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ISDA Announces Preliminary Results of LIBOR Pre-cessation Fallbacks Consultation

By [Paul Hastings LIBOR Transition Task Force](#)

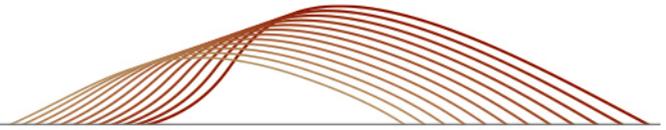
On April 15, 2020, the International Swaps and Derivatives Association, Inc. (“ISDA”) announced preliminary results of its second consultation (the “Consultation”) on the implementation of pre-cessation fallback triggers for derivatives transactions referencing the London Interbank Offered Rate (“LIBOR”).¹ A final report analyzing the results of the Consultation and information on next steps will be made available by ISDA in the coming weeks.

Preliminary Results

ISDA announced that the initial results indicate that a significant majority of respondents were in favor of including both permanent cessation and pre-cessation fallback triggers with respect to LIBOR in the amended 2006 ISDA Definitions (the “Definitions”) and in a single protocol addressing legacy trades.² While the results of the Consultation are still subject to ongoing analysis, ISDA expects to move forward applying both pre-cessation and permanent cessation fallbacks to all new and legacy derivatives referencing LIBOR that incorporate the Definitions. Certain other interbank offered rates (“IBORs,” and together with LIBOR, “Covered IBORs”), however, will continue to include permanent cessation fallback triggers only.

Background

- ISDA originally planned to enable market participants to incorporate permanent cessation triggers, but not pre-cessation triggers, of Covered IBORs and corresponding fallbacks into their future and existing derivatives contracts by publishing a supplement (the “Supplement”) to the Definitions and an ISDA protocol.
- **FSB March 2019 Letter**: The Financial Stability Board’s Official Sector Steering Group (the “FSB”) requested ISDA to obtain market feedback regarding the addition of a fallback trigger based on a non-representativeness determination of a rate by the U.K. Financial Conduct Authority (the “FCA”) or any other relevant regulatory authority (a “Pre-Cessation Event”).³
- **ISDA May 2019 Consultation**: ISDA published its first consultation on Pre-Cessation Event triggers for feedback on the preferred approach for addressing Pre-Cessation Events—the results found that while market participants generally would not want to continue using a Covered IBOR after a Pre-Cessation Event, there was no consensus on how to implement the pre-cessation fallbacks.



- **FSB November 2019 Letter/ISDA Response:** The FSB expressed its view that Pre-Cessation Event triggers relating to LIBOR, along with permanent cessation triggers, should be included in the Supplement to the Definitions and in an ISDA protocol.⁴ As a response, in December 2019, ISDA noted that it would continue to work to build a consensus on the implementation of Pre-Cessation Event trigger fallbacks.⁵
- **ISDA February 2020 Consultation:** After receiving feedback from the FCA and the ICE Benchmark Administration on the length of time a non-representative LIBOR would be published,⁶ and observing through LCH's consultation how central counterparties would react to a Pre-Cessation Event,⁷ ISDA published the Consultation on February 25, 2020, which remained open for market participant feedback until April 1, 2020.

Conclusion

With LIBOR's anticipated cessation expected to occur at the end of 2021, market participants are encouraged to familiarize themselves with the relevant risk-free rates, such as the Secured Overnight Financing Rate ("SOFR").⁸ In 2019, interest rate derivatives ("IRD") contracts referencing USD LIBOR amounted to \$119.4 trillion of traded notional, accounting for 46.8% of total IRD-traded notional, while IRD contracts referencing SOFR totaled \$392.7 billion and represented only 0.15% of total IRD-traded notional.⁹

The significant portion of IRD contracts that still reference LIBOR underscores the need to build appropriate triggers into legacy and new derivatives contracts. Although ISDA will be publishing a Supplement to the Definitions and a protocol to address permanent cessation event triggers and Pre-Cessation Event triggers, market participants should actively focus on transitioning away from LIBOR to avoid potential market disruptions.



If you have any questions concerning these developing issues, please do not hesitate to contact any of the following Paul Hastings lawyers:

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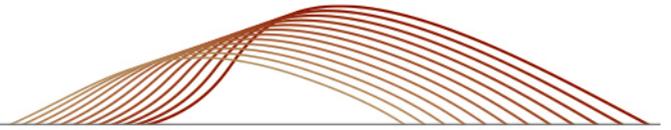
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¹ "ISDA Announces Preliminary Results of Consultation on Pre-cessation Fallbacks for LIBOR," available [here](#).

² *Id.*

³ The FSB's March 2019 letter to ISDA is available [here](#).

⁴ The FSB's November 2019 letter to ISDA is available [here](#).

⁵ ISDA's December 2019 letter to the FSB is available [here](#).

⁶ The FCA's January 2020 letter to ISDA is available [here](#), and the ICE Benchmark Administration's January 2020 letter to ISDA is available [here](#).

⁷ LCH is a British clearinghouse that serves major international exchanges and certain OTC markets. LCH's January 2020 consultation is available [here](#).

⁸ For more information on SOFR, the Alternative Reference Rates Committee's recommended risk-free rate fallback to USD LIBOR, please see our publications, "ARRC Releases White Paper Regarding SOFR – The New U.S. Dollar LIBOR Alternative," available [here](#), and "ARRC Releases Practical Implementation Checklist for SOFR Adoption," available [here](#).

⁹ ISDA, Interest Rate Benchmarks Review: Full Year 2019 and the Fourth Quarter of 2019, at 2-3 (Jan. 2020), available [here](#).

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