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March 8, 2021

Mr. Clinton Jones
General Counsel
Federal Housing Finance Agency
Eighth Floor
400 Seventh Street, SW
Washington, DC 20219

Re: Comments on Enterprise Resolution Planning, RIN 2590-AB13

Dear Mr. Jones:

The Housing Policy Council ("HPC")[1] appreciates the opportunity to comment on the Enterprise Resolution Planning proposed rule issued by the Federal Housing Finance Agency ("FHFA").[2]

HPC commends FHFA for proposing a rule that would direct the Federal Home Loan Mortgage Corporation ("Freddie Mac") and the Federal National Mortgage Association ("Fannie Mae") (collectively, the "GSEs" or the "Enterprises") to "… develop plans to facilitate their rapid and orderly resolution in the event FHFA is appointed receiver…"

The proposed rule offers a valuable perspective to the marketplace, highlighting not only that Freddie Mac and Fannie Mae are systemically important financial institutions, but also and, perhaps more importantly, that GSE resolution cannot be addressed as effectively as a Federal Deposit Insurance Corporation (FDIC) resolution of one of the nation's largest banks. FHFA simply lacks the funding tools Congress has given to the FDIC to resolve bank failures and the variety of resolution options available to the FDIC.

By highlighting the shortcomings FHFA's statutory authority, the proposed rule reinforces our view that true housing finance reform is best achieved with congressional action.[3] The proposed rule follows a legal construct crafted by Congress in 2008 that is at odds with current conditions in the market for housing finance. Absent legislative reform, the future

[1] HPC is a trade association comprised of the nation's leading mortgage lenders, servicers, mortgage insurers, and title and data companies. HPC advocates for the mortgage and housing finance interests of its members in legislative, regulatory, and judicial forums. Our interest is in the safety and soundness of the housing finance system, the equitable and consistent regulatory treatment of all market participants, and the promotion of lending practices that create sustainable home ownership opportunities that lead to long-term wealth-building and community-building for families.
[2] 86 Fed. Reg. 1326 (January 8, 2021).
[3] FHFA has long advocated for legislated housing finance reform that provides a federal guarantee on mortgage-backed securities (MBS) in order to avoid any doubt about the credit risk to MBS holders and the resulting potential for enormous mispricing of securities or market disruption in the event of a guarantor's failure.

appointment of a receiver for Fannie Mae or Freddie Mac per the terms of the rule and the existing statute would inevitably result in serious market disruption.

An Enterprise Failure Resolution is not the Same as a Bank Resolution Yet the Enterprises are Systemically Important Financial Institutions

In the preamble to the proposed rule, FHFA explains that its resolution authorities are modeled on those the FDIC has for resolving failed banks and that the Limited Life Regulated Entity (LLRE) FHFA is required to establish in the event of a receivership is derived from FDIC's authority to establish a bridge bank.

FHFA then explains a fundamental difference between FDIC's resolution capabilities and those of FHFA. While FDIC manages a Deposit Insurance Fund that provides FDIC with liquidity to finance a bank failure resolution, FHFA has no such funding source. Indeed, FHFA only has access to the resources of the failed Enterprise to finance the resolution. Thus, an insolvent Enterprise that ends up in receivership can only raise resolution funds by imposing some of its losses on equity investors and then creditors (i.e., "haircutting" the amount that they may be repaid). FHFA clearly states in the proposed rule that if creditors believe the federal government is going to protect them, as was done in 2008, they will be mistaken.

Beyond the lack of funding to facilitate a receivership, FHFA also lacks the full suite of disposition authorities available to the FDIC. While FDIC may sell a failed bank, liquidate it, break it into pieces, combine it with one or more other failed banks, or some combination, Congress gave FHFA only one path to resolve an Enterprise that is placed into receivership: create an LLRE, which succeeds to the failed Enterprise's charter. Most people appreciate how disruptive the failure of one or two large banks can be to our banking system and to our larger economy. Yet even if one or two such large banks failed, there are thousands of banks remaining to meet the needs of consumers and businesses. If Fannie Mae and Freddie Mac both failed, as we saw in 2008, the country's housing finance system would be left with two LLREs that lack any official backing or source of funding from the federal government.

As the FHFA proposal makes plain, both Enterprises are systemically important institutions and resolving any future failure must be undertaken in recognition of critical market operations that cannot be shut off and that lack readily available market substitutes. These factors all lend support for FHFA's desire to have thoughtful, detailed resolution plans in place. But they do more than that. They raise the question of whether any of what FHFA proposes can be practically implemented without creating enormous market disruption? Will investors be willing to purchase mortgage securities from an LLRE that lacks official backing from the federal government? Indeed, all the pre-planning in the world cannot change how investors will react; only legislation to move beyond this broken structure can do that. Viewed that way, the resolution planning exercise required by the proposed rule seems less important than working towards much-needed legislative reforms.

Only Congress can Remedy These Built-In Systemic Risks

FHFA is working within a statutory construct Congress created in 2008. As the proposed rule makes clear, that construct would require FHFA to implement some future Enterprise receivership by funding the receivership through losses imposed on debt and mortgage-backed security holders and other creditors. As FHFA notes:

> Considering the Enterprises' statutory purposes and mission and FHFA's statutory duties and authorities, the goals of Enterprise resolution planning are to facilitate the continuation of Enterprise functions that are essential to maintaining stability in the housing market in the establishment of an LLRE by FHFA as receiver and ***to allocate losses to creditors in their order of priority***.[4]

Implementing the Proposed Rule Will Require Persistent Market Discipline

HPC appreciates that FHFA is implementing a needed rule to prepare for a post-conservatorship world in which Congress has not addressed the Enterprises' failure in 2008 nor the flaws inherent in their charters.

Through this proposed rule and other means, FHFA makes clear to all categories of investors in GSE securities that the future post-conservatorship world requires market discipline by investors due to a clear absence of both a federal guarantee and any identified source of federal support in the event of a receivership. Understanding this, market participants will need to judge their investment decisions in GSE equity, debt, and mortgage-backed securities, including the return they will require, accordingly.

Some would say that is the world we had pre-conservatorship, but few believed the government would truly follow through and the market priced a future government rescue into the market. In, fact, Congress enacted a rescue. FHFA is warning everyone in this rule: next time will be different, so plan accordingly.

Legislative Reform is Needed to Provide an Alternative Resolution Scenario

As just noted, pre-conservatorship, GSE investors believed the government would step in despite the lack of legal authority, which the government ultimately did. While FHFA wants to reinforce the need for investors to beware, the government's past actions will inevitably resurrect market uncertainty. Thus, HPC is concerned that some future GSE failure, resolved according to the terms of current law and the proposed rule, would result in a systemic disruption.

To be clear: HPC is not saying that there is any oversight or omission by FHFA here. The agency is proposing to carry out the law as written. It is a simple statement that trying to

[4] Ibid. P. 1329. Emphasis added.

resolve the failure of one, let alone both Enterprises, *in the manner required by current law* would risk a sizeable, systemic disruption.[5]

In many ways, the proposed rule poses a hypothetical exercise. FHFA is asking us to assume a post-conservatorship world that does not exist today. If and when it does, we do not know what government backing arising from the existing Senior Preferred Stock Purchase Agreements would be in place nor how market participants would price Enterprise securities based upon such backing, or lack of such backing.

We appreciate that FHFA undertook this proposed rule with a view that the Enterprises should be considered as operating without any government backing, per existing statutes:

> To clarify the status of the Enterprises as privately owned companies, FHFA seeks to make explicit in this resolution planning rule that no extraordinary government support will be available to prevent an Enterprise receivership, indemnify investors against losses, or fund the resolution of an Enterprise. Each Enterprise must incorporate that assumption into its resolution plan, and this assumption must be apparent in the plan's public section.[6]

This is the real service of this proposed rule. It reminds lawmakers, the Administration, investors, and all other stakeholders that fundamental questions surrounding the operations of Fannie Mae and Freddie Mac post-conservatorship are unanswered. The failure to enact legislation that resolves certain fundamental issues leaves the housing finance system stuck in some interim space where few want to remain. It is taxpayers, represented by the U.S. Department of Treasury, that continue to be the ultimate risk-holder, and the recent changes to the Treasury support agreements for the Enterprises leave taxpayers with nothing more than a growing "IOU" for this ongoing support.

Technical Observations

HPC offers the following comments and observations on certain aspects of the proposed rule:

- HPC questions whether three months is adequate for the Enterprises to undertake a complete internal review, including with senior management and their respective boards of directors, and produce an initial notice.
- FHFA asked whether "there would be benefit to FHFA's providing notice to each Enterprise of all core business lines identified or any removal of a core business line identification, across both Enterprises." In light of their nearly identical statutory authorities, HPC believes such information should be shared across both Enterprises.

[5] FHFA has long advocated for legislated housing finance reform that provides a federal guarantee on mortgage-backed securities (MBS) in order to avoid any doubt about the credit risk to MBS holders and the resulting potential for enormous mispricing of securities or market disruption in the event of a guarantor's failure.
[6] Ibid. P. 1330.

Conclusion

Thank you for the opportunity to respond to this proposed rule. We would be glad to engage with FHFA in any way that would be useful. If you have any questions or would like to discuss these comments, please contact Meg Burns, EVP for the Housing Policy Council, at 202-589-1926.

Yours truly,

Edward J. DeMarco
President
Housing Policy Council