



MF SOFR Loans New Offering Training

August 19, 2020

Agenda

SOFR Loan Offering Overview

- SOFR Background
- LIBOR Transition Key Dates
- New Offering Index & Payment Structure
- Interest Rate Cap Index Optionality
- Interest Rate Cap Fallback Protocol & FAQ

Production & Underwriting

- Lender Production Process Changes
- Lender Underwriting Process Changes

Legal

- Commitment & Loan Doc Changes
- Term SOFR “Jump”

SOFR Background: Overview

- The publication of **LIBOR** is expected to cease at the end of 2021.
- The **Secured Overnight Financing Rate (“SOFR”)** has been chosen by the Alternative Reference Rates Committee (“ARRC”) as the best alternative index to USD LIBOR.
 - » SOFR is a broad measure of the cost of borrowing cash overnight collateralized by U.S. Treasury securities in the repurchase agreement (repo) market.
 - » SOFR is produced by the New York Fed in cooperation with the Office of Financial Research.
 - SOFR Average publication page: <https://apps.newyorkfed.org/markets/autorates/sofr-avg-ind>

“SOFR is a much more resilient rate than LIBOR because of how it is produced and the depth and liquidity of the markets that underlie it. As an overnight secured rate, SOFR better reflects the way financial institutions fund themselves today. The transaction volumes underlying SOFR regularly are around \$1 trillion in daily volumes. The volumes underlying SOFR are far larger than the transactions in any other U.S. money market. This makes it a transparent rate that is representative of the market across a broad range of market participants and protects it from attempts at manipulation.”

- <https://www.newyorkfed.org/arrc/sofr-transition>

SOFR Background: SOFR vs. LIBOR Comparison

- **Historically, 30-day Average SOFR has trailed 1-Month LIBOR**
 - » This is in part driven by SOFR being secured by Treasury securities, compared to LIBOR which is unsecured.

Date	30-day Average SOFR	1-Month LIBOR	Variance
8/12/2020	0.10%	0.16%	-0.06%
8/11/2020	0.10%	0.16%	-0.06%
8/10/2020	0.10%	0.17%	-0.07%
8/7/2020	0.10%	0.16%	-0.06%
8/6/2020	0.10%	0.16%	-0.05%
8/5/2020	0.10%	0.15%	-0.05%
8/4/2020	0.11%	0.15%	-0.04%
8/3/2020	0.11%	0.16%	-0.05%
7/31/2020	0.11%	0.15%	-0.05%
7/30/2020	0.11%	0.16%	-0.05%

LIBOR Transition Key Dates

**SOFR Loan
Quoting Begins**
September 1st, 2020
(Discontinue new LIBOR-
indexed quotes)

**LIBOR Full Underwriting
Package Cut-off**
November 9, 2020

LIBOR Purchase Cut-off
December 31, 2020

**LIBOR-indexed Loan
Application Cut-off**
September 30th, 2020

**LIBOR Final Delivery Package
Submission Cut-off**
December 11, 2020



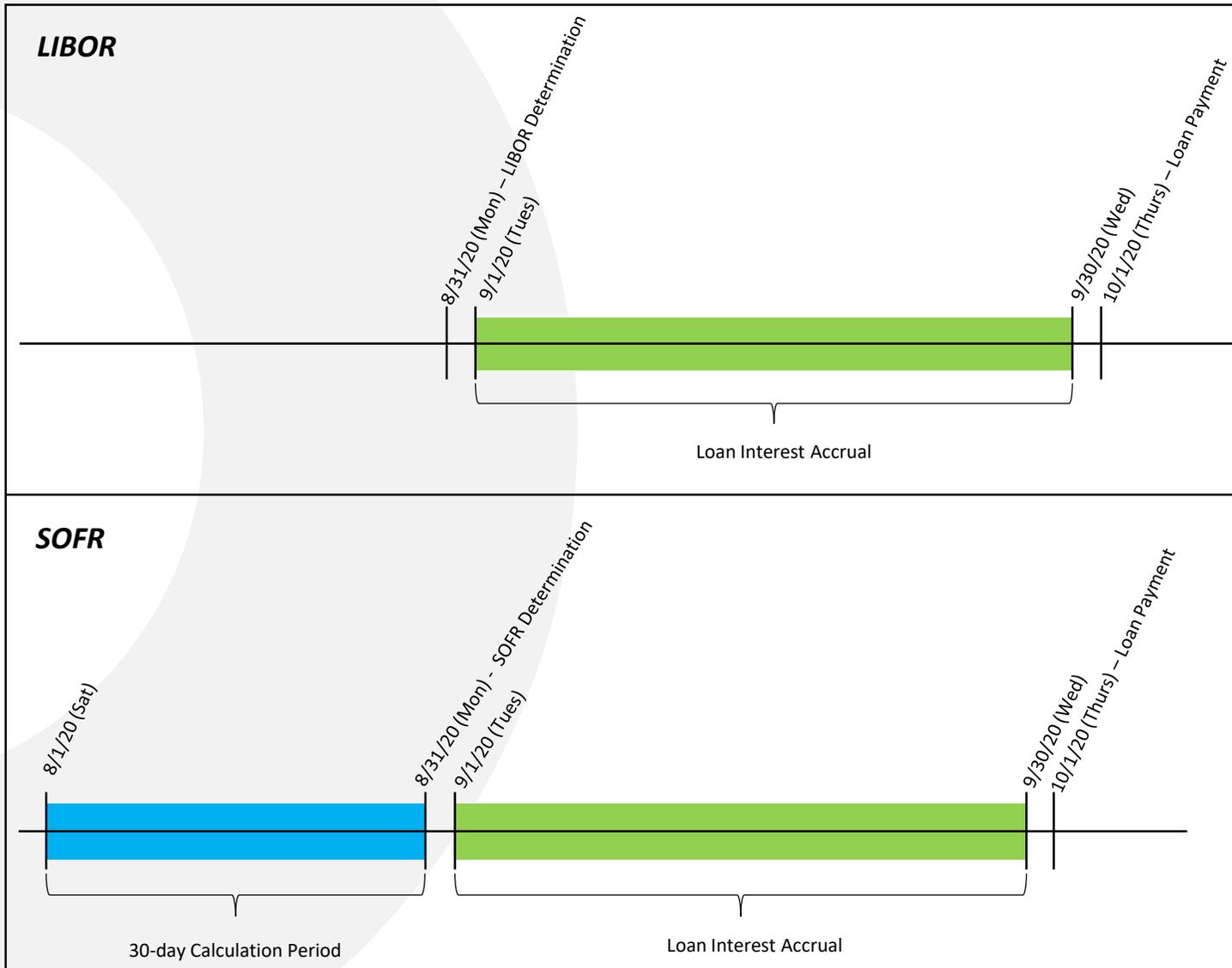
New Offering Index & Payment Structure

- **Index:** 30-day Average SOFR – “In Advance”
- **Publisher:** Federal Reserve Bank of New York
- **Interest Accrual Period:** Calendar Month (unchanged)
- **Interest Rate Reset Frequency**
 - » Conventional/Seniors/Targeted Affordable: Monthly (unchanged)
 - » SBL Hybrid: every 6 months during the floating-rate period (unchanged)
- **Rate Determination Date:** 1st day preceding the beginning of such Interest Accrual Period for which 30-day Average SOFR has been released by the FRBNY (*timing unchanged*)

SOFR- vs LIBOR-indexed Loan Offerings

	Metric	LIBOR	SOFR
Index	Index	London Inter-Bank Offered Rate (LIBOR)	Secured Overnight Financing Rate (SOFR)
	Index Rate Term	TAH & Conventional: 1-month Term Rate SBL Hybrid: 6-month Term Rate	FRBNY-published 30-day Average SOFR is known "In Advance" of Accrual Period
	Publisher	Intercontinental Exchange (ICE)	Federal Reserve Bank of New York
	Access Provider	Various sources that publish LIBOR as described in the Note.	FRBNY website
Loan Payments	Interest Accrual Period	Calendar Month	
	Interest Rate Reset Frequency	Conventional & Targeted Affordable: Monthly SBL Hybrid: Every 6 months during floating-rate period	
	Rate Determination Date	1st day preceding the beginning of such Interest Accrual Period for which LIBOR has been released by the IBA	1st day preceding the beginning of such Interest Accrual Period for which 30-day Average SOFR has been released by the FRBNY
	Loan Installment Due Date/Frequency	Monthly, first day of calendar month	

SOFR “In Advance” vs. Term Rate



- LIBOR is a term rate, meaning it is “forward-looking” and represents a rate that is fixed over a specified term, with a maturity date in the future.
 - » In contrast, 30-day Average SOFR represents a “backward-looking” calculated rate; calculated by taking the compounded average of daily SOFR over the preceding 30-days.

- SOFR “in advance” is defined as referencing an average of SOFR observed before the current interest accrual period begins.
 - » An “in arrears” structure would reference an average of SOFR over the current interest accrual period; however, it provides very little notice before payment is due.

Interest Rate Caps – Index Optionality

- **Interest Rate Cap Optionality:** Borrowers will be permitted to purchase either a LIBOR- or SOFR-indexed third-party cap for SOFR-indexed loans. **This optionality will not impact timing of rate cap determination; the borrower may make their final choice after rate lock.**
- If an initial LIBOR cap is purchased, the following requirements apply:
 - » Replacement Cap Reserve: Equal to 125% of the cost of a replacement SOFR cap.
 - » Accelerated Reserve Collection: Borrower will be required to make monthly replacement cap reserve deposits with the servicer sufficient to purchase a replacement SOFR-indexed third-party cap within 12 months of the loan closing.
 - » Lender Replacement Cap Purchase: Lender will have the right to apply amounts in the reserve toward the purchase of a replacement SOFR-indexed third-party cap if 30-day Average SOFR is above 1.25% and higher than 1-month LIBOR by more than 0.25% on the SOFR Determination Date for any Interest Adjustment Period.
 - » Reserve Shortfall Guarantor: A guarantor will guaranty payment of the difference between the reserve amount and the cost of the replacement cap, even if the guarantor requirement is otherwise waived.
 - » ISDA LIBOR Fallback Protocol: Borrower and the cap provider must agree to use Freddie Mac's updated form LIBOR cap documentation, including provisions governing the transition to SOFR.
- If an initial SOFR cap is chosen, no change to existing cap policy will apply.
- Freddie Mac expects that the option to purchase a LIBOR cap will be phased out over a period of months as the SOFR derivatives market matures and the availability of SOFR caps increases.

Interest Rate Caps - Fallback Protocol & FAQ

- **Frequently Asked Question #1: What happens to LIBOR caps when LIBOR cessation occurs?**
- Borrowers will not need to purchase a new cap until the existing cap expires, because the existing cap will remain in effect after LIBOR ceases to be published
 - On older LIBOR caps, the cap provider will pick a new index in consultation with Freddie Mac, and that index will govern the cap going forward.
 - On newer LIBOR caps that reference the ISDA LIBOR fallback protocol, the parties will be required to adhere to the protocol.
- **Frequently Asked Question #2: Where can I find information on SOFR cap pricing and availability?**

Freddie Mac does not provide interest rate caps for floating rate loans, so we are unable to provide cap pricing indications. For information related to SOFR cap pricing and availability, we recommend that Optigo Lenders reach out to their internal hedging group or preferred hedge advisory/consulting firm.

- **Frequently Asked Question #3: If a borrower elects to purchase a LIBOR cap for a SOFR loan, how do the replacement cap reserve requirements differ compared to a SOFR cap?**

Larger monthly replacement cap reserve deposits will be required, since the reserve must be fully funded within 12 months instead of immediately prior to termination of the existing cap (typically 3 years). The total reserve amount remains unchanged, and will be equal to 125% of the cost of a replacement SOFR cap with a 2 year term.

Lender Production Process Changes

Optigo Lenders will follow the process changes outlined below when submitting quote requests:

- **Narrative:** Lender will clearly note the requested loan index in the Narrative.
- **Loan Submission Template (LST):** Lender will select “30-day Avg SOFR” from the “Applicable Index Type” drop-down menu located on the LST “Input Sheet”.

1st Mortgage	
Applicable Index Type	30-day Avg SOFR
Index Rate (%)	0.100%

» *Data validation will be introduced in the near future to ensure U.S. Treasury is not chosen if the interest type is floating.*

- **Refinance Test:** Lender will select “SOFR” from the “Index Rate” drop-down menu in the Refinance Test.

Index Rate (for Float and Fixed to Float)	SOFR
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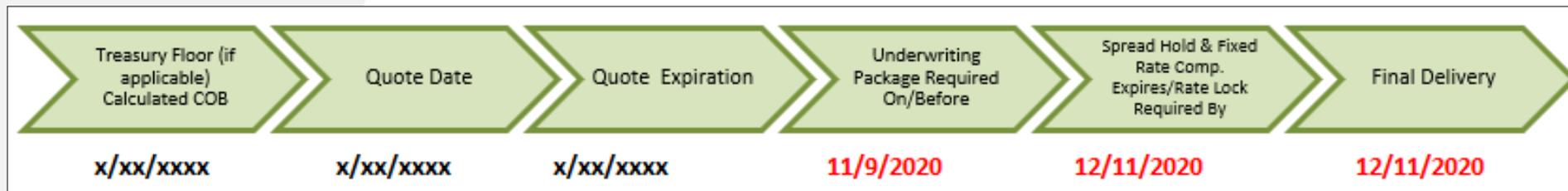
- **Digital Loan Submission:** Lender will select “30-day Avg SOFR” for the “Index Type”.

Interest Rate Spread	
Index Type	30-day Avg SOFR

Managing to LIBOR Cut-off Dates – Quote Forms

- To ensure compliance with the 12/31/2020 purchase deadline for LIBOR-indexed loans, the following cut-off dates apply:
 - » Full Underwriting Package for LIBOR-indexed loans must be delivered by **November 9, 2020**
 - » Final Delivery Package for LIBOR-indexed loans must be delivered by **December 11, 2020**

- To implement the new cut-off dates, the following quote form updates have been introduced:
 - » The LIBOR Transition stipulation has been updated.
 - » Auto-generated dates in the quote form have been updated so that the required dates for LIBOR-indexed loans will be the earlier of (i) the auto-calculated dates generated using existing logic and (ii) the new cut-off dates, shown in red text below:



Lender Underwriting Process Changes

Optigo Lenders will follow the process changes below when submitting a full underwriting package:

- **Narrative:** Lender will clearly note the requested loan index in the Mortgage Transaction Narrative Analysis.
- **Loan Submission Template (LST):** Lender will select “30-day Avg SOFR” from the “Applicable Index Type” drop-down menu located on the LST “Input Sheet”

	1st Mortgage
Applicable Index Type	30-day Avg SOFR
Index Rate (%)	0.100%

- **Refinance Test:** Lender will select “SOFR” from the “Index Rate” drop-down menu in the Refinance Test.

Index Rate (for Float and Fixed to Float)	SOFR
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Commitment Modifications

- **Exhibit A**

Index	CHOOSE ONE: 1-month LIBOR OR 30-day Average SOFR
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- **Exhibit C**

USE FOR A FLOATING RATE MORTGAGE (LIBOR)

1. Floating Rate Mortgage (LIBOR)
[Text]

OR

USE FOR A FLOATING RATE MORTGAGE (30-day Average SOFR)

1. Floating Rate Mortgage (30-day Average SOFR)
[Text]

- **Exhibit D**

- » Updates to Exhibit D provision for interest rate caps reflecting option to use LIBOR cap with SOFR loan

Loan Document Modifications

- **Updated Loan Documents for SOFR Loans have been posted on our website.**
 - » New floating rate note form for SOFR loans
 - » Updated rate cap rider to the loan agreement
 - » New guaranty rider for SOFR loans with LIBOR caps
 - » Updated Seller representations and warranties (solely to reflect floating rate can be based on SOFR or LIBOR)

Conventional Cash SOFR Loan Documents

Note – Floating Rate (30-Day Average SOFR) [\[DOC\]](#) (08-03-2020)

Note – Floating Rate – Value Add Transaction (30-Day Average SOFR) [\[DOC\]](#) (08-03-2020)

Rider to Guaranty – SOFR Mortgage with Initial LIBOR Cap [\[DOC\]](#) (08-03-2020)

Rate Cap Agreement Reserve Rider to Loan Agreement [\[DOC\]](#) (08-03-2020)

SBL SOFR Note

Note Hybrid ARM – SBL (30-Day Average SOFR) [\[DOC\]](#) (08-03-2020)

TEL SOFR Loan Documents

Project Note – Variable Rate – Forward – TEL (30-Day Average SOFR) [\[DOC\]](#) (08-03-2020)

Project Note – Variable Rate – Immediate Funding – TEL (30-Day Average SOFR) [\[DOC\]](#)
(08-03-2020)

Rate Cap Agreement Reserve Fund Rider to CCA – TEL [\[DOC\]](#) (08-03-2020)

Rider to Guaranty – SOFR Mortgage with Initial LIBOR Cap – TEL [\[DOC\]](#) (08-03-2020)

Term SOFR “Jump”

- **Although Term SOFR is not currently available, it is expected to become available at a later date, potentially in 2021.**
 - » SOFR note form provides that the index will automatically transition (“jump”) from 30-day Average SOFR to 1-month term SOFR when available. “Availability” will occur only when ARRC endorses Term SOFR and when Freddie Mac determines that transition to Term SOFR is technically, administratively, and operationally feasible.
- **SOFR Note - new definitions related to the Term SOFR “jump”**
 - » **“Term SOFR Transition”** means the transition of the SOFR Rate from Compounded SOFR to Term SOFR.
 - » **“Term SOFR Transition Date”** means the date on which the Term SOFR Transition occurs, which will be the date Lender determines in its sole discretion that the Term SOFR Transition will be operationally, administratively and technically feasible, provided that the Term SOFR Transition may occur only if such transition will not cause an Adverse Tax Event.
 - » SOFR Floating Rate Note, Section 3(q)(ii):
 - (ii) If a Term SOFR Transition occurs:
 - (A) Lender will provide Notice to Borrower of the Term SOFR Transition Date before the first Installment Due Date following the Term SOFR Transition Date.
 - (B) Beginning on the Term SOFR Transition Date, interest will accrue at the Floating Interest Rate calculated using Term SOFR as specified in such Notice, without the necessity of any amendment or other modification of this Note.

Q&A



- Detailed information can be found on our website at: <https://mf.freddiemac.com/libor/index.html>
- Feel free to contact your Producer and/or the MFLIBOR@freddiemac.com mailbox with your questions.