
Moving on from LIBOR: Squire Patton Boggs

The IRS has issued proposed regulations that allow issuers to replace LIBOR rates associated with their bonds and swaps without triggering a reissuance of the bonds or a deemed termination of the swaps. The replacement rate must be a “qualified rate,” which includes the Secured Overnight Financing Rate (“SOFR”). A rate isn’t a “qualified rate” unless the fair market value of the bond or swap is the same before and after the replacement, taking into account any one-time payment made in connection with the switch. Although they’re only proposed regulations, issuers can apply them immediately.

Background – Once again, let us dazzle you with the most boring part of a very interesting topic.

Countless municipal bonds and countless derivatives[1] that relate to those bonds depend on the continued existence of one or more of the London Interbank Offered Rates, which are referred to generically as “LIBOR.”[2] In particular, many variable rate bond documents contain rates that are based on LIBOR, and many derivatives contain a variable stream of payments or receipts that is based on LIBOR. For municipal bonds that bear interest at a rate that is based on LIBOR, if LIBOR can’t be determined, then in most cases the bond documents will move the interest rate on the bonds into a “fallback” rate that could be very financially unattractive for the issuer. The same could be true for an interest rate swap with a stream of payments or receipts that is based on LIBOR.

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