sifma®

Invested in America

July 15, 2016

By Electronic Mail to (arrc@ny.frb.org)

Re: <u>Interim Report and Consultation of the Alternative Reference Rates Committee</u>

The Securities Industry and Financial Markets Association ("*SIFMA*")[1], including SIFMA's Asset Management Group ("*SIFMA AMG*")[2], appreciates the opportunity to respond to the Alternative Reference Rates Committee ("*ARRC*") in connection with the consultation on potential alternatives to U.S. dollar LIBOR (the "*Consultation*"). SIFMA supports the overarching goals of the ARRC's Interim Report and Consultation, which seeks to identify a set of alternative reference interest rates that are more firmly based on transactions from a robust underlying market and that comply with emerging standards, and to identify an adoption plan with means to facilitate the acceptance and use of these alternative rates.

<u>SIFMA/GFMA Support for Benchmark Reforms</u>

The Consultation highlights that in recent years, global regulators have recognized that the secular decline in wholesale unsecured short-term funding by banks poses serious structural risks for unsecured benchmarks. SIFMA, as the U.S. regional member of the Global Financial Markets Association ("*GFMA*")[3], was an early proponent of global reform efforts with the November 2012 publication of its Principles for Financial Benchmarks (the "*GFMA*

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[1] SIFMA is the voice of the U.S. securities industry, representing the broker-dealers, banks and asset managers whose 889,000 employees provide access to the capital markets, raising over $2.4 trillion for businesses and municipalities in the U.S., serving clients with over $16 trillion in assets and managing more than $62 trillion in assets for individual and institutional clients including mutual funds and retirement plans. SIFMA, with offices in New York and Washington, D.C., is the U.S. regional member of the Global Financial Markets Association (GFMA). For more information, visit http://www.sifma.org.

[2] SIFMA AMG's members represent U.S. asset management firms whose combined global assets under management exceed $34 trillion. The clients of SIFMA AMG member firms include, among others, tens of millions of individual investors, registered investment companies, endowments, public and private pension funds, UCITS, and private funds such as hedge funds and private equity funds.

[3] The Global Financial Markets Association (GFMA) brings together three of the world's leading financial trade associations to address the increasingly important global regulatory agenda and to promote coordinated advocacy efforts. The Association for Financial Markets in Europe (AFME) in London and Brussels, the Asia Securities Industry & Financial Markets Association (ASIFMA) in Hong Kong and the Securities Industry and Financial Markets Association (SIFMA) in New York and Washington are, respectively, the European, Asian and North American members of GFMA. For more information, visit http://www.gfma.org.

Principles").[4] GFMA later participated in the different consultations conducted by global regulatory bodies such as the Financial Stability Board ("*FSB*"), as well as by the International Organization of Securities Commissions ("*IOSCO*") regarding the market standards and principles for benchmarks.

GFMA supports the work by the FSB to develop reform proposals for major interest rate benchmarks that are considered to play the most fundamental role in the global financial system. Furthermore, GFMA has endorsed IOSCO's Principles for Financial Benchmarks (the "*IOSCO Principles*"),[5] published in July 2013, which has become a global market standard for the benchmark process. SIFMA supports the overall work by the ARRC and its mandate. In particular, we note the appropriate focus on derivatives markets, given the dominance of derivatives in products referencing LIBOR.

Potential Alternative Reference Rates

As noted in the Consultation, the scarcity of underlying transactions poses a continuing risk of discontinuity or even the cessation in the production of U.S. dollar LIBOR. In response, the ARRC considered a range of alternatives against criteria aligned with the IOSCO principles and we generally agree with the framework for that evaluation and the suitability or limitations of some alternatives. The ARRC has preliminarily narrowed the list of potential rates to two that it considers to be the strongest alternatives, the **Overnight Bank Funding Rate** ("*OBFR*") and some form of **overnight Treasury general collateral repurchase agreement ("*GC repo*") rate**.

SIFMA believes that although these rates appear to be appropriate alternatives, the most important factor to consider is the underlying liquidity. Therefore, it is important that the ARRC engage with end-clients, including pension funds, insurance companies, direct investors, and issuers, to ensure that they understand and weigh in on the alternatives. Asset managers and other market participants will be unable to move to a new rate until clients ask for the move, or until there is sufficient liquidity to cause an asset manager to ask its end clients to permit the move.

Further, given the inherent need to develop a sufficiently liquid market in any potential alternative benchmarks, it is imperative that the proposed rates have sufficient publication histories to facilitate the diligence required to transition to a new benchmark rate and to allow for an informed choice among alternatives. Therefore, it may be premature to further narrow the potential alternatives at this junction. The Federal Reserve Bank of New York only began its publication of OBFR on March 2, 2016, and there is currently no published overnight Treasury GC repo rate as described above. However, we do believe that

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[4] GFMA's Best Practices for Financial Benchmarks, GFMA Provides its Updated Principles for Financial Benchmarks to the Global Regulatory Community | Correspondence | GFMA

[5] IOSCO Principles for Financial Benchmarks, http://www.iosco.org/library/pubdocs/pdf/IOSCOPD415.pdf

the development of a GC repo rate could prove advantageous more generally to the market, while permitting for a more informed future choice or preference.

Transition Strategies

SIFMA generally agrees with the ARRC's initial transition strategy (the "*paced transition*") that does not identify a specific timeline but rather identifies the essential elements necessary to minimize disruption while seeking to create a robust source and demand for underlying liquidity. We are mindful that a timeline may only emerge as the initial elements materialize to permit confidence in a more finite schedule. As the Consultation notes, "If adopted, a paced transition would represent a first step in creating a liquid market for the alternative rate, but further work will be required – following consultation and close involvement with end users – both in developing the details of an initial transition strategy and in planning for a full transition strategy that would move a more significant portion of the derivatives markets away from LIBOR to the new rate." We highlight, however, that the wide use of LIBOR in many types of financial agreements necessitates a long transition. Further, while successful implementation of the paced transition strategy would likely include voluntary trading by ARRC member banks and other market participants sufficient to achieve a critical mass of liquidity, we reiterate that the pace of a broader industry transition will ultimately rest with end users.

Additionally, it is noted that the ARRC envisions a paced transition focusing on new transactions rather than a "big bang" that would seek to change existing trades – thereby minimizing market disruptions while still creating a robust source of demand for and underlying liquidity in hedging markets for the new rate. As mentioned above, LIBOR is currently used in many types of agreements for many types of transactions. The "repapering" of these agreements could be cumbersome and potentially disruptive to market functioning. Market participants will need the flexibility to make judgements about the timing of any transitions to a new benchmark for new contract agreements, but also to judge whether and when it may be in their best interests to transition existing agreements to any new benchmark to mitigate risks or frictions.

End User Input

As noted above, SIFMA appreciates the efforts by the ARRC to seek input from market participants both through this Consultation and the June industry roundtable. Going forward, SIFMA encourages the ARRC to directly reach out to end clients to ensure that ARRC receives robust feedback from a diverse and large number of constituents. In many cases, the true end user will provide the most valuable feedback on everything from the wide-reaching consequences of moving from LIBOR to the likelihood that a new rate will develop sufficient liquidity.

SIFMA appreciates the opportunity to comment on the ARRC's Consultation and would be pleased to discuss any of these comments in greater detail, or to provide any other assistance that would be helpful. We applaud the leadership provided by the AARC and the Federal Reserve Bank of New York in furthering these reform discussions. If you have any questions or require further information, please contact either Sean Davy, Tim Cameron, or Rob Toomey at sdavy@sifma.org, tcameron@sifma.org, or rtoomey@sifma.org respectively. Thank you again for your consideration of our comments.

Regards,

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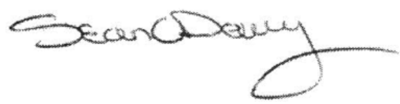

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