

## Appendix B: Analysis of Counterparty Risk Posed by Enterprise Securitizations

The chart on the following pages provides a comparative analysis, in legal terms, of how an investor’s claim for nonpayment on an Enterprise security held by such investor would be satisfied under both: (A) current Enterprise securitizations and (B) future Enterprise securitizations under the Single Security program. This legal analysis of counterparty risk is presented at two levels: first, with respect to the basic, single-class pass-through security of each Enterprise (the “**First Level Securitization**,” resulting in a “**Level 1 MBS**”) and second, with respect to further securitizations of those basic securities, whether in a single-class or multiclass/REMIC form (the “**Second Level Securitization and other Re-Securitizations**,” resulting in a “**Level 2 Security**”). To place the legal analysis in context, it will be helpful to discuss the relevant principles with illustrations from typical transactions under the Single Security program, as follows.

The guiding principle in considering counterparty risk, in both the current context and under Single Security, is that the holder of any security looks to the issuer of that security for performance of the issuer’s guarantee. For example, if an investor purchases two Freddie Mac-issued Level 1 MBS, the investor’s counterparty is Freddie Mac, as the issuer and guarantor of those Level 1 MBS securities. Accordingly, Freddie Mac’s performance is directly relevant to the investor; Fannie Mae has no performance obligations regarding those securities.

This issuer-as-guarantor principle described above remains true in the case of a Level 2 Security, regardless of whether the guarantor of the Level 2 Security is different than the guarantor of any underlying Level 1 MBS. Continuing the example from above, the investor that purchased two Freddie Mac-issued Level 1 MBS could thereafter tender those two securities (and/or others issued by either Enterprise, since “commingling” of Enterprise securities is permitted in Level 2 Securities) to Fannie Mae in exchange for a Fannie Mae-issued Level 2 Security. The Level 2 Security in this example would be issued and guaranteed by Fannie Mae, and backed by the collateral tendered by the investor (i.e., the two Freddie Mac-issued Level 1 MBS, and/or other Level 1 MBS). Once the Level 2 Security in this example is issued and delivered by Fannie Mae, the investor’s counterparty for that security is Fannie Mae. Freddie Mac’s original guarantee of its Level 1 MBS remains in effect, but as a result of the Second Level Securitization, Freddie Mac’s guarantee now runs to the trust of the Level 2 Security, not the investor.



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Let us return to the example from above, for purposes of analysis. After the Level 2 Security issuance date, the investor in the Level 2 Security would look to Fannie Mae for timely payment of principal and interest on the Level 2 Security. Assuming that Fannie Mae performs, any hypothetical payment default by Freddie Mac on any underlying Level 1 MBS, or any hypothetical receivership of Freddie Mac, would not affect the Level 2 Security investor. If, however, Fannie Mae was to default on its guarantee of its Level 2 Security or was to enter into receivership, the analysis differs.<sup>1</sup> First, since the trust for the Level 2 Security owns the underlying Level 1 MBS, the Level 2 Security investor would continue to be entitled to principal and interest received on the underlying Level 1 MBS. The Housing and Economic Recovery Act of 2008 (HERA) provides that the underlying Level 1 MBS are unavailable to satisfy the claims of other Fannie Mae creditors if Fannie Mae enters into receivership.<sup>2</sup> Second, FHFA, in its role as receiver, would need to determine, consistent with applicable law, how to treat the Level 2 Security investor's claim regarding Fannie Mae's guarantee obligations.

Whether under current Enterprise securitization programs or the Single Security, neither Enterprise's securities are guaranteed by, or represent the debts or obligations of, the United States or any federal agency or instrumentality other than the issuing Enterprise. Through the Senior Preferred Stock Purchase Agreements,<sup>3</sup> however, the United States Department of the Treasury provides each Enterprise with financial support, under certain conditions, to eliminate deficits in their net worth. As of March 31, 2015, the amounts of available funding remaining under these agreements were \$140.5 billion for Freddie Mac and \$117.6 billion for Fannie Mae.

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<sup>1</sup> If either Enterprise was to enter receivership, that event would trigger a guarantor default without any further action by certificate holders. For either Enterprise, such a guarantor default would allow investors representing a majority of the voting rights of the trust to select a new trustee/administrator.

<sup>2</sup> See 12 U.S.C. 1367(b)(19)(B). A similar analysis would apply to the underlying Level 1 MBS issued by Freddie Mac if both Freddie Mac and Fannie Mae were in receivership at that time.

<sup>3</sup> Amended and Restated Senior Preferred Stock Purchase Agreement between the United States Department of the Treasury and Federal Home Loan Mortgage Corporation dated as of September 26, 2008, as amended (for Freddie Mac), and Amended and Restated Senior Preferred Stock Purchase Agreement between the United States Department of the Treasury and Federal National Mortgage Association dated as of September 26, 2008, as amended (for Fannie Mae).



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<b>FIRST LEVEL SECURITIZATION</b>		
	<b>TODAY</b> <b>(UNDER CURRENT ENTERPRISE PROGRAMS)</b>	<b>FUTURE</b> <b>(UNDER SINGLE SECURITY PROGRAM)</b>
<b>Name of Security Created</b>	<ul style="list-style-type: none"> <li>Gold PC (Freddie Mac) or MBS (Fannie Mae)</li> </ul>	Single-Class Pass-Through Level 1 Agency MBS <b>("Level 1 MBS")</b>
<b>Issuer of Security</b>	<ul style="list-style-type: none"> <li>Issuing Enterprise (either Freddie Mac or Fannie Mae)</li> </ul>	NO CHANGE
<b>Original Purchaser of Underlying Assets and Depositor into the Trust</b>	<ul style="list-style-type: none"> <li>Issuing Enterprise (100%)</li> </ul>	NO CHANGE
<b>Guarantor</b>	<ul style="list-style-type: none"> <li>Issuing Enterprise</li> </ul>	NO CHANGE
<b>Guarantee Terms</b>	<ul style="list-style-type: none"> <li>For Gold PCs and MBS, timely principal and interest</li> </ul>	NO CHANGE
<b>If Loan Defaults</b>	<ul style="list-style-type: none"> <li>Issuing Enterprise pays on guarantee</li> <li>If default continues, loan generally is repurchased from pool at 120 days delinquency, per the Issuing Enterprise's loans-in-acceleration ("<u>LIA</u>") policy; repurchase proceeds are passed through to investors as prepayment.</li> </ul>	NO CHANGE
<b>If Issuing Enterprise Defaults on its Guarantee Obligations or if Issuing Enterprise in Receivership</b>	<ul style="list-style-type: none"> <li>Investors continue to have an interest in the underlying assets of the trust and thus would be entitled to principal and interest received on those assets in accordance with the terms of the trust (as set forth in the Trust Agreement).</li> <li>Underlying assets are legally isolated (not available for general creditors of the Issuing Enterprise) by trust structure and pursuant to the Housing and Economic Recovery Act of 2008 ("HERA").</li> <li>Funding available to each Enterprise under its Senior Preferred Stock Purchase Agreement (SPSPA) with the U.S. Department of the Treasury limits the risk of a guarantor payment default. In the event of such payment default, and in the event the U.S. Department of the Treasury fails to perform its obligations to the relevant Enterprise in respect of the financial support committed under that Enterprise's SPSPA, affected investors are entitled to file claims in the United States Court of Federal Claims for relief requiring the U.S. Department of the Treasury to pay liquidated damages to the relevant Enterprise.<sup>1</sup> In the event of such payment default, investors would have an unsecured claim against the Issuing Enterprise for any funds owed by the Issuing Enterprise as guarantor. If the Issuing Enterprise were to be in receivership, FHFA would evaluate such claims pursuant to HERA.</li> </ul>	NO CHANGE



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<b>FIRST LEVEL SECURITIZATION</b>		
	<b>TODAY (UNDER CURRENT ENTERPRISE PROGRAMS)</b>	<b>FUTURE (UNDER SINGLE SECURITY PROGRAM)</b>
	<ul style="list-style-type: none"> <li>Failure by the Issuing Enterprise to make a guarantee payment would constitute a Guarantor Event of Default: For Freddie Mac, if such payment failure lasts for 30 days; and for Fannie Mae, 15 days after at least 5% of the relevant certificate holders give notice of such failure (assuming the failure is not cured). For either Enterprise, such Guarantor Event of Default would allow investors representing a majority of the voting rights of the trust to select a new trustee/administrator.</li> </ul>	
<b>If Non-Issuing Enterprise in Receivership</b>	<ul style="list-style-type: none"> <li>No impact to investors or the Issuing Enterprise because there is no “commingling” of loans underlying Gold PCs or MBS.</li> </ul>	NO CHANGE

<b>SECOND LEVEL SECURITIZATION AND OTHER RE-SECURITIZATIONS</b>		
	<b>TODAY (UNDER CURRENT ENTERPRISE PROGRAMS)</b>	<b>FUTURE (UNDER SINGLE SECURITY PROGRAM)</b>
<b>Name of Security Created</b>	<ul style="list-style-type: none"> <li>Giant (Freddie Mac), Mega (Fannie Mae), Freddie Mac REMIC or Fannie Mae REMIC</li> </ul>	<ul style="list-style-type: none"> <li>Single-Class Pass-Through Level 2 Agency MBS or REMIC (“<b>Re-Securitization MBS</b>”)</li> </ul>
<b>Issuer of Security</b>	<ul style="list-style-type: none"> <li>Issuing Enterprise (either Freddie Mac or Fannie Mae)</li> </ul>	NO CHANGE
<b>Original Issuer of Underlying Securities</b>	<ul style="list-style-type: none"> <li>Issuing Enterprise (100%)</li> </ul>	<ul style="list-style-type: none"> <li>Any mix of TBA-eligible or REMIC securities from either or both Enterprises (commingling of Level 1 MBS and/or Re-Securitization MBS originally issued by either Enterprise permitted)</li> </ul>
<b>Guarantor to Investors</b>	<ul style="list-style-type: none"> <li>Issuing Enterprise</li> </ul>	<ul style="list-style-type: none"> <li>NO CHANGE (i.e., Enterprise issuing most recently-issued Re-Securitization MBS)</li> </ul>



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SECOND LEVEL SECURITIZATION AND OTHER RE-SECURITIZATIONS		
	<b>TODAY</b> <b>(UNDER CURRENT ENTERPRISE PROGRAMS)</b>	<b>FUTURE</b> <b>(UNDER SINGLE SECURITY PROGRAM)</b>
<b>Guarantee Terms</b>	<ul style="list-style-type: none"> <li>For Gold Giants, Megs and REMICs, timely principal and interest<sup>ii</sup></li> </ul>	NO CHANGE
<b>If Loan Defaults</b>	<ul style="list-style-type: none"> <li>Issuing Enterprise pays on guarantee</li> <li>If default continues, loan generally is repurchased from pool at 120 days delinquency per the Issuing Enterprise’s LIA policy; repurchase proceeds passed through to investors as prepayment.</li> </ul>	<p style="text-align: center;">Same as today, plus:</p> <ul style="list-style-type: none"> <li>Issuing Enterprise will fully guarantee its Re-Securitization MBS, regardless of the original issuer of the underlying securities.<sup>iii</sup></li> </ul>
<b>If <u>Issuing Enterprise</u> Defaults on its Guarantee Obligations or if Issuing Enterprise in Receivership</b>	<ul style="list-style-type: none"> <li>Investors continue to have an interest in the underlying assets of the trust and thus would be entitled to principal and interest received on those assets in accordance with the terms of the trust.</li> <li>Underlying assets are legally isolated (not available for general creditors of the Issuing Enterprise) by trust structure and pursuant to HERA (12 U.S.C. 1367(b)(19)(B)(i)).</li> <li>Funding available to each Enterprise under its SPSPA with the U.S. Treasury limits the risk of a guarantor payment default. In the event of such payment default, and in the event the U.S. Treasury fails to perform its obligations to the relevant Enterprise in respect of the financial support committed under that Enterprise’s SPSPA, affected investors are entitled to file claims in the United States Court of Federal Claims for relief requiring the U.S. Treasury to pay liquidated damages to the relevant Enterprise.<sup>iv</sup> In the event of such payment default, investors would have an unsecured claim against the Issuing Enterprise for any funds owed by the Issuing Enterprise as guarantor. If the Issuing Enterprise</li> </ul>	<p style="text-align: center;">Same as today, plus:</p> <ul style="list-style-type: none"> <li>Investors will continue to receive guarantee payments that are passed through from the Non-Issuing Enterprise, to the extent the Non-Issuing Enterprise’s Level 1 MBS backs the Re-Securitization MBS.</li> </ul>



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	<b>TODAY</b> <b>(UNDER CURRENT ENTERPRISE PROGRAMS)</b>	<b>FUTURE</b> <b>(UNDER SINGLE SECURITY PROGRAM)</b>
	<p>is in receivership, FHFA, as receiver, would evaluate such claims pursuant to HERA.</p> <ul style="list-style-type: none"> <li>Failure by the Issuing Enterprise to make a guarantee payment would constitute a default: For Freddie Mac, if such payment failure lasts for 30 days; and for Fannie Mae, 15 days after at least 5% of the relevant certificate holders give notice of such failure (assuming the failure is not cured). For either Enterprise, such default would allow investors representing a majority of the voting rights of the trust to select a new trustee/administrator.</li> </ul>	
<p><b>If <u>Non-Issuing Enterprise</u> Defaults on its Guarantee Obligations or if Non-Issuing Enterprise in Receivership</b></p>	<ul style="list-style-type: none"> <li>No impact to investors or Issuing Enterprise because no commingling of loans underlying second-level securities or REMICs.</li> </ul>	<ul style="list-style-type: none"> <li>Issuing Enterprise will fully guarantee its Re-Securitization MBS<sup>v</sup></li> <li>No rights of investors to makes claims against the Non-Issuing Enterprise</li> </ul>
<p><b>If <u>Issuing Enterprise</u> Defaults on its Guarantee Obligations and <u>Both Enterprises</u> in Receivership</b></p>	<ul style="list-style-type: none"> <li>Not applicable because no commingling of loans underlying second-level securities or REMICs. Analysis is similar to discussion above under “<i>If Issuing Enterprise Defaults on its Guarantee Obligations or if Issuing Enterprise in Receivership.</i>”</li> </ul>	<ul style="list-style-type: none"> <li>Investors continue to have an interest in the underlying assets of the trust and thus would be entitled to principal and interest received on those assets in accordance with the terms of the trust and HERA (underlying assets would not be available for the general creditors of the Enterprises).</li> <li>Investors will continue to receive guarantee payments that are passed through from the Non-Issuing Enterprise, to the extent the Non-Issuing Enterprise’s Level 1 MBS backs the Re-Securitization MBS.</li> <li>Funding available to each Enterprise under its SPSPA with the U.S. Treasury limits the risk of</li> </ul>



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SECOND LEVEL SECURITIZATION AND OTHER RE-SECURITIZATIONS		
	<u>TODAY</u> (UNDER CURRENT ENTERPRISE PROGRAMS)	<u>FUTURE</u> (UNDER SINGLE SECURITY PROGRAM)
		<p>guarantor payment default. In the event of such payment default, and in the event the U.S. Treasury fails to perform its obligations to the relevant Enterprise in respect of the financial support committed under that Enterprise’s SPSPA, affected investors are entitled to file claims in the United States Court of Federal Claims for relief requiring the U.S. Treasury to pay liquidated damages to the relevant Enterprise.<sup>vi</sup> In the event of such payment default, investors would have an unsecured claim against the Issuing Enterprise for any funds owed by the Issuing Enterprise as guarantor. FHFA, as receiver, would evaluate such claims pursuant to HERA.<sup>vii</sup></p> <ul style="list-style-type: none"> <li>• Failure by the Issuing Enterprise to make a guarantee payment would constitute a default: For Freddie Mac, if such payment failure lasts for 30 days; and for Fannie Mae, 15 days after at least 5% of the relevant certificate holders give notice of such failure (assuming the failure is not cured). For either Enterprise, such default would allow investors representing a majority of the voting rights of the trust to select a new trustee/administrator.</li> <li>• No rights of investors to make claims against the Non-Issuing Enterprise</li> </ul>



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<sup>i</sup> See Letter Opinion for the Secretary of the Treasury, dated September 26, 2008, from the Office of Legal Counsel, U.S. Department of Justice.

<sup>ii</sup> For Freddie Mac Giants, in addition to a guarantee of principal by the final payment date, Freddie Mac guarantees timely payment of interest and payment of principal as principal payments are made on the underlying assets. Freddie Mac Giants backed by Gold PCs (“Gold Giants”) therefore receive the benefit of the guarantee of timely payment of both interest and principal on such Gold PCs.

<sup>iii</sup> If a defaulting loan backs a Level 1 MBS or Re-Securitization MBS issued by the Non-Issuing Enterprise, the Issuing Enterprise will also have an unsecured indemnity or contractual claim against the Non-Issuing Enterprise for the Non-Issuing Enterprise’s underlying guarantee payments.

<sup>iv</sup> See Letter Opinion for the Secretary of the Treasury, dated September 26, 2008, from the Office of Legal Counsel, U.S. Department of Justice.

<sup>v</sup> To extent the Non-Issuing Enterprise’s Level 1 MBS backs the Re-Securitization MBS, the Issuing Enterprise will also have an unsecured indemnity or contractual claim against the Non-Issuing Enterprise for the Non-Issuing Enterprise’s underlying guarantee payments.

<sup>vi</sup> See Letter Opinion for the Secretary of the Treasury, dated September 26, 2008, from the Office of Legal Counsel, U.S. Department of Justice.

<sup>vii</sup> To extent the Non-Issuing Enterprise’s Level 1 MBS backs the Re-Securitization MBS, the Issuing Enterprise will also have an unsecured indemnity or contractual claim against the Non-Issuing Enterprise for the Non-Issuing Enterprise’s underlying guarantee payments.

