

MEMO# 33587

June 14, 2021

LIBOR Update: SEC Chair Gensler Discusses LIBOR, SOFR, and BSBY at Financial Stability Oversight Council Meeting

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TO: ICI Members

ICI Global Members

ICI Global Regulated Funds Committee

LIBOR Transition Working Group SUBJECTS: Financial Stability RE: LIBOR Update: SEC Chair Gensler Discusses LIBOR, SOFR, and BSBY at Financial Stability Oversight Council Meeting

On June 11, members of the Financial Stability Oversight Council discussed LIBOR transition during the open session of their meeting.[\[1\]](#) As a reminder, USD LIBOR is set to cease publication on June 30, 2023 and the Alternative Reference Rate Committee has recommended SOFR, a rate based on the cost of borrowing cash overnight collateralized by US Treasury securities in the repo market, as the replacement for USD LIBOR.

Among other FSOC members' remarks about the effort to transition from LIBOR,[\[2\]](#) Securities and Exchange Commission Chair Gary Gensler spoke about his concerns about LIBOR as a reference rate.[\[3\]](#) Specifically, Gensler stated that LIBOR, which is based on the rates at which panel banks in London lend to each other, encountered problems as banks ceased making many unsecured loans to each other. In his view, this created an inverted pyramid where \$220 trillion of market transactions referenced a rate that itself was based on very few transactions, leaving the rate susceptible to manipulation.

Gensler equated his concerns about the shortcomings of LIBOR to the concerns he has about an alternative rate that Bloomberg has recently developed - the Bloomberg Short-Term Bank Yield Index (BSBY). Bloomberg created BSBY to provide a credit sensitive replacement rate for USD LIBOR with a forward term structure. These attributes are in contrast to SOFR, which is not credit sensitive and does not have term rates at this time.

Gensler stated that, like LIBOR, BSBY has the same inverted-pyramid problem as LIBOR, with the commercial paper markets that underpin BSBY "virtually disappear[ing] in a crisis." Further, Gensler stated "When a benchmark is mismatched like that, there's a heck of an

economic incentive to manipulate it."

As a result, Gensler believes that SOFR, "which is based on a nearly trillion-dollar market, is a preferable alternative rate."

Other FSOC members noted their understanding that market participants are eager for a forward-looking term rate for SOFR. Treasury Secretary Yellen recommended that "market participants ? act promptly to support the switch in derivatives from LIBOR to SOFR this summer" because doing so would lay the groundwork necessary to support a SOFR term rate "quite soon."^[4]

Bridget Farrell
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endnotes

^[1] See Readout of Financial Stability Oversight Council Meeting on June 11, 2021, available at https://home.treasury.gov/system/files/261/FSOC_Readout_6-11-21.pdf.

^[2] See, e.g., Remarks by Secretary of the Treasury Janet L. Yellen to the Financial Stability Oversight Council on LIBOR Transition ("Yellen Remarks") (June 11, 2021), *available at* <https://home.treasury.gov/news/press-releases/jy0224> ("[W]e have reached a critical juncture, and more must be done to facilitate an orderly transition?While important progress is being made in some segments of the market, other segments, including business loans, are well behind where they should be at this stage in the transition."); Statement by Michael J. Hsu at the Financial Stability Oversight Council (June 11, 2021), *available at* <https://www.occ.gov/news-issuances/speeches/2021/pub-speech-2021-65.pdf> ("We expect every bank, regardless of size, to demonstrate that its replacement rate selections are appropriate for the bank's products, funding needs and operational capacities"). Federal Reserve Board Vice Chairman Randal K. Quarles also spoke at the meeting, warning market participants against procrastinating on LIBOR transition and recommending that capital market participants switch to SOFR now.

^[3] See Chair Gary Gensler, LIBOR Statement (June 11, 2021), *available at* https://www.sec.gov/news/public-statement/gensler-fsoc-libor-2021-06-11?utm_medium=email&utm_source=govdelivery.

^[4] See Yellen Remarks.