Infrastructure and Projects Authority

PFI Guidance Note

Discontinuation of Synthetic LIBOR –

Update to Contracting Authorities – July 2022

July 2022

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Introduction and Purpose

1. The purpose of this guidance note is to update PFI Authorities regarding the proposed cessation of 6-month sterling synthetic LIBOR at the end of March 2023. This will impact many Private Finance Initiative (PFI) projects that have not already successfully transitioned from LIBOR to SONIA. This note should be read in conjunction with the previous IPA guidance note of October 2021 on the cessation of LIBOR[1].

2. The majority of PFI projects have already transitioned successfully with Authority approval for the transition being provided in a timely manner. However, market feedback is that the transition of some PFI projects is being held up by the Authority not providing approval for the transition without any valid reasons for the delay in approval. **This guidance note therefore reminds Authorities of the previous IPA guidance which is that, subject to any project specific concerns, Authority approval for the transition should be given as soon as practicable.**

Background

3. The interest rate benchmark LIBOR is being wound down. The Bank of England has developed an alternative benchmark (SONIA). Market participants were expected to have transitioned contracts (including most PFI contracts) away from LIBOR by the end of 2021[2]. However, in order to mitigate the risk of disruption to legacy LIBOR contracts, the FCA compelled the continued publication of certain LIBOR settings (including 6-month sterling LIBOR) for a limited time after 31 December 2021 using a 'synthetic' methodology.

4. Most PFI project senior debt finance uses 6-month interest rate settings. For many of those PFI projects that didn't transition to SONIA by the end of 2021, a viable option for the PFI Special Purpose Vehicle (SPV) at the beginning of 2022 was therefore to use these synthetic 6-month LIBOR rates until such time as the transition to SONIA was completed. However, these synthetic LIBOR settings were always meant by the FCA to be temporary. The FCA has recently released a new consultation paper[3] in which it proposes that the publication of 6-month synthetic sterling LIBOR settings will end at the end of March 2023.

5. Proposed cessation of 6-month sterling synthetic LIBOR by the end of March 2023 creates a 'hard date', whereby all PFI projects that utilise LIBOR must have transitioned to an alternative interest rate benchmark (presumed to be SONIA). Failure to have transitioned by this date may have adverse consequences for the SPV with potential knock-on consequences for the project and for the Authority. It should be noted that interest rollover dates may require much earlier action to ensure transition is completed before this date.

[1] PFI Guidance Note - Discontinuation of LIBOR - applied to PFI Projects – October 2021
[2] For some PFI projects (e.g. Bond financed), LIBOR is not used and the LIBOR/SONIA transition is not relevant.
[3] CP22/11 – Winding down synthetic sterling LIBOR and US Dollar LIBOR

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6. As long as the appropriate Refinancing transition information has been provided by the SPV to the Authority, and provided that there are no project specific risks identified, consent to the transition should be provided by Authorities as soon as is practicable. Authorities should not link their consent to this transition to the agreement of any other commercial issues or disputes that are currently the subject of discussions or negotiations with the SPV. This guidance is unchanged since IPA's previous guidance note in October 2021.

7. Authorities are reminded that provision by the SPV of information, responses and documentation consistent with the standard documents that were provided with the October 2021 IPA Guidance Note, should provide the Authority with sufficient confidence that there will not be a Refinancing Gain arising as a result of the transition. Further, the standard documents protect the Authority from any increase in potential liabilities as a result of the transition. The standard documentation is in the form of templates that require amendment to reflect project specifics, however the IPA recommends that SPVs and Authorities try to follow the standard documentation where possible. This should enable a more efficient transition process, and minimise external advisor fees.

8. It is noted that if the LIBOR to SONIA transition is not expected to lead to a Refinancing Gain, the transition is a Refinancing, but it is not a Qualifying Refinancing. As such, Authority approval would not usually be required under the Project Agreement. However, PFI market practice over the last 12 months has been that most PFI financiers have requested Authority approval for this transition anyway.

9. Feedback from the PFI market is that PFI financiers have a strong desire to obtain Authority approval for the transition from LIBOR to SONIA prior to completing the transition. This is because when the transition from LIBOR began, PFI Financiers did not wish to take the risk (although remote) that with the implementation of an alternative interest rate benchmark, a small Refinancing Gain might inadvertently arise, or be deemed in future to have arisen, possibly creating a contract breach in the absence of approval for the transition.

10. In the first instance the responsibility for making the transition from LIBOR to SONIA (and any risk inherent in the transition) lies with the private sector - not with the Authority. However, if the SPV cannot transition by end March 2023 when synthetic sterling LIBOR may end, the resulting financing issues for the SPV may negatively impact the SPV's ability to provide the contract services, and may complicate future discussions between the Authority, the SPV, and its funders on financing-related contract matters.

11. It is therefore in both the Authority and the SPV's interests to conclude the transition. As long as the appropriate Refinancing transition information has been provided by the SPV and provided that there are no project specific risks identified, consent to the transition should be provided by Authorities as soon as is practicable. If unclear how to proceed, Authorities should seek guidance from sponsoring departments prior to appointing external advisors.

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Contact IPA

www.gov.uk/IPA

IPA@ipa.gov.uk

@ipagov

Cabinet Office
Correspondence team
70 Whitehall
London
SW1A 2AS
publiccorrespondence@cabinetoffice.gov.uk
General enquiries: 020 7276 1234

HM Treasury
Correspondence team
1 Horse Guards Road
London
SW1A 2HQ
public.enquiries@hmtreasury.gsi.gov.uk
General enquiries: 020 7270 5000