WARSHAW BURSTEIN

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LIBOR TO BE PHASED OUT BY 2021

On July 27, 2017, Andrew Bailey, Chief Executive Officer of the UK Financial Conduct Authority ("FCA") announced that the use of The London Interbank Offered Rate, or LIBOR, will be phased out by the end of 2021.

LIBOR is the underlying reference rate for more than $350 trillion in financial products, ranging from derivatives and corporate bonds to home mortgages and small business loans.

LIBOR is regulated by the FCA and is calculated by the ICE Benchmark Administration Limited ("ICE"). On a daily basis, ICE surveys certain "contributor" banks to determine the rates at which they would be prepared to lend money to other banks, on an unsecured basis (the mean of these solicited rates is used to set LIBOR).

While LIBOR has been linked to scandals in the past decade relating to rate-rigging, Mr. Bailey indicated that the FCA's decision to end its use was not rooted in these past problems but instead is attributable to a lack of borrowing transaction data sufficient to calculate LIBOR – in short, the market of unsecured lending between banks has not been active enough to ensure that LIBOR reflects actual practices and transactions. In place of active underlying markets, LIBOR has been sustained by the "expert judgment" of the contributing banks in offering their proposed rates, which can raise concerns about the rate's susceptibility to manipulation.

Given the pervasiveness of the use of LIBOR in jurisdictions worldwide and across an enormous swath of financial products, Mr. Bailey acknowledged that an effective transition from LIBOR will need to be "planned and orderly." The FCA and the contributor banks will continue to sustain LIBOR until the end of 2021, during which time a replacement system of alternative reference rates will be discussed, evaluated and put into place. At this point in time, the specifics of what those rates will be, and the manner in which the transition will be implemented, have not been determined.

Obviously, a transition away from LIBOR-based rates will have overwhelming repercussions on existing and to-be-documented transactions.

As a starting point, language in existing loan and other financial contracts that utilize LIBOR should be reviewed to determine if they provide for a replacement rate or for a specific process for arriving at a substitute benchmark rate when LIBOR is unavailable. In many cases, however, such language may only serve as a temporary fix. When LIBOR eventually is replaced, the new reference rate may be based on different economic factors and the "spread" or "margin" above any future replacement rate may not reflect the economics originally intended by the parties. Careful consideration should be given to LIBOR-related transactions currently being documented (especially those that have maturities extending beyond 2021) to ensure that they address – to the best extent possible – the 2021 replacement.

The structure of the FCA's phase out of LIBOR and the identification of the alternative benchmark rate will dictate the best practices going forward. Until those are determined, however, there will be a period of uncertainty.

Warshaw Burstein will continue to monitor this situation, including any specific plans enacted by the FCA, ICE or any other regulatory or oversight authorities, and will keep our clients updated.

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If you have any questions regarding the impending transition away from a LIBOR and the implications for the documentation and negotiation of financial transactions, please call Steve Semian, any of the undersigned or your regular Warshaw Burstein attorney.

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