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4810-AS-P

DEPARTMENT OF THE TREASURY

[Docket No. TREAS-DO-2020-0007]

Development and Potential Issuance of Treasury Floating Rate Notes Indexed to the Secured Overnight Financing Rate.

AGENCY: Department of the Treasury.

ACTION: Notice and request for information.

SUMMARY: The Department of the Treasury (Treasury) is requesting comments on the possibility of issuing a floating rate note (FRN) indexed to the Secured Overnight Financing Rate (SOFR) published by the SOFR Administrator, currently the Federal Reserve Bank of New York (FRBNY). Treasury has not made a decision whether to issue FRNs indexed to SOFR (SOFR-indexed FRNs). Treasury will continue to weigh the merits of SOFR-indexed FRNs, and comments received as part of this request for information will serve as valuable input into this decision.

DATES: Comments are due by [INSERT DATE 45 DAYS AFTER DATE OF PUBLICATION IN THE FEDERAL REGISTER].

ADDRESSES: You may submit comments using any of the following methods:

Federal eRulemaking Portal: www.regulations.gov. Follow the instructions on the website for submitting comments.

E-mail: govsecreg@fiscal.treasury.gov. Include docket number TREAS-DO-2020-0007 in the subject line of the message.

All submissions should refer to docket number TREAS-DO-2020-0007. Please submit your comments using only one method, along with your full name and mailing address. We will post all comments on www.regulations.gov and www.treasurydirect.gov. In general, comments received, including attachments and other supporting materials, are part of the public record and are available to the public. Do not submit any information in your comments or supporting materials that you consider confidential or inappropriate for public disclosure.

FOR FURTHER INFORMATION CONTACT: Fred Pietrangeli, Director, Office of Debt Management, Office of the Assistant Secretary for Financial Markets, at debtmanagement@treasury.gov or Fredrick.Pietrangeli@treasury.gov. Questions about submitting comments should be directed to Lori Santamorena, Government Securities Regulations Staff, at (202) 504-3632 or govsecreg@fiscal.treasury.gov.

SUPPLEMENTARY INFORMATION:

I. Background

Treasury continually seeks to finance the government at the lowest cost over time, manage its liability profile, foster healthy secondary markets, and expand the investor base for Treasury securities. Treasury is examining potential new products in pursuit of these goals.

Following substantial analysis and consideration of input from market participants, in 2014 Treasury began issuing FRNs indexed to the 13-week Treasury bill rate (13-week T-bill FRNs). Since their launch, Treasury has issued more than $1.1 trillion of 13-week T-bill FRNs. A Treasury analysis released in 2017 showed that issuing 13-week T-bill FRNs had reduced realized interest costs by $1.3 billion (when compared to 2-year fixed-rate notes).[1]

In light of the success of the 13-week T-bill FRN program and recent market developments, Treasury is exploring the possibility of issuing SOFR-indexed FRNs.[2] Treasury has discussed the potential issuance of SOFR-indexed FRNs with the Treasury Borrowing Advisory Committee (TBAC),[3] the primary dealers,[4] and other Treasury market participants. These discussions have provided helpful feedback,[5] and Treasury now seeks additional views from the public on the questions below.

Treasury's primary motivation for exploring SOFR-indexed FRNs is the consideration of new debt products that can be issued at the lowest cost of financing for the U.S. government. Treasury is cognizant that its issuance decisions can have broader effects on other issuers and market practices. Regardless of any decision about issuing SOFR-indexed FRNs, Treasury, as an ex-officio member of the Alternative Reference

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[1] *See* 4th Quarter 2017 Treasury Borrowing Advisory Committee Discussion Charts, available at https://www.treasury.gov/resource-center/data-chart-center/quarterly-refunding/Documents/Q42017CombinedChargesforArchives.pdf.

[2] *See* October 30, 2019 Quarterly Refunding Policy Statement, available at https://home.treasury.gov/news/press-releases/sm810 and February 5, 2020 Quarterly Refunding Policy Statement available at https://home.treasury.gov/news/press-releases/sm896.

[3] TBAC is a federal advisory committee that advises Treasury on debt management and other topics. *See* 2nd Quarter 2019 TBAC Discussion Charts, available at https://www.treasury.gov/resource-center/data-chart-center/quarterly-refunding/Documents/q22019CombinedChargesforArchives.pdf and 3rd Quarter 2019 TBAC Discussion Charts, available at https://www.treasury.gov/resource-center/data-chart-center/quarterly-refunding/Documents/q32019CombinedChargesforArchives.pdf.

[4] The primary dealers serve as trading counterparties to FRBNY in its implementation of monetary policy. Primary dealers are also required to participate in all Treasury marketable securities auctions.

[5] *See* May 6, 2020 Quarterly Refunding Policy Statement, available at https://home.treasury.gov/news/press-releases/sm1001.

Rates Committee (ARRC), is committed to promoting the transition away from U.S. dollar London Interbank Offered Rate (LIBOR).[6]

II. Solicitation for Comments

Treasury invites views on the following topics. Please include: (1) the data or reasons, including examples, supporting any opinions or conclusions; (2) alternative approaches and options that should be considered, if any; and (3) any specific comments regarding general terms and conditions for the sale and issuance of Treasury SOFR-indexed FRNs.

**1. Market Demand**

1.1 Which types of investors would be the primary buyers of Treasury SOFR-indexed FRNs? Would Treasury SOFR-indexed FRNs attract new investor types or additional demand from existing Treasury investors? Assuming the possibility of a 1-year or 2-year maturity, how would the tenor of a Treasury SOFR-indexed FRN affect demand?

1.2 Please estimate annual demand for Treasury SOFR-indexed FRNs. Would demand be greater for a shorter tenor? How would potential growth in issuance of SOFR-indexed FRNs by other issuers affect long-term demand for Treasury SOFR-indexed FRNs?

**2. Pricing and Liquidity**

2.1 Would introducing a Treasury SOFR-indexed FRN help Treasury finance the government at the lowest cost over time? Why or why not?

2.2 How would you expect a Treasury SOFR-indexed security to price relative to a comparable maturity 13-week T-bill FRN security? How would this pricing vary across the economic cycle and interest rate environments? Please provide pricing estimates.

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[6] The ARRC is a group of private-market participants convened by the Board of Governors of the Federal Reserve System and FRBNY to help transition from U.S. dollar LIBOR to SOFR. See https://www.newyorkfed.org/arrc.

2.3 SOFR has risen significantly for certain short time periods, such as around some ends of months, quarters, and years. To what extent would such patterns, if they continue, affect the interest cost for Treasury on a SOFR-indexed FRN, the interest payments of which would be based on a SOFR averaged or compounded rate over a longer interest accrual period? To what extent would investors be willing to bid lower discount margins at auctions for Treasury SOFR-indexed FRNs in expectation of such patterns continuing? Please elaborate.

2.4 During the global financial crisis, repurchase agreement rates were persistently higher than Treasury bill rates. More recently, during the COVID-19 outbreak, liquidity in Treasury and other markets (including repurchase agreement markets) exhibited signs of stress. How would potential future periods of market stress affect SOFR? In a potential future period of market stress, how might interest costs for Treasury differ between a Treasury SOFR-indexed FRN and the 13-week T-bill FRN? Please elaborate.

2.5 How liquid would Treasury SOFR-indexed FRNs be in secondary markets? Please compare the expected liquidity of Treasury SOFR-indexed FRNs to Treasury bills, the existing 13-week T-bill FRN, and off-the-run short-dated coupons.

**3. Security Structure**

3.1 What are the primary considerations Treasury should evaluate when structuring a Treasury SOFR-indexed FRN? How would different potential security structures affect investment decisions by market participants, including with respect to activity in derivatives markets?

3.2 Some previously gathered feedback has suggested a 1-year final maturity for original issuance of a Treasury SOFR-indexed FRN. Is this maturity or another maturity preferable for a Treasury SOFR-indexed FRN? Please elaborate.

3.3. Is a quarterly issuance frequency with two reopenings appropriate for a Treasury SOFR-indexed FRN, similar to the existing 13-week T-bill FRN? What factors should Treasury consider in making this decision?

3.4 When during the month should Treasury auction SOFR-indexed FRNs? When should auctions settle?

3.5 Should interest on Treasury SOFR-indexed FRNs be calculated based on a simple average or a compounded average of SOFR? Should Treasury consider indexing the security to an average rate based on SOFR, such as those recently published by FRBNY as administrator for SOFR?[7] If so, what would be the optimal averaging period for a SOFR-indexed FRN?

3.6 What coupon frequency should be used for a Treasury SOFR-indexed FRN? Note that the existing 13-week T-bill FRN pays coupons quarterly. Would a semi-annual, or other coupon frequency be preferred? When during the month should coupon and principal payments be made?

3.7 Should the index rate for a Treasury SOFR-indexed FRN reset daily, weekly, or at some other frequency?

3.8 Should a Treasury SOFR-indexed FRN incorporate a lockout (i.e., last *k* rates for an interest period set at SOFR *k* days before the period ends), a lookback or “lag” (i.e., for

[7] For more information on the SOFR averages, see FRBNY, Statement Introducing the SOFR Averages and Index (March 2, 2020), available at https://www.newyorkfed.org/markets/opolicy/operating_policy_200302.

every day in the interest period, use SOFR from *k* days earlier), or a payment delay (i.e., coupon and principal payments made *k* days after the end of the interest period) in its structure?[8] If so, what values would be appropriate for each attribute? Please explain relevant considerations for these features.

3.9 In light of FRBNY's data contingency procedures for the publication of SOFR,[9] what contingency measures should Treasury consider incorporating into the terms of a SOFR-indexed FRN if SOFR, or an average rate based on SOFR, is temporarily unavailable or revised?

**4. Existing 13-week T-Bill FRN**

4.1 If Treasury decides to issue SOFR-indexed FRNs, what, if any, changes should Treasury make to the existing 13-week T-bill FRN issuance program?

4.2 Should Treasury issue FRNs indexed to both indices, or should Treasury consolidate FRN issuance on a single index?

4.3 If there is not sufficient demand for both Treasury FRNs to coexist, which index would generate the greater long-term demand and better meet Treasury's issuance objectives? Please elaborate.

4.4 Should Treasury consider issuing 13-week T-bill FRNs with a 1-year final maturity? How should the decision regarding issuance of Treasury SOFR-indexed FRNs affect this possibility?

**5. Market Transition**

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[8] See ARRC, A User's Guide to SOFR (April 2019), pp. 10-11, available at https://www.newyorkfed.org/medialibrary/Microsites/arrc/files/2019/Users_Guide_to_SOFR.pdf), and ARRC, ARRC Floating Rate Notes Working Group Statement On Use Of The SOFR Index (May 2020), available at https://www.newyorkfed.org/medialibrary/Microsites/arrc/files/2020/Statement_on_SOFR_Index.pdf.

[9] For additional information, see FRBNY, Additional information about the Treasury Repo Reference Rates, available at https://www.newyorkfed.org/markets/treasury-repo-reference-rates-information.

5.1 What proportion of likely investors is currently operationally ready to purchase Treasury SOFR-indexed FRNs?  For those investors that are not ready, what are the main impediments?  How much lead time and investment would be required for additional investors to become operationally ready to purchase Treasury SOFR-indexed FRNs? Would any of the security structure choices mentioned in Section 3 above affect the operational readiness of likely investors?

5.2 To what extent would Treasury's issuance of SOFR-indexed FRNs advance the overall market transition away from U.S. dollar LIBOR?  How would different market segments (e.g., FRNs, derivatives, business loans, consumer products) be affected by Treasury's decision to issue SOFR-indexed FRNs?  What effect would Treasury's issuance of SOFR-indexed FRNs have on the overall market transition away from LIBOR beyond that caused by current issuance of SOFR-indexed FRNs by other issuers? Please provide specific details of the cause and effect relationships you expect.

Brian Smith,

Deputy Assistant Secretary for Federal Finance.

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