Department of Financial Services

ANDREW M. CUOMO
Governor

LINDA A. LACEWELL
Superintendent

December 23, 2019

Industry Letter: Request for Assurance of Preparedness for LIBOR Transition

To the CEO or the Equivalent of Regulated Institutions:

As you may know, the United Kingdom's Financial Conduct Authority announced in 2017 that it would no longer compel LIBOR panel banks to furnish data to support the determination of the reference rate known as the London Interbank Offered Rate (LIBOR) after 2021. As a result, LIBOR is unlikely to continue past the end of 2021. Efforts in the US to create reference rate alternatives are underway, as discussed below. Your institution should be carefully following these developments.

As regulated institutions are engaged in credit, derivatives, and securities transactions that are linked to LIBOR, its cessation will have a significant impact on such institutions as well as the broader market. LIBOR has been a widely used reference rate since 1986. It has been estimated in the U.S. alone that the gross notional value of all financial products linked to U.S. dollar LIBOR is approximately $200 trillion (about 10x U.S. GDP); this comprises $3.4 trillion of business loans, $1.8 trillion of floating rate notes and bonds, $1.8 trillion of securitizations, $1.3 trillion of consumer loans (held by about four million retail consumers) and $1.2 trillion of residential mortgage loans. The remaining 95% of exposures are in derivative contracts, notably interest rate swaps.

Therefore, financial institutions that have LIBOR exposures on the asset or liability side of their balance sheets need to be prepared for this event. Prudent risk management requires that all regulated institutions with exposure to LIBOR fully understand its cessation and transition risks, and the implications for them and their customers and counterparties. Inadequate preparation for transition to alternative rates could have an adverse impact on the safety and soundness of regulated institutions and may cause harm to consumers and markets. Such transition requires a significant amount of work, which should have already commenced.

The New York State Department of Financial Services (Department) understands that there are a large number of commercial loans that are expected to mature or be renegotiated or amended before 2021. As such, they may be converted to an alternative rate and/or incorporate fallback language provisions identifying triggers for introducing new rates prior to the discontinuation of LIBOR.

Similarly, there are a large number of OTC derivatives transactions that are short term and mature prior to the likely cessation of LIBOR. However, for those that extend beyond 2021, they may be amended to incorporate new rates and/or fallback language provisions potentially through a protocol that the International Swaps and Derivatives Association (ISDA) may put in place.

Additionally, the Department understands that the documentation relating to LIBOR-based residential mortgage loans typically provides the lender with the option to choose a comparable rate if LIBOR ceases to exist. However, it should be noted that changing the interest rate basis of any consumer loan presents various risks, such as legal, reputational and operational risks, that need to be carefully considered and managed.

There are also a significant number of notes, securitization products, and other instruments that are linked to LIBOR. Many of these instruments may have no successor rate provisions or may convert to fixed rate instruments, which may also present valuation, portfolio matching concerns and monitoring issues.

The Board of Governors of the Federal Reserve (FRB), and the Federal Reserve Bank of New York (FRBNY), in conjunction with the U.S. Treasury Department's Office of Financial Research, have created a new rate called the Secured Overnight Financing Rate (SOFR), which the FRBNY has been publishing since April 2018. SOFR measures the cost of overnight borrowings through repo transactions collateralized with U. S. Treasuries. After evaluating a range of possible alternative rates, the Alternative Reference Rates Committee (ARRC), convened by the FRB and the FRBNY, has chosen SOFR as its recommended alternative to U.S. dollar LIBOR and continues to work through transition issues and provides guidance on the process.

As stated above, the likely cessation of LIBOR by the end of 2021 poses significant risks if not appropriately managed. Therefore, the Department is issuing this letter to seek assurance that regulated institutions' boards of directors, or the equivalent governing authorities, and senior management fully understand and have assessed the risks associated with LIBOR cessation, have developed an appropriate plan to manage them and have initiated actions to facilitate transition.

To that end, the Department requires that each regulated institution submit a response to the Department describing the institution's plan to address its LIBOR cessation and transition risk. The plan should describe (1) programs that would identify, measure, monitor and manage all financial and non-financial risks of transition, (2) processes for analyzing and assessing alternative rates, and the potential associated benefits and risks of such rates both for the institution and its customers and counterparties, (3) processes for communications with customers and counterparties, (4) a process and plan for operational readiness, including related accounting, tax and reporting aspects of such transition, and (5) the governance framework, including oversight by the board of directors, or the equivalent governing authority, of the regulated institutions.

Responses are to be provided to the Department by February 7, 2020.

Please submit your response to the designated email address for your category of institution:

- Depository Institutions (including banks, credit unions and savings associations): depository@dfs.ny.gov

- Non-Depository Institutions (including licensed lenders, sales finance companies and premium finance companies, mortgage companies, money transmitters and virtual currency companies): non-depository@dfs.ny.gov

- Property Insurance Companies: DFS.Property-Casualty.Letters@dfs.ny.gov

- Health Insurance Companies Healthbureaulibor@dfs.ny.gov

- Life Insurance Companies and Pension Funds SpecialReport@dfs.ny.gov

Sincerely,

Linda A. Lacewell, Superintendent
New York State Department of Financial Services