
*Summary of Responses to the ISDA 2020
Consultation on How to Implement Pre-
Cessation Fallbacks in Derivatives*

PREPARED FOR

International Swaps and Derivatives Association
("ISDA")

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This report was prepared for ISDA by The Brattle Group (“Brattle”). Brattle assists clients in a wide range of litigation and consulting matters. Brattle provides expert testimony, analysis, and financial economic consulting in litigation and regulatory matters affecting, among others, financial institutions. Our experts include former senior staff of large financial institutions, as well as former regulators and senior government officials, allowing us to provide our clients with detailed, real-world knowledge of how various financial institutions actually operate. All results and any errors are the responsibility of the authors and do not represent the opinion of Brattle or its clients.

Brattle has been engaged by ISDA to provide an independent summary and analysis of the market participant responses to the ISDA 2020 consultation pre-cessation fallbacks in LIBOR derivatives (the “2020 pre-cessation consultation”). Brattle understands that ISDA will rely on the analysis contained in this report to determine whether it should add a pre-cessation trigger to the permanent cessation fallbacks that it is implementing for IBORs in its standard documentation for derivatives.

As part of this analysis, Brattle reviewed the content of all responses to the 2020 pre-cessation consultation, and evaluated (based on the number and diversity of respondents), with input from ISDA’s legal advisor, the degree to which the process followed by ISDA allowed for the consideration of different market perspectives. This report also presents areas of consensus across respondents and areas where any new or additional considerations were raised.

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I. Executive Summary

1. On February 24, 2020, the International Swaps and Derivatives Association, Inc. (“ISDA”) published a market-wide consultation on whether to add a pre-cessation trigger to the permanent cessation fallbacks for IBOR derivatives in its standard documentation (“2020 Pre-Cessation Consultation”).¹ The 2020 Pre-Cessation Consultation is the second consultation on pre-cessation issues. ISDA issued the first consultation on pre-cessation issues on May 16, 2019 (“2019 Pre-Cessation Consultation”) the results of which were summarized in a report by The Brattle Group (commissioned by ISDA).²

2. Although a significant majority of respondents (71.9%) to the 2019 Pre-Cessation Consultation preferred to not continue referencing IBORs in future derivative contracts following a public statement by a regulator that such IBORs were no longer representative, the respondents expressed a wide variety of views regarding whether and how to implement a pre-cessation fallback trigger related to non-representativeness in derivatives.

3. Following the publications of the results of the 2019 Pre-Cessation Consultation, the Financial Stability Board Official Sector Steering Group (“FSB OSSG”) requested³ that ISDA include a pre-cessation trigger alongside the permanent cessation triggers as standard language in its fallbacks for IBOR derivatives. ISDA responded to the FSB OSSG⁴ that it would continue with the finalization of permanent cessation fallbacks while simultaneously working with regulators and the industry to increase market understanding of the implications of ‘non-representative’ IBORs, and attempting to build consensus on how to implement fallbacks following the occurrence of a pre-cessation trigger. ISDA subsequently announced that it would re-consult on the implementation of pre-cessation fallbacks in derivatives before delivering a fallback documentation solution.⁵

¹ <https://www.isda.org/a/iioTE/2020-Consultation-on-Pre-Cessation-Issues-Final.pdf>.

² <https://www.isda.org/a/kkaTE/2019.10.21-Anonymized-Pre-Cessation-Consultation-Report.pdf>.

³ <https://www.fsb.org/wp-content/uploads/P191119.pdf>.

⁴ <https://www.isda.org/a/IwcTE/December-2019-Letter-to-the-FSB-OSSG-FINAL.pdf>.

⁵ <https://www.isda.org/2020/02/05/isda-to-re-consult-on-pre-cessation-fallbacks/>.

4. Since ISDA's 2019 Pre-Cession Consultation, the market had received several pieces of additional information.⁶ LCH and several central clearing counterparties ("CCPs") made statements related to ISDA's letter.⁷ On January 10, 2020, LCH launched a consultation regarding pre-cessation triggers.⁸ On January 20, 2020, the UK Financial Conduct Authority ("FCA") sent a letter to ISDA providing additional information to the market on a 'non-representative' LIBOR scenario.⁹ On January 24, 2020, the ICE Benchmark Administration ("IBA") sent ISDA a letter, explaining how it would respond to a determination by the UK FCA that LIBOR is no longer representative.¹⁰ ISDA therefore published the 2020 Pre-Cession Consultation to solicit current market participant feedback. The 2020 Pre-Cession Consultation primarily contained one binary question (i.e., a question with either a "Yes" or "No" answer), asking whether ISDA should "publish a Supplement to the 2006 ISDA Definitions so that the Rate Options for LIBOR in the relevant currencies (USD, GBP, CHF, JPY, EUR) all contain fallbacks that would apply upon the first to occur of (i) a permanent cessation trigger or (ii) a 'non-representativeness' pre-cessation trigger, and publish a Protocol to allow adherents to include the amended definitions (i.e., the definitions with the combined permanent cessation and pre-cessation fallback provisions) in all of their legacy contracts with other adherents."¹¹ Respondents were informed that any responses that did not clearly indicate "Yes" or "No" would not be counted towards the assessment of the Criteria. The Consultation also asked respondents who selected "No" to indicate whether they would be "unavoidably harmed by, and/or unable to use, a Supplement and Protocol that implement pre-cessation fallback provisions." ISDA communicated the 2020 Pre-Cession Consultation widely with market participants, with a link to the Consultation being sent to more than 60,000 recipients.¹²

⁶ This is summarized by ISDA in the 2020 Pre-Cession Consultation (<https://www.isda.org/a/iioTE/2020-Consultation-on-Pre-Cession-Issues-Final.pdf>).

⁷ <https://www.youtube.com/watch?v=kGHrNSTyUM&feature=youtu.be>.

⁸ <https://www.lch.com/membership/ltd-membership/ltd-member-updates/lch-limited-rule-change-committee-10-january-2020>.

⁹ <https://www.isda.org/a/E1LTE/FCA-letter-to-ISDA-on-Non-representative-LIBOR-January-2020.pdf>.

¹⁰ <https://www.isda.org/a/M1LTE/IBA-Letter-to-ISDA.pdf>.

¹¹ <https://www.isda.org/a/iioTE/2020-Consultation-on-Pre-Cession-Issues-Final.pdf>.

¹² ISDA also conducted a webcast to further explain the Consultation. Market participants received communication from ISDA about the webcast, the recording of the webcast, as well as the deadline of the Consultation, with a number of reminders. Further, in response to changes in market conditions due to COVID-19, ISDA extended the original Consultation deadline by one week to allow market participants extra time to respond to the Consultation.

5. Due to the mixed feedback ISDA received from market participants in the 2019 Pre-Cessation Consultation, and to provide transparency on ISDA’s approach to the 2020 Pre-Cessation Consultation, in advance of issuing the 2020 Pre-Cessation Consultation, ISDA established certain criteria and communicated that if these criteria were satisfied, ISDA intended to publish the Supplement and Protocol as described in the 2020 Pre-Cessation Consultation. ISDA also communicated that any counterparties that did not want to use this approach would be able to bilaterally negotiate fallback terms outside of the standard ISDA Definitions and related Protocol.

6. The criteria specified in the ISDA 2020 Pre-Cessation Consultation intended to achieve:

- a minimum number of 70 responses from market participants (which do not include professional services firms or trade associations);
- a minimum of 35% of responses from market participants other than banks/broker-dealers and infrastructure providers;
- a minimum of 65% “Yes” responses from market participants and at least 35% of those “Yes” responses from market participants who are not bank/broker-dealers or infrastructure providers; and
- assurance that no major portion of a particular segment of the market would be unavoidably harmed and/or be unable to use the Supplement and Protocol.¹³

7. A total of 142 entities submitted valid responses to the 2020 Pre-Cessation Consultation, of which 138 were market participant respondents¹⁴ and four were professional services firms or trade associations. Collectively, the responses to the 2020 Pre-Cessation Consultation represent a diverse group of industry affiliations, reflecting different perspectives from different industries and regions. All of the above criteria were met, and further details are discussed in Section III of this report.

8. 91% of the market participant respondents to the 2020 Pre-cessation Consultation (126 out of 138 respondents) answered “Yes” to the Consultation question. Some “Yes” respondents chose

¹³ The 2020 Pre-Cessation Consultation criteria provided: “Respondents who select ‘No’ *and* indicate that they would be unavoidably harmed by, and/or unable to use, such a Supplement and Protocol do not represent a significant portion of a particular segment of the market.”

¹⁴ The 2020 Pre-Cessation Consultation was open to anyone (including ISDA members and non-members) but the criteria to determine the outcome of the Consultation were based on the number of market participant respondents, which do not include professional firms or trade associations.

to provide additional explanation for their responses. A key reason cited by several of these respondents is the need for consistency across asset classes (most often discussed as consistency between cash and derivative markets by respondents) and between cleared and non-cleared derivative markets. These respondents noted that the inclusion of a pre-cessation trigger for OTC derivative contracts would be in alignment with what is happening in the cash markets, as well as with the arrangements expected to apply to cleared derivatives like swaps. A number of other market participants cited general support for the Consultation, noting that it would be challenging to use non-representative benchmarks.

9. Consistency (across asset classes and markets) was brought up as an important consideration by several market participant respondents who answered “Yes” to the Consultation question.¹⁵ Most respondents who brought up this topic highlighted consistency in the context of the inclusion of a pre-cessation trigger (in the derivative markets and markets for other products, as well as in the cleared and non-cleared derivatives markets). A few respondents emphasized consistency in the definition of triggering events, in the timing of triggering events and in the calculations of the spread adjustment.¹⁶ However, while some respondents cited consistency as a reason for their “Yes” answer, others brought up consistency to emphasize the need for regulators and relevant authorities to coordinate and ensure that the same approach would apply across markets, noting that consistency was not a given at this time. Some respondents even highlighted that actual consistency was a condition for their “Yes” response. Further, as described below, several market participant respondents who answered “No” also cited consistency as the reason for their “No” response.

10. Respondents who answered “Yes” also brought up a number of other considerations. Several respondents expressed concerns around the clarity of the announcement of the pre-cessation event, with some indicating that their “Yes” response was conditional on the pre-cessation trigger being worded in a clear manner. Other respondents who answered “Yes”

¹⁵ Out of a total of 138 market participant respondents to the 2020 Pre-Cessation Consultation, only 57 respondents provided further comments/explanations to their answers. More than half of these respondents mentioned or discussed the topic of consistency.

¹⁶ Consistency has been a topic raised repeatedly by market participants in prior consultations. For example, see section V of the Brattle Group Report “Anonymized Summary of Responses to the ISDA Supplemental Consultation on Fallbacks in Derivatives Referencing EUR LIBOR and EURIBOR and Other Less Widely Used IBORs”, March 5, 2020 and the discussion on Question No. 3 of the Final Parameters Consultation (“Summary of Responses to the ISDA Consultation on Final Parameters for the Spread and Term Adjustments”, November 15, 2019).

expressed their preference to not allow for optionality in the Protocol because they believed this would result in implementation challenges and fragmented markets.

11. Consistency across asset classes and markets appears to have been a central consideration amongst all respondents who responded “Yes” and “No” alike. Of the 12 market participant respondents who answered “No” to the Consultation question, several expressed concerns around consistency, highlighting the hedging risk due to potential inconsistencies across asset classes/markets as the rationale for their “No” answer. One such respondent in particular acknowledged what was discussed by the “Yes” responses, stating that it understood that “other asset classes [(e.g., cleared derivatives)] are moving in the direction of adopting a ‘non-representativeness’ pre-cessation fallback trigger...and alignment across asset classes is desirable.” This respondent nevertheless selected “No” since “it is more preferable for there to be consistency within an asset class [(e.g., non-cleared derivatives)]. [Non-cleared] derivatives which reference one IBOR rate should transition away from that rate at the same time (i.e., at the time of a permanent cessation).”

12. Some respondents who answered “No” indicated that they would not be able to adhere to a Protocol that included a pre-cessation trigger. A few other respondents cited anecdotal evidence that other market participants would not adhere to a Protocol that includes a pre-cessation trigger, and therefore, the inclusion of a pre-cessation trigger would negatively impact the market adoption rate of ISDA’s IBOR fallbacks Protocol. Seven respondents indicated that the inclusion of the pre-cessation fallback provisions would result in harmful consequences for themselves and/or other market participants. A number of other reasons were cited in support of the “No” responses, such as the potential for pre-cessation fallbacks to add uncertainty/complexity, impede the ability of market makers to price the transition into a permanent cessation, and increase the fragmentation of the market. One respondent in particular noted that there are other (better) means for ensuring that the cash and derivatives market will not be confronted with various pre-cessation dates.

13. A majority of market participant respondents that participated in both the 2019 and 2020 Pre-Cessation Consultations agreed with the inclusion of a pre-cessation trigger in the ISDA 2006 Definitions Amendment in response to the 2020 Pre-Cessation Consultation. The market participant respondents that did not support the inclusion of a pre-cessation trigger in response to the 2020 Pre-Cessation Consultation cited similar considerations in response to both Pre-Cessation Consultations; including maintaining consistency across asset classes and optionality/flexibility preferences. Further, those respondents who answered “No” to Question No. 5 in the 2019 Pre-

Cessation Consultation generally cited the same concerns as the respondents who answered “No” to the 2020 Pre-Cessation Consultation.

II. Demographics of Respondents to the 2020 Pre-Cessation Consultation

14. ISDA received responses from 142 respondents from 19 countries across Europe, Asia-Pacific, and the Americas. Collectively, the responses to the 2020 Pre-Cessation Consultation represent a diverse group of different industries and regions. Table 1 summarizes the industry affiliation, as self-identified by each of the 142 respondents based on ten categories¹⁷ included in the 2020 Pre-Cessation Consultation. Table 1 shows that the 142 respondents fall most commonly in the categories of “Bank/Broker-dealer” (52 respondents), “Pension Fund” (34 respondents), “Asset Manager” (19 respondents) and “Local or regional government entity/government sponsored entity” (16 respondents). In addition, the respondents include a few hedge funds, insurance companies, central counterparties, professional services firms/trade associations and some other end users. Note that while Brattle reviewed all 142 responses, we do not include the preferences from the four professional service firms/trade associations in the assessment of the 2020 Pre-Cessation Consultation criteria.

¹⁷ One of the categories is “Energy/Commodity firms”. However, there was no respondent that self-classified into this category, therefore Table 1 only has nine categories.

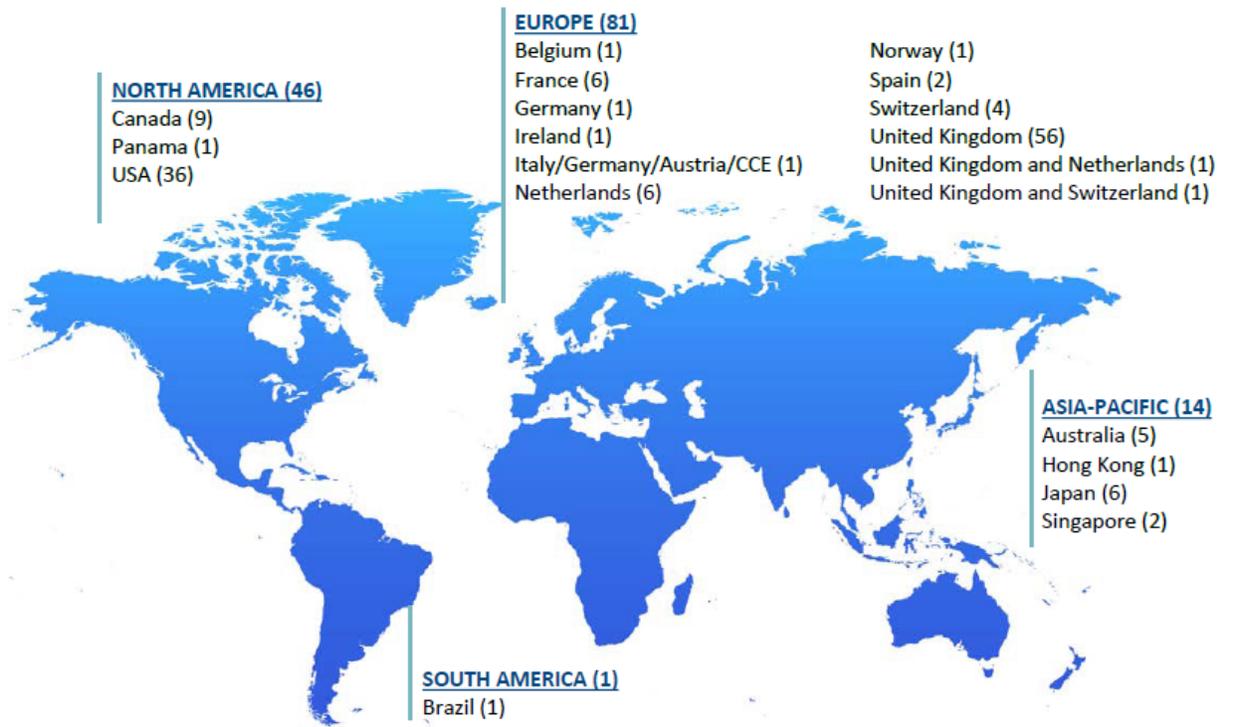
Table 1
Breakdown of Responses by Industry Affiliation

Respondent Type Industry Classification [A]	Number of entities [B]
[1] Asset Manager	19
[2] Bank/broker-dealer	52
[3] Hedge Fund	3
[4] Insurance Company	5
[5] Local or regional gov entity/gov sponsored entity	16
[6] Market Infrastructure - central counterparty	6
[7] Pension Fund	34
[8] Professional Services/Trade Association	4
[9] Other end user (e.g. corporate)	3
Total	142

Sources and notes: Respondent types as self-identified by the entities that responded to the ISDA 2020 Pre-Cessation Consultation. One entity self-identified as “Legal Counsel” which was not one of the respondent type options presented in the ISDA 2020 Pre-Cessation Consultation. This entity is included in the Bank/broker-dealer category.

15. Figure 1 and Table 2 break down the respondents by region and by country. The largest number of respondents by region (81 entities) came from Europe, including 56 entities from the United Kingdom. North America accounted for 46 of the responding entities, 36 of which came from the United States. There are 14 respondents from Asia-Pacific, mostly comprised of respondents from Japan (six entities) and Australia (five entities). There was one respondent from South America, specifically, Brazil.

Figure 1
Breakdown of Entities (Respondents) by Geography



Sources and notes: Regions and countries represented by the entities that responded to the ISDA 2020 Pre-Cessation Consultation. 142 entities total.

Table 2
Breakdown of Respondents (Entities) by Geography

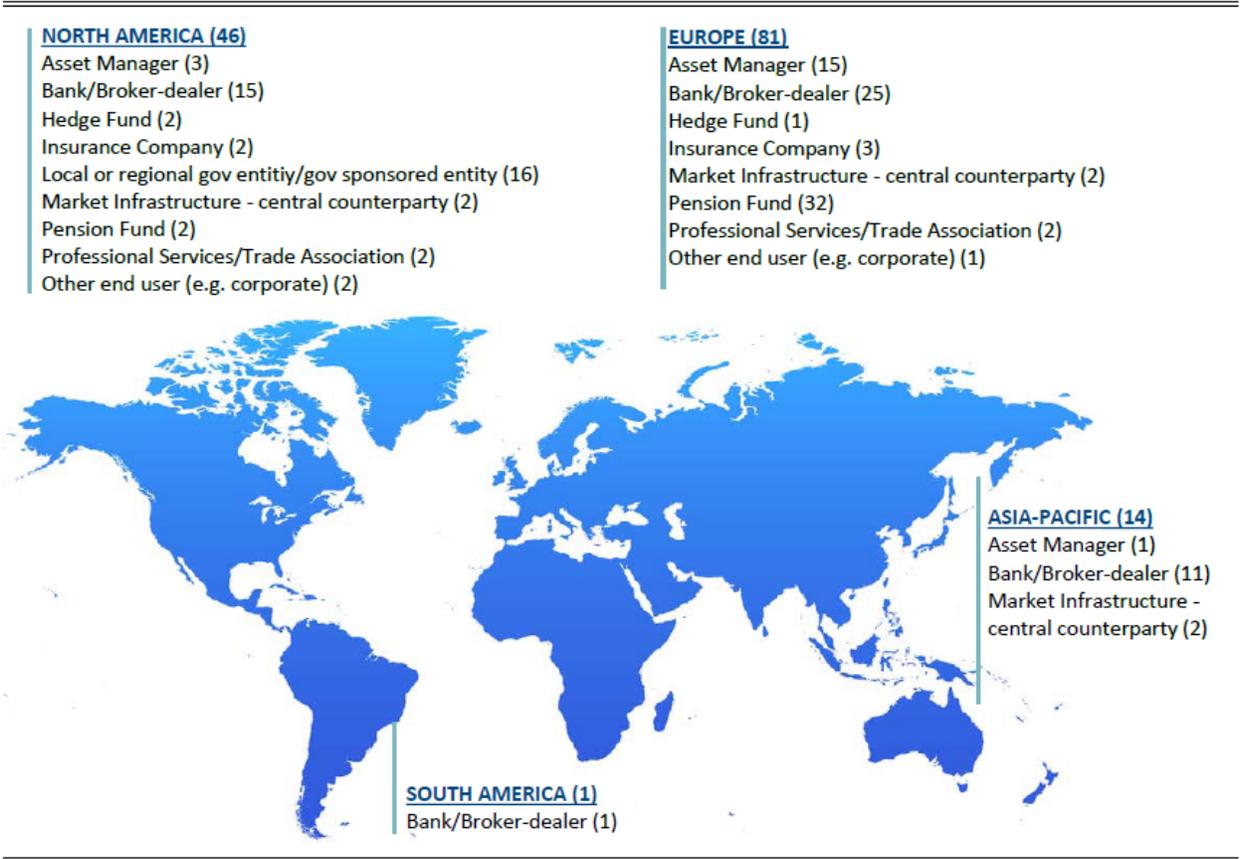
Region	Country	Number of entities
[A]	[B]	[C]
Asia-Pacific		14
	Australia	5
	Hong Kong	1
	Japan	6
	Singapore	2
Europe		81
	Belgium	1
	France	6
	Germany	1
	Ireland	1
	Italy/Germany/Austria/CEE	1
	Netherlands	6
	Norway	1
	Spain	2
	Switzerland	4
	United Kingdom	56
	United Kingdom and Netherlands	1
	United Kingdom and Switzerland	1
North America		46
	Canada	9
	Panama	1
	USA	36
South America		1
	Brazil	1
Total		142

Sources and notes: Regions and countries represented by the entities that responded to the ISDA 2020 Pre-Cessation Consultation.

16. Figure 2 summarizes the demographics of the respondents by both industry affiliation and geography. Figure 2 shows that the majority of pension funds and asset managers that responded to the 2020 Pre-cessation Consultation are from Europe. All of the local or regional government entities/government-sponsored entities that responded to the Consultation are from North America. In comparison, there are banks/broker-dealers across the Americas, Europe as well as Asia-Pacific that participated in the Consultation. Compared to the entities who responded to the

2019 Pre-Cessation Consultation, those who responded to the 2020 Pre-Cessation Consultation represented generally a wider range of industry affiliations. Bank/broker-dealers made up approximately half of all respondents to the 2019 Pre-Cessation Consultation compared to 37% of all respondents to the 2020 Pre-Cessation Consultation. The 2019 Pre-Cessation Consultation reflected responses from only two pension funds compared to the 34 pension funds that responded to the 2020 Pre-Cessation Consultation. While North America was the most represented region in the 2019 Pre-Cessation Consultation, 68% of the respondents to the 2020 Pre-Cessation Consultation were from outside of North America. The majority of respondents to the 2020 Pre-Cessation Consultation are from Europe.

Figure 2
Breakdown of Entities (Respondents) by Affiliation



Sources and notes: Regions and countries represented by the entities that responded to the ISDA 2020 Pre-Cessation Consultation. One entity self-identified as “Legal Counsel” which was not one of the respondent type options presented in the ISDA 2020 Pre-Cessation Consultation. This entity is included in the Bank/broker-dealer category. 142 entities total.

III. Assessing the Criteria of the 2020 Pre-Cessation Consultation

17. Table 3 summarizes the criteria set out in the 2020 Pre-cessation Consultation and the corresponding assessment based on the market participant responses to the consultation.

Table 3
Assessment of the 2020 Pre-cessation Consultation Criteria

Criteria		Satisfied (Yes/No)
At least 70 market participants submit responses, excluding professional services firms or trade associations	[A]	Yes
At least 35% of responses are from market participants other than bank/broker-dealers and infrastructure providers	[B]	Yes
At least 65% of respondents select “Yes”	[C]	Yes
At least 35% of those who select “Yes” are not bank/broker-dealers or infrastructure providers	[D]	Yes
Respondents who select “No” and indicate that they would be unavoidably harmed by, and/or unable to use, such a Supplement and Protocol do not represent a significant portion of a particular segment of the market	[E]	Yes

18. Table 4 shows the assessment of the first four criteria set out in Table 3. Overall, all criteria were met. With regard to the last criterion, of the 12 market participant respondents who selected “No”, ten indicated that they would be unavoidably harmed by, and/or unable to use the Supplement and Protocol as specified in the Consultation question. Of these ten market participant respondents, there are eight banks/broker-dealers (out of a total of 52 banks/broker-dealers who responded to the Consultation), one local or regional government entity/government sponsored entity (out of a total of 16) and one other end user (out of a total of 3). Therefore, respondents who selected “No” and indicated that they would be unavoidably harmed by, and/or unable to use, such a Supplement and Protocol did not represent a significant portion of a particular segment of the market.

Table 4
Assessment of the 2020 Pre-cessation Consultation Criteria

Criteria		Count of Relevant Responses	Count (%)	Consultation Criteria	Criterion Satisfied
		[1]	[2]	[3]	[4]
At least 70 market participants submit responses, excluding professional services firms or trade associations	[A]	138	NA	70	YES
Percentage of market participant respondents not Bank/broker-dealer OR infrastructure provider	[B]	80	58%	35%	YES
Percentage of market participant respondents that selected "YES"	[C]	126	91%	65%	YES
Percentage of market participant respondents that selected "YES" and are not Bank-broker-dealer OR infrastructure providers	[D]	78	62%	35%	YES

Notes:

[B][2]: [B][1]/[A][1].

[C][2]: [C][1]/[A][1].

[D][2]: [D][1]/[C][1].

IV. Preferences Regarding the 2020 Pre-Cessation Consultation

19. This section summarizes the responses to the question in the 2020 Pre-Cessation Consultation. As mentioned above, while Brattle reviewed all 142 responses to the 2020 Pre-Cessation Consultation, the criteria set by ISDA to assess the results are based on responses from market participants, which do not include professional services firms or trade associations.¹⁸ Subsections A and B analyze the responses from the 138 market participant respondents. For completeness, Brattle provides a discussion of the responses from the four professional services firms/trade associations in subsection C.

20. The 2020 Pre-Cessation Consultation asked whether ISDA should “publish a Supplement to the 2006 ISDA Definitions so that the Rate Options for LIBOR in the relevant currencies (USD, GBP, CHF, JPY, EUR) all contain fallbacks that would apply upon the first to occur of (i) a permanent cessation trigger or (ii) a ‘non-representativeness’ pre-cessation trigger, and publish a Protocol to allow adherents to include the amended definitions (i.e., the definitions with the combined permanent cessation and pre-cessation fallback provisions) in all of their legacy contracts with other adherents.” ISDA also specified in the Consultation that “the spread adjustment would be calculated as of the relevant announcement date regarding either ‘non-representativeness’ (i.e., the date that the UK FCA states that LIBOR ‘is no longer capable of being

¹⁸ <https://www.isda.org/a/iioTE/2020-Consultation-on-Pre-Cessation-Issues-Final.pdf> (“At least 70 market participants (which do not include professional services firms or trade associations[]) submit responses.”)

representative’) or ‘permanent cessation’, as applicable, but the fallback rates would not apply until the date on which that LIBOR is ‘non-representative’ (based on the statement by the UK FCA) or is discontinued...”

A. SUMMARY OF MARKET PARTICIPANT RESPONDENTS’ PREFERENCES

21. Table 5 summarizes the market participants’ responses to the question in the 2020 Pre-Cessation Consultation. Overall, Table 5 shows that 91% of market participant respondents (126 out of 138 market participant respondents) answered “Yes” to the Consultation question and 9% (12 out of 138 respondents) answered “No.”

Table 5
Summary Statistics of Responses to the 2020 Pre-Cessation Consultation

Response	Total	% of Total
Yes	126	91%
No	12	9%
Total	138	100%

22. Table 6 shows a breakdown of respondent preferences by affiliation. Of the 12 respondents that answered “No,” there are ten banks/broker-dealers. That means of the 52 banks/broker-dealers, 19% answered “No” and 81% answered “Yes” to the Consultation question. The remaining two respondents that answered “No” include one regional entity/government sponsored entity (out of 16 entities) and one other end user (out of three end users who responded). Most other industry affiliations, including asset managers, central counterparties, hedge funds, insurance companies, and pension funds, were unanimous in their preference (i.e., all respondents in these industry affiliations answered “Yes” to the Consultation question).

Table 6
Summary Statistics of Responses to the 2020 Pre-Cessation Consultation by Industry Affiliation

Respondent Type Industry Classification	Yes	No	Total	Yes (%)	No (%)
	[1]	[2]	[3]	[4]	[5]
Asset Manager	19	0	19	100%	0%
Bank/broker-dealer	42	10	52	81%	19%
Hedge Fund	3	0	3	100%	0%
Insurance Company	5	0	5	100%	0%
Local or regional gov entity/gov sponsored entity	15	1	16	94%	6%
Market Infrastructure - central counterparty	6	0	6	100%	0%
Pension Fund	34	0	34	100%	0%
Other end user (e.g. corporate)	2	1	3	67%	33%
Total Across All Market Participant Respondents	126	12	138	91%	9%

Notes:

[4]: [1]/[3].

[5]: [2]/[3].

23. Table 7 shows a breakdown of respondent preferences by region. Except for South America (which only has one respondent that answered “Yes”), each region has at least one respondent who answered “No”; however, the majority of respondents in every region answered “Yes” to the Consultation question.

Table 7
Summary Statistics of Responses to the 2020 Pre-Cessation Consultation by Respondent Region

Respondent Region	Yes	No	Total	Yes (%)	No (%)
	[1]	[2]	[3]	[4]	[5]
Asia-Pacific	13	1	14	93%	7%
Europe	73	6	79	92%	8%
North America	39	5	44	89%	11%
South America	1	0	1	100%	0%
Total Across All Market Participant Respondents	126	12	138	91%	9%

Notes:

[4]: [1]/[3].

[5]: [2]/[3].

B. COMMENTARY FROM MARKET PARTICIPANT RESPONDENTS

1. Review of “Yes” Responses

a) Primary Considerations Raised by “Yes” Responses

24. Of the 91% of overall respondents (126 out of 138 market participant respondents) that answered “Yes” to the Consultation question, 81 respondents did not provide further explanations for their answer. The remaining 45 respondents provided several rationales for their answers and highlighted a number of issues for ISDA to consider. A number of respondents cited general

support for ISDA to publish a Supplement to the 2006 ISDA Definition and the related Protocol, noting that it would be challenging to use non-representative benchmarks. Many respondents cited the need for consistency—across asset classes and between cleared and non-cleared derivative markets—as the underlying factor for their support to ISDA’s Supplement and related Protocol. Most respondents emphasized the need for consistency in the inclusion of a pre-cessation trigger across markets and products. A small number of respondents highlighted the need for consistency in the definition of triggering events, in the timing of the triggers, and in the calculation of the spread adjustment. It is worth noting that while a number of respondents cited consistency as the reason underlying their “Yes” answer, several other respondents who answered “Yes” brought up the issue of consistency mainly to emphasize the need for regulators/relevant authorities to coordinate and ensure consistency, noting that consistency was not a given at this time.

25. With regard to the need for consistency across asset classes, one European infrastructure provider stated “consistency between cash and derivative markets is very important. The inclusion of a ‘non-representativeness’ pre-cessation trigger for derivative contracts will be in alignment with ARRC recommendation for all cash products.” Similarly, a North American bank/broker-dealer said “Federal Reserve Board’s ARRC (Alternative Reference Rate Committee) committee has recommended inclusion of pre-cessation triggers for cash products including loans. As loans would include pre-cessation triggers, including parallel pre-cessation triggers in corresponding hedges (derivatives) would create more consistency between the fallback provisions of loans and the corresponding hedge, thereby maintaining the hedge’s effectiveness.” An Asian-Pacific bank/broker dealer agreed, stating “[i]n the absence of a pre-cessation trigger, we would be relying on ICE Benchmark Administration (IBA) to cease the rate within a reasonable time period after panel bank departures have rendered the rate non-representative and this in itself may have been sufficient. However we believe consistent fallback mechanics and unambiguous cessation triggers applying across the widest possible sweep of product segments to be highly desirable. Recommended template fallback language of other industry bodies (for example the Alternative Reference Rates Committee in respect of cash products and the Loan Market Association) already include pre-cessation triggers. It is however unfortunate that the derivative and non-derivative market segments are not aligned and this poses a genuine threat to orderly markets.” One North American bank/broker-dealer emphasized that the inclusion of a pre-cessation trigger would “[e]liminate basis risk between cash market transactions incorporating the 2019 ARRC

recommended triggers (i.e., FRNs, bilateral loans, syndicated loans and securitizations) and any related rate derivatives hedges governed by ISDA documentation.”

26. Several other respondents who answered “Yes” also brought up the issue of consistency across asset classes. However, rather than this being a reason supporting their “Yes” answer, these respondents emphasized the need for regulators and relevant authorities to coordinate and ensure consistency, noting that consistency was not a given at this time. For example, a North American asset manager stated “[w]e believe that consistency, where practicable, is important when making implementing fallback language. Because of a shift in the industry to greater incorporate a pre-cessation trigger in documents, we think it is appropriate for ISDA to adopt such a trigger in its 2006 definitions updates. This view is predicated on maintaining consistency with other cash asset classes: 1) fallback language generally includes a pre-cessation trigger; 2) the CCPs’ statements on rule book changes, where it has been stated that CCPs may trigger fallbacks on a ‘non-representativeness’ statement; and, 3) the guidance that the ARRC has provided regarding the potential legislative solution for legacy cash products which also includes a pre-cessation trigger. Due to the interconnectivity across markets, we prefer to avoid inconsistencies between a ‘cash asset’ and an associated ‘derivative hedge’. This support for this view is grounded in that consistency belief and if, for instance, the legislative solution was not going to be pursued, we would reconsider the appropriateness of ISDA including such a trigger.”

27. Similarly, one North American government-sponsored entity emphasized that its “primary focus is on consistency of rules between its derivative contracts and the financial instruments it hedges. Inconsistent triggering events between the Bank’s derivatives and cash products will almost certainly introduce risks that would make it extremely difficult to measure or manage.” A European bank/broker-dealer shared a similar view, emphasizing “the need of convergence between the derivatives and cash worlds in order to avoid any broken hedges and basis risks.” Another European bank/broker-dealer reiterated that “the pre-cessation trigger should not be considered for derivatives in isolation since there is a serious mismatch risk across other products. For this reason, it would be highly valuable when consistency is ensured across all products for example by liaising of ISDA with LMA and ICMA.”

28. In addition to consistency across asset classes, a number of respondents highlighted the need for consistency between cleared and non-cleared derivative markets, again either as a rationale for their “Yes” response or as an important issue for relevant authorities to consider. For example, one European infrastructure provider stated “supplemented ISDA definitions which

contain fallbacks that would apply on the first to occur of a permanent cessation or a ‘non-representativeness’ pre-cessation trigger and which apply to the majority of OTC derivatives transactions that are governed by bilateral master agreements will lead to outcomes that are more compatible with the arrangements that apply to cleared swaps. Many market participants could find it difficult to maintain live contracts linked to a rate that has been ruled no longer representative by the relevant regulatory authority. In this scenario the existence of a pre-cessation trigger helps to ensure such contracts will be able to continue performing along clearly defined lines.” A European pension fund noted “[a]s the London Clearing House (LCH) has already included¹⁹ pre-cessation triggers in its clearing documentation, we believe that it is vital to ensure consistency between the cleared swap market and the bilateral swap market. This consistency should help preserve market liquidity, and standardisation should ensure fair treatment of all interest rate swap holders.”

29. One European bank/broker-dealer said it was “cognisant of LCH and other institutions undertaking similar consultations” and that “it will be advantageous if these approaches are aligned, so that overall industry can achieve a robust and reliable IBOR transition.” A North American government-sponsored entity shared a similar view, stating “[w]e believe that a statement by the relevant regulatory authority with respect to a benchmark covered by the rule amendments (referred to herein as an “IBOR”) that an IBOR is no longer representative would introduce legal and financial uncertainty to derivatives contracts that continue to reference such IBOR. [We] strongly believe[] that it is important that the fallback arrangements for cleared derivatives transactions and OTC derivatives transactions be consistent. We believe that the potential for diverging responses to pre-cessation events between cleared and OTC transactions will have significant negative consequences for the swaps market.”

30. An Asian-Pacific bank/broker dealer indicated that its response was “Yes” “only if the same fallbacks apply to centrally-cleared transactions referencing such LIBORs.” This respondent requested that “ISDA will ask the regulator to ensure that the non-representative announcement

¹⁹ While the 2020 Pre-Cessation Consultation was outstanding, LCH was already consulting on including pre-cessation triggers in its clearing documentation. The LCH consultation period ended on March 23, 2020. See <https://www.lch.com/membership/ltd-membership/ltd-member-updates/lch-limited-rule-change-committee-10-january-2020>. After the 2020 Pre-Cessation Consultation closed, LCH made an announcement regarding its intention to include pre-cessation fallbacks. See <https://www.lch.com/membership/ltd-membership/ltd-member-updates/summary-feedback-lchs-consultation-regarding-proposed>.

will not occur for a reasonable time period after the finalization of the LIBOR fallbacks framework, so that market participants will be able to sufficiently prepare for the transition (including operational set-ups) before it happens.” Similarly, a European bank/broker-dealer asked that “[i]f a ‘non-representativeness’ pre-cessation trigger for fallbacks is incorporated into the ISDA Supplement, the same must also be incorporated into the LCH Rulebook as well as the rulebooks of other clearing houses and exchanges (CME, Eurex, ICE etc).”

31. A number of respondents cited general support for ISDA to publish a Supplement to the 2006 ISDA Definition and the related Protocol, noting that it would be challenging to use non-representative benchmarks. For example, one North American bank/broker-dealer stated “[a]n un-representative LIBOR...would not be reflective of the economics of the funding market. Continuing to reference un-representative LIBOR, rather than moving to Adjusted SOFR, would result in hedge positions that don’t reflect market economics and therefore would be inadequate and inefficient for their intended purposes.” Similarly, one Asian-Pacific infrastructure provider commented that “[u]sing non-representative benchmarks would be a challenge from legal/regulatory and risk perspectives.” A North American asset manager said “[g]enerally, we would prefer to avoid exposure to a Covered IBOR after the relevant supervisor deemed that IBOR is no longer representative of bank borrowing costs in the particular jurisdiction/currency. We would prefer to transition to contracts that reference a more robust interest rate index to reflect actual economic conditions rather than continue to reference an irrelevant or weakened LIBOR that might no longer be reflective of actual interest rates.”

32. A small number of respondents highlighted the need for consistency in the definition of triggering events, in the timing of the triggering events and in the calculations of the spread adjustment. For example, one North American hedge fund emphasized “[f]rom the perspectives of liquidity, effective risk management and the proper execution of certain trading strategies, there is a need to promote consistency of outcome across cleared and uncleared products in this regard. We encourage coordination between ISDA and other stakeholders, such as the clearing houses, to promote consistency in the manner in which pre-cessation triggers are defined.” A North American government-sponsored entity reiterated “[i]nconsistent triggering events between the Bank’s derivatives and cash products will almost certainly introduce risks that would make it extremely difficult to measure or manage.” One European bank/broker-dealer stated “[a]djustment calculations, irrespective of whether such calculations are applied to an OTC derivative pursuant to the ISDA Supplement or a cleared derivative pursuant to the LCH Rulebook or such other

exchange or clearing house rulebook as may be relevant, should be perfectly aligned by using identical ‘non-representativeness’ announcement dates. If adjustment calculations do not use identical ‘non-representativeness’ announcement dates, this will lead to artificially created price differences between OTC derivatives and LCH cleared derivatives.” A European infrastructure provider added “[c]lear and unique trigger definitions as well as spread calculated only once will contribute to consistency and simplification in the fallback methodology and hence strengthen its robustness.”

33. A number of other remarks were cited by respondents in support of their “Yes” answer. For example, one North American asset manager noted that the industry was already experiencing a shift to include a pre-cessation fallback trigger in contracts referencing LIBOR. One European asset manager indicated that templates for bilateral transactions from ISDA would be beneficial. An Asian-Pacific bank/broker-dealer said “[w]e are hopeful that the introduction of pre-cessation triggers by ISDA and the widest possible acceptance of ISDA standards, facilitated by a well-understood protocol might serve to cement acceptance and adoption of an equivalent pre-cessation trigger in adjacent segments.” One European asset manager noted it “support[ed] the consultation as a means to ensure market participants should continue to be able to rely on the appropriate functioning of derivatives markets to ensure all their investment objectives are met without being negatively impacted by non-representative rates.”

b) Additional Considerations Raised by “Yes” Responses

34. As discussed above, a number of respondents who answered “Yes” to the Consultation question reiterated the need for ISDA and other relevant authorities to ensure consistencies across asset classes, as well as between cleared and non-cleared derivative markets, with five respondents emphasizing that consistency was a condition for their “Yes” response. Respondents who answered “Yes” also raised a number of other issues, as summarized below.

35. Several respondents expressed concerns around the clarity of the announcement of the pre-cessation event. For example, a European infrastructure provider reiterated “[i]n order to avoid uncertainty, the provision on a pre-cessation event should be drafted in a way that does not give rise to any doubts whether a certain action or statement of a regulatory authority has triggered the pre-cessation event. The provision as proposed by ISDA in its webcast on pre-consultation (cf. slide 12) meets this requirement, if and to the extent the text in square brackets (“[and (b) the intention of that statement or publication is to constitute a trigger for fallbacks in derivative contracts]”) will

actually be upheld.” A European bank/broker-dealer said it would like to seek clarity on “the exact criteria and definition of LIBOR being deemed non-representativeness” and “the timing, process of and transparency around any such non-representativeness assessment, findings and announcement.” Three respondents specifically indicated that their “Yes” response is subject to the pre-cessation trigger being clearly drafted. For example, a European bank/broker-dealer emphasized that its answer was “Yes” only if “the announce [sic] of non-representativeness by the UK FCA and/or ICE Benchmark Administration is clear and irrevocable.” A North American hedge fund said its response was “subject to review of the text of the proposed trigger event.” Similarly, a North American pension fund said that its “Yes” answer was subject to the condition that “[t]he pre-cessation trigger must be drafted in a specific and clear manner so that market participants are clearly able to determine under what circumstances the pre-cessation trigger would apply. The protocol must also be drafted in a manner that is clear and concise...”

36. A few respondents commented that there would be certain instances where ISDA’s Protocol would not apply. For example, a European asset manager noted “whilst we have selected ‘Yes’, we acknowledge that we have certain clients where we will have no choice other than to negotiate bilaterally unless it is possible to insert pre-cessation triggers in legacy loan contracts as derivatives hedges linked to these will need to be excluded. If not, our clients run the risk of having significant mismatches between the derivatives cashflows and the positions they are hedging. Our answer to this question would have been ‘No’ had the protocol been mandatory for all contracts.” Similarly, two European bank/broker-dealers noted while they answered “Yes”, they “would definitely prefer a Protocol allowing to exclude some specific deals (specifically hedges facing cash products) and not all the deals.” A European asset manager added “[w]hilst [we] maintain the base case course of action, to voluntarily transition away from discontinuing IBOR contracts we recognise that there will be instances where such IBOR contracts will continue and therefore support the proposal to implement consistent fallbacks for the Cessation and Pre Cessation of certain IBORs.”

37. Conversely, some respondents expressed preference to not have optionality in the Protocol. A European bank/broker-dealer indicated that “a bilateral template to incorporate the pre-cessation trigger, as an alternative to a revised Supplement and Protocol, is not our preference, as it would incur significant implementation challenges, likely resulting in fragmented take-up and market uncertainty and disruption.” A North American bank/broker-dealer shared a similar view, stating it was “not supportive of introducing optionality in the protocol should the criteria set out

by ISDA not be satisfied. [We] strongly believe[] there is a need for market consistency, including consistency with cleared derivatives. Protocols are a useful industry tool to allow for a large number of amendments between varying counterparties to be executed in an operationally efficient way. These two advantages, market consistency and operational efficiency, are directly at odds with any modulation of the protocol. If the criteria set out by ISDA are not met, [our] position is that there should not be a ‘Rate Option 2’ in the protocol in order to avoid the operational challenge of having to track two separate types of adherences. For the avoidance of doubt, development of templates for modifications for legacy transactions outside of the protocol is acceptable as well as providing for optionality in the Supplement to the 2006 ISDA Definitions for transactions on a going-forward basis. In the case of such bilateral templates (including any version that incorporates a ‘Rate Option 2’), [we] would appreciate affirmative confirmation that such templates would be deemed substantially similar to the IBOR Fallbacks Protocol for purposes of the related IRS tax safe harbor.”

38. Similarly, a European infrastructure provider said “[t]o the extent possible, the inclusion of the provisions on the pre-cessation trigger should not be optional for the parties in order to avoid differing contract terms that ultimately may lead to issues with hedging, hinder proper hedge accounting and result in discrepancies between the bilateral world and the CCP world.” A European asset manager commented “[w]e believe market consistency is vital. This means consistency with cleared and non-cleared markets, as well as ensuring no optionality for firms to implement pre-cessation trigger across non-cleared markets.” A European asset manager noted the need to “[e]nsure that the protocol applies to all contracts referring LIBOR ...”

39. A few respondents raised some other specific questions/issues. A European bank/broker-dealer asked that “the ‘non-representativeness’ pre-cessation trigger shall be triggered only if... the competent authorities have not requested ICE (or the successor administrator of the LIBOR) the adoption of remedy measures to revert the situation or having requested them such measures have failed.” A European bank/broker-dealer emphasized that “[a]djustment calculations, irrespective of whether such calculations are applied to an OTC derivative pursuant to the ISDA Supplement or a cleared derivative pursuant to the LCH Rulebook or such other exchange or clearing house rulebook as may be relevant, should be perfectly aligned by using identical ‘non-representativeness’ announcement dates. If adjustment calculations do not use identical ‘non-representativeness’ announcement dates, this will lead to artificially created price differences between OTC derivatives and LCH cleared derivatives.”

40. A North American bank/broker-dealer and a North American asset suggested that “In the event that the requisite criteria for the consultation are not met and market participants would need to bilaterally agree to a LIBOR pre-cessation trigger, we would encourage ISDA to recommend a single spread adjustment based on the earlier to occur (pre-cessation or cessation) and for that single spread adjustment to become effective on either (i) the effective date for the related event if both pre-cessation and cessation triggers apply to the contract or (ii) the cessation effective date if that is the only trigger incorporated into the contract. Likewise, if the requisite criteria for the consultation are met and ISDA provides market participants with a bilateral template to opt-out of the pre-cessation trigger, we would recommend the above approach with respect to a single spread adjustment apply as well.”

41. One respondent, a European bank/broker-dealer, in particular raised several concerns: “We are concerned about potential market uncertainty and volatility during the period between the regulator's announcement of LIBOR non-representativeness and the permanent cessation of LIBOR. We would suggest that the official sector and the industry should consider taking measures to shorten such period to the greatest extent possible to ensure a smoother transition. We are concerned about potential divergence of timing around when the IBOR fallbacks would come into play across CCPs, exchanges and other market participants following the regulator's announcement of LIBOR non-representativeness, creating mis-matches across derivative portfolios, operational chaos and market confusions. We would request the relevant official sector and regulator specifying in their public announcement a 'pre-cessation effective date' (i.e., the date when the ISDA IBOR Fallbacks would come into play) across the board.” This respondent also reiterated several concerns it raised as part of the 2019 Pre-cessation Consultation, amongst which were “insufficient market take-up of the ISDA IBOR fallbacks and protocol as we are concerned that certain counterparties may not sign up to the ISDA IBOR fallbacks depending on their economic outcomes (for example if they have historical cash hedging positions with a different set of triggers and fallbacks)”; “an overly complicated ISDA Definition Supplement and IBOR protocol with election mechanisms may significantly increase complexity of implementation and affect take-up of protocol, particularly in the event if this consultation criteria were not met.”; and “uncertainty around whether the transition would trigger requirements from mandatory clearing/margining, tax, accounting or capital rules; formal confirmations and guidance/safe harbours are required from regulators globally and national competent authorities.”

2. Review of “No” Responses

42. There are 12 market participant respondents (out of 138) that answered “No” to the Consultation question. Of the 12 respondents, seven indicated that the inclusion of the pre-cessation fallback provisions would have harmful consequences to themselves and/or other market participants. The most common concern raised by these respondents is consistency across asset classes and markets. This concern also was raised by several respondents who answered “Yes,” reflecting that consistency is an important consideration among all market participants who responded to the 2020 Pre-Cessation Consultation. Similar to the “Yes” responses, the “No” responses emphasized the need for consistency in the inclusion of a pre-cessation trigger across markets and products, as well as in the definition of triggering events, in the timing of the triggers, and in the calculation of the spread adjustment. One concern raised by the “No” respondents but not the “Yes” respondents is the level of market adoption to the ISDA Protocol. These respondents indicated that the inclusion of a non-representative pre-cessation fallback trigger would potentially deter market participants from adhering to the Protocol.

43. Many respondents cited hedging risk due to potential inconsistencies across asset classes/markets as their rationale for a “No” answer. A European bank/broker-dealer stated, “we treat loan/bond linked derivatives separate from the rest of the derivatives in our portfolio. This serves the purpose of an alignment between cash, loan, bond and derivatives products in order to avoid a mismatch risk. Adding precessation triggers for the derivatives, whereas the same would be challenging for cash/loan/bond markets and we see no appreciable effort or work (so far) of the other leading associations in these markets for incorporating precessation triggers into their recommended fallbacks, would jeopardise the consistency across all asset classes.” Similarly, another European bank/broker-dealer noted, “LIBOR is used in many other products than derivatives. If pre cessation is triggered in derivatives but not for other asset classes, it would create an unnecessary basis and hedge accounting risk for our firm and our clients. As we are not aware of any similar initiatives in respect to the other asset classes there is a potential fragmentation risk amongst products in the event where the ‘nonrepresentativeness’ trigger would be triggered for the derivatives but not for loans or bonds.” A different European bank/broker-dealer said that it “would be unavoidably harmed by a Supplement and Protocol that implement pre-cessation fallbacks in the manner described above, because counterparties which do not have a pre-cessation trigger in their cash products and face the risk of disconnection of the related hedge will be discouraged from adhering to a protocol which includes both triggers and applies whichever occurs first (no optionality). This may concern a great number of counterparts, with a high risk of dispute

and operational burden arising from multiple bilateral negotiations.” A North American end user emphasized that it “mitigates the financial risk associated with consumer-facing loans through a strategy that includes the use of fair value and cashflow derivative hedges that minimize the economic impact of changes in interest rates and foreign exchange rates. Each swap was entered into as a deliberate hedge for specific assets or liabilities (‘Exposures’), as opposed to a speculative position. These Exposures do not include pre-cessation triggers relating to a transition away from LIBOR. If ISDA’s protocol for legacy swaps includes pre-cessation triggers, and a legacy hedged swap portfolio adheres to that protocol, then the hedge swap portfolio would transition to a new benchmark before the Exposure (and while LIBOR continues to exist). The resulting basis risk would be highly problematic. Additionally, the majority of these positions conform to FAS 133 hedge accounting rules; as a result, changes in the value of an asset are offset by changes in the value of a derivative. If one instrument were to transition before the other, the result would cause mark-to-market volatility that is not representative of our economic performance.”

44. A North American bank/broker-dealer acknowledged what was discussed by some of the “Yes” responses, stating that it understood that “other asset classes are moving in the direction of adopting a ‘non-representativeness’ pre-cessation fallback trigger (most notably cleared derivatives at central counterparties subject to the EU Benchmark Regulation such as LCH) and alignment across asset classes is desirable.” This respondent, however, selected “No” and emphasized the need for timing consistency: “it is more preferable for there to be consistency within an asset class. OTC derivatives which reference one IBOR rate should transition away from that rate at the same time (i.e., at the time of a permanent cessation).” This respondent added that “where OTC derivatives are used to hedge LIBOR linked cash products that do not have a pre-cessation fallback trigger related to non-representativeness, those counterparties will refuse to include such a trigger in respect of their derivative trades to ensure alignment between the cash product and the hedge. These types of counterparties are unlikely to adhere to the ISDA Protocol. All LIBOR referencing derivatives documentation with each of those counterparties would have to be renegotiated bilaterally instead to incorporate new fallback provisions. This would vastly increase complexity and execution risk for the transition of the OTC derivatives market, as well as drain additional resources and time in order to complete this task.”

45. A few respondents indicated that they would not be able to adhere to a Protocol that included a pre-cessation trigger. A North American end user stated, “[i]t would not be possible for us to adhere to a Protocol that included a pre-cessation trigger in the Protocol in the manner

described above. We strongly prefer to adhere to a Protocol in order to adopt a permanent cessation fallback provision in our existing swaps but would be unable to do so if the Protocol included a pre-cessation trigger.” A European bank/broker-dealer also noted that it “would be unavoidably harmed by, and/or unable to use, a Supplement and Protocol that implement pre-cessation fallback provisions in the manner described in the question as this provision would introduce a mismatch of fallback trigger date as well as the spread adjustment between cash products and their hedging that would incur a basis risk and impact financial stability.” This respondent also added that “[t]his provision could also negatively affect the adherence to the ISDA protocol.” A European bank/broker-dealer said that “[i]f precessation trigger is hardwired into the Protocol, we would also face an issue of the loss of flexibility in how to address LIBOR cessation across the entirety of our contracts. This would put us in an undesirable position to reconsider our willingness to adhere to the Protocol.” A North American bank/broker-dealer, while indicating that it “would be able to use a Supplement and Protocol that implements pre-cessation fallback provisions,” said it “view[ed] such a method of implementation as likely to cause unnecessary and quite frankly harmful repercussions for market participants.”

46. Five respondents cited anecdotal evidence that other market participants would not adhere to a Protocol that includes a pre-cessation trigger. A European bank/broker-dealer stated “incorporating pre-cessation triggers on the basis set out will add further uncertainty and impede the ability of market makers to price the transition into LIBOR – RFR basis. While the impact on GBP LIBOR – SONIA in terms of basis pricing may be limited (the market has priced in the transition as evidenced by a general flattening of the LIBOR – SONIA basis over the last two years), the same is not true for other currencies. This will have also have a knock on impact on buy side / client adoption of the protocol. The follow on impact of adding a pre-cessation trigger on the loan and Floating Rate Note market should also be considered.” A European bank/broker-dealer shared a similar view, noting that “[a pre-cessation fallback] provision could also negatively affect the adherence to the ISDA protocol.” This respondent raised the concern regarding consistency in timing and spread adjustment calculation, stating “[a pre-cessation fallback] provision would introduce a mismatch of fallback trigger date as well as the spread adjustment between cash products and their hedging...” A North American bank/broker-dealer added, “We believe the inclusion of pre-cessation fallback provisions in the ISDA Supplement and Protocol would have a negative impact on the adoption rate of the ISDA Protocol, particularly from buy-side market participants. As pre-cessation is somewhat of a tail event in our view, and as such, we do not believe

we should risk the widest possible adoption of the ISDA Protocol to ensure orderly transition to RFRs upon permanent cessation of LIBORs for this tail risk.”²⁰

47. Similarly, a North American bank/broker-dealer emphasized that “[i]t is important that the market broadly adopts the proposed Supplement to the 2006 ISDA Definitions to add new fallbacks to certain IBOR Rate Options and the related Protocol. ISDA should not include the ‘non-representativeness’ pre-cessation fallback trigger as standard language as it will potentially deter thousands of market participants from adhering to the related ISDA Protocol and thereby potentially hindering the broader market transition away from the IBORs to the RFRs. Based on anecdotal evidence, we understand that buy-side asset managers and smaller counterparties are opposed to the inclusion of a ‘non-representativeness’ pre-cessation fallback trigger. Several asset managers cannot accept this type of trigger for their derivative trades as it could violate their fiduciary duty to their clients. Further, where OTC derivatives are used to hedge LIBOR linked cash products that do not have a pre-cessation fallback trigger related to non-representativeness, those counterparties will refuse to include such a trigger in respect of their derivative trades to ensure alignment between the cash product and the hedge. These types of counterparties are unlikely to adhere to the ISDA Protocol.”²¹

²⁰ This respondent further explained “The reason why we believe the buy-side market participants will not want to adhere to an ISDA Protocol containing a pre-cessation trigger is that the methodology being proposed to calculate the credit spread ... is a sample taken at generally tighter levels. If, after a determination is made that LIBOR rates are non-representative, LIBOR continues to be published and that spread is greater than the ISDA fallback credit spread, our clients (asset managers) would have the fiduciary responsibility to their clients to continue to use the non-representative LIBOR as it produces the greater return. This scenario would most likely become systemic as LCH (and potentially CME) cleared swaps would move to RFRs while bilateral swaps with counterparties not having adhered to the ISDA Protocol and cash instruments generally would continue to reference LIBOR. This would be harmful to the industry by introducing basis to previously hedged transactions, introducing the need to possibly re-negotiate millions of contracts (industry wide) and forcing swap desks to possibly run their business out of many portfolios as the need to group like risks together would dictate.” This respondent said it would “prefer a ‘hard date’ being set in advance for the LIBOR discontinuation and consequent transition to RFR to any other option that involves uncertainty, but that’s not exactly the object of this consultation.

²¹ This respondent further added that “[e]ven if ISDA does not include a ‘non-representativeness’ pre-cessation fallback trigger as a standard term in the new Supplement to the 2006 ISDA Definitions, the proposal does provide counterparties the optionality to include it if they choose. If counterparties want a pre-cessation fallback trigger to apply to all or a subset of their trades, they can bilaterally agree to incorporate them. This may be appropriate in the institutional and interdealer markets, where OTC derivatives are hedged through cleared derivatives which will likely include pre-cessation fallback provisions related to non-representativeness. As the institutional and interdealer markets are smaller in

48. A North American bank/broker-dealer noted that it would be “in favour of ISDA including an ‘Annex’ to the Protocol to allow market participants to ‘opt-in’ to the pre-cessation fallback provisions with counterparties who also opt-in to those fallback provisions as part of their adherence to the Protocol implementing the permanent cessation fallbacks.” This respondent said that a key reason for its suggestion was that it would “allow the largest number of market participants to adhere to the Protocol. In determining our response, we consulted with a wide spectrum of market participants. The feedback we received was that some were against a protocol with a pre-cessation trigger and would consider it a material issue in determining whether they would adhere. In order to avoid a result where certain segments of the market do not adhere, thereby necessitating that we engage in bi-lateral negotiations to amend our agreements with these parties, we prefer that the pre-cessation triggers remain optional.” This respondent further added “an optional pre-cessation trigger...would be critical in promoting to the greatest extent possible, alignment with respect to the benchmark rate referenced between and amongst products.”

49. There are a number of other remarks added by respondents that answered “No” to the Consultation. A North American government-sponsored entity said it “would be harmed by discontinuing LIBOR, even if it could be slightly flawed. The cost...of moving away from LIBOR far exceeds the benefit of switching...” A European bank/broker-dealer highlighted the lack of information on “a) the exact criteria that would be applied to assess if LIBOR has become ‘non-representative’ and b) the precise duration of the ‘reasonable period’ during which a ‘non-representative’ LIBOR would be published.” A European bank/broker-dealer answered “No” since it viewed that “there are better means for ensuring that both the cash and derivatives market will not be confronted with various (pre-)cessation dates embedded in contracts in the event the benchmark is no longer representative or will no longer be published.” This respondent stated that “the market should not continue referencing a benchmark in contracts if that benchmark was no longer representative. Therefore, in line with IOSCO principles for financial benchmarks and the EU Benchmarks Regulation (BMR), it is the task of the administrator -as the owner- of such benchmark to have a protocol in place that describes appropriate actions to either (1) timely strengthen the benchmark to ensure its representativeness or (2) inform its supervisor of a material change or permanent cessation if the benchmark is no longer representative. It is then up to the

terms of the number of firms, negotiating the inclusion of a pre-cessation trigger within these markets is manageable (especially when compared to the vast population of counterparties that will likely decline to adopt the ISDA Protocol if the 2006 ISDA Definitions are amended to include this pre-cessation fallback trigger as a standard term).”

supervisor of such benchmark to approve this, in line with BMR article 35. Taking into account the requirements that are already set in the IOSCO principles and BMR for an orderly cessation of a benchmark, [we are] of the opinion that -as soon as the situation arises that a benchmark may no longer representative- the administrator and supervisor of such benchmark should work together in determining one single date for a permanent cessation of the benchmark that will trigger fallback measures in the wide variety of contracts simultaneously.” This respondent also emphasized the need for consistency in the fallback language and reiterated that “[t]o ensure an orderly transition where institutions can continue these hedge relationships (1) as were designed to and (2) to avoid market fragmentation between products, it is crucial that fallback trigger dates and fallback language are aligned between products. So that in the event a benchmark will no longer be representative, a joint announcement of the benchmark’s administrator and supervisor will set one single date for a permanent cessation of the benchmark that will trigger fallback measures in the wide variety of contracts simultaneously. Therefore, [we] encourage[] ISDA, other market associations and the various working groups on risk-free rates to strive for generic fallback clauses that will include these measures.”

C. COMMENTARY FROM NON-MARKET PARTICIPANT RESPONSES

Table 8
Summary Statistics of Responses to the 2020 Pre-Cessation Consultation
for Non-Market Participants

Response	Total	% of Total
Yes	3	75%
No	1	25%
Total	4	100%

50. There are four professional services firms/trade associations that responded to the 2020 Pre-cessation Consultation. Three of these entities answered “Yes” to the Consultation question and one entity answered “No.” Only two entities provided additional explanations to their answers. Specifically, a North American professional services firm noted “[w]hile we understand it is impossible for the Protocol to fit every market participant’s needs, [our firm] believes that including pre-cessation fallback triggers will accommodate the needs of many market participants, which will allow for broader market adoption. That said, [our firm] supports ISDA’s efforts to publish templates for standard modifications to allow for market participants to bilaterally negotiate terms outside of the standard ISDA Definitions and related Protocol. Entities transacting

with multiple counterparties will likely prefer the convenience and efficiency of a protocol, but [our firm] expects many end users may instead prefer template language for bilateral incorporation. This may be operationally easier and potentially less costly for end users facing only one or a few counterparties, and will also give end users the most flexibility to customize language to fit their particular needs.”

51. In contrast, a European professional services firm emphasized that “[i]n the current master agreements, the only event that leads to a fallback is the non-publication of the rate, there is no notion of announcement date and even less pre-cessation trigger. A pre-cessation trigger forces extra complexity and increases the fragmentation of the market. Legacy trades only have non-publication as a trigger, adding a pre-cessation trigger create a discrepancy between the trades under the new definitions and the legacy trades. The discrepancy would make it more complex to hedge the legacy book. A new fragmentation of the market will be created.” This entity noted, “To achieve the required exposure on new trades, the fallback has to be trigger as late as possible. Any pre-cessation trigger is a negation of the trade existence itself. The LIBOR fixing, even if not perfect or deemed not representative by a third party – e.g., a regulator – is better than a fixing based on a RFR plus a spread which is not credit and liquidity dependent. Fallback should be a last resort mechanism and used only in last resort. The pre-cessation event is not an event requiring last resort. The estimation by a single entity, even a regulator, without review and recourse mechanism in place, regarding a major interest rate standard that has been working for more than 30 years and is still working, should not be consider as a case of last resort.”

V. Comparing the 2020 Pre-Cessation Consultation to the 2019 Pre-Cessation Consultation

52. The number of market participant respondents who participated in the 2020 Pre-Cessation Consultation (138) was significantly larger than the number of market participant respondents who participated in the 2019 Pre-Cessation Consultation (88).²² As discussed in Section I of the

²² This number of market participant respondents does not include any professional services firms or trade associations that responded to both the 2019 Pre-Cessation Consultation and the 2020 Pre-Cessation Consultation for purposes of comparing the relevant responses. One market participant respondent answered on behalf of themselves and three additional respondents to the 2019 Pre-Cessation Consultation, but responded only on behalf of themselves to the 2020 Pre-Cessation Consultation. One of the three respondents provided a response to the 2020 Pre-Cessation Consultation and the other two did not.

report, the 2020 Pre-Cessation Consultation primarily comprised of a single binary (i.e., “Yes” or “No”) question.²³ In addition, the 2020 Pre-Cessation Consultation was shorter than the 2019 Pre-Cessation Consultation and was preceded by the release of additional market information from the FSB OSSG, the UK FCA, IBA and LCH, as well as statements from several other CCPs, and included clearly defined criteria by ISDA.

53. Approximately 73% of market participant respondents that responded to the 2019 Pre-Cessation Consultation also responded to the 2020 Pre-Cessation Consultation (i.e., 64 respondents responded to both Pre-Cessation Consultations).²⁴ There were 24 market participant respondents who responded to the 2019 Pre-Cessation Consultation but not to the 2020 Pre-Cessation Consultation, as shown in Figure 3.

54. Figure 3 shows how the 64 market participant respondents who participated in both Pre-Cessation Consultations responded in each of the two consultations. With regard to the 2019 Pre-Cessation Consultation, nine answered “Yes” to Question No. 5, another 35 also answered “Yes” but conditioned their response on optionality and/or flexibility, 17 answered “No” and three were considered as “Maybe”.²⁵ However, across all these categories of answers to Question No. 5 of the 2019 Pre-Cessation Consultation (including those who answered “No” or “Maybe,”) the majority of respondents supported the inclusion of a pre-cessation trigger in 2020. In particular, of the 64 respondents who responded to both Pre-Cessation Consultations, 56 supported the inclusion of a pre-cessation trigger and eight did not in 2020.

55. Of the eight market participants that did not support the inclusion of a pre-cessation trigger in response to the 2020 Pre-cessation Consultation, most cited similar considerations in response to both Pre-Cessation Consultations; including mainly consistency across asset classes, uptake, and

²³ While the primary question to the 2020 Pre-Cessation Consultation was binary with a “Yes” or “No” answer, a number of market participant respondents also included a narrative discussion. The answer to the binary question in the 2020 Pre-Cessation Consultation is used to compare the responses of market participants who participated in both the 2019 and the 2020 Pre-Cessation Consultations.

²⁴ One market participant respondent answered on behalf of themselves and three additional respondents to Question No. 5 of the 2019 Pre-Cessation Consultation, but responded only on behalf of themselves to the 2020 Pre-Cessation Consultation. This respondent’s answers are accounted as being on behalf of themselves for purposes of comparing the relevant responses between consultations.

²⁵ In comparing the responses in Figure No. 3, a “Yes but wanted optionality/flexibility” response to Question No. 5 of the 2019 Pre-Cessation Consultation aligns most closely with a “No” response to the 2020 Pre-Cessation Consultation given the preference in favor of optionality and flexibility.

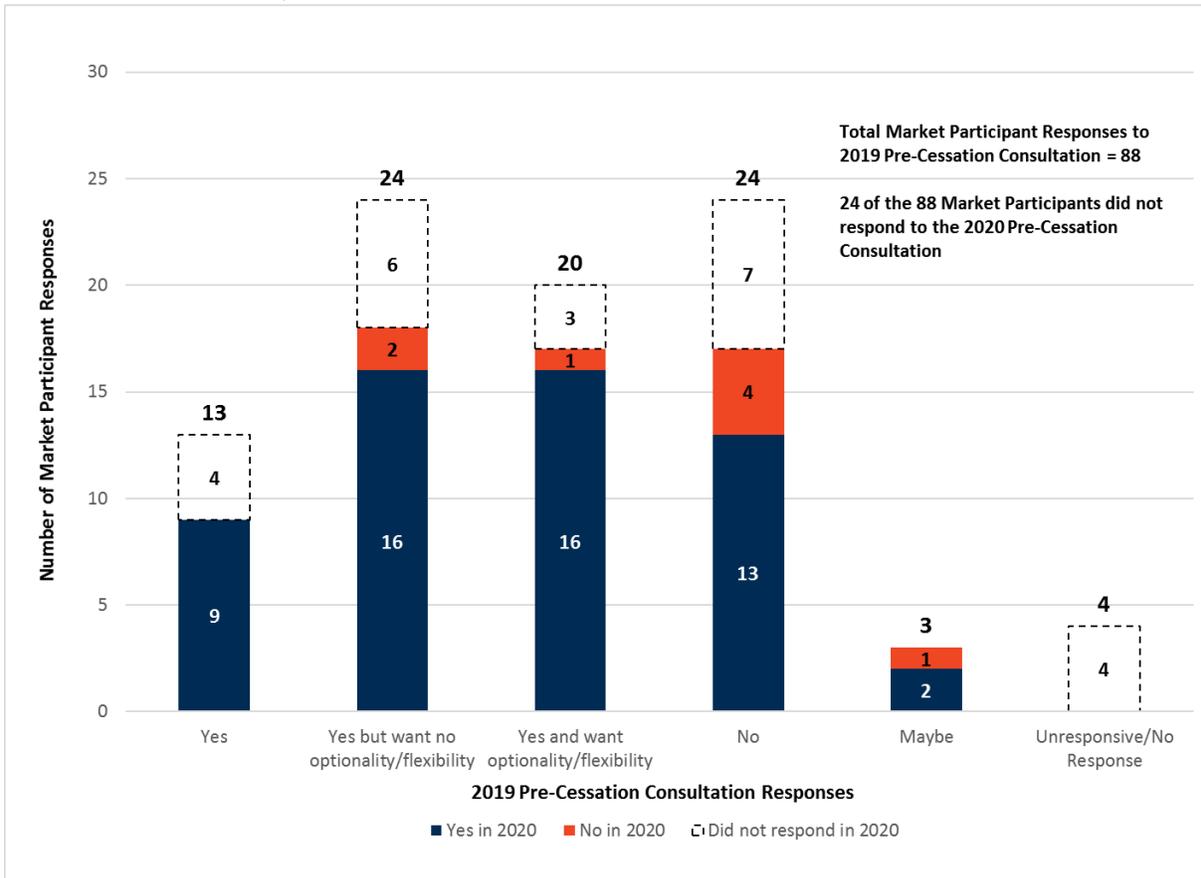
optionality/flexibility. For example, in response to the 2019 Pre-Cessation Consultation, a European Bank/Broker-dealer did not support the inclusion of a pre-cessation trigger stating that “...we are concerned that this approach lacks a properly decisive trigger and that as a result take up would be likely to be partial. We would want to see decisive amendments to the 2006 ISDA definition, as are being discussed for cessation, and a clear replication of a transition path that will be decided by the relevant IBOR supervisor, administrator and industry.” This same respondent answered “No” to the 2020 Pre-Cessation Consultation stating, “[it] would be unavoidably harmed by a Supplement and Protocol that implement pre-cessation fallbacks in the manner described above, because counterparties which do not have a pre-cessation trigger in their cash products and face the risk of disconnection of the related hedge will be discouraged from adhering to a protocol which includes both triggers and applies whichever occurs first (no optionality).”

56. Only a few market participant respondents that answered “No” to the 2020 Pre-cessation Consultation cited different considerations in response to the 2019 Pre-Cessation Consultation. For example, in response to Question No. 5 of the 2019 Pre-Cessation Consultation, a North America government sponsored entity’s answered “Yes but want no optionality or flexibility” stating that “ISDA could greatly assist in the reduction of fallback exposures through the adoption of clear market standards for LIBOR derivatives triggers and fallback(s), and the development of protocols which ensure broad market alignment in fallback upon cessation or pre-cessation trigger events.” In response to the 2020 Pre-Cessation Consultation this same respondent answered “No” to the inclusion of pre-cessation triggers stating that “[it] would be harmed by discontinuing LIBOR, even if it could be slightly flawed. The cost to the Bank, of moving away from LIBOR far exceeds the benefit of switching...”

57. Three market participant respondents answered “Maybe” to the 2019 Pre-Cessation Consultation, two of which answered “Yes” and one answered “No” to the 2020 Pre-Cessation Consultation question.²⁶

²⁶ One European Market Infrastructure-central counter-party; One Asian-pacific Bank/Broker-dealer; and One European Asset Manager.

Figure 3
Mapping of 2020 Pre-Cessation Consultation Market Participant Responses to their Responses to Question No. 5 of the 2019 Pre-Cessation Consultation



Notes: 2019 Pre-Cessation Consultation Question No. 5: “Should a pre-cessation trigger be included in the ISDA 2006 Definitions Amendment?”

2020 Pre-Cessation Consultation Question No. 1: “Should ISDA publish a Supplement to the 2006 ISDA Definitions so that the Rate Options for LIBOR in the relevant currencies (USD, GBP, CHF, JPY, EUR) all contain fallbacks that would apply upon the first to occur of (i) a permanent cessation trigger or (ii) a ‘non-representativeness’ pre-cessation trigger, and publish a Protocol to allow adherents to include the amended definitions (i.e., the definitions with the combined permanent cessation and pre-cessation fallback provisions) in all of their legacy contracts with other adherents?”

VI. Conclusion

58. Given the mixed feedback ISDA received from the 2019 Pre-Cessation Consultation, ISDA published the 2020 Pre-Cessation Consultation with one binary question to solicit specific feedback from market participants on their desired approach to pre-cessation fallbacks. Overall, 91% of market participant respondents to the 2020 Pre-Cessation Consultation showed support for combining pre-cessation and permanent cessation fallbacks without optionality or flexibility in the Supplement and Protocol that ISDA expects to publish (as specifically described in the 2020

Pre-Cessation Consultation). All the criteria set in advance by ISDA to assess the 2020 Pre-Cessation Consultation results were met.

59. Consistency across asset classes and between cleared and non-cleared derivative markets is a common theme cited by many respondents, including those who answered “Yes” to the Consultation question as well as those who answered “No.” Based on these results, ISDA expects to move forward on the basis that pre-cessation fallbacks based on a ‘non-representativeness’ determination and permanent cessation fallbacks would apply to all new and legacy derivatives referencing LIBOR that incorporate the amended 2006 ISDA Definitions.

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