March 27, 2020

ARRC Releases Consultation on Fallback Language for New Variable Rate Private Student Loans for Public Feedback

Proposed Draft Language Aims to Minimize Market Disruptions if LIBOR is No Longer Usable; ARRC Seeks Feedback by May 15, 2020

The Alternative Reference Rates Committee (ARRC) today released a consultation on U.S. Dollar (USD) LIBOR fallback contract language for new variable rate private student loans. This consultation outlines draft language for new contracts that reference USD LIBOR to minimize risks in the event that LIBOR is no longer usable. Feedback should be submitted no later than May 15, 2020.

This effort is part of the ARRC's work to help support a smooth transition away from LIBOR and to encourage adoption of the ARRC's recommended alternative reference rate, the Secured Overnight Financing Rate (SOFR). This is the sixth consultation on fallback language that the ARRC has released.

The U.K Financial Conduct Authority has warned that LIBOR could end or be judged to no longer be representative of its underlying market after 2021. "2021 is fast approaching, and it's critical that consumers have clarity about how it will impact the financial products they hold," said Tom Wipf, ARRC Chair and Vice Chairman of Institutional Securities at Morgan Stanley. "This draft fallback language is an important step in providing consumers with LIBOR-based student loans more certainty about when and how a replacement rate would be selected. We hope that feedback from market participants helps us develop robust fallback language that can be voluntarily incorporated into contracts well in advance of the transition date."

New Variable Rate Private Student Loans

Similar to the ARRC's recommendations for fallback language in new residential closed-end adjustable rate mortgages, the consultation on fallbacks for new variable rate private student loans proposes two different steps in a successor rate waterfall: an "ARRC Replacement Index" and a "Note Holder-Determined Replacement Index." The two steps are:

- ***ARRC Replacement Index*** – The first step of the recommended successor rate waterfall is the adoption of a replacement index selected or recommended for use in consumer products, including variable rate private student loans, by the Board of Governors of the Federal Reserve System, the Federal Reserve Bank of New York, or a committee endorsed or convened by the Board of Governors of the Federal Reserve System or the New York Fed (e.g., the ARRC).
- ***Note Holder-Determined Replacement Index*** – If there is not a rate selected or recommended as outlined in the first step, then the second step of the recommended waterfall would require the Note Holder to choose a replacement index, a step that is similar to the language in currently used LIBOR fallbacks for variable rate private student loans. The recommended variable rate private student loan fallback provision explicitly spells out the possibility that the Note Holder may determine an adjustment to be made to the loan's margin to bring the overall

interest rate calculated using the replacement index (or a future index and its replacement) more in line with the overall interest rate calculated using LIBOR.

Submitting Feedback about Consultations

The ARRC is seeking feedback on each proposed approach and on the key issues involved from the widest possible range of stakeholders. The release of these consultations marks the start of a public comment period, during which the ARRC intends to work closely with stakeholders in these markets, including issuers, intermediaries, and end users, to solicit and incorporate their input. The consultations include multiple questions about each aspect of the potential fallback provisions.

Comments should be sent to the ARRC Secretariat (arrc@ny.frb.org) no later than May 15, 2020. Comments will be posted on the ARRC's website after the close of the consultation period without alteration except when necessary for technical reasons. Comments will be posted with attribution unless respondents request anonymity. If your institution is requesting anonymity, please clearly indicate this in the body of your email and please ensure that the PDF document you submit is anonymized. Questions regarding the consultations should also be sent to the ARRC Secretariat (arrc@ny.frb.org) and will not be posted for attribution.

About the ARRC

The ARRC is a group of private-market participants convened by the Federal Reserve Board and Federal Reserve Bank of New York in cooperation with the Consumer Financial Protection Bureau, the Federal Deposit Insurance Corporation, the Federal Housing Finance Agency, the Office of Financial Research, the Office of the Comptroller of the Currency, the Commodity Futures Trading Commission, the Securities and Exchange Commission and the U.S. Treasury Department. It was initially convened in 2014 to identify risk-free alternative reference rates for USD LIBOR, identify best practices for contract robustness, and create an implementation plan with metrics of success and a timeline to support an orderly adoption. The ARRC accomplished its first set of objectives and identified the SOFR as the rate that represents best practice for use in certain new USD derivatives and other financial contracts. It also published its Paced Transition Plan, with specific steps and timelines designed to encourage adoption of the SOFR. The ARRC was reconstituted in 2018 with an expanded membership to help to ensure the successful implementation of the Paced Transition Plan, address the increased risk that LIBOR may not exist beyond 2021, and serve as a forum to coordinate and track planning across cash and derivatives products and market participants currently using USD LIBOR.

Sign up here to receive email updates about the ARRC.

Contact for ARRC Chair Tom Wipf
Paige Mandy
Morgan Stanley

Contact for the ARRC's Outreach/Communications Working Group
Andrew S. Gray
JPMorgan Chase

Contact for the Federal Reserve Board
Darren Gersh

Contacts for the Federal Reserve Bank of New York
Suzanne Elio and Betsy Bourassa