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The LIBOR Iceberg Is Dead Ahead – Now Is The Time To Start Steering Clear

18/10/2019

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The Titanic's sinking is one of the most tragic accidents of all time. In finance, we are faced with a transition of titanic proportions that will occur at the end of 2021 as LIBOR ceases to exist as a reference rate and is replaced by SOFR/SONIA or other alternatives. Fortunately, unlike the Titanic's iceberg, we can see this transition coming in advance, but we can only avert disaster if we heed the warnings and begin to plan now to safely navigate away from LIBOR.

Over $350 trillion (240+ trillion GBP) financial contracts reference LIBOR and unfortunately, more continue to be ill-advisedly created to this day. Many authorities, governing bodies and thought leaders will continue to admonish financial institutions that LIBOR will cease to exist at the end of 2021. The ARRC as recently as September 15th issued a battle cry to Wall Street to act now and not wait. An incalculable number of financial instruments, contracts, and automation processes have LIBOR embedded as a reference rate, so those who have not prepared properly may crash into their own version of an iceberg.

One of the most challenging parts of the LIBOR transition is to understand its full impact and reverberations before-the-fact. There are many unknown variables, ranging from the effect on balance sheets, potential stress scenarios resulting from new reference rates, not to mention client reaction and pushback. Many contracts and legal documents contain fallback provisions if LIBOR becomes unavailable. However, since LIBOR is generally for floating rate transactions and SOFR, SONIA and others apply to fixed rate transactions, there is a wide variety of potential financial and reputational damages. An ill-executed transition, or lack of one, can have catastrophic impact to financial institutions.

Without a standardized, planned and comprehensive transition away from LIBOR, the risks of litigation are nearly infinite. A spate of lawsuits and cautionary tales will inevitably follow in 2022 and beyond, pummeling those who have not taken it seriously and done their due diligence.

Law firms and alternative legal service providers (ALSPs) are gearing up today to support the LIBOR transition in some major financial markets (NYC, London, Hong Kong). These firms will supplement in-house teams and contract with partner providers to keep costs manageable while delivering value to their clients when the floodgates open. Firms aren't always able to assess the financial risk implications of reference rate transitions and the long term impact of the rate change from a dollar/value perspective. However, they can be instrumental in working with their clients to manage the onerous amount of documentation (contracts, prospectuses, and other legal documentation such as marketing collateral and product details) that requires remediation. Mentions of LIBOR as a reference rate must be replaced with new language.

Using a traditional law firm typically comes with enormous cost and these firms are not miracle workers for institutions which procrastinate too long. ALSPs which are accustomed to automating processes efficiently will provide an operational edge. A technology-enabled solution can provide scale to deal with the Herculean task that the Libor transition will present. But more importantly, leveraging technology can help mitigate risk and provide budget predictability.

The best defense for banks is to assemble a LIBOR Task Force leveraging internal stakeholders and retaining outside assistance that can seamlessly provide both the focus and expertise to manage the plan. Leadership buy-in and prioritization of this Task Force will be crucial. The Task Force will definitely need a Program Manager and multiple project managers to ensure a transition initiative is effectively implemented within the remaining days of LIBOR. An experienced Program Manager can manage several projects simultaneously, hold teams accountable, and drive activity. Communication is the most critical linchpin. Institutions without a Program Manager in place today need to find one – yesterday.

Banks preparing for the LIBOR transition can consider this 4-part plan:

Assess: Estimate the expected difficulty and risk for each task. Using Artificial Intelligence (AI) tools and experienced personnel, scope out what must be transitioned/developed (documentation, systems, fallback provisions, standard operating procedures, limiting new transactions, training, etc.). This is not only a repapering project but is a complex process requiring both human and technology resources. Analysis and metadata should be provided by producers in a user-friendly format. AI and enhanced machine learning technology is incredibly helpful for identifying active and active agreements and pinpointing their contents.

Prioritize: Determine risk profile, order and priority. Identify potential pain points and bottlenecks so they can be eliminated preemptively. Six Sigma principles can be enormously helpful throughout this process. Clear priorities will then dictate what to assign internally and what external help will be needed from ALSPs or law firms.

Strategize: Map out a detailed and strategic roadmap for success, complete with specific steps, stakeholders, vendors, resources, order and procedures. A transition initiative this massive will live or die by its strategy. Create standardized approaches/playbooks for legal document drafting, remediation, amendment and outreach.

Execute: Execution is everything. Deploying the strategy in a streamlined, sensible and diligent way is the final step toward transition. Track your strategic plan to ensure all milestones are met and compliance is achieved. The initiative/transition team must be able to pivot as new risks come to light. For example, new analysis of bank balance sheets could alter the risk profile of certain transition action). Transition activities will need to be re/de-prioritized on the fly. Throughout execution, a strong communication function and rigorous calendar must be maintained to keep stakeholders informed and hold all participants accountable.

Financial institutions still have more than two years to prepare for LIBOR's discontinuation. In the volatile, unforgiving world of finance, it's fortunate to have so much notice to prepare for an upcoming regulatory change. That advantage cannot be squandered with delay and neglect. Though the sheer enormity of the LIBOR transition is formidable now, imagine how much more daunting it will be six months or one year from now. The iceberg still seems far away, but it won't be for long. By getting the best crew on board now and mapping out a sound and strategic path, financial institutions can avoid disaster.

About the Author
Jeffrey Catanzaro recently joined **Integreon** as Senior VP of Contracts, Compliance and Commercial Services. He is spearheading a new **LIBOR Transition Readiness Task Force** for the large global ALSP (Alternative Legal Services Provider), as well as driving other initiatives and partnerships.