November 26, 2018

Alternative Reference Rates Committee (“ARRC”)

Via email submission to: arrc@ny.frb.org

Re: Consultation Response – Syndicated Business Loans

Wells Fargo & Company (“Wells Fargo”) submits this response to the ARRC Consultation Regarding more Robust LIBOR Fallback Contract Language for New Originations of Syndicated Business Loans. Wells Fargo recognizes the critical work of the ARRC to identify best practices for effective contractual fallback language. We hope these efforts will reduce market disruption in the event that LIBOR is discontinued. In addition, Wells Fargo appreciates the tremendous work of the ARRC Business Loans Working Group in developing this consultation, taking into consideration a wide range of views from members regarding the complex issues related to the LIBOR transition.

Responses to Questions:

A. General Approach of the Two Fallback Proposals

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?

Answer: Wells Fargo supports the hardwired approach because using flexible fallback provisions (like the amendment approach) may result in divergent outcomes as well as disputes and ambiguity at a critical time. In addition, we feel it would be very challenging for firms to reopen numerous credit agreements at once. To provide clarity and consistency, the hardwired fallback proposal uses clear and observable triggers and fallback rates/spread adjustments, subject to some flexibility at the end of the waterfalls.

B. Triggers

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?

Answer: Despite reservations expressed below, we believe that triggers 3, 4, and 5 should be included. Trigger 3 provides a mechanism to transition when regulators have not acted but market participants are left in limbo. Trigger 4 provides an avenue to transition should LIBOR no longer be appropriate, but a regulatory agency has not yet opined. Trigger 5 should be included

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to allow banks to respond to regulatory guidance. In the case that the regulator opines and triggers are not otherwise engaged elsewhere, nationally-chartered banks will need an opportunity to transition the loan to respond to regulatory requirements or guidance.

(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.

**Answer:** Wells Fargo’s primary concern around pre-cessation triggers relates to potential basis risk with derivatives. Otherwise, we would be fully supportive of these proposed pre-cessation triggers.

(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?

**Answer:** If pre-cessation triggers are not included, we would seek to amend loan documents in these circumstances which would be challenging and likely not achievable.

**Early “Opt-in” Triggers**

**Question 3.**

(a) Is an “opt-in” trigger appropriate to include? Why or why not?

(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.

**Answer:** We believe that these opt-in triggers provide too much ambiguity on timing, which may cause unbalanced incentives between market participants depending on market conditions. Marking an opt-in to “at least two” loans utilizing term SOFR is not necessarily indicative of broad market preparation, readiness, acceptance, or convention. While we understand that opt-in could encourage proactive adoption, the standards set forth in this trigger could encourage market timing and premature adoption. Opt-in triggers would be more appropriate after more robust observable adoption of the new rate.

**Other Triggers**

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

**Answer:** No.
C. The Replacement Benchmark

Step 1: The Forward-Looking Term SOFR

**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.

**Answer:** Given the structure of most syndicated deals, Wells Fargo supports a best-fit fallback from term LIBOR to a forward-looking term SOFR, should term SOFR be endorsed by the ARRC. This fallback would result in some basis risk with derivatives (which products will fall back to an overnight version of SOFR); however, we believe most syndicated loan customers would accept this risk and still prefer to have a forward-looking term rate if endorsed by the ARRC.

**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?

**Answer:** Of the two options presented, Wells Fargo supports option (i) because any non-published rate presents operational challenges and will not have the desired degree of transparency.

Step 2: “Compounded SOFR”

**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?

**Answer:** Wells Fargo supports Compounded SOFR as step 2. If term SOFR has not been endorsed by the ARRC, we believe that Compounded SOFR appropriately attempts to accommodate for the loss of term structure. Please note that our answer could change based on the results of the ISDA Consultation.

**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.

**Answer:** In the absence of a term SOFR endorsed by the ARRC, Wells Fargo supports Compounded SOFR “in arrears” as the second step in the waterfall, primarily because it is reflective of the relevant interest period. We note that there are significant operational and other considerations related to switching a LIBOR-based loan to an “in arrears” convention because payments would not be known at the onset of the payment period and will require changing loan mechanics. We believe, however, that publication of a Compounded SOFR in arrears would make this rate more transparent and assist market adoption.
Step 3: Overnight SOFR

**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.

**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.

**Answer:** We would prefer to remove spot SOFR from the waterfall. Our concern is that it would not be acceptable to fix one observation for a loan lasting three months or longer. We are also concerned about potential unanticipated accounting implications. Please note that our answer to this question could change based on the outcome of ISDA’s recent consultation.

Other Fallback Rates

**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?

**Answer:** We did not identify any other replacement rates to suggest.

D. Spread adjustments

Step 1: ARRC Spread Adjustment

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

**Answer:** Yes, we believe it would provide the market greater certainty and reduce market disruption if the ARRC, when recommending a forward-looking term SOFR, also recommends a corresponding spread adjustment methodology.

Step 2: ISDA Spread Adjustment

**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.

**Answer:** Yes, while it may not be ideal (if the replacement rate for syndicated loans differs from the fallback rate used for derivatives in the ISDA Definitions), it will be a published spread adjustment that lenders or agents can look to that reduces uncertainty in the absence of an ARRC recommended spread adjustment.
**Other Spread Adjustments**

**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?

**Answer:** We did not identify any other spread adjustments to suggest.

**E. Lender vote**

**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?

**Answer:** Yes. Different classes attract different types of lenders and their interests may not be aligned.

(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.

**Answer:** Yes. Different classes attract different types of lenders and their interests may not be aligned.

**Question 16.** (a) Under the hardwired approach proposal, if parties must fall back 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?

**Answer:** Yes. Different classes attract different types of lenders and their interests may not be aligned so voting by class is appropriate.

(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.

**Answer:** We believe that voting by class is most appropriate, as different types of lenders tend to participate in different classes and their interests may not be aligned. We will accept the Required Lenders voting threshold.

**F. The role of the administrative agent**

**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.

Answer: We believe some of these actions could be challenging and will require operational
builds. We believe clause (i) above may be operationally impractical, depending upon the
number of impacted loans.

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?

Answer: Wells Fargo believes a published rate would be beneficial to all market participants as it
would increase transparency and thereby encourage adoption and minimize disputes.

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?

Answer: Given the complexity, Administrative Agents should have the ability to make transition-
related changes for a limited time period (e.g. 2-3 interest accrual periods).

G.  Operational considerations

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.

Answer: For products like loans, we believe a term rate is particularly important. However, if a
robust term rate has not been endorsed by the ARRC, we think operational capabilities would be
established to allow use of a published Compounded SOFR in arrears which would be preferable
to a SOFR compounded in advance. We note such capabilities do exist today for some products
(e.g. derivatives). As noted earlier, we believe that publication of a SOFR compounded in
arrears would be beneficial for market adoption.

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

Answer: There would be a high degree of complexity when converting a high volume of loans.
Especially since at the time of transition there will be several “versions” of fallbacks to evaluate
and transition properly.

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

**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.

**Answer:** We encourage the ARRC to issue a separate consultation for bilateral business loans.

I. **General feedback**

**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.

**Answer:** An important consideration for Wells Fargo is additional clarity on accounting implications of the fallbacks.

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

**Answer:** No further comments to add at this time.

Wells Fargo wishes to thank the ARRC Business Loans Working Group for the opportunity to provide this feedback on the Syndicated Business Loans LIBOR Fallback Consultation. We are happy to discuss our responses further or provide any additional information that may be helpful.

Thank you,

Wells Fargo