March 11, 2021

Federal Reserve Directs Examiners to Review Banks' Exit Plans As LIBOR Deadline Approaches

On the heels of the announcement by the UK Financial Conduct Authority last Friday clarifying the cessation deadlines of all LIBOR tenors,[1] on March 9, 2021, the Federal Reserve (the "Fed") issued guidance to examiners to evaluate banks' LIBOR exit plans in the coming months.[2] In a letter to supervisory and examination staff and supervised institutions, the Fed advised examiners to review supervised firms' plans and progress in moving away from LIBOR during examinations and other supervisory activities in 2021.[3]

Citing the Interagency Statement on LIBOR Transition issued on November 30, 2020,[4] the Fed reiterated the risks involved in entering into new contracts that reference LIBOR after December 31, 2021, the expected deadline for cessation of LIBOR's publication. Citing safety and soundness risks to banks and to the financial system more broadly, the Fed urged examiners to "consider issuing supervisory findings and other supervisory actions if a firm is not ready to stop issuing LIBOR-based contracts by December 31, 2021."[5]

The Fed issued two sets of examiner guidance for assessing LIBOR transition efforts: one for institutions with less than $100 billion in total consolidated assets and one for institutions with $100 billion or more in total consolidated assets.[6] Each set enumerates factors for examiners to consider in assessing six key aspects of transition efforts: (1) transition planning; (2) financial exposure measurement and risk assessment;

[1] *LIBOR Cessation: FCA Announcement on the End of LIBOR Triggers ISDA's Spread Adjustment Fixing Date*, Paul, Weiss Client Alert, Mar. 5, 2021, available here (last visited March 11, 2021).

[2] *SR 21-7: Assessing Supervised Institutions' Plans to Transition Away from the Use of the LIBOR*, Fed, Mar. 9, 2021, available here (last visited March 11, 2021) (hereinafter "Federal Reserve Letter"). The Fed's guidance follows Fed Chairman Jerome Powell's recent statement to the House Financial Services Committee advising that the central bank supports federal legislation to help facilitate the financial industry's transition away from LIBOR for tough legacy contracts. *See Fed Chief Backs Congressional Fix On Legacy Libor Contracts*, Jon Hill, Law 360, Feb. 24, 2021, available here (last visited March 11, 2021).

[3] *Federal Reserve Letter*.

[4] *SR 20-27: Interagency Statement on LIBOR Transition*, Fed, Nov. 30, 2020, available here (last visited March 11, 2021).

[5] *Federal Reserve Letter*.

[6] *See Examiner Guidance for Assessing LIBOR Transition Efforts at Firms with Less Than $100 Billion in Total Consolidated Assets Supervised by the Federal Reserve*, Fed, Mar. 9, 2021, available here (last visited March 11, 2021); *Examiner Guidance for Assessing LIBOR Transition Efforts at Supervised Firms with $100 Billion or More in Total Consolidated Assets*, Fed, Mar. 9, 2021, available here (last visited March 11, 2021).

(3) operational preparedness and controls; (4) legal contract preparedness; (5) communication; and (6) oversight.

In the guidance relating to institutions with less than $100 billion, the Fed provides an overview of steps a supervised firm in this classification should take for each of the six key areas. In contrast, in its guidance for institutions with $100 billion or more, the Fed outlines in greater detail the actions those institutions should take with respect to the six key areas. For example, pertaining to transition planning, the Fed recommends that institutions with less than $100 billion "should plan to transition away from LIBOR-based financial products" and "[t]he detail and scope of transition planning should be commensurate with the firm's LIBOR exposures." For larger institutions, the Fed recommends that the institution "should have a LIBOR transition plan that includes a governance structure that clearly defines roles and responsibilities needed to execute the plan and a project roadmap with defined timelines and milestones." The guidance then goes on to list six additional aspects that should be examined in relation to any such plan. A supervised firm would be well advised to review the applicable guidance to ensure that its LIBOR transition planning is in line with the Fed's expectations.

Other regulatory agencies continue to be similarly focused on preparation efforts to ensure a smooth LIBOR transition. In January, the Commodity Futures Trading Commission ("CFTC") published a no-action letter authorizing futures commission merchants to invest customer funds in certain permitted investments, including investments that contain an adjustable rate of interest benchmarked to the Alternative Reference Rate Committee and Federal Reserve Bank of New York-endorsed Secured Overnight Financing Rate ("SOFR").[7] The CFTC noted that "[t]his relief recognizes the increasing use of SOFR as an alternative reference rate to LIBOR in financial markets, and is consistent with previous CFTC staff relief issued to facilitate transition by market participants away from LIBOR."[8] In February, the Office of the Comptroller of the Currency published a self-assessment tool for bank management to use to evaluate bank risk management processes and to identify and mitigate the bank's transition risks associated with LIBOR's cessation.[9]

Legislators, regulators, industry leaders, and working groups continue to emphasize adequate preparation for the anticipated cessation of LIBOR, recommending that market participants prioritize and devote the necessary resources to transition planning, especially as the year-end deadline approaches.

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[7] *CFTC Letter No. 21-02*, CFTC, Jan. 4, 2021, available here (last visited March 11, 2021).

[8] *CFTC Staff Provides Temporary Relief to Futures Commission Merchants Regarding Certain SOFR-Linked Investments*, CFTC, Jan. 4, 2021, available here (last visited March 11, 2021).

[9] *LIBOR Self-Assessment Tool*, OCC, Feb. 10, 2021, available here (last visited March 11, 2021).

This memorandum is not intended to provide legal advice, and no legal or business decision should be based on its content. Questions concerning issues addressed in this memorandum should be directed to:

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