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National Association of Federally-Insured Credit Unions

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:

On behalf of the National Association of Federally-Insured Credit Unions (NAFCU), I am writing in response to the notice of proposed rulemaking (NPRM) issued by the Board of Governors of the Federal Reserve System (Board) regarding its proposed regulation that would implement the Adjustable Interest Rate (LIBOR) Act. NAFCU advocates for all federally-insured not-for-profit credit unions that, in turn, serve over 131 million consumers with personal and small business financial service products. NAFCU appreciates the Board's efforts to provide a smooth transition away from the London Inter-Bank Offered Rate (LIBOR). NAFCU supports the Board's proposed establishment of benchmark replacement rates based on the Secured Overnight Financing Rate (SOFR) and particularly the extent to which the proposed regulation would provide continuity of contracts and shield credit unions from litigation risk associated with contracts that do not have terms that provide for the use of a clearly defined and practicable replacement benchmark rate. However, the Board should work to ensure that any licensing fees or other costly usage terms are minimized and that potential mismatches between the Board-selected benchmark replacement rates are resolved.

General Comments

After the announcement of the transition away from LIBOR, NAFCU expressed general support for the move, while noting that some credit unions still have a small number of legacy LIBOR contracts in their consumer loan portfolios, some of which do not contain fallback language that would allow for the contract to be amended and continued when LIBOR sunsets (Tough Legacy Contracts). NAFCU continually advocated for Congressional action[1][2] through legislation to

[1] *See* NAFCU Letter to Senate Banking Committee re: The LIBOR Transition: Protecting Consumers and Investors Nov 1, 2021, *available at* https://www.nafcu.org/system/files/files/11-1-21%20Letter%20to%20Senate%20Banking%20on%20LIBOR%20Transition%20Hearing.pdf

[2] *See* NAFCU Letter to House Financial Services Committee re: The End of LIBOR: Transitioning to an Alternative Interest Rate Calculation for Mortgages, Student Loans, Business Borrowing, and Other Financial Products April 14, 2021, *available at* https://www.nafcu.org/system/files/files/4-14-21%20Letter%20to%20HFSC%20Cap%20Mkts%20Subcommittee%20on%20the%20End%20of%20LIBOR.pdf

establish a process for these legacy LIBOR contracts to be appropriately updated to ensure a smooth transition from LIBOR, and to prevent any unneeded disruption during continued periods of economic uncertainty. On March 15, 2022, NAFCU was pleased to see Congress enact the LIBOR Act as part of the Consolidated Appropriations Act, 2022.

Although NAFCU is supportive of the Board's provision of benchmark replacement rates for Tough Legacy Contracts, as the Board works to finalize the proposed replacement rates, it must be cognizant of the impacts that complex or costly regulations will have on credit unions. Specifically, the mandatory transition from LIBOR to the replacement benchmarks based on SOFR has the potential to subject credit unions to licensing requirements imposed by CME Group Benchmark Administration, Ltd. (CME) as the publisher of Term SOFR. For example, a Category One Use License would be required to use Term SOFR as a reference in a loan, mortgage, bond, note, or money market instrument or in valuation and pricing activities, including interest rate and collateral calculations.

NAFCU recognizes that licenses are not required for the use of SOFR itself, which is produced by the Federal Reserve Bank of New York, and that CME has waived related licensing fees through 2026, however Tough Legacy Contracts with longer maturities might still be subject to these fees. While large banks can brush off these fees as incidental, credit unions, and small credit unions in particular, have limited ability in to shoulder the burden of these types of additional costs. This monetary burden drains the few resources that small credit unions have, leaving them with precious little to devote to the business of growing and serving their members and investing in their communities. Therefore, the Board should make every effort to ensure that any benchmark replacement rates mandated in the proposed regulation are made available at low to no cost to credit unions and other not-for-profit institutions.

For similar reasons, the Board should avoid implementation of benchmark replacement rates that are overly complex to calculate or that have the potential to conflict with other Board-selected replacement rates creating ambiguous or confusing scenarios. Credit unions, and especially smaller credit unions, often struggle with limited staffing and the introduction of novel accounting issues can strain a credit union's operations. Because the Board's proposed benchmark replacement selections vary by type of contract, there is potential for hedging mismatch issues. For example, a loan that referenced 6-month USD LIBOR would switch to 6-month Term SOFR, while a derivative transaction that hedged the loan would switch to 6-month compounded average SOFR. This scenario could result in flawed hedging and has the potential to create accounting issues. Finally, NAFCU requests that the Board consider issuing a broad range of alternative rates to best accommodate the judgement of individual credit unions that will rely on the safe harbor granted by the LIBOR Act and also want to guard against asset-liability mismatch issues.

The Board should work to avoid any mismatch between their benchmark replacement rates and spare credit unions from additional burdens. Despite these concerns, NAFCU appreciates the proposed regulation's provision of continuity of contracts and litigation related safe harbor protections in connection with the selection or use of the applicable Board-selected benchmark replacement. NAFCU has continuously advocated for legislative and regulatory action to ensure that credit unions with Tough Legacy Contracts have a path forward for these contracts and that they are protected from litigation risk as LIBOR sunsets.

Conclusion

NAFCU appreciates the opportunity to provide comments on this NPRM. NAFCU supports the Board's decision to use SOFR-based benchmark replacement rates and appreciate the continuity of contract and litigation safe-harbor that this proposed regulation provides. NAFCU asks that the Board work to reduce costs and complexity associated with implementation of these regulations and minimize any mismatch between the Board-selected replacement rates. If we can answer any questions or provide you with additional information, please do not hesitate to contact me at 703-615-5109 or jakin@nafcu.org.

Sincerely,

James Akin
Regulatory Affairs Counsel