ARRC Fallback Consultation Webinar: Securitizations

Consultation Regarding More Robust LIBOR Fallback Contract Language for New Originations of LIBOR Securitizations

Speakers
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Presentation Overview

- **Background**
  - A Brief History of LIBOR
  - The Alternative Reference Rates Committee (ARRC) and the Securitizations Working Group (SWG)
  - Comparison of LIBOR and the Secured Overnight Financing Rate (SOFR)
- **Key Issues Addressed by the ARRC's Securitizations Consultation**
  - Triggers
  - Replacement Benchmark Waterfall
  - Replacement Benchmark Spread Waterfall
- **Seeking Your Feedback: Reviewing Key Consultation Questions for the Securitization Industry**
- **Next Steps**

Background

A Brief History: How We Got Here

- **The London Interbank Offered Rate (LIBOR) has been called the world's most important number**
    - Quoted daily across 5 currencies & 7 maturities, LIBOR underpins hundreds of trillions of dollars in contracts around the world from residential to commercial mortgage loans to complex derivatives to credit cards and auto loans
- **LIBOR-related scandals and concern that LIBOR was based off an inadequate number of underlying transactions led to the passage of several reforms to strengthen the system**
    - In 2012, the newly-created Financial Conduct Authority (FCA) was given regulatory oversight of LIBOR
    - In 2014, Financial Stability Board (FSB) published a report recommending the transition away from LIBOR to new reference rates supported by actual market transactions as opposed to bankers' judgments (http://www.fsb.org/2014/07/r_140722/)
    - Thereafter, regulatory bodies and governmental agencies around the world began in earnest to identify these new reference rates
- **On July 27, 2017, Andrew Bailey, Chief Executive of the FCA, announced that the FCA would no longer compel banks to submit quotes for LIBOR after 2021**
    - The announcement further galvanized global efforts to transition to these new reference rates

LIBOR Only Exists if Banks Submit Quotes; They Won't Have to After 2021

- More than $200T of USD LIBOR contracts outstanding
- However, the median daily volume of three-month funding transactions (three-month LIBOR is the most heavily referenced tenor of USD LIBOR) is less than $1 billion, and there are many days with volumes of less than $500 million
- Any abrupt cessation of LIBOR, a less than robust rate as noted earlier, could create material risks for the $200T of outstanding contracts

Beyond LIBOR: Firms Must Start to Prepare if They Haven't Already

The UK's Financial Conduct Authority said it would not compel panel banks to submit quotes to the range of LIBOR currencies after 2021, leaving less than three years to prepare for transition to a new benchmark rate

- *"I hope it is already clear that* ***the discontinuation of LIBOR should not be considered a remote probability 'black swan' event****. Firms should treat it is as something that will happen and which they must be prepared for."*

  Andrew Bailey, Chief Executive of the Financial Conduct Authority

- *"The public and private sector share the recognition that* ***there is a strong possibility that LIBOR may discontinue, and the associated risks are considerable****. That's why these consultations for fallback contract language are a crucial development in creating a more resilient financial regime."*

  Sandra O'Connor, Chair of the Alternative Reference Rates Committee and JPMorgan Chief Regulatory Affairs Officer

- *"Internally, if you have not already done so,* ***mobilize a formal transition program in your firm****, bundle your arrows. In that bundle,* ***include a budget with ample resources, a governance structure, and work streams with clear mandates*** *to: conduct impact assessments; develop inventories of legacy exposures and contracts that mature after 2021; prepare for new products and financial instruments that will be linked to the new [risk-free rates]; and develop internal education and client outreach and communication plans."*

  Rostin Behnam, Commissioner of the Commodity Futures Trading Commission

About the Alternative Reference Rates Committee (ARRC)

- What is the ARRC?
    - In November 2014, Board of Governors of the Federal Reserve System and Federal Reserve Bank of NY formed the ARRC to identify a replacement rate for USD LIBOR
- Comprised of financial institutions, trade associations, official sector
- Initial charge was to determine a new reference rate to replace LIBOR
- ARRC originally focused on the derivatives market
- In June 2017, ARRC selected SOFR as its preferred replacement rate
- In March 2018, ARRC was reconstituted to develop strategies to facilitate the transition from LIBOR across cash products:
    - Floating rate notes (FRNs)
    - Syndicated business loans
    - Securitizations
    - Consumer products
    - Bilateral business loans

ARRC Members	
AXA	JP Morgan
Bank of America	LCH
BlackRock	MetLife
Citigroup	Morgan Stanley
CME Group	National Assoc. of Corp. Treasurers
Deutsche Bank	PIMCO
Fannie Mae	TD Bank
Freddie Mac	FHLBNY
GE Capital	Independent Community Bankers of America
Goldman Sachs	LSTA
Govt Finance Officers Assoc.	SIFMA
HSBC	Wells Fargo
Intercontinental Exchange	World Bank Group
ISDA	
ARRC Ex-Officio Members	
CFTC	Board of Gov. of the Federal Reserve System
CFPB	Office of Financial Research
FDIC	Office of the Comptroller of the Currency
FHFA	SEC
Federal Reserve Bank of NY	U.S. Treasury Department

ARRC's Focus on Cash Products

- **ARRC mandate for Cash Markets**
    - In the Spring of 2018, the ARRC organized Cash Market Working Groups for each product area to develop strategies to transition from LIBOR as appropriate
    - Working groups specifically tasked with producing a "consultation" for public comment that would help address risks in contracts referencing LIBOR and outline the steps for an effective transition from LIBOR
    - For Securitizations, the ARRC selected the CRE Finance Council (CREFC) and the Structured Finance Industry Group (SFIG) as co-chairs of the Securitizations Working Group (SWG)
    - Note that the SWG Consultation also incorporates the views of the Loan Syndications and Trading Association (LSTA) and its members as it relates to corporate CLO securitizations

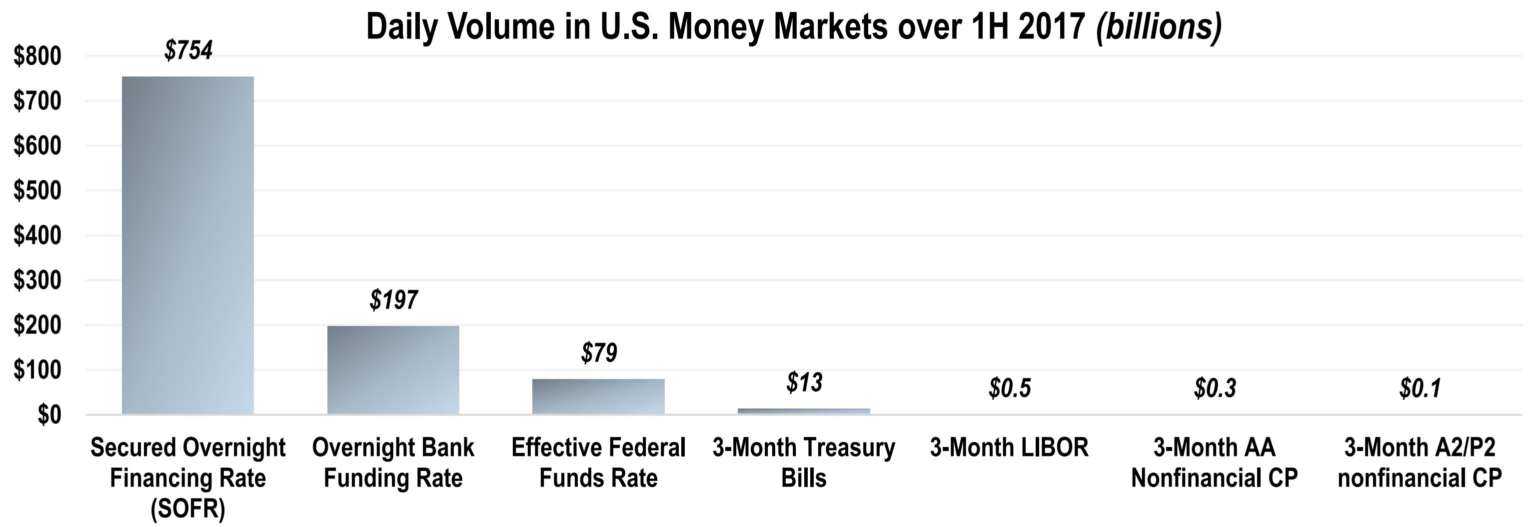
ARRC's Securitization Working Group

- **Composition of the ARRC's Securitizations Working Group (SWG) is varied and attempts to cover as much of the securitization markets as possible**
    - SWG is comprised of the leading lenders, investors, advisors, and associations across the securitization market and numbers over 60 companies. SFIG and CREFC are extremely grateful for all the time and effort put into this Consultation.
    - Focus of the SWG is to help the securitization markets transition from LIBOR with minimum disruption to the securitization markets

Securitizations Working Group Member Companies				
AIG	Citi	GM Financial	Morgan Stanley	State Street
Annaly	Credit Suisse	Goldman Sachs	Morningstar	TIAA
AXA	CREFC	Guardian	Natixis	TPG
Bank of America	Dentons	HSBC	Navient	US Bank
Bank of the West	Deutsche Bank	Huntington	New York Life	Vanguard
Barclays	Discover	JP Morgan	Nomura	Volvo
Berkadia	Fannie Mae	Key Bank	PIMCO	Wellington
BlackRock	Federal Reserve Bank of NY	Kroll	PNC	Wells Fargo
Blackstone	FHFA	LSTA	Prudential	Wilmington Trust
Board of Gov. of the Federal Reserve	FHLB	Met Life	RBC	
Brighthouse Financial	Fitch	Mizuho	S&P	
Cadwalader	Ford	Moody's	SFIG	
Chatham Financial	Freddie Mac	Morgan Lewis	SIFMA	

Why LIBOR Is No Longer Viable…and Why the ARRC Chose SOFR

"LIBOR is measuring the rate at which banks are not borrowing from one another," Andrew Bailey, FCA



Median Daily Number of Unsecured Wholesale Borrowing Transactions Observed for USD LIBOR Panel Banks

	1-Month LIBOR	3-Month LIBOR	6-Month LIBOR	1-Year LIBOR
2017 Q1	6	6	3	1
2017 Q2	8	6	3	0
2017 Q3	7	5	2	1
2017 Q4	9	6	2	1
2018 Q1	7	8	3	1
2018 Q2	5	7	2	0

- Globally, policymakers have looked for robust, highly traded replacement rates
- Almost all liquidity and trading is in overnight markets
- U.S. selected SOFR:
  - Combination of 3 Treasury repo rates
  - Very deep, very liquid; $800 billion of daily trading vs <$1 billion in 3M LIBOR
- Why not other rates?
  - Fed Funds – <$80 billion of trading; fewer counterparties and highly reliant on GSEs; using a policy target rate could have monetary policy implications
  - T-Bills – Insufficient daily trading

Source: Federal Reserve Bank of New York; Financial Industry Regulatory Authority; DTCC Solutions LLC, an affiliate of the Depository Trust & Clearing Corporation; and the Board of Governors of the Federal Reserve System

Comparison of LIBOR and SOFR

LIBOR	SOFR
• Term structure	• Overnight (to begin)
• Unsecured	• Secured
• Reflects bank cost of funds(ish)	• Risk-free rate
• Higher rate given bank credit component	• Lower rate
• Not liquid, deep, transparent	• Liquid and deep
• Less than $1B of daily trading	• Nearly $800B of daily trading
• Easily manipulated	• Not easily manipulated
• USD trillions of long-dated cash contracts	• Over $30B of SOFR issuance since July

Understanding the ARRC's Securitizations Consultation

Introducing the Consultation for New Securitizations

- What is LIBOR fallback language?
  - Legal drafting in credit agreements that details the steps taken to replace LIBOR if it’s no longer available or deemed to be no longer representative.

- What are the three components of LIBOR fallback language for securitizations?
  - **Triggers:** What events would result in a transition from LIBOR to the new replacement rate?
  - **Replacement Benchmark Waterfall:** What should the new replacement rate be? We know that the ARRC has selected SOFR as its preferred rate but what if there isn’t a term structure for SOFR at the time of transition? Or what if SOFR isn’t around anymore?
  - **Replacement Benchmark Spread Waterfall:** How should the rates be adjusted to account for the differences between LIBOR and the new rate? LIBOR has both a term and bank credit risk component while SOFR is a secured, risk-free overnight rate. Therefore, what should the additional spread be to compensate for these differences?

Introducing the Consultation for New Securitizations

- The Consultation recommends, as suggested best practice, triggers, fall back rates, and spreads with the aim of minimizing discretion in the event of a LIBOR cessation

- While the goal of the language is to be clear in the steps that should be followed, **there will still need to be agreement among issuers, sponsors, servicers, managers, trustees, agents, and perhaps other third parties** on who will determine whether a trigger has occurred, what the new rate and spread should be, and who should perform the calculations
    - The Consultation uses the placeholder defined term "**Designated Transaction Representative**" to allow the parties to a transaction to agree to certain parties taking on specific roles and obligations

- While every effort was made to ensure that all critical points were addressed, the Consultation may not have taken into account all facets of the transition from LIBOR for the securitization markets
    - For these reasons, the Consultation includes questions to allow for comments on these areas

Triggers: We Begin with the ISDA Triggers

- Consultation proposes **six triggers** that would signal the conversion from LIBOR ("Benchmark") to a new reference rate
- The first two triggers match ISDA's triggers for derivatives

Critical takeaway from the ISDA triggers is that they assume a permanent cessation of LIBOR and will require the market to move to the new replacement rate once LIBOR has ceased

The ISDA Triggers

1. **A public statement** or publication of information **by or on behalf of the administrator** of the Benchmark announcing **that such administrator has ceased or will cease to provide the Benchmark permanently or indefinitely**, provided that, at the time of the statement or publication, there is no successor administrator that will continue to provide the Benchmark.
2. **A public statement** or publication of information **by the regulatory supervisor for the administrator** of the Benchmark, the central bank for the currency of the Benchmark, an insolvency official with jurisdiction over the administrator for the Benchmark, a resolution authority with jurisdiction over the administrator for the Benchmark or a court or an entity with similar insolvency or resolution authority over the administrator for the Benchmark, which states **that the administrator of the Benchmark has ceased or will cease to provide the Benchmark permanently or indefinitely**, provided that, at the time of the statement or publication, there is no successor administrator that will continue to provide the Benchmark.

Triggers: Pre-Cessation

- The remaining four triggers contemplate a transition to a new reference rate **in the absence of a permanent cessation** of LIBOR and are referred to as **"pre-cessation" triggers**
- The first three of these pre-cessation triggers are intended to describe situations that signal a meaningful disruption or an unannounced stop to LIBOR and include significant events that are both observable and objective

Pre-Cessation Triggers

3. **Trigger Signals the Unannounced Stop to LIBOR**. A Benchmark rate is not published by the Benchmark administrator for five consecutive business days and such failure is not the result of a temporary moratorium, embargo or disruption declared by the Benchmark administrator or by the regulatory supervisor for the Benchmark administrator.
4. **Trigger Signals a Change in the Quality of LIBOR**. A public statement or publication of information by the administrator of such Benchmark that it has invoked or will invoke, permanently or indefinitely, its insufficient submissions policy.
5. **Trigger Reflects Regulator View that LIBOR Is No Longer Representative**. A public statement by the regulatory supervisor for the administrator of the Benchmark [or another regulator or Governmental Authority with jurisdiction over the Designated Transaction Representative] announcing that such Benchmark is no longer representative or may no longer be used.
6. **The Asset Replacement Percentage is greater than [50]%**, as reported in the most recent servicer report (see next slide).

Triggers: Asset Replacement Percentage

- **Trigger 6 addresses the mismatch that could occur if LIBOR-based assets and liabilities do not convert to the same replacement rate at the same time**

- **This trigger introduces the concept of the Asset Replacement Percentage (ARP)**, which measures, by principal balance, the percentage of underlying assets that have moved to the new replacement rate

  - "**Asset Replacement Percentage**" (ARP) means, on any date of calculation, a fraction (expressed as a percentage) where the numerator is the outstanding principal balance of the assets that were indexed to [the][any] Replacement Benchmark [for the Relevant Tenor] as of such calculation date and the denominator is the outstanding principal balance of the assets as of such calculation date

  - In the Consultation, if the ARP is greater than 50% (meaning that more than 50% of the underlying assets are now using the new reference rate), this would trigger the securities to move to the new reference rate

Replacement Benchmark and Benchmark Waterfall

- Once a trigger event occurs, the transition away from LIBOR to a new rate (which is referred to in the Consultation as the "Replacement Benchmark") will occur

- The Replacement Benchmark Waterfall in the Consultation lays out the priority of rates to use at the time of transition

- As indicated in the ARRC timeline, the ARRC estimates that a term structure for SOFR (which is currently only quoted on an overnight basis) should be completed by the end of 2021

Securitizations Replacement Benchmark Waterfall
Step 1: Term SOFR
Step 2: Compounded SOFR
Step 3: Replacement rate recommended by the Relevant Governmental Body (the ARRC)
Step 4: Replacement rate in then-current ISDA Definitions
Step 5: Replacement rate proposed by the Designated Transaction Representative

Replacement Benchmark Waterfall Explained

- Per the Replacement Benchmark Waterfall:
    1. **Term SOFR**. If a term SOFR is published at the time of transition then that would be the Replacement Benchmark
    2. **Compounded SOFR**. If SOFR only exists as an overnight rate (i.e., there is no term structure available), the Replacement Benchmark would be the overnight SOFR compounded over the particular term of the contract (i.e., one-month, three-month, etc.)
    3. **Replacement rate recommended by the Relevant Governmental Body (the ARRC)**. In the event that SOFR is not available at all, the rate would then be the rate recommended by the Relevant Governmental Body (e.g., the ARRC) at that time
    4. **Replacement rate in then-current ISDA Definitions**. If a Relevant Governmental Body rate is unavailable, the rate would then be what is recommended in the ISDA Definitions (inclusive of the embedded fallbacks contained in the definitions)
    5. **Replacement rate proposed by the Designated Transaction Representative**. In the very remote scenario in which none of the above rates is available, the Consultation discusses what would happen and the options available in greater detail

Replacement Benchmark Spread and Spread Waterfall

- Given the key differences between LIBOR and SOFR (as discussed earlier in this presentation), the transition from LIBOR will require a spread adjustment to produce more comparable rate levels and not lead to value transfer
  - The Consultation provides for a spread adjustment to be included in the determination of any Replacement Benchmark
  - The particular spread adjustment to be used is selected at the time the Replacement Benchmark is identified

Securitizations Replacement Benchmark Spread Waterfall
Step 1: Spread recommended by Relevant Governmental Body (ARRC)
Step 2: Spread in fallbacks for derivatives in ISDA Definitions

- The first step of the proposed waterfall is a spread adjustment selected, endorsed, or recommended by the Relevant Governmental Body (the ARRC)
  - This would apply to the first 3 steps of the Replacement Benchmark waterfall
- If there is not a spread adjustment available from the ARRC, the second step is a spread adjustment applicable to fallbacks for derivatives that ISDA anticipates implementing in its definitions

Reviewing the Consultation Questions

The Consultation Questions: Your Input Is Vital

- The Consultation contains **18 questions including several with multiple parts (31 questions in total)**
- The questions are divided along the three key areas of the Consultation:
  - Triggers
  - Replacement Benchmark Waterfall
  - Replacement Benchmark Spread Waterfall
- The Consultation also contains general questions as well as questions that allow for comments on areas that may not have been considered
- In what follows we provide a summary of some of the key questions contained in the Consultation

Foundational Question

Question 1 on Page 6: *Which Securitization asset classes are you referring to in your response to this consultation if limited to only certain asset classes? If there are particular features of these asset classes that shape your response to the questions in this survey, please describe them to the extent possible?*

- The Securitization Consultation and its proposed triggers, replacement benchmark, and replacement benchmark spread (collectively the fallback language) encompass a significant variety of securitized products

- Question 1 asks respondents to identify which asset classes they are referring to in their response (if limited to certain asset classes), and is meant to better understand any concerns and whether those concerns are particular to an individual asset class or apply broadly across the securitization market

Securitization Operational Challenges – 30-Day Transition Period

Question 2 on Page 7: *The ISDA triggers contemplate a permanent cessation of LIBOR as of a date certain which may be announced in advance (the "Cessation Date"), at which point the transition from LIBOR to SOFR would occur. As there may be operational challenges for securitizations as both assets and liabilities will have to be transitioned, some have asked for the ability to transition in advance of the Cessation Date in order to address any operational issues that may arise. Specifically, the Designated Transaction Representative (as defined in Appendix I) will have the ability to pick one date within a 30-day period prior to the Cessation Date to facilitate an orderly transition. Do you feel the inclusion of this ability to transfer prior to the Cessation Date is needed? If so, please explain the specific, critical and tangible needs that support its inclusion?*

- Question 2 asks whether securitizations – with both assets and liabilities to consider – should allow for the ability to transition in advance of the Cessation Date, selecting one date within the 30-day period prior to the Cessation Date in order to address any operational issues that may arise

Question 4 on Page 10: *Should the proposed securitization fallback language permit the Designated Transaction Representative to transition the securities after a trigger has occurred but before the Benchmark Replacement Date? Should any limitations be placed on its use? Should there be a limited date range (e.g., 60 days) prior to the Benchmark Replacement Date in which this could be used? Should the Designated Transaction Representative be limited in the circumstances under which it could elect to utilize the additional time? If so, what standard should be utilized to assess whether the additional time is necessary? In each case, please explain why.*

- Question 4 asks whether the DTR should be given discretion to transition the securities at any time between the cessation announcement date and that actual cessation (i.e., the Cessation Date)

Addition of Pre-Cessation Triggers to ISDA Triggers

Question 3(a): General Thoughts on Pre-Cessation Triggers. *Should fallback language for Securitizations include any of the pre-cessation triggers (clauses (3), (4), (5) and (6) of the Benchmark Discontinuance Event definition)? If so, which ones? Also, please identify any pre-cessation triggers that you do not believe should be utilized for a particular securitization product and explain why.*

Question 3(b): If any concerns, are they focused on differences between the securitization triggers and the two core ISDA triggers or do they relate specifically to the pre-cessation triggers themselves. *Please indicate whether any concerns you have about these pre-cessation triggers relate to the differences between these securitization triggers and those for standard derivatives or whether your concerns relate specifically to the pre-cessation triggers themselves.*

Question 3(c)**: **Do you have any concerns about the Asset Replacement Percentage Trigger? *If you believe that the pre-cessation trigger in clause (6) (Asset Replacement Percentage) should not be retained, please note any specific concerns leading to this conclusion. If you believe that it should be retained, are there any changes you believe should be made to this trigger? Please explain.*

Question 3(d): Efficacy of Asset Replacement Percentage. *If you believe the pre-cessation trigger in clause (6) (Asset Replacement Percentage) should be retained, how would you address concerns that it could result in a transfer of value in a transaction where the Designated Transaction Representative has the ability to change the benchmark used on the underlying assets and, as a result, determine the timing of this pre-cessation trigger? Are there other changes that should be made to the Asset Replacement Percentage trigger? Note that this trigger relates to a mismatch between the securities and the Securitization assets that results from changes in the assets. A mismatch may also arise from a change in the securities due to a trigger event under these fallback provisions. Any concerns with the latter scenario can be addressed in responses to Question 16.*

Question 3(e): Asks whether there are other ways beyond pre-cessation triggers to address asset/liability mismatches. *If pre-cessation triggers are not included, are there options available to market participants to manage the potential risks involved in continuing to reference a Benchmark in the circumstances contemplated by each of these pre-cessation triggers?*

Replacement Reference Rate Questions: Compounded SOFR

Questions 6(a) thru 6(c) on Page 13:

- ***6(a): Should Compounded SOFR be the second step in the waterfall?*** *Would this preference be influenced by whether ISDA implements fallbacks referencing Compounded SOFR or overnight SOFR?*

- ***6(b): Compounding in Arrears or in Advance.*** *If you believe that Compounded SOFR should be included, which compounding period is preferable ("in arrears" or "in advance")? Please explain why. Would this preference be influenced by whether ISDA implements fallbacks referencing Compounded SOFR "in arrears" or "in advance"? Please explain whether your preference is based on operational concerns in implementing a particular approach or on economic concerns.*

- ***6(c): Who Is Responsible for the Calculations?*** *If it was necessary to calculate Compounded SOFR and a third party was not available to perform those calculations, are there parties to the Securitization transactions with sufficient resources to perform those calculations accurately and efficiently? Are there other considerations relating to the calculation of Compound SOFR that would make it an undesirable Replacement Benchmark without the availability of a third-party provider?*

No SOFR-Based Fallback Rate and Spread Adjustment

No SOFR-Based Fallback Rates

- Question 8 on Page 13 contemplates a future circumstance where there is no SOFR-based fallback rate and asks whether the replacement rate determined by the Relevant Governmental Body (Step 3 in the Replacement Benchmark waterfall) is the best alternative at this level of the waterfall

- Question 9 on Page 14 asks if there is no SOFR-based fallback rate and the Relevant Governmental Body has not recommended a replacement rate, is the fallback for SOFR-linked derivatives set forth in the ISDA definitions the best alternative at this level of the waterfall and whether that fallback rate is appropriate if ISDA definitions only include overnight fallback rates

Replacement Benchmark Spread

- Question 11 on Page 15 asks if there are concerns if a spread adjustment was utilized with cash products that is calculated by a spot rate comparison of the difference between LIBOR and the Replacement Base rate at the time of conversion and should this option be included in the spread waterfall? **It currently is not.**

- Question 12 on page 16 asks whether the ARRC should recommend a spread adjustment that could apply to cash products, including securitizations. Note that the Securitization Benchmark Spread Waterfall is two-fold – the 1st being a Spread recommended by a Relevant Governmental Body and 2nd being the Spread in fallbacks for derivatives in the ISDA definitions

Responsibility for Decision Making and Calculations

Question 14(a): *What type of institution can and should take on the responsibility to (i) determine whether the proposed triggers have occurred, (ii) select screens where reference rates or spreads are to be found, (iii) make calculations of a rate or spread in the absence of published screen rates, (iv) interpolate term SOFR if there is a missing middle maturity and/or (v) elect to cause an early transition under the proviso to the definition of Benchmark Replacement Date?*

Question 14(b): *Whether as issuer, sponsor, servicer or calculation agent, would your institution be willing to (i) determine whether the proposed triggers have occurred, (ii) select screens where reference rates or spreads are to be found, (iii) make calculations of a rate or spread in the absence of published screen rates, (iv) interpolate term SOFR if there is a missing middle maturity and/or (v) elect to cause an early transition under the proviso to the definition of Benchmark Replacement Date?*

- Questions 14(a) and 14(b) on page 16 and 17 ask the general questions as to what type of institution should take on the responsibility to make decisions as to triggers, post/calculate reference rates or spreads, interpolate term SOFR if missing a middle maturity or elect to cause an early transition. In addition it asks whether an issuer, sponsor, servicer or calculation agent would be willing to do the same.

General Feedback

Question 15: *Is there any provision in the proposal that would significantly impede Securitization issuances? If so, please provide a specific and detailed explanation.*

Question 16: *Given the fallback language for the Securitization and the underlying assets may operate independently, please identify any sources of misalignment between those components that are not addressed in the consultation.*

***Question 17**:* *Are there specific operational challenges that implementing the proposed fallback language might create for securitizations? If so, what are those challenges and under what circumstances might they occur? How might they be mitigated?*

Question 18: *Please provide any additional feedback on any aspect of the proposal.*

Next Steps

Next Steps

- Please submit responses to the Consultation by email to the ARRC Secretariat (arrc@ny.frb.org) no later than February 5, 2019
  - More details on the submission process can be found in the Consultation
  - **General feedback is welcome**, but it will be most helpful if you address the specific questions in the consultation
  - Importantly, note that, unless you clearly specify otherwise, your Consultation feedback will be **posted with attribution**
- In addition to company-level responses, CREFC and SFIG, separately, plan on responding to the Consultation as Associations
  - Please contact CREFC or SFIG if you would like to participate in formulating our respective responses
- Following the consultation, the ARRC will recommend fallback language for new Securitizations for voluntary adoption in the marketplace
- The expectation is that market participants will choose whether and when to begin using the Securitization fallback language in new issuances of LIBOR-based transactions, as they deem appropriate – the goal here is to not continue to make legacy loans and securities
- Please see the appendices that follow: one lists all of the questions in this consultation and the other provides a timeline of the ARRC's progress to date

Appendices

The Consultation Questions: Triggers

Category	Question
General	**Question 1:** Which securitization asset classes are you referring to in your response to this consultation if limited to only certain asset classes? If there are particular features of these asset classes that shape your responses to the questions in this survey, please describe them to the extent possible.
Triggers	**Question 2:** The ISDA triggers contemplate a permanent cessation of LIBOR as of a date certain which may be announced in advance (the "Cessation Date"), at which point the transition from LIBOR to SOFR would occur. As there may be operational challenges for securitizations as both assets and liabilities will have to be transitioned, some have asked for the ability to transition in advance of the Cessation Date in order to address any operational issues that may arise. Specifically, the Designated Transaction Representative (as defined in Appendix I) will have the ability to pick one date within a 30-day period prior to the Cessation Date to facilitate an orderly transition. Do you feel the inclusion of this ability to transfer prior to the Cessation Date is needed? If so, please explain the specific, critical and tangible needs that support its inclusion?
	Question 3(a): Should fallback language for Securitizations include any of the pre-cessation triggers (clauses (3), (4), (5) and (6) of the Benchmark Discontinuance Event definition)? If so, which ones? Also, please identify any pre-cessation triggers that you do not believe should be utilized for a particular securitization product and explain why.
	Question 3(b): Please indicate whether any concerns you have about these pre-cessation triggers relate to the differences between these securitization triggers and those for standard derivatives or whether your concerns relate specifically to the pre-cessation triggers themselves.
	Question 3(c): If you believe that the pre-cessation trigger in clause (6) (Asset Replacement Percentage) should not be retained, please note any specific concerns leading to this conclusion. If you believe that it should be retained, are there any changes you believe should be made to this trigger? Please explain.
	Question 3(d): If you believe the pre-cessation trigger in clause (6) (Asset Replacement Percentage) should be retained, how would you address concerns that it could result in a transfer of value in a transaction where the Designated Transaction Representative has the ability to change the benchmark used on the underlying assets and, as a result, determine the timing of this pre-cessation trigger? Are there other changes that should be made to the Asset Replacement Percentage trigger? Note that this trigger relates to a mismatch between the securities and the Securitization assets that results from changes in the assets. A mismatch may also arise from a change in the securities due to a trigger event under these fallback provisions. Any concerns with the latter scenario can be addressed in responses to Question 16.
	Question 3(e): If pre-cessation triggers are not included, are there options available to market participants to manage the potential risks involved in continuing to reference a Benchmark in the circumstances contemplated by each of these pre-cessation triggers?
	Question 4: Should the proposed securitization fallback language permit the Designated Transaction Representative to transition the securities after a trigger has occurred but before the Benchmark Replacement Date? Should any limitations be placed on its use? Should there be a limited date range (e.g., 60 days) prior to the Benchmark Replacement Date in which this could be used? Should the Designated Transaction Representative be limited in the circumstances under which it could elect to utilize the additional time? If so, what standard should be utilized to assess whether the additional time is necessary? In each case, please explain why.

The Consultation Questions: Replacement Benchmark Waterfall

Category	Question
Replacement Benchmark Waterfall	**Question 5(a):** If the ARRC has recommended a forward-looking term rate, should that rate be the primary fallback for the securities referencing LIBOR even though derivatives are expected to reference overnight versions of SOFR? Please explain why.
	Question 5(b): Is there a specific reason that the securitization market should first fall back to forward-looking term SOFR instead of another rate? Please explain why.
	Question 5(c): Is the use of an Interpolated Period appropriate in the securitization markets? Please explain any limitations that should be applied to the use of an Interpolated Period.
	Question 5(d): In the event a Replacement Benchmark is determined other than under Step 1 of the waterfall, should the waterfall provide that the Replacement Benchmark be changed in the future as soon as a rate can be established under Step 1 of the waterfall?
	Question 6(a): Should Compounded SOFR be the second step in the waterfall? Would this preference be influenced by whether ISDA implements fallbacks referencing Compounded SOFR or overnight SOFR?
	Question 6(b): If you believe that Compounded SOFR should be included, which compounding period is preferable ("in arrears" or "in advance")? Please explain why. Would this preference be influenced by whether ISDA implements fallbacks referencing Compounded SOFR "in arrears" or "in advance?" Please explain whether your preference is based on operational concerns in implementing a particular approach or on economic concerns.
	Question 6(c): If it was necessary to calculate Compounded SOFR and a third party was not available to perform those calculations, are there parties to the Securitization transactions with sufficient resources to perform those calculations accurately and efficiently? Are there other considerations relating to the calculation of Compound SOFR that would make it an undesirable Replacement Benchmark without the availability of a third party provider?
	Question 7: As noted, this consultation does not include Spot SOFR as a third step in the waterfall. Do you believe that Spot SOFR is an appropriate fallback reference rate for Securitization contracts or should the second step in the replacement rate waterfall be Compounded SOFR , after which the replacement rate would be, first, recommended by the Relevant Governmental Body, second, default to then-current ISDA Definitions, and third, proposed by the Designated Transaction Representative?

The Consultation Questions: Replacement Spread Waterfall and General / Other

Category	Question
Replacement Spread Waterfall	**Question 11**: Are there any concerns if a spread adjustment was utilized with cash products that was calculated by a spot rate comparison of the difference between LIBOR and the Replacement Base Rate at the time of conversion? Should this option be included in the spread waterfall? If so, where?
	Question 12: Do you believe that the ARRC should consider recommending a spread adjustment that could apply to cash products, including Securitizations?
	Question 13(a): Is a spread adjustment applicable to fallbacks for derivatives under the ISDA definitions appropriate as the second priority in the spread waterfall? Please explain why.
	Question 13(b): If the ARRC has recommended a forward-looking term SOFR but has not recommended a corresponding spread adjustment under Step 1 above, do you believe that the ISDA spread adjustment described in Step 2 (which may be intended to apply to a different Replacement Base Rate) should apply to Securitizations? Please explain why.
	Question 13(c): Given that ISDA has not yet decided upon the spread calculation methodology (see Appendix III and preliminary results of the ISDA consultation), should Step 2 be excluded from the waterfall? Please explain why.
General / Other	**Question 14(a):** What type of institution can and should take on the responsibility to (i) determine whether the proposed triggers have occurred, (ii) select screens where reference rates or spreads are to be found, (iii) make calculations of a rate or spread in the absence of published screen rates, (iv) interpolate term SOFR if there is a missing middle maturity and/or (v) elect to cause an early transition under the proviso to the definition of Benchmark Replacement Date?
	Question 14(b): Whether as issuer, sponsor, servicer or calculation agent, would your institution be willing to (i) determine whether the proposed triggers have occurred, (ii) select screens where reference rates or spreads are to be found, (iii) make calculations of a rate or spread in the absence of published screen rates, (iv) interpolate term SOFR if there is a missing middle maturity and/or (v) elect to cause an early transition under the proviso to the definition of Benchmark Replacement Date?
	Question 15: Is there any provision in the proposal that would significantly impede Securitization issuances? If so, please provide a specific and detailed explanation.
	Question 16: Given the fallback language for the Securitization and the underlying assets may operate independently, please identify any sources of misalignment between those components that are not addressed in the consultation.
	Question 17: Are there specific operational challenges that implementing the proposed fallback language might create for securitizations? If so, what are those challenges and under what circumstances might they occur? How might they be mitigated?
	Question 18: Please provide any additional feedback on any aspect of the proposal.

ARRC Timeline: Originally Convened in 2014, Significant Progress to Date

Paced Transition Plan

- Oct. – ARRC **Paced Transition Plan** adopted
- ✓ Apr. – New York Fed/OFR began **publishing SOFR**
- ✓ May – **CME launched SOFR futures**
- ✓ Jul. – **LCH began clearing SOFR swaps**
- ✓ Fannie Mae issued **first SOFR-based FRN**
- ✓ Oct. – **CME began clearing SOFR swaps using SOFR PAI/discounting**
- 2019 – Continue to build **SOFR-linked cash and derivatives instruments**
- Q1 **–** CCPs to begin allowing a **choice between clearing new or modified swap contracts in current PAI/ discounting environment or SOFR for PAI/discounting**
- Q2 – CCPs to **no longer accept new swap contracts for clearing with EFFR as PAI and discounting**
- EOY – Create a **forward-looking SOFR term reference rate**

2016 | 2017 | 2018 | TODAY | 2019 | 2020 | 2021

Key ARRC and Other Developments

- May – ARRC's **Interim Report and Consultation** published
- Jun. – **ARRC selected SOFR** as its recommended alternative to USD LIBOR
- Jul. – FCA Bailey said **panel banks will not be compelled to submit to LIBOR past 2021**
- Mar. – ARRC's **second report** published
- **ARRC reconstituted** with expanded membership
- Jul. – FCA, CFTC, FRB regulator **speeches highlighting need to prepare for transition**
- ARRC issued **guiding principles for fallback contract language**
- S&P announced **SOFR is an "anchor money market reference rate"**
- Sept. – ARRC issued **consultations on fallback language for FRNs and syndicated loans**
- Dec. – ARRC issues **consultations on fallback language for bilateral loans and securitizations**
- ARRC is seeking to produce an **indicative SOFR-based term reference rate** based on futures data to help promote market familiarity with the term rate
- ARRC expects to produce **final recommendations for safer contract language in FRNs, business loans, and securitizations**

Key
- ● Complete
- ○ Anticipated Completion
- ✓ Completed ahead of schedule

Thank You