Milbank

August 15, 2017

CONTACT

Marc Hanrahan
Partner
+1-212-530-5306
mhanrahan@milbank.com

Kevin O'Shea
Partner
+1-212-530-5254
koshea@milbank.com

Douglas Landy
Partner
+1-212-530-5234
dlandy@milbank.com

Erwin Dweck
Partner
+1-212-530-5255
edweck@milbank.com

Yaakov Sheinfeld
Partner
+1-212-530-5274
ysheinfeld@milbank.com

Suhrud Mehta
Partner
+44 (20) 76153046
smehta@milbank.com

Neil Caddy
Partner
+44 (20) 76153145
ncaddy@milbank.com

Milbank Client Alert: LIBOR on Life Support?

On July 27, 2017, Andrew Bailey, the CEO of the Financial Conduct Authority (the "FCA"), stated that the FCA would no longer sustain LIBOR as a benchmark beyond 2021. As LIBOR is the primary reference rate used in floating rate commercial mortgage lending (and many other financial transactions), this announcement has generated uncertainty in affected markets about existing transactions and the structuring of future floating rate transactions.

WHAT WILL REPLACE LIBOR?

While there have been suggestions made by numerous market participants in the UK and US about new rates to replace LIBOR, it is too early for the financial industry to coalesce around one or more replacement rates. A decision will be made over the next few years, and we expect lenders and borrowers to lobby for those rates that are consistent and favor each side's interests.

ARE YOU AFFECTED?

LIBOR is widely used as a reference rate in a variety of contexts ranging from consumer credit (e.g. home equity lines, credit cards and car loans) to derivatives to commercial credit agreements. Therefore, a disruption in LIBOR may have a meaningful impact across a wide spectrum of commercial products.

Most floating rate commercial mortgage loans (and virtually all CMBS products) use LIBOR as their reference rate and are structured with fully-extended maturities of no longer than five years. Theoretically, the five year phase-out period should therefore have minimal impact on these loans. However, given the uncertainty of the index, atypical LIBOR fluctuations may be on the horizon which may result in unintended consequences to borrower and lenders. Moreover, many loans continue to quote floating rates loans based on LIBOR.

WHAT DO MY DOCUMENTS SAY?

Many agreements generally contemplate the unavailability of LIBOR, the ability of a lender to select an alternative index if LIBOR is no longer accurately reflecting the costs to the lender of making the loan, and the selection of a substitute index if any of those circumstances exist. However, these provisions have traditionally been viewed as "boilerplate" and involved limited negotiation, attention and focus. In some cases, the substitute index may be significantly more costly than the LIBOR-based rate. Further exacerbating the confusion, not only do different lenders have different provisions, but, even provisions from the same lender may vary from loan to loan.

WHAT SHOULD I DO?

- Evaluate your current transactions with a duration of three or more years to determine the extent of potential exposure to LIBOR based transactions. It is not enough to simply see if your loan is a floating rate LIBOR loan, but also determine whether you have any additional obligations in such loan that may be tied to LIBOR (e.g. a rate cap or swap for such Loan also dealing with or based on LIBOR).

- Determine with your counsel if existing provisions in such transactions address the issue and, if so, carefully work through how the new base rate will be determined and/or calculated. There are a number of existing reference rates, some of which vary widely from each other. It may be prudent to modify your existing agreements now to address the issues while the transaction is still in good standing rather than wait until LIBOR actually goes away.

- Ensure that this issue is addressed in prospective transactions. We have both model provisions and a list of considerations to assist you depending on which side of the transaction you sit on.

- Stay Informed: The situation is likely to evolve and many industry groups such as ISDA are looking into the issue.

Please feel free to discuss any aspects of this Client Alert with your regular Milbank contacts or any of the members of our Global Leveraged Finance, Financial Institutions Regulatory and Real Estate Groups.

If you would like copies of our other Client Alerts, please visit our website at www.milbank.com and choose “Client Alerts” under “News.”

QUESTIONS?

NEW YORK
28 Liberty Street, New York, NY 10005

Marc Hanrahan	mhanrahan@milbank.com	+1-212-530-5306
Kevin O'Shea	koshea@milbank.com	+1-212-530-5254
Douglas Landy	dlandy@milbank.com	+1-212-530-5234
Erwin Dweck	edweck@milbank.com	+1-212-530-5255
Yaakov Sheinfeld	ysheinfeld@milbank.com	+1-212-530-5274

LONDON
10 Gresham Street, London, UK EC2V 7JD

Suhrud Mehta	smehta@milbank.com	+44 (20) 76153046
Neil Caddy	ncaddy@milbank.com	+44 (20) 76153145