# IBOR TRANSITION NEWSLETTER

Edition 12: November 2020



## THE PUZZLE COMES TOGETHER

Welcome to our Newsletter. This is our twelfth edition, and it provides an update on the transition away from the London Interbank Offered Rate (LIBOR) and other Interbank Offered Rates (IBORs). With the end of 2021 fast approaching, these newsletters aim to raise awareness of key developments on an ongoing basis. This will be our last newsletter until January 2021. We wish you a happy holiday season. The key topics for this month are:

- **FURTHER PROGRESS MADE**
- **IBA ANNOUNCEMENT**
- **LMA UPDATE ON PRE-CESSATION**
- **LEGISLATION & TOUGH LEGACY**
- **OTHER SUNDRIES**
- **A CLOSER LOOK: ISDA FALLBACKS SUPPLEMENT AND PROTOCOL**

Please contact your Relationship Team if you have any questions or queries on the contents.

## FURTHER PROGRESS MADE

The past two months have seen some key milestones passed on the road towards IBOR transition. Back in July, in a speech to an International Swaps and Derivatives Association (ISDA) Symposium, Edwin Schooling Latter, the Finanical Conduct Authority's (FCA) Director of Markets, raised the possibility that there could be announcement of LIBOR non-representativeness and/or cessation by year end. We have now seen the publication of ISDA's IBOR Fallbacks Supplement and Protocol on 23 October beginning to catalyse preparations for LIBOR's end. International bodies such as the Financial Stability Board, in its October release of the Global Transition Roadmap, are providing information directly to inform those with exposure to LIBOR benchmarks on the steps they should be taking between now and the end of 2021. Most recently, the FCA published a consultation on their proposed new powers in relation to a "Synthetic LIBOR" and the LIBOR administrator, ICE Benchmark Administration (IBA) signalled that consultations on LIBOR cessation will be published in the near future. The various pieces of the transition puzzle are now quickly coming together.

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## IBA ANNOUNCEMENT

ICE Benchmark Administrator (IBA) has announced that it will consult in the near future on its intention to cease publication after 31 December 2021 on LIBOR settings for key tenors of GBP, EUR, CHF, and JPY. Regarding the notable absentee, USD LIBOR, IBA advised that discussions with the FCA, and other official sector bodies and the panel banks are continuing with regards to its future and further announcements will be made when these discussions conclude. The IBA stressed that this does not offer any certainty or guarantee that it will be able to publish any USD LIBOR settings after 31 December.

Most importantly, the IBA was careful to highlight this was not an announcement that it will either continue or cease the publication of any of the LIBOR settings after 31 December 2021. Such an event would have implications for certain financial contracts. Instead, the IBA made clear it expects to make separate announcements in this regard following the outcome of the consultations, and subject to any rights of the FCA to compel IBA to continue publication.

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## LMA UPDATE ON PRE-CESSATION

The Loan Market Association (LMA), in anticipation of the ISDA publication, released notes on a revised Replacement of Screen Clause and Pre-cessation Trigger for loan agreements. As the title suggests, the notes provide a template for a new trigger to fallbacks based on a determination of "non-representativeness" made by the FCA. These notes may be included in loan documentation, particularly where there are related derivative transactions using the same trigger.

The LMA in October also published an updated version of their list of the near risk-free rate (RFR) referencing loans. The list is based on publically available information and seeks to raise awareness of the emerging market in RFR-referencing loans by providing information on the conventions used.

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## MORE REFRENCE MATERIALS

Further market support has been provided by the Bank of England (BoE) Working Group on Sterling Risk-Free rates (RFR WG) who published their RFR and Term Rates Guide; the document provides a summary of freely available independent RFR calculators on the market and the key attributes of Beta versions of Term SONIA Reference Rates (TSRRs) that are currently being published by independent benchmark administrators. This information is intended to be of assistance to both market participants and vendors especially in consideration of whether any amendments may be required to their systems.

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## LEGISLATION & TOUGH LEGACY

Further work is also being conducted on the subject of 'Tough Legacy': those contracts which for a variety reasons it is not possible to transition away from LIBOR. In the UK, the Government laid the Financial Services Bill before Parliament providing detail on the powers to be granted to the FCA to require a change to be made to the methodology of a critical benchmark, such as LIBOR, if it is deemed to no longer be representative. The Bill outlines how the representativeness of critical benchmarks will be assessed for this purpose and how the new powers can be used to help manage any wind-down period. The presentation of this bill follows the UK Government's 23 June statement of intent that it intended to legislate to facilitate LIBOR transition for 'tough legacy' contracts in response to the RFR WG Tough Legacy report published on 29 May. In a latest move, the FCA published a consultation on 18 November covering some of the new powers that they expect to be granted next year; responses are due by 18h January.

In contrast, the US, which has a different legislative framework, is considering imposing a direct change to LIBOR referencing contracts. A New York Senate Bill was introduced on 28 October substantially adopting the language from the proposed legislative solution produced by the Alternative Reference Rate Committee (ARRC) in March 2020. The legislation is expected to be taken up in the legislation session that begins in January 2021. Such an approach does not come without challenges, as the hard wired nature of the switch creates the potential for 'winners and losers' and mismatches within portfolios.

Elsewhere, the European Commision (EC) proposals are currently moving through the EU legislative process and expected to enter into 'trialogue negotiations' in mid-November: trialogue negotiations involve the EC, European Parliament, and the Council of the European Union. The proposals enable the EC to select replacement benchmarks for LIBOR or other widely used benchmarks when they cease. The successor rate would be decided by the EC and apply upon certain trigger events, including cessation and non-representativeness.

For a more detailed information about Tough Legacy please see the A Closer Look section of our July 2020 newsletter.

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## OTHER NEWS

Other notable news includes the London Clearing House's (LCH) completion of the Secured Overnight Financing Rate (SOFR) discounting switch. Tom Wipf, Chairman of the ARRC said: "The CCP discounting conversion is a huge milestone in the overall LIBOR transition. We expect this to be the catalyst for a step-change in trading volumes in SOFR derivatives, bringing a transition in the broader market much closer."

An often overlooked area is the European Central Bank (ECB) requirement for enhanced Euro Interbank Offered Rate (EURIBOR) fallbacks to be put in place. These are needed despite the fact that EURIBOR will not cease at the end of 2021. In this regard, on 22 October, the Working Group on Euro Risk-Free Rates (EU RFR WG) signalled the imminent publication of two public EURIBOR consultations which will cover the fallback trigger events and fallback rates for cash products based on €STR. The due date for responses will be 8 January 2021.

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## A CLOSER LOOK: ISDA FALLBACKS SUPPLEMENT AND PROTOCOL

On 23 October ISDA launched the IBOR **Fallbacks Supplement** and **Fallbacks Protocol**. This initiative provides a critical safety net for those market participants that still have exposure to IBORs in the event of cessation. ISDA has prepared this short video to explain what fallbacks are and how they operate.

The **Fallbacks Supplement** amends ISDA's standard definitions to incorporate robust fallbacks for interest rate derivatives linked to certain IBORs and comes into effect on 25 January 2021. From this date all **new derivatives** that reference the ISDA definitions will automatically include these new fallbacks, irrespective of whether parties adhered to the Fallbacks Protocol.

The **Fallbacks Protocol** allows the Supplement to be applied to **existing derivatives** providing that both parties to a trade have signed up to it**.**

ISDA has invited all market participants to adhere to the Protocol. At its launch the Protocol had 257 adherents and this number has more than trebled since. The initiative has received widespread support from regulators globally including the Bank of England who confirmed their own adherence on the 23 October 2020.

Market participants can sign up to the Protocol via the ISDA website. For non-ISDA members the adherence fee of US$500 is waived until 25 January 2021. It will be possible to sign up after that date on payment of the fee.

Lloyds Bank plc, Bank of Scotland plc and Lloyds Bank Corporate Markets plc have adhered to the Protocol.

Alternatively, the fallback terms can be incorporated into existing derivatives contracts by means of a bi-lateral agreement.

It should be noted that active transition to an alternative reference rate before LIBOR cessation is preferred by both regulators and industry. Andrew Bailey, Governor of the Bank of England has said that whilst signing-up to the ISDA Fallbacks Protocol is encouraged, it is 'not a substitute for continuing to move business onto near risk-free rates'. We consider that adhering to the Protocol will be useful, particularly if active transition proves impossible for any reason.

If you need further details on what is required or how the Protocol and fallbacks will operate then please get in touch with your usual contact, or email isdaiborfallbacksprotocol@lloydsbanking.com.

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IBOR Transition Programme
Bank of Scotland Commercial Banking

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