Benchmarking update: Economic Issues, the Potential for Value Transfer and the Potential for Disputes

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ISDA Initiatives for New vs. Legacy Derivatives Transactions

I. New Transactions
   - ISDA 2018 Benchmark Supplement
   - ISDA is amending Section 7.1 of the 2006 Definitions through a Supplement
   - Counterparties should ensure that their Confirmations reference the ISDA 2006 Definitions
   - Nothing else needs to be done

II. Legacy Transactions
   - ISDA is preparing a Protocol which will be open for 3 months to enable legacy contracts to incorporate the fallbacks
   - Both parties must adhere – adherence is from when last party adhered
Other Industry and Regulatory Initiatives for LIBOR Transition

I. Regulatory
   – “Dear CEO Letters”

II. Industry
   – Loan Market Association for syndicated loans
     • Considered behind, but issues are more complex due to multilateral/multicurrency and be-spoke structure and had hoped for the development of a forward looking term rate and agreement on backward looking compounding in arrears methodology
     • Market regulators have set a target of no new £LIBOR loans after Q3 2020
     • Legacy contracts will not be dealt with through a Protocol but through an LMA Reference Rate Selection Agreement (standardised agreement to agree the replacement rate)
     • New contracts will have to agree the LMA Replacement of Screen Rate Clause (requires lower consensus) vs. hard wired approach
   – International Capital Market Association for bonds and floating rate notes
     • Replacement generally requires consent
     • Increased issuances using the RFRs
I. Legal working group of the Alternative Reference Rates Committee (ARRC) is developing draft potential New York State legislation to amend LIBOR legacy contracts governed by New York law to SOFR rate/spread adjustment contracts
   - Mandatory Application – silent and LIBOR-based fall back contracts
   - Discretionary Application – contracts whereby a calculation/administrative agent is required to determine the applicable alternative rate

II. Possible Roadblocks
   - Constitutional Challenge – Article 1, Section 10 of the US Constitution
   - Which SOFR/rate spread adjustment will be applied?
   - Domestic Solution – legislation will not apply to non New York law governed contracts
   - Enforceability? – will the legislation be enforceable outside of the U.S.?

III. *Is global internationally coordinated legislation a possible solution?*
What Market Participants Should Be Doing Now

• Determine exposure to LIBOR across all products
• Review your derivatives and cash transactions to determine which will mature before the end of 2021 and which mature after
• Identify and amend fallback language in both legacy and new transactions with the goal to developing uniform fallback language for all new transactions
• Consider doing some test trades in the RFRs in various products to become familiar with the mechanics and systems issues
• Consider when to transition new transactions to reference RFRs
• Consider adhering to the ISDA Protocols or using other industry documentation
• Update your systems, accounting/pricing/valuation models
Thank you