Tabletop Working Group Meeting #2

Meeting Name	Tabletop Meeting #2		
Meeting Date	09/10/2018 11:00AM – 2:00PM	**Meeting Location**	MetLife Building 200 Park Ave
Attendees	• Freddie Mac & Fannie Mae • APG • BAML • BlackRock Solutions • Bloomberg • BNP Paribas • BNY Mellon • Broadridge • Charles Schwab • Chase • Citi • Credit-Suisse • CSS • DoubleLine • DTCC • FHFA	• iHS Market • JP Morgan • Land Home Financial • Mesirow Financial • NY Fed • Pershing • PGIM • PIMCO • PNMac • Prudential • SIFMA • State Street • The ICE • Tradeweb • Wells Fargo • Morgan Stanley	

Scenario 1 & 2: TBA Trade/Roll

- For the OTR roll, would have to close out and pair it off.
- Margining requirements: Should this be a concern? What price will they be utilizing, where will the spread be?
    - If you roll from Freddie TBA to UMBS TBA, the CUSIP will change and it will be a new contract. There will be an additional margin call.
    - What price are we taking? Is it inclusive of the float comp?
        - The margin is calculated on strike price vs market price. But what would the strike price be? Would it be inclusive?
        - Should be clean. The same way it is today. Margin process should not change
- Question of what would happen if everyone takes in their rolls. There would be a lot of deliveries, and a lot of fails. Some discussion of whether TMPG could be asked to suspend fails charges. On the other hand, TMPG action could disincentivize filling the transaction immediately. Could also try and extend it slightly.
    - A key will be to make pricing for the Gold deliverable visible for rolls/exchanges
    - **SIFMA has talked about good delivery into a fail over conversion date. Does it have to be a Gold into a Gold fail? Or can it be UMBS into a Gold fail? Will need to clarify.** Delivering one CUSIP into a different CUSIP's trade to settle it.
    - There should be some guidance or best practice out from SIFMA about a Fannie fail being able to be filled with a UMBS or only a Fannie.
    - It sounds like it will be impossible to clear an 02R trade with an 01F. Would need to pair off if you want to enter into 01F
- FICC is central counterparty to TBA transactions. Cannot give up the other side of the transaction without the buyer's position. Could make this a rule through SIFMA. Need to be willing to give up yourself as the counterparty.

Scenario 3: Exchange Dealer-facilitated

- Critical that custodian banks and investors reconcile before exchanging to make sure that the bonds are not out on repo or on loan. This is necessary to ensure smooth exchange. Custodians and clients need to talk days before the expected exchange.
- There is a limit to how much a dealer will be willing to exchange on a given day, due to daylight overdraft concerns. Dealers pay cash to clients, but delivering free to Freddie. During the hour before the dealer gets the bonds back from Freddie, they are in daylight overdraft. Will need to structure the exchange flow so dealers do not exceed their credit limit. Should have coordination. Clients can't expect to call the day before and ask to do a $10m exchange.
- CS: Plans to keep investor portfolios anonymous to Traders via some type of firewall
    - Designate a point person most likely a trade operator (registered personnel)
    - Still deciding who this would be (most likely will differ company to company)
- If one custodian fails to deliver, don't want to jeopardize all the transactions that a dealer does.
- Will require lots of preparation between dealers/custodians/clients a few days prior to exchanges.
- Should standardize this process. A standard form for Dealer Direct is beneficial for communicating with clients.
    - This format could be the output from float comp calculator tool investors can use via Freddiemac.com
- If trading with Freddie, investors may need a service level agreement (SLA).
- In going through Broker Dealer, do most investors book exchange at market value?

- If the exchange generated a gain on the transaction, would it be non-taxable still?
    - Minimizing intra-day credit risk. Would rather make adjustments on a P&L. Should bring accountants into discussion.
- This issue is solved by going directly with Freddie, and using book price.
- Freddie can expect to see a large spike in deliveries at 8:30am when Fed opens
    - Time zone should not be a problem
- Clearing instructions for investors to custodian banks. Since using market price, will need a code to block taxability. Custodians' SWIFT message proposal was discussed; more to come on this following SIFMA meeting on 9/17.
- If there is a scenario where the dealer can't deliver to Freddie, would likely DK it back. Unclear. Would have to be a conversation between dealers and clients. The larger baskets would be a different conversation.
- If Freddie can't send back the 55-day, current plan is trust language.
    - Depending on the size of the fail, could be a financing issue for dealers. Dealers may need a formal trust receipt that can be used as collateral. May need to consult Dealers legal dept.

Scenario 4: Exchange Direct to Freddie path

- OMS – how will an exchange work? Connecting OMS to Tradeweb (TW).
    - Unsolicited flow and solicited
        - Unsolicited: log into TW, cut and paste your transactions into TW
        - Solicited: TW is working with each OMS to link in their systems with TW. Individual conversations with major OMS's
- Are there any requirements that investors will have to do for legal agreements for free of payment?
    - Have heard from custodians w/ 40-act requirements. They can't deliver free to dealers, but can to issuers. Investors should talk to their legal teams about this.

- For investors with their own OMS's, please reach out to Tradeweb.
- There will be flexibility in the pricing since its DVF.
- Trying to extend the exchange deadline past 11am.
- When will instructions be available to set up the account with Freddie?
    - They are available now and will be included in the playbook. Freddie will have 2 accounts – 1 for cash wire out, one for securities in (same ABA number for both)
- Investors would cancel internally and send a SWIFT to custodians. This is BAU.
- Need to take into consideration that investors are losing opportunities if Freddie fails to deliver back the 55d. Could be using those securities to lend and make money.
- Can have 45d and 55d securities in the same REMIC, but would have to be different groups. Supers can go into either Fannie or Freddie REMICs. But no commingling within the same REMIC group.
- Can still issue Freddie giants after go-live.
- Fannie will securitize 45d securities, since anything that is TBA can be securitized by either Enterprise. Would not mix 45d with 55d in the same group. Not impossible, but difficult for modelling.

Direct to Freddie Exchange Q&A

- State Street: Freddie has a transaction limit. How is that determined and communicated back when booking?
    - TW will be communicating with Freddie on the back end. They won't let you confirm a settlement date unless the date is available.
- PGIM: After factors are released?
    - Similar to Giants setup, you can't initiate the exchange until factors are released so that Freddie will know the float comp. The 5th business day of the month will be the first business day exchange will open each month.
- Can you schedule something in the future if there are capacity issues?
    - You must wait until the 5th business day of the following month.
- BNY: Can be expected to be notified via SWIFT message?
    - Yes
- JPM: If you fail during the end of the month, it will roll towards the next available settlement?
    - No. If it fails you must start over and rebook.
- Float comp tax treatment?
    - IRS said exchange of securities is not taxable, and were silent on float comp.

Exception scenarios

- PGIM: For the exchange of 100 CUSIPs across 100 sub accounts **-** If we had one thing that was out on repo, does that cause the other 99 transactions to be cancelled?
    - It would be on a line item by line item basis. If one failed, the other 99 would go through.
- BR: If DK is not possible, Freddie will hold the securities in trust for the investors
    - There will be trust language in the offering documents. Will not be a trust receipt for each transaction.
- PGIM: If Freddie Mac fails, will there be a priority from Freddie to take care of these first? Could cause the investor to fail on a TBA trade.
    - **If Freddie was at fault, it would make sense for them to make the investor whole as soon as possible. Freddie will take this back to the group to consider.**
- Barclays: For exception #1, whoever submitted the request will receive an email to alert them. Will there be a similar notification to the investor for exception #2?
    - **Will have to make sure this is documented as part of the process. Freddie will take note to ask about what the formal notification will be.**
- Mesirow: For rebooking, we would have to do it through Tradeweb?
    - Yes
- PGIM: For cancelling and rebooking for a few days after, this is not ideal for our workflow and would be something we'd have to internally look at. There will be an impact to client accounts in the meantime.
    - For a specified trade, how would the fail work?

        - I would not rebook my transactions through my system if it failed. You can't cancel a trade once it is in the system. I would go right into Tradeweb and re-execute with Freddie, and settle on that day. If it settled for a different month end that would be an issue because the cash would change. Would have to correct for this.
        - If the trade date or settlement date were to change, that wouldn't be an issue because you can change that. This shouldn't be an issue for compliance.
- Is there a way we can consider doing a modification functionality that would allow the transaction ID to be the same? So that we wouldn't run into compliance issues on the investor side? Rather than cancelling and submitting a new transaction.
    - **TW: Since every institution will have a different flow, take this away.**
- Since custodians will not get notified of the transaction until the day before or day of, if custodians are the ones loaning the position, this might be difficult for T+1.

Next steps

- Will schedule a phone call in late September, early October to discuss the commingled Supers scenario.
- Determine an agenda and format for the live exercise. Stakeholder engagement and preparation will be key, along with vendor screen mock-ups.