Federal Housing Finance Agency

400 7th Street, SW

Washington DC 20024

February 10, 2021

Re: Proposed Rule on Resolution Planning RIN-2590-AB13

Acting as a private citizen, I have examined the proposed rule in depth. Between my seven years as CEO of Freddie Mac (2012 to 2019) and my prior banking experience, where I rose from a trainee to become Vice Chairman of JPMorgan Chase, I am very qualified to do such an examination.

The results of my examination are that the proposed rule needs a wholesale revision. This is primarily because there are, at its core, two major design requirements that are demonstrably flawed and in error, i.e. at odds with the facts.

Error #1: The requirement that the resolution planning *not* include the support provided to each Government Sponsored Enterprise (GSE) by its Preferred Stock Purchase Agreement (PSPA). While short of a full faith and credit guarantee, each PSPA is a legally binding contract by which the Federal government is committed to providing very strong support to the two GSEs. The proposed rule specifies that this support is nevertheless to be ignored as somehow just a perception in the minds of investors, which is contrary to the undeniable legal right of each GSE to benefit from its PSPA. Any conclusions reached by such an analysis will be materially distorted and wrong as they will not reflect the reality of that considerable support.

Error #2: The requirement that each GSE’s resolution plan state how its affiliated Limited Life Regulated Entity (LLRE) will continue operations to enable the national housing markets to still function normally, but specifically requiring that no PSPA or other form of extraordinary government support be available to benefit the LLRE. This is an impossibility – the entire business model of the GSEs and the agency mortgage-backed securities (MBS) markets is predicated upon enough government support so that the MBS issued by the GSEs are perceived by investors as having nil credit risk, but only interest rate and liquidity risks. If there is to be no PSPA (or alternative extraordinary) support to the MBS that the GSEs issue, investors have made it clear that they will no longer perceive nil credit risk, and thus will functionally stop purchasing the securities. This in turn will require the GSEs to stop purchasing mortgages from primary market lenders. This is completely understood b*y all* participants in the agency MBS markets.

These two errors mean that the proposed rule is critically and fundamentally flawed, and – as stated above – needs wholesale replacement.

In addition, I have three other significant concerns about the proposed rule:

One, many clauses of the proposal are unusually vague as to how they will operate, which is inconsistent with quality regulation. An example would be the determination of what assets, in receivership, would be placed into an LLRE versus left in a bankrupt estate to be liquidated. This is an incredibly important aspect of the resolution plan but one where the proposed rule leaves it fully to future qualitative judgments by the FHFA with seemingly no obvious constraint upon its decisions. The FHFA should be materially more specific in this and other components of the proposed rule to provide reasonable transparency to the public of how resolution planning would actually operate.

Two, the value of this living will resolution planning is, for a GSE as compared to a large and systemically-important bank, very modest. A GSE has an ultra-simple corporate structure as compared to a large bank and also has a dramatically superior liquidity profile (as about 90% of its balance sheet is funded by “pass-through” MBS). Yet, the proposed rule calls for a major effort to meet its requirements, taking years and necessitating, I estimate, thousands of pages of submissions each. The two should be put into balance so that complying with the resolution planning regulation has a cost scaled to the very modest value of the regulation, which is currently not the case.

And three, certain aspects of the rule seem to run counter to Congressional intent as expressed in the legislation establishing the two GSEs, known as their “charters.”

All of these points are made in greater depth and with more supporting detail and explanation in a paper I recently wrote, reflecting my personal views, that was published via Harvard’s Joint Center for Housing Studies: [The FHFA’s Proposed GSE 'Living Will' Rule: Fatally Flawed and Unusually Vague*.*](https://harvard.us7.list-manage.com/track/click?u=32bdef9ad4f5c24e42bebf634&id=933ebc19d6&e=d6fb725d3d) I incorporate it by reference at <https://www.jchs.harvard.edu/research-areas/working-papers/fhfas-proposed-gse-living-will-rule-fatally-flawed-and-unusually>.

Sincerely,

Donald H. Layton