Eiger Regulatory Partners
Human Capital & Consulting

Are you prepared for LIBOR Transition?

Do you fully understand your conduct and compliance risks during conversion?

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The UK regulators have set clear expectations and obligations on firms

- The UK FCA and PRA have clearly demonstrated that good conduct and treating clients fairly is high on their agenda for transition to new interest rate benchmarks.
- Conduct must be embedded within a firm's transition programme, it should be a constant, open-ended consideration across all other work streams, and it must be central to a firm's strategic decision making.
- LIBOR Transition Conduct Risk is the risk that action or inaction by firms and their employees during LIBOR transition leads to client detriment or has an adverse impact on market stability or effective competition.
- Most Conduct Risks and scenarios (see next page) are not new to LIBOR Transition. However, compared to existing risks they are unique and may be magnified because this is a market driven rather than regulatory driven transition programme, it is a global, multi-asset change with huge operational complexity and because the economic consequences of the conversion of legacy contracts will create 'winners and losers' all of which potentially give rise to incentives for misconduct.
- The regulatory obligation to treat customers fairly when replacing IBORs includes the following components:

  (i) effective communication with clients to ensure they understand the risks of continuing to transact in LIBOR linked products in the short term and how new fallback provisions in existing contracts will operate;

  (ii) helping clients understand the features and conventions of new risk free linked products (which are still evolving for some products and vary across jurisdictions);

  (iii) the process for selection of replacement reference rates in contracts needs to be fair.
- The UK regulatory expectations are very clear. The application of UK regulatory standards across EMEA and into the Asian and Americas regions creates additional operational challenges with differences in regulatory expectations and approaches. Firms who have clients with multiple cross entity and region relationships have the additional conduct and operational challenge of inconsistent messaging and approaches to LIBOR conversion which may lead to poor outcome for clients.
- The FICC Markets Standards Board has recently issued a Spotlight Review which provides helpful guidance on how to manage LIBOR Transition conduct risks and cases studies on the risks around the issuance or sale of new RFR linked products and buy-side risks.

The role of Compliance in LIBOR Transition – how are you doing?

- What is the specific role of Compliance, as a second line function, in your LIBOR transition programme – what are the functional deliverables and responsibilities?
- Do you have an active or passive role and voice in programme governance?
- Are your UK, EMEA and Global Compliance teams connected within your programme and sharing information and adopting similar conduct and compliance standards? How are you managing remote booked business?
- What is your comfort level with your firm's understanding and articulation of its key conduct risks and scenarios which need active risk management?
- Do you have a LIBOR Transition Conduct Risk Register?
- How well trained and engaged are your client facing employees and support function colleagues on their treating customers fairly and conduct risk obligations as the industry commences conversion discussions?
- How are you planning to differentiate clients by knowledge, understanding and complexity of products to manage client specific conduct risk issues?
- How have you developed your monitoring, surveillance and testing programmes to address LIBOR Transition and RFR product development?
- What management information have you developed to monitor the effectiveness of your conduct risk management programme?

How can Eiger Regulatory Partners (ERP) help you?

ERP can provide immediate help to firms who need dedicated Conduct and Compliance SME's to work alongside programme resources and help drive the development and implementation of appropriate conduct risk and compliance control programmes.

We can provide support in a broad range of areas, including:

- Building frameworks for the development and management of LIBOR transition conduct risk during client outreach and engagement (e.g. risk theme and scenario identification and risk mitigation strategies)
- The development and operation of conduct risk governance either within a firm's existing Conduct Risk framework or as a standalone framework
- Advice on how to respond to and risk manage specific conduct risk issues during the engagement process
- Design and delivery of conduct risk training to client facing employees
- Advice on the FCA expectations and obligations of Senior Managers in LIBOR Transition and Conduct Risk Management
- Support in developing LIBOR specific conduct risk registers
- Independent reviews of the set-up of your LIBOR conduct and compliance programme
- Market intelligence on how other firms are managing specific conduct issues

LIBOR Transition conduct risk themes and scenarios

Examples of risk themes	Examples of risk scenarios
Inadequate client communications: The risk communications with clients about LIBOR Transition and alternative references rates and products are clear fair and not misleading	▪ A firm transacts in a LIBOR-linked product with a client which matures after 2021 without appropriate disclosure that LIBOR is likely to discontinue post the end of 2021 and has no fall-back provisions ▪ Failures to communicate in a timely manner adequate or accurate information to clients about a firm's transition programme to enable clients enough time to make informed conversion decisions
Conflicts of interest: The risk a firm's interests with its clients not being aligned, resulting in detriment to the client	▪ A firm puts its commercial interests ahead of its clients' interests during transition and negotiations (eg in use of discretion in the selection of alternative reference rates or the methods for calculating spread) ▪ The risk of information asymmetries where firm's misuse its information advantage during transition and negotiation to the detriment of its clients
Confidentiality & data protection risks: The risk a firm shares client confidential information with unauthorised internal or external parties during transition	▪ Risk that client conversion information is shared across group entities without client consent or to non-authorised staff during the transition. ▪ Risk that client information is shared with a third party without appropriate client consent
Product Risks Potential risk of changes in product performance and valuation when an IBOR is replaced with an ARR.	▪ The risk client enters into a new RFR product which is not deemed appropriate for the client's needs and does not fully understand ▪ The risk that firms falls to adequately explain to retail structured product clients the impacts of LIBOR cessation on product performance or manufacture and distribute new RFR retailed structured products that MUFG produce are not suitable or appropriate for retail clients, or have unfair pricing
Operational readiness The risk a firms' system and operational infrastructure and resources are not ready for conversion	▪ Risk the firm is unable to trade new RFR products and respond to client demand to restructure existing transactions or trade new products ▪ Risk the firm's operational infrastructure and RFR product capability is not able to support the conversion discussions in line with market practice and standards which cause client detriment and delay to clients
Market conduct risks The risk the firm fails to observe proper standards of market conduct during transition	▪ Risk that firms misuse client confidential information or trade on the back of non-public information relating to the price and liquidity of RFR / LIBOR linked products or client trading intentions ▪ Risks of market manipulation during transition (e.g. price positioning, misleading signals, manipulating transactions, collusion)
Anti-competitive practices: Breaches of competition law (eg the exchange of commercially sensitive information, collusion and anti-competitive strategies	▪ Risk of exchange of commercially or competitively sensitive information with third parties (eg between participants at Trade Associations and Industry Working Groups in contravention of competition law) ▪ Perception of employing anti-competitive strategies, such as new RFR product allocations amongst banks, client allocations or new RFR price/spread fixing

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