Consultation Response – Syndicated Business Loans

While our bank is a significant originator of, and participant in, syndicated business loans to C&I and CRE customers, the vast majority loans for which we act as agent bank are "club" transactions with only 1-5 additional lenders. Deals in which we are a participant are more evenly split between widely syndicated loans and club deals. We believe that the ARRC should consider whether different approaches should be recommended/adopted for widely syndicated transactions versus club transactions. In considering that approach, it is notable that the borrowers in club transactions are often not as sophisticated, or represented by as sophisticated of counsel, as those in the widely syndicated market, and therefore some of the triggers and the mechanics of amendment provisions may be difficult to explain/digest for them.

Question 1. If the ARRC were to adopt one or more sets of 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 hard-wired approach? Why?

> For the present, at least, the Amendment Approach is more appropriate. The existence of, and (ideally) relatively widespread adoption in loan documents of, Term SOFR is a necessary condition to the adoption of a hardwired approach. While it is easy to say that borrowers and lenders will simply approve the hardwired changes, we would suggest that the same potential for winners and losers is present as in the amendment approach in many situations given the lack of prepayment/refinancing fees in syndicated loans. This is more problematic on the bank side – since the borrower can still extract value in a borrower-friendly environment, while it is more difficult for the lenders to do so. Moreover, the appropriate amount and basis for determining the Replacement Benchmark Spread is too uncertain at this time, and likely will remain so until a significant number of loans begin using Term SOFR as a rate option.

Question 2(a). Should fallback language for business loans include any of the pre-cessation triggers (triggers 3, 4 or 5)? If so, which ones?

> In an Amendment Approach, pre-cessation triggers could be included. All of the suggested triggers would be acceptable in that context. Although we would prefer for the pre-cessation triggers not be included at all in a Hard Wired Approach, (4) and (5) would not be overly objectionable.

Question 2(b). 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.

In a Hard Wired Approach context, the concerns are both related to the triggers themselves and the fact that they may not match up with derivative triggers.

Question 2(c). 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 or a Benchmark permanently or indefinitely based on a number of submissions that the Benchmark's administrator acknowledges to be insufficient to allow for production in a standard manner?

While not ideal, given our book of mostly club transactions, if a significant disruption occurred, we would seek to either undertake consensual amendments quickly and/or rely on generic "unavailability" language and flip to Prime based loans for a short time until amendments could be agreed.

Question 3(a). Is an "opt-in" trigger appropriate to include? Why or why not?

We generally favor opt-in provisions, particularly if they do not contain specific time frames for making a transition. From an administrative agent perspective, such provisions have clear advantages in terms of spreading the load of amendments across a longer time period. One concern of opt in provisions is that system capabilities may not be fully on-line at a time that another agent bank (and the necessary other lenders in the group) decide to make the election. But, on balance, the opt in provisions seem beneficial.

Question 3(b). If you do believe an "opt-in" trigger should be included, do you prefer the approach in the hardwired proposal or the amendment proposal? Please explain.

We would be slightly more comfortable with the opt in provisions in an Amendment Approach, but can see their value in both approaches.

Question 4. Are there any other trigger events that you believe should be included for consideration? If yes, please explain.

No.

Question 5. If the ARRC has recommended a forward-looking term rate, should that rate be the primary fallback for syndicated loans referencing LIBOR even though derivatives are expected to reference overnight versions of SOFR? Please explain.

Yes. A relatively small number of the syndicated loans that we make/participate in are hedged through our bank, so there is not the need to match the approach used for derivatives in most cases. Further, even if derivatives generally reference overnight SOFR, we are confident that non-cleared (or even cleared) swaps will be available that reference Term SOFR and that counterparties to existing trades will be able to amend the trades to move to Term SOFR. Finally, even if Term SOFR is the primary fallback, lenders and borrowers can amend documents to include an overnight SOFR tranche of debt if needed for hedging purposes – especially in the smaller transactions we are generally part of.

Question 6. Should the administrative agent (by itself or with some other party) be able to eliminate certain interest period options if there are no equivalent SOFR terms available? If so, consider the following options: (i) the administrative agent (and/or some other party) may remove all interest periods for which there is not a published term rate or (ii) the administrative agent (and/or some other party) may remove only the interest periods for which there is not a published term rate and a term rate cannot be interpolated. Which of the options do you support? Why?

Yes. Option (i) would be our preference. It would be administratively very difficult for our bank to interpolate rates on our own for deals in which we act as agent and/or to develop a control to verify that another agent bank has correctly interpolated a rate. Published rates are necessary.

Question 7. Should "Compounded SOFR" be included as the second step in the waterfall? Why or why not? Would this preference be influenced by whether ISDA implements fallbacks referencing compounded SOFR or overnight SOFR?

No. The in arrears version would be operationally very difficult and would not serve the needs of our borrowers well either. If the rate is not fixed in advance, it might as well just be a daily floating rate from the borrower perspective. The historical in advance method would in many cases lead to artificially low rates to borrowers when interest rates have moved or are expected to move. Since interest periods can vary, generally from 1 to 6 months, and are chosen by the borrower, even in a declining interest rate environment, the borrowers would have an advantage.

Question 8. If you believe that Compounded SOFR should be included, would a Compounded SOFR in advance or Compounded SOFR in arrears be preferable for syndicated loans? Please explain.

N/A

Question 9. Is Overnight SOFR an appropriate fallback reference rate for syndicated loans or should the final step in the replacement rate waterfall be Compounded SOFR (after which the hardwired approach defaults to a streamlined amendment process)? Would this preference be influenced by whether ISDA implements fallbacks referencing compounded SOFR or overnight SOFR? Please explain.

Overnight SOFR would be a more appropriate final fallback, for the reasons stated above, regardless of whether ISDA implements compounded SOFR.

Question 10: Is it acceptable to fix one observation of Overnight SOFR as the reference rate for a loan lasting three months (or longer)? Would lenders refuse to offer longer-duration loans if they were priced over one Overnight SOFR observation? Please explain.

As a last resort, we could see interest periods being limited to one month and being based on a single Overnight SOFR observation (or historical Compound SOFR). Anything longer than one month raises too great of concerns regarding the pricing not being reflective of the bank's cost of funds for the period.

Question 11. Is there any another replacement rate that should be added to the hardwired approach waterfall before parties move to the streamlined amendment process? If so, what is the appropriate rate or rates and at which stage in the waterfall should they be applied?

Fed Funds plus a replacement spread could be a last waterfall before a streamlined amendment process.

Question 12. Do you believe that the ARRC should consider recommending a spread adjustment that could apply to cash products, including syndicated business loans?

It depends if other bodies have made recommendations. A regulatory recommendation would be ideal, and if one existed, an ARRC recommendation would not be appropriate. If an ISDA recommendation exists (as to the same rate and time), it would be good to posit a recommendation, but it would not

be good for the ISDA recommendation and the ARRC recommendation to ultimately come to different conclusions.

Question 13. Is a spread adjustment applicable to fallbacks for derivatives under the ISDA definitions appropriate as the second priority in the spread waterfall even if syndicated business loans may fall back at a different time or to a different rate from derivatives? Please explain.

Definitely not if it is based on a different rate. If it is done at a different time, it could be acceptable if that time is not more than a few months different from the switch in the loan.

Question 14. Is there any another spread adjustment that should be added to the hardwired approach spread waterfall before parties move to the streamlined amendment process? If so, what is the appropriate spread and at which stage in the waterfall should it be applied?

No.

Question 15(a). Under the amendment approach proposal, if parties are selecting a replacement rate through the amendment process, should the objection of the Required Lenders be by class (if applicable) (see clause (b) of the section titled "Effect of Benchmark Discontinuance Event" in Appendix I)? Why or why not?

No. The potential operational and administrative complexity of having different tranches with different interest rates and computation methods is a far greater risk than the lender interests in the different tranches being so out of line that they cannot agree on an approach.

Question 15(b). Under the amendment approach proposal, if parties choose to select a replacement rate through the "opt-in" amendment process, should the affirmative consent of the Required Lenders be by class (if applicable) (see clause (b) of the section titled "Effect of Benchmark Discontinuance Event" in Appendix I)? Is affirmative consent appropriate or should negative consent be considered instead? Please explain.

No. See above. Negative consent would be fine, and possibly preferred.

Question 16(a). Under the hardwired approach proposal, if parties must fallback to selecting a replacement rate through the amendment process because none of the options in the replacement rate waterfall are available, is the objection of the Required Lenders by a class appropriate (if applicable) (see clause (d) of the section titled "Effect of Benchmark Discontinuance Event" in Appendix II)? Why or why not?

No. See above.

Question 16(b). The hardwired approach proposal provides two bracketed options for a successful declaration of the "opt-in" amendment process - Required Lenders (typically a majority) vs. supermajority (2/3) of lenders (see clause (B) of the definition of "Benchmark Transition Determination" in Appendix II). What should be the standard affirmative lender voting threshold for consenting to the "opt-in"? Please explain.

This is an example of where widely syndicated and club transactions very well may have different "correct" answers. In a club deal, supermajority is more appropriate, as the number of lenders that need to respond is lower and concerns of individual lenders are more likely to be addressed by the agent bank and borrowers. In widely syndicated loans, required lenders is probably the better standard.

Question 17. For respondents that act as administrative agents in the syndicated 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 term SOFR if there is a missing middle maturity and, (v) execute one-time or periodic technical or operational amendments to allow the administrative agent to appropriately administer the replacement benchmark? Please respond to each and explain.

Majority for consent, but supermajority for negative consent. Although not all that relevant for our bank, requiring a supermajority of lenders to affirmatively consent to a change in a loan transaction can lead to administrative burdens in chasing down parties that simply have not responded. On the other hand, where negative consent is the standard, if more than a third of the lenders are unhappy, that likely signals a problem.

Question 18. 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?

Yes. Screen rate availability is necessary for both administrative ease and for control purposes.

Question 19. Given that market practices and conventions may change over time, should the administrative agent's limited ability to make conforming changes be available only at the point of transition or on a periodic, ongoing basis? Why or why not?

One time change is preferable. On balance, especially given our relatively small lender groups and strong borrower relationships, the additional burden of monitoring for and making changes to documents over time outweighs the possibility that a needed amendment is not accepted by the other parties to the document once identified.

Question 20. How important is it for the fallback rate to be available prior to making a borrowing/advancing funds? For instance, if the rate was a compounded three-month rate calculated at the ***end*** *of the interest period, would that be problematic? Please explain.*

Very important. System issues would be much greater. Mechanics of even simple things would become much more complicated (for example, calculating a payoff amount and per diem). Further, our borrowers would not like the approach.

Question 21. Are there operational concerns about having the ability to convert many loans over a very short period of time? Please explain.

There are some concerns, but at this point, we believe that the issues will be able to be addressed appropriately.

Question 22. Do you see other operational challenges that fallback language should acknowledge or of which the ARRC should be aware? Please explain.

The fallback language should consider an agent option to move to an overnight rate other than SOFR for some period of time once a trigger has occurred to ease the administrative burden of trying to make changes to many documents at one time. Fed Funds plus a margin or Prime minus a margin might be an appropriate choice for such a rate.

Question 23. What modifications to the syndicated loan consultative language may be helpful to market participants as they consider more robust fallback language in a bilateral or single-bank business loan context, if any? Please explain. Specifically, what modifications to the language may be appropriate in instances in which the bilateral loan is fully or partially hedged? Please explain.

An exclusively opt in version of the language may be more appropriate for single lender loans, perhaps coupled with additional lender discretion on the final rate and methodology. Many single lender loans exist that are relatively small. Both the lenders and the borrowers may be more concerned with an orderly rate transition and easily understood legal language in the documents than with the precision of the adjustments in that context. If a bilateral loan is fully or partially hedged, we would anticipate negotiating amendments at the time the rate is replaced rather than trying to incorporate language in the documents now for bilateral loans.

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

No.

Question 25. Please provide any additional feedback on any aspect of the proposals.

N/A