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LIBOR reform

Repapering with a competitive edge

How financial institutions can prepare for the London Interbank Offered Rate transition

In July 2017, the UK Financial Conduct Authority announced it would transition away from London Interbank Offered Rate (LIBOR) and no longer compel banks to submit to LIBOR after 2021. And though LIBOR may be the most significant Interbank Offered Rate (IBOR), transitioning away from other IBORs is also on the regulatory agenda.

While repapering contracts is not a new phenomenon, financial institutions may face a colossal task of identifying and inventorying the contracts that need to be transitioned from LIBOR to alternative reference rates (ARRs) in a timely manner. Replacing LIBOR will impact a significant number of financial agreements. Identifying impacted agreements across many products and business areas, understanding remediation approaches, and analyzing the terms of the agreement for fallback provisions will require a significant amount of work and risk.

Given the volume of contracts that reference LIBOR and the uncertainty around fallback provisions, a manual approach to scoping, outreach, and remediation could result in a significant amount of cost and risk. The use of technologies such as artificial intelligence (AI), natural language processing (NLP), and online platforms for generation and negotiation of contract amendments can help make the transition more achievable. Leveraging these technologies can provide organizations the opportunity to scale, understand the content of agreements, and provide a more informed outreach to counterparties.

Common repapering challenges

In addition to identifying impacted agreements, the disruption of LIBOR challenges organizations to understand whether their agreements contain robust fallback provisions. Since few market participants anticipated the permanent cessation of LIBOR, key fallback provisions in contracts were potentially never extracted, captured, and stored in an easily accessible central repository. Instead, fallback language is typically embedded within the terms of lengthy agreements across multiple storage locations. This, along with the need to analyze the fallback language for acceptability and robustness during a transition to ARRs across practice areas, makes scoping and remediation an extensive exercise.

Compounding the challenges of the transition are a multitude of proposed replacement rates across currencies and jurisdictions. When this occurs, work already underway by the industry and the official sector on revised fallback language—including trigger events, fallback rates, and adjustment spreads—is critical. LIBOR, for example, is a forward-looking term rate with a range of different maturities that are calculated based on loan rate submissions from panel banks. In contrast, ARRs are retrospective overnight rates. This means renegotiation of contracts could be difficult, especially if one party feels it is entering into an amendment that may have negative economic impact.

Considerations for a LIBOR repapering program

Given the diversity of products and number of contracts impacted by LIBOR transition, a wait-and-see approach may be unwise. At Deloitte, we believe that an organization's repapering preparedness journey can be split into six distinct phases: planning, scoping, program design, outreach, negotiation, and execution. Below are some examples of activities and considerations at each phase:

Planning, scoping, and program design

Develop a full inventory of contracts referencing LIBOR. Managing legal agreements remains a challenge for many organizations. As a result, most organizations may find a need to compile an inventory of all agreements and identify which ones could include a reference to LIBOR. Having a full view of the contract inventory and the location of agreements can help enable planning for the digitization and extraction of information when required.

Review contracts for exposure and maturity. After identifying the contracts that may have exposure to LIBOR, organizations need to determine which ones will require amendments. This will call for a review to confirm that a reference to LIBOR is present, the clauses related to LIBOR are within, whether the contract is due to terminate post-2021, and an analysis of existing fallback provisions among other specific terms. Mapping of the relationships and dependencies between agreements will also be a necessary step at this stage.

Update existing fallbacks into new agreements. As contracts that reference LIBOR continue to be written, organizations should ensure that these contracts include fallback language as recommended by the various national working groups to accommodate the permanent cessation of LIBOR.

Manage program and disparate stakeholders. Centralizing program management can help coordinate, support, and drive effective stakeholder management and will be important to help align cross-functional stakeholders as they work to address specific issues.

Outreach

Develop an amendment method and templates. To enable a smooth transition, organizations will likely need to develop a playbook on how to move forward based on the specifics of each product, industry segment, and industry agreement. The methods to do so include the International Swaps and Derivatives Association (ISDA) Protocol, which aims to address benchmark fallbacks in several derivatives documents, one-way notices, and bilateral amendments.

Plan outreach strategy. Develop and implement a client outreach strategy with clear objectives to proactively engage, consistently communicate, and increase levels of education with impacted internal stakeholders and clients. The strategy should be designed to educate clients and account for their multiple IBOR-linked contracts where applicable. It will be important to consider the information and timing for each communication addressing IBOR reform.

Outreach to counterparties. Using a tiered approach where applicable, outreach should commence with the initial/priority clients. This should be supported by outreach and migration tools to facilitate a smooth approach to counterparties.

Ensure data quality. A lack of quality data, access to root systems, and static data can create the need for multiple data reconciliations across systems. This can consume resources and delay outreach, remediation, and execution activity. Organizations should be cognizant of this and mitigate data quality issues where possible.

Prioritize client outreach. Early identification of "out of scope" clients or those that are not commercially viable for renegotiation can significantly reduce volume and lower cost of compliance.

Negotiation and execution

Generate amendments. Amendments, whether one-way notices or bilateral, will need to be drafted in consideration of the product types involved. While amendments may be subject to negotiations with counterparties, many organizations have been exploring a modular approach which proposes that one amendment can have annexes covering the amendment of multiple agreement types. When possible, technology can be used to support the generation of these amendments in bulk.

Negotiate and execute amendments. Preparing for these negotiations, including the development of playbook rules to guide negotiators as described above, could be an important factor that contributes to an efficient approach.

Track and report progress. Reporting should provide transparency for both internal and external stakeholders. Our experience from assisting clients with previous repapering initiatives suggests that understanding the current status of renegotiations at a granular level is critical to overall success. For example, client account managers or relationships managers, traders, investment bankers, or corporate bankers will likely be interested in ensuring their clients are getting appropriate attention and that there are no barriers in their ability to do business. Additionally, integration with downstream systems will be required to allow values negotiated within the documents, such as legal terms, to be extracted and used by operational processing systems once a negotiation is complete.

Leveraging technology to guide repapering efforts

Based on the challenges faced by organizations in their preparedness for the LIBOR transition, the use of AI and online platforms to support the generation and negotiation of amendments is becoming a critical consideration in their transition strategies.

Repapering projects often require large teams of in-house lawyers supported by outsourced advisers and external counsel, which can make such projects tedious, time-consuming, and economically unfeasible. In addition, bespoke contract negotiations often require a granular contract review. Technology can help reduce the manual burden on legal departments and increase the quality, accuracy, and accessibility of data. By applying NLP, a form of AI, organizations can automate the extraction of relevant data points from agreements that are pertinent to scoping, outreach, and repapering, as well as other downstream consumers of extracted information.

By investing in these capabilities, organizations can achieve granular reporting with a unified view of the same data for stakeholders while reducing manual processing costs. Furthermore, such an approach can help organizations leverage data in other systems and efficiently manage similar projects in the future.

Deloitte's dTrax

Deloitte's dTrax, an AI-enabled contract lifecycle management tool, is designed to help organizations during LIBOR transition by providing an end-to-end scoping, outreach, and remediation process. Using NLP to extract and integrate contract-related data with business data, dTrax provides standardized templates, first-draft automation, and workflow management of the negotiation process—streamlining the contract management process by helping organizations execute contracts in one place.

Designed by Deloitte's leading analytics team, dTrax can be used by global organizations to support initial margin (IM), US qualified financial contract (QFC) stay rules, and business as usual (BAU) programs. Specific to the LIBOR transition, dTrax enables organizations to:

Extract information from contracts. dTrax NLP can extract and integrate contract-related data with business data. Underpinned by data governance, this capability helps organizations determine the contracts that require amendments that can also be used to inform the transition program.

Generate and negotiate amendments automatically. Using the power of AI, dTrax is designed to reduce cycle time and streamline the contract management process. It provides standardized templates, automates first drafts of agreements, and allows companies to automate the project management of the negotiation process and workflow, including appropriate escalations and approvals, all while consolidating executed contracts in one place and providing an audit trail.

Work according to your needs. dTrax can be configured to meet an organization's specific needs. Our team of experienced practitioners work in conjunction with software developers and product designers to better understand processes, requirements, and how an organization functions. We then configure dTrax to fit the organization's IBOR transition program and improve the efficiency of in-house and external legal teams.

Provide end-to-end reporting. Tailored specifically to an organization's needs, dTrax provides real-time reporting on end-to-end scoping, outreach, and remediation processes for IBOR transition programs. This gives senior leadership real-time insight into completion status and negotiation process bottlenecks, as well as a breakdown of the amendment method (e.g., protocol or bilateral amendment).

Feed data to downstream systems. By developing broad data models within documents, dTrax feeds data to downstream systems with the negotiated terms, such as the fallbacks negotiated by the counterparty, to provide for a smooth and effective integration.

The capabilities and applicability of dTrax technology extend beyond LIBOR transition programs, so many organizations may find it to be a differentiating factor, enabling adoption of one platform that can be leveraged across many regulatory and BAU activities.

Now is the time for action

The transition away from LIBOR will require thoughtful preparation. Organizations that invest in productivity improvements today can be better prepared for the repapering to come. Those that don't may find themselves overwhelmed by the transition.

To discuss your LIBOR specific requirements and learn how dTrax can help with your repapering program, please contact us.

Get in touch

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