



Financial Services

2013 LIBOR UPDATE

BACKGROUND

LIBOR, or London InterBank Offered Rate, is a rate representing the average rate at which a LIBOR contributor bank can obtain unsecured funding in the London interbank market for a given period and currency.

This is the primary benchmark for short-term interest rates globally and is used in relation to at least C\$300 trillion worth of financial products. Rates are calculated based upon submissions from LIBOR contributor banks, though submissions are not necessarily based on actual transactions as not all contributing banks will require funds in a reasonable market size each day for each applicable currency and maturity. If this is the case, banks submit rates based on their credit and liquidity risk profiles and construct a curve to best predict the correct rate in which they have not been active. Rates are submitted at approximately 11:00am London time each day on a confidential basis to a designated calculation agent who processes submissions before they are released to the market by Thomson Reuters and other licensed data vendors. It was misrepresentation of these numbers by certain submitting banks that is at the heart of the ongoing investigation of rate manipulation by applicable regulators.

Given the LIBOR rate fixing scandals that came to light this past summer, the British government commissioned Martin Wheatley, the chair of the newly formed Financial Conduct Authority, to provide his recommendations on how to prevent the recurrence of such rate manipulation and reinstate market confidence in the benchmark rate.

CONSULTATION PAPERS AND LEGISLATION:

On September 28, 2012, the list of 10 recommendations in the “**Wheatley Review of LIBOR: final report**” were published:

1. *The new Financial Conduct Authority should regulate the submission to, and administration of, LIBOR – and there should be criminal sanctions for any attempted manipulation.*
2. *The British Bankers’ Association should make an orderly transfer of responsibility for LIBOR to a new administrator, selected by an independent committee.*
3. *The new administrator should scrutinize submissions and regularly review the effectiveness of LIBOR.*
4. *There should be a new code of conduct for submitters, approved by the Financial Conduct Authority.*
5. *LIBOR should, as far as possible, be corroborated by transaction data in line with the guidelines in the Review.*
6. *To improve this ability to corroborate submissions, the number of currencies and maturities for which submissions are made should be cut substantially to achieve a sharper focus on the more heavily used benchmarks.*

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7. *Submissions should be published, but after three months to avoid the incentive for banks to try to flatter their perceived credit standing and reduce the opportunity for collusion.*
8. *The Government should provide the Financial Services Authority with a reserve power to compel banks to submit to LIBOR.*
9. *All market participants should consider whether LIBOR is the most appropriate rate for their needs and to ensure that their contracts have workable contingency provisions.*
10. *The UK, European and International Authorities should establish clear principles for global benchmarks.*

The Government fully endorsed each of the foregoing, which led to their November 2012 publication of "**Implementing the Wheatley Review: draft secondary legislation**". This report proposes the following changes to legislation:

- Amendment to the *Financial Service and Markets Act 2000* to allow specification of LIBOR-related activities as being regulated thereunder (formerly self-regulated by the British Bankers' Association (the "BBA") since the LIBOR's inception in 1986).
- Expanding the scope of criminal offences relating to misleading statements and impressions in the determination of LIBOR.
- Provision of powers to the Financial Conduct Authority to allow it to make rules requiring authorized persons to contribute to a specified benchmark (e.g. LIBOR).

The BBA also issued its consultation paper in November, issuing its support for the Wheatley Review recommendations, including the replacement of the BBA as the LIBOR administrator (to be selected by an independent committee) and specific timelines to accommodate Item 6 above of the Wheatley Review—the deletion of currencies and maturities for which there is insufficient corroborative data for the rate determination process due to underuse (and therefore more potential for fraud). The BBA proposes that the process can be completed by March 2013, as follows:

- By the end of January 2013, the removal of the following maturities from all 10 currencies in the current LIBOR Framework: 2-week, 2-month, 4-month, 5-month and 7- to 11-month maturities.
- By the end of February 2013, the discontinuation of all remaining LIBOR maturities for the Australian Dollar and New Zealand Dollar.
- By the end of March 2013, the discontinuation of all LIBOR rates relating to the Canadian Dollar, the Danish Krone and the Swedish Krona.

From April 2013, only the Euro, Japanese Yen, Pound Sterling, Swiss Franc and US Dollar would remain as LIBOR currencies if the BBA's suggestions are adopted.

CONCLUSION:

Participants in the financial markets will need to consider the impact of the foregoing changes on their existing agreements; in particular, the potential elimination of certain currencies and maturities from the LIBOR scope, together with any references to the BBA as administrator of LIBOR. A review should be conducted of existing credit, derivative and other financial product documentation asking the following questions:

- Does your existing documentation provide for availability of the marginal LIBOR currencies that are to be dropped? If so, ensure appropriate language for an alternate index for each such currency is in place. It should be noted that Canadian Dollar LIBOR is an interest rate rarely used and that Canadian-based loans with LIBOR as an interest rate option typically provide for LIBOR only in US Dollars. As a result, the deletion of Canadian Dollar LIBOR should have little impact on Canadian loan documentation.

- Do your credit products permit interest period elections in the less commonly used LIBOR maturities to be eliminated? If so, the “Interest Period” definitions relating to LIBOR rate elections will likely require amendment.
- Does your credit documentation reference BBA LIBOR or the BBA’s determination of LIBOR in a manner that, upon replacement of the BBA, will be inapplicable or provide ambiguity in the determination mechanism for LIBOR? If so, these references should be revised to reference the new applicable administrator of the benchmark.
- If you would like any assistance with this process, please contact the Financial Services Practice Group at Heenan Blaikie:

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