ERROR POLICY

Introduction

ICE Benchmark Administration Limited ("IBA") became the Administrator for LIBOR, now known as ICE LIBOR,[1] on 1 February 2014 and has strengthened its integrity through enhanced governance and surveillance. As part of its continuing work, IBA is committed to a) minimising the risk of inaccuracies in the publication of ICE LIBOR and b) providing full transparency to stakeholders about any errors in calculating the rate.

Being a Benchmark Submitter to LIBOR became an FCA-regulated activity on 2 April 2013 and the Contributing Banks have committed significant resources to put in place robust LIBOR processes and internal governance within their organisations.

Banks are continually enhancing their procedures and controls but IBA is realistic in recognising that errors may still occur from time to time. We therefore wish to articulate clearly and transparently our approach to handling errors identified subsequent to the publication of ICE LIBOR rates.

Background

ICE LIBOR has global significance and is referenced by an estimated US$ 300 trillion of outstanding business in maturities ranging from overnight to more than 30 years. This means that there is a very wide diversity in the interests and priorities of users of ICE LIBOR.

On 1 August 2014, IBA presented for consultation an error policy that sought to achieve a balanced compromise between the diverse interests of stakeholders and that could promote the objectives of benchmark integrity and transparency. IBA requested feedback to a number of consultation questions and we are grateful to all those who responded.

Operational impacts

The consultation paper noted a number of operational implications which arise from an error policy, including that:

- market participants will be exposed to basis risk if their hedging of a contract referencing ICE LIBOR is valued at the refix rate

- contingent transactions and option exercises may be automatically triggered as a consequence of a refix without either party necessarily anticipating or wanting the resulting transaction, and

- significant time and effort may be expended in amending downstream transactions if the refix values are used.

[1] formerly known as BBA LIBOR.

Considerations

It was recognised in the consultation paper that there are many considerations associated with an error policy for ICE LIBOR, including

- promoting and maintaining the integrity and transparency of ICE LIBOR
- achieving an accurate and reliable representation of the underlying interest
- complying with international best practice standards and regulation
- acknowledging the operational impacts on users of ICE LIBOR
- safeguarding contractual integrity, and
- facilitating an orderly market transition by implementing any new policy in a way which minimises disruption for market participants.

These considerations suggested:

- a threshold for materiality of errors
- a cut-off time for reporting an error to IBA for any intraday refix
- transparency for errors discovered after the cut-off time, and
- allowing a sufficiently long notice period before the changes come into effect.

Cut-off time for intraday refix

The reasons for errors have included technical issues at panel banks, misallocation by banks of supporting transactions and booking a trade in the wrong currency. Errors are usually discovered during post-submission compliance checks on the day of submission but may not be found until a later occasion.

The Consultation Questionnaire stated that IBA's interim refix policy has a cut-off time of 15.00 London time for reporting an error to IBA for an intraday refix. Respondents were invited to give their views on such cut-off time and most favoured a continuation of the interim policy.

Accordingly, an error must be reported to IBA by 15.00 London time for an intraday fix to be considered.

Mindful of the operational impacts that an intraday refix is likely to have on users, IBA will, if an intraday refix is under consideration on any day:

- make an announcement at https://www.theice.com/iba/market-status shortly after 15.00 London time that a refix is under consideration, stating the affected currency and tenor, and
- any refixed rates will be published by IBA by no later than 16.00 on that day.

Threshold for materiality of errors

The consultation paper asked respondents about their preferred materiality threshold for an intraday refix. The consensus was for 3 bps of the published LIBOR rate and this is now the confirmed threshold.

Transparency of later or smaller errors

Some errors may be identified after the cut-off time for an intraday refix - possibly weeks or months later – for example, during the course of an audit.

IBA intends to publish on a quarterly basis the incidence of errors. This will include errors that did not lead to an intraday refix, either because the error came to light after the cut-off time for the relevant day or because the error was smaller than the materiality threshold. The absolute change in published ICE LIBOR will be stated but not the direction of change.

IOSCO Principles

Principle 16 (Complaints Procedures) of IOSCO's Principles for Benchmarks states that Administrators should have a detailed process to follow in the event that a complaint results in a Benchmark determination being changed.

Any determination of ICE LIBOR which is changed following a complaint will be notified in the quarterly publication of errors since it is unlikely that a considered response to a complaint would fall within the time parameters identified above for intraday refixing.

Policy review of thresholds

IBA will review the thresholds periodically to accommodate different rate environments, giving a notice period of at least 3 months unless a change in a shorter timeframe is required as a matter of urgency or is mandated by law or regulation.

Additional comments

IBA confirms that, if a refix is carried out, it will be a re-fixing of the LIBOR rate "as of 11.00 am" to ensure that the refixed LIBOR would be the rate referenced under existing market standard documentation in the loan market.
