

ARRC Formally Recommends Term SOFR and Related Loan Conventions in Major Step Towards LIBOR Cessation

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On July 29, 2021, the Alternative Reference Rates Committee (ARRC) of the Federal Reserve formally [announced](#) and recommended CME Group's forward-looking Term Secured Overnight Financing Rate (Term SOFR) rates, marking the final step in the ARRC's Paced Transition Plan it released in 2017. Tom Wipf, the ARRC's Chairman, stated that "market participants now have all the tools they need as we enter the transition's homestretch", and he urged "everyone with LIBOR exposures to immediately take action and base their new contracts on forms of SOFR." As Meredith Coffey, Executive Vice President of Research and Co-Head – Public Policy of the Loan Syndications & Trading Association (LSTA), noted in a [market update](#) last week, the fallback to Term SOFR (i.e., the first step in the ARRC's recommended fallback waterfall) will now be available for existing contracts that have adopted the ARRC's recommended fallback language, providing certainty to all parties as to the exact fallback rate upon the cessation of LIBOR.

The latest announcement follows the ARRC's July 21, 2021 [announcement](#) regarding ARRC's endorsement of the CME Group's [loan conventions](#) and best practices for use of SOFR term rates in anticipation of this formal approval. The conventions closely mirror the existing LIBOR conventions, including holiday, weekend, and business conventions, borrowing notice period, daycounts, interest rate floors and rounding. This will likely lead to a seamless transition if individuals and entities continue being proactive in their steps to mitigate LIBOR exposure, as adopting SOFR in future loan documents will be relatively plug-and-play. For legacy contracts that fall back to a SOFR-based rate, the ARRC continues to recommend a spread adjustment and identical rate floor as the LIBOR floor in the existing contract. The ARRC emphasized in its best practices those areas in which "use of the SOFR Term Rates will be helpful to support a smooth transition away from USD LIBOR".

Now that Term SOFR has been officially recommended by the ARRC, we expect to see market movement towards the adoption of SOFR as the benchmark rate in new transactions in the coming months. In the words of the ARRC's Chairman, "keep in mind: the end of 2021 and of new LIBOR is coming quickly, so take action now".

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