JONES DAY

COMMENTARY

MAY 2019

ARRC Publishes Final LIBOR Transition Recommendations for Floating Rate Notes and Syndicated Business Loans

IN SHORT

The Situation: Financial industries around the world are addressing the probable cessation of LIBOR interest rates before 2022 by, among other things, developing language designed to substitute an industry-approved successor rate—most likely to be based on the Secured Overnight Financing Rate ("SOFR") for the U.S. dollar—seamlessly in the event of such a cessation.

The Result: The Alternative Reference Rates Committee (the "ARRC") has recently released its final "fallback language" recommendations for USD-denominated floating rate notes ("FRNs") and syndicated loans. While the recommended language is "final," it leans heavily on future market developments to provide fundamental calculation conventions.

Looking Ahead: We are aware of a number of major financial institutions that have already adopted the ARRC language, and market participants can expect to start seeing the ARRC language in transaction documents at an increasing pace.

Following up on its September market consultations for FRNs and syndicated loans, the ARRC published final recommended fallback language for both products on April 25, 2019. The recommended fallbacks differ in certain notable respects from those proposed in the consultations and reflect elements of both growing industry consensus as well as fundamental differences between the products. Most notably, the final recommended language for syndicated loans (the "Syndicated Loan Language") continues to avail itself of the flexibility and frequency of amendments in that market by continuing to offer two options (the so-called "Amendment (or "wait and see") Approach" and the "Hardwired Approach") for addressing LIBOR transition, while the recommended language for FRNs (the "FRN Language") reflects the greater difficulty in effecting amendments for that product and accordingly adopts an all or nothing "hardwired" approach.

Because it is significantly more straightforward, we address the FRN Language and certain elements it has in common with the Syndicated Loan Language before addressing some of the unique features of the Syndicated Loan Language.

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FOUR KEY TAKEAWAYS

1. The FRN Language and the Syndicated Loan Language are, at a high level, broadly aligned but with significant differences in detail, most notably in the existence of the Amendment Approach under the

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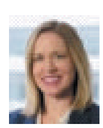

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Syndicated Loan Language.

2. The timing and substance of the ARRC's recommendations reflect a balance between providing the market specific language it can start using immediately and accommodating the future development of highly technical details such as the conventions for calculating Compounded SOFR.

3. While Term SOFR remains the "first choice" under both waterfalls, the ARRC has recently begun to admonish market participants not to await the approval of a Term SOFR but to start utilizing Compounded SOFR or other daily SOFR accrual as the primary benchmark rate in amendments and new financings ***immediately***. Compounded SOFR (in arrears), moreover, still has the maximum potential to cohere with developing conventions for derivatives and enable "perfect" hedging.

4. Notably, the ARRC's recommended language includes cessation and pre-cessation triggers that are consistent with ISDA's still-in-process consultations to mitigate potential "trigger basis risk."

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