

EVERSHEDS
SUTHERLAND



**Making it
plain sailing**

We can help you
navigate through
the end of IBORs

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What's happening?

All firms will soon be required to end their reliance on interbank offered rates ("IBORs"). IBORs are the foundations on which much of the global financial markets are built. Over time however, cracks in these foundations have appeared and global regulators have decided the time for repair is now.

Wide-spread reliance on IBORs means that the transition firms must undertake will be amongst the most significant in recent memory, and regulatory pressure is building for firms to demonstrate progress.

Financial products referencing IBORs have been a feature of the global financial markets since the 1970s. Since their introduction, the volume of IBOR referencing products has continued to grow. Today IBORs underpin approximately US\$ 370 trillion in notional exposure globally across multiple currencies.

After decades as the dominant benchmark, global regulators have decided that, due to flaws with IBOR, long-term reliance on it is no longer viable. These flaws include IBOR's vulnerability to misconduct and a lack of actual transaction data to verify the rates (as, following the financial crisis, the unsecured interbank market is used less frequently for bank funding).

Global regulators have therefore taken steps to replace IBORs with risk-free rates ("RFRs"). Whereas IBORs are determined using expert judgement, RFRs are calculated using actual transaction data from active markets. The differences in calculation methodology means that the flaws inherent in IBORs are not characteristics of RFRs.

In the United Kingdom, the Financial Conduct Authority (the "FCA") has stated that it will no longer compel or persuade panel banks to submit data for the calculation of sterling LIBOR into 2022. This has had the effect of creating a clear deadline for market participants to end their IBOR reliance.



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Development of RFRs

In February 2013, the G20 instructed the Financial Stability Board (the “FSB”) to undertake a review of the major interest rate benchmarks and plans for reform in order to ensure that these plans were consistent and coordinated, and that the benchmarks used were robust and used appropriately. In July 2014, the FSB published a report recommending the development and use of RFRs.

Various working groups were established in order to identify appropriate RFRs for different markets. These working groups have now identified the RFRs. A summary of the different RFRs are set out on the following page.



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Currency	IBOR	RFR	Secured/ Unsecured	Working Group	The state of the rate
Sterling	LIBOR	Sterling Overnight Index (SONIA)	Unsecured	Working Group on Sterling Risk-Free Reference Rates	<p>SONIA is an unsecured wholesale rate which has been available since March 1997. A reformed SONIA was published in April 2018.</p> <p>SONIA swaps trading is approaching 50 per cent. of the market. There is a liquid market for swaps and futures based on SONIA.</p> <p>A number of SONIA-linked floating rate notes have been issued.</p>
US dollar	LIBOR	Secured Overnight Financing Rate (SOFR)	Secured	Alternative Reference Rates Committee (“ARRC”)	<p>SOFR is a secured treasury repo rate. SOFR was first published in April 2018. SOFR futures became available for trading in May 2018. Clearing in SOFR-referencing swaps began in October 2018.</p> <p>ISDA recently recorded the 1000th SOFR-swap transaction in the year to date, but SOFR swaps are still a very small part of the US dollar swaps market.</p>
Euro	EURIBOR	Euro Short Term Rate (€STR)	Unsecured	Working Group on Euro Risk-Free Rates	<p>€STR is a recently introduced wholesale unsecured overnight bank borrowing rate administered by the European Central Bank.</p> <p>€STR is not only the selected RFR for EUR LIBOR but will also replace the Euro Overnight Index Average (EONIA). EONIA does not meet the requirements of the EU Benchmarks Regulations and will be discontinued from 3 January 2022.</p>
Yen	LIBOR	Tokyo Overnight Average Rate (TONA)	Unsecured	Study Group on Risk-Free Reference Rate	<p>TONA is a unsecured wholesale rate based on overnight transactions brokered in uncollateralised call money markets first published on 1 November 1997.</p> <p>Although both Yen LIBOR and TONA are unsecured rates, there is a spread caused by differences between the underlying markets.</p> <p>There are no developed cash and futures markets in TONA. Number of OTC derivatives referencing TONA is increasing.</p>
Swiss franc	LIBOR	Swiss Average Rate Overnight (SARON)	Secured	National Working Group on Swiss Franc Reference Rates	<p>SARON was first published in August 2009. SARON is the overnight tenor of the Swiss References Rates (SRR). The SRR are based on transactions and executable quotes from the CHF repo market.</p> <p>SARON swap clearing has been available since October 2017. SARON futures have been available for trading since October 2018.</p>



IBORs and RFRs: What’s the difference?

There are a number of fundamental differences between IBORs and RFRs. Firms will need to consider these differences carefully in order to understand whether changes to their systems and processes are needed in order to transition to RFRs. We have identified some of the key differences that firms should consider in the table below.

IBORs	RFRs
Based largely upon expert judgement	Based only upon transaction data in active markets
Forward-looking rates	Backward-looking rates calculated using historic transaction data
Available in multiple tenors	Currently overnight rate only, but term rates are in development
Incorporate a bank credit risk premium	Do not incorporate a bank credit risk premium
A liquidity premium is applied to longer term rates	No liquidity premium is applied

Key issues

IBORs are a ubiquitous feature of the financial markets. For firms that participate in those markets, any change to the IBOR will impact their legal documents, operations and business activity. Any transition away from IBORs will therefore generate a host of issues that firms will need to consider at each stage of the transition process.

What should you do to address these issues?

You should now have established a formal transition program to deal with IBOR cessation. You should ensure that the program has a robust governance structure with appropriate profile and resource. The program should involve the following steps in relation to the transition of derivatives contracts:

Step 1: Identify	You should take steps to identify the use of IBOR in their contracts (in particular those with a stated maturity beyond the end of 2021).
Step 2: Transition	Wherever it is viable to do so, you should enter into new contracts that reference RFRs rather than IBORs. Firms should also consider amending legacy contracts that reference IBORs to instead refer to relevant RFRs.
Step 3: Fallback	You should ensure that the documentation including IBOR references includes appropriate contractual fallbacks (i.e. contractual terms that set out what happens if an IBOR ceases to be available).

Creating a solution that works for you

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An ideal team for large-scale documentation projects

We have the technical skills and experience to deliver comprehensive and cost effective support in relation to large scale projects.

- **directly relevant knowledge:** our dedicated teams have advised a number of clients regarding IBOR transition and is currently working with firms to ensure that they meet the requirements by the implementation date
- **flexible, client-focused solutions:** the advice we provide ranges from discrete, ad hoc advice, to providing you with a managed service of conducting thousands of negotiations
- **proven delivery approach:** we take a pragmatic and commercial approach and will deal with any queries or concerns quickly and efficiently





Step 1: Identify

Our teams offer genuine market insight to guide you in creating an inventory of products and identifying IBOR referencing contracts. We have set out a typical steps plan that clients can follow in order to identify IBORs in their contracts.

Action	Process
Data collation	We will discuss with you the most efficient way to identify and bring together all documents that contain references to IBORs. Once a strategy has been agreed, we will work with you to collate the data in the most useful and accessible way possible.
Data interrogation	We will use the data collated in order to provide you with a global view of your IBOR referencing contracts. This global view can be used to scope your transition project.
Analysis	We will analyse the data in order to provide you with strategic, product specific, guidance regarding the implications of the IBOR references contained in your contracts.

Assurance over the completeness of population of contracts

It is critical that a detailed and methodical approach is taken to establishing the completeness of relevant contracts and the extraction of salient data. Where necessary, we can hold discussions with relevant stakeholders in your business to verify the completeness of the types of systems used to record open contracts and we will sample check the information in these systems to underlying contracts. For transparency, the information we collect will be recorded online in our Collaborate system (see page 17).

A global approach

The global presence of Eversheds Sutherland in all major financial markets means that we are ideally placed to work collaboratively with your local teams and deliver local knowledge where needed.

US

Atlanta
Austin
Chicago
Houston
New York
Sacramento
San Diego
Washington DC

Europe

Austria
Vienna
Belgium
Brussels
Czech Republic
Prague
Estonia
Tallinn
Finland
Hämeenlinna
Helsinki
Jyväskylä
Tampere
Turku
France
Paris

Germany
Berlin
Düsseldorf
Hamburg
Munich
Hungary
Budapest
Ireland
Dublin
Latvia
Riga
Lithuania
Vilnius
Luxembourg
Luxembourg City

Netherlands
Amsterdam
Rotterdam
Poland
Warsaw
Romania
Bucharest
Italy
Milan
Rome
Russia
Moscow
St Petersburg
Slovakia
Bratislava
Spain
Madrid

Sweden
Stockholm
Switzerland
Berne
Geneva
Zurich
United Kingdom
Belfast
Birmingham
Cambridge
Cardiff
Edinburgh
Ipswich
Leeds
London
Manchester
Newcastle
Nottingham

Africa

South Africa
Durban
Johannesburg
Tunisia
Tunis
Mauritius
Port Louis

Middle East

Iraq
Baghdad
Erbil
Jordan
Amman
Qatar
Doha
Saudi Arabia
Riyadh
United Arab Emirates
Abu Dhabi
Dubai

Asia

Singapore
Singapore
Brunei
Brunei Darussalam
China
Beijing
Hong Kong
Shanghai



Step 2: Transition

You should consider taking steps to (i) enter into transactions that reference RFRs rather than IBORs wherever possible in the future and (ii) amend existing contracts that refer to IBORs to refer to RFRs instead. The transition process is, however, likely to present a number of material issues for firms.

In addition, you should monitor the progress made by quantifying IBOR exposure and familiarize yourself with key publications by the FSB, the Official Sector Steering Group and individual working groups.

Liquidity

A lack of liquidity in some markets referencing RFRs may create challenges for firms. Many of these markets are still new and it is difficult to project how quickly these markets will become as deep as those referencing IBORs as this will depend upon market uptake.

Credit spread adjustments

When parties replace a reference to an IBOR with the relevant RFR in an existing contract, the bank credit risk premium element of the rate will be removed. In order to preserve the economic equivalence for the new contract, a spread adjustment may need to be agreed as a proxy for the premium.

Regulatory concerns

You should consider whether an amendment to the terms of your contracts will mean that those contracts no longer benefit from regulatory grandfathering arrangements.

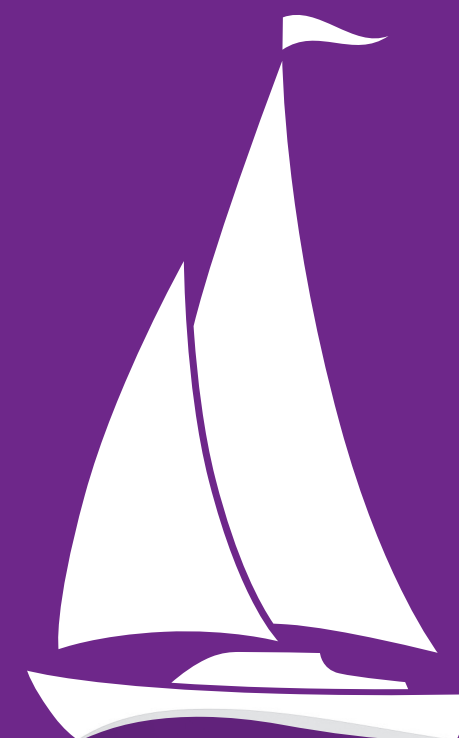
Tax and accounting

The transition from IBORs to RFRs is likely to have far-reaching tax and accounting consequences. In particular, transition is likely to impact hedge accounting where their hedging instruments, hedged risks and/or hedged items are indexed to an IBOR. Key questions also arise as to whether an amendment of hedge designations to refer to a new benchmark would be viewed as a de-designation of existing hedging arrangements and the designation of a new one or whether IBOR cash flows in longer-term cash flow hedges still have a highly probability of occurring.

Development of term rates

RFRs are principally overnight rates. There are efforts across various markets to develop forward-looking term reference rates based on the alternative RFRs. These efforts are being led predominately by the cash markets.

IBORs are forward-looking rates with a number of different tenors. The forward-looking term structure of IBORs means that they can be used to calculate future contractual payments (e.g. interest) in advance at the beginning of an accrual period. As RFRs are backward-looking, the payment due can only be calculated at the end of the accrual period.



Step 3: Fallback

The most favorable transition from IBORs will be one in which contracts that reference IBORs are replaced or amended before fallback provisions are triggered. If you are unable to transition entirely from IBORs to RFRs prior to the date that the IBOR ceases to be available or a regulatory announcement is made that the IBOR is no longer representative, you should, as a minimum, ensure that appropriate contractual fallbacks are adopted.

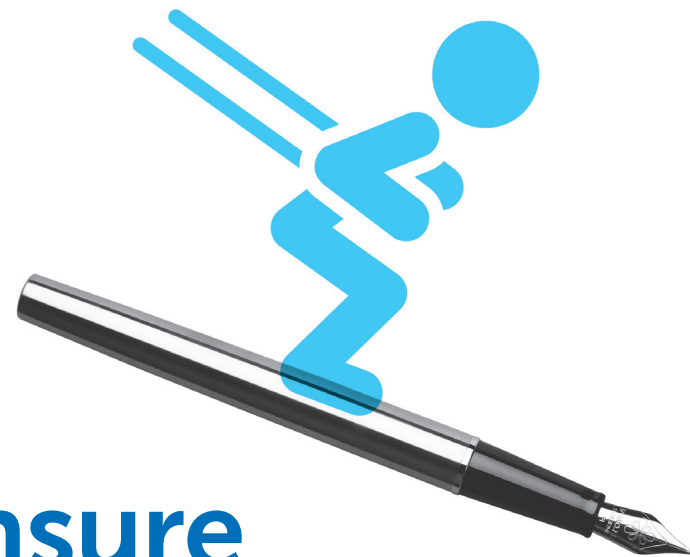
What are fallbacks?

Fallbacks are terms in contracts that determine the “when?” and “what?” if a rate becomes unavailable.

- **When** does a fallback rate to apply?
- **What** is the fallback rate?

Existing fallbacks

Existing fallback provisions included in contracts can be designed for short-term interruptions to the publication of a rate rather than its complete cessation. For example, the fallback provisions contained in some financial contracts rely upon a process of collating quotations from third parties. Such an approach does not represent a viable long term solution because, even if quotations were available in the near-term, it is unlikely that this would continue to be the case for a material length of time.



How we can help ensure a smooth transition

Developing a strategy

We can work with you to develop project plans and offer strategic advice at each stage of the transition process.

Keeping you updated

We participate in numerous industry working groups and are therefore aware of the latest market developments. We can also work with you to ensure that you are up-to-date with product developments and industry documentation initiatives and trends.

Training your team

We can offer tailored training to relevant teams within your business.

Efficient tech solutions

We offer AI solutions as a cost and time efficient way of identifying references to IBORs within contracts.

Helping you keep track

We can also develop tailored reports to help firms track progress.

Helping you communicate with your clients effectively

We can develop a client communication strategy, including documentation that can be used for client education. We can work with you to ensure that all client communications are regulatory compliance and follow your internal processes and procedures.

Global cross-product coverage

We have a global presence in all of the major financial markets across all major products (including cash and derivatives) and offer firms a joined up solution across all products.

Collaboration using technology

We provide a blend of legal advice and technology as a fully integrated part of our business. By advising on, developing and deploying legal solutions using technology, our legal teams are enabled to deliver smarter legal services and our clients benefit from faster and more effective processes.

We are experienced in delivering a wide range of complex projects using technology, with experience in:

- automatic extraction technology and machine learning
- automation of knowledge and playbooks using expert systems
- data capture and manipulation
- data analytics and visualisation
- robotic process automation and document automation

We have a broad range of technology capabilities which act as a toolkit that can be combined to provide a technology solution that works for you.

Collaborate

Our global, client extranet is called Collaborate. Accessible on PCs, mobile phones and everything in-between, Collaborate is a platform that allows us to provide constant access to documents, tools and management information to your team anywhere in the world (or, if you prefer, from specific locations).

At its core, Collaborate provides smart cloud storage. We provide a secure storage facility for legal agreements, travelling drafts and ancillary documents. Collaborate's features include:

- version control
- global searching (including scanned PDFs)
- electronic signature

Users can subscribe to particular folders or documents of interest and receive email alerts when, for example, new documents are added, a document is edited or comments are added.

All of the content contained in Collaborate is permissionable, meaning that different parts of your business can be given access to different features. It can be used as a data room and your counterparties and their advisors can be given access to specific areas or documents. At the end of negotiations, or after a set interval, the team can download a complete and organized bible of all documents.

We also use Collaborate to store documentation that we maintain for our clients. We take a client-centric approach to these templates. Consistency and automatic referencing are used. Collaborate can be used to implement document automation, to allow agreements documenting any changes to rates to be generated and populated automatically using templates in a matter of seconds, reducing time spent and the potential for human error.

For project and volume work, we also use a task tracker which allows tasks to be assigned to specified individuals with built-in priority ratings and work stream management. This also allows us to generate a live Gant chart showing multiple dependencies. Your personnel are able to hone in on their own tasks and those they have allocated to Eversheds Sutherland.

We can also build a data-rich management information dashboard which provides graphical snapshots of the legal terms agreed with third parties.

Where local meets global

Konexo, a Division of Eversheds Sutherland

Legal managed services

We work with you to create, deliver and implement a range of operations including strategy; documents, policies and procedures; processes; legal technology transformation (existing and new); and legal risk.

We have access to the latest technology and processes and can provide you with efficient delivery, high-quality output, risk management, and detailed management information.

Our proven track record includes over 75 consulting projects with in-house legal teams, and we have worked with client teams across Europe, Asia, Middle East and North America.

Legal resourcing

Whether it's experienced lawyers to advise on the latest legal, regulatory or market developments, or more junior teams to deal with high-volume work, our legal resourcing team can support you.

Highly flexible, our candidates will work on your premises, remotely from home or at an Eversheds Sutherland office, full or part-time, or even for a number of hours, allowing you to implement resources exactly where and when you need them.

Why Konexo?



Technology-enabled managed service capability covering data extraction, client outreach and repapering



Experienced management consultants and financial services regulatory consultants



Robotics and legal fintech advisory



Interim resources across the IBOR spectrum including lawyers, paralegals and legal operational staff

Where can Konexo help you with IBORs?

Expert legal advice

We will work with you to create an inventory and identify IBOR referencing contracts. The Konexo team has a deep knowledge of financial products, industry protocols and ultra-high complexity documentation solutions. We offer bespoke designed managed services, with input into playbook, management information and control framework.

Service design and oversight

We understand client-specific scenarios. Collating data, we will calibrate technology, define quality assurance, set our suggested staffing profile and robotics support to build, operate, and oversee the managed service and define quality assurance routines. This will provide you with a global view of your IBOR referencing contracts.

Technology enabled managed service

Technology is at the forefront of our support. We will extract data by scanning OCR physical docs, extract data to an agreed data model, automate quality and accuracy checks, and implement independent QA and transmission to system of record.

We provide client outreach support, helping you provide accurate guidance, such as client communication and education, protocol process, negotiated protocol/ addendum, terms of business update and full bilateral negotiation.

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