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ARRC Welcomes Fannie Mae and Freddie Mac's Decision to Use ARRC Recommended Fallback Language in New Adjustable Rate Mortgages

The Alternative Reference Rates Committee (ARRC) welcomed Fannie Mae and Freddie Mac's announcements that they will use the ARRC's recommended fallback language for new U.S. dollar (USD) denominated closed-end, residential adjustable-rate mortgages (ARMs). This fallback language is for market participants' voluntary use in new residential ARMs that reference USD LIBOR, and was developed to reduce the risk of serious market disruption in the event that LIBOR is no longer available. The ARRC's fallback language provides clear wording that would replace USD LIBOR with a spread-adjusted index based on the Secured Overnight Financing Rate (SOFR), the ARRC's recommended alternative to USD LIBOR.

In response to the ARRC's release of the ARMs fallback language, Fannie Mae and Freddie Mac announced that they plan to publish updates to their uniform ARM notes in the first quarter of 2020. These updates will incorporate the ARRC's recommended fallback language for all newly-originated ARMs. Fannie Mae and Freddie Mac have indicated that they plan to work closely with the ARRC, the Federal Housing Finance Agency, and other industry participants throughout the transition away from LIBOR.

"Fannie Mae and Freddie Mac's decision to use the ARRC's recommended fallback language for ARMs marks a consequential vote of confidence in the ARRC's work. This will go a long way in our efforts to safeguard mortgages so lenders, investors, and consumers are ready when LIBOR inevitably becomes unusable after 2021," said Tom Wipf, ARRC Chair and Vice Chairman of Institutional Securities at Morgan Stanley. "I commend these institutions for taking this step, and encourage others with LIBOR exposures to similarly support the transition to SOFR by adopting robust fallback language wherever possible."

The ARMs provisions mark the fifth set of recommended contractual fallback language that the ARRC has released. The ARRC expects to consult with a broad range of stakeholders on proposals for fallback language in other consumer products in the future.

About the ARRC

The ARRC is a group of private-market participants convened by the Federal Reserve Board and Federal Reserve Bank of New York in cooperation with the Consumer Financial Protection Bureau, the Federal Deposit Insurance Corporation, the Federal Housing Finance Agency, the Office of Financial Research, the Office of the Comptroller of the Currency, the Commodity Futures Trading Commission, the Securities and Exchange Commission and the U.S. Treasury Department. It was initially convened in 2014 to identify risk-free alternative reference rates for USD LIBOR, identify best practices for contract robustness, and create an implementation plan with metrics of success and a timeline to support an orderly adoption. The ARRC accomplished its first set of objectives and identified the Secured Overnight

Financing Rate as the rate that represents best practice for use in certain new USD derivatives and other financial contracts. It also published its Paced Transition Plan, with specific steps and timelines designed to encourage adoption of SOFR. The ARRC was reconstituted in 2018 with an expanded membership to help to ensure the successful implementation of the Paced Transition Plan, address the increased risk that LIBOR may not exist beyond 2021, and serve as a forum to coordinate and track planning across cash and derivatives products and market participants currently using USD LIBOR.

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