May 29, 2020

Mr. Thomas G. Wipf
Chair
Alternative Reference Rates Committee
1585 Broadway
New York, NY 10036-8293

Dear Chairman Wipf,

The Student Borrower Protection Center, Americans for Financial Reform Education Fund, and the National Consumer Law Center (on behalf of its low-income clients) offer the following comments in response to the Alternative Reference Rate Committee's (ARRC) recent "Consultation Regarding More Robust LIBOR Fallback Contract Language for New Variable Rate Private Student Loans" ("Consultation").[1]

The undersigned organizations previously emphasized that student loan borrowers face unique risks stemming from the transition away from LIBOR.[2] The private student loan market lacks key protections found among other consumer financial products affected by the transition. Further, the contracts underlying most private student debt could allow lenders to use the transition as a pretext to raise borrowers' interest rates.[3] In response, we called on the ARRC to do the following: redouble its commitment to ensuring that the transition be executed in a way that will "minimize expected value transfer;" insist on greater transparency from industry; and more actively encourage private sector participants to begin moving away from LIBOR. Our comments also highlighted several steps that the Consumer Financial Protection Bureau (CFPB) should take in its role as the nation's top consumer watchdog to protect borrowers ahead of LIBOR's impending cessation.[4]

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[1] *See* Fed. Reserve Bank of N.Y., *ARRC Consultation Regarding More Robust LIBOR Fallback Contract Language For New Variable Rate Private Student Loans* (Mar. 27, 2020), https://www.newyorkfed.org/medialibrary/Microsites/arrc/files/2020/ARRC-VRPSL-consultation03272020.pdf.

[2] Letter from Student Borrower Protection Center, Americans for Financial Reform Education Fund, National Community Reinvestment Coalition, and the National Consumer Law Center to Thomas G. Wipf, Chair, Alternative Reference Rate Committee (Mar. 6, 2020), *available at* https://protectborrowers.org/wp-content/uploads/2020/03/LIBOR-Spread-Adjustments-Coalition-Letter.pdf.

[3] *Id.*

[4] Ben Kaufman, *Are Millions of Student Loan Borrowers About to Pay for Banks' LIBOR Fraud?*, THE STUDENT BORROWER PROTECTION CENTER (Mar. 6 2020), https://protectborrowers.org/are-millions-of-student-loan-borrowers-about-to-pay-for-banks-libor-fraud/.

Unfortunately, the twelve weeks since those warnings were raised have been cause for concern. The transition from LIBOR is rapidly approaching, but the CFPB and private-sector stakeholders across the student loan market have missed several opportunities to ensure that borrowers will be protected when it arrives. We are also concerned that the ARRC has not called for more transparency from industry regarding plans to transition away from LIBOR, let alone to substantively encourage companies to act on phase-out plans expeditiously. The CFPB has yet to define index "comparability" or clarify the affirmative disclosure obligations of Note Holders to borrowers pursuant to the Truth in Lending Act. Industry participants have failed to answer such basic questions as what index they will adopt to replace LIBOR, when they will transition to it, and how they will ensure that borrowers remain protected and informed throughout the process. In all, little progress has been made.

Even in light of the disruptions caused by the coronavirus pandemic, the collective lack of action in the past three months is troubling. The UK's Financial Conduct Authority has made clear that it does not intend to push the date of LIBOR's cessation past the end of 2021.[5] Consumers cannot afford for lenders to continue to postpone preparations for their transition away from LIBOR.

Against this backdrop, we believe that the ARRC's publication of the Consultation was an important first step. The fallback language included in the Consultation includes several critical consumer protections and will help usher industry toward preparing for the transition.

We offer the following responses to questions posed in the Consultation:

- **Question 1: Should fallback language for variable rate private student loans include a pre-cessation trigger (trigger 4(G)(ii))?**

  In keeping with fallback language that the ARRC has already recommended for other cash products,[6] fallback language for variable rate private student loans should include a pre-cessation trigger. Industry has noted in previous Consultations for other cash products that a pre-cessation trigger similar to the one included in section 4(G)(ii) is appropriate.[7] Such a trigger will prevent a scenario where LIBOR is deemed unrepresentative by the Financial Conduct Authority (FCA) but remains available (possibly through an extremely small panel of submitting banks) and therefore continues to be used by Note Holders. If

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[5] Financial Conduct Authority, *Impact of the coronavirus on firms' LIBOR transition plans* (Mar. 25, 2020), https://www.fca.org.uk/news/statements/impact-coronavirus-firms-libor-transition-plans.

[6] *See, e.g.*, Fed. Reserve Bank of N.Y., *ARRC Recommendations Regarding More Robust LIBOR Fallback Contract Language For New Closed-End, Residential Adjustable Rate Mortgages* (Nov. 15, 2019), https://www.newyorkfed.org/medialibrary/Microsites/arrc/files/2019/ARM_Fallback_Language.pdf.

[7] *See* Consultation Response from Wells Fargo to Alternative Reference Rates Committee (Sep. 9, 2019), *available at* https://www.newyorkfed.org/medialibrary/Microsites/arrc/files/adjustable-rate-mortgages/ARM-Wells-Fargo.pdf.

this were to happen, borrowers could be left to grapple with erratic swings in their interest rate until LIBOR becomes entirely unavailable.

- **Question 4: The variable rate private student loan language proposed uses simplified language in an effort to be more comprehensible for the consumer market. Is the simplified language proposed here appropriate, or are there concerns with the language not matching ISDA [the International Swaps and Derivatives Association] or other cash product language precisely?**

  The simplified language proposed in the Consultation is both appropriate and necessary. Similar plain language has been used in ARRC recommendations for other cash products.[8] As discussed below, we encourage the ARRC not only to maintain this existing plain language, but to strengthen efforts to coordinate consumer-facing communications so that borrowers have early, effective notice about the upcoming transition from LIBOR.

- **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 for the first step of the waterfall? Why or why not?**

  We agree that 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 is the best choice for the first step of the waterfall.

  However, we state that agreement with the understanding that, as it pertains to the transition from LIBOR, the committee in question is the ARRC and the replacement index it has recommended is spread-adjusted SOFR.

  We believe that spread-adjusted SOFR, as determined using the ARRC's proposed methodology, is the best replacement for LIBOR for cash products.[9] Spread-adjusted SOFR was selected through a rigorous, transparent process and avoids many of the faults of LIBOR by being based on actual transaction data in a deep and liquid market. New variable rate private student loans should first fall back to this ARRC-endorsed rate

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[8] See, e.g., Fed. Reserve Bank of N.Y., *ARRC Consultation Regarding More Rebust LIBOR Fallback Contract Language for New Closed-End, Residential Adjustable Rate Mortgages* (July 12, 2019), https://www.newyorkfed.org/medialibrary/Microsites/arrc/files/2019/ARRC-ARM-consultation.pdf.

[9] Fed. Reserve Bank of N.Y., *ARRC Announces Recommendation of a Spread Adjustment Methodology for Cash Products* (Apr. 8, 2020), https://www.newyorkfed.org/medialibrary/Microsites/arrc/files/2020/ARRC_Spread_Adjustment_Methodology.pdf.

before moving to any other option as doing so will ensure an orderly and fair transition away from LIBOR.

We frame our answer this way given the growing risk that some industry participants will successfully lobby for the ARRC to rubber-stamp the use of an index that suffers from the same defects as LIBOR, or that an entirely different committee could be empowered to approve flawed but industry-friendly replacement index rates. Our belief in this possibility stems from recent actions by various industry participants, many of whom continue to demand that they be able to replace LIBOR with index rates that are not based on actual transaction data in deep and liquid markets.[10] Our fears have been bolstered by regulators, who have recently signaled an intent to acquiesce to demands for the approval of additional replacement rates and have already formed alternative groups that could sign off on such rates in the place of or in parallel to SOFR.[11]

Since at least 2012, LIBOR's structural flaws have been publicly known and industry has been on notice that the index might eventually need to be replaced.[12] In 2017, SOFR was selected as the replacement rate for LIBOR following a years-long, extensively documented process.[13] Late-stage efforts to push alternatives to SOFR are nothing more than a self-interested attempt to prioritize what industry participants find familiar and

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[10] *See, e.g.*, Fed. Reserve Bank of N.Y., *Responses to the ARRC Consultation on Spread Adjustment Methodologies for Fallbacks in Cash Products Referencing USD LIBOR*, 229, https://www.newyorkfed.org/medialibrary/Microsites/arrc/files/2020/ARRC_Spread_Adjustment_Consultation_Responses.pdf ("We believe that SOFR, alone, is not well suited as a successor benchmark for every 'cash' product . . . . In addition to those rates, multiple other rates including the constant maturity treasury rate . . . are used in lending markets."). The constant maturity treasury rate is based on "indicative" rate quotations and not on actual transaction data. *See* U.S. Dep't of the Treasury, *Daily Treasury Yield Curve Rates*, https://www.treasury.gov/resource-center/data-chart-center/interestrates/Pages/TextView.aspx?data=yield (last accessed Feb. 26, 2020).

[11] *See* Victoria Guida, *Otting: Agencies will launch dialogue on LIBOR alternative for loans*, POLITICO (Jan 22, 2020), https://subscriber.politicopro.com/financial-services/whiteboard/2020/01/otting-agencies-will-launch-dialogue-on-liboralternative-for-loans-3975896 ("SOFR 'would not appear to be a logical solution' for loans because the rate might drop in a crisis, even as banks' cost of funds increases, Otting said."); *see also* Hannah Lang, *Fed's Powell open to more than one LIBOR alternative*, AM. BANKER (Feb. 12, 2020), https://www.americanbanker.com/news/feds-powell-open-to-more-than-one-libor-alternative ("Powell acknowledged that a number of banks have publicly said that they would prefer using a different rate than SOFR, and that the Fed is supportive of the possibility of creating a different rate. 'A number of banks have come forward and said that they want to work on a separate rate, which would not replace SOFR, but would be credit sensitive, and so they're doing that now and ... we're working with them to support that process,' he said."); Fed. Reserve Bank of N.Y., *Transition from LIBOR: Credit Sensitivity Group Workshops* (Feb. 25, 2020) https://www.newyorkfed.org/newsevents/events/markets/2020/0225-2020.

[12] *See, e.g.*, David Hou and David Skeie, *LIBOR: Origins, Economics, Crisis, Scandal, and Reform*, FED. RESERVE BANK OF N.Y. STAFF REP. (Mar. 2014), *available at* https://www.newyorkfed.org/medialibrary/media/research/staff_reports/sr667.pdf.

[13] Fed. Reserve Bank of N.Y., *Interim Report and Consultation of the Alternative Reference Rates Committee* (May 2016), *available at* https://www.newyorkfed.org/medialibrary/microsites/arrc/files/2016/arrc-interim-report-and-consultation.pdf; Joshua Frost, *Introducing the Secured Overnight Financing Rate (SOFR)*, FED. RESERVE BANK OF N.Y. (Nov. 2, 2017), *available at* https://www.newyorkfed.org/medialibrary/media/newsevents/speeches/2017/Frostpresentation.pdf.

comfortable while perpetuating the use of rates that suffer from the same flaws and pose the same consumer risks as LIBOR.

We therefore ask that the fallback language proposed in the Consultation be amended to more clearly state that the "committee endorsed or convened by the Federal Reserve Board or the Federal Reserve Bank of New York" is the ARRC and that the "replacement index determined by" that group is spread-adjusted SOFR for the purpose of the transition away from LIBOR. As confirmed in a recent meeting of the ARRC's Consumer Products Working Group, the ARRC's intent in drafting the proposed fallback language, which does not mention the ARRC or SOFR, was to allow for flexibility in the event of an additional rate cessation event *after* the transition away from LIBOR (that is, the hypothetical event of SOFR cessation and/or of the need to replace a rate that might replace SOFR).[14] As it pertains specifically to the current transition from LIBOR, though, the ARRC has stated that the fallback language included in the Consultation was designed neither to open the possibility of a group other than the ARRC being empowered by the Federal Reserve Board or the Federal Reserve Bank of New York to recommend a replacement index for LIBOR nor to provide a backdoor for an additional LIBOR replacements beyond SOFR to find last-minute approval. However, given the recent events discussed above, we fear that the fallback language as drafted could do precisely that.

The language in the final recommendation resulting from the Consultation should more closely reflect the stated intention of its drafters. The recommended fallback language should clarify that while the Federal Reserve Board or the Federal Reserve Bank of New York may designate a different group from the ARRC for hypothetical replacement rate selection exercises in the future, the transition from LIBOR should involve only the ARRC and the replacement rate it has already chosen—SOFR.

- **Question 8: Should the Note Holder have the ability to make adjustments (positive or negative) to the loan's margin to more closely approximate the LIBOR-based interest rate present 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?**

As in the draft fallback language, the Note Holder should have the ability to make adjustments to the loan's margin only after making "a reasonable, good faith effort to select a Replacement Index and a Replacement Margin that, when added together, the Note Holder reasonably expects will minimize any change in the cost of the loan, taking

[14] ARRC Consumer Products Working Group Meeting via teleconference (May 11, 2020).

into account the historical performance of the Index and the Replacement Index." It is absolutely critical that Note Holders structure their products' transition from LIBOR in a way that will "minimize expected value transfer based on observable, objective rules determined in advance."[15] Retaining the language of "a reasonable, good faith effort to . . . minimize any change in the cost of the loan" in the recommended fallback language will be crucial for the purpose of ensuring that such structuring takes place.

Further, the CFPB should require Note Holders to publicly document the analysis behind any margin adjustment determination, including the data and methodology used to arrive at any prescribed changes.

- **Question 12: Please provide any additional feedback on any aspect of the proposal.**

  Given how little time remains between now and the anticipated date of LIBOR's cessation, the ongoing disruptions from the coronavirus pandemic, and industry's lack of urgency to date, we call for the ARRC to take the following additional steps to advance the transition from LIBOR in the private student lending space:

  - **Encourage companies to discontinue LIBOR-based lending immediately.** The Consultation outlines proposed fallback language for new LIBOR-based private student loans. However, there is no reason why a lender should not simply move now to a different reference rate for new loans ahead of LIBOR's cessation. With FHFA rapidly moving mortgage lenders from LIBOR to SOFR and many student lenders active in other consumer finance markets, there is ample reason for lenders to immediately begin transitioning their new student loan products away from LIBOR.[16] The ARRC should more vocally encourage student lenders to begin that move as quickly as possible. Simply put, there are already enough LIBOR-based private student loans to worry about.

  - **Insist on more robust involvement from industry.** Industry continues to drag its feet in choosing and implementing a new index rate for its loan products, as well as in communicating with borrowers regarding the upcoming transition away from LIBOR for legacy loans. The ARRC should be more proactive in encouraging lenders to begin transitioning to replacement indices. Further, the ARRC should accelerate efforts to focus industry attention on developing consumer-facing informational materials and communications plans. As of this

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[15] Fed. Reserve Bank of N.Y., *Guiding Principles and Scope of Work for the ARRC Consumer Products Working Group* (2019), https://www.newyorkfed.org/medialibrary/Microsites/arrc/files/2019/ARRC_Consumer_Products_Guiding_Principles.pdf.

[16] Fed. Hous. Fin. Agency, *LIBOR* Transition, https://www.fhfa.gov/SupervisionRegulation/LIBORTransition.

letter's publication, the ARRC's Consumer Outreach and Education subgroup has not held a scheduled twice-monthly meeting since February 2020. Borrowers will need ample time to learn about the transition, understand how it might affect their loans, and determine whether they want to refinance their student loans away from LIBOR. However, given how little guidance has been provided by the ARRC or the lenders that participate in it, borrowers may not be afforded that choice.

- **Collaborate more closely with the CFPB.** To date, the Bureau has been woefully inactive regarding the transition away from LIBOR. The absence of the nation's consumer watchdog has not only left borrowers vulnerable, but has also served as tacit endorsement of industry's passive stance regarding LIBOR's cessation. By more closely collaborating with the CFPB, including by providing detail on the types of guidance that industry is waiting for ahead of the development of appropriate consumer communication and transition plans, the ARRC and the Bureau can help ensure that consumers are protected.

The Consultation represents an important step toward a successful transition from LIBOR for the private student loan market. With the steps outlined above, the ARRC, the CFPB, and industry can ensure that the remainder of the transition proceeds smoothly.

Sincerely,

Student Borrower Protection Center
Americans for Financial Reform Education Fund
National Consumer Law Center (on behalf of its low-income clients)

CC:
Honorable Kathleen Kraninger, Director, Consumer Financial Protection Bureau
Honorable Brian Brooks, Acting Comptroller of the Currency, U.S. Department of the Treasury
Honorable Jelena McWilliams, Chairwoman, Federal Deposit Insurance Corporation
Honorable Jerome Powell, Chairman, Board of Governors of the Federal Reserve System
Honorable Randal Quarles, Vice Chair for Supervision, Board of Governors of the Federal Reserve System
Honorable John Williams, President and Chief Executive Officer, Federal Reserve Bank of New York