

## LIBOR Preparedness Exams Are Coming – Is Your Firm Ready?

July 6, 2020

### KEY POINTS

- The Securities and Exchange Commission’s (SEC) Office of Compliance Inspections and Examinations (OCIE) recently released a Risk Alert warning investment advisers, broker-dealers, investment companies, municipal advisors, transfer agents and clearing agencies (“registrants”) about prospective SEC exams focusing on their London Interbank Offered Rate (LIBOR) transition preparedness. (See “Examination Initiative: LIBOR Transition Preparedness” (Risk Alert)).<sup>1</sup>
- This follows OCIE identifying, in January 2020, the preparedness for the transition away from the LIBOR as a current fiscal year SEC exam priority.<sup>2</sup>
- The Risk Alert stated that “OCIE intends to engage with [investment advisers, investment companies and broker-dealers, among others] 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 [firms] with additional information about the scope and content of these examinations.”
- Firms and their compliance professionals should carefully review the Risk Alert and consider the firm’s LIBOR transition action plans.

LIBOR is used extensively as a benchmark rate to set interest rates for various commercial and financial contracts. It is expected that LIBOR will be discontinued after 2021. The discontinuation of LIBOR, as pointed out in the Risk Alert, “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.”

### LIBOR Exams

The OCIE exams will assess a firm’s efforts “to prepare for the expected discontinuation of LIBOR and [the firm’s] transition to alternative reference rates.” This will include a review of whether and how a firm has evaluated the potential impact of the LIBOR transition on the firm’s: (1) business activities; (2) operations; (3) services; and (4) customers, clients, and/or investors (collectively, “investors”).

<sup>1</sup> Office of Compliance Inspections and Examinations, Risk Alert: Examination Initiative: LIBOR Transition Preparedness (June 18, 2020), [https://www.sec.gov/files/Risk%20Alert%20-%20OCIE%20LIBOR%20Initiative\\_1.pdf](https://www.sec.gov/files/Risk%20Alert%20-%20OCIE%20LIBOR%20Initiative_1.pdf).

<sup>2</sup> OCIE, 2020 Examination Priorities, <https://www.sec.gov/about/offices/ocie/national-examination-program-priorities-2020.pdf>.

The Risk Alert provides a roadmap of what OCIE will review when examining a firm, including:

- 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
- the clients' efforts to replace LIBOR with an appropriate alternative reference rate.

### Sample Exam Document Request List

Notably, OCIE included a sample examination document request list in an appendix to the Risk Alert. This sample list is available [here](#).

Firms and compliance professionals, in particular, should carefully review the sample document request list. OCIE specifically notes that this list "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." The request list, which many firms might find useful as they begin to prepare for SEC exams, includes:

- information regarding any individuals or groups (e.g., internal committees, working groups or transition teams) assigned responsibility to oversee or manage the effects of LIBOR transition, including information regarding the frequency of any meetings on this topic and whether minutes are kept;
- the identity of any third parties used or proposed to be used to assess the impact of LIBOR transition on the firm or its clients, customers or investors;
- 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;
- 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;
- 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;
- any written assessments, strategic plans (including remediation plans, as applicable), roadmaps or timelines prepared by or for the firm regarding preparation for the LIBOR transition, including the consideration of alternative reference rates;
- information regarding any third-party vendors the firm uses that may be impacted by LIBOR transition, including the services provided (e.g., back office) and how the vendor may be impacted;
- information regarding any LIBOR-linked contracts or obligations that extend past the current expected discontinuation date that are held and/or issued by the firm or its investors, including the implications and impact of any incorporated fallback language;

- any guidance provided by the firm 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; and
- 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.

## Conclusion

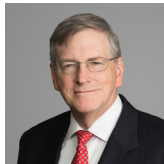
Given OCIE's clear emphasis on LIBOR transition preparedness, impacted firms should review OCIE's sample examination document request list and the firm's LIBOR transition plans generally. The full Risk Alert is available [here](#).

## CONTACTS

For more information on LIBOR discontinuance, please contact any of the following members of Katten's [Financial Markets and Funds](#) practice.



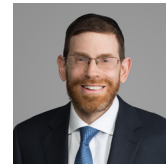
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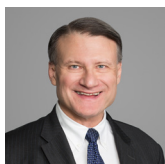
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7/1/20