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Answers of the European Financial Congress[1] in relation to the European Commission's consultation regarding the designation of a statutory replacement rate for CHF LIBOR[2]

Methodology for preparing the answers

The answers were prepared in the following stages:

Stage 1
A group of experts from the Polish financial sector were invited to participate in the survey. They received the EC's consultation document and a form with consultation questions translated onto in Polish. The experts were guaranteed anonymity.

Stage 2
The European Financial Congress obtained 24 responses from experts representing:
- commercial banks
- cooperative banks
- consulting firms
- the academia.

Stage 3
The survey project coordinators from the European Financial Congress prepared a draft synthesis of opinions submitted by the experts. The draft synthesis was sent to the experts participating in the survey with the request to propose modifications and additions as well as marking the passages they did not agree with.

Stage 4
On the basis of the responses received, the final version of the European Financial Congress' answers was prepared.

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[1] European Financial Congress (EFC – www.efcongress.com). The EFC is a think tank whose purpose is to promote debate on how to ensure the financial security and sustainable development of the European Union and Poland.
[2] https://ec.europa.eu/info/sites/default/files/business_economy_euro/banking_and_finance/documents/2021-chf-libor-rate-consultation-document_en.pdf

Answers of the European Financial Congress to the consultation questions

1. ON THE EFFECTIVE NEED FOR A REPLACEMENT FOR CHF LIBOR

Pursuant to article 23a of the EU BMR, the Commission may only designate replacement rates for third-country benchmarks "*if their cessation or wind-down would significantly disrupt the functioning of financial markets in the Union or pose a systemic risk to the financial system in the Union.*".

Question 1. Do market participants agree that the situation as described above, requires that the Commission exercises the statutory replacement powers for the CHF LIBOR?	
X	Yes
☐	No
☐	No opinion

In our opinion, the discontinuation of the CHF LIBOR creates a significant risk of disruption to financial markets in the EU and thus meets the conditions enabling the Commission to exercise its statutory power to designate a replacement rate. Looking through the prism of the Polish market, loans based on the LIBOR CHF constitute a significant part of the mortgage loans at banks. At the end of 2020, there were still more than 400 thousand CHF LIBOR denominated mortgage loans agreements in the banks' portfolios. The volume of these loans amounted to approximately PLN 99 billion, which accounted for approximately 21% of the entire mortgage loan portfolio. In particular, the risk related to a significant share of the CHF LIBOR loans in mortgage portfolio results from the fact that these loans were granted mainly in 2005-2008, i.e. before the introduction of BMR regulation. As a result, these agreements do not contain fallback clauses that would regulate the discontinuation of CHF LIBOR. In this situation, the lack of a statutory replacement rare for CHF LIBOR would result in the necessity to sign amendments by clients, which in the context of low responsiveness indicated by market participants may create additional risk for the continuation of loan agreements.

Designating replacement rate for CHF LIBOR will be a systemic limitation of the potential risk of destabilizing the banking sector in the future and will be beneficial both for the banks themselves and their clients, not only for those who repay mortgage loans denominated or indexed to CHF. The statutory designation of replacement rate for LIBOR CHF will, on the one hand, contribute to the smooth management of the existing loan portfolio based on the LIBOR CHF, and, on the other hand, will ensure fair treatment of consumers on the market. As a result, it will contribute to increasing the safety of the banking sector and reduce the risk of significant disruption in the financial market throughout the European Union.

Considering the fact that loan agreements do not contain only 3M CHF LIBOR, market participants indicate the need to systematically designate a replacement rate for all currently used maturities, including in particular 6M.

2. ON THE FAIRNESS AND ACCEPTABILITY OF THE SOLUTION RECOMMENDED BY THE SWISS NATIONAL WORKING GROUP

Question 2. Do consumers, small and medium enterprises and relevant consumer bodies agree that the proposed replacement rate (3M SARON calculated as a compounded SARON under a last reset methodology) plus the ISDA adjustment spread (calculated as a historical median approach over a five-year lookback period) is a fair and equitable solution for a replacement of CHF LIBOR in mortgages and small business loans and consumer credit agreements?	
X	Yes
☐	No
☐	No opinion

In our opinion, this situation interferes with the contractual relationship between customer and bank, and may not always be well perceived by consumers and small enterprises. Nevertheless, the proposed replacement rate plus the ISDA adjustment spread is currently the only acceptable solution and, with its proper implementation, should be accepted by the entities indicated in the question as a fair and equitable solution and, consequently, ensure the continuity of loan agreements. However, it is important that the proposed replacement rate maintains similar business conditions (ie that the new benchmark is at a stable and comparable level to the CHF LIBOR). It is crucial that there is no imbalance and that one side does not gain at the expense of the other.

The use of the so-called last reset methodology will enable the fulfilment of the obligation to inform the client about the amount of interest before the beginning of the interest period. Due to the application of the spread, at the moment of switching from LIBOR CHF to SARON rate, there will be no significant change in the client's liability, hence it can be assumed that this solution will be considered neutral in the bank-client relationship.

Market participants also regard the above proposal as the best available solution. First, the SARON index is provided under BMR regime. Second, setting the amount of the spread based on the methodology of ISDA as an independent institution minimizes the risk of future legal disputes. This is a much safer and more reliable approach than a situation in which banks would calculate the amount of the correction on their own, which could potentially lead to different results resulting from different formulas, time scope and other assumptions. The limitation, however, is the lack of research by consumer groups that would confirm this thesis.

Market participants indicate that an important factor for the acceptance of the proposed solution is the financial education of consumers, hence the very important role of a properly prepared and conducted information campaign.

3. ON THE COMPATIBILITY OF THE CHOSEN METHODOLOGY WITH EU AND MEMBER STATES LAWS PROTECTING CONSUMERS

Question 3. Do market participants agree that the proposed calculation method (so called last reset) is compatible with the requirements of the MCD, the CCD, Directive 93/13/EEC and of other legislation protecting consumer credit and national implementation laws and with any other applicable legislation?	
X	Yes
☐	No
☐	No opinion

In our opinion, the proposed calculation method (so called “last reset”) is compatible with the requirements of Directive 2014/17 / EU, Directive 2008/48 / EC, Directive 93/13 / EEC as well as Polish implementation laws. SARON calculations based on historical data makes it possible to meet the requirement to inform the client about the amount of instalments at the beginning of the interest period. Nevertheless, it is important that European and national regulators are responsible for ensuring that the implemented legal solutions are consistent with each other, and that the proposed change is introduced in the legislative formula as an irrefutable legal act.

It is also necessary for consumer protection bodies to take initiatives endorsing that the method of determining the new index is fair, reliable and does not infringe upon the interests of consumers.