September 2020

Statement on behalf of the Working Group on Sterling Risk-Free Reference Rates – Recommendation of Credit Adjustment Spread Methodology for fallbacks in cash market products referencing GBP LIBOR[1]

In a statement in response to the coronavirus pandemic on 25 March 2020, the Working Group on Sterling Risk-Free Reference Rates (the "**Working Group**"), the Financial Conduct Authority and the Bank of England said: "The central assumption that firms cannot rely on LIBOR being published after the end of 2021 has not changed and end-2021 should remain the target date for all firms to meet. The transition from LIBOR remains an essential task that will strengthen the global financial system."

A further statement on 29 April 2020 said that the Working Group, the Financial Conduct Authority and the Bank of England would support the delivery of the Working Group workplan in key areas that will continue the momentum on LIBOR transition. This includes building on the strong consensus on how to calculate a fair credit adjustment spread methodology in legacy cash products (including, but not limited to, floating rate notes, covered bonds, capital securities, securitisations, structured products, syndicated loans, retail loans and bilateral loans), to assist transition from LIBOR in cash markets.

The Summary of Responses to the Working Group's Consultation on credit adjustment spread methodologies for fallbacks in cash products referencing GBP LIBOR (the "**Consultation**") identified a strong consensus in favour of the historical five-year median spread adjustment methodology (referred to in the Consultation as the "ISDA historical median approach") as the preferred methodology for credit adjustment spread calculations across both cessation and pre-cessation triggers[2] for cash products maturing beyond end-2021.

In light of this, the Working Group recommends the use of the historical five-year median spread adjustment methodology when calculating the credit adjustment spread which should then be applied to any relevant Sterling Overnight Index Average ("**SONIA**") rate chosen or recommended to replace GBP LIBOR pursuant to contractual fallback and replacement of screen rate provisions following a permanent cessation or pre-cessation trigger in relation to GBP LIBOR.

The Working Group will monitor the availability of data sources to support use of this spread adjustment methodology for use in cash products and consider whether any further work is needed in this area in due course.

The Working Group's recommended credit adjustment spread methodology to produce spread adjustments is solely intended for GBP LIBOR contracts that contain contractual fallbacks and replacement of screen rate provisions which result in the selection of a spread-adjusted SONIA rate as a fallback.[3]

If market participants whose contractual fallbacks result in the selection of an alternative rate (being a rate other than a spread-adjusted SONIA rate) choose to use the historical five-year median spread adjustment methodology, they would need to take account of any differences between SONIA and that alternative rate when determining an appropriate credit adjustment spread.

[1] The overall objective of the Working Group on Sterling Risk-Free Reference Rates (the "**Working Group**") is to catalyse a broad-based transition to SONIA by the end of 2021 across the sterling bond, loan and derivative markets, in order to reduce the financial stability risks arising from widespread reliance on GBP LIBOR. The Bank of England and the Financial Conduct Authority ("**FCA**") are each ex-officio members of the Working Group. The views and outputs set out herein do not constitute guidance or legal advice from the Bank of England (including the Prudential Regulation Authority ("**PRA**")) or the FCA and are not necessarily endorsed by the Bank of England (including the PRA) or the FCA.

[2] The timing of application of the relevant fallback will depend upon the drafting of the applicable contractual provisions for the relevant cash product. In this recommendation, cessation and pre-cessation triggers are as described in the Consultation and do not include any early opt-in fallback trigger, as defined in the Consultation.

[3] However, this recommendation does not affect parties' ability to agree alternative fallback provisions or credit adjustment spread methodologies if they choose to do so.