

Deloitteⁱ US LIBOR Transition Newsletter

A summary of US regulatory and market updates related to the transition from LIBOR

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Executive Summary

The Alternative Reference Rates Committee (ARRC) has released a Request for Proposal (RFP) to identify a potential administrator who will publish the forward-looking Secured Overnight Financing Rate (SOFR) term rates intended to replace LIBOR. The creation and publication of SOFR term rates by a recommended administrator are the final stages of the ARRC's transition plan and are expected on June 30, 2021 as specified by the RFP. Although the ARRC does not guarantee that any SOFR term rate or administrator will ultimately be recommended, proposals are intended to be judged on technical, firm, public policy, and calculation methodology criteria.

The International Swaps and Derivatives Association (ISDA) published a letter to regulators delaying the expected effective date of the supplement to the 2006 ISDA Definitions (and related protocol) to mid-to-late January 2021. The supplement is meant to introduce robust fallbacks for derivative contracts in an attempt to reduce the disruption which could arise from the cessation of LIBOR and other IBORs. As detailed in the letter, timeframes are dependent on a confirmation from the US Department of Justice (DoJ). Once approved, ISDA will give a two weeks' notice before the launch date, currently expected October 23, 2020. The supplement and protocol can then be officially launched and plans to take effect approximately three months later in January 2021.

The European Securities and Markets Authority (ESMA), the EU markets watchdog who plans to act as supervisor of the Euro Interbank Offered Rate (EURIBOR) as of January 2022, has commented that EURIBOR performed well throughout the recent pandemic-related volatility and will be available for the foreseeable future. This marks a distinct contrast from the path forward for LIBOR in the coming year. Although the discontinuation of EURIBOR is not in ESMA's plans, chair Steven Maijoor urges market participants to include fallbacks into contracts to prepare for the possible cessation of EURIBOR.

Key Upcoming Dates

- **October 23, 2020** – ISDA's expected release of the IBOR Fallbacks Supplement and the IBOR Fallbacks Protocol.
- **January 25, 2021** – ISDA's expected effective date of the IBOR Fallbacks Supplement and the IBOR Fallbacks Protocol.



Our Perspective

ARRC RFP to Identify SOFR Administrator

As one of the first steps to begin publishing the long sought after SOFR term rate, the ARRC's publication of the RFP and the RFP Frequently Asked Questions (FAQs) demonstrates the ARRC's attempt at beginning to publish the forward-looking term rate within the first half of 2021. The Central Counterparty Clearing Houses' (CCPs) (i.e. London Clearing House (LCH), Chicago Mercantile Exchange (CME) and Eurex) October switch of discounting rates from Effective Federal Funds Rate (EFFR) to SOFR has just recently passed and we would expect an increase in trading of SOFR products as the need for hedging increased exposure to SOFR rises. A significantly larger volume of trading of the various derivative products such as futures, swaps, etc. may need to take place to provide enough data sources to begin publishing SOFR term rates by ARRC's goal of June 30, 2021. We urge vendors to review the ARRC RFP and FAQs and consider applying to become an administrator of the rate, if possible. Firms may also want to keep monitoring the progress of the RFP and trading volumes to evaluate their systems and operational readiness on expected timelines when the term rates begin to publish.

ISDA Fallback Supplement to Definitions and Protocol

The announcement of ISDA's expected release date and effective date of the ISDA IBOR Fallbacks Supplement and IBOR Fallbacks Protocol marks an important step towards the LIBOR transition efforts. Although the release and effective dates are later than expected (October 2020 and January 2021, respectively), the Supplement and the Protocol intend to provide substantial relief and benefits to the financial industry. During the ARRC office hours, David Bowman, Senior Associate Director at Board of Governors of the Federal Reserve (FRB) noted that there it should be expected that the DoJ will approve the updated ISDA definitions and Protocol but acknowledged that the internal approval process may take some time. The delay does not impact the ARRC's Transition Plan, as their main milestones are the CCP discounting change and the publication of the term rates. The release of ISDA's Protocol is not included as a milestone for the ARRC. The delays into January 2021 were also attributed to the holiday schedule, and it was noted that ISDA wanted to make sure that firms have enough time to review the Protocol in full detail without year-end or holiday schedules impacting their reviews.

ESMA Continuing EURIBOR

ESMA's comments that EURIBOR does not plan to be discontinued is expected, as they have reformed the rate back in July 2019 with the authorization from the Belgian Financial Services and Markets Authority (FSMA). There currently are no definitive plans on if euro short-term rate (€STR) plans to have a forward-looking term rate, so EURIBOR plans to continue to fill that role for the foreseeable future. Although the rate may not be discontinued, firms should still consider reviewing the contracts which reference EURIBOR and their legal department's plans to ensure that EURIBOR-linked contracts have plans to incorporate robust fallback language in case there is an event in the future where EURIBOR is no longer representative.



Regulatory Updates

Summary of ARRC Office Hours Q&A with David Bowman (The Federal Reserve Board (FRB))

This section represents a summary of the ARRC office hours Q&A with David Bowman from September 1, 2020 until September 30, 2020. Weekly office hour information can be found [here](#). The information below does not represent the view of the Federal Reserve but represents the personal views of David Bowman outside of his official capacity. Below are some of the specific topics discussed:

Forward-Looking Non-Representativeness Declaration

- The date of the forward-looking non-representative announcement is significant as it is the date that both the ARRC and ISDA set the new reference rate spread adjustment. The ARRC has made public statements to this effect although it is not officially listed in the amended fallback language.

ARRC Lookback Periods

- Lookbacks and payment delays are examples of what the ARRC considers “conforming changes”. The industry seems to gravitate towards a five-business day lookback, however contractual parties have discretion over lookback periods.

NYS Legislative Solution Progress Before Financial Conduct Authority (FCA) Announcement

- Although Edwin Schooling Latter, head of markets policy at the FCA, suggested a LIBOR discontinuation announcement by the FCA is possible for November or December of this year, LIBOR will continue to exist until the end of 2021. The ARRC continues to have discussion with the NYS Legislature, however the main question remains when the NYS Legislature will have bandwidth for issues other than COVID and the budget crisis.

Selecting the Forward-Looking SOFR Term Rate Administrator

- The ARRC has no power in mandating who can and can't produce a term rate. It is quite likely that vendors may create term rates and charge users for access. The ARRC, however, can only recommend one rate and administrator to be determined based on the proposal which best meets the thresholds the ARRC has set. Parties using the ARRC recommended fallback language and the ARRC recommended term rate, would see their agreements fallback to the ARRC recommended term rate once LIBOR ends (which would also happen in the event NYS legislation is passed).

FCA Statement of Non-Representativeness

- Edwin Schooling Latter, head of markets policy at the FCA, recently said it is possible the FCA could make a statement of non-representativeness as early as late this year regarding certain LIBOR tenors. The potential statement would discuss LIBOR ending at the end of 2021, or a specific tenor not being representative as of December 31, 2021. If the FCA to make a such a statement, the ISDA and ARRC long term spreads would be set on that date (contracts would not trigger or move under the ISDA protocol or ARRC fallbacks until LIBOR ceased to exist). It is possible that FCA could make an announcement before the ISDA protocol is available but would only mean the spread would be set. A non-representativeness statement would not affect ARRC interim deadlines as the plan is to be ready for December 31, 2021. The ARRC plans to release additional operational materials in the near future.

SOFR Discounting Curves

- Discounting using the SOFR curve will yield many benefits in the long run as a method of transitioning away from LIBOR. If the SOFR curve is helpful for transitioning away from LIBOR, it should be used. However, the primary focus should be the transition itself, as opposed to the specific curve used to that effect.

Regulatory Highlights

- The ARRC released an RFP to identify a potential administrator who will publish the forward-looking SOFR term rates intended to replace LIBOR. The RFP is available [here](#) and the RFP FAQ's are available [here](#).
- The ISDA published a letter to regulators delaying the expected effective date of the supplement to the 2006 ISDA Definitions, and related protocol, to January 2021. The letter is available [here](#).
- The ESMA commented that EURIBOR performed well throughout the recent pandemic-related volatility and will be available for the foreseeable future. The article is available [here](#).

ARRC Working Group

- The ARRC released an RFP for the administration of recommended spread adjustments and spread-adjusted SOFR to facilitate contractual fallbacks. The press release is available [here](#).
- The ARRC's Best Practices were updated to include new target dates for the incorporation of hardwired fallbacks for Bilateral and Syndicated Business Loans. The updated best practices are available [here](#) and updated factsheet is available [here](#).
- The ARRC released an addendum to its recommendations for voluntary compensation for swaptions impacted by the CCP discounting transition to SOFR. The press release is available [here](#).
- The Credit Sensitivity Group Workshop #4 meeting materials are now available. The agenda is available [here](#) and the minutes are available [here](#).
- The ARRC published its August- September newsletter. The newsletter is available [here](#).

ISDA Updates

- ISDA-Clarus RFR Adoption Indicator (August 2020) which is intended to track global trading activity (DV01) conducted on RFRs was published. The indicator is available [here](#).
- ISDA conducted a webinar and published materials covering September presentation on Collateral Changes for USD and Euro Derivatives. The webinar is available [here](#) and the presentation is available [here](#).
- ISDA published its IQ September 2020 newsletter. The newsletter is available [here](#).

Other News/ Useful Reading

- Fundamental Review of the Trading Book (FRTB) and the issues arising from the LIBOR transition and COVID-19. The article is available [here](#).
- LIBOR transition and non-linear products. The article is available [here](#).
- TraditionDATA integrates AMERIBOR with reference rate data sets. The article is available [here](#).
- US Commodity Futures Trading Commission (CFTC) provides additional LIBOR transition relief to swaps participants. The article is available [here](#).
- LCH published the SOFR discounting auction indicative portfolio. The notification is available [here](#).
- CME SOFR futures volumes jump as packs and bundles liquidity arrives. The article is available [here](#).
- SOFR discounting: CCPs prepare for make or break auctions. The article is available [here](#).
- Accounting rules snare insurers in SOFR discounting switch. The article is available [here](#).
- SOFR basis tightens on 'big bang' auction disclosure. The article is available [here](#).
- LIBOR transition efforts continue despite COVID-19 impacts. The article is available [here](#).
- Fannie Mae pauses some Re-REMICs for Freddie Mac legacy LIBOR CMOs. The announcement is available [here](#).
- Risk.net published an article titled "IFRS 9 Update Will Lead to Hedge Accounting Breakdown if New Rates Markets Lack Depth". The article is available [here](#).
- Michael Held (FRB) remarks at the IMN Virtual Investors' Conference were published. The speech is available [here](#).



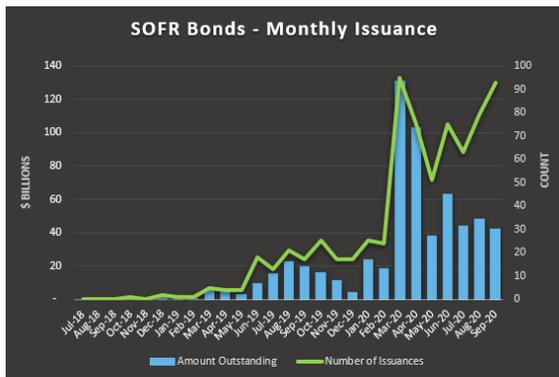
Market Updates

Decrease in Debt Issuance Referenced to SOFR

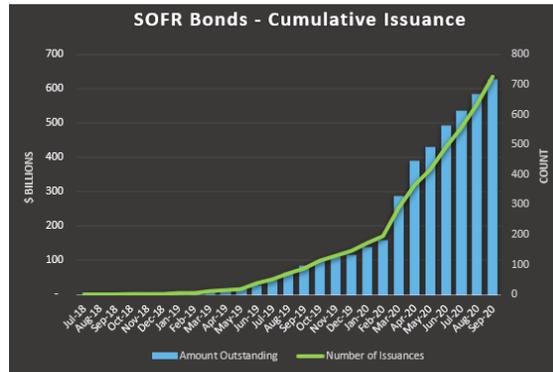
The issuance size of SOFR referenced debt decreased in September 2020 compared to the issuances in August 2020. The issuance was \$42.3 billion in September 2020 which decreased from \$48 billion in August 2020. The graphs below represent data through September 30, 2020.

The cumulative issue size of SOFR bonds outstanding (this excludes matured bonds) is currently \$619.5 billion with 725 bonds through October 14, 2020. There were 93 new issuances in September 2020 compared to 79 and 63 issuances in August 2020 and July 2020 respectively.

In September 2020, federal agencies issued 51 SOFR referenced Floating Rate Notes (FRNs) worth \$27.3 billion. There were 39 other institutions which contributed \$15 billion to the outstanding amount of SOFR referenced debt.



Source: Bloomberg, compiled by Deloitte
*Data as of Sept 30, 2020

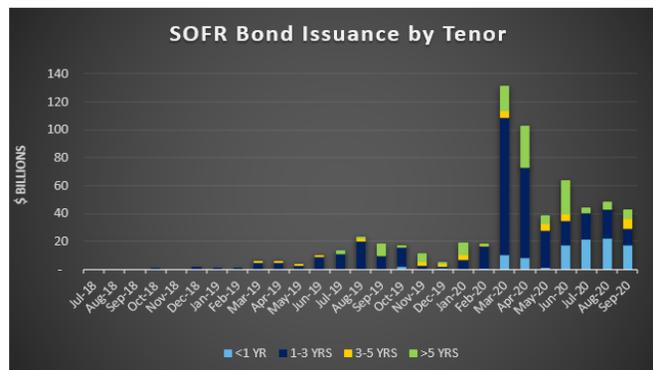


Source: Bloomberg, compiled by Deloitte
*Data as of Sept 30, 2020

Increase in Longer Dated Debt issuance (maturity >=5 years) referenced to SOFR

SOFR debt issuances with a maturity greater than or equal to five years increased in September 2020 compared to the previous month of August 2020. During September 2020, there were 5 bonds issued which have a maturity between five and ten years. The issuances during September 2020 includes 28 bonds with an amount outstanding of \$2.73 billion which have a maturity greater than or equal to ten years, which has increased as compared to \$2.37 billion in August 2020.

There were 210 issuances of SOFR bonds outstanding worth \$132.5 billion, with a maturity greater than or equal to five years, through October 14, 2020 including 170 issuances worth \$80.4 billion with a term greater than or equal to 10 years.



Source: Bloomberg, compiled by Deloitte
*Data as of Sept 30, 2020

Cumulative SOFR Interest Rate Derivatives

SOFR Swaps

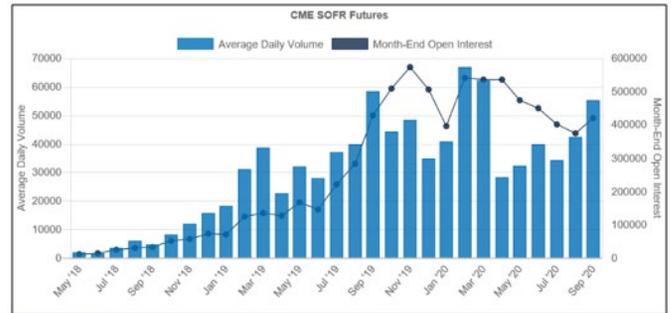
- The cumulative traded notional for SOFR based interest rate and basis swaps totaled \$1098.3 billion through October 2, 2020.
- For the month of September 2020, the notional volume of SOFR-based interest rate and basis swaps totaled \$100 billion compared to the \$54.3 billion in August 2020, and \$64.5 billion in July 2020.



Source: <http://swapsinfo.org/>, compiled by Deloitte
*Data as of Oct 2, 2020

SOFR Futures

- As per the data available on CME, for September 2020, SOFR futures average daily volume reached 55K contracts/ day. The data is available [here](#).
- The month-end open interest for September 2020 was around ~420K contracts. The data is available [here](#).



Source: CME Group
*Data as of Sept 30, 2020

Global IBOR Activity

The market activity in Sterling Overnight Index Average (SONIA), Swiss Average Rate Overnight (SARON) and Euro Short-Term Rate (€STR) based debt issuances and swaps have continued to increase. The table below represents the cumulative bond issuances (does not exclude matured bonds) and the cumulative notional of swaps outstanding through October 2, 2020.

Alternative Reference Rate	Swaps Cumulative notional amount (US \$ Billions)	Bonds Cumulative issuance amount (US \$ Billions)
SONIA	29,512.4	86.9
SARON	57.1	NA
TONA	549.4	NA
€STR	39.1	4.2

Source: Bloomberg, <http://swapsinfo.org/>, compiled by Deloitte
Data as of October 2, 2020



Global Highlights

United Kingdom

- Bank of England (BoE) The Working Group on Sterling Risk-Free Reference Rates (RFRWG) released a number of papers intended to support firms in the transition of their existing sterling LIBOR-linked contracts. The press release is available [here](#), statement on the timeline and COVID-19 is available [here](#), transition of referencing loans is available [here](#), transition of bonds is available [here](#), and a statement on the recommendation of credit adjustment spread methodology is available [here](#).
- The FCA and the BoE encourage market participants in further switch to SONIA in interest rate swap markets. The statement is available [here](#).
- BoE RFRWG's letter to Intercontinental Exchange (ICE) Benchmark Administration (IBA) regarding supporting transition in non-linear derivatives was published. The letter is available [here](#).
- BoE RFRWG published its August 2020 newsletter. The newsletter is available [here](#).
- FCA publication of "Messages from the Engine Room: 5 Conduct Questions" covering a roundtable with wholesale banks were published. The feedback is available [here](#).
- BoE RFRWG published its news release: Securing a SONIA-based sterling loan market. The article is available [here](#).
- The BoE has advised that several prototype alternatives to LIBOR produced by rival financial data companies need to be tested. The article is available [here](#).
- Financial Reporting Council (FRC) published: "Call for comments on draft UK Endorsement Criteria Assessment: IBOR Phase 2 Amendments." Press release with links to assessment and invitation to comment are available [here](#).

European Union

- Reuters published an article titled "EU Markets Watchdog Has No Plans to Scrap EURIBOR Benchmark." The article is available [here](#).
- Euromoney published an article titled "LIBOR Transition and COVID-19." The article is available [here](#).
- LIBOR webinar playback: spotlight on euros. The webinar is available [here](#).
- European Central Bank (ECB)'s Holthausen urges market to ditch EONIA. The article is available [here](#).
- Euribor fallback consultation set for November. The article is available [here](#).

Asia

- The People's Bank of China published a White Paper "Participating in International Benchmark Interest Rate Reform and Improving China's Benchmark Interest Rate System". The press release is available [here](#).
- The Swap Offer Rate (SOR) to Singapore Overnight Rate Average (SORA) transition roadmap with key priorities was published. The roadmap is available [here](#).
- The Association of Banks in Singapore (ABS) roundtable speech by Chairman Samuel Tsien on September 9, 2020 was published. The speech is available [here](#).
- Asiaone published an article on Singapore Interbank Offered Rate (SIBOR), SORA and SOR rates and their effects on home loans. The article is available [here](#).
- Hong Kong plots HONIA-linked floater debut. The article is available [here](#).
- Landmark loan sets the pace for the industry's future syndicated SORA loans. The article is available [here](#).

Contact Us

For further details on how we can help firms experience an effective transition away from LIBOR, please visit our website:

[DELOITTE LIBOR TRANSITION WEBSITE](#)

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