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September 24, 2019

Federal Reserve Board
Alternative Reference Rate Committee
Consumer Products Working Group
Submitted via Email

Dear ARRC Securitization Working Group:

On behalf of the Farm Credit Banks (FC Banks), CoBank, ACB appreciates the opportunity to comment on the Alternative Reference Rate Committee (ARRC) Consultation - Regarding More Robust LIBOR Fallback Contract Language for New Closed-End, Residential Adjustable Rate Mortgages (ARMs).

The FC Banks are government-sponsored enterprises of the United States that provide loans, leases, and financial services to rural American farmers, ranchers, and agricultural, aquatic, infrastructure cooperatives and providers, across all fifty states and the Commonwealth of Puerto Rico.[1] The FC Banks are: (1) AgFirst Farm Credit Bank; (2) AgriBank, FCB; (3); CoBank, ACB and (4) Farm Credit Bank of Texas. Together, the FC Banks are among the leading lenders to rural America; they provide credit for rural housing, agricultural processing and marketing activities, utilities providers, and certain farm-related businesses.

Congress created the FC Banks, as part of the Farm Credit System (FCS), to provide a permanent, stable source of credit and related services to support rural America and improve the lives of its residents. Specifically, the FC Banks, as part of the FCS, were created “to accomplish the objective of improving the income and well-being of American farmers and ranchers by furnishing sound, adequate, and constructive credit and closely related services to them, their cooperatives, and to selected farm-related businesses necessary for efficient farm operations”[2]. Since its creation, CoBank was granted authorities to provide credit to rural infrastructure providers, who are vital to creating successful businesses and healthy rural communities.

[1] See generally 2017 Annual Report on the Farm Credit System by the Farm Credit Administration.
[2] 12 U.S.C. § 2001(a)

The FC Banks and their associations hold rural residential real estate loans as part of their mission. As of June 30, 2019, the FC Banks hold just under $7.4 billion of rural housing loans. Before addressing the questions in the ARRC LIBOR ARMs Consultation, the FC Banks would like to provide several general comments related to the transition from USD LIBOR to an alternative reference rate.

First, the FC Banks would like to compliment the previous ARRC fallback language recommendations in developing a reasonably coordinated approach to the fallbacks language across cash products. We have also asked the ISDA in our response to their consultations to work to align key aspects of the fallback language for USD LIBOR bi-lateral derivative with the ARRC cash products recommendations. In our view a lack of coordination could create needless substantial financial basis risks to all financial institutions if, for example, triggers for different types of instruments are invoked at varying times or alternative reference rates (including spread adjustments) are inconsistent. The FC Banks would like to encourage the ARRC to take a leadership role in encouraging greater coordination with other working groups on these issues.

Additionally, the FC Banks are also concerned that regulators do not have a full appreciation of the complexity, expense and legal ramifications related to the transition to alternative rate indexes. It would be regrettable if global and domestic financial markets encounter a major systemic event related to implementation to an alternative reference being done too quickly.

Finally, the FC Banks would like to express their concern related to the ARRC's white paper on "Using an Average of SOFR to Build an Adjustable-Rate Mortgage Product for Consumers" published July 11, 2019. The paper discussed the possibility of utilizing SOFR averages "in advance" as a possible fallback index. The FC Banks are concerned that applying this possible alternative reference rate on one class of loans could create significant volatility in earnings during periods of monetary activity. Additionally, the effect of the lagging index could also lead to ineffectiveness of hedges and create issues with hedge accounting. As stated previously, the FC Bank strongly advocate for coordinated fallback language across derivative and all cash market products.

Attached are the FC Banks' current responses to the specific questions put forth in the ARRC ARM Consultation. The responses have been developed jointly by the FC Banks. This feedback represents our current thoughts and might be subject to changes as we see developments in the markets and regulatory environment.

The FC Banks welcome the opportunity to discuss our comments with you. Please contact the following staff with any comments or questions:

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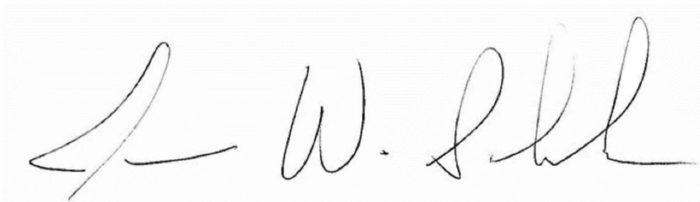
Sincerely,



James W. Shanahan, CFA
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ARRC CONSULTATION REGARDING MORE ROBUST LIBOR FALLBACK CONTRACT LANGUAGE FOR NEW CLOSED-END, RESIDENTIAL ADJUSTABLE RATE MORTGAGES

Question 1: Should fallback language for ARMs include either of the pre-cessation triggers (triggers 4(G)(ii) and 4(G)(iii))? If so, which ones?

FC Banks response: The FC Banks would recommend that the trigger in 4(G)ii of the fallback language be structured in the same manner as the pre-cessation fallback language in the previously release of ARRC recommended fallbacks. As for the 4(G)(iii) trigger, we do not think that it needs to be included, since any legal prohibition of the use of LIBOR as an index by federal or state laws or regulations would supersede any provision in the fallback language. This issue is probably best handled in a risk disclosure.

Question 2: Please indicate whether any concerns you have about these pre-cessation triggers relate to differences between these triggers and those for standard derivatives or relate specifically to the pre-cessation triggers themselves.

FC Banks response: The FC Banks have concerns about a lack of coordination between cash instruments as well as derivative transactions with respect to fallback language triggers. As stated in the Guiding Principal and Scope of Work for the ARRC Consumer Products publish by the Work Group, there may be instances were retail consumers have unique needs, but the 4(G)(i) and 4(G)(ii) could be replaced with triggers consistent with the previously recommended ARRC trigger language and result in substantially the same effect. Again, we do not see the need to introduce new language that is inconsistent with other products and create additional uncertainty unless it addresses a clear unique requirement that needs to be addressed for retail consumers.

Question 3: If pre-cessation triggers are not included, what options would be available to market participants to manage the potential risks involved in continuing to reference a Benchmark whose regulator has publicly determined that it is not representative of the underlying market?

FC Banks response: The FC Banks endorse the use of the pre-cession trigger being included in the ARRC recommended fallback language for other cash products. If pre-cessation triggers are not utilized, a lender could address the issue by refinancing or amending the loans. This would be very time intensive and costly.

Question 4: The ARM language proposed uses simplified language in an effort to be more comprehensible for the consumer market. Is the simplified language appropriate or are there concerns with the language not matching ISDA or other cash product language precisely?

FC Banks response: Again, the FC Banks continue to encourage the ARRC to coordinate fallback language provisions and other items within the recommendation. To that end, the FC Banks do not feel that the simplified language was needed and could create wider room for interpretation. Consequently, we would encourage the ARRC make the language as consistent as possible between all products.

Question 5: Is the replacement index determined by the Federal Reserve Board, the Federal Reserve Bank of New York, or a committee endorsed or convened by the Federal Reserve Board or the Federal Reserve Bank of New York the best choice as the first step of the waterfall? Why or why not?

FC Banks response: The FC Banks would prefer that the ARRC adopt an alternative reference rate index waterfall consistent with the ARRC recommendation for Bilateral Loans.

Question 6: As noted in the narrative, the ARRC has committed to recommending spread adjustments for cash products that reflect the general difference between various tenors of LIBOR and SOFR. In addition, the ARRC has committed to seeing all-in, "spread-adjusted" rates published for use in cash products (e.g., a SOFR-based spread-adjusted replacement index for 1-year LIBOR). Should the ARRC recommend a spread adjustment for LIBOR ARMs and other consumer products, and should the corresponding spread-adjusted rate be the replacement index for the LIBOR ARMs?

FC Banks response: The FC Banks would prefer that the ARRC adopt a spread adjustment waterfall consistent with the ARRC recommendation for Bilateral Loans.

Question 7: As noted in the narrative, in addition to recommending SOFR, the ARRC may recommend forward-looking term SOFR rates if it is satisfied that a robust, IOSCO-compliant term rate that meets its criteria can be produced. If the ARRC recommends forward-looking term rates (e.g., 1-month, 3-month, 6-month, etc.) and a corresponding spread adjustment, should a spread-adjusted term rate be the replacement index for LIBOR ARMs, or would a spread-adjusted average (simple or compounded) of SOFR be more appropriate? Please provide support for your answer.

FC Banks response: The FC Banks support the movement to forward-looking term SOFR including the spread adjustment. The creation of a forward-looking term SOFR would the best solution for the replacement rate for LIBOR since it would function in a similar manner to current LIBOR and would substantially increase the

pace of the adoption the LIBOR alternative rate. The FC Banks have been working with its customers for several years on the transition from LIBOR and feel the move to a daily SOFR acts as an impediment to the transition. Further, the determination of any spread adjustment should be consistent with other ARRC fallback recommendations, such as the Bilateral Loans.

Question 8: Should the Note Holder have the responsibility as the 2nd and last step of the waterfall? Why or why not?

FC Banks response: Again, the FC Banks would prefer that the ARRC adopt an index waterfall consistent with the ARRC recommendation for Bilateral Loans.

Question 9: Should the Note Holder have the ability to make adjustments (positive or negative) to the loan's margin to more closely approximate LIBOR at the time of replacement? Why or why not? If you do not believe the Note Holder should make adjustments to the loan's margin, and potential replacement indices diverge from the value of the current Index, what provision or step should be taken to preserve that consistency?

FC Banks response: The FC Banks would like to see a more determinist methodology, such as the spread adjustment contained in the ARRC Bilateral Loan recommended fallback. This would provide a consistent approach across different products and markets, which might act as a risk mitigate to potential litigation risks.

Question 10: If the Note Holder is a trust (for example, as may occur in private label MBS), is there some entity other than the Note Holder that should be responsible for identifying the Replacement Index if Step 1 of the waterfall fails? Please provide sufficient rationale for your answer.

FC Banks response: If the ARRC recommendation for the fallback language was structured similar to the ARRC Bilateral Loan recommendation, this issue would not be as significant. That said, if the language requires the Note Holder to act in a certain capacity, their ownership structure should not change the requirement.

Question 11: Will this language have unintended consequences not considered by the ARRC working group, such as title insurance restrictions, state law endorsement or filing restrictions, etc.? If so, please explain and provide information about why this language would present challenges. If there are concerns with this proposed language, please be sure to specify if concerns relate to this proposed language, or index replacement language in general.

FC Banks response: The FC Banks do not have a specific comment at this time.

Question 12: Is there any provision in the proposal that would significantly impede ARM originations? If so, please provide a specific and detailed explanation.

FC Banks response: The FC Banks feel the lack of consistency with other ARRC recommended fallback language provisions and the ISDA proposal could be perceived to create additional basis risks and thus could affect the demand and/or pricing for consumer products.

Question 13: Please provide any additional feedback on any aspect of the proposal.

FC Banks response: The FC Banks do not have a specific comment at this time.