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Federal Reserve Issues Proposed Rules under LIBOR Act



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On July 19, the Federal Reserve issued a [notice of proposed rulemaking](#) (“NPR”) that would implement the Federal LIBOR Act. The NPR focuses primarily on identifying the particular version of SOFR that will apply to legacy contracts covered by the Act. For contracts that reference 1-, 3-, 6- or 12-month LIBOR, the NPR would apply the following SOFR-based rates plus a spread adjustment (as specified in the Act):

- For most contracts and securities, Term SOFR rate with a comparable tenor;
- For derivatives, the SOFR rate used in the ISDA protocol (30-day compounded SOFR in arrears);
- For contracts and securities issued by the GSEs (Freddie, Fannie), 30-day average SOFR; and
- For consumer contracts, Term SOFR but the spread adjustment would be implemented over a one-year period starting with the end of LIBOR.

The NPR also requests comment on “synthetic” LIBOR. The UK’s Financial Conduct Authority has indicated that it may direct the LIBOR administrator to publish a “synthetic” version of USD LIBOR after June 30, 2023 (which would primarily be designed to assist non-U.S. law contracts that reference USD LIBOR and that are not covered by the Act). If “synthetic” LIBOR were published, it would no longer be a “representative” rate, but it could arguably be considered to be “available” under the language of legacy contracts that do not include a “pre-cessation trigger” (*i.e.*, a trigger to replace LIBOR when LIBOR is no longer representative). The Federal Reserve stated that it believes that it is consistent with the purpose of the Act for those contracts to fall back to their replacement rate even if LIBOR continues to be published in its synthetic form. It is requesting comment on whether, for clarity, the final rule should allow a determining person to replace LIBOR with the benchmark specified in the contract, even in the event a nonrepresentative rate

called “LIBOR” in the form of synthetic LIBOR continues to be published on or after the LIBOR replacement date.

The proposed rulemaking also addresses other issues of importance to the market:

- Many legacy contracts (especially in the consumer space) reset their interest rate by “looking back” to the LIBOR rate in effect at an earlier date (e.g., 45 days). The proposed rule clarifies that if the reset occurs after the LIBOR Replacement Date (i.e., June 30, 2023) but looks back to a date occurring *before* the LIBOR Replacement Date (when LIBOR was still available), then the reset would be based on LIBOR (until a reset that looks back to a date occurring *after* the LIBOR Replacement Date).
- In general, the Act does not apply to legacy LIBOR contracts that have fallbacks to specific non-LIBOR rates (such as Fed Funds or Prime). However, the NPR would clarify that a determining person may choose the SOFR-based rate identified by the Fed.

Finally, the transition from LIBOR to SOFR-based rates will require some technical changes to legacy LIBOR contracts to administer the new rate (known as “Benchmark Replacement Conforming Changes”). The Act contemplates that Fed rule-making may define the scope of such changes that become a part of the legacy contract by operation of the Act. Changes to non-consumer contracts are also permitted if required in the reasonable judgment of the person calculating payments under the legacy contract. However, the Fed declined to recommend any such Benchmark Replacement Conforming Changes at this time, but specifically asked for comment on this issue.

Comments on the proposal are due 30 days after publication in the Federal Register.
