June 5, 2020

Board of Governors of the Federal Reserve System
20th Street and Constitution Avenue, NW
Washington, DC 20551

Attention: Staff Group for the Term Asset-Backed Loan Facility
Cc: Ann E. Misback, Secretary

Ladies and Gentlemen:

This comment and request for guidance is submitted by the Business Law Section (the “Section”) of the American Bar Association on behalf of the Committee on Securitization and Structured Finance (the “Committee”) regarding the establishment of the Term Asset-Backed Securities Loan Facility (the “TALF”) by the Board of Governors of the Federal Reserve System (the “Board”) on March 23, 2020, pursuant to its authority under Section 13(3) of the Federal Reserve Act (the “Act”).

The views expressed herein represent the views of the Section. They have not been approved by the House of Delegates or the Board of Governors of the American Bar Association and, accordingly, should not be construed as representing the position of the Association.

We appreciate the willingness of the Board and its staff as well as the Federal Reserve Bank of New York (“FRBNY”) and its staff to work with us and with other market participants in adjusting the terms of the TALF as reflected in the May 20, 2020 TALF term sheet (the “Updated Term Sheet”), the FAQs: Term Asset-Backed Securities Loan Facility published by the FRBNY on May 20, 2020, as updated May 26, 2020 (the “FAQs”), and the Master Loan and Security Agreement (“MLSA”). The Section is submitting this letter to:

1. request that either: (a) the requirement for a borrower to certify that it is unable to secure adequate credit accommodations from other banking institutions (the “Credit Certification”) be removed or, in the alternative, (b) additional clarification be provided as to the acceptable bases on which a borrower or its TALF agent can determine that the only available lending is “at prices or on conditions that are inconsistent with a normal, well-functioning market;” and

2. address concerns regarding material ambiguities in the Material Investor definition as it relates to foreign government ownership of the TALF borrower or the manager of a TALF borrower that is an investment fund.
Requiring Borrowers to Submit a Credit Certification is Problematic and May Impede the Key Goals of the TALF Structure

As business lawyers, we are concerned that the requirement to provide a Credit Certification subjects TALF borrowers to an unusual risk of liability that may be grounded in something as simple as a difference of opinion on what constitutes “normal market conditions” for asset-backed securities (“ABS”). As a result, the Credit Certification may make it more difficult to attract the volume of investors needed to achieve the market relief that the TALF is designed to effect.

Unlike the other programs established by the Board to address the market dislocation created by the COVID-19 pandemic, the TALF program is designed to “help meet the credit needs of consumers and businesses by facilitating the issuance of [ABS] and improving the market conditions for ABS more generally.” It is not a program to provide financing to individual borrowers that are in need of credit accommodations but rather is a program that is dependent on the participation of non-conventional investors that may not ordinarily invest in ABS. In fact, many of the borrowers that are being formed to support the TALF program are being specifically formed for the sole purpose of providing the equity to support the program. Indeed, traditional investments in highly-rated ABS are not typically financed through borrowing, meaning that there isn’t an obvious basis for TALF borrowers to make a determination about changed credit conditions.

According to the Updated Term Sheet, “TALF will serve as a funding backstop to facilitate the issuance of eligible ABS on or after March 23, 2020.” If this funding backstop works, it will be because it lowers the overall cost of funds to an issuer while providing a return to the TALF borrower with the leverage provided by the TALF. The non-recourse nature of the TALF loan further supports this goal by giving the borrower confidence that it is not taking a risk of loss beyond the value of the collateral supporting the TALF loan.

By its nature, financing under the program is available only to acquire or finance eligible ABS collateral. As a result, the credit provided by the FRBNY under the TALF program is by definition not a credit accommodation to a specific borrower but is instead a credit support for ABS collateral, the issuance of which supports the availability of credit in the market as a whole.

In light of the nature of the program, the Credit Certification creates significant uncertainty for market participants because of the lack of concrete guidance regarding the facts upon which a Credit Certification is to be based. The current guidance provided in the May 26, 2020 FAQs states that—

In making this certification, a TALF participant may rely on unusual economic conditions in the ABS market or markets intended to be addressed by the TALF, such as ABS spreads that are elevated relative to normal market conditions. Lack of adequate credit does not mean that no credit is available. Credit
may be available, but inadequate in its amount, price, or terms because, for example, ABS spreads are elevated relative to normal market conditions.\(^1\)

The current FAQs do not provide strong guidance about what objective factors or information should be used by a person making the Credit Certification to determine the diligence that such person must undertake to support the fact attested to—that the borrower is unable to secure adequate credit accommodations from other banking institutions. It is troublesome for a borrower to attest affirmatively to whether other sources of lending are available because what constitutes “normal market conditions” is subject to a wide variety of interpretations that are likely to be evaluated differently in hindsight. This is especially true when under normal market conditions ABS market participants generally do not use leverage to finance their purchases of ABS. Furthermore, a borrower’s individual circumstances or creditworthiness may not allow it to access credit even though others can or can do so on better terms than are available to such borrower.

Indeed, because the Credit Certification does not define precisely what an “adequate credit accommodation” means in the context of a program that does not provide financing directly to an individual business or consumer, we are concerned that a borrower will have difficulty concluding that it has sufficient information to execute a Credit Certification without taking on unusual liability. Attesting to facts that can only be based largely on subjective belief about what constitutes normal market conditions creates a risk of liability that is compounded by the absence of a knowledge qualifier or a good faith safe harbor in the MLSA text.

A borrower could face potential liability for acceleration of a TALF loan and assertion that the TALF loan is no longer non-recourse, based on a claim that the Credit Certification is inaccurate, even where the borrower believed that the market was not a normal, well-functioning market. Other attendant liability may arise in the form of regulatory enforcement action, civil liability arising under the False Claims Act, and potential qui tam actions. The risk associated with submitting a Credit Certification attesting to a fact that is challenging to objectively support may be too great, and may result in substantially reduced participation in the TALF.

\(^1\) We note that the MLSA provides very similar guidance in explaining that: “Being unable to secure adequate credit accommodations does not mean that no credit from other sources is available to the borrower. Rather, the borrower may certify that it is unable to secure “adequate credit accommodations” because the amount, price, or terms of credit available from other sources are inadequate for the borrower’s needs during the current unusual and exigent circumstances. Borrowers are not required to demonstrate that applications for credit had been denied by other lenders or otherwise document that the amount, price, or terms of credit available elsewhere are inadequate.”
The Statutory Basis for the Credit Certification can be Satisfied in an Alternative Manner

Given the uncertainty regarding the basis for making the Credit Certification, we respectfully request that the Board and the FRBNY reassess the need to include the Credit Certification as a requirement on the part of borrowers to participate in the TALF. As noted in the FAQs, the TALF is not designed to provide loans directly to businesses or consumers but is instead “designed to increase credit availability for businesses and consumers by facilitating the issuance of ABS backed by loans to consumers and businesses at more normal interest rate spreads.” To achieve this goal, the TALF is designed to serve as a mechanism to encourage TALF borrowers to enter a market they otherwise would not participate in because the characteristics of the market are too uncertain, adverse or distorted to participate in.

We note that neither Section 13(3) nor the Board’s Regulation A absolutely requires that a Credit Certification be submitted. Section 13(3) provides that, in extending credit under an emergency lending program, the Federal Reserve Bank extending the credit “shall obtain evidence that such participant in any program or facility with broad-based eligibility is unable to secure adequate credit accommodations from other banking institutions.” There is no requirement that such evidence be in the form of a borrower certification or otherwise be obtained directly from the borrower. The Credit Certification is only one of many forms of relevant evidence that a Federal Reserve Bank may collect. Indeed, the borrower certification language was only added to Regulation A in 2015, even though, as the Board noted, “Section 13(3) has always required that a Federal Reserve Bank, prior to extending credit to any participant in a program or facility under that section, obtain evidence that such participant is unable to secure adequate credit accommodations from other banking institutions.”

Importantly, the first TALF program, established by the Board in 2009, did not require a Credit Certification to be made by borrowers, even though many of the other programs at that time required some form of credit certification. We do not see any legal reasons why the current TALF program would require a Credit Certification when the program is structured in substantially the same way as the first TALF program and there has been no change in law that would now require a Credit Certification to be made.

Given that the FRBNY may rely on ABS market conditions without certifications from TALF borrowers, we believe that requiring the Credit Certification unnecessarily adds a risk of liability that could impede participation in the TALF, thereby potentially undermining the usefulness of the TALF program. The ABS market is a transparent market, and the FRBNY has the ability to monitor credit spreads and other relevant data in both the primary and secondary market without such information being provided by the

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borrower. We submit that the market information that is otherwise available to the FRBNY through its normal monitoring functions is much more valuable and determinative in any event than a certification from a TALF borrower. We also submit that, in the case of the TALF, it may be more appropriate for the FRBNY to rely on a finding by the Board that adequate credit accommodations are not available in the ABS markets, which may be self-evident by the Board’s establishment of the TALF, rather than a Credit Certification.

If Credit Certifications Are Required, More Guidance is Needed

Should the Board and the FRBNY nevertheless require Credit Certifications to be submitted, we request that more guidance regarding the diligence that should underlie a Credit Certification be provided. In particular, we believe it would be helpful if the Board or the FRBNY affirmatively states that the Credit Certification can be based on one or more of the following factors:

- The statement of the TALF agent that it would not independently provide loans to the borrower with terms as good as or better than a TALF loan (including, without limitation, the non-recourse nature of the TALF loan and lack of a mark-to-market or margin call term, and not only the pricing of the loan) and making clear that the TALF agent is not responsible for inquiring with any other financial institution as to whether alternative credit accommodations are available.

- That the person making the certification is unaware of any credit accommodations available to it on terms as good or better than a TALF loan.

- Other objective factors such as elevated rates and haircuts in the ABS repo markets or securities repo markets generally.

We also suggest that, if a Credit Certification requirement remains, the certification be a good faith certification based on the reasonable belief of the person making the certification and speak only as of the loan subscription date and not at any time thereafter. We also suggest that the certification provide a form of reasonable diligence basis for the certification similar to what is provided in MLSA Appendix 2C: Form of Borrower Conflicts of Interest Certification.

The Foreign Government As a Material Investor Prohibition Presents Compliance Issues For Publicly Traded Borrowers and Publicly Traded Managers of Investment Fund Borrowers

The current MLSA provides that if a borrower is no longer an Eligible Borrower then an automatic Collateral Enforcement Event shall have occurred. An automatic Collateral Enforcement Event has adverse consequences, especially when the borrower is an investment fund, inasmuch as the immediate payment of the loan would ultimately harm the investment fund’s investors. Accordingly, TALF borrowers must be diligent in monitoring their status as an
Eligible Borrower. However, there are certain questions raised by the current guidance in determining whether a borrower is an Eligible Borrower.

The FAQs provide that a borrower is expected to have in place a mechanism for determining whether the borrower has a Material Investor that is a foreign government. This requirement is unworkable for publicly-traded companies, which cannot determine share ownership on their own, given the market infrastructure through which shares are held, and so would only become aware of a large holder if and when the holder disclosed its position. Instead, we ask that the FAQs include the same guidance provided in the 2009 TALF FAQs, which permitted borrowers and TALF agents to rely on public filings required to be made by large shareholders or control persons of publicly traded companies.

In addition, a publicly-traded company cannot control whether a foreign government acquires ownership of the company’s securities on the open market. Accordingly, we believe that the subsequent acquisition by a foreign government without the knowledge of a fund manager or borrower that results in such foreign government becoming a Material Investor should not create an automatic Collateral Enforcement Event with respect to a publicly-traded borrower or manager or a publicly-traded ultimate parent company of a borrower or manager.

There is also uncertainty regarding what constitutes a foreign government. We believe it would be helpful if guidance were provided regarding how to monitor for a foreign government Material Investor, especially in light of the many forms in which foreign governments may invest in a company. For example, it is unclear how many layers of entities (and what percentage of ownership makes an entity relevant) must a borrower look through to determine if a foreign government is a Material Investor. It is also unclear whether a foreign public pension fund or sovereign wealth fund should be deemed to be a foreign government.

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The Section appreciates the opportunity to submit this request for removal or modification the Credit Certification requirement and for modification of the foreign investor requirement, and respectfully requests that the Board consider our recommendations. The leaders of the Committee and the members of the Committee’s comment letter task force copied below are available to discuss these matters and to respond to any questions at your convenience.

Very truly yours,

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