October 9, 2014

Federal Housing Finance Agency
Office of Strategic Initiatives
400 7th St, S.W.
Washington, D.C. 20024

To Whom it May Concern:

On August 12th, 2014 the Federal Housing Finance Agency (FHFA) released Request for Input: Proposed Single Security Structure (the White Paper). The White Paper describes a proposed structure that would allow Fannie Mae and Freddie Mac (the GSEs) to issue a common mortgage-backed security (MBS) to serve the single-family market. Highlighted in the White Paper are key changes to the structure of both the Fannie Mae MBS and the Freddie Mac PC that would align key terms while enabling some level of competition between the two enterprises.

The Mortgage Bankers Association (MBA)[1] appreciates the opportunity to provide comments on this important issue. For more than two years, MBA has advocated to the GSEs, policymakers, and other stakeholders about the widespread benefits of a single GSE security. Increased standardization and alignment of key terms across issuers has led to increased liquidity, efficiency, and transparency in other markets where it has been attempted.[2] In considering this impact, it is worth noting that the operational and financial differences between issuers is far greater in the corporate bond market than in the GSE residential MBS market.

Adopting a single security would enable the GSEs to compete on a more level playing field, providing benefits to homebuyers, taxpayers and lenders. Ending the trading differential between Fannie Mae and Freddie Mac securities should make our housing finance system more efficient, allowing borrowers to receive the best price on their respective loans. It should also eliminate the Market-Adjusted Pricing (MAP) payments

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[1] The Mortgage Bankers Association (MBA) is the national association representing the real estate finance industry, an industry that employs more than 280,000 people in virtually every community in the country. Headquartered in Washington, D.C., the association works to ensure the continued strength of the nation's residential and commercial real estate markets; to expand homeownership and extend access to affordable housing to all Americans. MBA promotes fair and ethical lending practices and fosters professional excellence among real estate finance employees through a wide range of educational programs and a variety of publications. Its membership of over 2,200 companies includes all elements of real estate finance: mortgage companies, mortgage brokers, commercial banks, thrifts, REITs, Wall Street conduits, life insurance companies and others in the mortgage lending field. For additional information, visit MBA's Web site: www.mortgagebankers.org.

[2] BlackRock, *Corporate Bond Market Structure: The Time for Reform is Now*, September 2014 (available at: https://www.blackrock.com/corporate/en-us/literature/whitepaper/viewpoint-corporate-bond-market-structure-september-2014.pdf)

made by Freddie Mac as a result of the trading differential, saving the enterprise, and ultimately the taxpayers, hundreds of millions of dollars per year. FHFA's action would be entirely consistent with sustaining the GSEs' important role within the current market, while also providing a bridge to an even more competitive and efficient market following reform along the lines of recently proposed legislation.

Additionally, a single security is a key step on the path to GSE reform, a bipartisan goal shared by both Houses of Congress and this Administration. Indeed, a common, "qualified" security formed the basis of the Johnson-Crapo Bill that was voted out of the Senate Banking Committee earlier this year. For these reasons, MBA commends FHFA for exercising leadership in this debate and producing a strong concept for the structure and functioning of a single GSE security.

In order to further the shared goals articulated in the White Paper, MBA convened a working group to identify those areas that must be further analyzed in developing and transitioning to a single security. The issues and questions identified by this group are included in Appendix A. In particular, it is critical that any transition to a single security maintain the liquidity of the to-be-announced (TBA) market for GSE securities. This market is critical to lenders' ability to hedge interest rate risks, and its disruption would ultimately cost borrowers in the form of higher interest rates.

Although FHFA has been clear regarding the importance of this issue, MBA believes that the extended timeframe to implementation poses a potentially unacceptable risk to its successful completion. Market participants need sufficient time to prepare for the change, but a multi-year timeframe coupled with the linkage of the single security to the as yet undeveloped common securitization platform (CSP) pose a risk that the status quo will continue to prevail. FHFA should act quickly to have the GSEs make the necessary changes to their processes within a relatively short timeframe and uncouple the single security process from the worthy, but necessarily complicated development of the CSP.

If the GSEs are unable to utilize their own systems in the near-term to issue the single security, FHFA should move instead to other solutions such as MBA's transition steps proposal that FHFA seek an opinion from the Securities Industry and Financial Markets Association (SIFMA) deeming the Fannie MBS and Freddie PC fungible for TBA purposes. Presently, investors in Freddie Mac PCs receive cash flow earlier than investors in Fannie Mae MBS, which should lead to higher values for the Freddie security, but Freddie Mac PCs trade behind Fannie Mae MBSs because of the market liquidity difference. Declaring them fungible should eliminate the liquidity differential, with no harm to investors.

MBA looks forward to working with FHFA on resolving stakeholder concerns and ensuring that the transition to a single security is smooth and effective. Once complete, a single, fungible, TBA-eligible MBS can restore much needed stability to the housing finance market and bring us one step closer to comprehensive GSE reform. For more information on this topic, please contact Dan McPheeters at (202) 557-2780 or dmcpheeters@mba.org.

Sincerely,

David H. Stevens
President and Chief Executive Officer

APPENDIX A

Key Issues in Transitioning to a Single Security

In response to the White Paper, MBA formed a working group dedicated to reviewing FHFA's request for comment and identifying areas that may warrant further FHFA analysis. Our goal was to provide a list of issues most pertinent from the perspective of both lenders and core mortgage investors. The questions below need to be addressed in some manner in order to successfully implement the single security initiative.

- To what extent will the enterprises be guaranteeing each other's credit risk? How does this impact the "name exposure" of investors? Some investors have identified this as a risk in light of restrictions on the amount of certain portfolios that can be exposed to a single counterparty.
    - This has the potential to harm liquidity in two ways: first, it could reduce potential buyers of the single security; and second, it could cause other market participants to shy away from the single security because of a perceived lack of interest from other investors.
    - FHFA has indicated, and the final single security plan should make it clear that whichever GSE is the top level security guarantor is the investor's counterparty for purposes of measuring counterparty risk. With this policy in place, investors should be able to quickly and at very low cost swap their exposure from Fannie to Freddie and the reverse. FHFA should ensure that both GSEs have the capability and willingness to conduct these swaps to support the market.
- What is the impact of the perception that the GSEs are "cross-guaranteeing" each other's risk?
    - The second-level resecuritization is effectively a guarantee of the performance on the bonds underlying the resecuritization pool. Each resecuritization platform will be open to first-level GSE securities, regardless of which GSE issued an underlying security.
    - Thus, one GSE could be viewed as guaranteeing the financial viability of the other through the resecuritization mechanism.
    - This links not only the operational risks of the two enterprises but the counterparty oversight as well. Further, Treasury may be impacted in the event a draw could be required – would the other GSE step in to fulfill the guarantee, or would a draw on the commitment amount be required?
    - Although there will be an element of cross guaranteeing occurring, as FHFA has noted, whichever GSE is the top level security guarantor of individual securities making up a second-level securitization is the

investor's counterparty for purposes of measuring counterparty risk. Therefore, the cross guarantee should be of little concern to the investor.

- How closely must the Guides/business practices be aligned to achieve desired "closeness?" What differences can/should be allowed? What are the enforcement mechanisms?
    - Many operational and counterparty oversight issues impact bond performance, and thus pricing.
    - Variations in key provisions, such as weighted average coupon, would need to be tightly managed to ensure similar prepayment experiences.
    - Further, differences in Seller/Servicer profile would need to be managed to ensure that the underlying collateral was similar across both GSEs. FHFA would need to monitor this closeness to ensure that secondary market competition is not unduly harmed.
    - On the one hand, investors would continue to retain the right to stipulate the underlying collateral for purposes of fulfilling a forward trade. Ideally, this competitive pressure would prevent a "race to the bottom" in GSE standards. However, it also introduces the possibility that differences between each GSEs' "cheapest to deliver" collateral pool could become sizable and consistent enough to cause the market to rely more heavily on stipulated trading, consequently reducing TBA liquidity.
- How will this impact the dollar roll market? In what way could this have an impact on consumers?
    - The dollar roll market is a critical part of TBA trading activity, both for funding and hedging purposes.
    - The accounting treatment of dollar rolls requires that the securities that are exchanged be "substantially similar" (i.e., same TBA characteristics), which may not be achieved under a single security if the issuer/guarantor is not the same.
    - If the accounting treatment is unfavorable, market liquidity would drop and funding costs would rise due to the use of repo transactions. However, if the FNMA and FRE issuances were deemed to be substantially similar, liquidity could rise due to the increased volume or float.
- Can other entities become issuers of the security if they adopt substantially similar manufacturing and R&W guidelines? If not, what would be needed?
    - A core concept behind many GSE reform proposals has been the introduction of more guarantors to compete with legacy GSE infrastructure and operations.

  - Would these potential entrants have access to the single security? If not, this could pose a significant barrier to entry going forward. MBA believes that any future approved guarantor should be able to issue the single security via the CSP.

- What administrative procedures, if any, need to be followed? Are there any formalities Treasury would need to perform in light of the Preferred Stock Purchase Agreements (PSPAs)?