Anonymized Narrative Summary of Responses to the ISDA Pre-Cessation Consultation

PREPARED FOR

International Swaps and Derivatives Association ("ISDA")

PREPARED BY

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This report was prepared for ISDA by The Brattle Group ("Brattle") in consultation with ISDA's outside counsel. Brattle assists clients involved in a wide range of litigation and consulting matters. Our experts present and defend principled economic and financial evidence, and identify and expose flaws in opposing opinions. 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 overview, summary, and analysis of the market participant responses to its Pre-Cessation Consultation. Brattle understands that ISDA will rely on the analysis of the Pre-Cessation Consultation market participant responses contained in this report, to assess whether and how to address a non-representative covered IBOR in derivatives documentation.

This report is an anonymized summary of the responses that incorporate comments from ISDA Staff, ISDA's outside counsel, ISDA's Board Benchmark Committee and others, including the Financial Stability Board Official Sector Steering Group. As part of its analysis, Brattle reviewed the content of all responses to the Pre-Cessation Consultation, and evaluated (based on the number and diversity of respondents) 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 additional considerations were raised.

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I. Executive Summary

1. In early 2019, statements by the UK Financial Conduct Authority (FCA) indicated that if one or more LIBOR panels shrunk so significantly in terms of the number of banks or the market share of banks remaining that it would no longer consider the relevant benchmark capable of being representative of the underlying market and economic reality, then it would make a statement to that effect.[1] Following this, the Financial Stability Board (FSB) Official Sector Steering Group (OSSG) wrote to ISDA noting that if "the [EU] Benchmark Regulation envisages some circumstances in which a critical benchmark that does not meet requirements of the Regulation (such as representativeness) continues to be published…it also envisages that EU supervised entities would no longer be able to enter into new derivative or securities transactions referencing LIBOR in those circumstances."[2] In light of this, the FSB OSSG suggested that market participants may want to include a "pre-cessation" trigger based on "non-representativeness" for fallbacks in existing contracts that use a LIBOR benchmark (sometimes referred to herein as "legacy" contracts).[3]

2. In a March 2019 letter to the International Swaps and Derivatives Association ("ISDA"), the FSB OSSG co-chairs asked that ISDA consult on determining the need for a potential pre-cessation trigger for fallbacks that would take effect if the FCA found LIBOR to be non-representative. In response to this request, ISDA issued a consultation on May 16, 2019 (the "Pre-Cessation Consultation"). The Pre-Cessation Consultation sought input from market participants on the preferred approach for addressing pre-cessation issues in derivative contracts that reference LIBOR and certain other IBOR benchmarks ("covered IBOR(s)")[4] if a regulator determines that a

[1] https://www.fca.org.uk/news/speeches/libor-transition-and-contractual-fallbacks.

[2] http://www.fsb.org/wp-content/uploads/P150319.pdf.

[3] The scope of so-called "legacy" or "existing" contracts for the purpose of a pre-cessation trigger based on non-representativeness will differ from the scope of "legacy" or "existing" contracts to be amended by ISDA's anticipated protocol for implementation of new fallbacks in contracts entered prior to the effective date of ISDA's incorporation of the new fallbacks in its standard definitions. This is because the effective date of the new fallbacks is expected to precede any determination that LIBOR is "non-representative." Contracts entered into between these two dates would be "legacy" or "existing" for purposes of the "non-representative" determination but not the protocol.

[4] This consultation does not cover TIBOR, Euroyen TIBOR, BBSW, HIBOR or CDOR. The consultation covers SOR only insofar as to consider if the SOR fallback for a USD LIBOR "index cessation event" – which is separately being consulted upon currently – should also apply in the event of a USD LIBOR pre-cessation trigger.

covered IBOR is no longer representative. Specifically, among other things, the consultation sought feedback regarding (a) the potential inclusion of a pre-cessation trigger based on such a statement in the 2006 ISDA Definitions and/or the related protocol that ISDA intends to publish, and (b) perceived challenges to the implementation of such a pre-cessation trigger.

3. A significant majority of respondents (71.9%)[5] stated that generally they would not want to continue referencing a covered IBOR in future derivative contracts following a public statement by a regulator that such IBOR was no longer representative.

4. A smaller majority of respondents (64.0%)[6] replied that generally they would not be content to continue referencing an unrepresentative covered IBOR in legacy contracts following such a statement. However, a notable portion (45.6%) of this majority explained that despite this position, they might nonetheless continue to reference an unrepresentative covered IBOR in certain circumstances. A minority of respondents (22.5%)[7] stated that they would continue to reference an unrepresentative covered IBOR in legacy derivative contracts following a statement by a regulator that such an IBOR is no longer representative. These respondents offered a variety of rationales for this choice, including that they would only take such an approach if no other viable alternative existed, others that would continue referencing an unrepresentative covered IBOR said they would do so to avoid creating a mismatch, and others suggested that only a permanent cessation trigger should be utilized for fallbacks.

5. Generally, the respondents to the Pre-Cessation Consultation broadly desired a uniform transition to fallback rates across products and currencies. However, the respondents expressed a wide variety of views regarding *whether* and *how* to implement a pre-cessation trigger for covered IBORs, related to non-representativeness for derivatives. In general, the respondents fell into four general categories with respect to *how* to implement a pre-cessation trigger, without a clear majority in any one category.

a. Those who supported adding a pre-cessation trigger to the permanent cessation triggers in the "hard wired" amendment to the 2006 ISDA Definitions but did not

[5] This figure includes responses categorized as "No" and "No with exceptions."
[6] This figure includes responses categorized as "No" and "No with exceptions."
[7] This figure includes responses categorized as "Yes" and "Yes with conditions."

specifically address a preference regarding optionality or flexibility (14.6% of respondents).

b. Those who supported adding a pre-cessation trigger to the permanent cessation triggers in the "hard wired" amendment to the 2006 ISDA Definitions and opposed the publication of a protocol with optionality or flexibility (26.97% of respondents).

c. Those who supported the use of a pre-cessation trigger and supported implementation with optionality and flexibility (22.5% of respondents).

d. Those who opposed the use of a pre-cessation trigger (28.1% of respondents).

6. The Pre-Cessation Consultation also asked market participants for feedback regarding any perceived challenges to implementing a pre-cessation trigger generally, and then more specifically about any challenges involving: (a) the possibility that market participants could calculate value transfer if the covered IBOR at issue continued to be published, and (b) the possibility of a different spread adjustment being applied as part of the fallback following a pre-cessation trigger by comparison to a permanent cessation trigger.

7. As to the potential to ascertain value transfer if the covered IBOR at issue continues to be published, some respondents indicated that this would not be an issue because the covered IBOR would no longer be representative, while others stated that there could be litigation risks and other issues associated with the continued publication. Some of these respondents suggested regulatory intervention to mitigate such risks.

8. As to the potential for different spread adjustments between a pre-cessation and permanent cessation trigger, most respondents opposed more than one spread adjustment transition per transaction. Respondents highlighted operational challenges and legal risks associated with having multiple spread adjustment transitions. Many respondents believed that if a pre-cessation trigger is implemented, the spread adjustment applied at that time should continue even upon a permanent cessation event. In contrast, respondents that opposed a pre-cessation trigger cited concerns around multiple spread adjustments as one of the reasons for their opposition.

9. The consultation responses were reviewed for the purpose of assessing what, if anything, ISDA should do to address pre-cessation triggers for fallbacks, in the event a covered IBOR is

determined to be no longer representative. In an effort to identify consensus among market participants, on this and other related issues, consultation responses were reviewed and categorized based on ISDA's staff and its advisors' overall analysis of the unique business perspectives and complexities presented in each of the respondent's answers as opposed to by strict quantitative analysis of responses to a particular question.

10. The Pre-Cessation Consultation solicited narrative, free-form responses and, as a result, the responses featured interrelated, compound and/or complex answers. Additionally, the answers to the consultation questions were often comingled across responses or included additional assumptions, conditions or caveats that were outside the scope of the question(s) being asked, increasing the complexity of the overall analysis of the responses. Although this lack of uniformity in the structure of the responses required a degree of judgment in order to categorize the responses, ISDA and its advisors do not believe that the judgement involved affected the overall conclusions set out in this report.

11. The analysis of the Pre-Cessation Consultation did not yield a consensus among market participants regarding *how* to address pre-cessation issues related to representativeness. Although a majority of respondents (64.0%)[8] supported the inclusion of a pre-cessation trigger in the amended 2006 ISDA Definitions, the responses revealed significant disagreement about *how* to implement such a trigger, and outlined in more detail below.

II. Demographics of Respondents to the Pre-Cessation Consultation

12. ISDA received 89 responses to the Pre-Cessation Consultation from entities in sixteen countries across the Americas, Europe, Asia-Pacific, and Africa. Respondents included asset managers, banks, pension funds, insurance companies, government entities, financial services firms, exchanges and clearinghouses and industry and trade associations. Overall, ISDA received responses from a variety of market participants that represented a broad range of perspectives and insights.

[8] This figure includes responses categorized as "Yes," "Yes, and want optionality/flexibility" and "Yes, but want no optionality/flexibility."

13. Figure 1 below summarizes the industry affiliation of the respondents. In total, the 89 respondents included primarily asset managers (17 respondents), bank/broker-dealers (43 respondents) and entities that fell into the “Other” category (17 respondents).

Figure 1: Breakdown of Entities (Respondents) by Industry Affiliation

	ISDA category	Number of entities
	[A]	[B]
[1]	Asset Manager	17
[2]	Bank/Broker-dealer	43
[3]	Insurance Company	4
[4]	Local or Regional Government Entity	1
[5]	Pension Fund	2
[6]	Other Professional Services Firm	1
[7]	Other	21
	Total	**89**

Sources and notes:

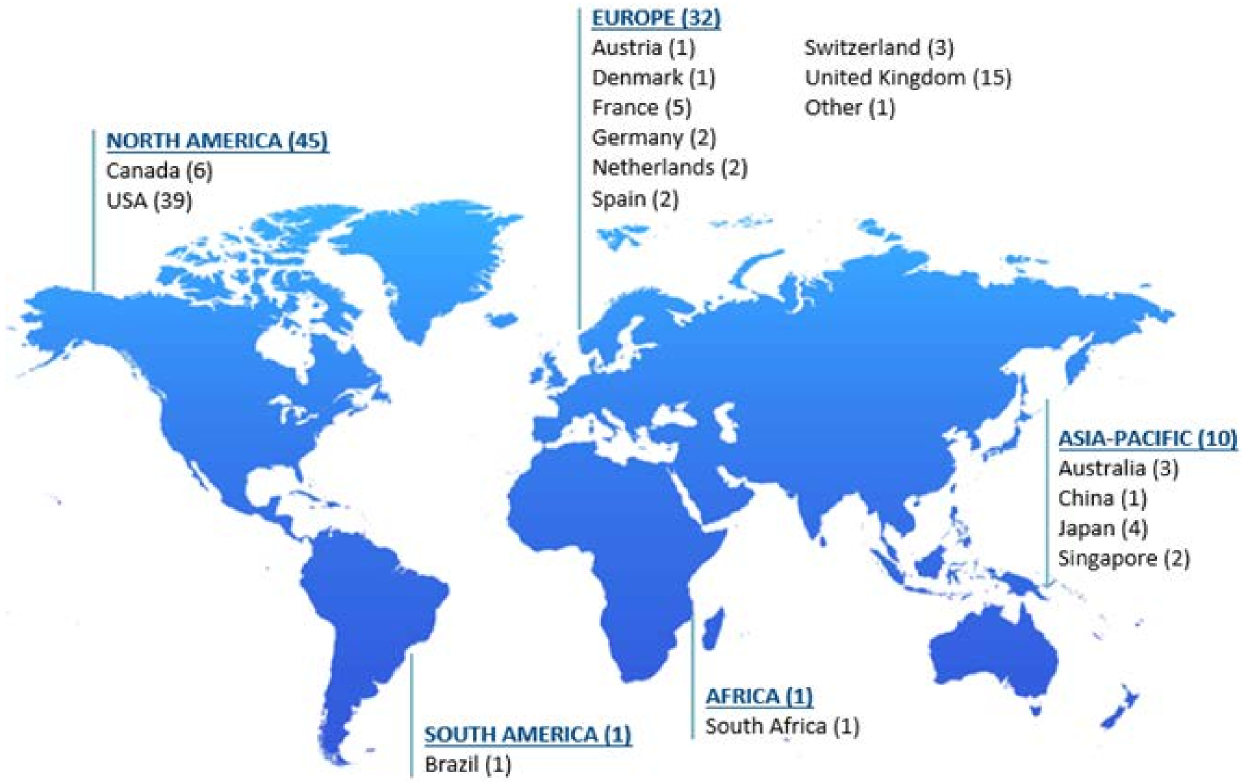
Industry affiliations represented by the entities that responded to the Pre-Cessation Consultation. Excludes individuals and associations that did not name their members.

[7]: This category includes: government-sponsored enterprises, central counterparties, reinsurance firms, exchanges, and student loan services.

[B]: When respondents are an association representing multiple members, we count the number of underlying institutions (members) named as participating in the response, in accordance with the 2018 ISDA Consultation FAQs.

14. Figure 2 Figure 3 below illustrate the respondents by country and region. The majority of respondents came from North America and Europe, and in particular the United States (36 respondents) and United Kingdom (15 respondents)

Figure 2: Breakdown of Entities (Respondents) by Geography



Sources and notes:

Regions and countries represented by the entities that responded to the Pre-Cessation Consultation. Excludes individuals and associations that did not name their members. "Other" entity in Europe does not have a country-specific jurisdiction. 89 entities total.

Figure 3: Breakdown of Entities (Respondents) by Geography

Region	Country	Number of entities
[A]	[B]	[C]
Africa		**1**
	South Africa	1
Asia-Pacific		**10**
	Australia	3
	China	1
	Japan	4
	Singapore	2
Europe		**32**
	Austria	1
	Denmark	1
	France	5
	Germany	2
	Netherlands	2
	Spain	2
	Switzerland	3
	United Kingdom	15
	Other	1
North America		**45**
	Canada	6
	United States of America	39
South America		**1**
	Brazil	1
Total		**89**

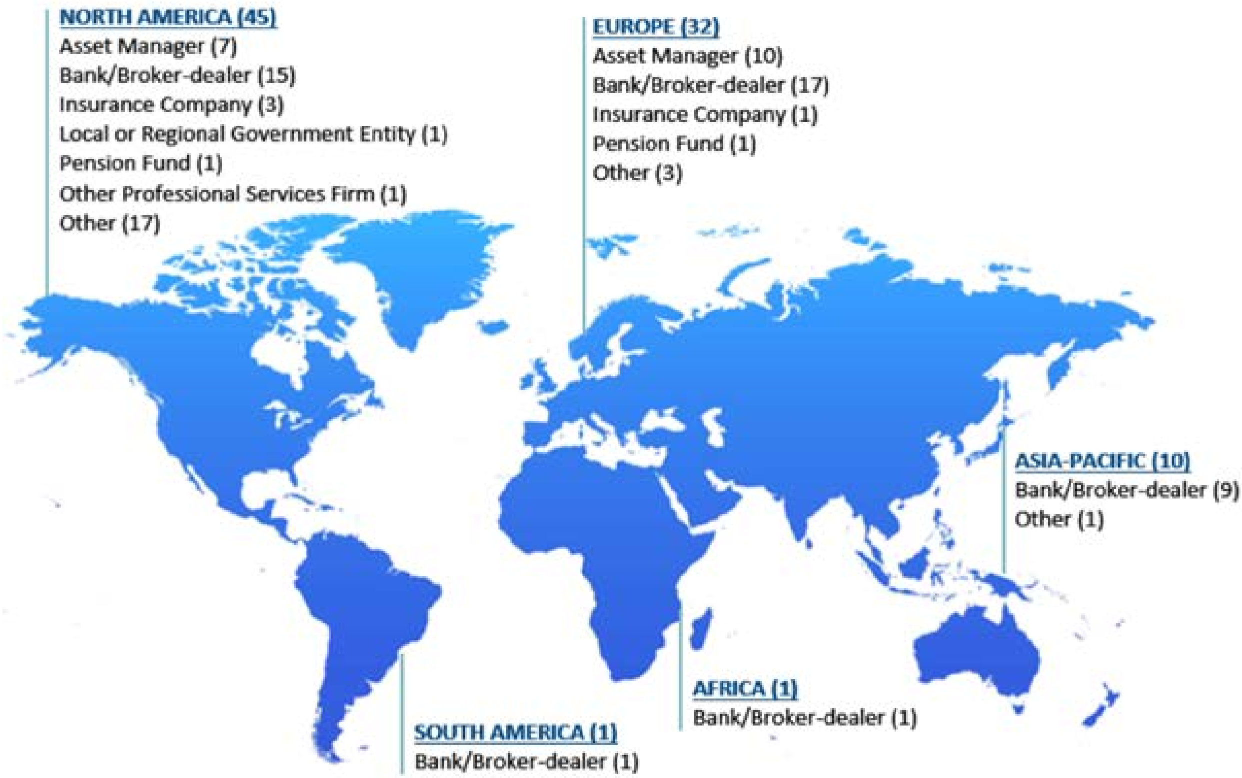
Source and notes:

Regions and countries represented by the entities that responded to the Pre-Cessation Consultation. Excludes individuals and associations that did not name their members. “Other” entity in Europe does not have a country-specific jurisdiction.

[C]: When respondents are an association representing multiple members, we count the number of underlying institutions (members) named as participating in the response, in accordance with the 2018 ISDA Consultation FAQs.

15. Figure 4 below shows the demographics of the respondents by both industry affiliation and geography. Banks/broker-dealers comprised the largest segment of respondents across geographies, though respondents in North America also consisted of a significant group of entities in the “Other” category.

Figure 4: Breakdown of Industry Affiliation of Entities (Respondents) by Geography



Sources and notes:

Regions and countries represented by the entities that responded to the Pre-Cessation Consultation. Excludes individuals and associations that did not name their members. 89 entities total.

III. Summary of Comments on Use of an Unrepresentative IBOR in New and Existing Derivative Contracts[9]

16. The Pre-Cessation Consultation asked market participants whether they would be content to have contracts that continue to reference a covered IBOR after the supervisor of that covered IBOR's administrator makes a statement that the covered IBOR is no longer representative and, if

[9] Please note that this report includes summarized responses and quotations of respondents. It therefore seeks to reflect the views of respondents rather than the views of ISDA itself. Although a degree of judgment was required in order to categorize some responses, ISDA and its advisors do not believe that the judgment involved affected the overall conclusions set out in this report. ISDA has not verified and does not endorse or otherwise confirm the accuracy of, logic behind, or supporting information for, any response made by a respondent. ISDA has also not considered whether the content of any response has already been addressed by any other publication or speech or statement by the FCA or any other person. ISDA encourages readers of this report to review the speeches and statements on the UK FCA's website (https://www.fca.org.uk/).

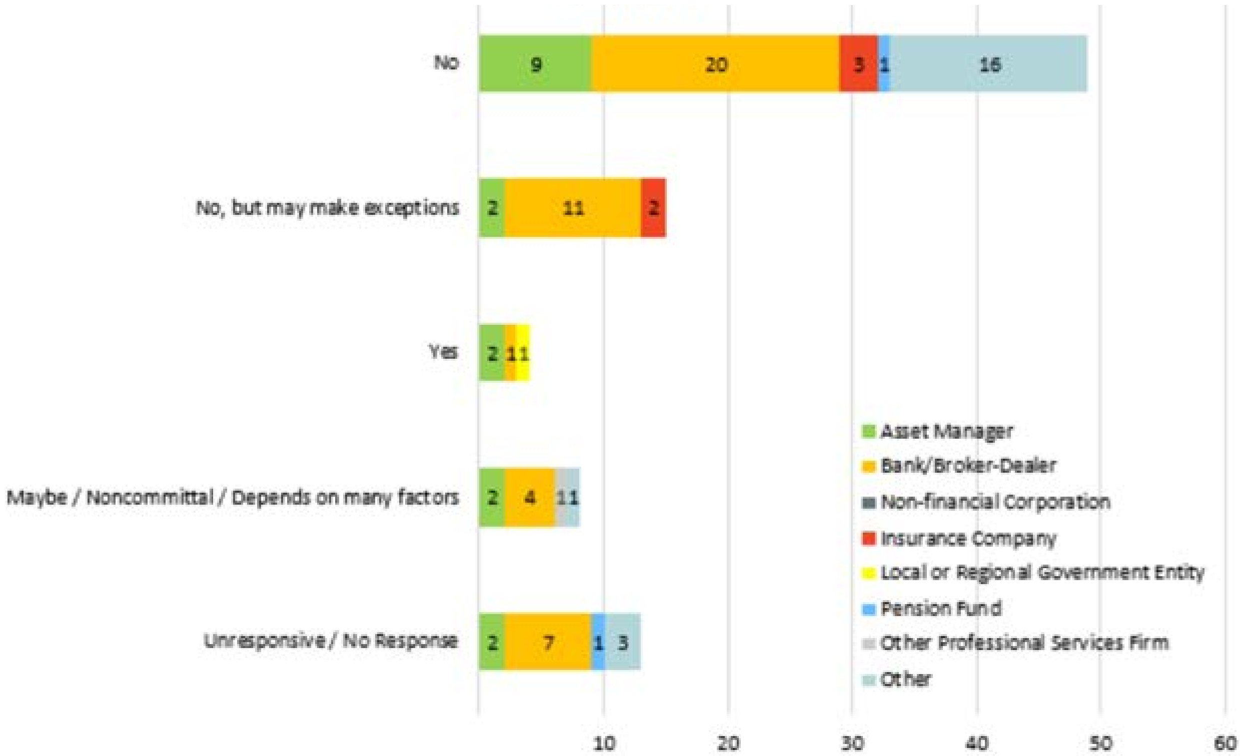
so, under what circumstances. The consultation further asked what actions a respondent would take in response to such a statement if the covered IBOR continued to be published, and to differentiate, if needed, between existing and new contracts.

17. Responses to the Pre-Cessation Consultation indicate that a majority of market participants would not be content, either outright or under certain circumstances, to continue referencing a covered IBOR in existing or future derivative contracts following a public statement from the supervisor of that covered IBOR that it was no longer representative.

18. The consultation responses suggested that market participants have serious reservations about the continued use of such an IBOR. For example, one asset manager observed that "[t]he confidence of market participants and regulators in the accuracy of the IBOR being representative of the bank funding rates will be eroded" following such a statement, and that "[t]he pricing and valuation of contracts that will continue to reference the Covered IBOR after such a statement, will be questionable and erroneous." Similarly, a bank/broker-dealer noted that such a statement would "indicat[e] a lack of regulatory confidence in the Covered IBOR" and "that the benchmark no longer accurately or reliably represents underlying markets or economic realities…"

A. New Contracts

Figure 5: Are you content to have unrepresentative LIBOR apply to future derivative contracts?



19. As shown in the above Figure 5, a significant majority of respondents (71.9%)[10] stated that they would not continue using a covered IBOR in future derivative contracts following a statement regarding its representativeness. In general, these respondents stated that they would cease using the covered IBOR and instead transition to the relevant RFR in new contracts.

20. A notable portion of respondents (16.9%) categorized as "No, but may make exceptions" envisioned that there may be circumstances in which they would want or need to continue referencing an unrepresentative covered IBOR in new contracts, even if it was not their preference. For example, some respondents indicated that their decision to move to the new rate would depend in part on whether there was sufficient liquidity therein. Some respondents believed that there could be some client demand for the continued use of the unrepresentative covered IBOR. Others expressed reluctance to transition derivatives away from a covered IBOR until there was use of specific alternative rates or broader use of fallbacks to specific rates in cash

[10] This figure includes responses categorized as "No" and "No, but may make exceptions."

products and noted that it was unclear whether such use would occur prior to a covered IBOR becoming unrepresentative.

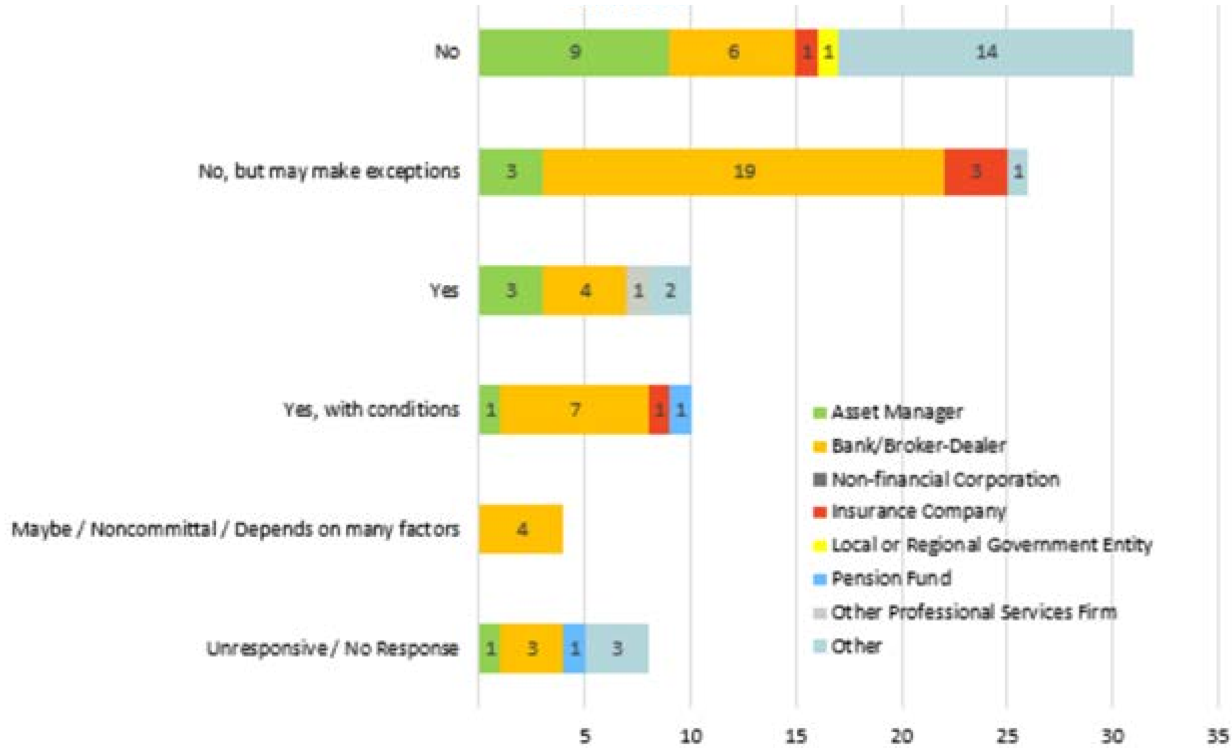
21. Similar concerns appeared to move some respondents to a "maybe" or "yes" response. For example, approximately 9% of respondents, categorized as "Maybe/Non-Committal/Depends on many factors," indicated uncertainty about whether they would continue to use an unrepresentative covered IBOR in future contracts, or stated that their decision hinged on multiple factors. More specifically, one professional services firm noted that its actions with respect to future contracts would "largely be informed by client- and trade-specific considerations." Other respondents echoed these comments, noting that their choices could depend on client wishes, as well as the context of the supervisor's announcement related to representativeness and the broader industry's reaction to the announcement.

22. A small minority of respondents (4.5%) stated that they would continue using an unrepresentative covered IBOR in future contracts. One bank/broker-dealer in this category explained that continued use of an unrepresentative covered IBOR in new contracts could be necessary to meet client needs and manage risk. An asset manager took the view that market participants should continue referencing the covered IBOR despite a statement that it was no longer representative, and that the more appropriate course of action would be for the administrator of the covered IBOR to cease production of said IBOR.

23. Thirteen respondents (14.6%) submitted replies that were deemed unresponsive or non-committal. For example, one bank/broker-dealer observed that it "seems reasonable" to stop offering future derivative contracts in such circumstances, but it could be challenging given client needs. Other responses were provided in letter format and did not directly answer the question of whether they would continue to reference a covered IBOR in future contracts following a statement by the supervisor that it was no longer representative.

B. Existing Contracts

Figure 6: Are you content to have unrepresentative LIBOR apply to existing derivative contracts?



24. As illustrated in the above Figure 6, a majority of the respondents (64.0%)[11] stated that they would not be content to continue to have existing contracts reference a covered IBOR following a statement regarding its unrepresentativeness. However, a noteworthy portion of these respondents (29.2%) stated that although they generally would not want to continue referencing an unrepresentative covered IBOR in existing contracts, they believed that it could be reasonable or necessary to continue doing so in certain circumstances.

25. Respondents offered a variety of reasons why they might continue to reference an unrepresentative covered IBOR in existing contracts despite their preference not to. Some respondents stated that in some circumstances, a cost-benefit analysis of transitioning to a RFR could weigh in favor of continuing to reference an unrepresentative covered IBOR. For example, one insurance company explained: "For some contracts, it may make sense to retain IBOR exposure in contracts where the cost-benefit trade-off suggests that the expense of amending the agreement

[11] This figure includes responses categorized as "No" and "No, but may make exceptions."

is greater than the probability weighted legal expense to mediate the situation after the LIBOR cessation." A bank-broker/dealer noted that if a contract was due to mature shortly after such an announcement, then it could make sense to leave the contract as-is.

26. Other respondents said that in some circumstances it could be too difficult to amend a contract referencing an unrepresentative covered IBOR, such as when the amendment requires third party or government approval, or when the counterparties are unable to come to an agreement. Respondents also stated that they may continue to reference an unrepresentative covered IBOR if the transition is premature - for example, if there is insufficient market liquidity in the fallback RFR, or if the relevant RFR and spread adjustment are not yet fully developed as the fallback replacement.

27. The respondents in the "maybe" category did not expressly state whether they would be willing to continue referencing an unrepresentative covered IBOR, but some of these respondents identified factors that would impact their decision. One bank/broker-dealer stated that its choice would depend on the liquidity in the unrepresentative covered IBOR at the time while another bank/broker-dealer stated that its decision "wholly depends on the availability of a suitable alternative for the benchmark referenced and the extent to which a coordinated transition to a new benchmark is possible at that point in time." Another bank-broker/dealer indicated that it would consider multiple factors, including the manner of the supervisor's statement and its underlying reasons, the materiality of its exposure to a covered IBOR, and other industry developments and reactions to the statement.

28. Approximately 22.5% of respondents said that they would be content to continue referencing an unrepresentative covered IBOR in existing derivative contracts; however, half of these respondents limited their position to when additional conditions were met. The respondents who did not condition their response (11.2%) provided a range of reasons for their answer. One bank/broker-dealer explained that it viewed the risk from mismatches with underlying products to be higher than the risk of potential claims based on the continued use of a covered IBOR that may not be representative. Two respondents agreed with the continued use of an unrepresentative covered IBOR because they believed that the more appropriate approach would be to simultaneously cease publication of the covered IBOR.

29. Some of the respondents who did caveat their responses shared concerns similar to those expressed by the respondents who preferred not to continue referencing an unrepresentative

covered IBOR but might make exceptions ("No, but may make exceptions" responses). For example, some entities categorized as "Yes, with conditions" responses indicated that they would continue to have derivatives reference an unrepresentative covered IBOR if the related underlying product also would not transition to a RFR. Similarly, some respondents categorized as "No, but may make exceptions" indicated that the need to remain aligned with cash products was a circumstance for which they might continue to reference an unrepresentative covered IBOR, despite generally disfavoring this approach.

30. Another respondent that qualified its "yes" response stated that it would be open to continue referencing an unrepresentative IBOR if it was "permitted legally to have the flexibility to manage [its] exposure to legacy positions in order to 'run off' those positions in an orderly fashion."

31. Approximately 9% of respondents either did not respond or provided answers that were deemed unresponsive because they did not directly answer the question asked.

IV. Summary of Comments on Inclusion of a Pre-Cessation Trigger

32. The Pre-Cessation Consultation asked market participants whether it would be appropriate to include a pre-cessation trigger regarding "representativeness" with the triggers for permanent cessation in the amendments to the 2006 ISDA Definitions that it intends to publish to introduce the covered IBOR fallbacks. The consultation asked that respondents explain their answer, and identify problems that could arise if such a trigger were or were not included in the amendments and protocol.

33. The consultation also asked market participants whether it would be helpful for ISDA to publish a protocol including pre-cessation triggers and related fallbacks that would allow adherents to include or exclude certain transactions and/or that would allow counterparties to agree to include or exclude a pre-cessation trigger with certain counterparties through a matching function.

34. The respondents expressed a wide variety of views regarding *whether* and *how* to implement a pre-cessation trigger related to non-representativeness for derivatives. In general, the respondents fell into four general categories with respect to *how* to implement a pre-cessation trigger, without a clear majority in any one category.

a. 14.6% of respondents generally supported adding a pre-cessation trigger to the permanent cessation triggers in a “hard wired” amendment to the 2006 ISDA Definitions but did not specifically address a preference regarding optionality or flexibility.

b. 26.97% of respondents supported the inclusion of a pre-cessation trigger in the 2006 ISDA Definitions and opposed the publication of a protocol with optionality or flexibility.

c. 22.5% of respondents supported the inclusion of a pre-cessation trigger in the 2006 ISDA Definitions and supported implementation with optionality and flexibility.

d. 28.1% of respondents opposed the inclusion of a pre-cessation trigger in the 2006 ISDA Definitions.

35. Outside of these categories, 3.4% of the respondents gave non-committal answers and 4.5% of the responses were considered unresponsive to the questions asked.

Figure 7: Should a pre-cessation trigger be included in the 2006 ISDA Definitions Amendment?

A. "Yes" Responses

36. Thirteen respondents (14.6%) supported the inclusion of a pre-cessation trigger in the amendment to the 2006 ISDA Definitions but did not specifically address a preference regarding optionality or flexibility.

37. Multiple respondents indicated that their support was based on a desire to ensure fallback uniformity across products. For example, one bank/broker-dealer supported alignment of the cash and cleared/uncleared derivatives markets, explaining that "[a] mismatch in proposed triggers across cash (cessation and pre-cessation) and derivatives (only references cessation) instruments may lead to divergent outcomes for counterparties and potentially limit hedge effectiveness." This respondent also encouraged consistency between ISDA's standard definitions and ARRC's recommended fallback language for inclusion in cash products. An exchange respondent similarly noted: "Without coordination among industry participants, across regulatory jurisdictions and across cleared and un-cleared derivative markets, there will be significant potential for market disruption."

38. Similarly, one clearing house respondent observed that inclusion of a pre-cessation trigger in the 2006 ISDA Definitions would be helpful to ensure consistency across major CCPs, who may otherwise adopt inconsistent alternative rate pursuant to their own rule books at the time of such a statement. An asset manager added that inclusion of a pre-cessation trigger "would allow for all existing derivative contracts to be converted simultaneously, and offsetting positions that are at different clearinghouses or that are bilateral would be converted concurrently using the same lookback periods, spreads, etc." A government-sponsored entity echoed these comments, writing that "as ISDA is keenly aware, alignment between derivatives clearinghouses and ISDA is an important topic for entities like us that have entered into cleared and bilateral trades. If the clearinghouses adopt pre-cessation triggers, but ISDA does not, basis risk can arise between cleared and un-cleared trades."

39. Some respondents highlighted logistical advantages of a "hard wired" approach. For example, one asset manager explained that "managing the situation through bilateral arrangements would be extremely difficult in such conditions." A bank/broker-dealer noted that such an approach would "make it easier for parties to include pre-cessation trigger language as part of the overall IBOR transition exercise." Another bank/broker-dealer added that inclusion of a definition

of representativeness would also "help the market apply such definition and transition, if necessary, should the rate be deemed no longer effective, reflective and/or usable…"

40. Some respondents supported the inclusion of a trigger based on representativeness, but added that any such trigger should be a permanent cessation to avoid the possibility of having two different fallback processes. For example, one asset manager explained: "A two stage cessation process (pre-cessation followed by permanent cessation) would add significant complexity and uncertainty to the process (for the reasons set out in the Pre-Cessation Consultation, noting in particular (i) the potential for differing adjustment spreads being triggered at each of the two stages and (ii) the enhanced challenge it would present for aligning the treatment of derivatives with other benchmark referencing product groups). This would also provide greater certainty for CCPs and promote consistency between cleared and bilateral transactions." One bank/broker dealer added: "If the market consensus were to be for a pre-cessation trigger to exist, we would also support such a trigger appearing alongside the triggers for permanent cessation, as opposed to within a separate protocol that ISDA may be contemplating. We would have significant concerns regarding the latter, as this would appear to create the possibility of a pre-cessation trigger and permanent cessation trigger occurring consecutively, which has the potential to create significant complexity and market disruption, e.g. having different credit spreads for the two triggers." This particular issue was specifically raised in the consultation questions, and is discussed further at Section VII below.

41. Finally, an exchange respondent encouraged the FCA to provide additional clarity around the function of a pre-cessation trigger: "[w]hile we understand the FCA's position that this should be considered the most likely outcome for LIBOR, and we agree that a suitable 'pre-cessation' trigger would be a useful tool to address this scenario and to promote orderly transition to the relevant fallback rate(s), it is our view that the FCA must provide greater certainty as to the operation of any such 'pre-cessation trigger' in order to build industry consensus in support of it."

B. "YES, AND WANT NO OPTIONALITY/FLEXIBILITY" RESPONSES

42. 26.97% of respondents supported adding a pre-cessation trigger to the permanent cessation triggers in the "hard wired" amendment to the 2006 ISDA Definitions, opposing publication of a protocol that provided flexibility for the inclusion or exclusion of the pre-cessation trigger and related fallback in certain transactions.

43. A leading reason that respondents preferred a "hard wired" approach was to avoid uncertainty and complexity in the market. Respondents generally noted that flexibility or optionality could undermine efforts to provide certainty to the market, leading to confusion, potential market fragmentation, and low uptake. One clearinghouse explained: "The presence of optionality increases complexity, and seems likely to lead to greater fragmentation and an absence of clarity and certainty in the marketplace. This could therefore undermine the adoption of other elements of the improved fallback arrangements that are important for the market."

44. Finally, some respondents warned that a flexible or optional approach could slow down the adoption process or could generate confusion and complexity that leads to low uptake. One bank/broker-dealer respondent referenced prior examples to support this point: "In our experience, protocols that are complex in nature or include any element of matching or optionality tend to be unsuccessful and are not widely adopted by the industry…" Another respondent similarly remarked: "As we have seen from the precedence, the more complexity and the more optionality there is in a protocol, the more complex implementation and the lower take-up of the protocol seems to be." A bank/broker-dealer respondent pointed out that, as an alternative, market participants that wanted flexibility could use bilateral amendments to achieve the same result.

C. "Yes, and want optionality/flexibility" Responses

45. 22.5% of respondents supported the inclusion of use of a pre-cessation trigger in the 2006 ISDA Definitions and supported the publication of a protocol that provided flexibility for the inclusion or exclusion of the pre-cessation trigger and related fallback in certain transactions.

46. Many respondents in this category indicated that a flexible approach would be helpful or necessary to allow market participants to ensure alignment across products, and in particular for users of derivatives to hedge cash products that may not contain the pre-cessation trigger. One government-sponsored entity explained that the inclusion of the pre-cessation trigger in derivatives used to hedge legacy cash instruments that cannot be amended to include a pre-cessation trigger "could nullify hedging relationships and cause basis risk." This respondent noted that to address this issue, the flexibility to modify only certain transactions "would be helpful from a risk management and an accounting impact standpoint."

47. In contrast to respondents who stated that flexibility would deter market uptake of the pre-cessation trigger, some respondents in this category stated that the inclusion of flexibility would lead to greater market uptake. Some respondents indicated that they would support any flexibility

or optionality that would facilitate wider adoption and thus a higher chance of a successful transition.

D. "Maybe/Non-Committal/Depends on many factors" Responses

48. 3.4% of the respondents gave answers categorized as "maybe" or non-committal. For example, a bank/broker-dealer stated that it could not make a decision about the inclusion of a pre-cessation trigger in the amendment at this time. Two other respondents indicated that they needed additional clarification around the definition of "representativeness" before a decision could be made; one respondent suggested that it was unclear what organization(s) could determine that a rate was no longer representative, and the second stated that it wanted a clear and objective methodology to determine when an IBOR was no longer representative.

E. "No" Responses

49. 28.1% of respondents opposed the inclusion a pre-cessation trigger in the amendment. Respondents offered a variety of reasons for their position, including the risk that parties could calculate value transfer if the covered IBOR continues to be published, an issue that the consultation specifically raised for consideration and is addressed in further detail at Section VI below.

50. Some respondents raised concerns with how a statement regarding representativeness would be phrased and timed, and whether such a statement could be a properly decisive trigger in order to ensure consistent movement across the market. A bank/broker-dealer respondent noted that "there is a danger for such a trigger to create more disruption as parties seek to determine exactly what statements would trip such a provision - the trigger event would need to be very clearly defined." An insurance company respondent similarly questioned what degree of "unrepresentativeness" would be necessary to make such a trigger operational.

51. Respondents in this category also highlighted the risk of including a pre-cessation trigger in the amendment creating a mismatch between derivatives and a hedged cash product. For example, one asset manager respondent stated that "[a] pre-cessation trigger could result in derivatives triggering in advance of legacy cash products which could impair the effectiveness of derivative hedges." Another asset manager replied: "Derivatives markets do not exist in isolation: for many investors, derivatives are a complement to other securities that reference LIBOR, and for those investors, it is important that LIBOR derivatives behave in a similar way to other asset classes.

Adding pre-cessation triggers would be very challenging for cash/loan/bond products, and thus if implemented for derivatives, could risk driving a further wedge between the behaviour of LIBOR in derivative and other markets."

52. Some respondents asserted that inclusion of a pre-cessation trigger in the amendment could be practically challenging, including one bank/broker-dealer that warned that a pre-cessation trigger could "create additional complexity and operational challenges to an already challenging process." One bank/broker-dealer predicted that the inclusion of such a trigger could cause confusion and bifurcation of the market between trades that continue to reference a covered IBOR and those that transition to the RFR. Another bank/broker-dealer pointed out that a complex framework could be challenging to explain to clients, and could lead to litigation risks.

53. Some respondents identified legal risks as a motivation for opposing the inclusion of a pre-cessation trigger in the amendment at all or in a way that is inextricably linked with the permanent cessation fallbacks. For example, some bank/broker-dealers flagged potential legal risks if the economic differences between the covered IBOR and fallback rate are calculable because the covered IBOR continues to be published.

54. Finally, in contrast to respondents who believed that a pre-cessation trigger in the amendment could encourage uptake of the permanent cessation trigger, some respondents who oppose a pre-cessation trigger asserted that such a trigger could deter or disrupt a transition to the permanent cessation fallbacks. One bank/broker-dealer explained its belief that "[l]imiting IBOR trigger events under derivatives contracts to actual cessation triggers will assist with an organic transition that is least likely to cause disruption to the financial markets." Another bank/broker-dealer stated: "We believe the inclusion of this trigger would negatively impact industry adherence to the protocol and jeopardize the market-wide adoption of the permanent cessation fallbacks."

55. As an alternative to inclusion of a pre-cessation trigger in the amended 2006 ISDA Definitions and a protocol, some respondents in this category instead supported publication of a separate template for a pre-cessation trigger that parties could use to bilaterally agree to include in legacy or new covered IBOR derivatives.

56. One bank/broker-dealer suggested that an organic process to transition away from LIBOR is the preferable approach, explaining: "After a statement from the supervisor of LIBOR's administrator that the benchmark is no longer representative for new derivative transactions, we

would expect [ourselves] and the broader industry to cease using LIBOR in new derivatives contracts and to accelerate the process of transitioning away from LIBOR, wherever possible. It would not be necessary to include a specific trigger in ISDA documentation in order to achieve this result. In fact, including a specific, additional trigger based on such a statement is likely to reduce the probability of an organic market driven transition, which we view as critical to avoiding disruption."

F. "Unresponsive/No Response" Responses

57. Four respondents (4.5%) submitted responses that were considered unresponsive. These respondents either did not provide a response to this question, or did not directly answer the question asked.

V. Summary of Comments on Protocol Options to Allow for Inclusion or Exclusion of Certain Transactions or a Matching Function

58. The Pre-Cessation Consultation proposed that, as an alternative to including a pre-cessation trigger based on representativeness in the amended 2006 ISDA Definitions and protocol, ISDA could potentially publish a protocol including pre-cessation triggers and related fallbacks that allows adherents to include or exclude certain transactions and/or that would allow counterparties to agree to include or exclude a pre-cessation trigger with certain counterparties through a matching function. 76 respondents opined as to whether they would or would not support such an alternative protocol.

59. The consultation asked respondents whether these options, or any variations thereof, would be helpful to address concerns regarding "non-representative" benchmarks, and asked respondents to comment on the relative advantages and disadvantages of such a protocol compared to the inclusion of a pre-cessation trigger in an amendment to the 2006 ISDA Definitions and protocol without any ability to elect for inclusion or exclusion of a pre-cessation trigger. Respondents who opposed optionality offered differing reasons, which are discussed below. In some cases, these respondents opposed optionality because they supported a "hard wired" pre-cessation trigger but, in other cases, these respondents opposed optionality because they opposed inclusion of a pre-cessation trigger altogether.

A. RESPONDENTS IN SUPPORT OF PROTOCOL OPTIONALITY

60. Multiple respondents who supported a protocol with optionality highlighted the flexibility of this approach as a benefit for market participants. For example, one bank/broker-dealer respondent observed that "such a protocol would be helpful as it allows certain users to still sign up to a protocol whilst maintaining the ability to handle the legacy of specifically designed swaps…The ability to designate trades it applies to and trades it doesn't is extremely helpful otherwise we would be faced with an all or nothing decision with regards to transition."

61. Other respondents posited that flexible protocols would encourage market uptake of an amendment to the 2006 ISDA Definitions regarding a pre-cessation trigger, with one bank/broker-dealer responding remarking that "[i]ncreased optionality could increase the number of market participants adhering to the protocol."

62. Some government-sponsored entities noted that a protocol with optionality was "the most efficient way of incorporating these features in legacy transactions, particularly for counterparties with large numbers of transactions and counterparties." A bank-broker dealer respondent echoed the benefits for market participants with a large volume of transactions: "We would prefer a protocol as it is [ ] cheaper and more effective to amend large numbers of existing contracts and easier to manage and track from [an] implementation standpoint."

63. Respondents also highlighted the operational advantages of a multi-option protocol over bilateral negotiations, and the benefits to reducing negotiation time and costs. One asset manager respondent commented that "use of a protocol encourages standardization while eliminating contract-by-contract analysis/negotiation and is the most efficient method of amending legacy contracts. We believe the use of protocol will maximize its 'up-take.'" Another asset manager stated: "Bilateral discussions are always long and seen as an opportunity to renegotiate other provisions that are not included in the scope of the intended technical amendment. We do prefer the possibility to fix many operations through a protocol approach and keep the negotiation to the minimum level."

64. One asset manager believed that protocols with optionality could be an attractive option to market participants with a range of opinions regarding a pre-cessation trigger, explaining that "this protocol would address some of the concerns around users who fall on either side of the issue of preference for/against using a pre-cessation trigger and is supportive of this flexibility. By using

these protocols, users of derivatives as a hedge for other products can more appropriately hedge based on the existence of a pre-cessation trigger in their other products."

B. Respondents in Opposition to protocol Optionality

65. By contrast, some respondents opposed the use of a protocol with optionality because they believed that such an approach was overly-complex and could lead to market fragmentation and reduced uptake of the pre-cessation trigger. For example, one bank/broker-dealer respondent asserted that "[s]uch a Protocol would impose additional levels of complexity to an already complex scenario and would be impossible to implement at the scale necessary for a smooth transition." Likewise, another bank/broker-dealer emphasized that "it is critical that the ISDA Protocol be as simple and transparent as possible" and advised that "building optionality into the ISDA Protocol or having multiple protocols will lead to complexity that would impede adherence and make it more difficult to assess the impact of a pre-cessation trigger."

66. One asset manager asserted that a protocol with optionality would undermine the transition process, stating: "This would harm the work that ISDA has done in trying to provide certainty to the derivatives market for the IBOR transition. We do not support any cessation triggers to be optional. Providing such optionality would create inconsistency between different transactions, hedges could breakdown and market can bifurcate between contracts with pre-cessation triggers to not. We think consistency is of utmost importance."

67. One professional services firm stated that a protocol with optionality would "likely prove cumbersome and operationally challenging for many end users, thereby limiting the usefulness of this approach." Similarly, an insurance company respondent observed that although a market participant may want to select a pre-cessation trigger for specific products, "the process of monitoring and tracking such transactions would create operational complexity and risk." One pension fund advised that a matching function would be "an operational nightmare" and that "such complexity would reduce adherence."

68. One bank/broker-dealer respondent explained: "Although the described specific protocol for pre-cessation issues may provide optionality to include or exclude certain legacy transactions and may be favoured by certain counterparties, we would want to avoid confusion in the market and challenges of having toggles across multiple protocols. As we have seen from the precedence, the more complexity and the more optionality there is in a protocol, the more complex implementation and the lower take-up of the protocol seems to be. We would therefore prefer a

uniform approach by having a simple, straightforward and workable IBOR Protocol in addressing both pre-cessation and permanent cessation issues."

69. Likewise, a clearinghouse respondent took the view that "[t]he presence of optionality increases complexity, and seems likely to lead to greater fragmentation and an absence of clarity and certainty in the marketplace. This could therefore undermine the adoption of other elements of the improved fallback arrangements that are important for the market."

C. RESPONDENT REACTIONS TO ENUMERATED PROTOCOL OPTIONS

70. As to the particular options posed in the consultation, some respondents expressed a preference for a single option listed, while others selected combinations and variations of the options listed.

71. Some respondents preferred an option that allowed parties to exclude certain transactions from the application of a pre-cessation trigger, and identified this as a benefit particularly for legacy transactions that did not include a pre-cessation trigger, as it would allow market participants to exclude these transactions and avoid a mismatch. One asset manager respondent noted that an "opt-out" approach was optimal, given the likely take-up of pre-cessation triggers by the CCPs.

72. A few respondents preferred only an opt-in approach. A bank/broker-dealer respondent explained that for this option, "[t]he main advantage is that it allows [us] to discriminate those transactions on which we want to include [a] pre-cessation trigger (e.g. transactions with entities in certain jurisdictions, or those hedging cash products that include pre-cessation triggers)."

73. Eight respondents clearly favored a matching function, and all but one preferred a matching function that allowed counterparties to agree to exclude particular transactions, over a matching function that allowed counterparties to agree to include particular transactions. According to one asset manager, a matching function that allowed counterparties to agree to exclude particular transactions "would easily allow for the fallback to be implemented across the entire market, while alleviating the concern that it will capture contracts, which both counterparties would prefer to exclude from the pre-cessation protocol." This respondent further noted that this approach would allow market participants that generally disfavored a pre-cessation trigger to include it in some contracts, so long as their counterparties also agreed. A government entity respondent also preferred this approach, which would allow counterparties to agree to exclude the pre-cessation trigger and related fallback though a matching process.

74. Some respondents selected combinations of options as their preference. For example, a professional services firm supported both the ability to apply the pre-cessation trigger to certain transactions only and a matching function that required both counterparties to agree to include the pre-cessation trigger, explaining that "these options make it less likely that end users will inadvertently include the pre-cessation trigger." This included some respondents who identified all options as beneficial. A bank/broker-dealer, for example, stated that "all are valid, the greater the flexibility the higher chances of a successful transition."

75. The consultation also asked whether respondents would prefer to use a protocol with optionality over template language for bilateral incorporation in derivatives contracts to address concerns regarding "non-representative" benchmarks and other pre-cessation concerns.

76. Many respondents preferred the use of a protocol as opposed to template language for bilateral incorporation, and noted that this approach was more efficient and would reduce the burden of negotiations. For example, a government sponsored entity explained that a protocol is "the most efficient way of incorporating these features in legacy transactions, particularly for counterparties with large numbers of transactions and counterparties." A bank/broker-dealer added that a protocol could "increase overall participation and allow for operational efficiencies to reduce the number of bilateral amendments in the event of industry wide support."

77. Some respondents stated that both a protocol and template language for bilateral negotiation could ultimately be needed. For example, one asset manager that preferred a protocol added that "it is important to note that there will need to be bilateral agreement for those transactions excluded from the protocol." Other respondents pointed out that even if a protocol were available, template language would still be necessary for bilateral negotiations of contracts with market participants that did not adhere to the protocol. A bank/broker-dealer noted that "it would be prudent for ISDA to produce bilateral templates as well for those in the market who are not accustomed to using Protocols." Another bank/broker-dealer echoed this comment, noting that "[t]he adherence rate to ISDA protocols is generally not high in the APAC region and it is important to include an option for bilateral incorporation of 'non representative benchmarks' as pre-cessation triggers."

78. Other respondents preferred the use of template language over a protocol. A bank/broker-dealer explained that this approach would provide "a level of risk management control over when to agree to such a trigger and thus to risk manage trades that include such a trigger" and "could be

useful in reducing basis between derivatives that hedge cash market products where a pre-cessation trigger has been adopted." A student loan servicer respondent cited a preference to use template language "to address concerns regarding 'non-representative' benchmarks on a deal-by-deal basis."

79. A professional services firm noted that unlike some entities that transacted with multiple counterparties and needed the efficiency of a protocol, it expected that end users facing only one or a few counterparties would likely prefer template language for bilateral incorporation.

80. A bank/broker-dealer clarified the type of template language it preferred: "[We] would be supportive of an effort by ISDA to develop template language and agreements that could be used to facilitate bilateral conversions of outstanding transactions, but not template language that would simply act as a substitute for the terms in the ISDA protocol. Note that the conversion agreements would need to be flexible enough to convert trades to market conventions that are not used by the ISDA protocol (e.g., to facilitate a legacy IBOR transaction being converted as a hedge to match a cash instrument that will use a simple average, forward looking term rate or have a different look back convention)."

81. Finally, the Pre-Cessation Consultation asked respondents for other suggested protocols to incorporate pre-cessation triggers and corresponding fallbacks on a voluntary basis that are less burdensome than template language for bilateral incorporation.

82. Respondents generally replied to this question by repeating their aversion to flexible approaches to incorporating pre-cessation triggers in the 2006 ISDA Definitions. For example, one bank/broker-dealer replied: "We do not have any other suggestions for flexible solutions, as flexible solutions are operationally challenging and may lead to unintended consequences." Similarly, another bank/broker-dealer answered: "We do not foresee any other viable solutions. Voluntary solutions will result in increasingly bespoke approaches that increase the likelihood that risk management will be misaligned, the full set of contract amendments will not be accomplished in a timely manner, and the transition to alternative rates will be more disjointed and problematic. We believe that ISDA is working on the correct pathway and correct set of tools, and that ISDA should proceed to complete the set of proposed tools that it is developing."

VI. Summary of Comments on the Ability to Determine Value Transfer

83. The Pre-Cessation Consultation asked market participants if a pre-cessation trigger were to be included in the 2006 ISDA Definitions, would it be appropriate or problematic to use the adjusted RFR plus a spread if the covered IBOR continues after counterparties convert to the adjusted RFR plus a spread, and the counterparties could determine whether they are receiving or paying more or less on the basis of the adjusted RFR plus the spread as compared to the unrepresentative covered IBOR that continues to be published.

84. Some respondents answered that the use of the adjusted RFR plus a spread is appropriate under these circumstances, particularly because such a statement would indicate that the covered IBOR no longer represents any economic reality and should no longer be used. One asset manager respondent noted that "[w]hile such comparisons could be made, there would be no benefit to counterparties to make them" because "[a]ccept[ance] [of] the new rate regime should render the old regime obsolete." Other respondents echoed this sentiment. For example, government sponsored entities commented: "Once the market has converted to its fallback alternative, the unrepresentative index observations are no longer meaningful." A government entity similarly observed: "If the Covered IBOR is no longer representative, it is useless to compare the fallback spread to the one calculated from IBOR rates."

85. A few respondents pointed out that to the extent both parties had already entered into contracts that included a transition to an alternative RFR plus a spread, they have already accepted those terms and would not have a basis to raise claims related to a value transfer.

86. By contrast, some respondents stated that it would be problematic to use the adjusted RFR plus a spread if the covered IBOR continues to be published. These respondents primarily highlighted the risk of litigation and the harm to some market participants by the value transfer that will benefit one party to a transaction. For example, one bank/broker-dealer explained: "This could be problematic as the scenario presents the potential for arbitrage of the protocol signing process and potential litigation risk should firms advise clients to sign and this results in a less than economically favorable outcome."

87. Another bank/broker-dealer further elaborated as to litigation risks: "It could be problematic as the adjusted RFR plus a spread could be economically different to the Covered

IBOR. Such economic differences would be known to us and our counterparties, an issue which would be exacerbated the longer the Covered IBOR continues to be published. This creates potential litigation and conduct risk because the economic transfer (if any) arising out of the change in rate would be used by counterparties to pursue mis-selling type claims against participants. For example, counterparties could claim that they were advised or encouraged to sign up to the revised protocol based on misstatements and/or misrepresentations about the nature and impact of the amendments. At the same time, we would also be open to similar risks if we were to continue to use an unrepresentative Covered IBOR in new contracts (if it is in some participants' economic interest to use the Covered IBOR)."

88. One bank/broker-dealer respondent explained that, as to the use of an RFR plus spread, "[t]his could become problematic as clients could specifically question this logic if the calculation is not in their favor. This becomes additionally problematic if, as we believe, you would need to have consistency with other asset classes where the sensitivity around this topic is greater, for example when considering retail business."

89. Multiple respondents stated that these potential issues highlighted why it was important that a covered IBOR cease at the same time or shortly after fallbacks are triggered, or why a pre-cessation trigger should not be used.

90. The Pre-Cessation Consultation also asked respondents if there was a way to mitigate concerns that counterparties could determine value transfer and what amendments to existing derivatives contracts might be preferable to replace references to the covered IBOR.

91. Many respondents raised potential regulatory solutions to this issue. Some respondents suggested that regulatory involvement or implementation of safe harbors from legal action may limit liability and thus reduce risk. Similarly, other respondents advocated for regulators to provide clear guidance to market participants in order to reduce risk. For example, one bank/broker-dealer respondent stated: "The regulators would need to be extremely clear in their communication and outline a robust and transparent framework to justify the movement away from an IBOR to a Risk Free Rate plus a spread. This would make it easier to persuade counterparties to adopt pre-cessation triggers."

92. Some respondents stated that market education can also play an important role in reducing risk. One asset manager respondent stated: "The best way to mitigate these concerns is through

outreach, education and disclosure that should be supported by all governmental and supervisory bodies." A bank-broker dealer respondent added: "The key point is that the market and market participants be well aware and informed about the issues."

VII. Summary of Comments on the Potential for Multiple Spread Adjustments

93. The second perceived challenge to inclusion and implementation of a pre-cessation trigger in the 2006 ISDA Definitions, related to the potential for multiple spread adjustments. The consultation explained that if derivative contracts are amended to reference the adjusted RFR plus a spread calculated by reference to historical data at the time the relevant regulator makes a statement that the covered IBOR is no longer representative, and the covered IBOR is subsequently permanently discontinued following an "index cessation event," then the spread that would apply for the permanent cessation fallbacks would differ from the spread that applied for the pre-cessation fallbacks.

94. First, the consultation asked whether the spread adjustment should automatically change to the permanent cessation spread at the time of permanent cessation (i.e., a spread calculated by reference to historical data at the time the announcement is made in respect of permanent cessation) or whether it should remain at the spread adjustment for the pre-cessation event.

95. Overall, nearly all respondents were in favor of only a single transition from the covered IBOR to an RFR plus spread adjustment, and did not want contracts that transitioned upon a pre-cessation trigger to move again upon a permanent cessation event.

96. Some respondents took the position that the spread adjustment should remain at the pre-cessation spread, and should not transition to a permanent cessation spread. According to one asset manager, this approach would "provide as much clarity and operational efficiency as possible." Similarly, a bank/broker-dealer explained that "…[m]ultiple spread adjustments would cause confusion and bring uncertainty."

97. Some respondents favored the use of multiple spreads instead of transitioning from the pre-cessation spread to the permanent cessation spread. One asset manager explained how this approach could work: "There should be two distinct cessation spreads. Contracts with a pre-cessation trigger would use the pre-cessation spread as determined by the pre-cessation mechanics

on/around the pre-cessation date. Contracts that do not contain pre-cessation triggers would use the Covered IBOR until a cessation event. Upon a cessation event, those contracts would be converted to the new RFR plus the cessation spread. There should be no ability to 'reset' the pre-cessation spread at cessation." This respondent noted that "a spread 'reset' at cessation approach would end up being more burdensome from a project management and program oversight perspective." Similarly, another asset manager added that "[r]esetting the spread of a contract that has already been converted in a pre-cessation event would increase confusion and complicate the hedging of existing, converted (SOFR + spread) swaps with new (SOFR) swaps." The option of using multiple spreads was directly addressed in a separate consultation question, and is discussed further below.

98. One bank/broker-dealer respondent replied that the spread adjustment should automatically change to the permanent cessation spread in order to avoid multiple spread adjustments for different trades.

99. Second, the consultation asked whether it would be problematic to have multiple spread adjustments apply based on when the fallbacks took effect.

100. Respondents appeared to interpret this question in two ways: some responded to a potential scenario in which two different spread adjustments were applied to a single transaction, while others responded to the potential scenario in which different spread adjustments were applied to different transactions. For example, one asset manager did not find the possibility of multiple spread adjustments in different transactions to be problematic, observing that "[d]ifferent derivatives could be tied to different indices, or to different spreads."

101. Many respondents addressed the possibility of applying two spreads to the same transaction, and asserted that multiple spread adjustments would be problematic.

102. Some respondents highlighted the practical challenges of implementing two spread adjustments. For example, one asset manager explained that "operationally changing the spread could be complex and potentially increases manipulation risk for LIBOR during the period between pre-cessation trigger and discontinuation." Another respondent observed that such a transition would "be operationally challenging and add to market confusion." Similarly, a bank/broker-dealer respondent explained that the use of multiple spread adjustments based on when the fallbacks took effect "…will result in increased operational burden to align the correct

trades to the correct spreads, which in turn will result in greater economic risk" and that "smaller market participants may find it difficult to deal with this operational burden in general."

103. Other respondents emphasized potential legal risks from the use of multiple spread adjustments. One bank/broker dealer explained: "Having multiple spread adjustments will imply an additional risk from a legal point of view. This may arise as two similar contracts could be modified to an adjusted RFR plus different spreads: prior to cessation or upon cessation. This treatment could also be challenging from an operational point of view." Similarly, an asset manager respondent observed that "[t]he creation of multiple spread adjustments may potentially confuse the market, result in legal challenges, and could impact market efficiency/liquidity."

104. A bank/broker-dealer respondent noted that the use of multiple spread adjustments could "imply value transfer and complicated operational setup for all involved stakeholders." Similarly, another bank/broker-dealer observed: "A valuation jump at the point of transition is problematic and two potential valuation jumps would be even more problematic. For example, technology systems will need to be updated to take into account multiple spread adjustments and embed new analytics to account for additional basis risks that may be introduced due to the presence of the multiple spread adjustments."

105. Many respondents stated that instead of transitioning to a second spread adjustment at the time of a permanent cessation event, the spread adjustment should remain at the pre-cessation spread adjustment. For example, one bank/broker-dealer asserted that "[a] single spread will be the cleanest from a risk management perspective. If there is a pre-cessation trigger with its own fallback methodology, then it would make most sense if the spread calculated would then persist through any index cessation event." Another bank/broker-dealer explained: "If a pre-cessation trigger event occurs prior to a permanent cessation trigger event, we take the view that the spread should remain at the spread adjustment fixed at the time when the non-representativeness statement is made. We do not recommend a subsequent spread adjustment due to a following permanent cessation trigger event. Having multiple spread adjustments may result in additional operation stress and confusion and the requirement for repeated customer engagement."

106. Some respondents also pointed to the covered IBOR's classification as unrepresentative as reason why the pre-cessation spread adjustment should be retained. One insurance company respondent explained that "the spread determined due to a pre-cessation trigger should supersede any adjustment that would be determined upon an actual cessation trigger. Once it is determined

that a Covered Libor is non-Representative upon pre-cessation, it is not reasonable to include the Covered IBOR quotes in the calculation of the spread adjustment for the period between Pre-cessation and an actual Cessation." A bank/broker-dealer respondent agreed: "We believe that the spread should remain at the spread adjustment for the 'pre-cessation' event given that the quality of the Covered IBOR is questionable between the pre-cessation's date and the permanent cessation's date."

107. Some respondents noted the risk of potential value transfer upon transition from a pre-cessation spread adjustment to a permanent cessation spread adjustment. One asset manager respondent explained: "Having two separate values for this spread would be particularly confusing and may be hard to practically implement. If an initial pre-cessation spread is applied initially, followed by a different index-cessation spread at a later date, one would expect some value transfer on the day the spread level is changed. It is therefore preferable to leave the post-cessation spread adjustment at same level as the one calculated at the pre-cessation trigger event."

108. The potential for P&L adjustments was also raised as a potential issue for transition from a pre-cessation spread adjustment to permanent cessation spread adjustment. For example, a bank/broker-dealer respondent maintained that "[i]f the underlying derivative does not have a pre-cessation trigger, the credit spread should not be readjusted after the occurrence of the pre-cessation event as the IBOR rate would no longer be representative. A readjustment could result in a P&L event. ISDA or the relevant regulator should consider making the permanent cessation spread equal to the pre-cessation spread regardless of subsequent movements in the Covered IBOR following the pre-cessation trigger."

109. Some bank/broker-dealer respondents also identified basis risk as a problem with the use of subsequent spread adjustments. One respondent explained: "The spread adjustment calibration window should end when the pre-cessation trigger happens, regardless of whether the contract includes the pre-cessation trigger. Changing the spread adjustment would introduce potential basis risk between contracts with and contracts without the pre-cessation trigger." Another respondent observed that "this would create some basis risk with other financial products and operational challenges. It could also re-inforce incentives for speculative market participants who do not adhere to the pre-cessation trigger at the expense of their swap dealer."

110. By contrast, one bank/broker-dealer respondent contended that the spread should be the permanent cessation spread adjustment because "in between the 'pre-cessation announcement' and

the actual discontinuance of LIBOR, the illiquidity of the market could result in large LIBOR movements. Leaving these out of the 'discontinuance' spread adjustment could result in unnecessarily large spread adjustments and NPV transfer."

111. One bank/broker-dealer respondent indicated that this potential problem justified avoiding pre-cessation triggers altogether: "This is exactly what we want to avoid. We believe there is no need of pre-cessation triggers. We need a permanent discontinuation trigger with a spread calculated at this time. We want to avoid having two different spread that will create confusion and risk of conflicts between parties."

112. Finally, the consultation asked whether adherents to the protocol that excludes a pre-cessation trigger for fallbacks in certain contracts and/or with certain parties should agree that the spread adjustment relate to the pre-cessation trigger should nonetheless apply if a permanent cessation occurs.

113. Responses to this scenario were mixed. Some respondents were in favor of applying the pre-cessation spread adjustment at the time of a permanent cessation, primarily to promote market consistency, to avoid operational challenges, and to avoid continued use of an unrepresentative IBOR. However, other respondents took the position that market participants that chose not to use a pre-cessation trigger should not be forced to use the pre-cessation spread adjustment at the time of a permanent cessation event, and that the permanent cessation spread should be used.

114. Respondents in favor of applying the pre-cessation spread adjustment generally cited the need for consistency across products. For example, one government-sponsored entity noted that "to the extent that market-wide adoption of pre-cessation triggers cannot be achieved, alignment in the calculation of spreads used for the substitution of RFR would mitigate some of the variability and basis risk incurred d[ue] to the misalignment of cessation/pre-cessation trigger activation." Another bank/broker-dealer explained that "the most important [point] is to ensure consistency on pre cessation triggers and calculation of spread adjustments across all products and contract types."

115. Other respondents emphasized the operational challenges of multiple spread adjustments. An insurance company respondent stated: "Given the additional operational complexity of having two spread adjustments, our preference would be for there to be only one trigger of the fallbacks.

Therefore, we would prefer for the pre-cessation trigger [and related spread] to nevertheless apply when a permanent cessation occurs."

116. A few respondents generally supported this approach, but noted that this issue was one reason to oppose optionality in a protocol to exclude certain transactions.

117. Some respondents who opposed applying the pre-cessation spread adjustment at the time of a permanent cessation when adherents to a protocol had excluded a pre-cessation trigger in certain contracts noted that since the parties had made this choice, they should not be required to adopt the pre-cessation spread. One asset manager respondent remarked that this approach "seems wrong," and another observed that "using a spread adjustment adopted at the time of cessation would seem to be more consistent with their desire to exclude pre-cessation triggers."

118. Multiple respondents in this category said that in this situation, the permanent cessation spread adjustment was the more appropriate spread to use. As one bank/broker-dealer respondent explained, "[i]f adherents exclude a pre-cessation trigger then the pre-cessation spread adjustment is not relevant to them and the cessation spread adjustment should be the only one that applies." Another bank/broker-dealer warned that "[a]llowing for a spread adjustment pegged to a pre-cessation trigger in such circumstances may introduce further market fragmentation and confusion for the end users."

119. Some respondents were undecided as to how this situation should be addressed. One asset manager stated that it could depend on the length of time between the pre-cessation event and permanent cessation event because "[t]he averaging aspect of the spread methodology should minimize any difference between these two spreads for any short time period" but "that does not necessarily hold true for longer periods." Other respondents generally replied that they favored consistency and homogeneity across the market, but did not take a specific position as to the preferred approach.

VIII. Conclusion

120. Responses to the Pre-Cessation Consultation indicate that a majority of market participants would not be content, outright or under certain circumstances, to continue referencing a covered IBOR in either existing or future derivative contracts following a public statement from the supervisor of that covered IBOR that it was no longer representative. However, the Pre-Cessation

Consultation did not yield a consensus among market participants regarding *how* to address pre-cessation issues related to representativeness. Although a majority of respondents (64%)[12] supported the inclusion of a pre-cessation trigger in the amended 2006 ISDA Definitions, a significant number of them disagreed about the implementation of such a trigger.

121. ISDA will continue to engage with market participants and the FSB OSSG regarding how to address a non-representative covered IBOR in derivatives documentation.

[12] This figure includes responses categorized as "Yes," "Yes, and want optionality/flexibility" and "Yes, but want no optionality/flexibility."

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