



LIBOR and the ISDA Protocol **Top Ten**

Ten questions you have about the ISDA Protocol
but didn't know how to ask¹

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1

Why is there a Protocol?² The contractual language for derivatives instrument that specifies the rate that will be used if LIBOR is unavailable was widely acknowledged to be insufficient under the prior ISDA definitions. As a result, ISDA³ developed more robust fallback language to specify the rate to be used upon a LIBOR cessation (the fallback rate) and established the Protocol as a tool to incorporate this fallback language in the existing agreements. The fallback rate for USD LIBOR under the Protocol is adjusted SOFR plus an adjustment spread to account for differences in tenor and credit. SOFR stands for the “Secured Overnight Financing Rate” and is the benchmark rate for dollar denominated derivatives and loans selected to replace LIBOR.⁴

2

What does it mean to adhere to the ISDA Protocol? Adhering to the ISDA protocol modifies the fallback language under your contract such that, upon a LIBOR cessation, the LIBOR leg under your contract will convert to SOFR compounded in arrears plus an adjustment spread. The adjustment spread will be calculated upon certain trigger events and will be based on a 5-year median between LIBOR and SOFR. If you have a LIBOR-based swap or other LIBOR-based derivatives, seek advice from your bond counsel and your municipal advisor. The Protocol is one way to amend your ISDA – and there are bilateral agreement options as well.

3

What does adhering to the Protocol accomplish? If you adhere to the Protocol, you will be automatically amending the provisions within your Protocol Covered Documents to the extent that the counterparty has also agreed to adhere to the Protocol. LIBOR references will instead reference the relevant fallback rate (SOFR) in the event that there is a (i) permanent cessation trigger statement by the Financial Conduct Authority (FCA),⁵ (ii) permanent cessation trigger – statement by ICE Benchmark Association (IBA),⁶ or (iii) pre-cessation trigger – statement of unrepresentativeness by FCA. Protocol Covered Documents comprise not only ISDA-published master agreements and credit support documents, but also certain other forms of master agreements and credit support documents enumerated in an annex to the Protocol.⁷

4

If I adhere to the Protocol, what documents will I be amending? You will be amending all documents that are considered Protocol Covered Documents. It would be prudent to check all of your swap documents, including ISDA Master Agreements, Credit Support Documents or Credit Support Annexes and Swap Confirmations.

5

Are any third-party (e.g. insurers, guarantors) consents needed in any of my agreements before I am able to implement the Protocol? You should review your documentation and discuss with your counsel and your municipal advisor to determine if any third-party consents are needed before you enter into the Protocol.

6

In adhering to the Protocol am I providing representations about the authority to enter into the Protocol and the legal, valid and binding effect of the Protocol? Yes. It is important to ensure that you have received the proper authorization from your governing body before entering into the Protocol. **Can I reverse my adherence to the Protocol?** No. If you want to make a subsequent change, you can do that through a bilateral agreement with the counterparty.

7

By adhering to the Protocol will I also be amending my loan/bond documents that govern the liability that I am hedging with my swaps? No. Your loan/bond documents will need to be separately amended. A consideration is whether you want to consult with your municipal advisor and your lender to determine if you can reach a simultaneous agreement for a consistent amendment of your loan/bond documents and your related swap documents.

8

If I do not adhere to the Protocol, are there other ways in which I can amend the Protocol Covered Documents and the related bond/loan documents? Yes, by entering into bilateral agreements with each of your counterparties to agree on the terms for amending the relevant documents.

9

Can I reverse my adherence and, if not, can I amend any of my Protocol Covered Documents subsequent to adherence? Adherence to the Protocol is irrevocable with respect to the documents amended by adhering to the Protocol. The Protocol Covered Documents can be subsequently modified by entering into a bilateral agreement with each of your counterparties. Additionally, a notice can be provided to ISDA essentially terminating your adherence with respect to any new documents entered into after your notice to ISDA becomes effective.

10

Don't I have until 2023 to change my LIBOR reference rate? What's the rush?

The administrator of LIBOR has announced it will consult on its intention to cease the publication of the one week and two month USD LIBOR settings immediately following the LIBOR publication on December 31, 2021. The remaining USD LIBOR settings will cease to publish immediately following the LIBOR publication on June 30, 2023. If your existing contracts utilize a LIBOR tenor of one week or two months or if the termination date for your existing contracts is after June 30, 2023, modifications will likely need to be made to your existing contracts. The GFOA urges municipal issuers to review their existing contracts and to work with their advisors as soon as practicable to put a plan in place for the completion of these modifications.^{8,9}

¹ See also Alternative Reference Rates Committee "Frequently Asked Questions" <https://www.newyorkfed.org/medialibrary/Microsites/arrc/files/ARRC-faq.pdf>

² ISDA 2020 IBOR Fallbacks Protocol: <https://www.isda.org/protocol/isda-2020-ibor-fallbacks-protocol/>

³ <https://www.isda.org/2020/05/11/benchmark-reform-and-transition-from-libor/>

⁴ <https://www.newyorkfed.org/arrc/sofr-transition#aboutsofr>

⁵ For more FCA LIBOR Information and Announcements here: <https://www.fca.org.uk/markets/libor>

⁶ For more information on the IBA LIBOR Methodology and Announcements here: <https://www.theice.com/iba/libor>

⁷ See list of protocol covered documents on ISDA Protocol FAQs: <http://assets.isda.org/media/3062e7b4/3cfa460a-pdf/>

⁸ See ARRC Communication Urging Action on Transitioning to SOFR: https://www.newyorkfed.org/medialibrary/Microsites/arrc/files/2021/ARRC_Press_Release_Wipf_Action_Transitioning_SOFR.pdf

⁹ See GFOA Document "The Transition Out of LIBOR: What State and Local Governments Should be Discussing with Their Financing Team" <https://www.gfoa.org/membalert-the-transition-out-of-libor>