Client Alert

May 2020

Leading the LIBOR Transition

Freddie Mac and Fannie Mae (together, the "GSEs") cemented their position as leaders in LIBOR transition this week not only with their widely-publicized release of the joint LIBOR Transition Playbook, Timeline and FAQs, but also, more impressively, by posting amendments and an omnibus trust supplement to the documents governing their legacy LIBOR-indexed collateralized mortgage obligations ("CMOs"). These amendments and the supplement sound the first salvo in the battle of how to handle LIBOR replacement in legacy residential mortgage securitizations.

The GSEs, together with Ginnie Mae, are uniquely positioned to lead the way in LIBOR transition given their position as issuers or guarantors of trillions of residential mortgage-backed securities ("RMBS") and as government-sponsored or government-owned enterprises. It is anticipated that where the GSEs and Ginnie Mae lead, much of the private label RMBS and related market will likely follow. The GSEs and Ginnie Mae have all adopted some form of the recommendations of the Alternative Reference Rates Committee (the "ARRC") for LIBOR replacement language in new LIBOR-indexed CMO issuances. With their announcement, the GSEs have taken steps to treat their existing CMOs in the same manner.

Legacy CMO Transactions: Freddie Mac and Fannie Mae Announce an Amendment/Supplement Approach to Adopting LIBOR Replacement Language

In two announcements, available here and here, the GSEs posted amendments and an omnibus trust supplement (together, the "amendments") to the documents governing legacy CMOs. These amendments add the ARRC recommended LIBOR replacement language to the governing documents for existing multiclass REMIC and strip securities. According to the GSEs, these documents did not contemplate a permanent cessation of LIBOR, and the amendments are intended to address that shortcoming. Under the amendments, as recommended by the ARRC, the Secured Overnight Financing Rate ("SOFR"), either term or compounded plus some spread adjustment, will replace LIBOR. With these amendments, previously announced moratoria on new REMIC issuances backed by legacy LIBOR-indexed CMOs have been lifted by both of the GSEs, permitting their inclusion in new REMIC issuances beginning in June 2020.

While these announcements did not capture the same headlines as the joint LIBOR Transition Playbook, Timeline and FAQs, they answer the question how the GSEs will address LIBOR replacement for their outstanding CMOs. Perhaps of equal or greater significance, these amendments, together with the prior actions of the GSEs and Ginnie Mae related to new issuances, provide an indicator of how LIBOR replacement will be addressed in both newly-issued and legacy private-label RMBS.

These announcements, the release of the joint LIBOR Transition Playbook, Timeline and FAQs and prior measures taken by the GSEs and Ginnie Mae may be enough to foster market acceptance of SOFR as LIBOR's successor and provide a game plan for all market participants to orderly transition legacy LIBOR-indexed issuances into a post-LIBOR world. Undoubtedly, this transition will be more complicated and more likely to grab headlines when the GSEs, Ginnie Mae and private-label RMBS sponsors expand their efforts beyond the GSE CMOs addressed by the amendments announced on May 28, 2020. If the market coalesces around SOFR, the challenge will be to marshal the resources necessary to amend or supplement legacy transactions with diverse stakeholders.

The Future of LIBOR & SOFR GSE Products: The Freddie Mac and Fannie Mae LIBOR Transition Playbook, Timeline and FAQs

As noted above, the GSEs have jointly published a LIBOR Transition Playbook, Timeline and FAQs on webpages specifically dedicated to the LIBOR transition. Freddie Mac's LIBOR Transition webpage may be accessed here and Fannie Mae's LIBOR Transition webpage may be accessed here.

The release of these materials is notable because they set forth a consolidated transition timeline and outline the anticipated impact of moving from LIBOR to SOFR on the future of the following GSE products:

- single-family adjustable rate mortgages ("ARMs") and related mortgage-backed securities;
- Fannie Mae multifamily ARMs and related mortgage-backed securities;
- Freddie Mac MF floating rate loans and securities;
- single-family credit risk transfer securities (e.g., STACR, CAS and CIRT) and multifamily credit risk transfer securities (e.g., SCR Notes, MCAS and MCIRT); and
- collateralized mortgage obligations.

As anticipated given their membership on the ARRC, the GSE's approach is consistent with the ARRC's recommendations – to adopt SOFR as the alternative index for new products and issuances. The GSEs have also announced plans to phase out their acceptance of LIBOR-indexed ARMs by December 31, 2020, limit the acquisition of LIBOR-indexed ARMs to those with applications dated on or before September 30, 2020 and require standard ARM Notes and Riders to include the ARRC fallback approach for the discontinuance of LIBOR.

Hunton Andrews Kurth has a deep bench of attorneys focused on counseling clients as they grapple with the LIBOR transition. Their experience bridges diverse practice areas and securities beyond those issued by the GSEs, Ginnie Mae and sponsors of private label RMBS and CMOs. Please check our website for future discussion of how Hunton Andrew Kurth anticipates the LIBOR transition will unfold.

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London Inter-bank Offered Rate ("LIBOR") is used as the reference rate for more than $200 trillion financial contracts and related securities, but perhaps not for much longer. As the United Kingdom Financial Conduct Authority has announced, a panel of banks have voluntarily agreed to continue to submit the rates used to publish LIBOR through the end of 2021. After 2021, the submission of these rates and the publication of LIBOR is expected to cease and, consequently, LIBOR is likely to be phased out as a widely-used benchmark interest rate in future and legacy transactions.