



LEADING TREASURY
PROFESSIONALS

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BRIEFING NOTE:

LIBOR ADMINISTRATOR CHANGE TO ICE BENCHMARKS FROM BBA LIBOR:

Implications for non-financial
companies

January 2014



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Briefing note

LIBOR Administrator change to ICE Benchmarks from BBA LIBOR: Implications for non-financial companies

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Quick read

Transition from BBA LIBOR to ICE LIBOR has been planned to cause as little disruption as possible. Corporate treasurers may need to give some attention of documentation. The key [LIBOR Code](#)² (that sets out how it is compiled and how confidence in the rates is assured) will continue unchanged (at least initially) except to reflect the new parties involved. Review processes may lead to changes in the future.

As from 1st February 2014 ICE Benchmark Administration Limited will take on the administration of LIBOR that was previously handled by BBA LIBOR Ltd. Whilst this particular change may have limited day to day implications for treasurers, it is indicative of the major processes going on that could in time trigger more fundamental changes. This briefing note aims to alert corporate treasurers to the immediate impact, to the possibilities that need to be taken into account in planning, to the potential implications and to further sources of information.

Change of Administrator

The Wheatley Review was set up by the Chancellor of Exchequer (the UK's finance minister) in July 2012. It considered the regulation of LIBOR and other benchmarks following the revelation of manipulation of the LIBOR rates. In September 2012 the [review's recommendations](#)¹ included:

- creation of a new framework of law and regulation
- making designated benchmark compilation and distribution a regulated activity under the Financial Conduct Authority (FCA)
- FCA confirmation of a Code of Conduct for Contributing Banks to

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https://www.gov.uk/government/uploads/system/uploads/attachment_data/file/191762/wheatley_review_libor_finalreport_280912.pdf

LIBOR as Industry Guidance, (the code setting out the internal governance, audit, compliance and so on required of banks contributing rates). The approved [Code](#)² also has annexed the submission methodology to be followed by contributing banks

- transition to a new independent LIBOR Administrator.

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After a process run by the Hogg Tendering Advisory Committee³, ICE Benchmarks Limited was selected as the new Administrator.

This change will officially become effective 1st February 2014 and ICE Benchmarks' first rates will be published on Monday 3rd February. The IntercontinentalExchange Group press release, [ICE Benchmark Administration to become new administrator of LIBOR](#)⁴, has the details. The rates will be known as ICE LIBOR (formerly BBA LIBOR).

² <http://www.bbalibor.com/download/9070>

³ Colin Tyler, Chief Executive of The Association of Corporate Treasurers was a member of the Hogg Committee.

⁴ <http://ir.theice.com/investors-and-media/press/press-releases/press-release-details/2014/ICE-Benchmark-Administration-to-Become-New-Administrator-of-LIBOR-on-February-1-2014/default.aspx>

ICE will be introducing their own Licence and usage fees. In the first instance these will apply to any provider redistributing the LIBOR rates who may in turn decide to charge users. Users simply viewing real-time Libor rate information through a redistributor will not require a licence⁵.

The methodology etc. set out in the LIBOR Code and used for collecting rates from contributors will not change, except to reflect the new parties involved. The key features of LIBOR, including the controlled use of judgement in compilation that give confidence in LIBOR and help ensure its availability on all business days remain unchanged.

Users should be aware that there will be new governance arrangements. There will be a new Oversight Committee⁶, which will administer the LIBOR code of conduct.

Immediate implications

Loan agreements, and some commercial contracts too, will typically make use of and therefore define LIBOR. Particular wordings will need to be checked to determine if they still hold good following the change of Administrator.

The wording used in recent loan agreements based on the Loan Market Association standard documents will refer to “the London interbank rate administered by the British Bankers Association (or such other person which takes over the administration of that

⁵ Non-financial companies using LIBOR as benchmark rates in, for example, intra-group financing or for interest on customer overdues, would in principle require a licence from ICE Benchmarks as they did from BBA LIBOR Ltd. ICE Benchmark’s terms and conditions are available from their web page <https://www.theice.com/iba.jhtml>.

⁶ The Association of Corporate Treasurers has been asked to be a member of the Oversight Committee

rate)...” and can therefore withstand the change, but new agreements should be adjusted.

Older agreements may not have catered for the possibility of a change. The outcome will depend on the precise terms of the contract, but, as an example, the English courts have a number of tools at their disposal to achieve continuity (notably contractual interpretation and implication of terms). Clifford Chance has prepared a briefing paper discussing [LIBOR reform and contractual continuity – issues for the financial markets](#)⁷ generally

Longer term implications of review processes

Regulators across the globe have been concerned over the integrity of the rate gathering process for interest rate benchmarks and other financial benchmarks in general use. IOSCO (The International Organisation of Securities Commissions) published its [Principles for Financial Benchmarks](#)⁸ in July 2013 and the European Commission published its legislative [Proposal for regulation of indices used as benchmarks in financial instruments and financial contracts](#)⁹ in September 2013.

At the behest of the G20 the Financial Stability Board is [considering interest rate reference rates that could be used as an alternative to LIBOR](#)¹⁰ and has established a Market Participants Group (that includes some

⁷ http://www.cliffordchance.com/publicationview/s/publications/2014/01/libor_reform_andcontractualcontinuityissue.html

⁸ <http://www.iosco.org/news/pdf/IOSCONEWS289.pdf>

⁹ http://ec.europa.eu/internal_market/securities/benchmarks/index_en.htm

¹⁰ http://www.financialstabilityboard.org/publications/r_130829f.pdf

corporate treasurers) to investigate. Their report is awaited with interest.

For treasurers, the availability of LIBOR rates provides considerable convenience as compared to the practice that preceded its establishment which in the past entailed borrowers or agents taking rate quotes from a reference panel at every drawdown and rate re-fixing date. Companies do value the availability of a rate, like LIBOR, that can continue to be available even if market liquidity is thin or conditions disturbed. The expectation of ongoing availability in a consistent manner for many years into the future is also a key feature.

It is therefore a crucial concern of non-financial companies that banks might be reluctant to contribute rates for reputational, competition law and other such concerns. If such concerns remain they must be addressed. But as the ACT has said repeatedly “The banks need to know that their customers expect them to contribute to reference rates if called upon to do so. Regulators and supervisors should insist that banks do so contribute.” Informal pressure continues and some moves towards a reserve power to require contributions have been included in draft European legislation, but banks’ own courage and confidence remain a weak link. The other threat to ~IBOR style rates is the financial-industry focused view of global regulators who at every turn have favoured transaction-rate-sampling type benchmarks over contributed rates involving judgements, even though recent scandals have shown how they too are vulnerable to manipulation.

LIBOR type rates, with appropriate governance and safeguards, have particular advantages for companies. LIBOR brings together components adding up to a bank’s reasonable short-term funding costs, including risk-free rates and other

adjustments reflective of the bank’s own credit risk. The controlled judgemental elements of the rates contributed to LIBOR mean that the benchmark can be published even at times of market disruption so the rate is reliably available – the fall-back arrangements in case of unavailability being pretty unacceptable or unavailable at times of crisis.

Alternative reference rates such as the OIS ([Overnight Index Swap¹¹](#)) rate, government T-bill rates, or repo rates could all have some applicability in many uses but they each have very different characteristics to LIBOR. The fact is that LIBOR is designed to be representative of unsecured bank funding costs of leading banks in the currency concerned and therefore does contain an element reflective of credit risk of the contributing banks. This element is not present to the same degree in OIS and repo rates nor at all in government rates. These would therefore require a new complication in loan agreements to convert the reference rate into something representative of a bank’s cost of funds and raise issues about corresponding rate-hedging contracts. Some may argue for the use of OIS rates + CDS spread + the borrower’s credit margin while others will point out the vagaries of the CSD rates.

As stated above, treasurers await with interest the report of the Financial Stability Board in 2014, but hope for continued availability of ~IBOR-type rates alongside others so that users can choose what suits them best.

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http://wiki.treasurers.org/wiki/Overnight_indexed_swap

Other ACT sources regarding LIBOR

Some history of LIBOR is available on the [Treasurer's Wiki](#)¹²

The ACT first expressed concern about LIBOR rates in 2008 in a [note](#)¹³ about rates in loan agreements. Since then the ACT responded to many consultations nationally, at a European level and internationally (available on the Policy submissions and responses listing at <http://www.treasurers.org/technical>) and has been active behind the scenes.

That “Responsible, well conducted banks that are significant participants in the relevant markets should feel an obligation” to continue contributing rates for ~IBOR benchmarks was the theme of an ACT release (“[ACT stresses the importance of LIBOR and EURIBOR to companies](#)”¹⁴) in 2011 when it seemed banks might try to slink out of their responsibilities.

The ACT welcomed the institution of the Wheatley Review in the UK in 2012 and that the discussion paper issued by the Review recognised the importance of judgement in banks’ contributions of rates to LIBOR setting. “[The real economy needs LIBOR](#)”¹⁵ was a theme of the ACT’s response.

Our Policy and Technical Director’s blogs supported the ACT’s themes. [Libor: \(2\) What should it look like?](#)¹⁶ stressed the need for continuity though some users may find other benchmarks suitable. In [Libor: \(1\) Banks are the risk](#)¹⁷ he set out that industrial and commercial firms were much more confident in the setting of LIBOR, especially as the FSA had imposed conduct requirements for banks submitting rates and in January 2011 had the banks attest to them that they were following those requirements, but, that a weak point was banks’ willingness to go on contributing rates.

The tendency of the authorities to interpret “users” of interest rate benchmarks as being financial services firms rather than end users such as commercial and industrial firms was stressed – and deprecated – in ACT [responses](#)¹⁸ to IOSCO, ESMA and EBA consultations in early 2013.

The importance of LIBOR as a benchmark rate was seen in its use by Apple Inc for floating rate tranches in the largest ever bond issue to that date in 2013 – despite the US controversy over the rate at the time (blog: [Apple Inc. sheds light on Libor](#)). The issue later in that year by Verizon, displacing Apple’s record issue as the largest, also used a LIBOR benchmark.

¹² <http://wiki.treasurers.org/wiki/LIBOR>

¹³ <http://www.treasurers.org/marketdisruption/pressrelease>

¹⁴ <http://www.treasurers.org/node/7329>

¹⁵ <http://www.treasurers.org/node/8170>

¹⁶ <http://www.treasurers.org/node/8043>

¹⁷ <http://www.treasurers.org/node/8044>

¹⁸ <http://www.treasurers.org/node/8872>





THE ACT WELCOMES COMMENTS ON THIS REPORT

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