CBA | CONSUMER BANKERS ASSOCIATION

August 29, 2022

Ann E. Misback
Secretary
Board of Governors of the Federal Reserve System
20th Street and Constitution Avenue NW
Washington, DC 20551

Re: Regulation Implementing the Adjustable Interest Rate (LIBOR) Act
Docket No. R-1775, RIN 7100-AG34

Dear Ms. Misback:

The Consumer Bankers Association (CBA)[1] is pleased to submit these comments on the Notice of Proposed Rulemaking (Proposal) by the Federal Reserve Board (Board) to implement the Adjustable Interest Rate (LIBOR) Act (LIBOR Act).[2] Among other things, the Proposal establishes the Secured Overnight Financing Rate (SOFR) as a benchmark replacement for U.S.-governed contracts that do not have contractual fallback provisions, or have an inadequate fallback provision, to replace LIBOR when it is expected to cease publication after June 30, 2023.

In the sections below, we write to request the Board clarify its Proposal to reduce litigation risk by affirmatively stating, consistent with the LIBOR Act's § 104(f)(6), this Proposal does not

[1] The Consumer Bankers Association is the only national financial trade group focused exclusively on retail banking and personal financial services—banking services geared toward consumers and small businesses. As the recognized voice on retail banking issues, CBA provides leadership, education, research, and federal representation for its members. CBA members include the nation's largest bank holding companies as well as regional and super-community banks that collectively hold two-thirds of the total assets of depository institutions.
[2] Regulation Implementing the Adjustable Interest Rate (LIBOR) Act, 87 Fed. Reg. 45,268 (July 28, 2022), available at https://www.federalreserve.gov/newsevents/pressreleases/files/bcreg20220719a1.pdf.

interfere with credit card agreements that have transitioned to another rate before the LIBOR replacement date.

The CFPB has already amended Regulation Z to facilitate the orderly transition of existing balances on variable-rate credit card accounts away from LIBOR.

In December 2021, the Consumer Financial Protection Bureau (CFPB or Bureau) provided credit card issuers with a comprehensive path to transition away from LIBOR. Previously, Regulation Z had prohibited credit card issuers from changing the index rate applicable to existing balances on variable-rate credit card accounts until certain conditions were met, most notably that no transition could occur unless and until the index rate became "unavailable."[3] Cognizant of the ambiguity surrounding exactly when, if ever, LIBOR will become literally unavailable, particularly given the Intercontinental Exchange's (ICE) discussion around the possible publication of a "synthetic" LIBOR[4], the CFPB amended Regulation Z.[5] Instead of conditioning substitution of LIBOR on its "unavailability," the amended Regulation Z permits credit card issuers to transition existing balances to other index rates, such as the Prime Rate[6], as early as April 2022.[7] The Bureau recognized issuers would have difficulty effectuating an orderly transition of accounts to another index rate -- which requires providing accountholders with at least 45 days' notice -- if Regulation Z effectively required them to wait until the last-

[3] *See* Official Interpretation 6 to 12 C.F.R. § 1026.55(b)(2) (2021), "Substitution of index" ("A card issuer may change the index and margin used to determine the annual percentage rate under § 1026.55(b)(2) if the original index becomes *unavailable*, as long as historical fluctuations in the original and replacement indices were substantially similar, and as long as the replacement index and margin will produce a rate similar to the rate that was in effect at the time the original index became unavailable. If the replacement index is newly established and therefore does not have any rate history, it may be used if it produces a rate substantially similar to the rate in effect when the original index became unavailable.") (Emphasis added).

[4] ICE Benchmark Administration (IBA) -- the administrator of LIBOR, which is overseen by the United Kingdom's Financial Conduct Authority (FCA) -- has since announced that panel banks will "will stop contributing" their U.S. dollar ("USD") lending rates to the IBA after June 2023. *See* Intercontinental Exchange, *LIBOR Cessation and "Synthetic" LIBOR*, https://www.theice.com/iba/libor (last visited Aug. 11, 2022). However, at the time of the CFPB's rulemaking, it was possible, and it *remains possible* -- however unlikely -- that the IBA might continue publishing a form of some USD LIBOR tenors ("synthetic LIBOR"): "The FCA has stated that it will consider the case for requiring *continued publication* of the 1-, 3-, and 6-Months USD LIBOR settings on a 'synthetic' basis *after June 2023* …." *Id.* (emphases added).

[5] *See* Facilitating the LIBOR Transition (Regulation Z), 86 Fed. Reg. 69,716 (Dec. 8. 2021) (to be codified at 12 C.F.R. pt. 1026), available at https://www.federalregister.gov/documents/2021/12/08/2021-25825/facilitating-the-libor-transition-regulation-z; *see also* Consumer Financial Protection Bureau, *CFPB Issues Final Rule to Facilitate Transition from LIBOR*, https://www.consumerfinance.gov/about-us/newsroom/cfpb-issues-final-rule-to-facilitate-transition-from-libor (last visited Aug. 11, 2022).

[6] The Bureau expressly recognized the Prime Rate as meeting Regulation Z's other primary requirement for changing the index rate: substantially similar historical fluctuations. *See* Facilitating the LIBOR Transition (Regulation Z), 86 Fed. Reg. 69,796 (Dec. 8. 2021) (to be codified at 12 C.F.R. pt. 1026), available at https://www.federalregister.gov/documents/2021/12/08/2021-25825/facilitating-the-libor-transition-regulation-z ("The Bureau has determined that effective April 1, 2022, the prime rate published in the Wall Street Journal has historical fluctuations that are substantially similar to those of the 1-month and 3-month U.S. Dollar LIBOR indices.").

[7] *See* Facilitating the LIBOR Transition (Regulation Z), 86 Fed. Reg. 69,716, 69,782 (Dec. 8. 2021) (to be codified at 12 C.F.R. § 1026.55(b)(7)(ii)), available at https://www.federalregister.gov/documents/2021/12/08/2021-25825/facilitating-the-libor-transition-regulation-z.

minute to make the change. "Since the LIBOR indices are likely to become unavailable after June 30, 2023, and [this final rule] will allow creditors and card issuers under Regulation Z to switch on or after April 1, 2022, creditors and card issuers may be able to switch contracts from a LIBOR index to other indices roughly 15 months earlier than they would without [this amendment] …."[8]

The Bureau's amendment has made it possible for credit card issuers to transition away from LIBOR, and the CBA is aware of at least one major issuer that is in the process of transitioning LIBOR-indexed accounts to other index rates.

Furthermore, some LIBOR contracts contain fallback provisions that are triggered only when LIBOR is unavailable and do not have a "nonrepresentative" trigger. This means the fallback provisions for these contracts would not be triggered when LIBOR is available but is "nonrepresentative." The Board notes there is potential ambiguity if publication of a "synthetic" LIBOR continues after 6/30/23 and then declared "nonrepresentative" by the UK's Financial Conduct Authority (FCA). The availability of such a synthetic LIBOR could create confusion for those contracts that are triggered only when LIBOR is unavailable, since LIBOR in such case would arguably still be available. Accordingly, the Board is seeking comment on whether to include in the final rule a clarification that these contracts would be triggered on 6/30/23, whether synthetic LIBOR is available or not. CBA is supportive of this clarification.

Most mortgages issued before the GSEs published updated fallback language in 2020, as well as many other consumer products, do not include a nonrepresentativeness trigger. If synthetic LIBOR is available and the Board does not provide clarification that such contracts' fallback language is triggered despite synthetic LIBOR's availability, these lenders will need to decide between remaining on synthetic LIBOR despite its nonrepresentativeness or interpreting that LIBOR is no longer available and transitioning such contracts, exposing them to potential disputes from customers.

Additionally, the Alternative Reference Rates Committee (ARRC) has recommended CME term SOFR plus a transition spread adjustment that gradually transitions from LIBOR to CME term SOFR plus the ARRC-recommended spread adjustment over the course of one year to minimize sticker shock for consumers, which will be published on an all-in basis by Refinitiv. The ICE Benchmark Administration (IBA) also publishes a version of term SOFR, but there is no all-in rate that includes the one-year transition spread adjustment associated with IBA term SOFR. Since the FCA is the IBA's regulator, there's a question as to whether synthetic LIBOR would be based on the IBA's version of term SOFR or not. If it were, consumers that have contracts that transition via the Act would not have a one-year transition spread adjustment and would have different pricing than consumers with contracts that transition according to ARRC recommendations. We are concerned that this pricing difference increases the risk for class action litigation.

CBA urges the Board to provide clarification that the existence of synthetic LIBOR does not constitute continued availability of LIBOR.

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[8] Facilitating the LIBOR Transition (Regulation Z), 86 Fed. Reg. 69,716, 69,774 (Dec. 8. 2021), available at https://www.federalregister.gov/documents/2021/12/08/2021-25825/facilitating-the-libor-transition-regulation-z.

Congress enacted the LIBOR Act in March 2022 to affect a uniform transition away from LIBOR and to minimize uncertainty and disruptive litigation.

In March 2022, Congress enacted the Adjustable Interest Rate (LIBOR) Act[9], in part, recognizing the fact that "the cessation or non[-]representativeness of LIBOR could result in disruptive litigation related to existing contracts that do not provide for the use of a clearly defined or practicable replacement benchmark rate."[10]

The LIBOR Act will essentially act to substitute the Secured Overnight Financing Rate (SOFR) plus a spread adjustment to be determined by the Board -- the "Board-selected benchmark replacement"[11]-- for LIBOR in all "LIBOR contracts"[12] that either (1) contain no fallback provision or (2) contain only an incomplete fallback provision[13] on, with limited exception, the first London banking day after June 30, 2023 -- the "LIBOR replacement date"[14].[15]

The LIBOR Act did not intend to alter or impair the CFPB's LIBOR transition efforts and expressly preserved the CFPB's authority to do so.

Congress did not intend the LIBOR Act to interfere with "existing [LIBOR] contracts that … provide for the use of a clearly defined and practicable replacement rate."[16] Nor did Congress intend the Act to interfere with the authorities of federal agencies administering Federal consumer financial laws.[17] Instead, the Act expressly *preserved* such authority by stating that "[n]othing in [the Act] may be construed to alter or impair … the rights or obligations of any person, or the authorities of any agency, under Federal consumer financial law, as defined in section 1002 of the Consumer Financial Protection Act of 2010 (12 U.S.C. 5481) … except as provided in section 105(c),"[18] the Act's Safe Harbor provision.[19] Those Federal consumer financial laws include the Truth in Lending Act and its implementing regulation, Regulation Z.[20]

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[9] Adjustable Interest Rate (LIBOR) Act, Pub. L. No. 117-103, Div. U, 136 Stat. 49, 825-35 (2022); *see also* H.R. Res. 2471, Div. U, 117th Cong. (2022) (enacted), available at https://www.congress.gov/bill/117th-congress/house-bill/2471/text.

[10] Adjustable Interest Rate (LIBOR) Act, Pub. L. No. 117-103, Div. U § 102(a)(3), 136 Stat. 49, 825-26 (2022).

[11] *Id.* at § 103(6), 136 Stat. 826.

[12] *Id.* at § 103(16), 136 Stat. 827.

[13] *Id.* at § 103(11), 136 Stat. 827.

[14] *Id.* at § 103(17), 136 Stat. 828.

[15] *Id.* at § 104(a)(1) & (a)(2), 136 Stat. 828.

[16] *Id*. at § 102(a)(3), 136 Stat. 826.

[17] *Id*. at § 104(f)(6), 136 Stat. 829-30.

[18] *Id*.

[19] *Id*. at § 105(c), 136 Stat. 830.

[20] *See* Dodd-Frank Wall Street Reform & Consumer Protection Act, Title X ("the Consumer Financial Protection Act of 2010"), Pub. L. No. 111-203, Title X, § 1002(12)(O) and (14) (2010) (codified at 12 U.S. Code § 5481) ("The term 'Federal consumer financial law' means the provisions of [the Consumer Financial Protection Act of 2010], the enumerated consumer laws, the laws for which authorities are transferred under subtitles F and H, and *any rule or order prescribed by the Bureau under this title*, an enumerated consumer law, or pursuant to the authorities transferred under subtitles F and H. The term does not include the Federal Trade Commission Act." (Emphasis added)); *see also id*. at § 1061(a)(1)(A) & (b)(1)(A) (transferring to the CFPB the Board's "consumer financial protection functions," including "all authority to prescribe rules … pursuant to any Federal consumer financial law ….").

<u>The most plausible interpretation of this Proposal is that it does not interfere with credit card agreements transitioned to another rate before the LIBOR replacement date, but the Board could provide greater clarity to reduce litigation risk.</u>

As a consequence of (1) the Bureau's amendments to Regulation Z and (2) the Act's preservation of the Bureau's authority to make those amendments, any LIBOR-based credit card agreements that are transitioned to another rate (consistent with the amended Regulation Z) *before* the LIBOR replacement date will not constitute a "LIBOR contract" because they will no longer "use LIBOR as a benchmark."[21] Hence, they will not be subject to § 104(a), *i.e.*, the provision specifying that the Board-selected benchmark replacement shall replace LIBOR.

The Proposal, however, neither re-states, nor echoes the Act's § 104(f)(6) -- the provision preserving the CFPB's authority to amend Regulation Z. Under-informed parties could, therefore, misinterpret the Board's rule as conflicting with, or somehow abrogating the effect of, the Bureau's amendment and conclude that issuers who transitioned LIBOR-based accounts to a rate *other than* SOFR are not in compliance with the law. For instance, credit card account holders could mistakenly conclude that issuers do not have authority to transition existing balances on LIBOR-based interest rates to an index other than SOFR (plus the appropriate spread adjustment), like the Prime Rate, and file suit seeking damages, to the extent that the applicable Prime Rate-indexed interest rates diverge from (and exceed) the SOFR-based interest rates.

When it finalizes this Proposal, the Board could significantly reduce uncertainty, consistent with Congress' intent to "preclude litigation"[22] by affirmatively stating that, consistent with the LIBOR Act's § 104(f)(6), this Proposal does not impact credit card agreements transitioned to another rate before the LIBOR replacement date pursuant to the amended Regulation Z.

<u>The Proposals scope of conforming changes for consumer loans and the inability of such changes to be covered under the safe harbor under Section 105(a) of the Act is inadequate and the Board should prescribe conforming changes that would resolve the issue for more complex consumer loans.</u>

Section 103(4)(A) of the Act allows the Board to determine Benchmark Replacement Conforming Changes (BRCCs) related to the implementation of the Board-Selected Benchmark Replacement (BSBR). The Board is not recommending any BRCCs under Section 103(4)(A) for consumer loans. Section 103(4)(B) goes further and permits BRCCs that are determined in accordance with "the reasonable judgment of a calculating person." However, Section 103(4)(B) is clear in that this would not apply to consumer loans. We are concerned that the Board's abstention on prescribing any conforming changes for consumer loans will affect consumer loans beyond the Board's intention. While most consumer loans have simple rate calculation language (mortgages, student loans, etc.), some consumer loans have more complex interest rate language (e.g., loans to high-net-worth individuals).

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[21] *See* Adjustable Interest Rate (LIBOR) Act, § 103(16), 136 Stat. 827.
[22] *See id.* at § 102(b)(2), 136 Stat. 826.

Since the Board is not recommending any BRCCs for consumer loans and a "calculating person" cannot make such changes for consumer loans, the result is that if a lender wants to implement BRCCs related to the implementation of a BSBR in a consumer loan, these BRCCs would not be protected by the safe harbor that is provided for BSBRs under Section 105(a). Again, it is likely not an issue for many consumer loans, such as mortgages and student loans, where the rate calculation language typically includes only a reference to the index rate (e.g., one-month LIBOR) and its source (e.g., Wall Street Journal). But for more complex consumer loans, a lender could have to decide between providing interest rate transparency to consumers via BRCCs or abstaining from providing transparency in order to avoid taking action outside of the Act's safe harbor.

CBA urges the Board prescribe conforming changes that would resolve the issue for more complex consumer loans so that any such conforming changes would qualify for the safe harbor under Section 105(a).

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Thank you for the opportunity to share our comments on this Proposal. CBA would be pleased to answer any questions or provide you with additional information.

Sincerely,

David Pommerehn
General Counsel