ArentFox Schiff

Interest Rate Benchmarks Are Changing Now: How to Protect Your Company from Higher Rates

The End of LIBOR and the Transition to SOFR – What You Need to Know.

- Due to bank manipulation, LIBOR will end in June of 2023.
- No new LIBOR based instruments are to be entered into after 2021, including extensions of existing facilities.
- The effect of this transition impacts numerous financial instruments ranging from corporate loans to derivatives.
- The transition will affect interest rates on all financing contracts and deals that are based on LIBOR.
- There is a lack of information and clarity from the financial world on the LIBOR transition.
- Borrowers and lenders are in flux on protecting their existing loans and bond financings, managing their financial risk, and preparing for the transition.
- The transition has significant risks for those currently entering into loans, bond financings, and other financial arrangements (including swaps).
- There are tax risks as well as financial risks to consider.

What You Can Expect

- Do you have a plan for the transition and have you received and/or reviewed the proposed changes to your contracts and financial arrangements from both a legal and a financial perspective.
- **Rates on bonds and loans will be affected.**
- You can typically expect to receive documents a few days before closing for new and existing deals with provisions relating to a new benchmark rate, but much of the language is vague and/or one-sided.
- Banks and other financial institutions will send you form documents, telling you they are industry-standard and non-negotiable.
- **Don't Let the Bank pick your interest rate.** We can help negotiate a rate in line with your existing interest rate, and mitigate tax and disclosure risks.

About Us

ArentFox Schiff is internationally recognized in core practice areas where business and the law intersect. With more than 650 lawyers and professionals, the firm provides strategic legal counsel and multidisciplinary solutions to a global roster of corporations, governments, nonprofits (including hospitals and colleges), and trade associations.

Our Services

How We Can Help:

- Complete an assessment of all loan documents to determine financial and tax exposure, and accurately measure risk and opportunities.
- Mark-up term sheets and help negotiate the best conversion.
- Build a plan of action to address the transition and create favorable outcomes systematically based upon current and expected market conditions.
- Determine a pre-litigation strategy to protect your interests.

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Frequently Asked Questions

Are Banks Offering SOFR on New and Existing Deals?

Currently, most banks are not offering SOFR or other non-LIBOR actual borrowing rates; instead offering rates based upon the futures market, which has fluctuated considerable in 2022.

Why Not Just Take the Terms Offered by the Bank?

We have seen banks readjust rates that can be as high as thirty basis points off of the existing market rate under the guise of the LIBOR transition. Importantly, other than for a retail customer, a bank may not be legally required to look out for the best interest of the client.

And most older deals have no relevant transition provision so, except if they are governed by unfavorable New York and parallel unfavorable law in other jurisdictions, as well as new Federal law, there may be no clear solution absent a new agreement between both sides. Instead, most companies have been rushed into executing one-sided agreements generally proposed by a bank and accepted without negotiation.

In addition, it is crucial that the provisions in your revised loan/bond documents match existing related interest rate swap agreements.

What's the Value of an Assessment of My Exposure to LIBOR Transition?

You need to know which contracts reference LIBOR, and understand how and when the transition will impact these deals. A careful review will inform you of changes and available options that may include amending contracts to reference alternative rates. We have been successful at negotiating more favorable rates for our clients than initially proposed by the banks. **By way of example, a 30 basis point interest rate differential for a 10-year $100 million loan/ bond could cost the client an aggregate of $3 million.**

How Long Will it Take?

Of course, it depends on many factors, but generally speaking:

— Initial assessment of a client's contracts and deal documents – One week

— Term Sheet Mark-Up and Rate Negotiation – Two Days

— Build a LIBOR transition plan – One week*

What if I'm Using Another Firm for Loan and LIBOR Advice?

We have found that many law firms and financial advisors have a conflict of interest because they represent both the borrowers and large financial institutions. We have an advantage as we are not afraid to challenge the status quo, and we have already had success assisting our clients.

***Note:** Though we generally can undertake the entire process in 1 week (assuming the bank accepts the changes to equate the pre-LIBOR and post-LIBOR cessation rates), timing varies and will be based on a myriad of issues including, but not limited to (i) Board governance/senior management engagement, (ii) disclosure, (iii) tax/financial statement, (iv) advisor/counsel, (v) litigation status/strategy, and (vi) the number of LIBOR based financial instruments.