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Christopher Kirkpatrick
Secretary of the Commission
Commodity Futures Trading Commission
Three Lafayette Center
1155 21st Street NW
Washington, D.C. 20581

*Submitted via CFTC Comments Portal*
*https://comments.cftc.gov*

**Re: <u>Margin Requirements for Uncleared Swaps for Swap Dealers and Major Swap Participants</u>** <u>(RIN 3038-AE71)</u>

Ladies and Gentlemen:

Navient Corporation and its subsidiary Navient Solutions, LLC (collectively, "Navient") appreciate the opportunity to submit this letter in response to the request of the Commodity Futures Trading Commission (the "Commission") for comments on the proposal to amend the Margin Requirements for Uncleared Swaps for Swap Dealers and Major Swap Participants ("CFTC Margin Rule") to clarify that any legacy uncleared swap that is not now subject to the margin requirements of the CFTC Margin Rule would not become so subject if it is amended to conform to the QFC Rules ("Proposed Amendment").

We support the Commission's initiatives to protect the integrity of the swaps markets by establishing margin requirements and we appreciate the Commission's recognition of impacts of the CFTC Margin Rule on entities that are not Covered Swap Entities ("CSE"). Navient also commends the coordinated effort between the Commission and the Office of the Comptroller of the Currency, the Board of Governors of the Federal Reserve System, the Federal Deposit Insurance Corporation, the Farm Credit Administration, and the Federal Housing Finance Agency (collectively, the "Agencies") to reexamine the CFTC Margin Rule. We support the Proposed Amendment and we respectfully request that the Commission expand the Proposed Amendment to clarify and codify CFTC Letter No. 17-52 which provides relief from the CFTC Margin Rule to uncleared swap contracts entered into with special purpose vehicles ("SPV") created for securitization transactions organized prior to its CSE-counterparty's applicable compliance date ("legacy securitizations").

**Background on Navient**

Navient is a leading provider of asset management and business processing solutions for education, health care, and government clients at the federal, state, and local levels. Navient is the largest private sector holder of education loans insured or federally guaranteed under the Federal Family Education Loan Program ("FFELP"). In addition, we hold the largest portfolio of private education loans and originate private education refinance loans.

Navient is a frequent sponsor of securitizations backed by FFELP loans and private education loans, including private education refinance loans. As of March 31, 2018, Navient had $71.7 billion aggregate outstanding principal of ABS backed by FFELP loans and $13.9 billion aggregate outstanding principal of ABS backed by private education loans.

We mitigate financial risk associated with these loans through a strategy that includes the use of fair value and cashflow derivative hedges that minimize the economic impact of changes in interest rates and foreign exchange rates.

**Comments to Proposed Amendment**

Navient supports the amendments proposed by the Commission to safeguard legacy swaps from being subject to the CFTC Margin Rule when the swap is amended solely to comply with the requirements of the QFC Rules. We appreciate the Commission's recognition that the CFTC Margin Rule did not contemplate that legacy swaps might be amended to meet other regulatory requirements, and we especially appreciate the Commission's efforts to address conflicts through no-action relief, staff letters, and proposed amendments such as this.

We agree that the QFC Rules are a prime example of a conflict imposed on legacy swaps by the CFTC Margin Rule. However, there are additional situations outside of the control of the end user of a legacy swap that cannot be navigated because of the requirements of the CFTC Margin Rule. For example, legacy swap contracts may need to be amended or novated in connection with the cessation of a commonly used benchmark rate, such as the London Inter-bank Offered Rate (LIBOR), or as a result of the downgrade of the credit rating of a swap counterparty below a minimum ratings threshold.[1] Additionally, a legacy swap might be amended or novated to reduce risk and in a way that is not economically equivalent to entering into a new uncleared swap. In fact, guidance within the base framework for global swap margin rules noted that, unless an amendment is intended to *extend* an existing contract to evade margin rules, an amended existing contract would not qualify as a new contract.[2] Non-U.S. legacy swaps maintain

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[1] The International Swaps and Derivatives Association discusses additional other instances requiring amendments in its letter to the Agencies on April 20, 2018. Please see: https://www.regulations.gov/document?D=OCC-2018-0003-0006

[2] See, "Margin requirements for non-centrally cleared derivatives" jointly released September 2013 by the Basel Committee on Banking Supervision and the Board of the International Organization of Securities Commissions.

the ability to make amendments without becoming subject to margin requirements because the rules adopted by non-U.S. jurisdictions reflect the base framework guidance.[3] Unfortunately, this guidance was not reflected in the CFTC Margin Rule or in the rules adopted by the Agencies (collectively, "U.S. Margin Rules"). We encourage the Commission to continue to examine the conflicts imposed on legacy swaps by the CFTC Margin Rule and reconsider harmonizing with the rules of foreign jurisdictions.

**Codifying Related No-Action Relief**

Swaps are an ideal method to hedge commercial risks associated with interest rate and foreign currency mismatches and are used by securitization SPVs to hedge those risks within the securitization structure.[4] Swaps entered into by securitization SPVs do not pose the risk of nonpayment as other financial end users and, therefore, do not pose the same risks to the safety and soundness of CSEs or of the broader financial system.[5] Further, securitization SPVs commonly do not have the contractual authority to allocate assets to post margin in compliance with the CFTC Margin Rule, causing a low likelihood that a securitization SPV would be able to amend or novate a legacy swap when the securitization transaction documents allow for or require that action.

We appreciate the Commission for acknowledging the significant difficulties faced by securitization SPVs and the work of the Commission to address aspects of the CFTC Margin Rule that impact the U.S. securitization market.[6] Furthermore, we are grateful for the

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[3] See, *e.g.*, Australian Prudential Regulation Authority Prudential Standard CPS 226, Japan Financial Services Agency Summary of the comments and the FSA's View on such Comments published on December 11, 2015, and Office of the Superintendent of Financial Institutions Canada Margin Requirements for Non-Centrally Cleared Derivatives.

[4] For further discussion about the use of swaps by securitization special purpose vehicles, please refer to the comment letters submitted by Navient to the Commission on February 24, 2017, July 13, 2017 and August 18, 2017.

[5] A CSE that enters into a swap with a securitization SPV is protected against the risk that a securitization SPV counterparty will fail to satisfy its payment obligations under a swap contract. Structural characteristics and credit enhancements offset the risk to the CSE and the financial system arising from the non-cleared swap. A more robust description of securitization SPVs and the protections afforded to swap providers who enter into swap contracts with securitization SPVs was provided in a comment letter submitted by the Structured Finance Industry Group to the Commission and the Agencies on November 24, 2014 ("SFIG Comment Letter"), and in a comment letter submitted by The Financial Services Roundtable to the Agencies on November 24, 2014. The letters can be found at: https://comments.cftc.gov/PublicComments/ViewComment.aspx?id=60007 and https://www.regulations.gov/document?D=OCC-2011-0008-0155, respectively. The International Swaps and Derivatives Association directed the Agencies to the SFIG Comment Letter in a comment letter submitted to the Agencies on November 24, 2014, which can be found at: https://comments.cftc.gov/PublicComments/ViewComment.aspx?id=60009

[6] See, *e.g.*, CFTC Letter No. 17-52 and CFTC Letter No. 15-21. The Division of Swap Dealer and Intermediary Oversight issued a No-Action Position for variation margin requirements applicable to swaps with legacy special

transparency provided by the Commission through the recently released white paper, and are encouraged that the Commission may consider providing relief to certain types of special purpose vehicles.[7]

Rating agencies view the U.S. Margin Rules as "credit negative" because of the restrictions on a legacy securitization SPV's ability to novate a swap contract to a new counterparty.[8] A downgrade in the credit rating assigned to a bond negatively affects the investor of the bond. We are grateful that the Commission took action to protect investors from such harm by issuing CFTC Letter No. 17-52. Unfortunately, Moody's Investors Service interpreted the scope of the relief to be narrow.[9] To the detriment of investors, Moody's Investors Service took actions that adversely affect the market value of an ABS, citing the CFTC Margin Rule. For example, on January 11, 2018 Moody's Investors Service downgraded the ratings assigned to 26 classes of ABS valued at approximately $9.6 billion and attributed the action to the reduced likelihood of counterparty replacement due to new margin requirements.[10]

We respectfully request that the Commission expand the scope of the Proposed Amendment to clarify and codify CFTC Letter No. 17-52. We believe that codifying and clarifying CFTC Letter No. 17-52 will satisfy concerns raised by Moody's Investors Service. Therefore, we respectfully request the Commission to clarify CFTC Letter No. 17-52 to (i) specify that the relief applies in circumstances in which a SPV enters into a swap with a replacement counterparty following the

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purpose vehicles on October 27, 2017, and issued a No-Action Position for certain regulations applicable to swaps with legacy special purpose vehicles on March 31, 2015.

[7] See, "Swaps Regulation Version 2.0: An Assessment of the Current Implementation of Reform and Proposal for Next Steps" authored by Chairman J. Christopher Giancarlo and Chief Economist Bruce Tuckman released by the Commission on April 26, 2018.

[8] The credit rating assigned to an ABS addresses the likelihood of timely payment of stated interest and the payment of principal at final maturity. Securitization SPVs typically enter into swap contracts as a means to manage a mismatch in the interest rate or currency between payments on the underlying loan assets owed to the securitization SPV and the payments owed by the securitization SPV on its ABS. The hedge provided by the swap contract helps ensure the stability of the cash flows available to make payments on the ABS. For more information about rating agency perspective regarding the impact of swap margin rules on existing securitizations, please see: https://www.fitchratings.com/site/pr/1014938 and https://www.moodys.com/researchdocumentcontentpage.aspx?docid=PBS_1038135.

[9] Moody's Investors Service discusses its interpretation of the no-action relief provided by CFTC Letter No. 17-52 in a Sector Comment made public on December 12, 2017, which can be found at: https://www.moodys.com/research/Structured-Finance-Global-CFTC-relief-from-margining-for-SPV-swaps--PBS_1103746

[10] Moody's Investors Service reduced the value of certain notching uplifts in connection with swaps that Moody's interprets would become subject to margining requirements upon counterparty replacement. Future downgrades will be driven by downgrades in the ratings assigned to CSE swap counterparties. The press release provides more information, which can be found at: https://www.moodys.com/research/Moodys-concludes-reviews-of-12-student-loan-ABS-securitizations-following--PR_377893

default of the original counterparty even in instances when the original counterparty defaulted prior to being downgraded by Moody's Investors Service, and (ii) clarify the relief applies to variation and initial margin posting requirements of the CFTC Margin Rule.[11]

**Equal Treatment for Securitization Vehicles**

In addition, we continue to believe that securitization SPVs should be provided an exception from the U.S. Margin Rules. We respectfully reiterate our request to amend the CFTC Margin Rule to provide an exception to swaps entered into by securitization SPVs that meet certain "Qualified Loan Financing" criteria, as outlined in comment letters previously submitted to the Commission by Navient.

Following the recommendation of the U.S. Department of the Treasury to harmonize margin rules with non-U.S. jurisdictions[12], we believe our request for an exception for securitization SPVs aligns with this recommendation and would level the securitization markets domestically and internationally.[13]

Domestic Implications of U.S. Margin Rules on Securitizations

The CFTC Margin Rule has made it infeasible for securitization SPVs sponsored by companies other than "captive finance companies"[14] to enter into a swap.[15] It is our understanding that, outside of captive finance companies, securitization derivative hedging[16] in the U.S. has ceased since March of 2017.

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[11] *See id,* section Principal Methodology "Factors that would lead to an upgrade or downgrade of the ratings".

[12] The U.S. Department of the Treasury released a report titled "A Financial System That Creates Economic Opportunities: Capital Markets" on October 6, 2017 detailing how to reform the U.S. regulatory system for the capital markets, in response to Executive Order 13772. The report can be found at: https://www.treasury.gov/press-center/press-releases/Documents/A-Financial-System-Capital-Markets-FINAL-FINAL.pdf.

[13] The Coalition for Derivatives End-Users discusses the importance of consistent treatment of securitization SPVs on page 9 of its letter to the Commission dated September 29, 2017. This letter can be found at: https://comments.cftc.gov/PublicComments/ViewComment.aspx?id=61410.

[14] See, *e.g.*, Section 2(h)(7)(C)(iii) of the Commodity Exchange Act for definition.

[15] Descriptions of the challenges faced by securitization SPVs to post margin and recommendations to exclude securitization SPVs from the rules were provided in a comment letter submitted jointly by the International Swaps and Derivatives Association and the Securities Industry and Financial Markets Association to the Commission on September 14, 2012, and in a comment letter submitted by the Japan Financial Markets Council to the Commission and the Agencies on November 21, 2014. The letters can be found at: https://comments.cftc.gov/PublicComments/ViewComment.aspx?id=58789 and https://comments.cftc.gov/PublicComments/ViewComment.aspx?id=60001, respectively.

[16] Excluding interest rate caps.

The CFTC Margin Rule provides an exception for a swap contract that hedges the commercial risk of a captive finance company, an exception that has been interpreted to cover any securitization SPV that is wholly-owned by, and consolidated with, a captive finance company.[17] Even though a securitization SPV qualifies as a financial end user due to its loan-pooling nature, captive finance companies are granted an exception from qualifying as a financial end user under the belief that the financing activities of such companies generally pose less systemic risk to the financial system. As it so happens, securitization SPVs meeting Navient's proposed Qualified Loan Financing criteria provide the same protections against the risk of nonpayment regardless of whether the securitization SPV is consolidated with a captive finance company. Therefore, all securitization SPVs meeting the proposed Qualified Loan Financing criteria should be granted the same exception afforded to captive finance companies.[18]

## Global Implications of U.S. Margin Rules on Securitizations

The Commission's position in the treatment of securitization SPVs differs from other jurisdictions causing disparity in securitization markets. Similar rules in foreign jurisdictions generally do not apply to swaps entered into by securitization SPVs, allowing ABS swap hedging to continue to occur outside of the U.S.[19] Securitization SPVs commonly enter into a cross-currency swap in order to compete in foreign securitization markets. However, the CFTC Margin Rule effectively prohibits U.S. securitization SPVs from competing in foreign-denominated securitization markets because it is infeasible for the SPV to enter into a cross-currency swap. Furthermore, swaps are the prevailing method to hedge interest rate mismatches and, therefore, will play an important role in the global transition to risk-free rates. This transition presents a need to hedge risk arising from the interest rate mismatches between legacy assets and financing standards that have transitioned to a new risk-free rate.[20] Unfortunately, U.S. securitization SPVs are impeded by the U.S. Margin Rules from entering into an interest rate

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[17] The Division of Clearing and Risk issued an interpretive letter to Ford Motor Credit Company LLC on May 4, 2015. CFTC Letter No. 15-27.

[18] A similar request and further discussion about the need to extend the relief awarded to captive finance companies to other securitization SPVs was provided in a comment letter submitted by the Coalition for Derivatives End-Users to the Commission on September 29, 2017, which can be found at: https://comments.cftc.gov/PublicComments/ViewComment.aspx?id=61410

[19] Jurisdictional differences in rules are discussed in research by Moody's Investors Service titled "Proposed Changes to Moody's Rating Criteria Reflect New Swap Margin Rules", which can be found at: https://www.moodys.com/researchdocumentcontentpage.aspx?docid=PBS_1062454. A discussion of the differences in the treatment of securitization SPVs by the Commission and the European Union was provided in a comment letter submitted by the Institute of International Bankers to the Commission and the Agencies on November 24, 2014, which can be found at: https://comments.cftc.gov/PublicComments/ViewComment.aspx?id=60020.

[20] For example, financing a group of LIBOR-indexed loans with debt obligation payments indexed to the Secured Overnight Financing Rate creates basis risk and reset risk that can be alleviated by a swap hedge.

swap. As a result of the CFTC Margin Rule, U.S. firms are placed at a competitive disadvantage to non-U.S. competitors.

**Concluding Remarks**

Thank you for considering our comments, and our request to protect investors through an expanded exception to the CFTC Margin Rule. Please do not hesitate to contact us if you have questions or desire clarification concerning any of the matters discussed in this comment letter. Please contact me via telephone at 302-283-4045 or via e-mail at chris.lown@navient.com. You can also contact Rachel Gleason George, Vice President & Deputy General Counsel, via telephone at 703-984-6585 or via e-mail at rachel.george@navient.com or Jennifer Earyes, Director, Treasury Risk, via telephone at 703-984-5623 or via e-mail at jennifer.earyes@navient.com.

Sincerely,

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