Freddie Mac
We make home possible®

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By Electronic Delivery Through the FHFA Website

Mr. Clinton Jones
General Counsel
Federal Housing Finance Agency
Constitution Center, Eighth Floor (OGC)
400 7th Street SW
Washington, DC 20219

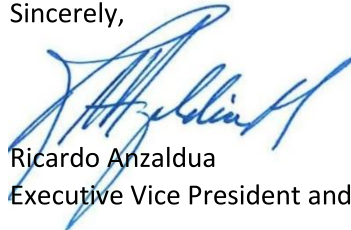
Re: Notice of Proposed Rulemaking on Enterprise Liquidity Requirements Comments/RIN 2590-AB09

Dear Mr. Jones:

Attached are the comments of Freddie Mac on the proposed Enterprise Liquidity Requirements rulemaking published by the Federal Housing Finance Agency in the Federal Register on January 8, 2021.

Freddie Mac appreciates the opportunity to provide our views on the proposed rule. Please contact me if you have questions or require any further information.

Sincerely,



Ricardo Anzaldua
Executive Vice President and General Counsel

Attachment

Executive Summary

We submit this letter to offer our comments on the proposed Enterprise Liquidity Requirements rule (the "Proposed Rule"), issued by the Federal Housing Finance Agency ("FHFA").[1] Freddie Mac has always valued the importance of a strong liquidity framework to meet our financial obligations and the needs of our customers in a timely and cost-efficient manner. Our existing liquidity policy has allowed us to fulfill our mission to provide liquidity, stability and affordability to the broader housing market, particularly during the unprecedented market events around the COVID-19 pandemic. As the market continues to evolve into a post-pandemic paradigm, Freddie Mac embraces enhancements to the existing liquidity framework for Freddie Mac and Fannie Mae (the "Enterprises") that will support the goals of our mission without imposing undue strain on the business or the broader housing market.

While we support FHFA's goal for the Enterprises to have adequate liquidity to serve as a buffer in a crisis so that the Enterprises are positioned to provide market liquidity in times of market stress, some of the technical requirements of the Proposed Rule may result in our holding excess liquidity. While maintaining excess liquidity could be thought of as additional safety, it may come with costs, which could affect the overall economics of our business, with consequent impacts on our ability to fully serve our mission.

In the Enterprises' current state in conservatorship, these economic costs are minimal because the Enterprises benefit from favorable debt funding costs due to the support provided by the Department of the Treasury through the Senior Preferred Stock Purchase Agreement ("PSPA"). However, the costs and availability of our debt funding could vary for a number of reasons, including the uncertainty about the future of the Enterprises. Moreover, there is the risk of these costs increasing in a post-conservatorship environment, depending on how the exit from conservatorship is structured.

If our funding costs increase, we believe that the additional liquidity requirements in the Proposed Rule may create a disproportionate economic drag on the firm as a higher amount of capital would be needed to fund this additional level of liquidity. Consequently, we have some proposed recommendations for consideration that we believe will reduce the risk of excess liquidity while achieving FHFA's goals for the safe and sound operations of the Enterprises.

We followed three guiding principles in developing our proposed recommendations to consider for incorporation into the final liquidity rule:

Definition of HQLA - To make an accurate measure of the firm's liquidity position, we recommend including additional eligible liquid assets in the definition of "high quality liquid assets" ("HQLA")[2] used

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[1] See Enterprise Liquidity Requirements, 86 Fed. Reg. 1306 (Jan. 8, 2021).

[2] See Proposed Rule, 12 C.F.R. § 1241.3 Definitions (High Quality Liquid Assets).

to comply with the proposed short-term 30-day and intermediate-term 365-day liquidity requirements. In that regard, we recommend revising the definition of HQLA in the Proposed Rule to include additional liquid assets that are eligible under the criteria for "high quality liquid assets" as set forth in U.S. banking regulations,[3] which have been shown to have deep, liquid markets, as described in more detail below.

Enterprise flexibility - In many cases, the Enterprises have options available in the event of a stress scenario that should be considered, including flexibility around future non-contractual activities to respond appropriately to liquidity demands that could arise during a period of economic stress. We recommend that due consideration be given to the Enterprises in instances where they are capable of adjusting their business to endure that economic stress.

Consistency with existing banking regulations - While we agree that there may be aspects of stress scenarios that are unique to the Enterprises, we believe that the stress assumptions should not be more conservative than those set forth in comparable U.S. banking regulations as those were already designed to be conservative.

Overview of the Proposed Rule

The Proposed Rule would establish four quantitative liquidity requirements for the Enterprises, as well as certain qualitative requirements for risk management practices. The following four quantitative liquidity requirements[4] would be measured daily and supported by detailed reporting:

- A short-term 30-day liquidity requirement based on: (i) the Enterprise's highest cumulative daily net cash outflows over 30 calendar days under certain specified stressed market assumptions, including a complete inability to issue debt; and (ii) an excess requirement in the amount of $10 billion;
- An intermediate 365-day liquidity requirement based on the Enterprise's highest cumulative daily net cash outflows over 365 calendar days under certain specified stressed market assumptions, including a complete inability to issue debt;
- A long-term liquidity and funding requirement based on the amount of an Enterprise's long-term unsecured debt divided by the amount of its less-liquid assets; and
- A second, model-based long-term liquidity and funding requirement based on an Enterprise's spread duration of its unsecured debt divided by the spread duration of its retained portfolio assets.

In the Preamble to the Proposed Rule, FHFA states that the 30-day liquidity requirement is designed to promote the short-term resilience of the liquidity risk profile of the Enterprises, thereby improving the

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[3] *See* 12 C.F.R. § 50.20 (Office of the Comptroller of the Currency ("OCC")); 12 C.F.R. § 249.20 (Board of Governors of the Federal Reserve System ("Federal Reserve")); 12 C.F.R. § 329.20 (Federal Deposit Insurance Corporation ("FDIC")).

[4] *See* Proposed Rule, 12 C.F.R. § 1241.11.

Enterprises' ability to absorb shocks arising from financial market and economic stresses. The 365-day liquidity requirement is intended so that the Enterprises manage their liquidity needs beyond the short term, and to provide additional incentives to fund their activities in a more stable fashion.[5]

FHFA also states that the two longer-term liquidity and funding requirements are designed to encourage the issuance of an appropriate mix of longer-term debt to reduce the Enterprises' rollover risk, to fund less-liquid assets with longer-term debt to avoid the risk of having to sell less-liquid assets into distressed markets for at least one year, to incent the Enterprises to issue an appropriate amount of long-term debt, and to incent the Enterprises to reduce the amount of less-liquid assets funded by unsecured debt held in the retained portfolio that are not eligible collateral for the Fixed Income Clearing Corporation ("FICC").[6]

As outlined in more detail below, we believe that the definitions and assumptions in the Proposed Rule are more conservative than Freddie Mac's historical liquidity risk limits and practices and the liquidity requirements applicable to U.S. banks.

Background

In the Preamble, FHFA cites the experience of the 2008 financial crisis, noting the rapid reversal in market conditions and the declining availability of liquidity during the financial crisis as illustrating both the speed with which liquidity can evaporate and the potential for protracted illiquidity during and following these types of market events. FHFA also mentions the recent COVID-19-related financial crisis as another example of the speed at which the detrimental effects of a liquidity and funding crisis can manifest, as the majority of funding markets locked up in mid-March 2020.[7]

FHFA further notes the actions taken since 2008 by U.S. and foreign financial regulatory bodies to establish international liquidity standards, including the supervisory expectations for liquidity risk management set forth in the "Principles for Sound Liquidity Management and Supervision" (Basel Liquidity Principles) along with quantitative standards for liquidity introduced to the U.S. banking supervision framework in the form of the liquidity coverage ratio ("LCR") and net stable funding ratio ("NSFR") regulations.[8] FHFA states that the Basel III LCR was designed by international banking regulators to focus on measuring liquidity resilience over a short-term period of severe stress, while the

[5] *See* 86 Fed. Reg. at 1306.
[6] *See* 86 Fed. Reg. at 1309.
[7] *See* 86 Fed. Reg. at 1307.
[8] *See* 12 C.F.R. Part 50 (OCC LCR regulation); 12 C.F.R. Part 249 (Federal Reserve LCR regulation); 12 C.F.R. Part 329 (FDIC LCR regulation); *see also* Office of the Comptroller of the Currency, Board of Governors of the Federal Reserve System, and Federal Deposit Insurance Corporation, Final Regulation, *Net Stable Funding Ratio: Liquidity Risk Measurement Standards and Disclosure,* 86 Fed. Reg. 9120 (Feb. 11, 2021) (hereinafter, the "NSFR Regulation").

NSFR final rule is intended to promote resilience by creating additional incentives for banking organizations and other financial companies to fund their activities with more stable resources and to encourage a sustainable maturity structure of assets and liabilities.[9]

FHFA describes the 30-day liquidity requirement in the Proposed Rule as similar to the LCR applicable to U.S. banks, with "some modifications to reflect characteristics and risks of specific aspects of the Enterprises' businesses."[10] FHFA also states that the purpose of the 365-day requirement and the two longer-term liquidity requirements in the Proposed Rule is similar to the intent of the NSFR, i.e., to encourage the Enterprises to issue appropriate amounts of longer-term debt and maintain a sustainable debt term structure.[11]

Specific Comments

Differences in Treatment of HQLA

Freddie Mac recommends that the treatment of HQLA in the final rule be consistent with the definition of HQLA that is used for the LCR applicable to U.S. banks.

In the Preamble, FHFA states that the short-term 30-day liquidity requirement is "substantially similar to the U.S banking regulators' LCR final rule."[12] Our view of the banking agencies' stress testing and LCR regulations indicates that they are conservatively designed to promote the stability of the U.S. financial system. Imposing requirements on the Enterprises that go well beyond those requirements, in Freddie Mac's view, could result in excess liquidity. Consequently, we propose that the definition of HQLA in the final rule be consistent with the definition of HQLA in the banking agencies' LCR regulation. Unlike the LCR regulations for banks, the Proposed Rule excludes agency mortgage-backed securities ("MBS") from the definition of HQLA that is used for the proposed short-term 30-day liquidity requirement.[13]

First, we note that all agency MBS, including reverse repurchase agreements of agency MBS, are excluded from the definition of HQLA in the Proposed Rule that is used for the 30-day liquidity requirement. While we acknowledge that there may be some "same-way" risk for agency MBS, we believe that this risk is adequately mitigated for reverse repurchase agreements of agency MBS by engaging in such transactions with highly rated counterparties such as FICC.

Second, unlike the U.S. banking regulators' LCR regulation, the Proposed Rule would restrict repurchase agreements on U.S. Treasuries that mature after a certain term for both the 30-day and the 365-day

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[9] *See* 86 Fed. Reg. at 1307-08.
[10] *See* 86 Fed. Reg. at 1308.
[11] *Id.*
[12] *Id.*
[13] *See* 86 Fed. Reg. at 1312.

requirements.[14] We note that the LCR regulation has no maturity restrictions on the term of U.S. Treasury repo contracts, as the underlying collateral can be easily rehypothecated and/or liquidated even in a stress environment. Additionally, it is common practice in the marketplace to unwind these repo trades at existing market prices without compromising on the liquidity. As a result, U.S. Treasury securities pledged to the Enterprises as part of a reverse repo should have no liquidity impact regardless of the term of the repo, and we believe that there is no basis for imposing term restrictions under the Proposed Rule. Consequently, we recommend the removal of the requirement that the remaining maturity term be no longer than the greater of 15 days or the number of days until the next agency MBS payment date.

Daily Excess Requirement

Freddie Mac recommends no daily excess requirement for the 30-day and 365-day requirements.

The Proposed Rule requires a $10 billion "daily excess requirement" for the 30-day liquidity requirement to "address the possibility of errors or other unforeseen operational errors."[15] FHFA requests comment on whether this proposed $10 billion daily excess requirement adequately addresses possible forecasting errors and other residual liquidity risks, and whether the amount should be higher or lower. FHFA also requests comment whether a buffer should be added to the 365-day requirement, which FHFA did not include in the Proposed Rule "because of the longer-term nature of the requirement."[16]

The 30-day requirement is calculated assuming the existence of adverse economic events as listed in the Proposed Rule, all of which are assumed to occur simultaneously. This requirement also assumes all contingent facilities are being drawn and allocated, and is inclusive of uncommitted, non-contractual activity all occurring within the 30-day period. The combination of all these events occurring simultaneously has not occurred even in the highly economically stressed periods of 2008 or during the recent COVID-19 pandemic. The Proposed Rule assumes that these events occur largely without warning, with no ability of the Enterprises or FHFA to adopt adequate mitigations. We believe the assumption that these stress events will occur both suddenly and simultaneously is more than adequate to address liquidity risk, making the existence of the additional buffer unnecessary. We also note that there is no daily excess requirement for the LCR in the banking regulation.[17]

However, if a daily excess requirement is to be retained in the final rule, we would recommend that the buffer be appropriately tailored to each Enterprise's specific circumstances. In particular, we suggest that the buffer be calculated as a small percentage of the Enterprise's 30-day requirement as opposed to using a fixed dollar amount. We also agree that there is no need for a buffer for the 365-day requirement.

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[14] *Supra* n. 2.
[15] *See* 86 Fed. Reg. at 1314.
[16] *Id.*
[17] *See* 12 C.F.R. § 50.10 (OCC); 12 C.F.R. § 249.10 (Federal Reserve); 12 C.F.R. § 329.10 (FDIC).

NSFR and Funding Requirements

Freddie Mac recommends that the highest stable funding requirement for less liquid assets be no greater than 100%.

Under the Proposed Rule, the Enterprises are required to maintain enough long-term unsecured debt (i.e., longer than one year to maturity) such that the amount is greater than 120% of all less-liquid assets in the retained portfolio. FHFA states that this metric is "intended to be a simple, transparent metric" and is "conceptually similar to the [NSFR]".[18] However, if the banking framework was applied to Freddie Mac, the highest stable funding requirement for Freddie Mac's assets would be 100%.[19] Consequently, we believe that the proposed funding requirement of 120% of unpaid principal balance ("UPB") for less liquid assets is far more conservative than the banking agencies' NSFR stable funding requirements. In addition, having a 120% funding requirement may increase the balances of our unsecured debt under the PSPA, which may limit our capacity to purchase delinquent loans in a stressed environment due to the current debt limits in the PSPA.

Additionally, although the long term-funding requirement in the Proposed Rule specifies the use of unsecured debt only, Freddie Mac believes the long term-funding requirement should include all liabilities and sources of capital that provide funding with maturities greater than one year, such as upfront fees and equity.

Treatment of Callable Debt Outflows

Freddie Mac believes that the Proposed Rule treats callable debt appropriately.

For the 30-day and 365-day requirements, FHFA states in the Preamble that the Proposed Rule does not require the Enterprises to maintain a liquidity portfolio large enough to fund the cash outflows associated with exercising the call option on all unsecured callable debt that was in-the-money at the close of business on Day 0.[20] For the spread duration of unsecured debt to spread duration of retained portfolio assets requirement, the Proposed Rule also would allow the Enterprises to use the maturity of the callable debt rather than the actual spread duration because the Enterprise does not have the obligation to call the debt early.[21] FHFA solicits commenters' views on this proposed treatment for Enterprise callable debt. Specifically, FHFA requests commenters' views on the proposed provisions that would allow the Enterprises not to call their unsecured callable debt even if it was in-the-money at the close of business on Day 0.[22]

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[18] *See* 86 Fed. Reg. at 1309.
[19] *See* NSFR Regulation, *supra* note 8, 86 Fed. Reg. at 9202 (establishing a maximum required stable funding adjustment percentage of 100%).
[20] *See* 86 Fed. Reg. at 1317.
[21] *See* Proposed Rule, 12 C.F.R. § 1241.11(c)(2)(ii)(C)(1). *See* 86 Fed. Reg. at 1319.
[22] *See supra* n. 20.

Freddie Mac has sole discretion to exercise the call option on the callable debt it issues. For the purposes of measuring Freddie Mac's liquidity in a stress scenario, we agree with FHFA that callable debt issued by us should be treated as debt outstanding until maturity. One of the main objectives of the Proposed Rule is to make sure that the Enterprises can operate while having impaired or limited access to unsecured debt markets. As such, it would be reasonable to assume that Freddie Mac's callable debt that is currently outstanding would be held to maturity. The value of an option is not simply a function of the current level of interest rates. If an issuer cannot replace funding with a more economically favorable source, then the option would not be exercised. For example, bank holding companies have issued callable debt securities that are callable before 30 days to maturity or one year to maturity to manage their firm-specific liquidity costs. An outside market participant might perceive the "at the money" strike differently from the issuer of these structures, where the threshold for calling the debt may be much higher due to its idiosyncratic limitations.

Projected Purchases and Commitments

Freddie Mac believes that, similar to bank regulation, the liquidity requirements in the Proposed Rule should be based on contractual future commitments, and not projected, non-contractual activity.

As the role of the Enterprises is critical during periods of market stress, Freddie Mac recognizes the importance of providing liquidity to loan originations through its Single-Family and Multifamily origination conduits. Freddie Mac has historically been able to maintain purchases across both single-family and multifamily business lines during recent market stresses so that the mortgage market is provided with adequate liquidity during those times. The Proposed Rule requires the Enterprises to maintain liquidity for projected single-family and multifamily cash window activity, while assuming a complete loss of ability to issue unsecured debt.[23] This requirement to hold liquidity for non-contractual activity during those times contrasts with the LCR and NSFR requirements applicable to banks, which do not require the banks to retain liquidity in anticipation of projected, non-contractually committed, loan origination activity.[24]

Treatment of TBA Sales

Freddie Mac believes that all inflows arising from the forward sale of TBA hedges, including TBA contracts sold in excess, should be considered inflows for determining the 30-day and 365-day liquidity requirements.

For purposes of this stress assumption, the Preamble states that, while TBA contracts can count as cash inflows at the contracted settlement dates, only TBA settlements that will occur at FICC are eligible. In addition, existing TBA contracts in excess of the amount needed to minimize the risk of existing loan purchases through the cash window or existing commitments to buy loans will not count as cash

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[23] *See* Proposed Rule, 12 C.F.R. § 1241.10(d)(2)(i)(A) and (ii) (A).

[24] *See, e.g.*, 12 C.F.R. § 50.32(d); 12 C.F.R. § 249.32(d); 12 C.F.R. § 329.32(d).

inflows. FHFA requests comment whether to allow the Enterprises to consider additional TBA contracts as cash inflows on the settlement date or just those TBA contracts cleared through the FICC. FHFA also requests comment whether FHFA should not allow the Enterprises to consider any existing TBA contracts as cash inflows on the settlement date.[25]

We recognize that banks subject to the LCR may not include in the LCR calculations those inflows that arise from forward mortgage sale activity tied to their origination activity. However, this is specific to the bank's origination business and, as part of that restriction, banks are required to hold only 10% of committed loans,[26] compared to the Proposed Rule's requirement for the Enterprises to fund 100%. In addition, as mentioned before, banks are not required to hold liquidity in anticipation of projected, non-contractual, commitment activity. The requirement for the Enterprises to hold 100% liquidity against contractual commitments and future uncommitted projections, as well as granting no inflows for the sale of committed loans, would not consider any of the offsetting factors provided to banks.

We propose that all forward sales that occur during the calculation period should be included as cash inflows, especially because we are required to fund 100% of contractual and non-contractual commitments. This approach permits a comparable treatment under the banking agencies' LCR regulation, which does not allow forward mortgage sales as inflow credit, but is offset by requiring banks to assume that only 10% of their mortgage loan commitments are funded.[27]

We also believe that allowing TBA forward sales as cash inflows is consistent with the overall treatment in the Proposed Rule of agency MBS as HQLA for the 365-day metric. To elaborate on the Proposed Rule's treatment of HQLA, if forward sales settlement failures occur, our HQLA position would not be impacted as Freddie Mac still has ownership of the TBAs. Additionally, TBAs that are settled through FICC are subject to the FICC Capped Contingency Liquidity Facility ("CCLF") requirement, which accounts for liquidity risks associated with FICC settlements. A final rule that does not permit any inflows from TBA sales will likely result in some double counting for this risk.

<u>Treatment of Non-Bank Servicer Default Return of Funds</u>

Freddie Mac believes a return of cash on Day 61 reasonably captures the liquidity disruption and return of funds in a non-bank servicer default.

For purposes of the 30-day and 365-day requirements, the Proposed Rule requires the Enterprises to assume that their five largest non-bank single-family seller/servicers by UPB fail to make scheduled principal, interest, tax and insurance ("PITI") payments on the next scheduled remittance date.[28] The

[25] *See* 86 Fed. Reg. at 1315.
[26] *See supra* n. 24.
[27] *See, e.g.*, 12 C.F.R. § 50.32(c); 12 C.F.R. § 249.32(c); 12 C.F.R. § 329.32(c).
[28] *See* Proposed Rule, 12 C.F.R. § 1241.10(d)[7] ("Increase in remittance shortfall by top non-bank seller-servicers under stress conditions").

assumption applies only to the first month, and allows the Enterprises to assume that such PITI payments are repaid by the original seller/servicer on day 61. FHFA requests comment on whether the Proposed Rule should allow for the cash inflow on Day 61 related to the repayment by these five non-bank seller/servicers for the 365-day requirement. FHFA also requests comment on whether to assume a longer period before repayment.[29] Freddie Mac believes a return of cash on Day 61 reasonably captures the liquidity disruption and return of funds in a non-bank servicer default. Historically, the return of funds has not exceeded more than 30 days unless fraudulent activity occurred at the servicer.

Treatment of Equity

Freddie Mac recommends that all sources of funds that qualify for regulatory capital should be considered as a long-term source of funding for both of the long-term liquidity metrics.

Under the two longer-term proposed requirements, the Enterprises would be required to identify the maturity of unsecured debt instruments based on their contractual maturity. In the Preamble, FHFA states that other balance sheet sources of funds, like stockholder's equity, typically do not have a contractual maturity. Consequently, "in the case of stockholder's equity, the Proposed Rule treats these funding sources as short-term funding substitutes and does not attribute any maturity to these sources of funds beyond one year."[30] FHFA requests comment on whether some portion of stockholder's equity should be considered as a longer-term funding source for the long-term liquidity and funding requirements.[31]

Consistent with the banking agencies' NSFR regulation, we believe that regulatory capital elements, as well as liabilities that mature one year or more from the calculation date, should be included. Such regulatory capital elements and long-term liabilities are described in the NSFR as the most stable form of funding because they are not susceptible to rollover risks and less likely to be drawn upon in a one-year period.[32] The same is true with respect to Enterprise equity capital and long-term liabilities. To remain consistent with the treatment afforded to banks under the NSFR, we believe that Enterprise equity, when appropriate, should be viewed as long-term funding in the final rule.

However, instead of just assigning equity funds a term greater than one year, we would recommend using an actual term for the two long-term funding metrics. Under the Proposed Rule, term assets such as mortgages are required to be majority (>=60%) funded by term debt. As proposed, equity would not count toward this funding requirement. This restriction would effectively require the Enterprises either to invest the majority of their equity funds in short-term liquidity assets (e.g., Treasuries, repo) or continue to issue debt to fund the majority of any longer-term mortgage investments.

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[29] *See* 86 Fed. Reg. at 1317.
[30] 86 Fed. Reg. at 1319.
[31] *Id.*
[32] *See* NSFR Rule, *supra* note 8, 81 Fed. Reg. at 9144.

To determine a term for equity, we first identify that the equity component discussed here is the cash component of equity that the firm retains. For example, this includes equity in the form of Retained Earnings, or cash retained from other forms of equity raises. Unlike GAAP equity, where changes in credit or market outlook may cause an immediate GAAP equity reduction, it would be unlikely that much of this retained cash would be immediately needed based on changes in market or credit outlook. Instead, increasing expectations around future losses may shorten equity's funding term as the expectations of cash needed to cover projected losses grow and move closer in time. To represent this timing, equity should be assigned a term based on the current projection of when equity cash needs occur, aligning these future cash needs with appropriate investment terms.

For example, one of the largest potential draws on equity comes from the single-family guaranty business. In the event of increasing projected credit losses, a reduction in GAAP equity may be recognized initially through loan loss reserves, well before any losses are realized as an equity cash need when the loan is later resolved. The projection of the amount and timing of actual equity cash needs can be modelled and captured as net outflows. Typically, this projection would show a significant portion of equity with a term longer than one year. Other shorter examples of equity cash in the firm may come from activities that create immediate cash needs, such as when investments are sold. For example, the multifamily securitization business purchases loans and realizes spread profits and losses a few months later when the securities are sold, so equity assigned to this business may have a shorter term.

Additionally, restricting equity investment to short-term Treasury-based assets may increase the capital the firm is required to hold based on the new capital rule, while also reducing earnings. Further, Treasury investment would increase Leverage Ratio requirements. If the firm is Leverage Ratio constrained, the choice to invest equity in Treasuries could increase the capital requirements of the firm compared to investment in its own Agency MBS.

Calculation of 30-Day Outflows

FHFA's proposed method for measuring short-term liquidity risk through cumulative net cash outflows appropriately captures the timing of inflows and outflows.

To determine the 30-day requirement as of the calculation date, the Proposed Rule would require an Enterprise to calculate its highest stressed cumulative net cash outflow amount for the next 30 calendar days following the calculation date to establish the dollar value that must be offset by the HQLA portfolio. FHFA believes that using the highest cumulative daily calculation (rather than using total cash outflows over a 30-calendar day stress period) is necessary because it takes into account potential timing mismatches between an Enterprise's outflows and inflows. FHFA requests comment on whether

this method for cumulative net cash outflows appropriately captures the potential mismatch between the timing of inflows and outflows under the 30 calendar-day stress period.[33]

Although different, we believe that FHFA's proposed method of calculation is comparable to a bank's LCR requirement in addressing timing mismatches. Under the Proposed Rule, the HQLA requirement is determined based on the most stressed net cash outflow day within the 30-day period as opposed to the cumulative net outflow over a 30-day period for a bank. The banking agencies' LCR regulation addresses the risk of a timing mismatch in the cumulative method of inflows and outflows through a separate adjustment known as the maturity mismatch add-on.[34] We believe the requirement to manage to the worst net cash outflow date within the 30-day period sufficiently addresses this timing mismatch risk and is consistent with the spirit of the banking regulators' implementation of the LCR.

Furthermore, as all liquidity facilities and stress facilities are assumed to be a T+1 outflow, this approach allows for additional liquidity buffers to absorb timing mismatches throughout the month to the extent that the stressors do not all occur at the same time.

Treatment of Liquidity Facilities

For the 365-day requirement, we propose that the assumptions should include an inflow of cash after the 30-day outflow period for FICC's CCLF.

Our interpretation of the FICC collateral need is that it should be treated as a liquidity facility where there is an inflow of cash in the near future, rather than a default fund where the inflow of cash is unknown. Given that the FICC's CCLF is used for a temporary disruption in liquidity, we believe that there should be a return date for this liquidity much like non-bank servicer defaults have a proposed return date. Without a return of funds assumption, this becomes implemented as a default fund rather than a liquidity facility.

Furthermore, the FICC CCLF requirements result in the exchange of cash for FICC-eligible securities, which are eligible liquid assets for the 365-day requirement. In the event a CCLF event is triggered, we may be called upon to engage in reverse repurchase agreements or withhold settlement on the sale of securities. In either case, Freddie Mac holds securities that are, at minimum, eligible liquid assets to cover the 365-day outflow requirement under the Proposed Rule. As such, we propose CCLF funds have a return of funds assumption after the 30-day outflow period.

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[33] *See* 86 Fed. Reg. at 1313-1314.

[34] *See* Office of the Comptroller of the Currency, Board of Governors of the Federal Reserve System, and Federal Deposit Insurance Corporation, Final Regulation, *Liquidity Coverage Ratio: Liquidity Risk Measurement Standards,* 79 Fed. Reg. 61440, 61476 (Oct. 10, 2014) (explaining the operation of the LCR regulation's mismatch add-on component).

Spread Risk

Freddie Mac believes the spread duration risk measure is more a measure of the economic risk of reissuing debt (rollover risk) and less of a measure of near-term liquidity risk. Consequently, we recommend that FHFA not include this measure in the final rule.

The Proposed Rule includes a long-term requirement that measures the ratio of the spread duration of an Enterprise's unsecured debt to the spread duration of its retained portfolio assets. FHFA states that this proposed requirement will cause the Enterprises to maintain an appropriate amount of long-term unsecured debt and reduce rollover risk and to create the incentive to better match the repricing risk of their debt with the repricing of their assets. FHFA also states that it will minimize the risk that an Enterprise would be forced to sell significant amounts of long-term assets into distressed markets.[35] FHFA requests comment on whether the spread duration requirement appropriately addresses these concerns, or whether there are alternative approaches to do so. In addition, FHFA requests comment on whether the value of including the spread duration requirement exceeds the costs and complexity of the calculation.[36]

We believe that the risk of a near-term inability to replace debt is adequately mitigated by the 365-day and the long-term unsecured debt to less-liquid asset ratio requirements in the Proposed Rule. Furthermore, the spread risk measure introduces a high degree of model dependency, which will result in inconsistent comparisons between the Enterprises. Therefore, we recommend removing this requirement from the final rule, as the liquidity risk targeted by this metric is already incorporated into the 365-day and other long-term debt requirements. However, if the spread risk measure is determined to be necessary, then we propose that all long-term liabilities, including upfront fees and equity, be included in the calculation as opposed to just unsecured debt.

Multifamily Loans and K-Deals

Freddie Mac proposes that the holding period and resale assumption for multifamily loans follow empirical holding periods that have occurred over the last calendar year so that the assumption is consistent with market conditions and business strategy.

For the 365-day requirement, the Proposed Rule requires a liquidity portfolio large enough to fund the first three months of multifamily loan purchases. The Preamble states that, if the Enterprises can demonstrate that they can securitize and sell all of their multifamily loans within 180 days, the Proposed Rule would allow them to use a six-month assumption for the securitization and sale of multifamily loans. FHFA requests comment whether the final rule should allow for a shorter or longer time period

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[35] *See* 86 Fed. Reg. at 1318.
[36] *See* 86 Fed. Reg. at 1319.

than six-month assumption, and whether FHFA should consider an alternative cash inflow process arising from the securitization and sale of multifamily loans.[37]

Based on the calendar year of 2020, we believe this projected purchase to securitization period would be 3 to 6 months for normal market conditions. However, given that the Proposed Rule assumes a complete loss of ability to issue unsecured debt, we believe that the final rule should also consider alternative channels for the sale projection assumption as Freddie Mac may choose to securitize multifamily loans through participation certificates, which may shorten the time period.

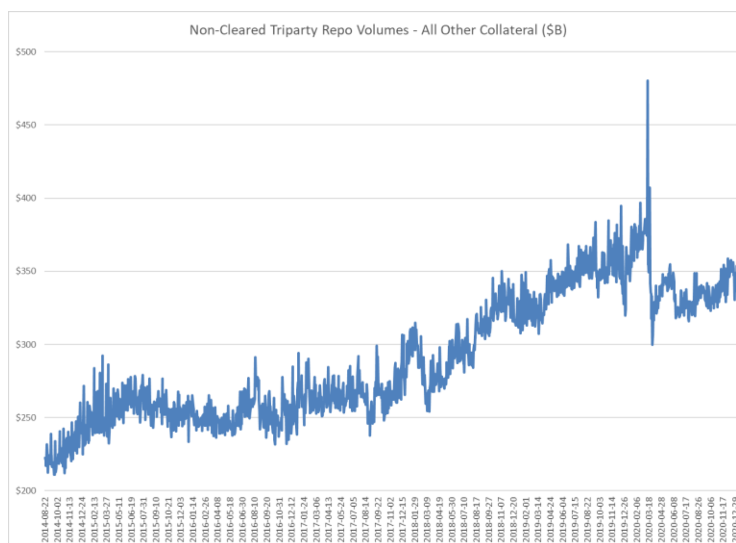
Definition of Liquid Assets

Assets that can be readily securitized into repo-eligible assets should be considered "liquid assets" and excluded from the long-term unsecured debt to less-liquid asset ratio metric, even if not eligible collateral at FICC.

The Proposed Rule includes a long-term liquidity and funding requirement that requires the Enterprises to maintain a minimum ratio of long-term unsecured debt to the amount of less-liquid assets in the retained portfolio of more than 120 percent. Because the Enterprises lack access to the Federal Reserve discount windows, FHFA proposes that only assets that are eligible to be posted as collateral through the FICC can be counted as liquid assets, and all other assets, including agency securities like agency CMOs and multifamily structured securities arising from the K-deals that are not eligible to be pledged to FICC, would be considered less-liquid and require long-term funding. FHFA requests comment whether it should broaden the definition of "liquid assets" to include certain non-FICC eligible assets, such as multifamily agency securities arising from K-Deal transactions and, if so, using what criteria.[38]

For purposes of this metric, we believe that the definition of "liquid assets" should not be tied to what is eligible collateral at FICC, which does not include the non-cleared repo market. For example, today FICC does not accept CMOs, Multifamily K-deal securities, corporate debt or other non-traditional collateral types. However, based on non-cleared triparty repo volume data published by the Office of Financial Research (as set forth in the chart below), the amount of daily non-cleared triparty repo transactions that occurred over the past year has been over $300 billion all throughout 2020, and greater than $200 billion in the available history since August 2014. As such, Freddie Mac believes that CMOs, Multifamily assets, and performing loans that can be readily securitized into repo-eligible assets, should be considered "liquid assets" and excluded from this metric, even if not eligible collateral at FICC.

[37] *See* 86 Fed. Reg. at 1316.
[38] *See* 86 Fed. Reg. at 1318.



(Data Source: https://www.financialresearch.gov/data/us-repo-data/)

Finally, being prescriptive about only allowing FICC-eligible securities may lead to unintended restrictions under the liquidity rule in the future. While we acknowledge that FICC is the largest exchange today for Treasury and MBS settlement, there may be additional avenues in the future where these settlements occur. We recommend that the final rule be less prescriptive while maintaining the intent of the rule.

DFAST Assumptions for Delinquent Loan Purchase Projections

For the 30-day and 365-day requirements, the stressed cash flow assumptions include an increased cash outflow requirement to fund delinquent loan buyouts under a stressed economic environment. To determine this increased cash outflow, the Proposed Rule requires the Enterprises to use the more severe of (i) the Dodd-Frank Act's Stress Testing ("DFAST") severe stress scenario assumptions or (ii) other supervisory stress assumptions as ordered by FHFA.[39]

We propose that FHFA not be prescriptive about the process used to determine the projections for delinquent loan purchases. While DFAST may be a reasonable assumption at times, it is not specifically designed to project loan delinquencies and, at times, other assumptions may also be relevant.

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[39] *See* Proposed Rule, 12 C.F.R § 1241.10(d)(4)(i)(A) and (B).