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Federal Housing Finance Agency
Eighth Floor
400 Seventh Street, SW
Washington, D.C. 20219
Attention: Clinton Jones, General Counsel

Attention: Comments/RIN 2590 – AB09
(Enterprise Liquidity Requirements)

Ladies and Gentlemen:

Fannie Mae welcomes the opportunity to comment on the Federal Housing Finance Agency's ("FHFA") proposed rule, "Enterprise Liquidity Requirements," published on January 8, 2021 (the "Proposed Rule").[1] The Proposed Rule would implement four quantitative liquidity requirements that would address the short, intermediate and long-term liquidity needs of Fannie Mae and Freddie Mac (together, the "Enterprises").

FHFA has a long history of supervising and establishing requirements for liquidity risk management at the Enterprises. FHFA issued a supervisory letter in December 2009 that established minimum 30-day and 365-day liquidity requirements for Fannie Mae, as well as requirements to maintain levels of cash or U.S. Treasury securities ("Treasuries") to meet those requirements. More recently, FHFA issued an advisory bulletin incorporating liquidity risk management practices consistent with the Basel Liquidity Principles and a directive to meet prescriptive liquidity risk requirements.

Fannie Mae supports the overall approach of the Proposed Rule and offers the following comments to improve the final liquidity rule.

Public Disclosures

The Proposed Rule would require an Enterprise to provide public disclosure of average and month-end liquidity positions in its monthly volume summaries.[2] We believe it is important to keep the public informed of our ongoing performance through our monthly and other financial disclosures, and we support the overall objective of using disclosure to improve transparency and facilitate market discipline. We do, however, have concerns that the disclosure requirements, as proposed, could have pro-cyclical impacts during an idiosyncratic or market stress by constraining the ability of an Enterprises to deploy its

[1] 86 Fed. Reg. 1306 (Jan. 8, 2021).

[2] 86 Fed. Reg. at 1325 (proposed 12 C.F.R. § 1241.20(c)).

liquidity. As a result, the proposed disclosure requirements could inadvertently increase the types of liquidity risk that the Proposed Rule is intended to address.

Our liquidity resources are intended to be used in times of idiosyncratic or market stress so that we can continue to fulfill our mission and support the U.S. mortgage finance system. However, monthly disclosures of a single point-in-time spot measurement, as contemplated by the Proposed Rule, could potentially exacerbate liquidity risk. For example, if we were to disclose a month-end spot measurement showing reduced liquidity, regardless of whether resulting from executing business strategies or a stressed environment, market participants may react by withdrawing liquidity, possibly at a time when it is most needed.

Large U.S. banking organizations subject to the liquidity coverage ratio ("LCR") and net stable funding ratio ("NSFR") have raised these types of concerns about similar liquidity disclosure requirements.[3] The Federal Reserve Board has also acknowledged risks associated with liquidity disclosures. In the preamble for its final LCR disclosure rule, the Federal Reserve Board stated that it was important that LCR disclosures "include a lag that provides market participants with a broad understanding of a firm's medium-term liquidity position without causing the release of current liquidity data that could potentially negatively affect the firm."[4] In the preamble for the final NSFR rule, the issuing banking regulators (the Office of the Comptroller of the Currency, Federal Reserve Board, the Federal Deposit Insurance Corporation) explained that they adopted semiannual disclosure requirements (covering the prior two quarters) – instead of the proposed quarterly disclosure requirements (covering the prior quarter) – in order to "balance[] the benefits of quarterly disclosures, which includes allowing market participants and other parties to assess the funding risk profiles of covered holding companies, with the concerns that more frequent disclosure could result in unintended consequences."[5] In another change from the proposed NSFR rule, the final NSFR rule requires disclosure on an average basis over the reporting period, instead of a spot measurement. Under these rules, LCR and NSFR disclosures must generally be made on a timeline consistent with the deadlines for periodic disclosure filings with the U.S. Securities and Exchange Commission ("SEC").[6]

To balance the market discipline benefits and pro-cyclical risks of public liquidity disclosure requirements, we recommend that FHFA revise the Proposed Rule to limit required disclosures to averages over the reporting period and provide for the disclosures to be made on a quarterly basis, concurrent with our quarterly and annual reports filed with the SEC.

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[3] Liquidity Coverage Ratio: Public Disclosure Requirements; Extension of Compliance Period for Certain Companies to Meet the Liquidity Coverage Ratio Requirements, 81 Fed. Reg. 94922, 94925 (December 27, 2016); Net Stable Funding Ratio: Liquidity Risk Measurement Standards and Disclosure Requirements 86 Fed. Reg. 9120, 9191 and 9193 (Feb. 11, 2021).

[4] 81 Fed. Reg. at 94925.

[5] 86 Fed. Reg. at 9193.

[6] 81 Fed. Reg. at 94924; 86 Fed. Reg. at 9194.

Eligible Liquidity Assets

Under the Proposed Rule, an Enterprise must satisfy its 30-day cash flow liquidity requirement with a high-quality liquid assets ("HQLA") portfolio, and must satisfy its 365-day cash flow liquidity requirement with an HQLA portfolio and counting certain mortgage loans and mortgage-backed securities.[7] Although we agree with the proposed types of assets that would qualify as liquid assets in the Proposed Rule, we recommend that FHFA permit additional assets to qualify as well.

Treasury Collateral with Associated Rehypothecation Rights

The Proposed Rule's definition of HQLA limits eligible loans secured by Treasuries either to (a) loans to the Federal Reserve Bank of New York ("FRBNY"), or (b) loans that clear through the Fixed Income Clearing Corporation ("FICC"), in either case, where the remaining term of the loan is not greater than (i) 15 days, or (ii) the number of days until the next agency mortgage-backed securities ("Agency MBS") payment date.[8]

While we believe the counterparty and maturity limitations in the Proposed Rule are appropriate in the absence of rehypothecation rights where monetization must occur through the repayment of the loan at maturity, if rehypothecation rights are present, we believe the counterparty and maturity limitations are unnecessary. With such contractual rehypothecation rights and with the capability to monetize the collateral pursuant to the Proposed Rule's operational requirements,[9] we recommend that the collateral received in reverse repurchase agreements be counted as an immediate liquidity resource for Fannie Mae, regardless of loan counterparty and maturity. For example, if we engage in a reverse repurchase agreement with associated rehypothecation rights, we would be able to raise cash using the underlying collateral received by entering into a repurchase agreement.

Eliminating counterparty and maturity limitations and focusing on the underlying collateral would be consistent with the LCR established by the banking agencies, which treats qualifying collateral from reverse repurchase agreements as HQLA if all operational requirements are met, regardless of the counterparty and regardless of the reverse repurchase agreement maturity.[10]

Agency MBS Collateral

In calculating Enterprise liquidity under the 365-day metric, the Proposed Rule would count Agency MBS, but not Agency MBS received as collateral in a reverse repurchase agreement.[11] Given the highly liquid market for Agency MBS, including its eligibility as general collateral financing ("GCF") collateral at the

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[7] 86 Fed. Reg. at 1324 (proposed 12 C.F.R. § 1241.11(a)-(b)).

[8] 86 Fed. Reg. at 1322 (proposed 12 C.F.R. § 1241.3).

[9] 86 Fed. Reg. at 1323 (proposed 12 C.F.R. § 1241.11(c)).

[10] Liquidity Coverage Ratio: Liquidity Risk Measurement Standards, 79 Fed. Reg. at 61469, "The agencies highlight that HQLA, *including assets received through repurchase agreements* and other borrowed assets, must meet all requirements set forth in § __.22 of the final rule to qualify as eligible HQLA." (emphasis added)

[11] 86 Fed. Reg. at 1324 (proposed 12 C.F.R. § 1241.11(b)).

FICC,[12] we recommend that Agency MBS collateral received in a reverse repurchase agreement also qualify as a liquid asset to meet net outflows in the 365-day metric.

According to the Federal Reserve Bank of New York, the average daily gross volume for overnight Agency MBS-backed GCF repo in the 2020 was $153.4 billion, which was approximately $84 billion higher than the volume for overnight US Treasury-backed GCF repo.[13] The high liquidity in the overnight Agency MBS-backed GCF repo market was especially resilient during the heights of the 2020 market stress, with an average volume of $165.7 billion, which was $108 billion higher than the volume for overnight US Treasury-backed GCF repo.[14]

The Proposed Rule's inclusion an Enterprise's Agency MBS holdings for the 365-day metric recognizes the highly liquid market for these securities. Accordingly, FHFA should consider including Agency MBS collateral received by an Enterprise in reverse repurchase agreements in this definition. And similar to Treasury collateral, where there are associated rehypothecation rights, counterparty and maturity should not limit the eligibility of such Agency MBS collateral.

FICC Collateral Requirements

Under FICC rules, all FICC participants (including the Enterprises) are required, if directed by FICC, to fund certain amounts pursuant to a capped contingency liquidity facility (the "CCLF") if FICC ceases to act for a member.[15] This obligation is intended to ensure that FICC has access to adequate liquidity in times of market distress. The CCLF funding obligation is structured as a short-term repurchase transaction, with the contributing participant receiving eligible collateral from FICC, either U.S. Treasury securities or Agency MBS, in exchange for the delivered cash.[16]

The Proposed Rule includes a stress assumption for its cash inflows and outflows that would require Fannie Mae to cover 100% of its CCLF cash funding obligation.[17] While the CCLF funding obligation needs to be part of every FICC participant's liquidity planning, the highly liquid securities the Enterprise would receive in exchange for the cash delivered to FICC should factor into the stress assumption. Instead of full apportionment of this amount, we recommend that an Enterprise's CCLF cash funding obligation be covered at a rate of 15% to give credit to the highly liquid collateral that the Enterprise would receive. This 15% treatment for the CCLF cash funding obligation would be consistent with the discount the Proposed

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[12] See, *Fixed Income Clearing Corporation, Government Securities Division, GCF Collateral Eligibility and GCF Collateral Types*, published, July 20, 2020, downloadable at: https://www.dtcc.com/-/media/Files/Downloads/Clearing-Services/FICC/GOV/GCF-Collateral-Eligibility-and-Types-v5.pdf.

[13] Based on 12 monthly data points from the Federal Reserve Bank of New York, downloadable at: https://www.newyorkfed.org/data-and-statistics/data-visualization/tri-party-repo#interactive/gcfrepos.

[14] Based on March, April, and May data from the Federal Reserve Bank of New York, downloadable at: https://www.newyorkfed.org/data-and-statistics/data-visualization/tri-party-repo#interactive/gcfrepos.

[15] Fixed Income Clearing Corporation, Government Securities Division Rulebook, Rule 22A, downloadable at: https://www.dtcc.com/~/media/Files/Downloads/legal/rules/ficc_gov_rules.pdf.

[16] *Id.* at §2a.

[17] 86 Fed. Reg. at 1323 (proposed 12 C.F.R. § 1241.10(d)(5)).

Rule applies in the 365-day metric to Agency MBS eligible as collateral for FICC[18]. This approach would also be consistent with the LCR rule, which gives credit to liquid collateral that would be received upon a draw on a facility such as the CCLF.[19]

In addition, the Proposed Rule would require the CCLF cash funding obligation to be a stress assumption in both the 30-day and 365-day liquidity requirement.[20] We note that Fannie Mae's CCLF funding exposure varies monthly, with the amount dependent in part on Fannie Mae's settlement activity with the mortgage-backed securities division ("MBSD") of FICC. We recommend that FHFA revise this section so that the amount of liquid assets an Enterprise is required to maintain to satisfy Fannie Mae's CCLF obligation under the 365-day metric be projected based on Fannie Mae's MBSD volume projections. We believe this calculation adjustment ties the measurement of our liquidity needs to a more precise projection of our CCLF obligation.

Monetization Tests

The Proposed Rule would require Fannie Mae to test the monetization of the assets that comprise HQLA, and the preamble to the Proposed Rule describes the testing to include asset class, counterparty, and maturity.[21] While we recognize that testing monetization channels is critical to ensure that an Enterprise has the operational capability to monetize its HQLA during a stress event, not all the characteristics listed in the preamble are relevant for such tests.

Specifically, because the maturity date of an asset such as Treasuries does not impact the operational capability of monetizing such asset, testing across asset maturities should not be required. Further, since the current definition of HQLA is restricted to Treasuries and short-term loans with FRBNY and FICC, we do not believe that testing by counterparty should be required for HQLA monetization testing. We note, however, that counterparty testing for HQLA monetization should be a requirement if FHFA accepts our recommendation to add collateral received in reverse repo transactions with associated rehypothecation rights, beyond just transactions with FRBNY and FICC.

Operational Payment Failures of Non-Bank Servicers

The Proposed Rule would include a minimum stress assumption requiring Fannie Mae to hold liquid assets to cover its exposure to the failure of its top five non-bank servicers to make scheduled principal, interest, tax, and insurance payments ("PITI payments") to Fannie Mae for 60 days.[22] The relatively short period of payment disruption in this liquidity assumption suggests that its purpose is to address temporary operational or liquidity issues at non-bank servicers that prevents them from making timely PITI payments to an Enterprise.

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[18] 86 Fed. Reg. at 1324 (proposed 12 C.F.R. § 1241.11(b)(3)).

[19] 12 C.F.R. § 249.32(e)(2) and (e)(3).

[20] We note that under §2a of Rule 22A of the Government Securities Division Rulebook, the duration of the CCLF transaction is 60 days.

[21] 86 Fed. Reg. at 1312.

[22] 86 Fed. Reg. at 1324 (proposed 12 C.F.R. § 1241.10(d)(7)).

Given this focus on operational or liquidity disruptions, we recommend that the time period should be reduced to reflect a more practical assumption regarding the duration of a payment default. We recognize that short-term disruptions are an appropriate consideration in a liquidity rule; however, historically, curing missed PITI payments from servicers takes significantly less time than 30 days, let alone 60 days. Based on this historical experience, we recommend FHFA reduce this risk assumption to a 30-day period in the final rule.

Excess Buffer for 30-Day Liquidity

The Proposed Rule would require Fannie Mae, when calculating its 30-day liquidity requirement, to hold HQLA in an amount $10 billion above the forecasted stressed net cash outflows.[23] The preamble to the Proposed Rule explains that this excess HQLA holding requirement is intended to serve as a buffer to address forecasting and other residual liquidity risks.[24]

We believe that a fixed buffer of this magnitude is unnecessary. Fannie Mae, like other regulated financial firms, manages its risk exposures and metrics using management-prescribed buffers set above minimum requirements. Given the existence of these management risk buffers and existing supervisory oversight by FHFA, we recommend that FHFA eliminate this additional buffer requirement from the 30-day metric calculation.

Method of Liquidity Reductions

The Proposed Rule allows FHFA to reduce minimum liquidity requirements for the Enterprises during periods of economic or market stress.[25] This flexibility is intended to allow the Enterprises to further their public purposes of providing liquidity to the secondary mortgage market, consistent with safety and soundness. We support this added flexibility and believe this authority will assist FHFA in responding to market events.

In order to help stabilize the markets in periods of market distress, we believe it is important that any FHFA reduction in Enterprise minimum liquidity requirements be clear to our stakeholders, including lenders, servicers, investors, and other market participants. Accordingly, we recommend that the Proposed Rule be amended by structuring the reduction in the form of a percent factor to be applied to the particular liquidity requirement, with such percent factor to be determined by FHFA based on the facts and circumstances of the financial stress. Structuring the reduction in liquidity requirements through a percent factor would be clear to all stakeholders and more effectively allow the Enterprises' liquidity to serve its countercyclical purpose.

Treatment of Regulatory Capital Elements

The Proposed Rule treats some regulatory capital elements, such as stockholder's equity, as a short-term funding substitute in its long-term liquidity metrics.[26] This treatment suggests that these regulatory capital elements are not a stable funding source. However, given the long-term nature of regulatory capital

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[23] 86 Fed. Reg. at 1324 (proposed 12 C.F.R. § 1241.11(a)(2)(ii)).

[24] 86 Fed. Reg. at 1314.

[25] 86 Fed. Reg. at 1325 (proposed 12 C.F.R. § 1241.12).

[26] 86 Fed. Reg. at 1324 (proposed 12 C.F.R. § 1241.11(c)).

elements, such as the perpetual nature of stockholder's equity, by definition, they are stable forms of funding.

We note that the preamble to the Proposed Rule states that the first long-term liquidity metric is designed to be conceptually similar to the NSFR.[27] In the NSFR rule, the banking agencies provided 100% available stable funding credit to regulatory capital, which reflects the perpetual and stable nature of this funding.[28] Accordingly, we recommend that FHFA provide credit to all regulatory capital elements, including stockholder's equity, in the long-term metrics of the final liquidity rule.

Calculation Time

The Proposed Rule would require Fannie Mae to choose a calculation time for liquidity measurement, which defaults to 6:00 pm, unless another time is elected by an Enterprise and approved by FHFA.[29] We recommend that the default language in the Proposed Rule be changed to a more flexible standard of "close of business," rather than a fixed time at which all positions must be measured. Running daily liquidity stress testing calculations is part of an enterprise data flow that encapsulates dozens of processes, and we recommend against including an exact time for this calculation in the final rule.

Timing of FHFA Report Submission

We recommend clarifying the timing of the report to FHFA in the Proposed Rule. The preamble indicates that we would be required to submit the report to FHFA the same day (T0).[30] However, the regulatory text provides the report should be delivered by the next day (T+1).[31] We seek clarification on the submission details and request the preamble align with the regulatory text and state that report submission to FHFA be on T+1. It is not operationally feasible to source enterprise-wide cashflows and prepare, validate and certify a report in near real-time for T0 reporting. In fact, Globally Systemically Important Banks in the U.S. are only required to submit their liquidity report (FR 2052a—which is used to calculate the Liquidity Coverage Ratio) to the Federal Reserve on a T+2 basis.[32]

Stress Assumptions

Section 1241.10(d) of the Proposed Rule states that an Enterprise should use minimum stress assumptions in determining its cash flow metrics, as well as for calculating its liquidity position and compliance with the long-term liquidity metrics. However, it is unclear how those minimum stress assumptions should be applied to an Enterprise's long-term liquidity metrics, as they are spot measures rather than cash flow forecasts. We recommend that FHFA revise this section to either (i) clarify the method an Enterprise should use for applying the minimum stress assumptions to its long-term metrics, or (ii) remove the reference to

[27] 86 Fed. Reg. at 1309.

[28] 86 Fed. Reg. at 9202 (§ __.104(a)(1)).

[29] 86 Fed. Reg. at 1322 (proposed 12 C.F.R. § 1241.3).

[30] 86 Fed. Reg. at 1320.

[31] 86 Fed. Reg. at 1325 (proposed 12 C.F.R. § 1241.20).

[32] See Federal Reserve Form FR 2052a, *Complex Institution Liquidity Monitoring Report*, downloadable at: https://www.federalreserve.gov/reportforms/forms/FR_2052a20200630_f.pdf.

long-term metrics in the definition of minimum stress assumptions, such that the minimum stress assumptions only apply to an Enterprise's cash flow metrics.

Conclusion

Fannie Mae appreciates the opportunity to comment on the Proposed Rule. The recommended changes in this comment letter are intended to further FHFA's objective of establishing liquidity requirements that enable the Enterprises' to fulfill their missions and provide countercyclical support to housing finance markets in times of stress.

If you have questions or require additional clarifications or supporting analysis, please contact the undersigned at *celeste_brown@fanniemae.com*. In addition, Fannie Mae would be pleased to facilitate a discussion of this letter.

Sincerely,

Celeste Mellet Brown
Executive Vice President and
Chief Financial Officer
Fannie Mae