



# SKADI Impact Piece

## LIBOR Transition Introduction



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### LIBOR Roll-off Timeline

GBP  
CHF, EUR, JPY  
1-Week USD  
2-Month USD

Overnight USD  
1-Month USD  
3-Month USD  
6-Month USD  
1-Year USD

Feb '21                      31<sup>st</sup> Dec '21                      30<sup>th</sup> June '23

Total estimated IBOR Outstanding \$400tn, with EUR largest component, >\$167tn\*



\*Notional size of EUR and JPY include EURIBOR and TIBOR respectively

### Summary

*LIBOR rates, ex the 5 major USD rates, will be suspended Dec-21*

*RFR replacements, with SONIA the preference in the UK*

*Issues around calculation of "synthetic LIBOR" for Tough Legacy contracts*

*Legal issues around multi-party contracts across different jurisdictions.*

### Background

In July 2017, following the investigation into a number of scandals relating to the setting of LIBOR after the 2008 financial crisis, the FCA announced that LIBOR would be suspended at the end of 2021. They cited a lack of activity in the underlying inter-bank market, causing the rate to be no longer representative of market conditions. All other currency LIBOR rates will be suspended except for the five major USD rates (currently pushed back to Jun-23). The move away from LIBOR has huge repercussions as many contracts will not have fallbacks in place for its cessation. In fact, it is estimated 40% of 100 million contracts using LIBOR will require remediation prior to the LIBOR suspension.

### SONIA

The replacement for LIBOR currencies will be Risk-Free Rates (RFRs). In the case of sterling, the rate to be introduced is the unsecured Sterling Overnight Index Average (SONIA). The USD alternative to the LIBOR is the Secured Overnight Financing Rate (SOFR). Unlike LIBOR, which was forward-looking and could be set over longer periods, RFRs are backwards-looking and are reset daily. Whilst SONIA and other rates will be used for contracts agreed since the announcement, it will not be a case of simply substituting SONIA for LIBOR in legacy contracts.

### Tough Legacy Contracts

The problem arises with the many contracts that reference LIBOR and continue past 2022 that have no rate alternative fallbacks and no ability to be amended or renegotiated. In these cases, known as *Tough Legacy Contracts*, it will not always be possible to simply substitute an RFR for LIBOR. The UK government are aiming to provide a Legislative Fix for this problem. Last October, draft legislation was put to Parliament, which would provide the FCA with the powers to make changes to the LIBOR-setting methodology. In essence, this would result in a *Synthetic LIBOR* to be used in place of LIBOR in these Tough Legacy Contracts. The Treasury has recently (Feb-21) released a consultation paper looking at incorporating "safe harbour" into legislation, to reduce the potential risk of contractual uncertainty and protect against litigation claims.

### Multi-jurisdictional Issues

It is inevitable that many aspects of the transition process will give rise to disputes between parties. For example, the matter of whether a legacy contract lies within the remit of the legislative fix is likely to be subjective in some cases. Furthermore, LIBOR is referenced in many complex multi-party financial instruments, such as syndicated lending agreements and bond issues. In such cases, it may not always be possible for an agreement to be reached between all parties. It is also likely that some contracts will be cross-jurisdictional, and legislators in these jurisdictions will have adopted divergent approaches to the LIBOR replacement.

Skadi is an independent consultancy providing advice to the Finance, Mining, Renewable Energy and Shipping Industries. Skadi's **LIBOR Transition Team** of complex product experts can assist with the process to help you determine how best to approach the transition.

- Cataloguing of current inventory of relevant contracts
- Valuation of exposure
- Scenario analysis
- Bilateral negotiation

Whether you have yet to consider the transition, are determining how to execute, or would benefit from independent experienced negotiators acting on your behalf, Skadi can offer help. We would welcome the opportunity for a short introductory call.

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