ICBA
INDEPENDENT COMMUNITY
BANKERS of AMERICA®

August 26, 2022

Ms. 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

Dear Ladies and Gentlemen:

The Independent Community Bankers of America ("ICBA")[1] appreciates the opportunity to comment on the notice of proposed rulemaking titled "Regulation Implementing the Adjustable Interest Rate (LIBOR) Act" ("Proposal"). This Proposal is designed to implement the provisions of the Adjustable Interest Rate (LIBOR) Act ("Act"), legislation passed in March of 2022 to mandate a uniform solution to systematically replace financial contracts that reference use of the London Interbank Offered Rate ("LIBOR") at various tenors spanning from overnight to one year.

The use of LIBOR, a longstanding and widely used reference rate for financial contracts in the global capital markets, has been repeatedly criticized by bank regulatory agencies worldwide because of weaknesses in its governance that have led to LIBOR panel banks manipulating the rate. The United Kingdom's Financial Conduct Authority, the regulator for LIBOR's administrator, has announced that LIBOR will be discontinued after June 30, 2023. Therefore, it is critical for the banking regulators to address so-called "tough legacy contracts"—those contracts that reference USD LIBOR and will not mature by June 30, 2023, but which lack adequate fallback provisions providing for a clearly defined or practicable replacement benchmark following the cessation of USD LIBOR. Without

[1] The Independent Community Bankers of America® creates and promotes an environment where community banks flourish. ICBA is dedicated exclusively to representing the interests of the community banking industry and its membership through effective advocacy, best-in-class education, and high-quality products and services. With nearly 50,000 locations nationwide, community banks constitute roughly 99 percent of all banks, employ nearly 700,000 Americans and are the only physical banking presence in one in three U.S. counties. Holding nearly $5.9 trillion in assets, over $4.9 trillion in deposits, and more than $3.5 trillion in loans to consumers, small businesses and the agricultural community, community banks channel local deposits into the Main Streets and neighborhoods they serve, spurring job creation, fostering innovation and fueling their customers' dreams in communities throughout America. For more information, visit ICBA's website at *www.icba.org*.

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the clear designation of a benchmark replacement rate and associated credit spread to existing LIBOR financial contracts where a replacement mechanism cannot be relied upon, these tough legacy contracts would be unnavigable by issuers, holders, administrators, and related parties.

The Proposal

The Act covers the resolution of three different types of LIBOR contracts and identifies those contracts that will need a comprehensive solution to replace existing reference rates.

1. Contracts in the first category have fallback provisions that establish a replacement rate that is not tied to LIBOR and does not require any person absent the duties of the administrator to obtain quotes for interbank lending or deposit rates. Such first category contracts are expected to follow their fallback provisions for replacing the benchmark interest rate once LIBOR ceases to be published or relied upon to be a representative rate.
2. Contracts in the second category do not contain fallback provisions or contain fallback provisions that identify a benchmark replacement based on US LIBOR values or require a person to obtain quotes for interbank lending or deposit rates. Second category contracts under the Act are subject to a benchmark rate replacement as selected by the Federal Reserve based on the Secured Overnight Financing Rate ("SOFR") plus a spread adjustment. Persons who use the Federal Reserve benchmark replacement shall not be subject to any claim or cause of action in law or equity or request for equitable relief,or have liability for damages arising out of the use of the replacement benchmark.
3. Third category contracts contain fallback provisions that authorize the determination of a benchmark replacement rate but the person designated to select the benchmark interest rate replacement fails to select a rate before the earlier of the LIBOR replacement date or the latest date for selecting a benchmark rate replacement. Under these contracts, the replacement rate becomes the Federal Reserve selected benchmark replacement. If the person designated to select the benchmark replacement rate chooses the Federal Reserve selected benchmark replacement rate, the selection must be irrevocable, made by the earlier of the LIBOR replacement date and the last date available to select a benchmark replacement rate under the terms of the contract, and used in any determinations of the benchmark interest rate occurring on or after the LIBOR replacement date. A person who chooses the Federal Reserve benchmark replacement rate generally shall not be subject to any claim or cause of action in law or equity or request for equitable relief, or have liability for damages arising from selecting the Federal Reserve benchmark replacement.

The proposed rulemaking applies the provisions of the Act to the types of contracts listed above that reference the overnight, one-month, three-month, six-month, or 12-month LIBOR rate tenors or have terms that do not clearly define a practicable replacement benchmark for LIBOR. Application of the proposed rulemaking only applies to existing contracts governed by federal or state law. Contracts under the proposed rulemaking listed above are known as covered contracts and, as specifically identified above have LIBOR benchmark reference rates with no fallback provisions, have fallback provisions that do not

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identify a specific benchmark replacement and determining person, or have fallback provisions that identify a determining person but that person has failed to select a benchmark replacement by the earlier of the LIBOR replacement date and the latest date for selecting a benchmark replacement according to the terms of the contract. A covered contract would not apply where the parties to the contract have agreed in writing that the contract will not be subject to the Act. LIBOR contracts would not be covered contracts as identified above when they have fallback provisions that identify a specific benchmark replacement, the LIBOR contract identifies a determining person that has selected a benchmark replacement, or the parties to the contract have agreed in writing that the contract shall not be subject to the LIBOR Act.

The proposed rule raises the question of the publication of synthetic LIBOR reference rates after the date that LIBOR fails to be representative of the interbank offered rate (potentially occurring on or around June 30, 2023) but does not provide a specific solution. The proposed rule scopes out these contractual relationships from the definition of a covered transaction because fallback provisions exist.

The proposed rule implements Federal Reserve selected benchmark replacements for specific types of LIBOR referenced contracts. Derivative contracts would adhere to the International Swaps and Derivatives Association ISDA 2020 IBOR Fallbacks Protocol to amend existing derivative contracts, which develops a rate equal to SOFR compounded in arrears based on the applicable tenor plus a stated spread adjustment. For cash transactions that are not consumer loans or covered government service enterprise ("GSE") contracts, overnight LIBOR will be replaced by SOFR plus a static spread adjustment of 0.644 basis points. Where the cash transaction requires a tenor extending beyond overnight, the proposed rule would establish the existing LIBOR tenor with the corresponding SOFR tenor as administered by the CME Group Benchmark Administration, Ltd[2] plus a tenor spread adjustment listed in the Act.

Cash transactions that are consumer loans will follow the Federal Reserve approved replacement benchmark rate with the corresponding SOFR tenor as determined by CME Group with a one-year transition tenor spread adjustment to prevent borrowers from experiencing significant changes in borrowing rates on and after the LIBOR replacement date. During the one-year transition period, the replacement benchmark will incorporate the difference between the benchmark replacement rate and the corresponding LIBOR tenor determined as of the day immediately before the LIBOR replacement date to the applicable tenor spread adjustment specified in the Act. Cash transactions that are deemed to be covered GSE contracts would follow SOFR plus the static spread adjustment for contracts referencing overnight LIBOR. For GSE contracts that reference tenors beyond overnight to 12 months, the proposed

[2] CME Group Benchmark Administration, Ltd is a registered benchmark administrator, authorized and supervised by the UK Financial Conduct Authority (FCA). CME Group supplies term SOFR reference rates that provide an indication of the forward-looking measurement of overnight SOFR, based on market expectations implied from derivatives markets.

rule selects 30-day average SOFR plus the applicable tenor spread adjustment as specified in the Act. This approach is consistent with GSE application of 30-day compounded SOFR to replace US LIBOR.

ICBA's Comments

ICBA appreciates the commitment of the Alternative Reference Rate Committee ("ARRC"), the Federal Reserve, other prudential bank regulators at the national level, as well as state banking agencies for their efforts to seek an appropriate and effective alternative to the use of LIBOR in financial contracts including cash lending products, deposits, and interest rate derivative contracts with community bank counterparties. As a member of the ARRC, ICBA is able to effectively communicate to regulators, standard setters, and key capital markets participants the concerns of community bankers as they navigate the transition away from LIBOR as a key reference rate in their financial contracts to a new reference rate endorsed by prudential bank regulators. The development of SOFR as a transparent and viable alternative to LIBOR and the inclusion of matching tenors to properly discount cash flows has provided a practical solution to the complex problem of identifying an alternative reference rate that reflects market risks.

ICBA is concerned that upcoming changes to financial contracts that currently reference LIBOR may not be fully understood by all impacted parties. In past conversations with ICBA, prudential bank regulators have acknowledged the need to educate member banks, consumers, other issuers of financial products, and impacted industry groups on the need to transition reference rates from LIBOR to a viable alternative like SOFR and what impact such a transition will have on financial instruments that currently use LIBOR as the designated reference rate. ICBA continues to believe that such education and awareness of key reference rate changes is warranted in light of the number of financial products outstanding that continue to reference LIBOR. Additionally, increased use of adjustable-rate financial products in consumer and commercial finance further highlights our concerns. ICBA requests that the regulators provide an educational response to impacted parties to both alert them to potential upcoming changes to their financial contracts and explain how such changes could affect them. For example, regulators could partner with industry groups like ICBA and capital markets participants to give community banks foundational education on how LIBOR will transition to other reference rates like SOFR, how SOFR and its key tenors are calculated, other alternatives to SOFR that regulators can support that provide a sound interbank offering rate, and how community banks should think about the use of interest-rate-sensitive financial products in their asset-liability management.

ICBA believes that while SOFR represents a solid path forward for the transition of financial contracts referencing LIBOR that will continue beyond the point of LIBOR's representation as a viable reference rate, other interbank borrowing rates may arise in the future that better reflect the true risk-free references needed in community bank lending and may gain traction as industry-accepted benchmark interest rates. If such rates ever rise to the level of common industry acceptance, ICBA asks that prudential bank regulators provide a path to allow community banks to embrace those reference rates as benchmark interest rates where appropriate for bank lending, derivatives, and cash products.

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ICBA appreciates the opportunity to provide comment on this proposed rule and hopes that the Board of Governors of the Federal Reserve System will consider our observations. If you have any questions or would like additional information, please do not hesitate to contact me at james.kendrick@icba.org.

Sincerely,

/s/

James Kendrick
First Vice President, Accounting & Capital Policy