had increased, LIBOR activity continued to dominate. The Working Group had worked to enable infrastructure vendors to support SONIA swaptions where necessary, whilst a non-linear “SONIA first” initiative could act to shift liquidity at some point in Q2.
29. Regarding legacy LIBOR-linked non-linear derivatives, Bob Goodfellow highlighted that benchmarks such as the GBP LIBOR ICE Swap Rate (the GBP LIBOR ISR) would no longer fix following the end of 2021. The Non-Linear Derivatives Task Force had developed a suggested formula that could be used to produce a replacement swap fixing (based on SONIA swap rates) to settle contracts that reference the GBP LIBOR ISR after the end of 2021.
30. ISDA highlighted that it would work with the Non-Linear Derivatives Task Force to consider an efficient way of hardwiring a replacement swap fixing into derivative contracts. Bob

Goodfellow agreed that the Non-Linear Derivatives Task Force would look to finalise the suggested formula for publication by the Working Group.

Loan Market Transition

End-Q1 2021 milestone: Cease new LIBOR lending expiring beyond end-2021

31. The Chair emphasised that the Working Group's recommended milestone to end new GBP LIBOR lending was fast-approaching, marking a critical step in the journey away from LIBOR. The Working Group's milestones have been visible to firms for some time and Working Group members are expected to support transition in the loan market.
32. Jamieson Thrower (Chair, Loan Enablers Task Force) noted significant progress in the development of SONIA lending, particularly in the bilateral GBP lending market. In the syndicated market, lenders continued to make extensive use of "agree to agree" mechanics, leaving a significant population to be actively transitioned in the remainder of 2021. Engagement with lenders outside of the Working Group would be a crucial part of resolving this remaining challenge. The Loan Enablers Task Force proposed to reinforce the Working Group's recommended timeline in a short statement, to support market clarity on established practices such as conventions. Other communications led by the task force would focus on education for borrowers and promoting awareness of relevant market infrastructure such as indices and calculators.
33. Edwin Schooling-Latter commented on the FCA's work to monitor GBP lending markets. As a supervisor, the FCA would be examining firms' governance and capability to offer SONIA products. The end of GBP LIBOR, which was expected to be imminent, made it legitimate for syndicate lenders to encourage RFR-based syndicates. Although USD markets may be slightly slower in transitioning, the expected timeline for ending new use of LIBOR in both currencies was closely aligned, making it critical that progress in expanding RFR-based lending was sustained.
34. Alastair Hughes reiterated that the lending market should not be dictated by the progress of the slowest firms and supervisors would take a keen interest in any remaining GBP LIBOR lending after the end of Q1 2021.
35. The ACT noted that corporates were reliant on syndicate banks' readiness to provide RFR-linked lending and expressed support for any initiative that would ensure banks are ready for the end-Q1 milestone.
36. The LMA queried whether the end-Q1 milestone should be made more flexible, by providing that the incorporation of switch mechanisms would meet the milestone, primarily to ensure that funds continue to flow to the real economy. The Chair expressed some reluctance to relax such a significant milestone. Edwin Schooling-Latter recognised the need to allow lending to continue, but emphasised that there was a clear expectation that lenders should be capable of offering SONIA-linked loans at scale. The Chair of the Loan Enablers Task Force concurred, noting that the Working Group should be trying to provide solutions to any market

difficulties, rather than relaxing a long-standing milestone.

RFR calculator paper update

37. Siobhan Clarke (Co-Chair, Infrastructure Sub-Group) noted an update to the Working Group's calculator paper. Although the Working Group did not propose to endorse any one particular calculator, it intended to encourage calculator providers to give more information to the public about their products. The updated paper aimed to suggest guidelines for vendors on the governance and transparency that users may expect to be present for any calculator product.
38. The Chair requested any final comments from members by 5 February 2021, ahead of publication of the updated paper.

Bond Market Transition

Outstanding Challenges in the Bond Market

39. Paul Richards (Chair, Bond Sub-Group) noted that the Bond Market had used overnight SONIA, compounded in arrears, in new Floating Rate Note issuance for some time. Remaining challenges for the market related primarily to legacy bonds, which needed to be amended individually through a consent solicitation process in order to be actively transitioned. The market was also keen to mitigate litigation risk as LIBOR was wound down, which interacted with the use of any synthetic LIBOR rate. More widely, USD LIBOR contracts governed by English law would need to be considered as USD LIBOR comes to an end.
40. Edwin Schooling-Latter noted that it remained too early to decisively state the FCA's position with respect to USD LIBOR. Market feedback on this issue would likely be sought in 2022 or 2023.

Consultation on the successor rate for type 2 & 3 bond fallbacks

41. Paul Richards introduced a proposed Consultation Paper from the Working Group, intended to seek feedback on whether it would be helpful for the Working Group to make a recommendation on a successor rate to GBP LIBOR for bonds upon the occurrence of a permanent cessation event or a pre-cessation event, and to seek feedback on the preferred successor rate to be recommended if so.
42. Toby Williams outlined the process for the consultation, with a 6-week public comment period. Working Group members and other market participants were strongly encouraged to respond to this process. Following this period, the RFR Secretariat would provide a factual summary of the consultation results, to inform a discussion at the Working Group on how to proceed.
43. The Chair requested any final comments from members by 29 January 2021, ahead of publication.

AOB

44. The Investment Association (IA) noted that they planned to publish a letter, highlighting investment managers' support for transition away from LIBOR in the bond market. The IA's members were also encouraged to engage directly with the relevant issuers.
45. Edwin Schooling-Latter welcomed the IA initiative. Mutually agreed conversion from LIBOR to risk free rates plus spreads, consistent with industry recommendations on transition arrangements, could enable both the bond's issuer and holders to avoid the uncertainty they would face upon LIBOR's proposed cessation. It would also allow conversion to the market standard of the RFR compounded in arrears that has now developed in bond markets – an advantage which synthetic LIBOR could not provide.

Private sector attendees

Tushar Morzaria	Barclays (Chair)
Paul Mansour	Barclays (Chair's Office)
Andreas Giannopoulos	Barclays (Chair's Office)
Helen Robinson	Barclays (Chair's Office)
Alan Coutts	Aberdeen Standard Investments
Shaun Kennedy	Associated British Ports
Sarah Boyce	Association of Corporate Treasurers
Alexandre Papadacci	AXA
Katherine Ashdown	Bank of America
Snigdha Singh	Bank of America
Doug Laurie	Barclays
Jonathan Brown	Barclays
Robert Mitchelson	Blackrock
Greg Olsen	Clifford Chance (Competition Law Counsel)
Zsolt Szollosi	Credit Suisse
Michael Barron	Deutsche Bank
Simon Goodwin	Deutsche Bank
Martial Collet-Billon	Deutsche Bank
Axel van Nederveen	EBRD
Chirag Dave	Goldman Sachs
John O'Sullivan	HSBC
Matthew Horton	ICE Futures Europe
Paul Richards	ICMA
Robert Gall	Insight Investment

Galina Dimitrova	The Investment Association
Rick Sandilands	ISDA
Kari Hallgrimsson	JP Morgan
Philip Whitehurst	LCH
Guy Whitby-Smith	Legal & General Investment Management
Ian Fox	Lloyds Banking Group
Clare Dawson	Loan Market Association
Siobhan Clarke	M&G
David Covey	M&G
Kwok Liu	National Grid
Tom Dyson	Nationwide
Bob Goodfellow	NatWest Markets
Phil Lloyd	NatWest Markets
Jamieson Thrower	NatWest Markets
Donal Quaid	NatWest Markets
Frances Hinden	Shell
Hannah Faith	UBS
Daniel Cichocki	UK Finance
Stephen Pegge	UK Finance

Official sector attendees

Alastair Hughes	Bank of England
Peter Balint	Bank of England
Arif Merali	Bank of England
Tom Horn	Bank of England
Nicole Stirk	Bank of England
Alieda Moore	Bank of England
Jugvinder Singh	Bank of England
Raza Rehman	Bank of England
Edwin Schooling Latter	Financial Conduct Authority
Helen Boyd	Financial Conduct Authority
Heather Pilley	Financial Conduct Authority
Anne-Laure Condat	Financial Conduct Authority
Toby Williams	Financial Conduct Authority
Devid Mazzonetto	Financial Conduct Authority
John Wadsworth	Financial Conduct Authority