Summary of public consultation on Recommendation of the NWG on applying a fallback rate for the WIBOR benchmark in interest rate derivatives

Document of the National Working Group for benchmark reform

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Background

The subject of the public consultation was a proposal for a *Recommendation of the NWG on applying a fallback rate for the WIBOR benchmark in interest rate derivatives*. The Recommendation was prepared by the National Working Group for benchmark reform (NWG) based on analyses and discussion of experts. The Recommendation aims to present the recommended method of replacing the WIBOR benchmark with an Alternative Benchmark in WIBOR-based interest rate derivatives in the event where a Fallback Trigger of a permanent nature occurs.

The Recommendation is one of the deliverables of the Preparatory Phase of the Roadmap for the replacement of WIBOR and WIBID benchmarks with the WIRON index.

Conclusions from the consultation

In the opinion of the NWG experts, the comments received on the draft Recommendation do not require any modification of the document being consulted on.

In order to address all doubts and being aware of the importance of raising awareness among market participants, the NWG experts provided a detailed answer to the comments. Please see the answer in section 'Summary'.

Scope and period of the consultation

The consultation on the draft document was held by:

1. publishing the following communications on the KNF website in the section dedicated to the NWG's activities:
    - https://www.knf.gov.pl/dla_rynku/Wskazniki_referencyjne/aktualnosci?articleId=82352&p_id=18
    - https://www.knf.gov.pl/en/news?articleId=82354&p_id=19
2. sending an invitation to the consultation and the document to professional associations of financial market entities

The consultation ran from 26 May 2023 to 13 June 2023.

All interested parties could send their comments to a dedicated e-mail address: konsultacjengr@knf.gov.pl.

Summary of the comments submitted during the public consultation and the NWG's answers

Until 13 June 2023, one opinion was received from a professional association.

Association's comment:

'As regards the proposal, it is important that the *Recommendation of the NWG on applying a fallback rate for the WIBOR benchmark in interest rate derivatives* is consistent with the recommendation on applying a fallback rate for the WIBOR benchmark for issues of floating-rate debt instruments. Derivatives are often used to hedge interest rate risk for floating-rate bonds issued. This is why it is of key importance that an approach to replacing the WIBOR reference rate is identical for both types of instruments. In case of any discrepancies, there is a risk of differences in the cash flows generated by those instruments and the risk of the hedge becoming ineffective. Another consequence may be the ineffectiveness of hedge accounting applied to recognise derivatives in books.'

Opinion of the NWG experts:

Responding to the comment submitted during the public consultation on a proposal for a *Recommendation of the NWG on applying a fallback rate for the WIBOR benchmark in interest rate derivatives* (hereinafter: 'Recommendation on derivatives'), we would like to clarify that the design of the Recommendation is of a general nature and refers primarily to the generally recognised standard for the conversion of derivatives, in accordance with the ISDA standard. Considering the particular conditions around certain interest rate derivative transactions, including the case you have mentioned, where a derivative transaction hedges a floating-rate bond, the Recommendation indicates that it does not restrict the option of financial market participants to apply different methods of converting WIBOR-based interest rate derivatives. In this context, the Recommendation also emphasises that it is not contradictory to the approach developed in other streams, that is in particular to the *Recommendation on the rules and methods of conversion of legacy issues of WIBOR-based debt instruments* (hereinafter: 'Recommendation on bonds').

It should also be noted that the Recommendation on derivatives provides, in point 2, for a different use of WIRON, including with 5-business-day lookback with observation period shift in relation to the interest period.

The provisions of the recommendation on bonds go in a similar direction, as they recommend the introduction of fallback clauses determining the use of WIRON, with 5-business-day lookback with observation period shift in relation to the interest period.

Therefore, both of the above-mentioned recommendations create conditions for allowing the conversion of bonds and hedging instruments in a way to avoid discrepancies and potential ineffectiveness.