

June 30, 2020

ARRC Announces Further Details Regarding Its Recommendation of Spread Adjustments for Cash Products

At its June meeting, after reviewing responses to its [supplemental consultation on spread adjustments](#), the Alternative Reference Rates Committee (ARRC) decided on two further technical details related to its recommended spread adjustments for cash products referencing U.S. dollar (USD) LIBOR. The ARRC's recommended methodology is for market participants' voluntary use, to produce spread adjustments intended for USD LIBOR contracts that have incorporated the ARRC's recommended hardwired fallback language, or for legacy USD LIBOR contracts where a spread-adjusted Secured Overnight Financing Rate (SOFR) can be selected as a fallback.

Following its consideration of feedback received on its initial public consultation, the ARRC recommended a spread adjustment methodology based on a historical median over a five-year lookback period calculating the difference between USD LIBOR and SOFR. The five-year median spread adjustment methodology matches the methodology recommended by the International Swaps and Derivatives Association (ISDA) for derivatives. For consumer products, reflecting support from both consumer advocacy groups and mortgage lenders responding to the consultation, the ARRC additionally recommended a 1-year transition period to this five-year median spread adjustment methodology.

The ARRC subsequently issued a supplemental consultation seeking feedback on further technical details related to its spread adjustment recommendations. The supplemental consultation invited participants to consider the option to use the same spread adjustment values that will be used by ISDA across all of the different fallback rates, rather than using the same adjustment methodology to calculate a different spread adjustment for each potential fallback rate. The supplemental consultation also sought views on whether the timing of the calculation of the ARRC's spread adjustment should match ISDA's timing if a pre-cessation event is operative.

The ARRC received 49 responses to its supplemental consultation from a mix of banks, government-sponsored entities, asset managers, insurance companies, and industry associations. Responses were broadly similar across these industry types. A clear majority of respondents to the consultation favored a recommendation of the same spread adjustment values as ISDA and respondents were unanimous that the timing of the ARRC recommendation on spread adjustments should align with timing of the ISDA spread adjustment. Respondents providing an explanation for their views generally cited the importance of consistency with ISDA values from a hedging perspective.

In light of this feedback, the ARRC has determined that it will implement its spread methodology recommendations as follows:

- For cash products other than consumer products, the ARRC's recommended spread adjustment will match the value of ISDA's spread adjustments to U.S. dollar LIBOR. Given the special considerations due to consumer products and that the ARRC will include a 1-year transition period as part of its recommended spread adjustments for consumer products, the ARRC will

ALTERNATIVE REFERENCE RATES COMMITTEE

further consider the most appropriate approach to the issue of methodology versus value for these specific products.

- For all cash products, in the event that a pre-cessation event is operative, the ARRC's recommended 5-year historical median spread adjustments will be determined at the same time as the ISDA's spread adjustments, which will be at the time of any announcement that LIBOR will or has ceased or will or has become no longer representative.

"Today's announcement of further details of the ARRC's recommended spread adjustments demonstrates that the ARRC is committed to providing clarity, and the responses to our consultations again show the high value that market participants place on ensuring consistent outcomes across cash and derivatives products," said Tom Wipf, ARRC Chair and Vice Chairman of Institutional Securities at Morgan Stanley.

The ARRC has committed to making sure its recommended spread adjustments and the resulting spread-adjusted rates are published and will work with potential vendors to make sure that these spreads and spread-adjusted rates are made publicly available. As the ARRC works to identify a vendor who will publish these spreads and rates, it will release further technical details related to them.

About the ARRC

The ARRC is a group of private-market participants convened by the Federal Reserve Board and Federal Reserve Bank of New York in cooperation with the Consumer Financial Protection Bureau, the Federal Deposit Insurance Corporation, the Federal Housing Finance Agency, the Office of Financial Research, the Office of the Comptroller of the Currency, the Commodity Futures Trading Commission, the Securities and Exchange Commission and the U.S. Treasury Department. It was initially convened in 2014 to identify risk-free alternative reference rates for USD LIBOR, identify best practices for contract robustness, and create an implementation plan with metrics of success and a timeline to support an orderly adoption. The ARRC accomplished its first set of objectives and identified the SOFR as the rate that represents best practice for use in certain new USD derivatives and other financial contracts. It also published its [Paced Transition Plan](#), with specific steps and timelines designed to encourage adoption of the SOFR. The ARRC was reconstituted in 2018 with an expanded membership to help to ensure the successful implementation of the Paced Transition Plan, address the increased risk that LIBOR may not exist beyond 2021, and serve as a forum to coordinate and track planning across cash and derivatives products and market participants currently using USD LIBOR.

Sign up [here](#) to receive email updates about the ARRC.

Contact for ARRC Chair Tom Wipf

[Paige Mandy](#)

Morgan Stanley

Contact for the ARRC's Outreach/Communications Working Group

[Andrew S. Gray](#)

JPMorgan Chase

Contact for the Federal Reserve Board

[Darren Gersh](#)

Contacts for the Federal Reserve Bank of New York

[Suzanne Elio](#) and [Betsy Bourassa](#)