



Deloitteⁱ US LIBOR Transition Newsletter

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

[Executive Summary](#)

[Regulatory Updates](#)

[Global Highlights](#)

[Our Perspective](#)

[Market Updates](#)



Executive Summary

On April 20, 2023, and May 25, 2023, the Alternative Reference Rates Committee (ARRC) held meetings to discuss the progress in the transition from London Interbank Offered Rate (LIBOR) to Secured Overnight Financing Rate (SOFR). The members noted continued progress in the transition from LIBOR to SOFR. The data indicated predominance of SOFR across cash and derivative markets. During these meetings members also noted some recent improvement in the pace of remediation of leveraged loans, one of the key remaining market segments which needed to accelerate the transition away from LIBOR before the deadline of June 30, 2023, now well achieved. While remediation of leveraged loans has picked up, ARRC members emphasized that further progress is still needed specifically for lower rated leveraged loans. The members also noted that both London Clearing House (LCH) and Chicago Mercantile Exchange (CME) achieved a major transition milestone with the successful completion of their cleared US Dollar (USD) LIBOR swap conversion events. Lastly, the ARRC members discussed the state of preparation for June 30 and noted continued action on communication of rate changes for securities, remediation of LIBOR loans and understanding fallbacks.

On April 21, 2023, the ARRC released a summary and update of its Term SOFR scope of use recommendations. Through this release, the ARRC provides recommendations for hedging Term SOFR risk. The ARRC's existing recommendations recognized the ability of end users to use Term SOFR derivatives to hedge Term SOFR business loans or legacy LIBOR

Deloitte LIBOR Transition Newsletter

products that have converted to Term SOFR. The updated recommendations allow for the use of Term SOFR-SOFR basis swaps in a wider range of circumstances. Interdealer trading of Term SOFR derivatives, including basis swaps, remains unchanged to ensure the robustness of Term SOFR.

On April 27, 2023, the International Swaps and Derivatives Association (ISDA) Chief Executive Officer Scott O'Malia offered comments on important over-the-counter (OTC) derivatives issues. Mr. O'Malia noted that once the final five USD LIBOR settings cease to exist or become non-representative, trillions of dollars of LIBOR-linked loans and other cash instruments will switch to fallbacks referencing Term SOFR, potentially adding to demand for Term SOFR hedges. This could push dealers closer to internal limits on the amount of Term SOFR risk they can take on, eventually restricting their ability to offer Term SOFR derivatives to end users. In response, the ARRC has refined its Term SOFR scope of use recommendations, introducing another avenue for dealers to lay off their risk, while continuing to recommend that overall use of Term SOFR remains limited.

On May 11, 2023, the Securities and Exchange Commission (SEC) released its observations from examinations of investment advisers and investment companies concerning LIBOR-transition preparedness. The types of firms reviewed in these examinations included advisers associated with large bank complexes; advisers to various types of registered investment companies (e.g., mutual funds, closed-end funds, exchange-traded funds, and business development companies); small, medium, and large fund complexes; advisers to private funds that invest in private credit, such as collateralized loan obligations; and large retail-oriented advisers. Firms' preparation efforts varied considerably, depending on the type and amount of LIBOR exposure. Most of the examined firms had significant direct exposure to LIBOR-linked contracts. A few, which had large retail client bases, had more limited and indirect exposure. The SEC staff observed certain practices firms have implemented to address the transition away from LIBOR. The SEC noted that firms have made significant efforts to prepare for the transition away from LIBOR, implementing a variety of practices depending on their business models and client base. Additionally, several challenges exist to a smooth and orderly transition away from LIBOR.

On May 15, 2023, ISDA released that the ISDA-Clarus Risk-Free Rate (RFR) Adoption Indicator increased to an all-time high of 60.7% in April 2023, compared to 56.6% in March 2023. The indicator tracks how much global trading activity (as measured by DV01) is conducted in cleared OTC and exchange-traded interest rate derivatives (IRD) that reference risk-free-rates (RFRs) in eight major currencies. On a traded notional basis, the percentage of RFR-linked IRD rose to 53.4% of total IRD transacted in April 2023 compared to 52.3% the prior month. On June 12, 2023, the ISDA released that the ISDA-Clarus RFR Adoption Indicator decreased to 58.7% in May 2023 compared to 60.7% in April 2023. On a traded notional basis, the percentage of RFR-linked IRD increased to 55.3% of total IRD transacted in May 2023 compared to 53.4% the prior month.

On May 31, 2023, the ARRC released a statement advocating market participants with USD LIBOR exposures to finalize their transition efforts immediately. With the cessation of the LIBOR panel at the end of June 2023, the ARRC emphasized the importance of completing the transition and utilizing the available resources and tools that have been provided over the past few years.

On May 31, 2023, the Financial Conduct Authority (FCA) issued final messages for the market participants ahead of the June 30, 2023 deadline. FCA confirmed that the administrator of LIBOR, IBA, would be required to publish the 1-, 3-, and 6-month USD LIBOR settings in synthetic form until the end of September 2024. Further, starting from July 1, 2023, all new use of USD LIBOR settings will be prohibited under the UK Benchmarks Regulation and the overnight and 12-month USD LIBOR settings will cease to be published after June 30, 2023.

On June 9, 2023, the CME Group released a rates recap indicating that open interest reached 17.8M contracts on May 2023, the highest level in 45+ years of trading. Treasury futures notional volume as a percentage of Trade Reporting and Compliance Engine (TRACE) cash volume reached a record high of 104.8%, as measured on a 52-week rolling basis.

On June 22, 2023 the ARRC designated Peter Phelan, Chief Administrative Officer of the Institutional Clients Group in North America at Citigroup, as ARRC Chair as of July 1, 2023. Mr. Phelan will oversee the conclusion of the ARRC's nearly decade-long effort, as it focuses on addressing final issues that arise, and memorializing the key tools and recommendations to ensure that the work to move to a strong reference rate foundation endures.

On June 30, 2023, the USD LIBOR Bank Panel ceased to exist as planned. USD LIBOR will no longer be published for 1-, 3- and 6-month settings. This has proved to be a landmark transition in the history of the financial industry.



ARRC'S Assessment of LIBOR Transition Readiness

The timely reconventions of ARRC's meetings, their discussions with related working groups, and circulation of the outcomes of their meeting serve as important inputs to market participants who are working steadfast to address their USD LIBOR inventory. The meetings conducted by ARRC are an important milestone in enabling ARRC to assess LIBOR transition readiness and any potential operational issues. While significant transition to SOFR has been observed in the cash and derivative markets, further progress was deemed to be required in the lower rated leveraged loans. These meeting allow the market participants to highlight any roadblocks experienced/anticipated in a timely manner and determine the next focus areas to achieve smooth transition.

ARRC'S Key Recommendations

The recommendations released by ARRC to hedge Term SOFR risk will allow the market participants an opportunity to reduce unnecessary uncertainty, avoid unintended adverse outcomes, and to mitigate associated operational risk. The refinements provided by ARRC including the use of Term SOFR-SOFR basis swaps, along with a broader understanding of its previous best practice recommendations, should help ensure the long-term usefulness of Term SOFR in the transition away from LIBOR while maintaining financial stability.

ISDA Update on ARRC's Term SOFR Guidance

The ARRC has been clear that Term SOFR plays an important role in the transition from USD LIBOR for the loan market but has emphasized that use of Term SOFR should be minimal to ensure this rate remains robust in future. While SOFR itself is based on USD repo transactions, Term SOFR is a separate rate based on derivatives referencing SOFR and therefore depends on a deep and robust SOFR derivatives market. Fewer people using SOFR-linked derivatives could therefore undermine the viability of Term SOFR. Term SOFR can be used as a reference rate for new business loans and certain securitizations and as a fallback for many legacy LIBOR cash products, which means there has been and will likely continue to be demand for Term SOFR hedges. In the update, the ARRC emphasized the purpose of the change is not intended to lower the cost of Term SOFR hedges, so they are in line with overnight SOFR, but to help ensure that Term SOFR liquidity remains available to those end users that need it. It reiterated its opposition to interdealer trading of Term SOFR derivatives, including Term SOFR-SOFR basis swaps.

LIBOR Transition and ARRC's New Leadership

ARRC and FCA provided guidelines to the market participants for achieving a smooth transition ahead of the June 30, 2023, deadline. These guidelines have played a critical role in providing direction to the market participants to plan and act by prioritizing areas which are yet to see significant progress. The already existing tools, processes, and procedures served as an important source of information towards achieving a seamless transition. Further, the publication of synthetic LIBOR until 2024 provided comfort to the market participants ensuring that no sudden disruption would be caused by the movements away from LIBOR. Since July 1, 2023 the newly appointed chair for ARRC has been providing a fresh outlook and solutions to any existing issues which have brought the decade long effort to its closure.

CME Rates Recap

The CME released a rates-recap in in April, May, and June of 2023, and stated that the vast majority of trading activity in short-term interest rates has migrated to SOFR futures and options. The shift from LIBOR to SOFR during this time consisted of the conversion of 7.5 million contracts in Eurodollar open interest (OI) and \$4 trillion in cleared USD LIBOR swaps to SOFR equivalents. With these historic conversion milestones now complete, the path ahead for short-term interest rate risk management is stronger than ever, with SOFR futures and options already larger and more resilient than Eurodollars. In June 2023, CME stated that there had been rising demand for deep and consistent liquidity when managing interest rate risks, leading to record hedging in US Treasuries.



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

This section represents a summary of the ARRC office hours Q&A with David Bowman from April 1, 2023, until June 30, 2023. Weekly office hour information can be found [here](#). The information below does not represent the view of the FRB but represents the personal views of David Bowman outside of his official capacity. Below are some of the specific topics discussed:

Determining Parties for Fixed Income Securities

- If the determining party of a fixed income security does not make a determination on fallback rate prior to LIBOR cessation on June, 30, 2023, so long as it is under US law, then it would be covered under the LIBOR Act and the Board selected benchmark replacement will apply.

September 2024 Extension Applicability

- Contracts that use the additional time will need to be remediated. If there are securities referencing the ICE Swap and not covered by the LIBOR Act, referring to the ARRC's recommended formula or even has a fallback, one would need to buy them back, swap them or change the contracts.

Contracts with LIBOR Fallbacks

- If a contract is covered by the LIBOR Act, then the replacement date is June 30, 2023, regardless of the trigger.

Borrower's Rights on Altering Rates

- Beginning on July 1, 2023, borrowers do not have the right to decline the use of CME Term SOFR, as it is the FRB selected benchmark rate covered under the LIBOR Act. The only exception is if the specific contract states otherwise, such as a re-negotiation clause. Under the LIBOR Act there is no process for borrowers to demand another rate, it will simply move to CME Term SOFR.

Non-Performing LIBOR Loans

- For non-performing loans that define the default interest rate as a LIBOR basis, as long as the contract is in effect post June 30, 2023, and references LIBOR in the contract, and is under US law, for both performing and non-performing loans, then it is potentially covered by the LIBOR Act. It then depends on what the fallback language is for LIBOR in that specific loan contract. If there is no fallback, then it is covered by the LIBOR Act and is you would cross out LIBOR legally and replace it with the FRB selected benchmark replacement, which would apply to the regular interest charge and any penalty charge for non-payment, as long as this penalty rate was initially based on LIBOR.

Regulatory Highlights

- ARRC published the readout from the April 20 meeting. Report is available [here](#) and meeting minutes are available [here](#).
- ARRC issued a summary and update to its Term SOFR scope of use recommendations. Summary and update are available [here](#).
- ARRC published the readout from the May 25 meeting. Report is available [here](#) and meeting minutes are available [here](#).
- ARRC statement on the last 30 days before USD LIBOR ends. Statement is available [here](#).
- ISDA published the ISDA-Clarus RFR Adoption Indicator for April 2023. Report is available [here](#).
- ISDA published the ISDA-Clarus RFR Adoption Indicator for May 2023. Report is available [here](#).
- ISDA article on Updating Term SOFR. Article is available [here](#).
- SEC examination of LIBOR transition preparedness. Report is available [here](#).
- Analysis: As sun sets on LIBOR, its successor rate may heighten bank risks. Article is available [here](#).
- FCA final messages before USD LIBOR cessation on June 30. Statement is available [here](#).
- CME published the rates recap for June 2023. Report is available [here](#)
- ARRC Designates Peter Phelan as new Chair. Article is available [here](#).

ARRC Working Group Updates

- ARRC webinar on using the Depository Trust & Clearing Corporation (DTCC) LIBOR replacement index communication tool. Announcement is available [here](#) and webinar is available [here](#).
- ARRC published the readout from the June 22 meeting. Report is available [here](#).
- ARRC designated Peter Phelan as Chair, replacing Tom Wipf. Statement is available [here](#).
- ARRC relaxes limits on trading Term SOFR derivatives. Article is available [here](#).

ISDA Updates

- ISDA published the ISDA-Clarus RFR Adoption Indicator for March 2023. Report available [here](#)
- ISDA SwapsInfo market data for Q1 of 2023. Report available [here](#)
- ISDA report on the transition to RFR for Q1 of 2023. Report available [here](#)
- ISDA's first webinar on IBOR fallbacks. Video available [here](#)
- ISDA's second webinar on IBOR fallbacks Q&A. Video available [here](#)
- ISDA's third webinar on IBOR fallbacks Q&A. Video available [here](#)
- ISDA's fourth webinar on IBOR fallbacks Q&A. Video available [here](#)
- ISDA's fifth webinar on IBOR fallbacks Q&A. Video available [here](#)
- ISDA's sixth webinar on IBOR fallbacks Q&A. Video available [here](#)
- ISDA's seventh webinar on IBOR fallbacks Q&A. Video available [here](#)
- ISDA webinar on the end of Canadian Alternative Reference Rate (CARR) and the transition from Canadian Dollar Offered Rate (CDOR) to Canadian Overnight Repo Rate Average (CORRA). Video available [here](#)
- ISDA webinar on USD LIBOR Final Steps. Video available [here](#)
- Tom Wipf/David Bowman IBOR transition discussion. Video available [here](#)

ICE / CME Updates

- CME published the rates recap for April 2023. Report available [here](#)
- CME published the rates recap for May 2023. Report available [here](#)
- CME updated the terms for Term SOFR use/licensing. FAQ available [here](#)
- ICE published the Interest Rates Report monthly newsletter. Report available [here](#)

Other News / Useful Reading

- Tradeweb lodges MAT application for SOFR and Sonia swaps. Article available [here](#)
- Joint statement on completing the LIBOR transition by five federal regulatory agencies. Statement available [here](#)
- Financial Stability Board statement on final preparations for the USD LIBOR transition. Press release available [here](#)
- Easing of trading curbs is no quick fix for Term SOFR swaps. Article available [here](#)
- FRB's Bowman confirms interdealer Term SOFR ban. Article available [here](#)
- [Counting down to dollar LIBOR transition](#). Article available [here](#)
- Forward Rate Agreement-Overnight Index Swap (FRA-OIS) demise leaves hole in bank treasury risk management. Article available [here](#)
- LCH SwapClear completes Libor to SOFR transition. Article available [here](#)

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- D-day for the rates market: solving the outstanding issues in US LIBOR transition. Article available [here](#)
- Regional banks face soaring Term SOFR spreads. Article available [here](#)
- LIBOR will at last be switched off in June. Article available [here](#)
- LIBOR's long goodbye. Article available [here](#)
- Loan market braced for rush to LIBOR finish line. Article available [here](#)
- Synthetic rate could sabotage USD LIBOR's end. Article available [here](#)
- US interest rate swap market embraces new rate as LIBOR deadline nears. Article available [here](#)
- Banks mull structures notes as Term SOFR basis hedge. Article available [here](#)
- The last days of LIBOR: ARRC appoints new chair. Article available [here](#)
- Term SOFR derivatives: the ARRC's latest usage guidelines. Article available [here](#)
- The end of LIBOR: The Grand Finale...or is it? . Article available [here](#)
- Dealers commence tackling US LIBOR swaptions transition. Article available [here](#)
- The International Organization of Securities Commissions (IOSCO) finds CSRs not reliable enough as alternatives to USD LIBOR. Article available [here](#)
- IOSCO Statement on Alternatives to USD LIBOR. Article available [here](#)

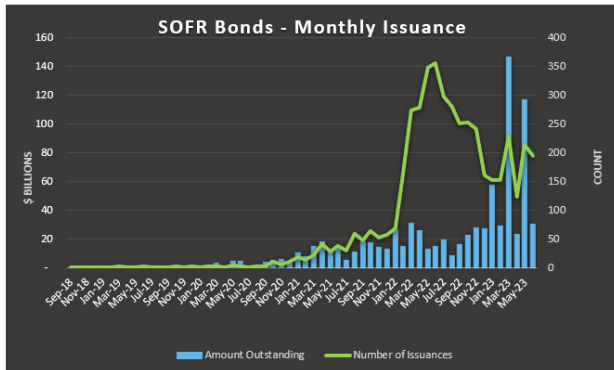


Decrease in Debt Issuance Referenced to SOFR

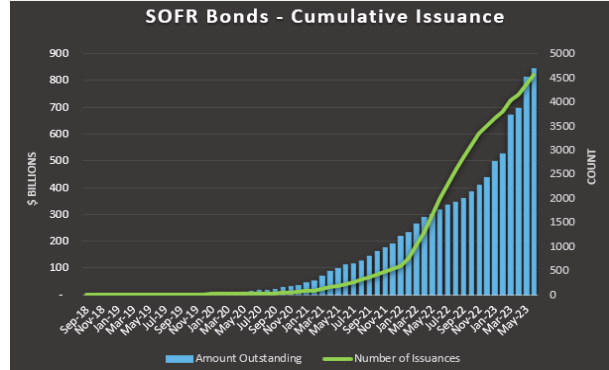
The issuance of SOFR referenced debt decreased in June 2023 compared to issuance in May 2023. The issuance size was \$30.3 billion in June 2023, which decreased from \$116.9 billion in May 2023. The graphs below represent data through June 2023.

The cumulative issue size of SOFR bonds outstanding (this excludes matured bonds) is currently \$851 billion with 4,598 bonds through July 06, 2023. There were 195 new issuances in June 2023 compared to 214 in May 2023 and 124 in April 2023.

In June 2023, federal agencies issued 24 SOFR referenced floating rate notes (FRN)s worth \$16.3 billion. There were 171 issuances from other institutions that contributed \$14 billion to the outstanding amount of SOFR referenced debt.



Source: Reuters, compiled by Deloitte
*Data as of June 30, 2023

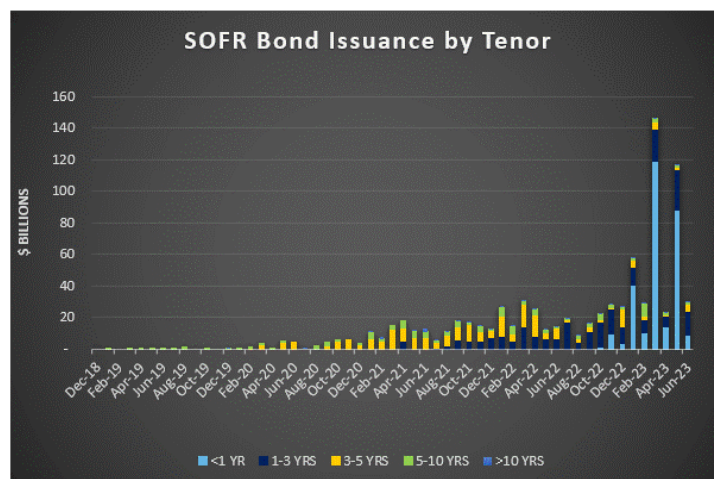


Source: Reuters, compiled by Deloitte
*Data as of June 30, 2023

Increase in Longer Dated Debt Issuance (maturity between 5- 10 years) Referenced to SOFR

SOFR debt issuances with a maturity between 5 and 10 years increased in June 2023 compared to May 2023. During June 2023, there were 77 bonds issued that have a maturity between 5 and 10 years, compared to 58 issuances in May 2023. There were 2 issuances during June 2023 that had a maturity greater than or equal to 10 years, as compared to 5 such issuances with a maturity greater than or equal to 10 years for May 2023.

There were 1,147 issuances of SOFR bonds outstanding worth \$94.5 billion, with a maturity greater than or equal to 5 years, through July 06, 2023, including 194 issuances worth \$11.3 billion with a term greater than or equal to 10 years.

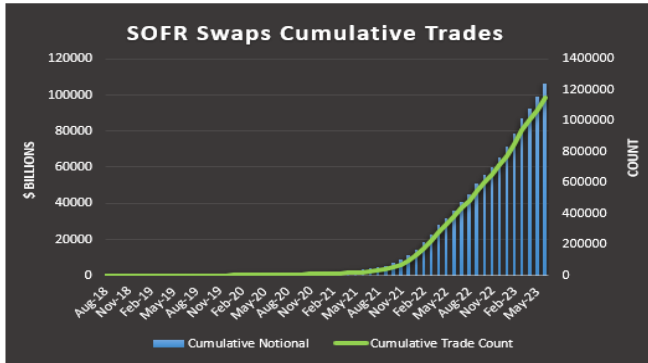


Source: Reuters, compiled by Deloitte
*Data as of June 30, 2023

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Cumulative SOFR Interest Rate Derivatives

SOFR Swaps

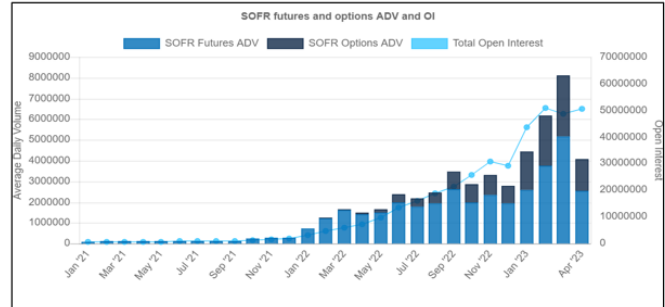
- The cumulative outstanding notional amount for SOFR based interest rate and basis swaps totaled \$106,907.5 billion through June 30, 2023.
- For the month of June 2023, the notional volume of SOFR-based interest rate and basis swaps totaled \$7,492.9 billion compared to \$6,510.8 billion in May 2023 and \$5,173.9 billion in April 2023.



Source: <http://swapsinfo.org/>, compiled by Deloitte
 *Data as of June 30, 2023

SOFR Futures

- CME website is currently updated with data until April 2023. According to data available on CME, for April 2023, SOFR futures and options average daily volume reached ~2.6M and ~1.5M contracts/ day, respectively. The data is available [here](#).
- The month-end open interest for SOFR 1-month and 3-month futures as of April 2023 was ~50.4M contracts.



Source: CME Group
 *Data as of April 30, 2023

Global IBOR Activity

The market activity in Sterling Overnight Index Average (SONIA), Tokyo Overnight Average Rate (TONAR), Euro Short-Term Rate (€STR), and Swiss Average Rate Overnight (SARON)-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 June 30, 2023.

| Alternative Reference Rate | Swaps Cumulative notional amount (US \$ Billions) | Bonds Cumulative issuance amount (US \$ Billions) |
|----------------------------|---|---|
| SONIA | 90,846.1 | 236.9 |
| SARON | 1,759.2 | NA |
| TONAR | 7,702.6 | NA |
| €STR | 60,374.3 | 17.1 |

Source: Reuters, <http://swapsinfo.org/>, compiled by Deloitte
 Swaps and Bonds data are as of June 30, 2023



United Kingdom

- FCA feedback statement for Consultation Paper CP22/21. Report available [here](#)
- UK regulator makes 'final call' to switch off LIBOR. Article available [here](#)
- FCA extends synthetic USD LIBOR to September 2024. Article available [here](#)
- THE USD LIBOR panel ceases at end-June 2023: Are you ready? Article available [here](#)

European Union

- The Eurodollar Is No More... Article available [here](#)
- Euro Across-the-Curve (AXI) rate proposed as Euribor fallback. Article available [here](#)
- Public consultation begins on Refinitiv Term €STR. Article available [here](#)
- CME converted your Eurodollars. This is what happened next. Article available [here](#)

Asia

- Reserve Bank of India tells banks to complete transition from LIBOR by July. Article available [here](#)
- OSTTRA releases cross-currency swap conversion service ahead of LIBOR cessation. Article available [here](#)
- Hedge funds boost new TONAR futures market. Article available [here](#)
- Singapore bids LIBOR farewell with surge in Singapore Overnight Rate Average (SORA) derivatives. Article available [here](#)

Contact Us

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