February 5, 2019

By Email (arrc@ny.frb.org)

Alternative Reference Rates Committee (ARRC)

Re: Consultation Response – Bilateral Business Loans

Compass Bank d/b/a BBVA Compass hereby submits responses to certain questions in the ARRC Consultation Regarding More Robust LIBOR Fallback Contract Language for New Originations of LIBOR Bilateral Business Loans, as follows.

**Question 1.** If the ARRC were to adopt one or more sets of bilateral business loan fallback language, which one or both of the recommended provisions (i.e., amendment approach and/or hardwired approach), in your view, is an appropriate policy? If you believe the amendment approach is more appropriate at present, what specific information (for instance, existence of term SOFR) would you need in order to get comfortable eventually adopting a hardwired approach? Why?

**Response to Question 1:**

We believe that the ARRC should recommend language based on the amendment approach, subject to our comments below in response to Question 2. We recognize the appeal of a finely-tuned approach that would mesh seamlessly with the underlying contract, but we believe that the hardwired approach might not provide more certainty in practice. Without a clear timeline for published SOFR-based forward-looking term rates or compounded rates, or officially-endorsed spread adjustments for such rates, the “waterfalls” could still lead to a party’s discretionary selection of an alternative rate or a stalemate between the parties. In addition, such a finely-tuned approach could turn out less robust than desired if there were unexpected developments or if an institution attempted to apply the same language across a range of different contracts.

Accordingly, we believe that the ARRC should recommend language based on the amendment approach. If the ARRC recommends language now for a hardwired approach, language for an amendment approach should be recommended as an alternative.
Response to Question 2:

There are at least two situations for which the proposed fallback approaches, as originally drafted, would be problematic: (1) where loans are documented on an internal platform with standardized templates designed to be relatively short and simple and geared for smaller commercial transactions, and (2) where loan documents do not include an express alternative base rate (i.e., one tied principally to the prime rate) that would apply in a LIBOR cessation or other “Benchmark Availability Period” scenario.

Loans Documented on Platforms Geared for Smaller Transactions:

For loans documented on an internal documentation platform that uses relatively short and simple language, the lengthy language proposed in the consultation could create unnecessary apprehension among borrowers and even hinder originations. We note that the language in this consultation was based on the earlier consultation regarding syndicated loans, for which long and complex loan documents are typical.

We believe that for these and similar categories of loans, lenders likely will find it necessary to render the concepts in the ARRC’s recommended language into shorter and simpler language that is more appropriate to the context.

For these reasons, it would be helpful if the ARRC were to acknowledge that parties may need to adapt the specific language in its recommendations in appropriate circumstances, such as those described above.

Loans Without an Express Alternative Base Rate (ABR) Tied to the Prime Rate:

Unlike syndicated loan agreements, bilateral loan agreements may not include a prime rate linked “alternative base rate” or “ABR” that could serve as a backstop in the absence of LIBOR. This may be the case, for example, in bilateral loans of the variety discussed above geared for smaller customers.

For transactions without a prime rate linked ABR, the “Benchmark Unavailability Period” provisions in both of the proposed approaches obviously would be inapplicable. It would be helpful if the ARRC’s recommendations specifically acknowledged that the “Benchmark Unavailability Period” provisions are optional, for example by putting them in square brackets with an explanatory footnote. Note that we did not read the consultation as suggesting that all loans are expected to include a prime rate linked ABR. We believe that such an expectation could introduce unnecessary complexity in certain transactions and could hinder originations.

In addition, for loan transactions without a prime rate linked ABR, we would not expect the LIBOR fallback provisions (whether based on the amendment or the hardwired approach) to
include consent or veto rights with respect to a lender-selected fallback rate. More generally, for practical reasons, fallback provisions containing such consent or veto rights may be difficult to administer for various categories of loans, particularly those in large portfolios. Accordingly, we believe that in the ARRC’s final recommendations these consent or veto rights should continue to appear in square brackets, as they did in the consultation.

**Question 15.** For respondents that act as Lenders in the bilateral business loan market, would your institution be willing to (i) work with the Borrower to identify a new reference rate or spread adjustment, (ii) determine whether triggers have occurred, (iii) select screen rates where reference rates are to be found, (iv) interpolate LIBOR or term SOFR if there is a missing middle maturity, and (v) execute one-time or periodic technical or operational amendments to appropriately administer the replacement benchmark? Please respond to each and explain.

**Response to Question 15:**

With regard to item (iv), we believe that providing for interpolation could yield considerable complexity and present operational challenges.

**Question 17.** Is it necessary that any replacement rate and/or applicable spread adjustment be published on a screen by a third party? Why or why not?

**Response to Question 17:**

To serve the interests of transparency, market acceptance and risk mitigation for all parties, having both replacement rates and spread adjustments published by a third party would be highly preferable.

**Question 24.** Are there any provisions in the fallback language proposals that would significantly impede bilateral business loan originations? If so, please provide a specific and detailed explanation.

**Response to Question 24:**

Please refer to the response to Question 2, above. Originations could be impeded if the effect of the ARRC’s recommendations were to somehow create an expectation that lengthy and highly complex provisions be included in loans otherwise documented on relatively straightforward templates, or that all loans should expressly include an alternative base rate tied to the prime rate.