

October 5, 2020

LIBOR Transition: ISDA Receives Positive Business Review Letter from the Department of Justice on Proposed IBOR Fallback Language

October 12, 2020 Update: On October 9, 2020, ISDA [announced](#) that it plans to launch its fallback language for over-the-counter derivatives contracts to address uncertainty stemming from the expected cessation of LIBOR and other interbank offered rates. ISDA stated that it has kept apprised various foreign competition authorities, including the Australian Competition and Consumer Commission (ACCC), the Canadian Competition Bureau (CCB), and the European Commission Directorate-General for Competition (DG Comp) of the issues covered in the DOJ's business review letter, discussed below. ISDA announced that it does not anticipate adverse action by these authorities, and will officially launch its IBOR Fallbacks Supplement and Protocol on October 23. The effective date(s) of the IBOR Fallbacks Supplement and Protocol will be January 25, 2021.

As we have [previously reported](#), the International Swaps and Derivatives Association, Inc. ("ISDA") has developed, and is now poised to publish, robust fallback language for over-the-counter derivatives contracts to address uncertainty stemming from the expected cessation of LIBOR and other interbank offered rates. The fallback language will be included in a new supplement (the "IBOR Fallbacks Supplement") to the existing 2006 ISDA Definitions governing most interest rate derivatives. ISDA also intends to publish a protocol (the "IBOR Fallbacks Protocol") to allow market participants to incorporate the new language in currently outstanding derivatives contracts. In preparation for the publication of the IBOR Fallbacks Supplement and launch of the IBOR Fallbacks Protocol, ISDA solicited support of the Antitrust Division of the U.S. Department of Justice ("DOJ") in the form of a positive business review letter.

On October 1, the DOJ [announced](#) that it had issued a [business review letter](#) finding that the proposal of ISDA "to amend its standardized model documentation for derivatives to account for the potential discontinuation of certain interbank offered rates [IBORs] . . . [is] unlikely to harm competition."¹ ISDA

¹ The anticipated cessation of the London Interbank Offered Rate ("LIBOR") remains the end of calendar year 2021. LIBOR is a benchmark interest rate at which large banks indicate that they can borrow short-term wholesale funds on an unsecured basis in the interbank market. The rate is published daily in five currencies and seven tenors, and represents the average of submissions from panel banks, resulting in the daily publication of 35 interest rates by the Intercontinental Exchange. As we have previously [written](#), U.S. and international regulators have made LIBOR transition preparedness a priority for 2021. While the COVID-19 pandemic has impacted certain interim deadlines imposed by international and U.S. regulators, working groups and associations, such as ISDA, remain focused on enabling a smooth transition for market participants.

[sought this business review letter](#) from the Antitrust Division because ISDA's "members are competitors in certain markets, [and ISDA's] work to develop a proposed fallback methodology could be viewed as coordination among competitors." ISDA informed the DOJ that ISDA "has worked with industry participants to develop a methodology that attempts to account for the inherent differences between the IBORs and the relevant" risk-free rates. ISDA specifically requested that this coordination between ISDA and market participants not be subject to Antitrust Division enforcement.

The Antitrust Division's business review letter program allows businesses to engage with the DOJ to receive antitrust guidance on proposed courses of conduct. The Antitrust Division will, on the basis of representations it receives, set out its present enforcement intentions with respect to the proposed course of conduct. Here, the DOJ stated that it "has no present intention to challenge ISDA's proposal to amend its standardized documentation" but that it "reserves the right to bring an enforcement action in the future if the actual operation of the proposed conduct proves to be anticompetitive in purpose or effect."

The proposed ISDA amendments at issue in the business review letter include the addition of designated fallback rates for certain IBORs through a supplement to ISDA's 2006 ISDA Definitions, and a protocol to apply these fallback rates to legacy contracts. As described by the DOJ, these fallback rates "are based on replacing a given IBOR with an adjusted 'risk-free rate ("RFR")." Adjustments to RFRs are required because RFRs, unlike IBORs, are overnight, risk-free rates. Therefore, RFRs will be adjusted to account for the difference in maturity between each RFR and corresponding IBOR (i.e., the "term" used for IBOR rates) and will incorporate a "spread" adjustment that "accounts for the risk premium reflected in IBORs but not RFRs." ISDA's IBOR Fallbacks Supplement also includes cessation and certain pre-cessation triggers following which a relevant IBOR will transition to its applicable fallback RFR. Market participants are able to agree to different triggers and fallback rates, or not use one at all. Contracting parties can also decide to seek bilateral amendments to outstanding contracts in lieu of adherence to the offered IBOR Fallbacks Protocol.

With respect to the proposed fallback rates, the DOJ's review determined the ISDA proposal "does not . . . indicate[] an agreement among its members to limit their choice of fall back rates to only the proposed fallback rates." The DOJ notes in the business review letter that "[i]f a user of ISDA's model documents does not wish to use the proposed fallback rates, nothing in the Proposed Supplement or Proposed Protocol prevents the user from entering into a derivatives contract (or amending one currently in place) that uses an alternative rate, including rates not included in the 2006 ISDA Definitions." The letter further notes that the "RFRs were chosen by public-private working groups tasked by the [Financial Stability Board] to identify suitable RFRs to replace their corresponding IBORs" and that ISDA received "breadth of support" for the RFRs "during its consultation process soliciting input from the industry regarding possible adjustment approaches." The DOJ's letter also notes that the Proposed Protocol is voluntary.

The DOJ's review also concluded that the ISDA proposals will have "substantial procompetitive benefits and that these benefits outweigh the possible anticompetitive effects," including "increasing . . . efficiency

and certainty,” including by avoiding the “time and effort needed to obtain quotes and calculate rates on a contract-by-contract basis”; allowing the easy incorporation of “the proposed fall back rates into existing derivatives contracts without having to individually re-negotiate the contracts”; and reducing “the number of disputes surrounding the calculation of fall back rates should their IBORs be discontinued.”

The favorable business review from the DOJ is an important step in ISDA’s launch of its IBOR Fallbacks Supplement and Protocol. As described in its [letter](#) to the Bank of England and the Federal Reserve Bank of New York, ISDA plans to next seek the review of the IBOR Fallbacks Supplement and Protocol from competition authorities in other jurisdictions, notably the European Union, Australia, and Canada. Following a favorable review from these authorities, ISDA will provide market participants with approximately two weeks’ notice of the official launch date(s) of the IBOR Fallbacks Supplement and Protocol. The effective date(s) of the IBOR Fallbacks Supplement and Protocol is expected to be in early 2021.

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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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