Consumer Financial Protection Bureau
1700 G Street NW, Washington, DC 20552

December 7, 2021

Executive Summary of the 2021 LIBOR Transition Rule

On December 7, 2021, the Consumer Financial Protection Bureau (Bureau) issued a final rule (2021 LIBOR Transition Final Rule or LIBOR Transition Rule) amending certain provisions in Regulation Z, which implements the Truth in Lending Act (TILA), to address the sunset of LIBOR.

Background

In the United States, financial institutions have used LIBOR as a common benchmark rate for a variety of adjustable-rate consumer financial products, including adjustable-rate mortgages, reverse mortgages, home equity lines of credit (HELOCs), credit cards, and student loans. The UK Financial Conduct Authority has stated that it cannot guarantee the publication of certain U.S. Dollar (USD) LIBOR tenors beyond June 30, 2023.

On June 18, 2020, the Bureau published in the Federal Register a notice of proposed rulemaking to amend Regulation Z to facilitate the LIBOR transition for open-end and closed-end credit. For closed-end products, the proposed provisions discussed example indices that were considered "comparable" to certain LIBOR indices and as a result, would not trigger a refinance of the transaction under the existing Regulation Z provisions. For open-end products, the proposed amendments included LIBOR-specific provisions and examples for certain open-end index change

This is a Compliance Aid issued by the Consumer Financial Protection Bureau. The Bureau published a Policy Statement on Compliance Aids, available at https://www.consumerfinance.gov/policy-compliance/rulemaking/final-rules/policy-statement-compliance-aids/, that explains the Bureau's approach to Compliance Aids.

requirements and credit card rate reevaluation requirements, and proposed additional triggers for change-in-terms notices. The proposal also included technical corrections including replacing references to a LIBOR index, with references to a Secured Overnight Financing Rate (SOFR) index, throughout Regulation Z.

This summary discusses the LIBOR Transition Rule, which generally finalizes these proposed amendments to Regulation Z.

Effective Date

Generally, the amendments take effect on April 1, 2022. For certain change-in-terms notice provisions applicable to HELOCs and credit card accounts, creditors and card issuers can begin complying on April 1, 2022, although mandatory compliance does not begin until October 1, 2022. Additionally, for changes to the Initial and Subsequent Interest Rate Adjustment sample forms in Appendix H applicable to certain closed-end ARMs, creditors (and assignees and servicers) may optionally rely on either a format substantially similar to the legacy sample forms or the updated sample forms beginning April 1, 2022, through September 30, 2023. However, beginning on October 1, 2023, those entities may only rely on a format substantially similar to the *updated sample forms*.

Closed-End Credit

The LIBOR Transition Rule adds an example to the commentary of an index that would be comparable to LIBOR for purposes of Regulation Z's requirements that apply to refinancings of closed-end loans.

Specifically, the LIBOR Transition Rule identifies SOFR-based spread-adjusted indices recommended by the Alternative Reference Rates Committee (ARRC) for consumer products to replace the 1-month, 3-month, or 6-month USD LIBOR index as an example of a comparable index for the LIBOR indices that they are intended to replace. This example allows a creditor to replace LIBOR indices with the respective SOFR-based spread-adjusted indices recommended by the ARRC for consumer products without triggering refinancing requirements under Regulation Z. The ARRC plans to announce no later than June 30, 2022, which SOFR-based spread-adjusted replacement index for consumer products it will recommend to replace the 1-year USD LIBOR. The Bureau is not finalizing the SOFR-based spread-adjusted index replacement for 1-year USD LIBOR for consumer products until it has a chance to review the details of the index recommended by the ARRC and make a determination about the index's comparability to 1-year USD LIBOR.

Additionally, the LIBOR Transition Rule adds commentary that provides a non-exhaustive set of factors for use in determining if indices are comparable to LIBOR indices. The determination of whether a particular replacement index meets the Regulation Z standards is fact-specific and, among other factors, depends on the replacement index being considered and the tenor of LIBOR being replaced. These factors provide insight for creditors when completing the analysis comparing LIBOR to other indices besides the SOFR-based spread-adjusted indices discussed above. The factors include, but are not limited to, whether:

- The movement of the index levels of the two indices over time are comparable (i.e., increases and decreases in value or the correlation);
- The replacement index will have a comparable impact on the consumers' payments (if there is sufficient data for this analysis);
- The index levels are comparable (i.e., although indices may increase and decrease at the same rate, is one index always a certain number of basis points higher than another or is a spread-adjustment required);
- The replacement index is publicly available; and
- The replacement index is outside the control of the creditor.

The LIBOR Transition Rule also updates the interest rate adjustment sample forms applicable to certain closed-end ARMs. The updates include replacing LIBOR references with references to a SOFR-based index and correcting an error in the sample form published in 2013. Given that most USD LIBOR tenors will not sunset until June 30, 2023, creditors (and assignees and servicers) may optionally rely on either a format substantially similar to the legacy sample forms or the updated sample forms beginning April 1, 2022, through September 30, 2023. However, beginning on October 1, 2023, those entities may only rely on a format substantially similar to the updated sample forms to be deemed in compliance.

The LIBOR Transition Rule also contains technical edits to other closed-end provisions to replace LIBOR references.

Open-End Credit

LIBOR-SPECIFIC INDEX CHANGE PROVISION FOR HELOC LOANS

The LIBOR Transition Rule includes revisions for changing an index on a HELOC (including an open-end reverse mortgage) under Regulation Z. First, the Rule amends the existing Unavailable

Provision, with updates that facilitate the transition from a LIBOR index when LIBOR is no longer available.

Second, the Rule adds an alternative provision, the LIBOR-Specific provision, which allows HELOC creditors to replace a LIBOR index used on the account and adjust the margin to calculate the variable rate on or after April 1, 2022, even if prior to the discontinuation of LIBOR.

Both options require certain conditions to be met, including:

1. *Historical fluctuation comparison:* Generally, the replacement index must have historical fluctuations substantially similar to those of the LIBOR tenor being replaced. This condition does not apply if the replacement index is newly established.
2. *APR comparison:* The replacement index and replacement margin must result in an APR substantially similar to the APR calculated generally using the LIBOR index values on a specified date and the account's existing margin.

The LIBOR Transition Rule identifies the following examples of replacement indices that meet the "historical fluctuation comparison" standard: 1) the prime rate published in the Wall Street Journal (Prime) with respect to 1-month and 3-month USD LIBOR indices; and 2) the SOFR-based spread-adjusted indices recommended by the ARRC for consumer products to replace the 1-month, 3-month, and 6-month USD LIBOR indices with respect to the LIBOR indices they are intended to replace.

The Bureau is not finalizing the safe harbor for the SOFR-based spread-adjusted index replacement for 1-year USD LIBOR until it has a chance to review the replacement index recommended by the ARRC and a chance to make a determination about whether that index meets the "historical fluctuation comparison" standard with respect to 1-year USD LIBOR.

The determination of whether a particular replacement index meets the Regulation Z standards is fact-specific and, among other factors, depends on the replacement index being considered and the tenor of LIBOR being replaced. The LIBOR Transition Rule contains a non-exhaustive set of factors used to determine if indices have historical fluctuations substantially similar to those of a particular LIBOR index. These factors provide insight for creditors when completing the analysis comparing LIBOR to other indices besides the SOFR-based spread-adjusted indices recommended by the ARRC for consumer products discussed above or Prime. These factors include but are not limited to, whether:

- The index movements (i.e., increases and decreases in value) of the two indices over time are substantially similar; and

- The consumers' payments using the replacement index compared to payments using the LIBOR index are substantially similar (if there is sufficient historical data for this analysis).

If the creditor selects a newly established index as the replacement index, the creditor need not compare the first criteria regarding historical fluctuations, but must still confirm the newly established index and replacement margin meet the "APR comparison" condition, discussed above.

LIBOR-SPECIFIC INDEX CHANGE PROVISION FOR CREDIT CARDS

Regulation Z allows a card issuer to change the index and margin only under certain conditions. For example, prior to the amendments of the LIBOR Transition Rule, Regulation Z allowed card issuers to change the index and margin on an existing contract for credit card accounts when the index used on the account to calculate variable rates becomes unavailable and other conditions are met. Similar as for HELOC accounts, the LIBOR Transition Rule includes revisions for changing an index on credit card requirements under Regulation Z. First, the Rule amends the existing Unavailable Provision, with updates that facilitate the transition from a LIBOR index when LIBOR is no longer available.

Second, the Rule adds an alternative provision, the LIBOR-Specific Provision, which allows credit card issuers to replace a LIBOR index used on the account and adjust the margin to calculate the variable rate on or after April 1, 2022, even if prior to the discontinuation of LIBOR.

Both options require certain conditions to be met, including:

1. *Historical fluctuation comparison:* Generally, the replacement index must have historical fluctuations substantially similar to those of the LIBOR tenor being replaced. This condition does not apply if the replacement index is newly established.
2. *APR comparison:* The replacement index and replacement margin must result in an APR substantially similar to the APR calculated generally using the LIBOR index values on a specified date and the account's existing margin.

Similar to the HELOC provision, the LIBOR Transition Rule also has a provision for newly established indices.

Additionally, as with the HELOC provision, the LIBOR Transition Rule identifies Prime and SOFR-based spread adjusted indices recommended by the ARRC for consumer products as examples of indices that have historical fluctuations that are substantially similar to LIBOR for purposes of the credit card provision and provides the same factors for comparison that can be used when looking at other indices.

CREDIT CARD RATE REEVALUATION REQUIREMENTS

The LIBOR Transition Rule provides a LIBOR-Specific Rate Reevaluation Exception from the credit card rate reevaluation requirements if the card issuer transitioned from a LIBOR index using either the Unavailable Provision or LIBOR-Specific Provision for credit cards, discussed above.

If a card issuer transitioning from LIBOR does so on or after April 1, 2022, and does not qualify for the LIBOR-Specific Rate Reevaluation Exception, or was subject to the rate reevaluation requirements prior to the transition from LIBOR (and is using LIBOR as the benchmark index for comparison), the LIBOR Transition Rule provides a replacement comparison formula. In these cases where the LIBOR-Specific Rate Reevaluation Exception doesn't apply, card issuers will need to identify an index to replace LIBOR as the benchmark index in the rate reevaluation so that they have future index values for the benchmark of comparison.

In selecting the replacement benchmark index in the replacement comparison formula, the card issuer must comply with the LIBOR-Specific Provision for index changes, discussed above.

Once a replacement benchmark index is identified, the card issuer uses the replacement benchmark index value on October 18, 2021 (or other applicable date), the LIBOR index on October 18, 2021 (or other applicable date), and the margin immediately prior to the rate increase to calculate the replacement margin.[1] The formula is as follows:

> (replacement index on October 18, 2021 [or other applicable date]) + (replacement margin) = (LIBOR index on October 18, 2021 [or other applicable date]) + (margin immediately prior to the rate increase)

The card issuer uses the replacement index values and the identified replacement margin to determine when the obligation to complete rate reevaluations is terminated.

---

[1] If the replacement index isn't available on October 18th, the creditor must use the first date that the replacement index and LIBOR are both published for selecting the index value to use in the replacement formula. However, for SOFR-based spread adjusted indices recommended by the ARRC for consumer products, which will not be available until July 2023, the creditor must use June 30, 2023 as the date for selecting the index value for LIBOR and the date of first publication as the date for selecting the index value for the SOFR-based spread-adjusted index.

CHANGE-IN-TERMS NOTICE REQUIREMENTS

The LIBOR Transition Rule revises disclosure requirements for change-in-terms notices for HELOCs and credit card accounts transitioning from LIBOR to a replacement index. Under the Rule, in addition to current requirements (such as the requirement to disclose the index that is replacing LIBOR), a creditor in change-in-terms notices for HELOCs and credit card accounts is also required to disclose any adjusted margin that will be used to calculate the consumer's rate for the LIBOR transition, regardless of whether the margin is being reduced or increased. Historically, Regulation Z required creditors to disclose the replacement index and any increase in the margin but not a margin reduction. While compliance is not mandatory until October 1, 2022, creditors are permitted and encouraged to comply with this change beginning April 1, 2022, the date the rule takes effect. This will ensure that consumers are notified of how the variable rates on their accounts will be determined going forward after the LIBOR index is replaced.

Additionally, the LIBOR Transition Rule adds new commentary to provide details on how a creditor may disclose information about the periodic rate and APR in a change-in-terms notice for HELOCs and credit card accounts if the creditor is using the SOFR-based spread-adjusted indices to replace the 1-month, 3-month, or 6-month USD LIBOR index in certain circumstances. If those conditions are met, the creditor may state that:

1. Information about the rate is not yet available but that the creditor estimates that, at the time the index is replaced, the rate will be substantially similar to what it would be if the index did not have to be replaced; and
2. The rate will vary with the market based on a SOFR index.

The Bureau is not finalizing the SOFR-based spread-adjusted index replacement for 1-year USD LIBOR until it has a chance to review the details of the index recommended by the ARRC and make a determination as to whether the replacement index and the account's existing margin would have resulted in an APR substantially similar to the rate calculated using the LIBOR index.