

U.S. DEPARTMENT OF THE TREASURY

Treasury Department and FHFA Amend Terms of Preferred Stock Purchase Agreements for Fannie Mae and Freddie Mac



January 14, 2021

WASHINGTON – The U.S. Department of the Treasury (Treasury) and the Federal Housing Finance Agency (FHFA) today announced an agreement to amend the Preferred Stock Purchase Agreements (PSPAs) between Treasury and each of Fannie Mae and Freddie Mac (the GSEs) to move the GSEs toward capitalization levels consistent with their size, risk, and importance to the U.S. economy, and to codify several existing FHFA conservatorship practices, including providing small lender protections and limiting future increases in certain higher risk lending practices. The agreement also outlines a plan for Treasury, in consultation with FHFA, to develop a proposal for continued GSE reform.

“Today’s agreement to extend capital retention marks an important step for housing finance reform and leaves behind a blueprint that we hope will help guide additional reforms amidst the complex legal and capital structure considerations that remain. Although we would have preferred to have been able to achieve further reforms to the housing finance system through legislative action over the past several years, we are pleased to announce today’s agreement and are thankful for all of the various stakeholders who have helped inform our work.” said Secretary Steven T. Mnuchin.

Treasury entered into the PSPAs on September 7, 2008, the day after FHFA placed the GSEs into conservatorship. Under the PSPAs, Treasury committed to invest in each GSE to the extent necessary to maintain a positive net worth. Treasury’s funding commitment was initially \$100 billion for each GSE, but was subsequently increased in order to ensure a level of capital support that would provide confidence to financial markets and ensure the continued flow of mortgage credit. Today, \$254 billion of the funding commitment remains available to the GSEs.

In return for its commitment, Treasury received from each GSE nonvoting senior preferred shares, warrants to purchase 79.9% of the GSEs’ common stock, and a right to a periodic commitment fee to be determined at a later date. The liquidation preference of the senior preferred shares increases by the amount of each draw on the PSPA funding commitment

and, after \$191.5 billion in combined draws and \$37.2 billion in non-cash increases, the GSEs' combined senior preferred liquidation preference now stands at \$228.7 billion.

Treasury's senior preferred shares were entitled to receive quarterly dividends at an annual rate of 10% of the liquidation preference. As neither GSE was able to consistently generate earnings sufficient to cover the required dividend, in August 2012, Treasury and FHFA amended the senior preferred shares to replace the fixed 10% dividend with a variable dividend equal to each GSE's positive net worth above a specified capital reserve. The August 2012 amendments also suspended the periodic commitment fee while the variable dividend is in place.

The capital reserve was initially set at \$3 billion for each GSE, with the amount declining by \$600 million each year until it was scheduled to decline to zero on January 1, 2018. In December 2017, Secretary Mnuchin and FHFA Director Mel Watt executed letter agreements allowing each GSE to retain additional capital by restoring the capital reserve to \$3 billion.

In September 2019, Secretary Mnuchin and FHFA Director Calabria again amended the PSPAs to permit additional capital retention — up to \$25 billion for Fannie Mae and up to \$20 billion for Freddie Mac. As compensation for taxpayers forgoing cash dividends, the December 2017 and September 2019 changes provided that the liquidation preferences for Treasury's senior preferred stock would increase by the amount of capital the GSEs were permitted to retain. As of September 30, 2020, Fannie Mae and Freddie Mac had retained equity capital of approximately \$21 billion and \$14 billion, respectively.

In order to better protect against unexpected future losses, Secretary Mnuchin and Director Calabria determined that the GSEs should be permitted to continue to accumulate more first-loss capital to stand in front of and protect taxpayers. To this end, Treasury and FHFA have today executed letter agreements that will allow the GSEs to continue to retain capital up to their regulatory minimums, including buffers, as prescribed in the FHFA Enterprise Capital Framework finalized in December 2020.

Key terms of the agreements are:

- **Extend Capital Retention:** Replace the variable dividend (i.e., net worth sweep) with alternative compensation to permit the GSEs to continue their recapitalization efforts. As compensation to Treasury, the liquidation preference will increase by the amount of retained capital until the GSE has achieved its regulatory minimum capital, including buffers (referred to as the capital reserve end date).

- Upon the capital reserve end date, the GSEs will resume quarterly dividend payments. The dividend amount at that time will be equal to the lesser of 10% of the liquidation preference of Treasury's senior preferred stock, or the incremental increase in the GSE's net worth in the prior quarter.
- Before the capital reserve end date, Treasury and the GSEs will determine a periodic commitment fee for Treasury's remaining funding commitment, to compensate taxpayers for their risk in supporting the GSEs.
- **Treasury Establishes No Exit From Conservatorship With Less Than 3% Capital:** The letter agreements provide that there will be no exit until all material litigation relating to the conservatorship is resolved or settled, and the GSE has common equity tier 1 capital of at least 3% of its assets.
- **Allow for Common Stock Issuance at Appropriate Time:** Treasury will allow each GSE to issue common stock upon the achievement of future conditions: first, Treasury must have exercised in full its warrant to acquire 79.9% of the GSE's common stock, and second, all material litigation relating to the conservatorship must have been resolved or settled. Treasury will permit up to \$70 billion in proceeds of stock issuances by each GSE to be used to build capital.
- **Limit Future Increases to the Retained Mortgage Portfolio:** The PSPA cap on the GSEs' retained mortgage portfolios will be lowered from the current cap of \$250 billion to \$225 billion by the end of 2022, aligning with the FHFA conservatorship cap the GSEs are required to comply with today, while providing the GSEs with flexibility to manage through the current economic environment. As of November 2020, Fannie Mae's mortgage portfolio was \$163 billion, and Freddie Mac's mortgage portfolio was \$193 billion.
- **Provide Small Lender Protections:** The letter agreements codify FHFA conservatorship directives that require the GSEs to purchase loans for cash consideration, and to operate this cash window with non-discriminatory pricing. Additionally, to ensure that the cash window is for the benefit of community lenders, each GSE will limit volume purchased through the cash window to \$1.5 billion per lender during any period comprising four calendar quarters.
- **Memorialize FHFA Multifamily Lending Caps:** Each GSE will cap multifamily acquisitions at \$80 billion over the trailing 52-week period and will require that 50% of these acquisitions are mission driven, as defined by FHFA.

- **Limit Risk to the GSEs by Keeping Certain Higher-Risk Single-Family Mortgage Acquisitions at Current Levels:** To safeguard Treasury’s funding commitment and to ensure the GSEs’ business activities are consistent with their mission and Treasury’s capital support, the GSEs will restrict the acquisition of higher-risk single-family mortgage loans.
 - The GSEs will limit the acquisition of single-family mortgage loans with multiple higher risk characteristics at their current levels. A maximum of 6% of purchase money mortgages and maximum of 3% of refinancing mortgages over the trailing 52-week period can have two or more higher risk characteristics at origination: combined loan-to-value (LTV) greater than 90%; debt-to-income ratio greater than 45%; and FICO (or equivalent credit score) less than 680.
 - The GSEs will limit the acquisition of single-family mortgage loans secured by second homes and investment properties to 7% of single-family acquisitions — aligned with their current levels — over the preceding 52-week period.
 - The GSEs will limit the acquisition of single-family mortgage loans to (i) qualified mortgages, (ii) loans exempt from the CFPB’s ability-to-repay requirement, (iii) loans for investment property subject to the restrictions above, (iv) refinancing loans with streamlined underwriting for high loan-to-value ratios, (v) loans originated with temporary underwriting flexibilities due to exigent circumstances, and (vi) loans secured by manufactured housing.
- **Require GSE Compliance with FHFA Capital Framework:** The letter agreements provide that the GSEs will comply with FHFA’s recently finalized regulatory capital framework, consistent with the [findings](#) of the Financial Stability Oversight Council (FSOC) in a statement issued in September 2020.
- **Outline a Plan to Develop a Proposal for Continued GSE Reform:** To ensure a path for Treasury to resolve its investment in the GSEs in a manner that fairly compensates taxpayers for the support they have provided and continue to provide, Treasury, in consultation with FHFA, has begun work to establish a timeline and process for further GSE reform. Pursuant to this commitment, Treasury has identified key considerations that will inform this effort, as a part of its Blueprint on Next Steps for GSE Reform.

[Executed Letter Agreement for Fannie Mae](#) 

[Executed Letter Agreement for Freddie Mac](#) 

[Treasury Department Blueprint on Next Steps for GSE Reform](#) 

