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GFOA Working Group Focusing on Libor Transition.

The Government Finance Officers Association has formed a working group to help issuers prepare for the phase-out of Libor at the end of 2021.

The group of around a dozen issuers, bankers, broker-dealers, bond attorneys, and municipal advisors will meet Tuesday for their second time to sort out their priorities for educating the public finance community.

"We're all looking at it from our different perspectives at what we can do in our respective roles to get the word out about the Libor transition and that the issuers who have that exposure are aware of it," said Cindy Harris, chief financial officer of the Iowa Finance Authority who is chairing the working group.

The working group plans to meet every other week to develop instructions to guide participants in the municipal bond market to make the transition.

"I feel that the Libor transition is probably not on the top of people's minds," said Harris, "Even if they have Libor they may think it's not as pressing a matter to deal with than a lot of the other challenges they are having to deal with in their jurisdiction. That's why I think it's good to get the word out that this is coming sooner than people may think. If you are changing contracts, you may need board approvals to do that. And that may need a month or two of lead time."

The International Swaps and Derivatives Association announced Oct. 23 its IBOR Fallbacks Supplement and IBOR Fallbacks Protocol.

"While fallbacks aren't designed to be a primary means of transitioning from Libor and other IBORs, they do mean a critical safety net will be in place for those participants that still have exposure to IBORs when a cessation or non-representativeness announcement is made," ISDA General Counsel Katherine Tew Darras said in a speech Monday.

ISDA said the supplement amends its standard definitions for interest rate derivatives to incorporate robust fallbacks for derivatives linked to certain IBORs, with the changes coming into effect on January 25, 2021. From that date, all new cleared and non-cleared derivatives that reference the definitions will include the fallbacks.

"During this period the fee is free for non-primary dealers," said Harris. "After January 25, new transactions will automatically contain the fallback language via the supplement. However, adherence to the protocol after January 25 for legacy contracts will incur the $500 fee. To avoid the fee, issuers can also execute bilateral amendments."

The $500 fee applies to each legal entity unless they have agency authority.

Additionally, ISDA said the protocol will enable market participants to incorporate the revisions into their legacy non-cleared derivatives trades with other counterparties that choose to adhere to the protocol. The protocol has been open for adherence since the Oct. 23 date of the announcement and also becomes effective on Jan. 25 with the supplement.

By the end of next month, the United Kingdom's Financial Conduct Authority is expected to officially declare Libor as nonrepresentative, which will establish an endpoint for this reference rate.

Harris said the endpoint will be used as a reference date for establishing a five-year lookback for a new reference rate.

"The announcement date will determine the five-year median window for purposes of calculating the fallback rate spread adjustment," Harris said. "The spread adjustment is based on the median five-year historical difference between LIBOR and SOFR compounded over each corresponding period."

Harris said GFOA is likely to advise issuers to consult with their swap advisor or qualified independent representative (QIR) to help them navigate that transition.

Harris said she intends to have her swap advisor perform a historical five-year regression of the Secured Overnight Financing Rate (SOFR) plus the spread for Libor and a separate calculation using the SIFMA rate as an alternative.

"GFOA will ramp up its effort to get the word out about Libor," she said. "The industry will also try to get together some guiding principles and not create new resources, but to aggregate them."

The group also wants to make the resources understandable to issuers who may only have used Libor occasionally and aren't familiar with the terminology.

In addition, the GFOA debt committee has a subgroup that reviewing GFOA's best practices to determine is any updates are needed.

By Brian Tumulty

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