



RISK ALERT

OFFICE OF COMPLIANCE INSPECTIONS AND EXAMINATIONS

June 18, 2020

Examination Initiative: LIBOR Transition Preparedness*

I. Introduction

LIBOR, formerly the London Interbank Offered Rate, is used extensively in the United States and globally as a “benchmark” or “reference rate” for various commercial and financial contracts, including corporate and municipal bonds and loans, floating rate mortgages, asset-backed securities, consumer loans, and interest rate swaps and other derivatives. The discontinuation of LIBOR, currently expected to occur after 2021, could have a significant impact on the financial markets and may present a material risk for certain market participants, including SEC-registered investment advisers, broker-dealers, investment companies, municipal advisors, transfer agents and clearing agencies (collectively, “registrants”).¹

Preparation for the transition away from LIBOR is essential for minimizing any potential adverse effects associated with LIBOR discontinuation. The risks associated with this discontinuation and transition will be exacerbated if the work necessary to effect an orderly transition to an alternative reference rate is not completed in a timely manner.² The Alternative Reference Rates Committee, as well as other working groups across the globe, are currently working on efforts to help ensure a successful transition from LIBOR.³

The Office of Compliance Inspections and Examinations (“OCIE”) identified registrant preparedness for the transition away from LIBOR as an examination program priority for FY 2020.⁴ Accordingly, OCIE intends to engage with registrants through examinations to assess their preparations for the expected discontinuation of LIBOR and the transition to an alternative reference rate. OCIE is issuing this Risk Alert to provide registrants with additional information about the scope and content of these examinations.

* This statement represents the views of the staff of the Office of Compliance Inspections and Examinations (“OCIE”). It is not a rule, regulation, or statement of the U.S. Securities and Exchange Commission (“Commission” or “SEC”). The Commission has neither approved nor disapproved of its content. This statement, like all staff guidance, has no legal force or effect: it does not alter or amend applicable law, and it creates no new or additional obligations for any person.

¹ See SEC Staff Statements from the Divisions of Corporation Finance, Investment Management and Trading and Markets, and the Office of the Chief Accountant, [Staff Statement on LIBOR Transition](#) (July 12, 2019).

² *Id.* Additional materials have discussed the risks associated with LIBOR discontinuation. See, e.g., speech by SEC Chairman Jay Clayton, [SEC Rulemaking Over the Past Year, the Road Ahead and Challenges Posed by Brexit, LIBOR Transition and Cybersecurity Risks](#) (December 6, 2018).

³ The ARRC’s membership comprises a broad set of private-market participants – including banks, asset managers, insurers, and industry trade organizations – and official sector ex-officio members, including the SEC.

⁴ See OCIE, [Examination Priorities for 2020](#).

II. Examinations

OCIE will conduct examinations of a variety of registrant types to assess their efforts to prepare for the expected discontinuation of LIBOR and their transition to alternative reference rates, if applicable. Among other things, OCIE will review whether and how the registrant has evaluated the potential impact of the LIBOR transition on the organization's: (i) business activities; (ii) operations; (iii) services; and (iv) customers, clients, and/or investors (collectively, "investors"). For example, OCIE will review the plans that registrants have developed and steps they have taken to prepare for the LIBOR discontinuation, including as applicable:

- The firm's and investors' exposure to LIBOR-linked contracts that extend past the current expected discontinuation date, including any fallback language incorporated into these contracts;
- The firm's operational readiness, including any enhancements or modifications to systems, controls, processes, and risk or valuation models associated with the transition to a new reference rate or benchmark;
- The firm's disclosures, representations, and/or reporting to investors regarding its efforts to address LIBOR discontinuation and the adoption of alternative reference rates;
- Identifying and addressing any potential conflicts of interest associated with the LIBOR discontinuation and the adoption of alternative reference rates; and
- Clients' efforts to replace LIBOR with an appropriate alternative reference rate.

OCIE is including as an Appendix to this Risk Alert the types of information and documents that may be used in these examinations.

III. Resources for Registrants to Aid with LIBOR Transition

OCIE encourages registrants and investment professionals to visit the AARC website ([here](#)) to receive updates about the latest transition-related developments and best practices. In addition, as indicated in previous SEC publications, OCIE welcomes a discussion of the transition and encourages the public to share information about the potential impact of the expected discontinuation of LIBOR via e-mail to LIBOR@sec.gov.

IV. Conclusion

These examinations are intended to help promote and facilitate an orderly discontinuation of LIBOR and transition to an alternative reference rate. The sample document request (Appendix A) is intended to help empower compliance professionals in the industry with questions and tools they may use to assess and assist with their organization's preparedness for the LIBOR discontinuation, regardless of whether they are included in OCIE's examinations.

This Risk Alert is intended to highlight for firms risks and issues that OCIE staff has identified. In addition, this Risk Alert describes factors that firms may consider to (i) assess their supervisory, compliance, and/or other risk management systems related to these risks, and (ii) make any changes, as may be appropriate, to address or strengthen such systems. These factors are not exhaustive, nor will they constitute a safe harbor. Other factors besides those described in this Risk Alert may be appropriate to consider, and some of the factors may not be applicable to a particular firm's business. While some of the factors discussed in this Risk Alert reflect existing regulatory requirements, they are not intended to alter such requirements. Moreover, future changes in laws or regulations may supersede some of the factors or issues raised here. The adequacy of supervisory, compliance, and other risk management systems can be determined only with reference to the profile of each specific firm and other facts and circumstances.

Appendix A

This document provides a sample list of requests for information that OCIE may use in conducting examinations of registered entities regarding their LIBOR discontinuation preparations.¹ OCIE has published this document as a resource for registered entities. This document should not be considered all-inclusive of the information that OCIE may review or specifically indicative of the validation and testing we may perform of a registrant's policies and procedures. Accordingly, OCIE will alter its requests for information, as well as potentially vary whether it asks for production of information in advance of an examination or review certain information onsite, as it considers the specific circumstances presented by each registrant.

1. Information regarding registrant's organizational structure and business lines, particularly regarding the individuals, positions, departments, and operations that may be impacted by discontinuation of LIBOR transition and transition to an alternative rate (collectively, the "LIBOR Transition").
2. Information regarding any individuals or groups (e.g., internal committees, working groups, or transition teams) assigned responsibility to oversee or manage the effects of the LIBOR Transition on the registrant, including information regarding the frequency of any meetings on this topic and whether minutes are kept.
3. The identity of any third parties registrant has utilized or plans to utilize to assess the impact of the LIBOR Transition on the firm or its clients, customers, or investors (collectively, "investors").
4. Documentation or descriptions of any analysis performed to identify contracts or obligations held and/or issued by registrant or its investors that may be affected by the LIBOR Transition and any remediation plans thereof.
5. Documentation or descriptions of any performance composites or performance advertising that use a benchmark that could potentially be affected by the LIBOR Transition and any remediation plans thereof.
6. Information regarding any investors whose fee structure (e.g., performance-based fees) or performance reporting (e.g., use of LIBOR-linked benchmark) could potentially be affected by the LIBOR Transition.
7. Any written assessments, strategic plans (including remediation plans, as applicable), roadmaps, or timelines prepared by or for registrant regarding preparation for the LIBOR Transition, including the consideration of alternative reference rates.

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8. Documentation of any risk management matrices or risk inventories of registrant that reference the LIBOR Transition, including a description of any LIBOR Transition-related vulnerabilities or exposure covered by the matrix or inventory.
9. Documentation or descriptions of any analysis performed to identify LIBOR-based risk or valuation models used by registrant, including information regarding changes that may be needed to account for a new reference rate, if any.
10. Materials referencing the LIBOR Transition provided to registrant's board of directors, any committee of the board of directors, any board member, the board or board member(s) of any investors, or the board, legislative body or member(s) thereof of any municipal entity or obligated person client, if applicable, or equivalent governing bodies or offices, if registrant is not organized as a corporation.
11. Information regarding any third-party vendors registrant uses that may be impacted by the LIBOR Transition, including the services provided (e.g., back office) and how the vendor may be impacted.
12. Information regarding any LIBOR-linked contracts or obligations that extend past the current expected discontinuation date that are held and/or issued by registrant, including the implications and impact of any incorporated fallback language.
13. Information regarding any LIBOR-linked contracts or obligations that extend past the current expected discontinuation date that are held and/or issued by registrant's investors, including the implications and impact of any incorporated fallback language.
14. Information regarding any contracts or obligations held and/or issued by registrant, or its investors, that reference a rate identified as an alternative to LIBOR (e.g., SOFR).
15. Information regarding any changes made or planned to be made to registrant's information technology systems (e.g., accounting, investor reporting, risk, valuation or trading) to accommodate the LIBOR Transition, including any changes to accommodate new instruments/contracts and rates with features that differ from LIBOR.
16. Disclosures provided in registrant's filings with the Commission and/or to investors (e.g., in prospectuses) about the LIBOR Transition, including fallback language for LIBOR instruments, as applicable, during the period of January 2019 to the present.
17. Any guidance provided by registrant to employees or supervised persons concerning recommendations to investors to purchase, sell, or enter into LIBOR-linked instruments or contracts that extend past the current expected discontinuation date, reviews of portfolios containing such instruments, or the underwriting of new instruments referencing LIBOR, if applicable.
18. Any guidance provided by registrant to employees or supervised persons regarding the provision of advice to issuers of new LIBOR-linked instruments.

19. Any guidance provided by registrant to employees or supervised persons regarding the provision of advice to clients regarding the replacement of LIBOR in outstanding contracts or obligations with an appropriate alternative reference rate.
20. Any implemented or planned changes to compliance procedures, controls, or surveillance systems designed to monitor for LIBOR-linked instruments or contracts recommended or sold to clients.