Minutes of LIBOR Trade Association Working Party Meeting

held on 25 November 2019

Present:

ACT
AFME
GFMA
ICMA
ICMSA
ISDA
JBA
JSLA
LMA
LSTA
TACT
UK Finance

1. Introduction

The purpose of the meeting was for the trade associations to provide updates on any developments in respect of LIBOR transition since the last meeting.

2. ACT update

ACT continues to engage with the Working Group on Sterling Risk-Free Reference Rates ("**Sterling RFR Working Group**"), including on facilitating outreach and education. It was noted that whilst corporates are aware of the issues arising from the transition, corporates have pushed back when talking to banks given other priorities.

The UK Financial Conduct Authority ("**FCA**") has been increasingly engaged with the ACT, including by speaking at a number of ACT events.

3. AFME update

AFME continues to work with the Sterling RFR Working Group.

In the securitisations market, a number of consent solicitations with respect to covered bonds and securitisations have gone through smoothly (either using a positive consent approach or AFME's negative consent language).

On 26 November 2019, the European Commission is hosting a roundtable on the review of the EU Benchmark Regulation in Brussels. The roundtable will consider, amongst other things, the regulatory aspects and the user perspective on IBOR reform. The roundtable is due to be attended by AFME, GFMA, ICMSA, ISDA and the LMA.

4. GFMA update

GFMA had been working on and regularly circulating its monthly newsletter focused on regional and global updates to help its members keep abreast of the developments with respect to the transition.

5. ICMA update

It was noted that eight consent solicitations to transition sterling LIBOR bonds to SONIA were now successfully completed.

On 21 November 2019, Edwin Schooling-Latter of the FCA delivered a speech at the Risk.net LIBOR Summit. Amongst other things, he noted that the Sterling RFR Working Group is looking to publish a document that will focus on lessons learned in relation to consent solicitations.

ICMA continues to participate in the Working Group on Euro Risk-Free Rates and the National Working Group on Swiss Franc Reference Rates.

ICMA is planning to respond to the EU Commission's public consultation on the review of the EU Benchmark Regulation, which **closes on 31 December 2019 (midnight Brussels time)**. The consultation focuses primarily on a number of topics the Benchmark Regulation itself puts forward for review, such as the regime for critical benchmarks and the effectiveness of the mechanism for authorisation and registration of EU benchmark administrators, as well as other broad topics.

6. ICMSA update

On 12 November 2019, ICMSA hosted a presentation from ConvEx - an independent financial institution providing calculation agency and other specialist services to the equity-linked market as well as to issuers of capital securities, bonds and derivatives. Historically, the "Independent Financial Adviser" role set out in the terms and conditions of instruments was generally performed by an investment bank, however in recent years, investment banks have become less willing to accept these roles, leading to the need for other more specialist players to become involved. As industry bodies have recommended enhanced fallback language for new issues across products, the bond market in Europe has generally moved towards hiring an Independent Financial Adviser to consult / determine the replacement rate, spread and other changes in the event of a "Benchmark Event". ConvEx is able to perform the role of a determination agent.

The ICMSA working group on IBORs is currently working on producing a number of bulletins for use by the market. ICMSA is hoping to publish these documents in due course.

7. ISDA update

On 15 November 2019, ISDA published a report that summarises responses to a consultation on the final parameters of adjustments that will apply to derivatives fallbacks for certain IBORs.

The new report covers technical issues on specific methodologies for the term and credit spread adjustments. Responses to the final parameters consultation show that a majority of participants preferred a historical median approach over a five-year lookback period prior to an announcement triggering a fallback. A majority also preferred not to include a transitional period in the spread adjustment calculation, not to exclude outliers, and not to exclude any negative spreads. For the compounded setting in arrears rate, a clear majority favoured a two-banking-day backward shift adjustment for operational and payment purposes. This effectively results in something similar to an OIS swap with an earlier observation date, however those conventions will not change the conventions used in the traditional OIS market, which instead would use a payment delay (outside of sterling where there is no payment delay). Consequently, all of ISDA's fallbacks will use the backward shift, including in those markets where traditionally there is no payment delay (such as in the case of a sterling LIBOR derivative that falls back to SONIA).

Bloomberg had been selected to publish the adjustments and ‘all in’ fallback rates and now needs to work on the final mathematical formula for fallbacks, which is a key outstanding issue before the final formula is available in first quarter 2020.

Following these results, ISDA will make the relevant amendments to the 2006 ISDA Definitions to incorporate fallbacks with these adjustments for new IBOR trades. ISDA will also publish a protocol to enable market participants to include fallbacks within legacy IBOR contracts if they choose to.

ISDA expects to shortly publish a new supplemental consultation on the spread and term adjustments for fallbacks in derivatives referencing euro LIBOR and EURIBOR, which will also cover the final parameters for these adjustments (this was subsequently published on 18 December 2019 and the **deadline for responses is 21 January 2019**). If the consultation results are consistent with prior consultations, ISDA expects to implement fallbacks for euro LIBOR and

EURIBOR in 2020, in line with fallbacks for the nine other IBORs covered by the earlier consultations.

One member of the Working Party highlighted that on the bond side, it remains difficult to implement the two-banking-day backward shift adjustment due to operational and payment reasons. This is because a longer period is required to enable parties to liaise with the clearing systems. It was noted that there is a significant shift in relation to the time expectations arising from the transition and this will be a significant challenge for the bond market.

In 2020, ISDA will undertake work focused on education, including by holding its conferences on the implementation of fallbacks on 12 February 2020 in New York, and on 26 February 2020 in London.

8. JBA update

The Cross-Industry Committee on Japanese Yen Interest Rate Benchmarks is working on compiling the final report on the results of the public consultation on the appropriate choice and usage of Japanese yen interest rate benchmarks (the results were subsequently published alongside a summary of main points of the final report on 29 November 2019). The public consultation sought feedback on five options to be used as alternative benchmarks to JPY LIBOR. In general, most respondents supported term reference rates based on swaps ("**Option 3**"), or term reference rates based on futures ("**Option 4**"); highlighting their capability with current business operations and systems, as well as trading practices. As development of term reference rates based on swaps is anticipated to take some time, consensus was reached on the need to enhance liquidity in the swaps market and to ensure the robustness and reliability of such rate. This will be achieved through adopting a phased approach. Consensus was also reached with respect to the need to use the other options until term reference rates based on swaps can be properly developed.

On 29 October 2019, the Committee issued a solicitation document for the calculating and publishing entities of prototype rates for term reference rates based on swaps.

The Committee will continue to examine the progress of interest rate benchmark reform and to provide support for market-wide initiatives towards the development of swap-based term reference rates.

9. JSLA update

JSLA is continuing to work closely with JBA, including with respect to market outreach and education.

In February 2020, the JSLA is holding an annual meeting where it will provide an update on the current workstreams and discuss the possible next steps with respect to the transition and the way forward with respect to the development of fallbacks.

10. LMA update

In its capacity as chair of the Sterling Sub-group on Benchmark Transition Issues in Syndicated Loan Markets, the LMA had been working closely with the US Alternative Reference Rates Committee ("**ARRC**") and the LSTA to solve for a number of key outstanding issues, including with respect to the precise calculation methodology for compounding RFRs for the loan market, as well as how to accommodate operational challenges for such rates (such as prepayments or secondary trading). Between 18 to 19 November 2019, the LMA, FCA and the Bank of England attended the ARRC Business Loans Operations Vendor Whiteboarding sessions, which was helpful in terms of discussing the relevant key outstanding issues and working towards achieving consistency between conventions in the different currency jurisdictions.

Progress had been made with respect to issuances of new bilateral sterling loans referencing SONIA.

The LMA continues to encourage market participants to provide feedback on the LMA exposure drafts of: (i) a compounded SONIA based sterling term and revolving facilities agreement; and (ii) a compounded SOFR based dollar term and revolving facilities agreement ("**LMA Exposure Drafts**").

On 25 October 2019, the LMA published an exposure draft of Reference Rate Selection Agreement for use in relation to legacy transactions transitioning from LIBOR to RFRs. The LMA welcomes comments from market participants on all exposure drafts, particularly that arising from experiences on transactions. The document is designed to be read in conjunction with the LMA Exposure Drafts. As the syndicated loan market does not have a protocol system for amendments (such as that operated by ISDA) given the multilateral nature of syndicated loans, each individual loan agreement referencing LIBOR would need to be amended to refer to a replacement benchmark rate. The purpose of the Reference Rate Selection Agreement is to streamline the process of transition to alternative reference rates through the use of the same form of agreement on different transactions. In addition, under the Reference Rate Selection Agreement, the parties would agree the basic commercial terms for the selection of the applicable alternative reference rate(s) and then authorise the Agent and the Obligors to determine the necessary amendments to the relevant facility agreement in accordance with the terms set out in the Reference Rate Selection Agreement. Whilst this is a two stage process, it is expected to make the process of agreement to such amendments easier to manage for the Agent and also the Lenders (who would not need to approve all of the changes to the relevant facility agreement).

11. LSTA update

As part of its role in the ARRC Business Loans Working Group, the LSTA continues to work on developing a set of conventions for SOFR-referencing loans, and especially the outstanding issues with respect to the compounded in arrear methodology. The LSTA continues to liaise with the LMA and other national loans sub-groups and central banks as part of the Joint Call on Loans to ensure global consistency between conventions. It was noted that progress is being made. The work on conventions will then inform the way forward in terms of the LSTA's work on the operational side.

The LSTA continues to proactively engage in facilitating education to the market, including through regularly holding online webcasts on the transition (including a webcast entitled "*Demystifying the LSTA's SOFR Concept Credit Agreement*", which covers the following topics: (i) the attributes of a compounded in arrear rate; (ii) a step-by-step look at the "Compounded SOFR" definition; (iii) a discussion of the conventions included in the draft; (iv) a survey on which LIBOR provisions change and which stay the same; and (v) next steps).

The LSTA is expecting to publish the Compounded SOFR in Arrears Concept Document as a recommended form document in early 2020.

The LSTA is aware of at least two new bilateral SOFR-referencing loans in the US.

12. TACT update

It was noted that in the context of refinancing loan transactions, many parties remain unconvinced about implementing any substantive changes with respect to the choice of a benchmark rate. The issue had been subsequently discussed at an International Women's Insolvency & Restructuring Confederation meeting in London, where members of the Confederation were advised to check in with their banking teams to ensure that the latest available benchmark discontinuation language is included in documentation.

In December 2019, TACT is holding a meeting to discuss issues relevant to the transition.

The LMA noted that some borrowers may not be willing to amend documentation to reference RFRs as they do not wish to be a test case for the implementation of RFRs, and might be more inclined to do so once there is more certainty and once certain key issues are resolved (such as the methodology for compounding and systems issues). It was also noted that the majority of loan transactions incorporate the LMA Recommended Revised Form of Replacement Screen Rate Clause which facilitates an amendment process at a lower threshold of lender consent, and do not hardwire any particular fallbacks given the uncertainty with respect to how these might function and what economic results they could produce.

ICMSA noted that benchmark discontinuation language is also frequently incorporated in the bond space.

13. UK Finance update

UK Finance noted that awareness levels with respect to the transition are low amongst customers and many do not understand the reasons for the implications of and the next steps for the transition. To assist with this process, UK Finance continues to work with the Sterling Communications sub-group to produce relevant communications. In November 2019, UK Finance published a Discontinuation of LIBOR – UK Finance Guide for Business Customers which can be used by direct lending banks to explain the key issues with respect to the transition and the next steps.

UK Finance has been working on raising awareness amongst smaller and specialist bank members. On 6 November 2019, the UK Finance Annual Mortgage Conference took place where Edwin Schooling-Latter delivered a presentation, where it was noted that there are still approximately 200,000 LIBOR linked legacy mortgages in the UK, against a background of continued uncertainty with respect to how the market might deal with the issues. UK Finance is working to provide further educational materials on this topic.

UK Finance continues to work with the FCA and the Bank of England to build out the timetable of the Sterling RFR Working Group so that firms can more easily plan their transition efforts with reference to the anticipated timings.

UK Finance has been engaged with its banking members who are involved in the export and trade finance sectors, where additional issues continue to come to light. For example, a number of firms have guarantees provided by UK Export Finance which may be subject to a technical default as a result of the transition. There is a strong need for the industry to work on documentation to mitigate such risk ahead of the 2021 deadline. UK Finance will be working with the LMA on raising awareness in the market. It was noted that the LMA has published article entitled *"The transition from LIBOR to risk-free rates: what the export finance market needs to know"* which was written for the Berne Union to raise awareness.