Our approach to LIBOR transition

Helping businesses understand how we are dealing with the phasing out of LIBOR

By the side of business

LLOYDS BANK

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Introduction

On 5 March 2021 the end dates for LIBOR were announced by the Financial Conduct Authority.

This was an important step and we now have greater certainty on the cessation of LIBOR. For more details see the section on The end of LIBOR.

The Bank of England-initiated Working Group on Sterling Risk-Free Reference Rates (Sterling Working Group) has set out milestones for banks to stop selling GBP LIBOR-based products. We now only offer SONIA or Bank of England Bank Rate (also known as Base Rate) for new GBP lending or derivatives that mature after end-2021.

The next key milestone is **end-Q3 2021** to complete the conversion of existing GBP LIBOR contracts expiring after end-2021, where active conversion is viable.

If we haven't been in touch already, we will contact you shortly to discuss how you wish to manage your affected LIBOR agreements with us. If you have syndicated lending we suggest you contact the agent bank as soon as possible to initiate discussions with the syndicate of lenders. Alternatively, you can contact your relationship manager for more information about the process.

You should think about how your business could be impacted by LIBOR cessation. You may need to update your systems, for example to deal with interest payments not being known until near the end of an interest period.

You may also have commercial contracts which reference LIBOR that need to be amended.

You should also consider obtaining independent advice on LIBOR transition, including on the financial, tax, regulatory, accounting and legal implications.

We hope you find this report useful.

If you have any questions or need help please do not hesitate to get in touch with your relationship manager.

We continue to support clients affected by the pandemic and you can visit our COVID-19 website for more information.

Best wishes,
Scott Barton and Paul Gordon

SCOTT BARTON
Managing Director,
Corporate and Institutional Coverage
Lloyds Bank Commercial Banking

PAUL GORDON
Managing Director,
SME & Mid Corporates
Lloyds Bank Commercial Banking

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The next RFR Working Group milestone for progress on [conversion of legacy contracts] in sterling markets is end-Q3. That is less than 3 months away.

The end-Q3 date is there for a good reason. It will help avoid risks of getting caught in a pre-Christmas rush – where we could see a squeeze in IT, legal or other resources, or would simply have too little time to adjust to unexpected hurdles."

Edwin Schooling Latter

Director of Markets and Wholesale Policy

FCA

5 July 2021

Key messages

1 The FCA confirmed the end dates for LIBOR in March

2 We are continuing to contact clients with affected bilateral products to discuss options for transition

3 You should think about how your own processes and systems are impacted by the end of LIBOR

The end of LIBOR

The end of LIBOR

WHY IS LIBOR BEING PHASED OUT?

The LIBOR methodology was designed to produce an average rate that is representative of the rates at which large, leading internationally active banks with access to the wholesale, unsecured funding market could fund themselves[1]. Since the global financial crisis banks no longer fund themselves in this way. The decline in the underlying market means that LIBOR is now primarily sustained by the use of expert judgement.

In the UK the Sterling Working Group has been tasked with facilitating transition away from GBP LIBOR to alternative reference rates, including near risk-free rates (RFRs). Similar working groups have been set up around the world to facilitate similar transition in those jurisdictions. Lloyds Banking Group is a member of the Sterling Working Group and a number of other official sector sub-groups.

LIBOR END DATES CONFIRMED

On 5 March 2021 the Financial Conduct Authority (FCA) announced that all LIBOR settings will either cease to be provided by any administrator or no longer be representative from the following dates:

Immediately after **31 December 2021**	**All settings:** – British pound – Euro – Swiss franc – Japanese yen **1-week and 2-month:** – US dollar
Immediately after **30 June 2023**	– US dollar; all remaining settings

"No longer representative" or "non-representative" means that LIBOR will no longer be representative of the market it seeks to represent. The FCA has said they expect this could lead to significantly reduced appetite for LIBOR-referencing instruments, potential issues with EU-supervised firms entering into or even holding LIBOR transactions, and central clearing difficulties, amongst other issues.

In their announcement they have advised that they do not expect any LIBOR settings to become unrepresentative before the dates set out on this page.

1 https://www.theice.com/publicdocs/ICE_LIBOR_Methodology.pdf

SPREAD ADJUSTMENTS

The International Swaps and Derivatives Association (ISDA) has confirmed that the FCA's announcement constituted an index cessation event for all LIBOR settings. As a result the credit adjustment spreads to be used in its IBOR fallbacks, which are calculated using the 5-Year Historic Median (5YHM), are now fixed for all sterling, euro, Swiss franc, US dollar and Japanese yen LIBOR settings. ISDA has selected Bloomberg to publish these spread adjustments and the full list is available here.

SYNTHETIC LIBOR AND TOUGH LEGACY

In addition, in their announcement the FCA said it will consult on requiring the continued publication of a small number of LIBOR settings, being 1, 3 and 6-month sterling and yen LIBOR, on a non-representative, 'synthetic' basis. This is required because authorities recognise that there is a very limited group of contracts that genuinely have no or inappropriate alternatives and no realistic ability to be renegotiated or amended, often known as 'tough legacy'.

The FCA consultation on how it proposes to use its powers over use of critical benchmarks closed on 17 June 2021. A consultation on how the applicable LIBOR settings are determined closes on 27 August 2021. A further consultation will be launched in Q3 on what legacy use to allow for any synthetic LIBOR. Final results are not expected until Q4 2021. In April 2021 the UK government enacted the Financial Services Act 2021 which granted the FCA the power it needs to effect these changes.

The FCA has been clear that any synthetic LIBOR setting will not be considered representative and will not be permitted for use in new contracts. It is intended for use in tough legacy contracts only. They have also made it clear that synthetic LIBOR will be a temporary solution, and that active transition is the best way for parties to achieve a contractually certain outcome.

INTERIM MILESTONES

The Sterling Working Group has issued a series of interim milestones, including:

End-Q1 2021
Banks to stop selling **GBP LIBOR**-linked loans, bonds, securitisations and linear derivatives, where expiry is after end-2021, except for the risk management of existing positions. Linear derivatives include interest rate swaps and basis swaps.

End-Q2 2021
Banks to stop entering into **GBP LIBOR**-linked non-linear derivatives that expire after end-2021, except for risk management of existing positions. Non-linear derivatives include interest rate caps, interest rate floors, swaptions and constant maturity swaps.

End-Q3 2021
Conversion of legacy **GBP LIBOR** contracts expiring after end-21 to be completed (where active conversion is viable). Note that "conversion" means making changes to the contract. The switch to the new rate may take place later, for example on or after 1 January 2022.

In the US the Federal Reserve, with other supervisory bodies, has confirmed the following milestone:

End-Q4 2021
Latest date for banks to cease issuing new **USD LIBOR** contracts.

What are the alternative rates?

What are the alternative rates?

Currency	**LIBOR**	**RFR recommendation** *from relevant working group*	**Administrator**	**Description**
British Pound	GBP LIBOR	**SONIA** (Sterling Overnight Index Average)	Bank of England (BoE)	Unsecured overnight rate calculated by the BoE from reported eligible transactions. Reformed SONIA has been published since April 2018.
Euro	EUR LIBOR	**€STR** (Euro Short Term Rate)	European Central Bank	Reflects wholesale euro unsecured overnight borrowing costs of euro area banks. Published since October 2019.
US Dollar	USD LIBOR	**SOFR** (Secured Overnight Financing Rate)	Federal Reserve Bank of New York	A broad-based secured US Treasuries repo financing rate. It has been published since April 2018.
Swiss Franc	CHF LIBOR	**SARON** (Swiss Average Rate Overnight)	SIX Swiss Exchange	References the Swiss franc repo market (i.e. secured). Published since August 2009.
Japanese Yen	JPY LIBOR	**TONA** (Tokyo Overnight Average Rate)	Bank of Japan	A measure of the cost of borrowing in the Japanese yen unsecured overnight money market. Also known as TONAR. Published since 2016.

These alternative rates are near risk-free rates, known as Risk-Free Rates (RFRs). Other options for alternative rates may include, in the UK, the Bank of England Bank Rate for sterling products, or a fixed rate. Bank Rate is an example of a central bank rate. In the context of LIBOR cessation, RFRs and relevant central bank rates are collectively called Alternative Reference Rates (ARRs). ARRs are materially different from LIBOR and are calculated using different methodologies. As such they are not direct replacements for LIBOR.

There are a number of other inter-bank offered rates (IBORs) affected by these changes. These include:

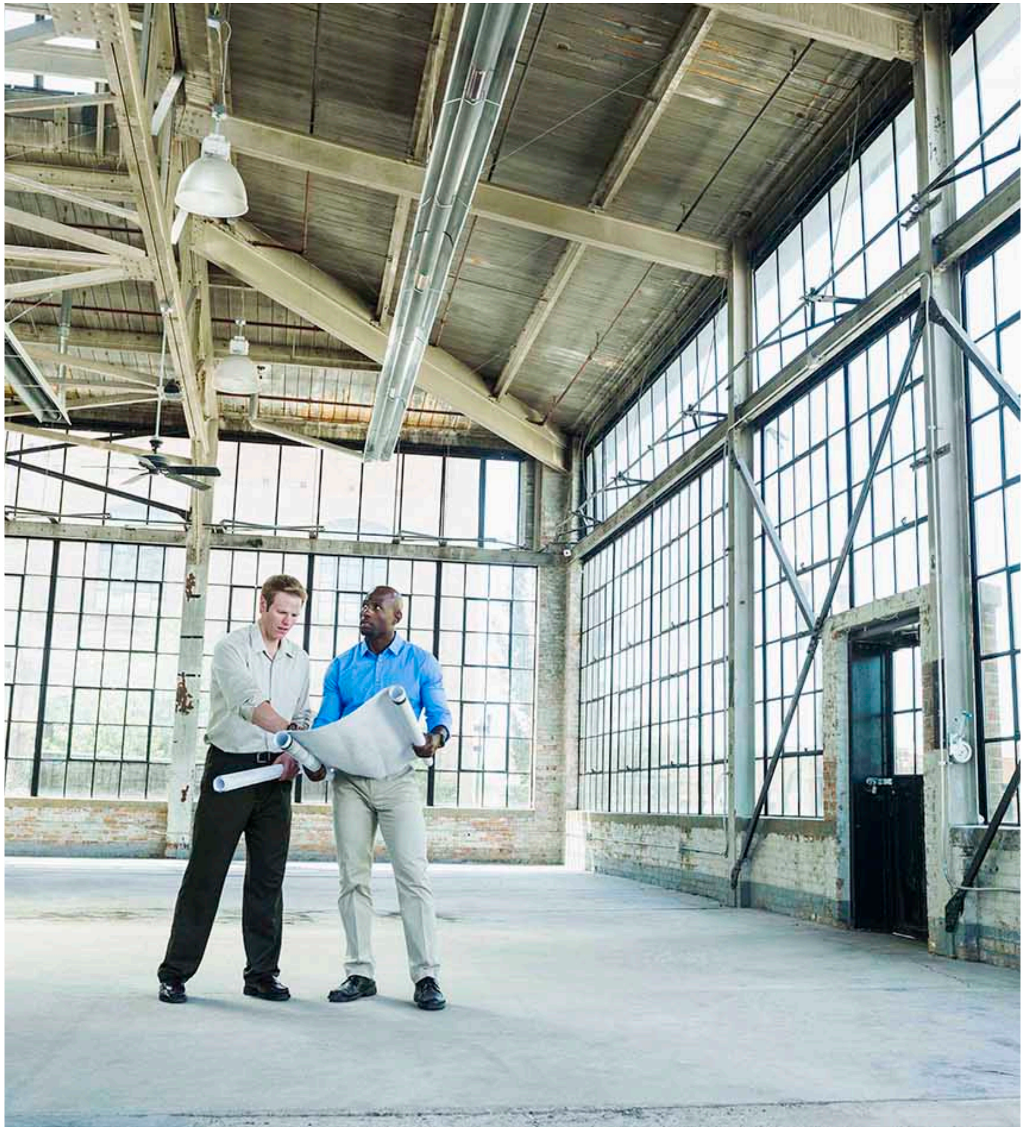
EURIBOR (Euro Interbank Offered Rate) has been reformed to comply with the EU Benchmark Regulation and there are no current plans to discontinue it. However, you should be aware that cash fallbacks might need to be strengthened in light of regulatory guidance and some products may transfer to other Euro rates.

EONIA (Euro Overnight Index Average) has been reformed and since 2 October 2019 has been quoted as €STR plus a fixed spread of 8.5 basis points and published on a T+1 basis. It is scheduled to be discontinued from 3 January 2022.

TIBOR (Tokyo Interbank Offered Rate) has been reformed and will continue to exist alongside TONA.

The main differences between LIBOR and RFRs are:

- LIBOR rates are forward-looking for certain identified terms (e.g. 1 month, 3 months), RFRs are point in time overnight rates.
- LIBOR prices in term risk and bank credit risk whereas the RFRs do not.
- RFR interest payable over a period is typically calculated by daily compounding a series of overnight rates with the interest due being calculated at the end of the relevant interest period, rather than at the beginning.
- These changes may have an impact on systems, operations and payments.



Things to know

Things to know

Here are some potential risks and impacts to be aware of:

NEW LIBOR PRODUCTS

- Our range of LIBOR products will be affected by interim milestones from the official sector, and availability will cease in accordance with the applicable guidance.
- Any LIBOR products taken out now that mature after the announced cessation dates may contain provisions to facilitate transition to alternative reference rates, including fallbacks that cater for the cessation of LIBOR or it being declared non-representative. However, you should be aware that changes to documents may still be required to effect transition. Differences between products may remain, leading to unintended mismatches, for example between loans and related interest rate hedging instruments. Some of the advisory costs you incur when you take out a new LIBOR product may be duplicated when the product transitions to an alternative reference rate.

EXISTING LIBOR PRODUCTS

- Existing documents may contain fallback provisions to deal with the non-availability of affected reference rates. However, these fallback provisions may not cater for the permanent cessation of LIBOR or it being declared non-representative. They may also differ across financial products which may lead to unintended mismatches, for example between loans and related interest rate hedging instruments.
- Existing documents are likely to need changing to replace affected reference rates with alternative reference rates and to update fallback provisions.
- Alternative reference rates do not include a measure of term risk or bank credit risk. As a result, when products are transitioned to these rates a spread adjustment will be applied to account for this. This adjustment is referred to as the credit adjustment spread (CAS) and there are different methodologies for its calculation. You can read more about CAS in the LIBOR Transition FAQs on our website.

ALL LIBOR PRODUCTS

- Alternative reference rates are materially different from LIBOR and are calculated using different methodologies. Methodologies and market conventions can vary within and across different markets. Transition activity is taking place at different speeds across products, markets and currencies.
- Execution costs can apply when transitioning derivative products. Execution costs vary depending on market liquidity of the alternative reference rate and other factors. As an example, execution costs of a Bank of England Bank Rate hedging instrument, such as a swap, are typically higher than a comparable SONIA instrument.
- Contracts that reference LIBOR may not perform as expected when LIBOR ends, and possibly even before that. For example, liquidity in LIBOR-referencing instruments may decline ahead of its discontinuation. A reduction in liquidity may negatively impact the value and transferability of any LIBOR contract.
- You may need to review aspects of your own business such as systems, accounting, regulatory matters, and potential effects on future liquidity and hedging.

WHAT ARE FALLBACKS?

Fallbacks are contractual terms that specify what happens if a relevant party is not able to look up, use or determine the specified reference rate, such as LIBOR, for a relevant period. The reference rate might be unavailable for a number of reasons. Fallbacks have traditionally catered for temporary or short-term unavailability of a reference rate but now need to cater for longer term issues, such as cessation. New fallbacks are intended to be more robust and provide more certainty about what happens when LIBOR ends.

For derivative products, in October 2020 the International Swaps and Derivatives Association (ISDA) launched the IBOR Fallbacks Supplement to the 2006 ISDA Definitions and the ISDA IBOR Fallbacks Protocol.

Lloyds Bank and other Lloyds Banking Group entities have adhered to both the ISDA IBOR Fallbacks Protocol and the ISDA Benchmark Supplement Protocol. ISDA has published a list of protocol-adhering entities, which is available under the "Protocols" section of their website.

ISDA confirmed that the FCA announcement on 5 March 2021 constituted an index cessation event for all LIBOR settings. As a result the credit adjustment spreads to be used in its IBOR fallbacks, which are calculated using the 5-Year Historic Median (5YHM), are now fixed for all sterling, euro, Swiss franc, US dollar and Japanese yen LIBOR settings. ISDA has selected Bloomberg to publish these spread adjustments and the full list is available here.

LLOYDS BANK

Our approach to LIBOR transition

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KEEPING YOU INFORMED

What: Your relationship manager will provide you with tailored support and general information, updated regularly, is available through our newsletters and website.

How:

- We sent a **disclosure notice** to affected clients informing them of the changes.
- Our regular **IBOR Transition Newsletter** aims to provide a high-level insight into latest market developments in the UK and globally. If you would like to be added to the mailing list please let your relationship manager know.
- Our website has newsletters, FAQs and other useful resources.

NEW PRODUCTS

What: We will talk to you about alternative reference rate products when discussing new business with you. Alternative reference rates and LIBOR typically vary daily, and we cannot guarantee that a product based on an alternative reference rate would not cost more than a LIBOR product or vice versa. Note that some products may not be available with an alternative reference rate and could be discontinued.

How: We are also making changes to the way some products operate so that they are compatible with the way some alternative reference rates function. We will be making updates to some of our systems and you may need to update your own systems as well. We offer a range of products based on the alternative rates and continue to increase our offering.

MOVING EXISTING PRODUCTS

What: For bilateral products such as lending and derivatives, if we haven't been in touch already we will contact you shortly to discuss how you wish to manage your affected LIBOR agreements.

For syndicated lending we suggest you contact the agent bank as soon as possible to initiate discussions with the syndicate of lenders. We are in the process of sending a syndicated lending transition guide to our borrowers – if you have not received this yet you can contact your relationship manager.

How: For bilateral products we will set up a meeting to discuss the options available to you to deal with your affected LIBOR agreements. We will then work with you to implement your chosen option.

For syndicated lending, in our role as a lender we can offer support by providing detailed information, discussing options and answering questions. However, you will need to agree the transition approach and terms with all the lenders in the syndicate, subject to the voting thresholds laid out in the facility documentation.

> **"The need to transition is clear. The economic terms of fair transition have been worked out, they stretch across markets and across jurisdictions."**

Edwin Schooling Latter

Director of Markets and Wholesale Policy

FCA

26 January 2021

New products

New products

Lending – For new lending we offer alternatives to GBP, USD, EUR, CHF and JPY LIBOR. These include SONIA, SOFR, EURIBOR, €STR, SARON, TIBOR, TONA and BoE Bank Rate. These rates can be used in Loans, including Revolving Credit Facilities, either single or multi-currency. For RFR lending products we use the compounded RFR in arrears with a lookback period, typically 5 days.

SONIA and SOFR indexes are published by the Bank of England and the New York Fed respectively. They could simplify compounding calculations, but the extent of their use is still to be determined by the market.

Due to an interim milestone from the Sterling Working Group, from 1 April 2021 we stopped entering into GBP LIBOR loans with maturity after end-2021. The Sterling Working Group has published two papers to support market participants with SONIA lending; 'Best Practice Guide for GBP Loans' and 'GBP loan market Q&A'.

Transaction Banking – We offer sterling working capital products based on compounded SONIA, as well as Bank Rate and fixed rates. New products in other currencies are being developed.

Turning to EURIBOR, which was reformed in 2019, we expect most products to continue as they do today - there are currently no plans to discontinue this rate. However, you should be aware that cash fallbacks might need to be strengthened in light of regulatory guidance and some products may transfer to other Euro rates.

Some trade finance products, such as supply chain finance, receivables purchasing and discounted letters of credit, work by discounting future cashflows.

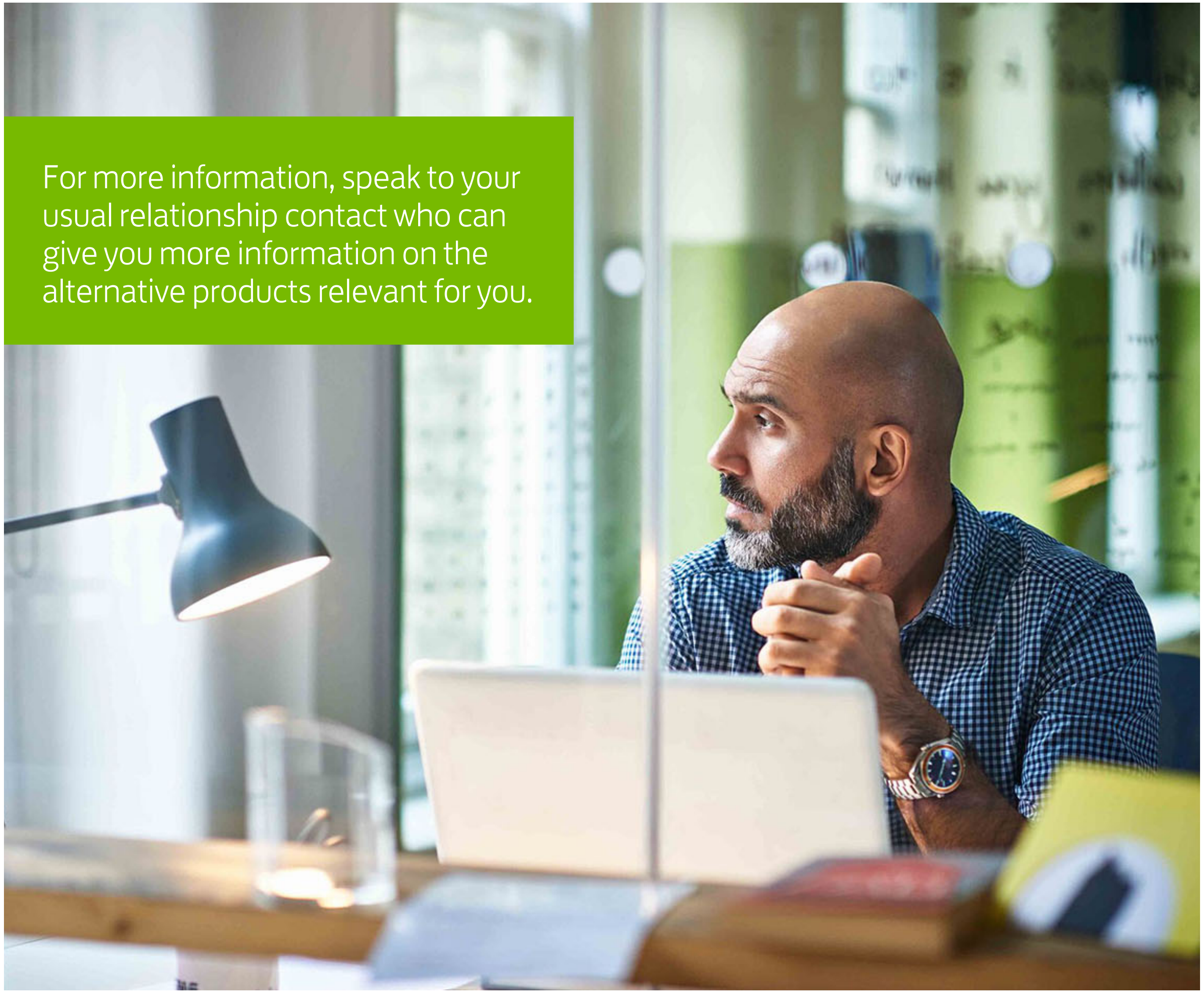
In the UK the Sterling Working Group identified these products as being able to use a Term SONIA rate, and we are aligning to this approach.

Term SONIA rates are now being published, and we launched Term SONIA trade finance products in Q2 2021. Trade finance products are normally short-term so we are still seeing some continued use of LIBOR during this transition period.

Markets – The SONIA derivatives market is already well-developed. In the SONIA cash market floating rate bonds and securitisations using compounding in arrears methodology are well established, although market conventions continue to evolve.

The SONIA swap market is increasingly liquid and is growing following the guidance from the BoE and FCA that market makers should change the convention for standard interbank sterling interest rate swaps from LIBOR to SONIA from October 2020. In the USD markets a similar initiative, called "SOFR First", came into effect from 26 July 2021.

We continue to increase our range of RFR-linked products across all LIBOR currencies, and plan to launch new products throughout 2021.



For more information, speak to your usual relationship contact who can give you more information on the alternative products relevant for you.

What can you do to make sure you are ready?

What can you do to make sure you are ready?

Keep up to date

- Understand the latest transition developments. The websites of the Sterling Working Group, the FCA, the US Alternative Reference Rates Committee and ISDA are good sources of information.
- Talk to your bankers and legal & financial advisers.
- Familiarise yourself with SONIA, SOFR and any other rates relevant to you, and how interest is calculated.
- Get involved through industry bodies (e.g. ACT, LMA, LSTA) and participate in working groups where possible.

Identify your LIBOR exposures

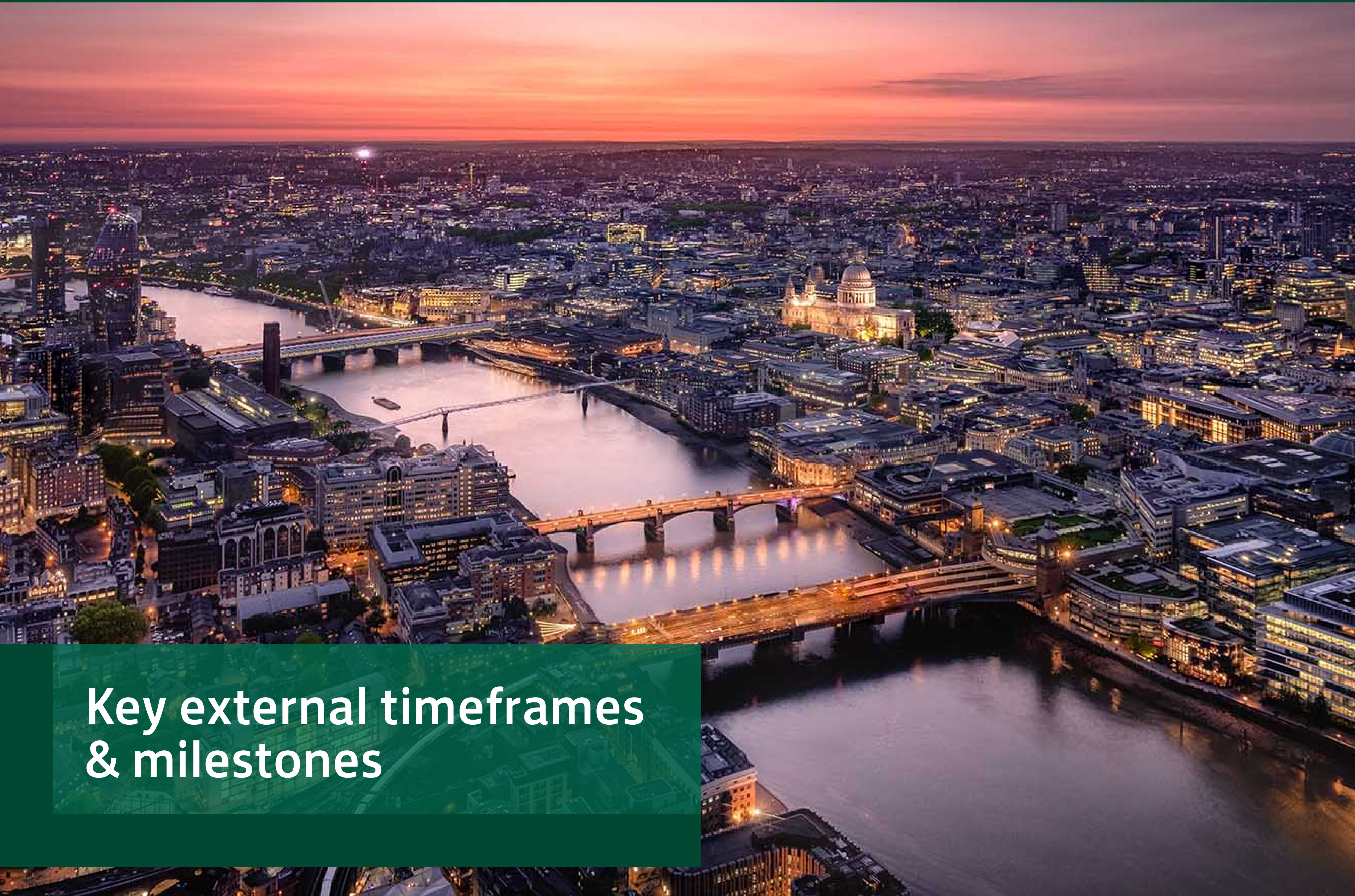
- Develop an inventory of all your transactions affected by LIBOR. Some exposures may be obvious such as floating rate loans, interest rate swaps; some less so such as intra-group agreements, working capital arrangements, etc.
- Identify which counterparties are involved – banks, investors, commercial counterparties, group entities.

Understand how transition could affect your products

- Review your existing contracts to understand where LIBOR is referenced and whether there are fallback provisions in place setting out what will happen when LIBOR is no longer available.
- Consider whether fallbacks across linked products are consistent where they are intended to match, and whether other provisions may be affected by transition away from LIBOR.
- For derivative products, consider whether signing the ISDA IBOR Fallbacks Protocol, or entering into a similar bilateral agreement, would be appropriate for you.
- Determine the expected outcomes of LIBOR transition for each group of transactions and consider the risks and impacts of not taking action.
- Understand how your systems, processes, operations, valuations, tax, and accounting may be affected.

Review and implement

- Consider which contracts might need to be amended either to replace LIBOR or to confirm the steps to be taken when LIBOR is no longer available.
- New transactions: can you use an alternative reference rate from the start, or if not, can you include a conversion mechanism where this is still permitted?
- Review and keep your plans updated: finalise actions, determine resource requirements, engage external advisers/ vendors if needed.



Key external timeframes & milestones

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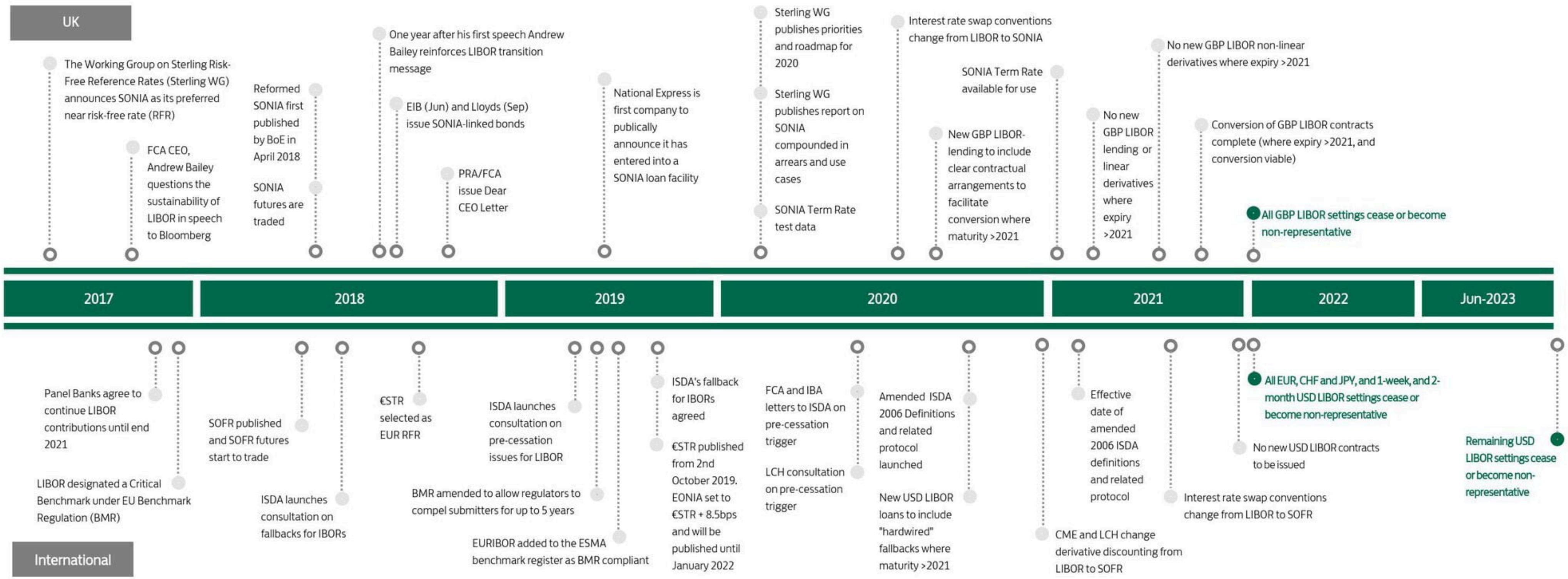

Source: Lloyds Bank, 4 August 2021

Glossary

Glossary

ACT	Association of Corporate Treasurers
ARRC	Alternative Reference Rates Committee
BoE	Bank of England
EMEAP	Executives' Meeting of East Asia-Pacific Central Banks
EMMI	European Money Markets Institute
EONIA	Euro Overnight Index Average
€STR	Euro Short Term Rate
EURIBOR	Euro Interbank Offered Rate
FCA	Financial Conduct Authority
FSB	Financial Stability Board
ISDA	International Swaps and Derivatives Association
LIBOR	London Interbank Offered Rate
LMA	Loan Market Association
New York Fed	Federal Reserve Bank of New York
PRA	Prudential Regulation Authority
RFR	Near risk-free rate
SARON	Swiss Average Rate Overnight
SOFR	Secured Overnight Financing Rate
SONIA	Sterling Overnight Index Average
TONA or TONAR	Tokyo Overnight Average Rate

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