HOUSING CONNECTION
Mortgage and Real Estate News That Matters

Fannie/Freddie Allowed to Keep More Capital (Again)

Late last week the Federal Housing Finance Agency (FHFA) and the U.S. Department of the Treasury (Treasury) **agreed to amend the Preferred Stock Purchase Agreements** (PSPAs) which govern the required distribution of dividends to Treasury from the government sponsored enterprises (GSEs) Fannie Mae and Freddie Mac. The amendments will bring the amount of capital the companies are permitted to retain into conformance with the 2020 Enterprise Capital Rule unveiled by FHFA in November. Under that rule, the GSEs will be allowed to retain earnings to **maintain tier 1 capital in excess of 4.0 percent of their guarantee obligations** to avoid restrictions on capital distributions and discretionary bonuses.

The PSPAs were written when the GSEs were placed in conservatorship in 2008. In return for financial assistance to sustain them through the housing crisis, Treasury was given senior preferred stock in the two GSEs and a quarterly dividend of 10 percent of the liquidation preference. The agreements were modified in 2012 to permit a net sweep of net worth above a steadily diminishing capital cushion each quarter. **This made it impossible for the GSEs to build capital.** This change, incidentally, occurred five weeks after the GSEs posted their first quarterly profit. PSPAs were further amended in 2018 as the capital buffers were nearing zero, to allow permit them to keep a specified cushion to protect them during any economic downturn.

Under last week's changes, Treasury has also agreed that the GSEs can raise private capital and exit conservatorship once certain conditions are met. To facilitate GSE equity offerings, Treasury has committed to work to restructure its investment in each company.

"Today's agreement that allows Fannie Mae and Freddie Mac to continue retaining earnings is a step in the right direction, but more hard work remains," said FHFA Director Mark Calabria. "Capital at Fannie Mae and Freddie Mac protects the housing finance system and taxpayers. **Retained earnings alone are insufficient** to adequately capitalize the Enterprises. Until the Enterprises can raise private capital, they are at risk of failing in the next housing crisis."

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Mortgage Bankers Association (MBA) President and CEO Bob Broeksmit, CMB, released the following statement regarding the amendments:

"Today's announcement preserves and extends a level playing field for lenders of all sizes and business models while avoiding near-term measures that could have threatened market stability. MBA has cautioned that a premature release of the GSEs from conservatorship could roil the mortgage market, hurting borrowers, savers and investors and harming a fragile economy **still recovering from the ravages of the pandemic.**"

Broeksmit is referring to the addition of section 5.12, Equitable Access to the Secondary Market to the PSPAs. That section reads in part: "Seller shall: not vary the pricing or any other term of the acquisition by Seller of any Single-Family Mortgage Loan (including by granting any variance) based on the size, charter type, or volume of business of the seller of such loan.

Broeksmit continued, "We are pleased with several provisions and will carefully analyze others, including the potential impact of limiting the GSEs' purchases of certain categories of loans. It is critically important that measures to guide the GSEs' market footprint carefully balance the need for them to meet their affordable housing mission for both single-family and multifamily homes. Some of the provisions may prove inflexible during market stress, and it will be vital for FHFA and the Treasury Department to monitor those impacts and remain open to changes as necessary, especially for untested standards.

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