

MEMO# 31885

August 2, 2019

Recent Developments in Benchmark Reform Transition

[31885]

August 2, 2019 TO: ICI Members

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Trading and Markets RE: Recent Developments in Benchmark Reform Transition

We wanted to provide you with a few updates about benchmark reform transition as the market prepares for LIBOR to be discontinued after 2021.

First, as you know, ISDA intends to amend its standard documentation to implement fallback risk-free reference rates (e.g., SOFR) that will apply when certain interbank overnight rates (IBORs), such as LIBOR, are permanently discontinued. In May, ISDA issued a consultation on options for adjusting risk-free rates if fallbacks are triggered for derivatives referencing US dollar LIBOR, Hong Kong's HIBOR, and Canada's CDOR, as well as Singapore's SOR.[\[1\]](#) ISDA recently reported the preliminary results of that consultation.[\[2\]](#) Consistent with the responses to ISDA's consultation last year on fallbacks for derivatives referencing GBP LIBOR, CHF LIBOR, JPY LIBOR, TIBOR, Euroyen TIBOR, and BBSW,[\[3\]](#) the majority of respondents preferred the "compounded in arrears rate" to adjust the overnight risk-free rate. This approach would take into account the relevant risk-free rate over the relevant LIBOR tenor and compound the rate daily over that period.

The consultation also asked about approaches to adjusting the spread between secured risk-free rates and the corresponding IBORs. Consistent with the responses to ISDA's consultation last year regarding the IBORs noted above, respondents preferred the "historical mean/median approach" based on the mean or median spot spread between the

IBOR and the adjusted risk-free rate calculated over a significant, static lookback period (such as 5 years). Based on this feedback, ISDA expects to proceed with developing fallback rates using these adjustments, although final decisions are subject to approval by the ISDA Board Benchmark Committee. Finally, ISDA also announced that it had selected Bloomberg Index Services to calculate and publish adjustments to the fallback rates.^[4]

In addition to the ISDA developments, IOSCO recently issued a statement recommending that all market participants consider their IBOR exposure now and noting regulatory consensus that the transition of most derivatives from IBORs to risk-free rates is a critical issue.^[5] The statement notes the work that ISDA is doing to develop contractual fallback language for new and existing derivatives. IOSCO also notes the ARRC's view that the current SOFR derivatives market in the US does not yet have enough depth to build a reliable, robust, transactions-based, forward-looking rate produced on a daily basis. The ARRC's transition plan expects that there will be a forward-looking SOFR term rate before the end of 2021, depending on the presence of a liquid derivatives market in SOFR.

For your reference, we have included links below to some helpful US resources on benchmark reform issues:

- **Securities and Exchange Commission:** Staff Statement on LIBOR Transition: <https://www.sec.gov/news/public-statement/libor-transition>^[6]
- **Alternative Reference Rates Committee (ARRC):** Transition from LIBOR <https://www.newyorkfed.org/arrc/sofr-transition> and Fallback Contract Language <https://www.newyorkfed.org/arrc/fallbacks-contract-language>
- **ISDA:** Resources on benchmark reform: <https://www.isda.org/category/legal/benchmarks/>

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endnotes

^[1] See *Supplemental Consultation on Spread and Term Adjustments for Fallbacks in Derivatives Referencing USD LIBOR, CDOR and HIBOR and Certain Aspects of Fallbacks for Derivatives Referencing SOR* (May 16, 2019), available at <https://www.isda.org/2019/05/16/may-2019-benchmark-fallbacks-consultations/>.

^[2] See *Preliminary Results of ISDA Supplemental Consultation on Spread and Term Adjustments for Fallbacks in Derivatives Referencing USD LIBOR, CDOR and HIBOR and Certain Aspects of Fallbacks for Derivatives Referencing SOR* (Jul. 30, 2019), available at <http://assets.isda.org/media/2d8f2c0d/92ec53e4-pdf/>.

^[3] See *Preliminary Results of ISDA Consultation on Certain Aspects of Fallbacks for Derivatives Referencing GBP LIBOR, CHF LIBOR, JPY LIBOR, TIBOR, Euroyen TIBOR and BBSW* (Nov. 27, 2018), available at <http://assets.isda.org/media/736bd0ed/1f0db5ee-pdf/>

and *Anonymized Summary of Responses* (Dec. 20, 2018), available at <http://assets.isda.org/media/04d213b6/db0b0fd7-pdf/>.

[4] See *Bloomberg Selected as Fallback Adjustment Vendor* (Jul. 31, 2019), available at <https://www.isda.org/a/uCqME/Fallback-Adjustment-Vendor-Selection-Press-Release.pdf>.

[5] See Board of the International Organization of Securities Commissions, *Statement on Communication and Outreach to Inform Relevant Stakeholders Regarding Benchmarks Transition* (Jul. 31, 2019), available at <https://www.iosco.org/library/pubdocs/pdf/IOSCOPD636.pdf>.

[6] See [ICI Memorandum No. 31855](#) (Jul. 15, 2019) for a summary of the SEC staff statement.

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