

Effective as of the close of business on 30 June of this year, the remaining tenors of the London Inter-Bank Offered Rate (LIBOR) (i.e. one-month, three-month, six-month and 12-month tenor) shall be permanently discontinued. In its place, the market and the federal government have coalesced around the Secured Overnight Financing Rate (SOFR).

The transition from Interbank Offered Rates (IBOR) to Alternative Risk Free Rates (RFR) has an impact on all financial and nonfinancial institutions having assets or liabilities that use the impacted floating reference rates.

Market participants should prepare for the USD LIBOR cessation on 30 June 2023 and complete the legacy USD LIBOR transition for their financial instruments by that date. This can be achieved either through active transition or via the operation of robust fallbacks. These transition efforts should largely be focused on the transition to alternative rates (such as SOFR), as well as careful consideration of the risks associated with credit-sensitive rates.

Market participants whose financial contracts (for example, loans, notes and swaps) are governed by US law might wish to analyse whether such contracts can rely on the Adjustable Interest Rate (LIBOR) Act and the implementing regulations of the US Federal Reserve Board (collectively, the LIBOR Act) and, if so, whether such reliance is in their economic interest.

While the LIBOR Act provides some legal certainty with respect to LIBOR transition, parties must examine whether reliance on the LIBOR Act makes sense economically. For example, commercial loans will default to Term SOFR, while swap contracts will default to Compounded SOFR. If the two contracts are intended to work in unison, then there can be a mismatch in the floating rate calculations. Similarly, there are many forms of SOFR that can be used, and parties should be alert as to which form best suits their economic interests.

Importantly, the LIBOR Act allows parties to amend their contracts to other than the mandated SOFR fallbacks. Proactive discussion and negotiation between the parties is, therefore, crucial to avoid unintended economic consequences. In addition, there is no comparable law outside the US, so the only feasible path is engagement between the parties to amend their contracts to provide for LIBOR transition.

Our lawyers have assisted a wide range of financial institutions and corporate clients with this transition as lenders, borrowers and issuers, and as end users and dealers of interest rate derivatives to achieve an orderly transition from LIBOR to SOFR.

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