ARRC Consultation regarding new issuances of <u>LIBOR Securitizations</u>

Topic	**##**	**Questions**
Approach to fallback provisions	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. Our responses are primary focused on consumer installment and floorplan/equipment asset-backed securities, but not intended to be limited to those asset classes.
Triggers	2	The ISDA triggers contemplate a permanent cessation of LIBOR as of a date certain 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? Yes. In cases when the assets of the securitization transaction are indexed to LIBOR as the asset contractual documents this would allow for some discretion on the date the transition from LIBOR is to be implemented; in order to best align the assets and liabilities of such securitizations and mitigate basis risk. If the transaction included a derivative that referenced LIBOR, such language could be added to the derivative contract as well. Some flexibility in setting a transition date from LIBOR prior to the Cessation Date would in many circumstances (when liabilities reset monthly) allow for the transition from LIBOR to occur on a determination date for the transaction, such that the interest accrual on the liabilities would include only a single Benchmark and spread during the accrual period, rather than 2 Benchmarks and spreads (if applicable) during the accrual period. For transactions that have liabilities that reset on a less frequent basis, it would be helpful to allow for a date even earlier than the proposed 30 day period prior to the Cessation Date, such as 90 days.
	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. We support in principle the use of pre-cessation triggers, to the extent that they allow parties to a securitized product to trigger the use of the replacement rate in their contract. Such pre-cessation triggers must be clear and related to objective event and not signal subject to interpretation as it is very important not to create uncertainty. However we do not think that such pre-cessation triggers should be used for the specific case of the transition from Libor to SOFR. We do consider that the transition from Libor to SOFR must be done in a smooth and coordinated manner and to do so the transition should be triggered by a communication or decision made by public and/or regulatory authorities so it can be simultaneous across markets and products and avoid fragmentation.
	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. Please see 3(a).
	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. Please see 3(a). In the context of our response to 3(a), but considering the specific case of an Asset Replacement Percentage

		pre-cessation trigger; it could be maintained, and the guidance from ARRC should allow for each securitization's transaction parties to negotiate and determine whether the pre-cessation trigger is necessary or advisable, as currently documented. In the case of residential mortgage transactions and other asset classes, some of the underlying assets, but not all, may be indexed to LIBOR. Thus, the trigger may need to be considered in terms of the percentage of underlying assets that are indexed specifically to LIBOR and tailored for that transaction. The applicable percentage upon which the trigger is hit, may need to be flexible to permit varying proportions of the asset pool in a transaction that are indexed to LIBOR.
	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. Please see 3(c) If in the circumstance that the sponsor or servicer has the ability to change the Benchmark used on the underlying assets independent of any pre-cessation trigger or other Benchmark Discontinuance Event relevant to the assets, then the reliance on the Asset Replacement Percentage as a trigger to transition the liabilities from LIBOR could be subject to a non-objection by the security holders to be confirmed the business day one day before the next determination date. In such circumstances the Asset Replacement Percentage could only be allowed to be triggered on a Determination Date, which would allow for at least a month for the response of security holders. One mitigant could be the inclusion of language on how to both determine and divide such a value between the sides of the transaction or an auto-revaluation feature.
	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? Please see 3(a).
Benchmark Replacement Date	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. Please see 2.
Replacement Benchmark	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. If the market consensus is to adopt a term rate for securitizations, we support a forward looking rate as the primary fallback. A term-rate with a term spread is in line with our clients' expectations Convergence between fallback & trigger definitions between asset classes (FRNs, Loans, Derivatives) is key in order to avoid fragmentation of SOFR indexed product liquidity, and limit operational/financial risks when dealing with all these products at portfolio level.
	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. In the cash markets, including securitization, a forward-looking term rate such as SOFR would be preferable as it is known in advance of a specified accrual period, which conforms to fixed income market convention, Compounding or averaging an overnight rate, whether in advance or in arrears creates unique circumstances in which either the calculated rates would reflect a prior period's cost of funding or would not be known until

		the end of an accrual period, making the accounting and operational aspects of managing the securities very complex. In addition, use of a forward-looking term rate on underlying assets while use of an overnight compounded or average rate for liabilities would cause transaction basis risk.
	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. Yes as long as the use is consistent across asset classes. Interpolated LIBOR and interpolated fixed/3m LIBOR swap rates are already used as a means to price debt in the securitization markets today – even for fixed rate securities. Since forward-looking term SOFR is the primary Replacement Base Rate, interpolating between two available forward-looking term SOFR rates would be preferable to alternative Base Rates, including compounded or averaged overnight SOFR.
	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? Yes, since forward-looking term SOFR is the primary Replacement Base Rate, re-testing the availability of such a rate should be performed. There may be circumstances under which re-testing should not take place, however, such as if a government or regulatory body has endorsed a forward-looking term rate other than SOFR.
	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? A forward looking term rate with a term spread is the preferred solution for cash products and a requirement for clients and end users, especially medium and small corporates. We also support convergence between fallback & trigger definitions between asset classes (FRNs, Loans, Derivatives) in order to avoid fragmentation of SOFR indexed product liquidity, and limit operational risks when dealing with all these products at portfolio level, but know that it may be difficult to achieve.
	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. Please see 6(a) We support convergence between fallback & trigger definitions between Asset Classes (FRNs, Loans, derivatives) in order to avoid fragmentation of SOFR indexed product liquidity, and limit operational risks when dealing with all these products at portfolio level. In this context and regarding the specific case of the conditions mentioned; setting in arrears may be preferred. However, we consider that shifting from an “in advance” fixing to an ”in arrears” fixing will be very challenging for some borrowers to manage as it would be a significant shift from their current way of managing debt. For this reason, we believe that the best solution is a forward looking term rate, which should ideally be a term SOFR recommended by the ARRC.
	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? Please see 6(a) Although there are parties in a securitization transaction that have the capability to make such calculations, it may be advisable for there to be a party performing the calculation, such as the issuer, and a confirming party to validate the calculation independently, such as a calculation agent or trustee, if such agent or trustee can be provided with clear guidance on the calculation methodology.

	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? Please see 6(a) Spot SOFR should not be included as a fallback reference rate for securitizations.
	8	In the future circumstance where there is no SOFR-based fallback rate, is the replacement rate determined by the Relevant Governmental Body the best alternative at this level of the waterfall? Please explain why. Please see 6(a) Yes, to ensure conformity in the markets. If the Relevant Governmental Body were to opine not just on securitizations, but all cash products, this would help align assets and liabilities in a securitization transaction with both assets and liabilities referencing LIBOR and/or SOFR.
	9	In the future circumstance where there is no SOFR-based fallback rate and the Relevant Governmental Body has not recommended a replacement rate for Securitizations, is the fallback for SOFR-linked derivatives set forth in the ISDA definitions at the time of cessation the best alternative at this level of the waterfall? Is this fallback appropriate if ISDA Definitions only include overnight fallback rates? Please explain why. Please see 6(a) Yes but, we support convergence between fallback & trigger definitions between Asset Classes (FRNs, Loans, derivatives) in order to avoid fragmentation of SOFR indexed product liquidity, and limit operational risks when dealing with all these products at portfolio level, so yes, in such case it would be the best alternative.
	10(a)	Since it is unlikely that there will be no ISDA fallback (clause (a) above), this provision is more likely to occur (if at all) when the ISDA fallback is deemed not appropriate for securitization securities (clause (b) above). In that scenario, is this provision appropriate as the final step in the Replacement Benchmark waterfall? Please explain why. Yes, it is appropriate as there could be circumstances when the overnight fallback rates from ISDA may not contemplate compounding or averaging such rates, or when there is an available term rate that would be more effective than a compounded or averaged overnight rate.
	10(b)	Should the provision allow for “re-testing” the waterfall to determine whether another Replacement Benchmark has become available in the scenario where investors have rejected the Proposed Replacement Benchmark? Should the waterfall be re-tested in any other circumstances (e.g., any time the Replacement Benchmark has been determined under a “less-desirable” clause)? How often? Please explain why. Yes, see comments in 10(a). Re-testing could be useful to allow for market confluence if there are different methodologies and triggers. The waterfall should be re-tested when the compounded or average SOFR is in effect as well, since the goal should be to move to forward-looking term SOFR or to another forward-looking term rate.
Replacement Benchmark Spread	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? A historical analysis of the mean or median difference between the applicable term LIBOR and the applicable term replacement rate should be conducted to determine the appropriate Replacement Benchmark Spread, over the longest available historical dataset.
	12	Do you believe that the ARRC should consider recommending a spread adjustment that could apply to cash products, including Securitizations? Yes. It would be preferable if the ARRC recommended a spread adjustment for ALL asset classes, including derivatives.
	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.

		This spread adjustment would not be appropriate if the securitized products or their underlying assets fallback to a term rate, which we consider to be the best option for cash product clients and end users. It would only be appropriate if products end up falling back to daily compounded SOFR, but this is not a replacement rate we would want to include in our waterfall.
	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 relevant to a different Benchmark Base Rate) should apply to Securitizations? Please explain why. No. Please see 11
	13(c)	Given that ISDA has not yet decided upon the spread calculation methodology, should Step 2 be excluded from the waterfall? Please explain why.
Responsibility for Calculations	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? We consider that trustees and calculation agents are unlikely to take on the responsibility of the abovementioned calculations/determinations. Although issuers/sponsors may be willing to take responsibility for the calculations/determinations, investors may require a third party or independent calculation/validation. To the extent that ARRC and/or a regulatory body can endorse specific methodologies and market data providers can confirm that data screens are providing such endorsed rates, spreads and information, it may make an independent third party such as a trustee or calculation agent more comfortable with taking some of the abovementioned responsibilities. The decision whether to elect an early transition to a Replacement Benchmark should be left to the issuer/sponsor to determine, as the underlying assets and any derivatives taken out by the issuer/sponsor must be considered as well.
	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? Yes however, investors in some or certain asset classes may not be in favor of an issuer/sponsor/servicer (especially if the servicer is not independent of the issuer/sponsor) taking on the sole responsibility for these actions without independent verification or validation.
General Feedback	15	Is there any provision in the proposal that would significantly impede Securitization issuances? If so, please provide a specific and detailed explanation. We see a risk of liquidity dislocation on SOFR-based products if the fallbacks methodologies (and triggers) are different between asset classes.
	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. Fallback language for the securitizations should align as much as possible with the fallback language of the underlying assets. Not all assets may move from a LIBOR benchmark to a SOFR benchmark even if forward-looking term SOFR develops in the next few years. For example, mortgage loans indexed to LIBOR may shift to a Treasury based index rather than a SOFR based index.

	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? N/A
	18	Please provide any additional feedback on any aspect of the proposal. N/A