Federal Housing Finance Authority
400 Seventh Street, SW, Eighth Floor
Washington, DC 20219

RE: RIN-2590-AA95

August 17, 2020

To Whom It May Concern:

This letter contains a response to your request for comment on RIN-2590-AA95 "Enterprise Regulatory Capital Framework" from the perspective of a current beneficial owner of preferred shares of Fannie Mae and Freddie Mac and future potential equity capital source.

<u>Comments on Section VII: Capital Buffers, Subsection C: Payout Restrictions</u>
Taken as a whole, the proposed capital rule is workable enough to finalize – exactly as it was proposed – and FHFA does not actually *need* to change a single thing. Under no circumstances should the comment period be extended because FHFA has already allowed for an unnecessarily lengthy comment period window and because the public has been aware of the existence of a capital rule-making process for years.

To the extent the FHFA feels inclined to change anything at all, the "Payout Restrictions" subsection is the most important section to "get exactly right" of all. To that end, detailed comments on FHFA's thoughtful questions #25 through #29, and #107 follow below.

<u>Comment on "Question 25":</u>
Yes, the payout restrictions are "appropriately formulated". No, the payout restrictions are not appropriately "calibrated". In order for the payout restrictions to be both "appropriately formulated and [appropriately] calibrated", the right-most column titled "Maximum payout ratio" of "Table 8: Calculation of Maximum Payout Ratio" of the final capital rule should read, from top to bottom, the following: "No payout ratio limitation applies, 80%, 60%, 40%, 20%" instead of the proposed "No payout ratio limitation applies, 60%, 40%, 20%, 0%."

Such a modification to the proposed rule would likely help lower the cost of equity capital by making GSE preferred and common equity securities materially more attractive to long-term-oriented shareholders. This, in turn, will help facilitate a successful and timely recapitalization.

For the sake of clarity, the final version of the payout restrictions table should appear as follows in the final rule:

Table 8: Calculation of Maximum Payout Ratio

Capital buffer	**Maximum payout ratio**
Greater than or equal to the Enterprise's prescribed buffer amount.	No payout ratio limitation applies
Less than the Enterprise's prescribed buffer amount, and greater than or equal to 75 percent of the Enterprise's prescribed buffer amount.	~~60~~ 80 percent
Less than 75 percent of the Enterprise's prescribed buffer amount, and greater than or equal to 50 percent of the Enterprise's prescribed buffer amount.	~~40~~ 60 percent
Less than 50 percent of the Enterprise's prescribed buffer amount, and greater than or equal to 25 percent of the Enterprise's prescribed buffer amount.	~~20~~ 40 percent
Less than 25 percent of the Enterprise's prescribed buffer amount.	~~0~~ 20 percent

Comment on "Question 26":
No! There should not be any additional sanctions or consequences other than payout restrictions triggered by an Enterprise not maintaining a capital conservation buffer or leverage buffer in excess of the applicable PCCA or PLBA. Dividend payout restrictions are an extremely powerful incentive and any additional sanctions or consequences would be essentially pointless and perhaps even counter-productive. FHFA should be crystal clear about this important point in all future communications.

Comment on "Question 27":
Yes, absolutely, the payout restrictions should be phased-in over an appropriate transition period. In order to accomplish one of the largest recapitalizations in history, the Enterprises need to attract an enormous amount of private capital. In order to attract that much capital, the Enterprises will need to pay dividends right out of the gate at a level that market participants believe will at least stay flat, and eventually increase, under almost any scenario. This is especially true given the "government-sponsored" status of the Enterprises, the long history of the federal government abusing shareholders and the absence of any dividend being paid in over a decade. The idea of the FHFA saying "Trust us. The Enterprises will pay you some undetermined amount of dividends if you just wait ~4 more years, in addition to the past ~12, and hope that a future administration doesn't re-sabotage the whole process." is a non-starter for all but the most naïve investor, especially in the context of a highly-profitable but low-growth public utility business model.

The appropriate transition period should be the exact number of days between the signing of the "Net Worth Sweep" and the date of the critically-important consent decree that makes the exit from conservatorship effective (subject to terms and conditions). In other words, the "Net Worth Sweep" was imposed upon the Enterprises 8 years ago, so the transition period should be at least 8 years.

During this transition period, the payout restrictions would not apply at all. The board of directors of each Enterprise would still have a fiduciary duty to not recklessly "over-payout" dividends, just like at every other public company. After this transition period, the official restrictions would seamlessly "snap" into place.

This phase-in period is an appropriate way to (1) tacitly apologize for the prior abuse of shareholders, (2) demonstrate that the FHFA intends to act in good faith toward shareholders in the future and (3) signal to the financial markets that the rule of law will always be respected in the U.S…eventually.

Comment on "Question 28":
Yes, the payout restrictions should provide an exception for allowing dividends on newly issued preferred stock, without any limitation whatsoever. The payout restrictions should also provide the exact same exception for the currently-outstanding or "old" preferred stock. Failing to also extend this exception to the pari-passu "old" preferred stock would be arbitrary and inherently unfair, which would therefore be unhelpful to the overall objective of a successful and durable recapitalization.

Comment on "Question 29":
Yes, the payout restrictions should provide an exception for common stock dividends during the dividend payout restriction transition period. The boards of the individual Enterprises should decide how much to pay out during the transition period. The FHFA does not need to micro-manage the common dividend level during the transition period. With that said, the FHFA should make it clear that it endorses the idea of the Enterprises paying at least $.01/share in common dividends per year (with the explicit policy of having that baseline increase each year subject to a transparent formula).

Management is already incentivized to hit FHFA's prescribed capital levels as quickly as possible due to the FHFA's pay restrictions. Allowing common stock dividends during the transition period will not materially delay the recapitalization process, but a dividend policy that includes a modest, growing common stock dividend will help raise common equity capital and help attract a stable shareholder base. Given the various incentives to complete a timely recapitalization, the idea that the Enterprises would choose to pay an overly-generous common dividend, even if they were allowed to, is just plain ridiculous.

Comment on "Question 107":
The biggest perceived risk to investors from participating in the GSE's recapitalization is not the business model, the economy, the law or even partisan politics. **The biggest perceived risk is the government's historical disdain for the rights of shareholders (under every single one of FHFA's directors) and fears about the potential for future disdain. The FHFA should do everything in its power to eliminate all "disdain risk" to shareholders.** That means FHFA must right the wrongs of the past and persuade investors that there will not *and cannot* be another bad faith "Net Worth Sweep"-like surprise in the future.

It is time for the FHFA to not only follow the law, but to do so with a sense of urgency that has been completely lacking. For starters, FHFA should relist the GSEs on the New York Stock Exchange, amend the Preferred Stock Purchase Agreement for the last time and settle all shareholder lawsuits immediately. The fact that the FHFA continues wasting time and money defending the indefensible "Net Worth Sweep" in court is a disgrace.

Furthermore, in order to "clear the decks" for raising many billions of dollars of low-coupon, newly-issued preferred shares, FHFA should consider having the Enterprises do an exchange offer. For example, the Enterprises could propose to swap all currently-outstanding junior preferred shares into common at 150% of par value using a 10% discount to the volume-weighted average price over that past 15 days. The premium to par is more than justified to execute a global settlement of preferred shareholder lawsuits. The premium is also justified as atonement for prior abuse of preferred shareholders, who have not received a dividend in 12 years (8 years since the Net Worth Sweep) for the simple reason that FHFA deliberately failed to "conserve and preserve" the Enterprises' assets. This conversion offer should happen in conjunction with the announcement that Treasury has: (1) been repaid in full with imputed interest exceeding 10% (2) has exercised its warrants and (3) has written off its Senior Preferred Stock liquidation preference to zero no later than November 4, 2020.

Should you have any questions or comments, please email roman.roik@protonmail.com

Thank you[i].

Roman Roik

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[i] Everything in this comment letter is solely the author's personal opinion as a concerned citizen, should not be "relied upon" and does not convey any legal, financial or other advice to anyone, or on behalf of anyone, whatsoever. Furthermore, the author disclaims any liability for the accuracy of any statement contained herein.