ON**POINT** /

DECHERT ON LIBOR: Officially the Beginning of the End

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Dechert LLP

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On Friday 5 March 2021, the Financial Conduct Authority (FCA) announced that all 35 LIBOR benchmark settings as currently published by ICE Benchmark Administration (IBA), the administrator of LIBOR, will either cease to be published or will lose representativeness on the time frames set out in the announcement; a landmark step signaling the beginning of the end for LIBOR[1].

The Story So Far

Since July 2017, when Andrew Bailey, then Chief Executive of the FCA (the regulator of IBA), announced that the FCA would no longer compel panel banks to contribute submissions to IBA for the purpose of determining a LIBOR after 31 December 2021, the market has slowly recognized that LIBOR will soon end as a benchmark interest rate in all forms of contracts.

A timeline was set for the cessation of LIBOR and market-led working groups and official sector bodies, including the Financial Stability Board, have established roadmaps to help market participants plan a smooth transition in advance of LIBOR ceasing. In the UK, for sterling LIBOR, the FCA and the Bank of England have already made clear what they expect from market participants in 2021[2]. The message from the regulators remains that use of LIBOR in financial and other contracts should stop *as soon as is practicable*.

As noted in our January LIBOR alert[3], in December 2020, IBA published a consultation on its intention to cease the publication of all sterling, euro, Swiss franc and Japanese yen LIBOR settings, and the 1-week and 2-month US dollar LIBOR settings, immediately following publication of these rates on 31 December 2021, and to cease publication of the Overnight and 1-month, 3-month, 6-month and 12-month US dollar LIBOR settings immediately following the publication of these rates on 30 June 2023.

What Happened on 5 March 2021?

A stream of high profile and important announcements were made, prompted by:

1. IBA publishing a much-anticipated feedback statement[4] on the results of their December consultation, including an announcement that, in the absence of sufficient panel bank support and without the intervention of the FCA to compel continued panel bank contributions to LIBOR, it would not be possible for IBA to publish the relevant LIBOR settings on a representative basis beyond 31 December 2021 or 30 June 2023 as specified above.
2. The FCA publishing a statement announcing the dates after which panel bank submissions for all LIBOR settings will cease and confirming the future cessation and loss of representativeness of LIBOR benchmarks[5].

[1] The FCA announcement confirming the future cessation and loss of representativeness of LIBOR benchmarks can be found ***here***.

[2] "**The final countdown: Completing sterling LIBOR transition by end-2021**". Published by the FCA and the Bank of England on 11 January 2021. The Working Group on Sterling Risk-Free Reference Rates simultaneously published an updated priorities and roadmap (which was then updated in February 2021), which can be found ***here***.

[3] Our "**Dechert on LIBOR - New Year Special**", can be found ***here.***

[4] IBA's Feedback Statement can be found ***here***.

[5] The FCA press release confirming the end of LIBOR can be found ***here*** and the FCA announcement confirming the future cessation and loss of representativeness of LIBOR benchmarks can be found ***here***.

The FCA announcement covered a range of LIBOR-related items including links to Statements of Policy with respect to its exercise of future powers, so called “Article 23A” and “Article 23D” powers, included in the Financial Services Bill which proposes amendments to the UK Benchmarks Regulation (“**UK BMR**”).

What the FCA Announcement Actually Means

Timing

- Publication of the following LIBOR settings will cease immediately after the rate-setting on 31 December 2021:
  - all 7 euro LIBOR settings;
  - all 7 Swiss franc LIBOR settings;
  - the Spot Next, 1-week, 2-month and 12-month Japanese yen LIBOR settings;
  - the overnight, 1-week, 2-month and 12-month sterling LIBOR settings; and
  - the 1-week and 2-month US dollar LIBOR settings.

- Publication of the following LIBOR settings will cease immediately after the rate-setting date on 30 June 2023:
  - overnight and 12-month US dollar LIBOR settings.

- The FCA will consult on requiring IBA to continue to publish the following settings after the end of 2021, on a synthetic LIBOR basis:
  - 1-month, 3-month and 6-month sterling LIBOR settings, for a further period of unspecified length; and
  - 1-month, 3-month and 6-month Japanese yen LIBOR settings, for an additional 12 months only, so publication of these settings is expected to cease permanently immediately after a final publication on 30 December 2022.

- For the three most popular US dollar LIBOR settings, 1-month, 3-month and 6-month, the position remains uncertain. Notably, the FCA announcement did not state that publication of these LIBOR settings would end on 30 June 2023 and as with the three most popular sterling LIBOR settings, there was no indication of the time period over which the FCA would permit or require IBA to publish synthetic LIBOR. The announcement did however indicate that the FCA may use its Article 23D powers to require continued publication of LIBOR for these US dollar settings on a synthetic basis after 30 June 2023.

“Synthetic” LIBOR

- The "synthetic" LIBOR basis would be determined pursuant to a change in methodology mandated by the FCA under the powers it expects to receive under new Article 23D of the UK BMR. These powers do not yet exist, and will be implemented into the UK BMR pursuant to the Financial Services Bill currently going through Parliament.

- Any LIBOR setting published pursuant to a change in methodology mandated under Article 23D of the UK BMR (so, any "synthetic" LIBOR) will not be representative of the underlying market and economic reality that the setting is intended to measure; so will not be a representative benchmark for the purposes of the UK BMR.

It is as a consequence of the foregoing that the FCA concludes that all 35 LIBOR settings will either cease to be provided by any administrator, or will no longer be representative, in each case from the applicable date set out above.

Use of Synthetic LIBOR

- Any LIBOR setting determined using synthetic LIBOR may only be used in respect of a critical benchmark that has been "designated" under Article 23A, so (a) may not be "used" (as that term is defined in the UK BMR) in any new contracts, and (b) use of "synthetic" LIBOR settings will be limited to "tough legacy" contracts.

- There is no definition of tough legacy. The FCA will issue a consultation paper in Q2 2021 on the types of contracts that will be designated as "tough legacy". Whilst we’ll have to await the final outcome of that consultation, the scene has certainly been set by previous descriptions of tough legacy using terms such as “irreducible core” and being those that “genuinely have no or inappropriate alternatives”.[6]

A Note on ISDA

ISDA’s work on benchmark reform has been widely publicised and in January 2021, the main product of ISDA’s work, the ISDA 2020 IBOR Fallbacks Protocol and Supplement went live.[7] Following the announcement on 5 March, ISDA confirmed in a statement[8] that the FCA's announcement constitutes "*an index cessation event under the IBOR Fallbacks Supplement and the ISDA 2020 IBOR Fallbacks Protocol for all 35 LIBOR settings*". This means that the fallback spread adjustment published by Bloomberg[9] is fixed as of 5 March 2021 for all euro, sterling, Swiss franc, US dollar and Japanese yen LIBOR settings (including for the US dollar LIBOR settings that will be published until June 2023).

By fixing the "spread adjustment", there is now clarity on the future terms of the numerous derivative contracts that incorporate these fallbacks set out in the Supplement and Protocol.

Effect on LIBOR in the United States

On 8 March 2021, the Alternative Reference Rates Committee (ARRC) issued a press release[10] stating that, in its opinion, the announcements by IBA and the FCA constitute a “Benchmark Transition Event” under the ARRC’s recommended fallback language for floating rate notes, securitizations, syndicated business loans and bilateral business loans. The occurrence of a Benchmark Transition Event may trigger obligations under agreements that use the LIBOR fallback language modelled on the ARRC’s recommendations. Contracts using other variations on LIBOR replacement language may also be affected. Parties responsible for making LIBOR replacement determinations under applicable contracts should evaluate whether, as a result of the announcements, a Benchmark Transition Event has occurred or if any notice or other obligations have arisen.

Although some of the US dollar LIBOR settings may continue to be published on a representative basis until mid-2023, the Board of Governors of the Federal Reserve System, the Office of the Comptroller of the Currency and the Federal Deposit Insurance Corporation previously issued a statement[11] that entering into new contracts that use US dollar LIBOR as a reference rate after 31 December 2021 would create safety and soundness risks. These regulators also encouraged banks to cease new LIBOR use as soon as practicable. On 10 March 2021, the Division of Supervision and Regulation of the Board of Governors of the Federal Reserve System issued guidance[12] to examiners of supervised firms instructing examiners to consider issuing supervisory findings and take other supervisory actions if supervised firms are not ready to stop originating LIBOR-based contracts by the end of 2021.

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[6] Statement made on 23 June 2020 by Rishi Sunak, The Chancellor or the Exchequer (see ***here***)

[7] Our most recent Dechert LIBORcast was with ISDA’s CEO Scott O’Malia. [You can find the recording ***here***].

[8] The ISDA statement on UK FCA LIBOR Announcement can be found ***here***.

[9] Bloomberg also issued a technical notice with respect to the spread fixing, which can be found ***here***.

[10] The ARRC press release can be found ***here***. A separate FAQ produced by the ARRC in response to the announcements by IBA and the FCA can be found ***here***.

[11] The statement by the Board of Governors of the Federal Reserve System, the Office of the Comptroller of the Currency and the Federal Deposit Insurance Corporation can be found ***here***.

[12] The letter from the Division of Supervision and Regulation of the Board of Governors of the Federal Reserve System to all firms supervised by the Federal Reserve can be found ***here***. The examiner guidance to can be found ***here*** and ***here***.

What next?

This announcement marks the beginning of the end for LIBOR and reinforces the urgency for market users to move away from LIBOR rates, including US dollar LIBOR settings, preferably on a voluntary basis because that is the only sure way of controlling the effect of these changes. With less than ten months to go until publication of the majority of LIBOR settings ceases, the message from the FCA could not be clearer:

"*This is an important step towards the end of LIBOR, and the Bank of England and FCA urge market participants to continue to take the necessary action to ensure they are ready*."

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For further information, Dechert has a dedicated LIBOR page, which is available **here** and has a dedicated podcast sharing views on LIBOR with industry participants, details can be found **here**.

Dechert also provides periodic global LIBOR update webinars. The next webinar, which will be held on 18 March, 2021, will cover these developments as well as other topics related to the LIBOR transition.

Registration for that webinar is available **here**. The previous session, recorded on February 4 2021 is available **here**.

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