## Single Security Tabletop Testing Working Session #1

<table>
<thead>
<tr>
<th>Hosted By:</th>
<th>Freddie Mac and Fannie Mae</th>
</tr>
</thead>
<tbody>
<tr>
<td>Meeting Date</td>
<td>07/30/2018</td>
</tr>
<tr>
<td></td>
<td>10:00AM – 1:00PM</td>
</tr>
<tr>
<td>Meeting Location</td>
<td>Bloomberg</td>
</tr>
<tr>
<td></td>
<td>120 Park Ave, NY, NY</td>
</tr>
<tr>
<td>Attendees</td>
<td><strong>GSEs and related:</strong> Fannie Mae, Freddie Mac, CSS</td>
</tr>
<tr>
<td></td>
<td><strong>Regulatory Agency &amp; Trade Groups:</strong> FHFA, SIFMA, NY Fed</td>
</tr>
<tr>
<td></td>
<td><strong>Custodians:</strong> BNY Mellon, JP Morgan, Pershing</td>
</tr>
<tr>
<td></td>
<td><strong>Seller/Servicers:</strong> Land Home Financial, Quicken</td>
</tr>
<tr>
<td></td>
<td><strong>Investors:</strong> BlackRock, Chase, JP Morgan, Mesirow Financial, BNY, PGIM</td>
</tr>
<tr>
<td></td>
<td><strong>Dealers:</strong> BNP Paribas, Citi, JP Morgan</td>
</tr>
<tr>
<td></td>
<td><strong>3rd Party Vendors:</strong> BlackRock, Bloomberg, Broadridge, Charles River, DTCC, FICC, The ICE, Tradeweb</td>
</tr>
</tbody>
</table>

### General Discussion:
- **Citi:** Will there be similar testing exercise for system integration testing?  
  - Not the focus for today.  
- Will Freddie be inviting a volunteer to do the test and share the results with the industry?  
  - This is a group effort. The group will discuss concerns, issues and scenarios that will be good for a tabletop exercise. The live exercise itself will have one or two key players representing each market area. One or two Broker Dealers, investors, custodians, etc. Freddie will take volunteers who are interested. We expect there will also be observers there, and will publish the discussion afterward.  
- APG: What types of exercises? Is it operational, front office, back office?  
  - Enterprises are thinking end-to-end. Front office trading all the way to back office. The focus will be operational, but want to run through from front-end to the back-end.  

### Part 1: Questions
- What is your experience managing industry-wide testing with other initiatives?  
  - CRD: Recent example is MiFID II in Europe. There was continuous planning and asking, “what else could go wrong?” Even after all that, we realized we didn’t focus on all important areas. Getting different perspectives from all participants is important.  
  - DTCC: Just completed MBS Novation initiative last year. Getting participants in early was important. We did not design our entire system and then present it to stakeholders, we were very active in involving industry participants along the entire process. Communication is key. Making sure everyone is involved from day 1 is important. Tremendous amount of internal testing, but client testing was open for 6-8 months. Scripted testing. Everyone had to go through a script and had to pass it before we moved forward.  
  - JPM: Everything was done in progression. It was gradual to make sure it’s working.
- DTCC: Did not want to jump into the deep end. Started slowly, ramped up, and once everyone felt comfortable we ramped it up more. The internal testing caught a lot of issues, same with external. We put lots of fixes in along the way.
  - SIFMA: Biggest was T2 conversion. That involved hiring consultants (Deloitte) and DTCC. Having a large playbook written out. Lots of testing.
  - In both of those scenarios, regulatory decisions were an inhibiting factor. In this (Single Security) case, we don’t have regulatory clarity yet either.
- What are your greatest operational concerns or challenges moving to Single Security?
  - APG: How are we going to make these transfers? Will they be DVP or internal transfers? When will this information be made public?
  - JPM: The version when a dealer facilitates it. Testing the volume and how quickly we can get the return of security back out.
  - Are there any concerns about the normal course of business trading activity? Doing regular trades and rolls
    - UMBS as an issuer is an important concept.
      - BRS: From Aladdin’s perspective, this is not a field that gets communicated to external systems. When you trade with Bloomberg, it won’t go to them. It’s only for your use with Aladdin.
      - Broadridge: We see it the same way. We will allow our clients to use the new UMBS issuer if they like. If they want to label it as FNCL, they can do that too.
      - SIFMA: Many players are waiting to see what the Treasury says about 817(h). This may determine what firms do with the UMBS issuer.
  - Netting
  - Rolls – want to make sure that rolls between May and June go smoothly from Fannie/Freddie or UMBS.
  - Pricing – trying to anticipate how these will trade. How long will Freddie TBA market survive? Makes it more difficult to put valuations on these securities.
- Are there other types of testing that could be possible besides tabletop and system to system?
  - BNY: DTCC made a very helpful playbook where they wrote out each scenario and provided checklists to make sure that everyone knows all the areas that we need to test. This exercise would be helpful for the market adoption playbook. [Believe this was part of the T+2 preparation by SIFMA with Deloitte]

**Part 2: Brainstorming scenarios**

**Commingling of Securities**
- Wellington: Supers and CMOs – the multi issuer problem is something we are concerned with. Representation and client guidelines. Some clients view the agencies as the same and some want them to distinguish. Will need to develop systems to recognize that we may get 100% Fannie or 100% Freddie.
- Wellington: Securitization of Supers and CMOs.
  - On a Fannie-backed Supers, if the Supers had a mix of Fannie/Freddie, would you have to parse the Supers?
    - Wellington will have clients that are fine with the top-level issuer, but some clients will undoubtedly want them to parse through because they don’t view Fannie and Freddie as the same. That data needs to be available and systems will need to test with that.
  - Bloomberg is developing a file to show that
- UMBS Commingling Re-securitization
Data vendors will have to figure out how to identify and display the information about the percentage of underlying between Fannie/Freddie in UMBS.

Bloomberg is going to show each pool with the percentage of the underlying. Planning on providing this all the way up for Supers, REMICs, and CMOs.

**TBA Trading**

- PGIM: Can we talk further about the BAU UMBS trading? Are we to assume that if I have a Fannie TBA in June, that I can have UMBS delivered into it?
  - This may need to be clarified. If you’re long in the Fannie position, need to talk about if that can turn into a UMBS.
- DTC: There are a lot of outstanding issues operationally on good delivery if there are fails, dollar rolls, etc. It’ll be very important for a working group across buy and sell side to hammer out guidelines. Leaving it up to just the two parties doesn’t always work.
- Freddie will have direct testing with the seller community for seller-relevant changes.
- Servicing side: TBA clearing will be important for the seller servicer community. Freddie Mac may follow-up and do a tabletop exercise directly with S/S rather than including in the industry-wide tabletop exercise.

**Part 3: Exchange tabletop**

- Freddie wants to make sure they have captured all the right steps. Asking participants to write additional considerations, steps, and put them up on the board.
- Must dealers be authorized to facilitate exchanges?
  - Yes. There are currently 40 Giant dealers authorized on dealer-direct.
  - The email about getting certified for exchanges just went out to current authorized dealers.
- What is the method of communication for an investor to tell their dealer they want to exchange?
  - Freddie is looking for the community to determine what that message will be (SWIFT, BIC) to tell the custodians they want to exchange these securities. Would ideally use this same message to communicate to the dealer, and for the dealer to communicate with Freddie.
  - From a dealer perspective, expectation is to do the buy transaction on the day of exchange. Investors would notify dealers prior, dealers would ask Freddie of availability, then dealers would communicate back to investors that it’s available. Dealers would book a buy of the new security with Freddie, and then sell it back to the investor.
- Investors may want to consider talking to their OMS to make sure they can capture it as an exchange.
- Settlement
  - Risk of delivering the 45d MBS to Freddie, and not receiving the 55d security back
  - Will Freddie be issuing trust receipts?
- How do you agree what price to use? At the portfolio level, it will be fine, but it could break down at the security level. Is the 10-day payment return of capital or income? Whatever that answer is, accounting systems will need to capture that. The operational impacts of capturing the payment.
  - Dealers will think of it by market convention.
  - Some investors would book this as an exchange in and exchange out. This is very different to booking a buy and a sell. There are implications that come with this in terms of settling it as a DVP and RVP.
    - Want to keep cost basis the same. Trying to jam this into the system will be a problem with a lot of manual work. The buy/sell framework with the imminent IRS decision does not work well.
• Custodians have an issue here as well. BNY will build logic in their system to recognize the exchanges and will need to figure out how to treat these transactions.
  o Custodians would like to have the calendar of availability for dealer direct.
  o There will there be blackout dates for exchanges.

Part 4: Next steps
• Based on the scenarios that we decide on for the next working sessions, participants can opt in to those sessions that are most relevant to them.
• Can Nick from DTCC comment on their certification requirements for Single Security?
  o Going to offer two types of testing. One for clearing members (BD community) and one testing for EPN only members. Each will be scripted, nowhere near as complicated as they were for Novation testing. Targeting November for the clearing members. First quarter of next year for the EPN only members.

<table>
<thead>
<tr>
<th>Action Items</th>
<th>Owner</th>
<th>Due Date/Status</th>
</tr>
</thead>
<tbody>
<tr>
<td>Determine Workstreams focused on the concerns/issue scenarios and assign Workstream Leads</td>
<td>Freddie Mac</td>
<td>8/15/2018</td>
</tr>
<tr>
<td>Schedule next industry wide meeting for early September</td>
<td>Freddie Mac</td>
<td>8/15/2018</td>
</tr>
</tbody>
</table>