June 15, 2020

Via email to the ARRC Secretariat at: arrc@ny.frb.org

Alternative Reference Rates Committee, convened by the Board of Governors of the Federal Reserve System and the Federal Reserve Bank of New York

Re: ARRC Summary of Feedback Received in the ARRC Spread-Adjustment Consultation and Follow-Up Consultation on Technical Details

The Structured Finance Association ("**SFA**") appreciates the opportunity to respond to the Follow-Up Consultation ("**Follow-Up Consultation**") of the Alternative Reference Rates Committee ("**ARRC**") regarding technical details related to the ARRC's previous Spread-Adjustment Consultation.

SFA is a member-based trade industry advocacy group focused on improving and strengthening the broader structured finance and securitization market. SFA's core charge is to support a robust and liquid securitization market, recognizing that securitization is an essential source of funding for the real economy. While the comments expressed in this letter represent the consensus views of our broad membership, this letter does not necessarily represent the perspectives of all SFA members. None of the recommendations expressed herein are binding on, or should be attributed to, any individual SFA member, each of which will decide for itself whether and to what extent to submit individual comments in response to the Follow-Up Consultation.

SFA views the Follow-Up Consultation as an important step in the overall process of transitioning globally from LIBOR to new benchmarks representing market-based risk-free rates. The Follow-Up Consultation seeks commentary on the certain technical details relating to the spread adjustment methodology the ARRC should include as part of its fallback provision recommendations for cash products referencing LIBOR and asks two specific questions relating to such methodologies ("**Questions**"). The Follow-Up Consultation seeks commentary from all market participants.

As you know, SFA is a member of ARRC and we also serve as co-chair of the ARRC Securitization Working Group. In an independent effort, we began convening our LIBOR Task Force in early 2018 to identify potential best practices that SFA members in particular believed would help ensure an as-seamless-as-possible transition away from LIBOR to successor benchmarks. The SFA LIBOR Task Force includes a broad cross-section of SFA members from all our constituency groups, including, among others, banks, issuers, investors, trustees, rating agencies, and servicers.

Submitted below, are SFA's responses ("**Responses**") to both Questions. For your convenience, the Responses have been placed in the order in which the Questions were presented, and the text of each Question is presented in italics before the associated Response. Capitalized terms that are used in this letter, unless otherwise defined, have the meanings set forth in the Follow-Up Consultation.

Question 1: *Do you believe that using the ISDA methodology of a 5-year median of the historical difference between LIBOR and the SOFR fallback rate is the best choice for cash products, or would you prefer that the same spread value to be used by ISDA , based on the 5-year median of the historical difference between LIBOR and a compound average of SOFR in arrears, should be applied to each potential fallback rate?*

☐ *5-year median methodology*
☐ *5-year median value*

Response to Question 1:

As discussed in SFA's March 25th response to the ARRC's Consultation on Spread Adjustment Methodologies for Fallbacks in Cash Products Referencing USD LIBOR (the "**March 25 SFA Response**")[1], SFA believes that that there is significant value in the securitization industry aligning with the spread adjustment methodologies used by other key market participants, including ISDA. Additionally, the March 25 SFA Response noted that SFA supports consistency in how various products and asset classes handle the transition from LIBOR to successor reference rates. As such, the vast majority of SFA members have indicated that they support securitization transactions using a spread adjustment equal to the 5-year median value between LIBOR and a compounded average of SOFR in arrears as calculated by ISDA for the relevant tenor. Such members believe that having securitization transactions incorporate the same methodology (rather than the value itself) as used by ISDA would add complexity without adding significant value.

Additionally, such SFA members have noted that using a single published number to act as a spread adjustment between each respective tenor USD LIBOR and any SOFR-based reference rate (e.g., overnight SOFR compounded in advance or in arrears, simple average overnight SOFR in advance or in arrears, or term SOFR) may be beneficial to the market. First, there is simplicity in having a single number represent the spread adjustment between LIBOR and any SOFR-derived reference rate for the relevant tenor. Second, if the median historical differences between LIBOR and multiple SOFR-derived reference rates for the relevant tenor were each calculated based on such methodology, it seems likely that such differences in the spread adjustment values calculated across different SOFR-derived reference rates would be small in relation to the size of the spread

[1] Available at https://structuredfinance.org/wp-content/uploads/2020/03/SFA-Response-to-ARRC-Spread-Adjustment-Consultation-March-2020.pdf.

adjustments. Furthermore, to the extent term SOFR is eventually published, there may not be sufficient historical data at that time to calculate a median difference for such term rate. For these reasons, the vast majority of SFA members support the use of the 5-year median value of the difference between each respective tenor LIBOR and SOFR as calculated by ISDA as the spread adjustment.

Question 2: *Do you believe that the ARRC's recommended spread adjustments should be set at the same time that ISDA's spread adjustments are set in the event that a pre-cessation event is operative?*

☐ *Should be set at same time as ISDA*

☐ *Should be set at the time that LIBOR is found to be no-longer representative, regardless of ISDA's timing*

Response to Question 2:

ISDA has recently indicated that they plan to incorporate a pre-cessation trigger into the 2006 ISDA Definitions this July.[2] Although the supplement to amend the 2006 ISDA Definitions which is not expected to be published before early July, ISDA has indicated that the pre-cessation trigger would occur on the date of a statement by the UK Financial Conduct Authority that LIBOR "is no longer, or as of a specified future date will no longer be, capable of being representative." To the extent a pre-cessation event occurs under the amended ISDA protocols, SFA believes that the ARRC's recommended spread adjustments should be set at the same time that ISDA's spread adjustments are set. We believe that this would be necessary in order to use the ISDA value as discussed in Question 1 and to support consistency between securitizations and any related derivatives.

However, we also believe that the ARRC must be prepared to provide guidance or publish a recommended spread adjustment on various dates until ISDA has published its spread adjustment value. Under the ARRC's recommended fallback provisions, pre-cessation events may occur prior to the occurrence of a pre-cessation trigger pursuant to the amended 2006 ISDA Definitions. For example, the ARRC's recommended fallback provisions for securitizations contain the Asset Replacement Percentage trigger while a similar trigger will not be included in the amended ISDA protocols. Whether the Asset Replacement Percentage will be triggered in any individual transaction will depend on characteristics unique to such transaction's underlying pool of assets. Similarly, the ARRC's recommended fallback provisions for syndicated loans and bilateral loans contain an Early Opt-in Election which can cause the benchmark to be replaced prior to the ISDA

[2] https://www.isda.org/2020/05/14/isda-publishes-report-summarizing-final-results-of-consultation-on-pre-cessation-fallbacks-for-libor/

pre-cessation trigger, and a similar provision will not be included in the amended ISDA protocols. Therefore, SFA believes it will be necessary for the ARRC to publish either recommended spread adjustments or a recommended methodology containing prescriptive calculations for determining such spread adjustment in advance of ISDA publishing the value of the spread adjustment to be used in the 2006 ISDA Definitions. To the extent securitizations will transition from LIBOR based upon the activation of the Asset Replacement Percentage trigger, having the ARRC publish a spread adjustment or guidance on how such spread adjustment should be calculated that can be applied on the replacement date will be necessary in order to determine the Benchmark Replacement Adjustment under the first alternative in the recommended fallback provisions. Lastly, to the extent the ARRC were to publish a recommended methodology for determining the spread adjustment values, we believe it would be beneficial to the securitization market for such methodology to align with the proposed methodology endorsed by ISDA. This would help ensure consistency between transactions that transition based on the non-representative trigger and the Asset Replacement Percentage trigger.

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SFA appreciates your consideration of these comments and welcomes the opportunity to discuss further. If you have any questions about this matter, please contact Kristi Leo, President, at (917) 415-8999 or Kristi.Leo@structuredfinance.org.

Very truly yours,

Kristi Leo
President
Structured Finance Association