Final recommendation regarding fallback rates for CIBOR

The purpose of this report by the Risk-Free Rate Working Group under Finance Denmark has been to produce a final recommendation on how fallback clauses for CIBOR can be formulated.

Following the public consultation regarding a fallback rate for CIBOR (a summary of the responses to the public consultation can be found on Finance Denmark's website) the Risk-Free Rate Working Group has conducted further investigations regarding potential fallback rates for cash- and banking products, which are diverse in respect of customer- and product types. International standards are in the same way still fragmented and typically reflect the relevant market size and characteristics. This causes specific issues for cross-currency products, e.g., syndicated loan and multi-currency facilities.

This work combined with the responses from the public hearing has led to the following changes to the recommendations:

1. The recommended fallback models for CIBOR are now formulated as three complementary and equally valid models (and thereby DESTR is not the "general" fallback), where:

   I. DESTR-fallback is now specifically recommended for derivatives.

   II. CITA fallback is recommended for mortgage loans and bonds.

   III. A third fallback model is added that may be used for cash and banking products (including syndicated loan and multi-currency facilities) where there is a need for more flexibility to secure the most appropriate fallback rate. In this respect the RFR WG have the following considerations:
      a) A CITA based fallback is less complex and may be used for retail banking loans and other customer- and banking products, which require a less complicated fallback.
      b) A DESTR based fallback may be more usable for professional customers and towards for example the syndicated loan markets.
      c) For other banking products and product combinations (e.g., loans or bonds hedged with derivatives) it might be relevant with other fallbacks models that adapt to the product and risk

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profile in the best manner and are agreed upon by the financial institutions and their counterparties.

2. Trigger event no. 5 is changed to be optional and to be agreed among the contract parties. In this way there is consistency with the recommendations made by the WG on Euro Risk-Free Rates.

3. Trigger no. 7 is still optional, but it is mentioned that it could provide a possible discrepancy with international standards for OTC (over the counter) derivatives.

The Risk-Free Rate Working Group furthermore finds it important to underline that this purpose of the work is to provide guidance and that the contracts parties have full flexibility to agree upon any fallback rate that adapts to the product and risk profile in the best manner.

In the following are the final recommendations regarding fallback rates for CIBOR from the RFR WG under Finance Denmark.

1.General recommendations

The RFR WG recommends that financial contracts that refer to CIBOR should regulate:

1. which trigger events in the contract imply that one or more tenors of, or the entire, CIBOR will cease to function permanently as a reference rate,
2. which interest rate replaces CIBOR if a trigger event occurs, which means that a tenor of, or the entire, CIBOR will cease to function permanently as a reference rate,
3. time when the fallback rate begins to apply to the financial contract.

Furthermore, the RFR WG recommends that market participants should seek consistency and use the same trigger events for all asset classes when developing and introducing fallback provisions in different financial instruments and contracts referencing CIBOR, to the extent possible and appropriate.

2. Recommended trigger events

The RFR WG recommends the following trigger events can be used in financial contracts that refer to CIBOR. **Trigger events 1–4** can be used in all financial contracts that refer to CIBOR. **Trigger events 5–7** can be used in financial contracts that refer to CIBOR if the contracting parties deem it necessary, and it is noted that trigger no. 7 might be in discrepancy with international standards for OTC derivatives.

Furthermore, the RFR WG finds that a statement by a public authority other than the parties referred to below that the CIBOR rate will be discontinued will not have any impact and will therefore not constitute a trigger event.

Recommended trigger events:

1. The supervisory authority for CIBOR's administrator makes a public statement or publishes information stating that one or more CIBOR rates will no longer be provided.
2. The administrator of CIBOR makes a public statement or publishes information stating that one or more CIBOR rates will no longer be provided.
3. The bankruptcy administrator of CIBOR's administrator or the administrator, according to the resolution regulations, of CIBOR's administrator makes a public statement or publishes information stating that one or more CIBOR rates will no longer be provided.
4. The supervisory authority for CIBOR's administrator makes a public statement or publishes information stating that:

a) One or more CIBOR rates are no longer, or will no longer be, representative of the underlying market that the CIBOR rate or CIBOR rates are intended to represent, and
b) The representativeness of the CIBOR rate or the CIBOR rates will not be restored.

5. The supervisory authority for CIBOR's administrator makes a public statement or publishes information stating that it is, or will be, illegal to use one or more CIBOR rates as a reference rate in financial contracts.

6. One or more CIBOR rates cease to be provided without a statement or publication of information in accordance with items 1–3 above. Contracting parties must agree on what is considered a permanent cessation if this trigger is to be included in the contract.

7. CIBOR's administrator or the supervisory authority for CIBOR's administrator makes a public statement or publishes information stating that one or more CIBOR rates should or may no longer be used, without reference to regulations.

3. Recommended fallback rates

In the following is the RFR WG's recommendation for fallback rates for CIBOR. The recommendation is based on the standards that have been developed internationally in recent years combined with the characteristics of the Danish mortgage market. The recommendation is very generally held to be able to work for all types of markets, instruments, and parties and the RFR WG finds it important to underline that this is only recommendations and that the contracts parties have full flexibility to agree upon any fallback rate that adapts to the product and risk profile in the best manner.

The fallback interest rates that can replace the CIBOR rate if a trigger event occurs and one or more tenors, or the entire CIBOR, permanently cease to function as a reference rate, is recommended to be:

I. For derivatives the adjusted (compounded) DESTR for the same term as CIBOR plus a spread adjustment is recommended.

II. For CIBOR based mortgage loans, mortgage bonds the CITA rate for the same term as CIBOR plus a spread adjustment is recommended.

III. For cash and banking products (including syndicated loan and multi-currency facilities) where there can be a need for more flexibility to secure the most appropriate fallback rate the RFR WG have the following recommendations:

a) A CITA based fallback is less complex and may be used for retail banking loans and other customer- and banking products, which require a less complicated fallback.

b) A DESTR based fallback may be more usable for professional customers and towards for example the syndicated loan markets.

c) For other banking products and product combinations (e.g., loans or bonds hedged with derivatives) it might be relevant with other fallbacks models that adapt to the product and risk profile in the best manner and are agreed upon by the financial institutions and their counterparties.

4. Recommendation regarding when the fallback rate takes effect

When a trigger event occurs, which means that the CIBOR rate ceases, the RFR WG recommends that the change to the fallback rate is to take place in connection with an interest rate determination opportunity. It is suggested that the change take place at the latest in connection with the first interest rate determination opportunity after CIBOR has ceased. The parties to the contract are recommended to agree on this time in advance.