Third Annual

MORTGAGE REIT SUMMIT

APRIL 29, 2021

MAYER | BROWN

Market and Policy Overview

April 29, 2021

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Mayer Brown
Third Annual Mortgage REIT Summit

April 29, 2021

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Jennifer Fuller, Managing Director, KBW Investment Banking
Victor Sack, Managing Director, Head of KBW Capital Markets

KBW KEEFE, BRUYETTE & WOODS
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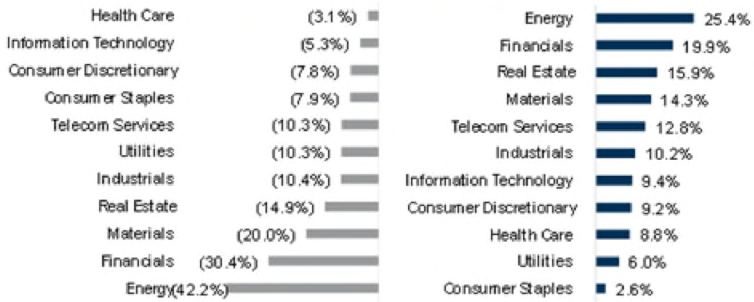
Agenda

Equity Market Overview

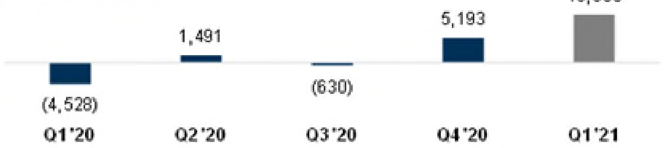
Major Indices Performance

S&P 500 Sector Performance



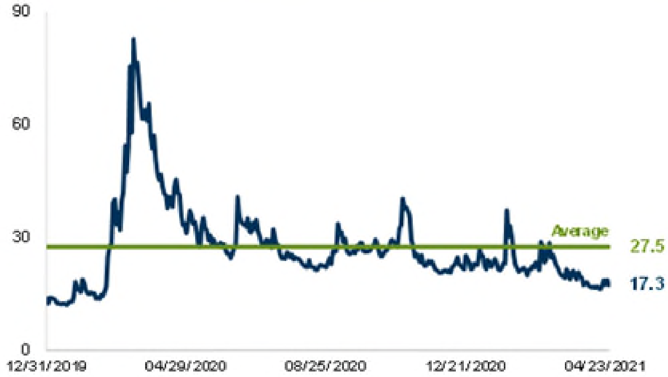
ETF Flows ($mm)

Financials ETFs



U.S. Listed ETFs[(1)]

CBOE Volatility Index (VIX)



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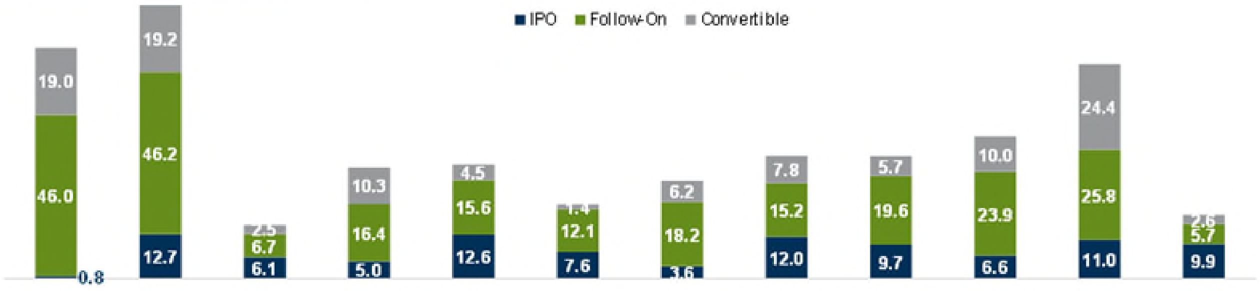
Source: KBW Research, Factset and Bloomberg as of 4/23/2021. Index Legend: BKX = KBW Bank Index, KRX = KBW Regional Bank Index, KSX = KBW Capital Markets Index, KIX = KBW Insurance Index and KFTX = KBW Financial Technology Index
(1) Passive listed

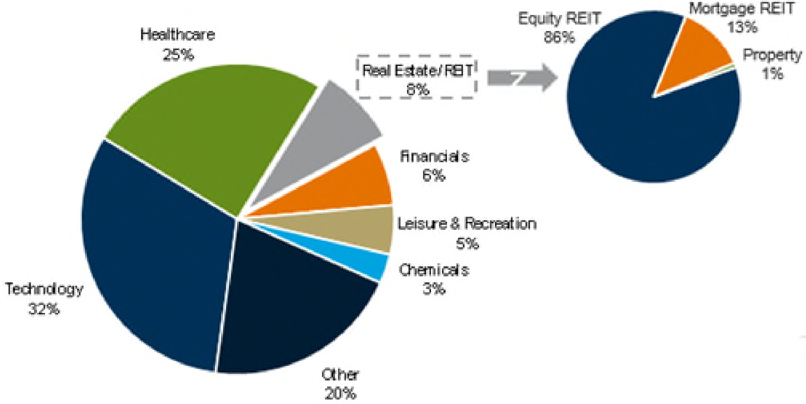
Equity Capital Markets Overview

LTM Equity and Equity-Linked Issuance ($bn)

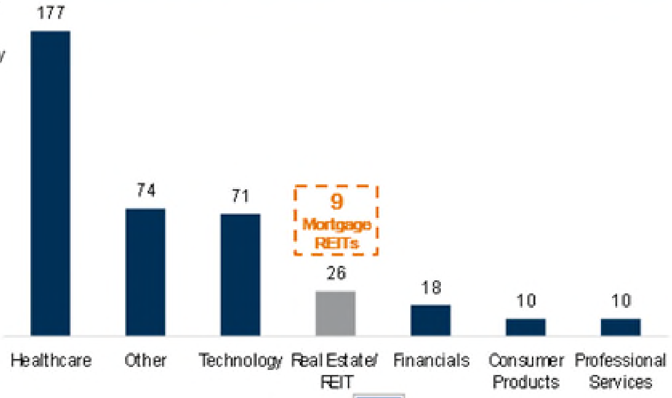


	May	June	July	August	September	October	November	December	January	February	March	April
# of IPOs	2	18	21	12	23	27	5	19	14	22	29	21
# of Follow-Ons	86	92	39	59	44	39	45	70	82	99	92	27
# of Convertibles	36	25	7	20	9	3	9	11	12	17	41	6

Common Stock YTD Sector Breakdown by Volume ($112bn)



Common Stock YTD Sector Breakdown by Number of Deals



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Source: Dealogic. Includes offerings from the U.S., P.R., Bermuda and Cayman Islands greater than $15mm. Excludes SPACs and best effort offerings

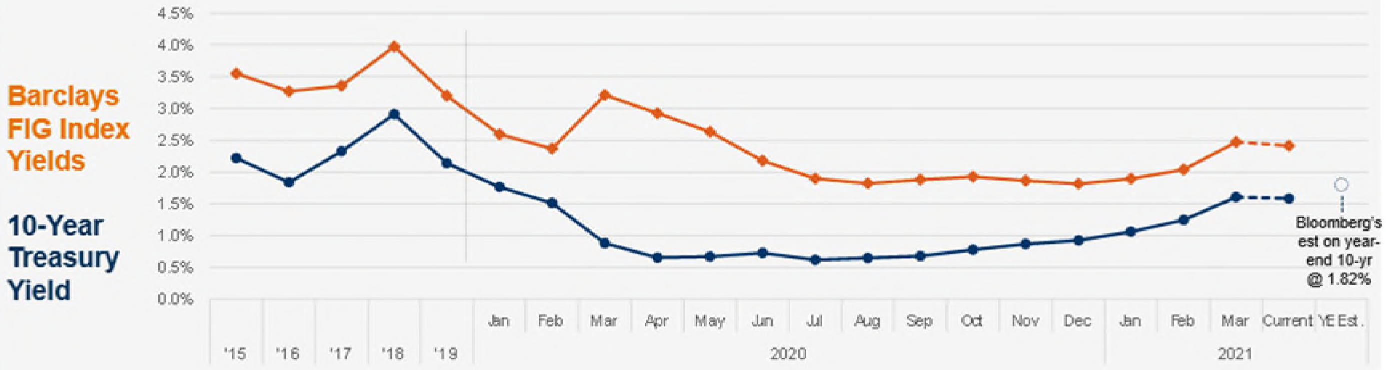
Market Backdrop for Debt Issuance Characterized By Still Historically Low Yields

Current Tailwinds

- ▲ **IG Coupons Near Record Lows** given persistent low yields and tight spreads
- ▲ Recent mREIT issuers achieved **Record Outcomes**
- ▲ **Deepened Buyer Base** with ample liquidity looking for yield security investments
- ▲ Reaffirmed government **Stimulus**, and Fed support

Potential Headwinds

- ▼ Possibility of **Higher Rates** sooner than expect
- ▼ Investor **Capacity Wanes** if more attractive alternatives emerge
- ▼ Credit or economic **Cycle Turns Negative**
- ▼ Systematic **Deterioration In Operating Or Credit Performance** of mortgage sector



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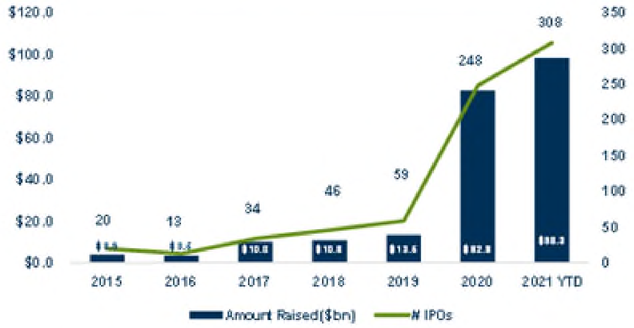
Source: Bloomberg. Note: Daily average 10-Year Treasury and Barclays Index yields for indicated period. Note: Bloomberg's consensus year end 10-year Treasury forecast as provided by Bloomberg's SWPM screen. Note: Barclays FIG index for senior & subdebt of all tenors as provided by Barclays index, and is used for trend analysis only and will not be indicative of secondary or new issue market levels

SPAC Issuance Statistics & Trends

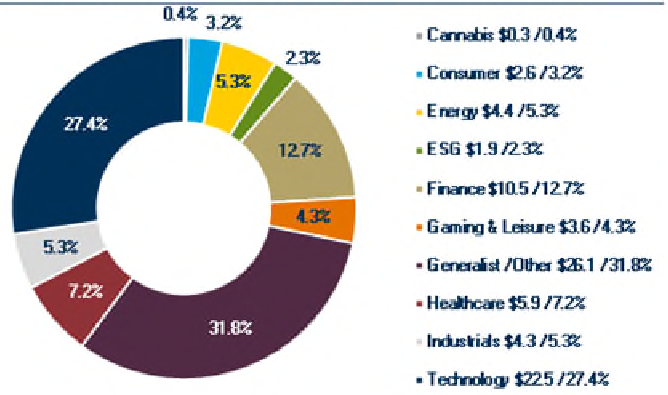
SPAC IPO Issuance Trends



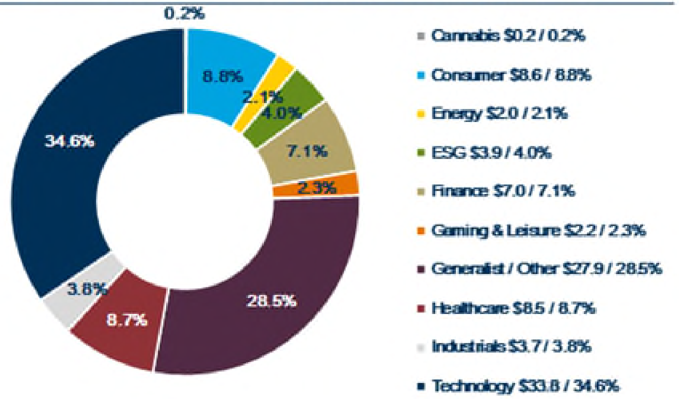
Select Announced / Closed SPAC Mergers

Company	Status	Industry
Offerpad	Pending	PropTech
doma	Pending	PropTech / Title Insurance
LATCH	Pending	PropTech
FINANCE of AMERICA	Closed	Mortgage Services
UWM	Closed	Mortgage
Opendoor	Closed	PropTech
BROADMARK REALTY CAPITAL	Closed	Mortgage REIT

2020 SPAC Proceeds Raised by Target Sector ($ in billions)



2021 SPAC Proceeds Raised by Target Sector ($ in billions)



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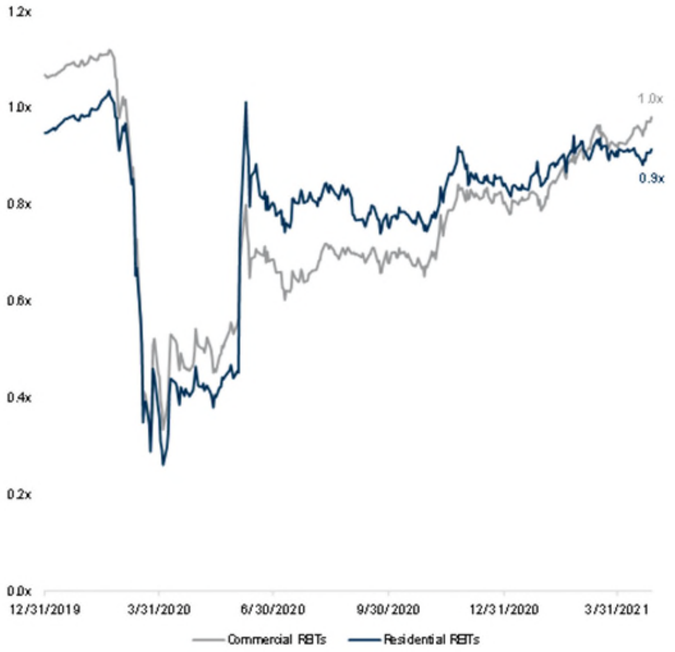
Source: Dealogic, Company Filings, Bloomberg as of 4/20/2021
Average current prices as of close on 4/20/2021

Mortgage REIT Post-COVID Recovery Has Lagged the Overall Market, but Has Returned to More "Normalized" Price/Book Valuations

Price Return[1] (2019-Current)

Commercial and Residential REIT Price / Book[1] (2019-Current)



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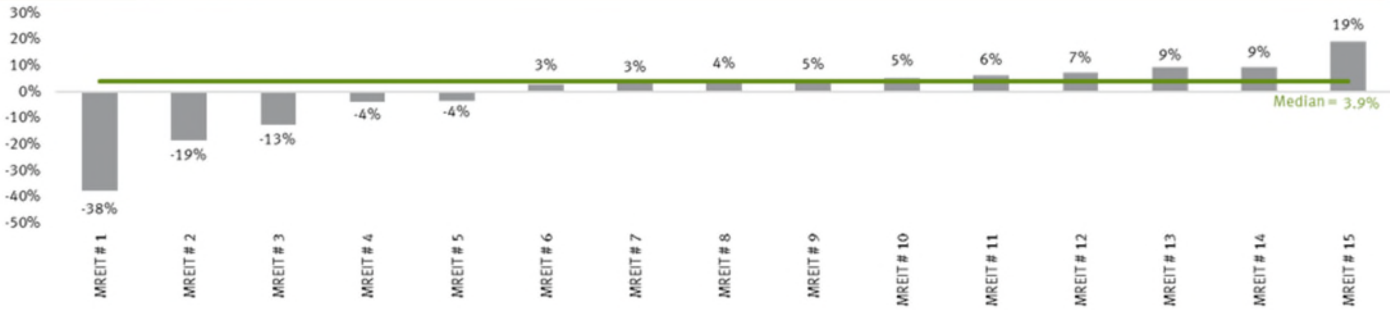
Source: S&P Global as of 4/27/21
(1) The "Commercial REITs" and "Residential REITs" series represent indices containing relevant public constituents weighted by market capitalization

Some MREITs Weathered COVID-Related Liquidity and Asset Quality Challenges Better Than Others

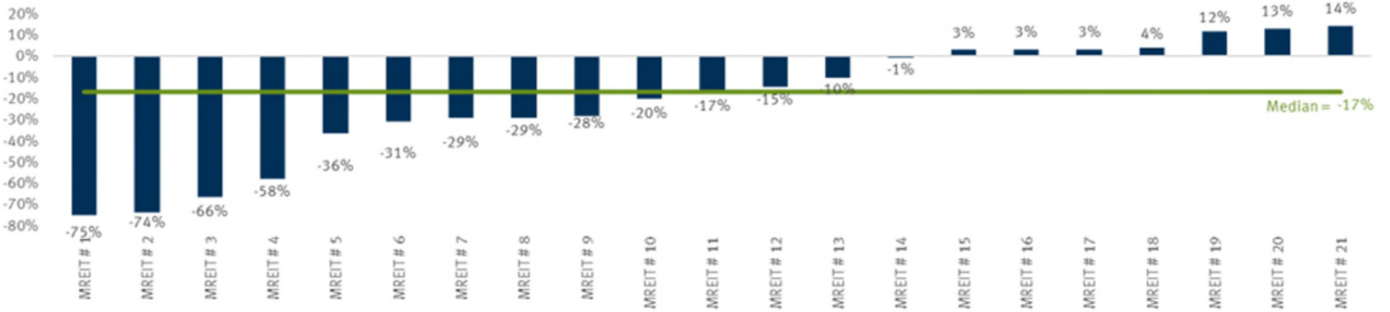
Commercial Mortgage REITs Fared Better Overall Than Residential Mortgage REITs

2020 Total Economic Return(1)

Commercial Mortgage REITs



Residential Mortgage REITs



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Source: S&P Global as of 4/27/21
(1) Economic return is calculated as ((ending TBV + annual declared dividends)/beginning TBV)–1

COVID Drove Significant Strategic Investments from Financial Investors

Announce Date	Issuer	Investor(s)	Deal Value ($mm)	Deal Terms/Summary
9/28/2020	Granite Point Mortgage Trust	PIMCO	$300	• $300 million five-year senior secured term loan with warrants to purchase common stock • Term loan has a cash-interest coupon of 8% • Six-year warrants to purchase up to 6.1 million shares of common stock at $6.47 per share

8/3/2020	Exantas	MassMutual
		Oaktree
			$375	• Done in connection with ACRES Capital's acquisition of Exantas' management agreement from C-III Capital Partners
				• $250 million seven-year senior secured financing facility
				  • 55% advance rate, 5.75% interest rate
				• $125 million senior unsecured notes
				  • Interest rate of 8.75% + payment in kind interest rate of 3.25% = annual interest rate of 12%

6/29/2020	MFA Financial, Inc.	Apollo Athene	$500	• Senior secured term loan • Apollo and Athene committed to purchasing the lesser of 4.9% or $50 million of MFA's common stock in the open market over a 12-month period • Warrant package
6/10/2020	Chimera Investment Corporation	Ares	$400	• Three-year secured loan commitment • 7% coupon • Price appreciation warrants
5/29/2020	TPG Real Estate Finance Trust	Starwood Capital Group	$325	• Strategic non-voting investment via preferred stock and detachable warrants to purchase TRTX's common stock
5/19/2020	New Residential Investment Corp	Canyon Partners, LLC	$600	• Senior secured three-year term loan facility • 11% interest rate • Price appreciation warrants
5/7/2020	Great Ajax	Flexpoint Ford Magnetar Capital Wellington Management	$30	• Private placement of $30 million preferred stock and warrants • 1,112,400 7.25% Series A preferred stock and 87,600 shares 5.00% Series B preferred stock at $25.00 per share • Two series of 5 year warrants to purchase 1.5 million shares at $10.00 per share; warrants include put
5/4/2020	Ladder Capital	Koch Goldman Sachs	$517	• $206.4 million in senior secured financing from Koch • $310.2 million matched-term non-mark to market and non-recourse private CLO with Goldman Sachs

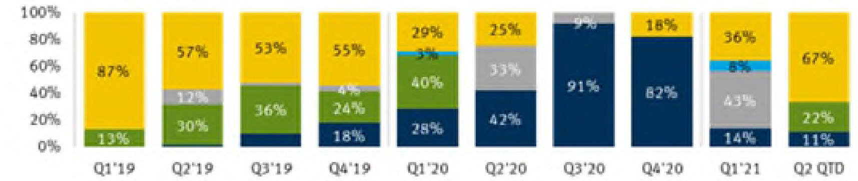
Source: CapitalIQ, press releases

Robust Pre-COVID Capital Markets Evolved to Non-Dilutive Capital Raising Through the Remainder of 2020

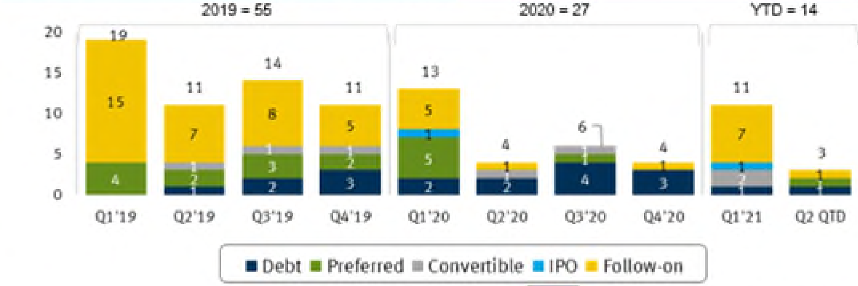
- Pre-COVID capital raising was dominated by follow-on capital raising and perpetual preferred capital offerings
- The immediate aftermath of COVID led to portfolio sales, private secured debt or structured capital raises, and other strategic processes
- As liquidity pressures eased, the mortgage REIT sector began to raise capital through underwritten offerings again, though the focus for the remainder of 2020 was rated unsecured debt, with larger issuers coming to market with larger average deal sizes than in 2019
- In 2021, capital markets are open again. Eight follow-on offerings have been completed this year to date, investor demand for rated debt is strong, and perpetual preferred capital offerings have begun again with a greater focus on institutional distribution

Capital Raised Through Underwritten Offerings By Type of Capital ($mm)

% Capital Raised Through Underwritten Offerings By Type of Capital



Underwritten Offerings By Type of Capital



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Source: Bloomberg and Dealogic for the period 1/1/2019-4/20/2021
Note: Represents aggregated transaction values for underwritten public debt, preferred, convertible, and equity offerings issued by select residential and commercial mortgage REITs in the United States

Commercial & Residential MREITs Have Distinct Valuation Drivers

Commercial Mortgage REITs

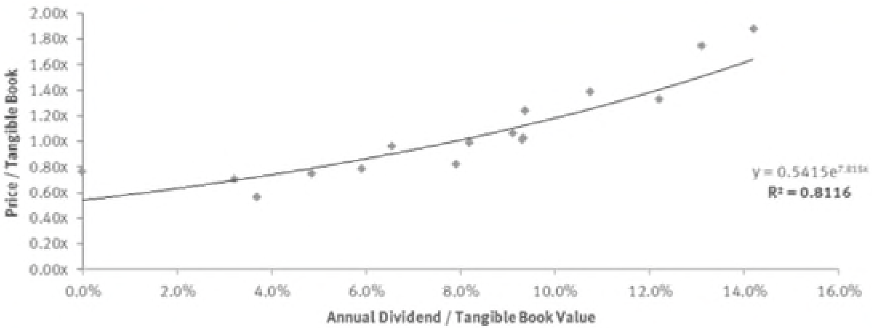
- **Current dividend** / TBV is **highly correlated** with commercial mREIT price / TBV valuations
- Market cap is not strongly correlated with price / TBV, though larger commercial mREITs have higher dividend / TBV ratios than smaller peers
  - Median dividend / TBV of 11.2% for >$2bn mkt cap, 8.2% for $1-2bn mkt cap, and 5.9% for <$1bn mkt cap

Residential Mortgage REITs

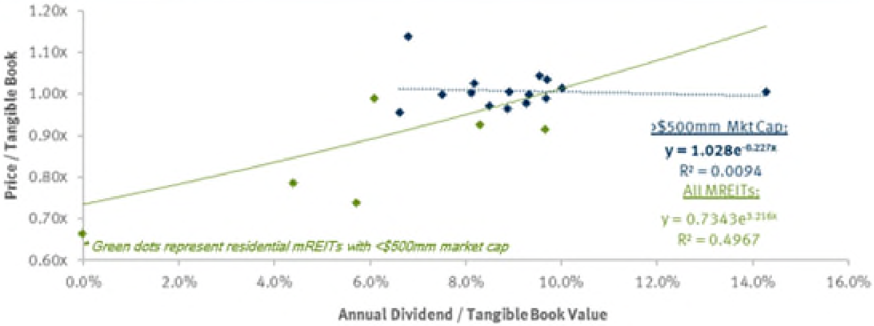
- Current dividend is not highly correlated with residential mREIT price / TBV
- Residential mREITs generally trade within a **tight band around TBV, with the exception of companies with <$500mm market cap**
  - 25th-75th percentile price / TBV for the 15 residential mREITs with >$500mm is 0.98-1.02x
  - The median price / TBV for the 6 residential mREITs with <$500mm market cap is 0.85x

Price / Tangible Book Value vs. Dividend / Tangible Book Value

Commercial Mortgage REITs



Residential Mortgage REITs



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Source: S&P Global as of 4/27/21

Disparate Drivers for 2020 and 2021 MREIT Sector M&A

Announce Date	Target	Buyer/Investor	Seller(s)	Deal Value to Equity Holders ($M)
4/26/2021	TREMONT MORTGAGE TRUST	RMR MORTGAGE TRUST	--	$54
4/22/2021	CHURCHILL REAL ESTATE	REDWOOD TRUST	--	N/D Minority Preferred Investment
4/14/2021	CALIBER HOME LOANS	NewRez	LONE STAR FUNDS	$1,675
3/25/2021	ANNALY *Commercial Real Estate Business (ACREG)*	SLATE	ANNALY	$2,330
12/7/2020	Anworth Mortgage	READY CAPITAL	--	$303

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Source: CapitalIQ; press releases

2020 Was An Unusually Active Year for External Manager Internalization and Sale Transactions

Announce Date	Company	Event Description
10/12/2020	GRANITE POINT MORTGAGE TRUST	• Internalized for cash consideration of $44.5 million
8/14/2020	TWO HARBORS Investment Corp.	• Internalized for no consideration • In April 2020, Two Harbors announced it would internalize for a cash termination payment of $144 million; in July 2020, Two Harbors terminated its management contract for "cause," which did not obligate it to pay a termination fee. The termination became effective in August 2020
8/3/2020	EXANTAS	• ACRES Capital Corp. acquired Exantas' management contract from C-III • ACRES' successful proposal to acquire the management contract was coupled with $375 million in new capital commitments from MassMutual and Oaktree, which were documented separately
2/12/2020	ANNALY	• Internalized for cash consideration of $1.00
1/6/2020	HUNT HUNT COMPANIES FINANCE TRUST	• Entered into new management agreement with a subsidiary of ORIX Corporation USA • No termination fee was due, but ORIX paid Hunt a negotiated payment • The new management contract was announced concurrently with the closing of ORIX's acquisition of Hunt Real Estate Capital, LLC, a subsidiary of Hunt Companies, Inc., which was previously announced in November 2019

Source: press releases

Biden Administration Financial Regulatory Policy

- **Key Priorities**:
  - Addressing Climate Risk.
  - Promoting an Inclusive Financial System.
  - Strong Regulatory Oversight and Involvement.

- **Key Personnel**:
  - Treasury Secretary, Janet Yellen
  - NEC Director, Brian Deese
  - SEC Chair, Gary Gensler

  Comptroller of Currency: Open
  Fed VC Supervision: Open Oct. 2021
  Fed Chair: Open Feb. 2021

ESG Policy & Financial Services

- The Securities and Exchange Commission (SEC) is likely to revise public company disclosures to incorporate environmental, social, and governance (ESG) information.
  - The SEC has already begun scrutinizing public filings to ensure they properly disclose climate-related risks.

- Federal banking regulators are examining how bank risk management frameworks should incorporate climate risk.

Infrastructure – American Jobs Plan

- $2.0 trillion dollar proposal.
  - $115 billion for bridges, highways, roads, and streets.
  - $85 billion for transit.
  - $174 billion for electric vehicle (EV) transition.
  - 100% high-speed broadband coverage.
  - $100 billion for public schools.
  - $25 billion childcare.
  - $400 billion for home health care infrastructure.
  - $180 R&D investment (AI, advanced energy tech, advanced biotech).
  - $100 billion for supply chain redeployment and critical industries.

Infrastructure – American Jobs Plan

- $213 billion to produce, preserve, and retrofit 2 million affordable and sustainable places to live.
- Eliminate exclusionary zoning laws.
- Build and rehabilitate 500,000 homes for low-income and middle-income homebuyers.
- $40 billion to improve public housing infrastructure.
- $27 billion Clean Energy and Sustainability Accelerator.
- $20 billion Neighborhood Homes Investment Act tax credits over 5 years.

Tax Policy (Infrastructure Part 2)

- Increase the corporate tax rate to 28%.
- Increase the minimum corporate tax to 21%, calculated on a country-by-country basis.
- Seek to establish a global minimum corporate tax.
- Strengthen enforcement of corporate tax law.
- Prevent corporations from writing off expenses related to off-shoring job and tax credit for on-shoring of jobs.
- Eliminate tax credits for fossil fuel industry.

American Families Plan

- $1.8 trillion.
- Universal Pre-K for 3- and 4-year olds.
- Free two years of community college.
- Increased Pell Grant funding.
- 12 weeks of paid FMLA.
- Funding to keep child care expenses below 7% of income for individuals earning less than 150% of state median income.
- Permanent Child and Dependent Care Tax Credit
- Permanent Earned Income Tax Credit for Childless Workers.
- Extend Child Tax Credit increase.

Tax Policy Part 2 (American Families Plan)

- Top individual rate to 39.6% from 37%.
- Tax capital gains at individual rate (39.6%) for individuals earning more than $1 million.
- Eliminate stepped up basis for estate tax for values above $1M/$2.5M.
- Eliminate 1031 exchanges for real estate gains above $500K.
- Enhanced IRS enforcement of corporations and high-income individuals.

Housing Policy

- **Housing Finance Reform**
  - The Supreme Court to decide Collins v. Mnuchin by June.
  - The Biden Administration has said very little about the future of the conservatorships of the GSEs.

- **HUD**
  - Fair Housing Act/Disparate Impact Rule.
  - Affirmatively Furthering Fair Housing Rule.

CFPB Updates

- Seila Law – US Supreme Court
  - Decides question of whether a single director, that may only be removed for cause, violates the President's authority to execute the laws of the land
- 5-4 decision on June 29, 2020 – CFPB single-director structure is unconstitutional
- 7-2 remedy – CFPB can continue to operate
  - Sever unconstitutional provision from Dodd-Frank Act
  - Director is now removable at will by the President
  - Acknowledges that Congress can pursue alternatives, like convert the CFPB to a multi-member agency

CFPB Updates

- President Biden’s Nomination for Director
  - Rohit Chopra
    - Commissioner at Federal Trade Commission
    - Former Student Loan Ombudsman at CFPB
  - Confirmation hearing held March 2, 2021 before the Senate Banking Committee
  - Decisions at FTC, past priorities at the CFPB, and statements at confirmation hearing provide clues about expected priorities and approach to enforcement

CFPB Updates

- Approach to Enforcement
  - Enforcement under former Director Kraninger
    - Fewer number of investigations compared to Cordray CFPB
    - Targets in public actions tended to be smaller companies
    - Less in consumer redress
  - Anticipated approach by Chopra
    - Creativity in the kinds of companies investigated and claims pursued
    - Focus on consumer redress
    - Target big and small companies
    - Willingness to litigate

CFPB Updates

- Priorities
  - Mortgage servicing and debt collection
    - COVID-related forbearance and other protections
    - Debt collection and UDAAP
  - Fair lending
    - Increased reliance on the disparate impact theory of liability
    - Use of technology and algorithms for decision making
  - Student lending
    - Protections for members of the military
    - For-profit institutions
    - Servicing and collection
  - Privacy – data protection
  - Credit score/credit bureau reform

THIRD ANNUAL

MORTGAGE REIT SUMMIT

Asset Finance and Tax Considerations

April 29, 2021

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Asset-Specific Financing Developments

Highlights and Market Developments

<u>Key trends driven by COVID and GSE Action</u>

- **Non-MTM facilities, trade-offs, and alternatives and the future**
  - Haircuts required
  - Forbearance loans
  - Liquidity demands
  - Pricing
  - Access to and role of term funding
- **EBO Finance**
  - Ginnie forbearance policies and partial claims
  - Inventories increase
  - Solutions include loans to servicers, acquisitions, leveraged acquisitions
  - What about term securitizations?
  - What happens when forbearance policies change?
- **Servicing Advances**
  - Original projections were daunting
  - FR and Fannie helped servicers avoid
  - Borrower performed surprisingly well with fiscal supports
  - But is a reckoning coming?

Highlights and Market Developments *(cont'd)*

Key trends tied to Demographics and Inflation

- **Single Family Rental**
  - Moratorium scare
  - Quick reversal and infusion of capital including raised for non-QM
  - The rise of build to rent
  - Strong securitization demand
  - Structural evolution
- **Fix and Flip**
  - Demographics similar to SFR
  - Legal structure
- **Developments in MSR Finance**
  - MSR performed well during COVID
  - Ownership of MSR/Excess MSR vs. Bonds
  - Strong recovery
  - Complexity with GSE acknowledgment agreements

How does the great leverage trade end?

a) No end in sight: Low rates and high growth validate MMT as “new paradigm”
b) Foreign sovereign rate increases drive Fed tapering
c) Inflation drives up rates
d) Recession/Tax Increases
e) Other dislocations

REITs and Renewable Energy Assets

Basic Principles

- General Principles
  - A REIT is taxed as a corporation.
  - However, unlike a regular corporation, a REIT may take a deduction against its gross income for dividends it pays to its shareholders.
  - Thus, REITs generally try to pay dividends in an amount that reduces taxable income to zero.
- Consequences of REIT Disqualification
  - If a REIT is disqualified, it will be taxed as a corporation for U.S. federal income tax purposes at rates up to 21%.
  - However, failure to meet any of the requirements discussed below should not be fatal. In general, such failures can be cured without losing REIT status.

Asset Tests

- A REIT must comply with two assets tests at the close of each quarter of its taxable year:
  - the 75% Asset Test; and
  - the 25% Asset Test
- The assets in the 25% "basket" are themselves subject to three limitations: (**i**) the 5% test, (**ii**) the 10% test, **and** (**iii**) the 25% test.
- There is a 30-day cure period after the quarter, if needed.
- For purposes of the Asset Tests, where a REIT invests in an entity treated as a partnership, the REIT is treated as owning a proportionate share of the entity's assets.

Asset Tests

- 75% Asset Test
  - At least 75% of the value of a REIT's total gross assets must consist of (among other things):
    - Interests in real property;
    - **Interests in mortgages/loans secured by real property.**
    - Shares in other REITs;
    - Cash and cash items (including receivables);
    - Government securities; and
    - Qualified temporary investments of new capital.

Income Tests

- There are **two** separate percentage tests relating to the sources of a REIT's gross income that must be satisfied for each taxable year:
    1. The 75% Gross Income Test
    2. The 95% Gross Income Test
- For purposes of the Income Tests, where a REIT invests in an entity treated as a partnership, the REIT is treated as earning a proportionate share of the entity's income.

75% Gross Income Test

On an annual basis, at least 75% of REIT's gross income must consist solely of:

- Rents from real property;
- **Interest on obligations by mortgages**;
- [...]

95% Gross Income Test

On an annual basis, at least 95% of REIT's gross income must be derived from:

- **Income qualifying for the 75% Gross Income Test**;
- Dividends;
- **Interest**; and
- [...]

In other words, a REIT may receive up to 5% of its annual gross income from sources that do not qualify for either 75% or the 95% Gross Income Tests.

Asset REIT Investment in Loans Secured by Renewable Assets

- In order for a loan to qualify under the 75% Asset Test it must be "secured by an interest in real property" under the Code
- Real property is defined under federal income tax law not local law
- IRS regulations finalized in 2016 try to define when an asset is a real estate asset

Real Property Definition

- The term real property means land and improvements to land. Reg. section 1.856-10(b)
- The term improvements to land means inherently permanent structures and their structural components. -10(d)(1).
- A distinct asset that serves an active function, such as an item of machinery or equipment, is not a building or other inherently permanent structure.-10(d)(2)(i).
- Other inherently permanent structures serve a passive function, such as to contain, support, shelter, cover, protect, or provide a conduit or a route, and do not serve an active function, such as to manufacture, create, produce, convert, or transport.

Loans Secured by Structural Components Only

- A mortgage secured by a structural component is a real estate asset only if the mortgage is also secured by a real property interest in the inherently permanent structure served by the structural component… -10(d)(3).

Case #1

- A REIT makes a loan adequately secured by the land underlying a wind farm or solar facility
- There is no security interest in the wind turbines or the solar panels
- This should be a loan secured by an interest in real property

Case #2

- A REIT holds a mortgage on an office building
- The mortgage is secured by the land, the building and "solar assets"
- The "solar assets" consist of a solar array on the building's roof
- The solar array's electricity is used only to power the building
- This should qualify as a mortgage on real property for REIT purposes
- What if the REIT makes a loan only secured by the solar assets?
- What if the solar array produces excess power that is sold to the local electricity grid?

Case #3

- A REIT makes a loan secured by an entire Solar Energy Facility
- Components
  - Land
  - Mounts for the Solar Cells
  - All the Solar Cells
  - Exit Wire (carries power from cells)

Analysis Under the Regulations

- REIT H owns a solar energy site, among the components of which are land, photovoltaic modules (PV Modules), mounts and an exit wire. ...The mounts support the PV Modules. The racks are affixed to the land through foundations made from poured concrete. The mounts will remain in place when the tenant vacates the solar energy site. The PV Modules convert solar photons into electric energy (electricity). -10(f), Ex 8.
- The PV Modules serve the active function of converting photons to electricity.

A Portion of the Solar Facility is Real Property

- **Land**: The land is real property as defined in paragraph (c) of this section.
- **Mounts for the PV Modules**: The factors described in this paragraph … all support the conclusion that the mounts are inherently permanent structures within the meaning of paragraph (d)(2) of this section and, therefore, are real property.

The Solar Panels are Not Real Property

- The PV Modules convert solar photons into electricity that is transmitted through an electrical power grid for sale to third parties. **The conversion is an active function.** Thus, the PV Modules are items of machinery or equipment and therefore are not inherently permanent structures within the meaning of paragraph (d)(2) of this section and, so, are not real property. The PV Modules do not serve the mounts in their passive function of providing support; instead, the PV Modules produce electricity for sale to third parties, which is income other than consideration for the use or occupancy of space. **Thus, the PV Modules are not structural components of REIT H's mounts within the meaning of paragraph (d)(3) of this section and, therefore, are not real property.**

Compare Example 9 (Solar Panels that Power a Building)

- REIT I owns a solar energy site similar to that described in Example 8, except that REIT I's solar energy site assets (Solar Energy Site Assets) are mounted on land adjacent to an office building owned by REIT I.
- Although the tenant occasionally transfers excess electricity produced by the Solar Energy Site Assets to a utility company, the Solar Energy Site Assets are designed and intended to produce electricity only to serve the office building
- The factors described in this paragraph …all support the conclusion that the Solar Energy Site Assets are a structural component of REIT I's office building within the meaning of paragraph (d)(3) of this section and, therefore, are real property.

Results

- **Case #1**: Yes
- **Case #2**: Probably Yes
- **Case #3**: Probably No

THIRD ANNUAL

MORTGAGE REIT SUMMIT

Securities Developments and What's on the Horizon…

April 29, 2021

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Agenda

- Changes to MD&A and Other Disclosure Requirements
  - Modernization of Regulation S-K Items 101, 103 and 105
  - Amendments to MD&A
- Changes to Requirements for Acquired Businesses and Pro Forma Financial Statements
  - Amendments to Financial Disclosures about Acquired Businesses
  - Financial Disclosures About Guarantors and Issuers of Guaranteed Securities
- Human Capital Disclosures—What did companies actually disclose?
- Mortgage REITs and the Demand for Additional ESG Disclosure
- What Mortgage REITs Should Expect from the SEC Under Gensler's Leadership

Amendments to S-K Item 105 Risk Factor Disclosure

As part of the SEC modernization amendments to Regulation S-K adopted this past August, the amendments to Item 105 regarding risk factors were adopted:

- Requirement of a summary of not more than two pages in the "forepart" of the annual report if the discussion exceeds 15 pages;
- Change to the disclosure standard from "most significant" risks to "material" risks;
- Required organization of risks under relevant headings; and
- Requirement that generic risks (not specifically relevant to a company's investors) be placed at the end of the discussion under a heading entitled "General Risk Factors".

Business Description (Item 101(c))

In addition to the amendment to the general approach to the business disclosure requirements of S-K, the requirements for this Item have several notable specific amendments.

- New Human Capital Disclosure;
  - The company's human capital resources; and
  - Human capital resources that the company focuses on in managing its business.
- Government Regulations – Not just environmental anymore; and
- Other Prescriptive Disclosure Items – Any item that is material to investment and voting decisions, rather than current quantitative thresholds.

Legal Proceedings (Item 103)

The amendments to legal proceedings disclosure also raise the threshold for disclosure of environmental proceedings to which a governmental authority is a party from $100,000 to $300,000, with the flexibility for the company to select a different threshold so long as such threshold:

- Is reasonably designed to disclose any material proceeding;
- Does not exceed the lesser of (**i**) $1 million **or** (**ii**) 1% of the current assets of the company and its subsidiaries on a consolidated basis; and
- Is disclosed, together with any changes, in <u>**each**</u> annual <u>**and**</u> quarterly report.

SEC Transitional FAQs re Items 101 and 103

- On November 5, 2020, the Staff issued FAQs with respect to the amendments to modernize Regulation S-K with the following points of clarification:
  - For prospectus supplements filed after November 9 for registration statements effective prior to November 9, issuers don’t need to comply with new Items 101 and 103 or amend the 10-K currently incorporated by reference in the registration statement to comply with the amended Items 101 and 103.
  - In addition, although 401(a) requires a prospectus supplement conform to applicable rules on the initial file date of the supplement and Item 3 of Form S-3 expressly requires Item 105 disclosure, the Staff has stated that it will not object if the prospectus supplement complies with previous Item 105 until the next update to the registration statement for Section 10(a)(3) purposes.
- The amendments don’t require 10-K disclosure of new 101 business developments for more than the fiscal year covered by the current 10-K.

Amendments to MD&A of Financial Condition and Results of Operations

Amendment to MD&A and Related Disclosures

- On November 19, 2020, the SEC
  - Amended Item 303 of Regulation S-K (Management's Discussion and Analysis of Financial Condition and Results of Operations or MD&A) and
  - Revised or eliminated several other requirements of Regulation S-K
- The SEC adopted these changes to
  - To eliminate duplicative disclosures and
  - Modernize and enhance MD&A disclosures for the benefit of investors, while simplifying compliance efforts for registrants.

Effective and Compliance Dates

- Effective Date
  - **February 10, 2021**
- Mandatory Compliance Date
  - Beginning with first fiscal year ending on or after August 9, 2021
  - Companies must apply the amended rules in a registration statement and prospectus that on its ***initial filing date*** is required to contain financial statements for a period on or after the mandatory compliance date
- Voluntary Early Compliance
  - Allowed at any time after the effective date as long as disclosure is responsive to an amended item in its entirety

New paragraph 303 (a) – Objective

- New paragraph (a) to Item 303 clarifies the objective of MD&A by incorporating much of current Instructions 1, 2 and 3
  - Emphasizes the objective of MD&A for both full fiscal years and interim periods.
  - Disclosure generally is expected to better allow an investor to view the company from management's perspective.
  - Current Items 303(a) and (b) have been recaptioned as Items 303(b) and (c), respectively

Capital Resources (reflected in new Item 303(b)(1) and Item 303(b)(1)(ii))

- Disclosure of material cash requirements, including
  - Commitments for capital expenditures,
  - Anticipated source of funds needed to satisfy these cash requirements, and
  - General purpose of the cash requirements
- The objective is to account for capital expenditures that are not necessarily capital investments, such as
  - Human capital or intellectual property
- Product lines may need to be discussed where necessary to understand a company's business

Results of Operations (reflected in Item 303(b)(2)(ii)

- Companies must disclose known events that are reasonably likely to cause a material change in the relationship between costs and revenues, such as known or reasonably likely future increases in
    - Costs of labor or materials
    - Price increases
    - Inventory adjustments
- Companies must disclose the reasons underlying material changes in net sales or revenues
- Elimination of specific disclosure with respect to the impact of inflation and changing prices
    - Companies will still be required to discuss these matters if they are part of a known trend or uncertainty that has had, or is reasonably likely to have, a material impact on net sales or revenue
    - This will allow companies to focus on material disclosure that is tailored to their business, facts and circumstances

Off Balance Sheet Arrangements

- Current requirement eliminated
- Companies should consider off-balance sheet arrangements within the broader context of their MD&A
- Instruction 8 requires companies to discuss commitments and obligations arising from arrangements with unconsolidated entities or persons that have, or are reasonably likely to have, a material current or future effect on their:
  - Financial condition,
  - Changes in financial condition,
  - Revenues or expenses,
  - Results of operations,
  - Liquidity,
  - Cash requirements, or
  - Capital resources.

Tabular Disclosure of Contractual Obligations

- Eliminated this disclosure requirement currently in paragraph (a)(5)
- Amended Item 303(b) requires disclosure of material cash requirements from known contractual and other obligations as part of a liquidity and capital resources discussion
- The adopting release explains that the "amendments are intended to focus only on material disclosures and specifically, disclosure of those periods where the cash requirements are reasonably likely effect of these cash requirements on liquidity and capital resources is material."

Line Item Changes and Critical Accounting Estimates

- If line item materially changes, disclose the underlying reasons for these material changes in quantitative and qualitative terms
- Disclosure of critical accounting estimates explicitly required
  - Qualitative and quantitative information necessary to understand
    - The estimation uncertainty
    - Impact the critical accounting estimate has or is reasonably likely to have on financial condition or results of operations

Quarterly Periods (reflected in new Item 303(c)

- Companies can compare their most recently completed quarter to either
  - The corresponding quarter of the prior year, or
  - The immediately preceding quarter
- If comparison from the prior interim period comparison changes
  - Explain the reason for the change, and
  - Present both comparisons in the filing where the change is announced

Supplementary Financial Information and Selected Financial Data

- S-K Item 301 (Selected Financial Data) eliminated
- S-K Item 302 (Supplementary Financial Information) amended
  - Replaced requirement to provide two years of tabular selected quarterly financial data with a principles-based requirement requiring disclosure only when there are one or more specified retrospective changes that that, individually or in the aggregate, are material
  - Disclosure could involve a single quarter in which the material retrospective change applies, or it may flow through to subsequent quarters during the relevant look-back period

Amendments to Financial Disclosures about Acquired Businesses

Amendments to financial disclosures about acquired businesses

- On May 21, 2020, the SEC amended financial disclosure rules with respect to business acquisitions required by Rule 3-05 and Article 11 of Regulation S-X
- Aims to improve financial information available to investors about acquired or disposed businesses, facilitate more timely access by issuers to capital, reduce complexity and costs to prepare disclosures
- Effective Date: January 1, 2021
- Amendments revise Rules 3-05 (financial statements of acquired businesses), 3-14 (real estate operations), Article 11 (pro forma financial information), other related rules of Reg S-X

Background

- Rule 3-05 requires audited annual and unaudited interim financial statements to be provided if a significant acquisition has occurred or is probable, and the business acquired or to be acquired would be considered a significant subsidiary under Rule 1-02(w) of Reg. S-X, substituting 20% for the 10% trigger threshold in that rule
- Rule 11-01 of Reg. S-X requires unaudited annual and interim pro forma financial statements if a significant acquisition has occurred or is probable, looking to the same tests in Rule 1-02(w) for determining whether a business acquisition is significant
- Rule 1-02(w) contains three tests for determining whether a subsidiary or business combination is significant – investment test, asset test, income test. Under Old Rule:

Investment Test	Asset Test	Income Test
$\frac{\text{Purchase Price}}{\text{Buyer's Total Assets}}$	$\frac{\text{Target's Total Assets}}{\text{Buyer's Total Assets}}$	$\frac{\text{Target's Pre-Tax Income}}{\text{Buyer's Pre-Tax Income}}$

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Revised Investment Test

- Changes to the Old Rule:
  - Replaces denominator with aggregate worldwide market value of voting and non-voting common equity for total assets when the registrant has a market value for its voting and non-voting common equity
    - If there is no aggregate worldwide market value, then use the denominator in Old Rule
  - Requires inclusion of fair value of any contingent consideration in calculating investments in or advances to the tested subsidiary, unless likelihood of payment is remote

Investment Test (Old Rule)	**Investment Test (New Rule)**
$\frac{\text{Purchase Price}}{\text{Buyer's Total Assets}}$	$\frac{\text{Purchase Price}}{\text{Buyer's Aggregate Worldwide Market Value of Common Equity}}$

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Revised Income Test

- Changes to the Old Rule:
  - Adds a revenue test that must be satisfied in addition to the income test
  - Both the revenue test and the income test thresholds must be exceeded for the income test to be met
  - The revenue test does not apply if either the registrant or the tested subsidiary did not have material revenue in either of the previous two years
  - Loss years reflected at absolute value, rather than a zero

Income Test (Old Rule)	**Income Test (New Rule)**
$\frac{\text{Target's Pre-Tax Income}}{\text{Buyer's Pre-Tax Income}}$	The ***lower*** of: $\frac{\text{Target's Pre-Tax Income}}{\text{Buyer's Pre-Tax Income}}$ **and** $\frac{\text{Target's Revenue}}{\text{Buyer's Revenue}}$

Periods for Rule 3-05 Financial Statements

PERIODS TO BE PRESENTED	
Significance Level	**Required Financial Periods**
If all significance tests less than 20%	No Rule 3-05 Financial Statements required
If any significance test greater than 20% but none exceed 40%	One year of audited financial statements; unaudited financial statements for most recent interim period (but no corresponding prior year interim period)
If any significance test greater than 40%	Two years of audited financial statements and unaudited financial statements for most recent, and corresponding prior year, interim period

Pro Forma Information to Measure Significance

- Filed pro forma financial information that only depicts significant business acquisitions and dispositions consummated after the latest fiscal year-end may be used to measure significance, if:
  - Rule 3-05 Financial Statements (or, for real estate operations, Rule 3-14 Financial Statements) have been filed for any such acquired business, and
  - Pro forma financial information required by Article 11 for any such acquired or disposed business has been filed
- Pro forma financial information used to measure significance may only give effect to the subsequently acquired or disposed business
- Pro forma information used to measure significance may not give effect to Autonomous Entity Adjustments, Management's Adjustments, or other transactions, such as the use of proceeds from an offering
- Once a registrant uses pro formas to measure significance, it must continue to use pro formas to measure significance until the next annual report on Form 10-K or Form 20-F

Individually Insignificant Acquisitions

- The Amended Rules clarify that "individually insignificant businesses" include:
  - Any acquisition consummated after the registrant's audited balance sheet date whose significance does not exceed 20%,
  - Any probable acquisition whose significance does not exceed 50%, and
  - Any consummated acquisition whose significance exceeds 20%, but does not exceed 50%, for which financial statements are not yet required because of the 75-day filing period
- Pre-acquisition historical financial statements only for those businesses whose individual significance exceeds 20%
- Pro forma financial information depicting the aggregate effects of all "individually insignificant businesses" in all material respects
- Exception permitting pro forma financial information not to be provided does not apply where the aggregate impact is significant

Pro Forma Financial Information Adjustments

- Amendments to Article 11 of Reg S-X modify criteria for pro forma adjustments and provide three new categories of permitted adjustments
- Adjustment criteria for pro forma financial information requirements broken out into three categories:
  - "Transaction Accounting Adjustments" which reflect only the application of required accounting to the transaction
  - "Autonomous Entity Adjustments" which reflect the operations and financial position of the registrant as an autonomous entity if it was previously part of another entity, and
  - Optional "Management's Adjustments" depicting synergies and dis-synergies of acquisitions and dispositions for which pro forma effect is being given if, in management's opinion, such adjustments enhance understanding of the pro forma effects of the transaction
    - As a condition for presenting Management's Adjustments, certain conditions related to the basis and form of presentation must be met

Basis for Management's Adjustments

- Management's Adjustments must satisfy the following conditions:
  - There must be a reasonable basis for each such adjustment
  - The adjustments are limited to the effect of such synergies and dis-synergies on the historical financial statements that form the basis for the pro forma statement of comprehensive income as if the synergies and dis-synergies existed as of the beginning of the fiscal year presented
    - If such adjustments reduce expenses, the reduction cannot exceed the amount of the related expense historically incurred during the pro forma period presented
  - The pro forma financial information must reflects all Management's Adjustments that are, in the opinion of management, necessary to a fair statement of the pro forma financial information presented
    - A statement to that effect must be disclosed
    - When synergies are presented, any related dis-synergies shall also be presented

Practical Considerations

Financial disclosures re acquired businesses

The Amended Rules:

- Ease burdens and costs involved in preparation of financial statements
  - Maximum of two (instead of three) years of audited annual financial statements
  - Corresponding prior year interim period required only at more than 40% significance
  - Increased significance threshold for dispositions from 10% to 20%
  - Permit abbreviated financials for acquisitions of a component of an entity
  - Allow omission of target financials once business included in registrant's post-acquisition financial statements for nine months or one year
  - Eliminated required three years of audited annual financials if real estate operation acquired from a related party
  - Allow presentation of Rule 3-05 Financial Statements of Foreign Businesses or Foreign Private Issuers in accordance with IFRS-IASB without reconciliation to U.S. GAAP

Practical Considerations

Financial disclosures re acquired businesses *(cont'd)*

The Amended Rules:

- Assist registrants to make more meaningful significance determinations
  - Using aggregate worldwide market value for investment test corrects fair value vs. book value mismatch in investment test under Old Rule
  - Adding revenue component to income test prevents anomalous results, especially for registrants with net loss or low net income
- Introduce new obligations and challenges for registrants
  - Management's Adjustments, while optional, require management to present reasonably estimable synergies and dis-synergies of the acquisition and to have a reasonable basis for each adjustment
    - Requires management to state that pro formas reflect all Management's Adjustments that are, in their opinion, necessary to a fair statement of pro formas
  - Registrants will need to get used to presenting pro formas under Amended Rules, including presentation of "Transaction Accounting Adjustments," "Autonomous Entity Adjustments," and related explanatory notes

Practical Considerations

Financial disclosures re acquired businesses *(cont'd)*

A few practical reminders and tips for reporting companies:

- Assess how Amended Rules impact your disclosures
  - Public companies that engage, or are considering engaging, in acquisitions or dispositions should involve their accounting departments and counsel
- Pay attention to the SEC's reminder that financial disclosures must be complete and not misleading:
  - *"In adopting these changes, we note that regardless of the number of years presented, if trends depicted in Rule 3-05 Financial Statements are not indicative or are otherwise incomplete, 17 CFR 210.4-01(a) ('Rule 4-01(a)') requires that a registrant provide 'such further material information as is necessary to make the required statements, in light of the circumstances under which they are made, not misleading.'"*
- Remember that Rule 3-13 waiver requests are available and can be utilized by registrants

Amendments to Financial Disclosures About Guarantors and Issuers of Guaranteed Securities

Financial disclosures about guarantors and issuers of guaranteed securities

- On March 2, 2020, the SEC amended financial disclosure rules in registered debt offerings involving guaranteed or collateralized securities under Rules 3-10 and 3-16 of Regulation S-X
- Aims to improve quality of disclosure, encourage issuers to conduct debt offerings on a registered basis and reduce compliance costs
- **Effective Date**: January 4, 2021
- Amendments revise Rules 3-10 and 3-16, relocate certain parts to a new Article 13, consisting of new Rule 13-01 and 13-02 of Reg S-X

Financial disclosures about guarantors and issuers of guaranteed securities *(cont'd)*

Rule 3-10

- General Rule: Each issuer and each guarantor of registered debt securities must file its own, separate, audited annual and unaudited interim financial statements
- Exception: <u>Old Rule 3-10</u> provides for 5 different exemptions that allow omission of separate financial statements, subject to conditions, including that:
  - Subsidiary issuer or guarantor must be "100%-owned" by parent company
  - Each guarantee must be "full and unconditional" and in case of multiple guarantees, "joint and several"
  - Parent company must provide alternative disclosures (commonly, in the form of *condensed consolidating financial information*) in its consolidated financial statement footnotes, for so long as guaranteed securities remain outstanding
- Exception based on eligible issuer-guarantor structure (*e.g.*, finance or operating sub issues, with parent guaranty; parent company issues with sub guaranty)

Financial disclosures about guarantors and issuers of guaranteed securities *(cont'd)*

Amended Rule 3-10/New Rule 13-01

- Replaces condition that subsidiary be *100%-owned* by parent company with condition that it be *consolidated* in parent's consolidated financial statements
- Replaces 5 eligible structures with two broad eligible categories, *i.e.* either:
  - (**x**) parent company issues security or co-issues security, jointly and severally, with one or more of its consolidated subsidiaries **or** (**y**) a consolidated subsidiary issues security or co-issues security with one or more other consolidated subsidiaries of parent company, and security is guaranteed fully and unconditionally by parent company
  - So, role of parent company, not subsidiary guarantor is relevant
- Simplifies conditions to allow omission of separate financials:
  - (**1**) consolidated financial statements of parent company have been filed, (**2**) subsidiary issuer or guarantor is a consolidated subsidiary of parent company, (**3**) guaranteed security is debt or debt-like, (**4**) issuer and guarantor structure must be one of two eligible structures above, **and** (**5**) parent company provides Revised Alternative Disclosures

Financial disclosures about guarantors and issuers of guaranteed securities *(cont'd)*

Amended Rule 3-10/New Rule 13-01

- Replaces condensed consolidating financial information with shorter, abbreviated "Summarized Financial Information" (SFI) and non-financial disclosures that will expand qualitative disclosures about guarantees, issuers and guarantors
  - SFI includes select (instead of all major captions of) balance sheet and income statement line items and accompanying note briefly describing basis of presentation, but unlike Condensed Consolidating Information, excludes cash flow statement items
  - SFI of subsidiary issuer or guarantor may be presented on a combined basis with parent
  - Information related to subsidiaries that are not issuers or guarantors not required
  - SFI covers only most recently ended fiscal year and year-to-date interim period included in parent company's financial statements
  - Non-financial disclosures to the extent material, to include qualitative disclosures about guarantees, issuer, guarantors, and information affecting payment to holders

EY Center for Board Matters

Enhancing human capital and other ESG disclosures

April 2021

EY

Building a better working world

New human capital disclosure requirements

SEC adopts principle-based approach

- In August 2020, the Securities and Exchange Commission introduced an important new requirement.
- Registrants now have to provide a description of human capital resources to the extent material to an understanding of their business.
- The rule says a registrant must disclose "a description of the registrant's human capital resources, including the number of persons employed by the registrant, and any human capital measures or objectives that the registrant focuses on in managing the business (such as, depending on the nature of the registrant's business and workforce, measures or objectives that address the development, attraction and retention of personnel)."

"

The rules we adopt today update various Regulation S-K items that essentially have not changed in over 30 years. Our economy, and the world economy, have changed markedly in that time, and many of our rules, which were well rooted in the characteristics of the economy of the 1970s and 1980s, simply have not kept up … Today's rules reflect that important and multifaceted shift in our domestic and global economy.

Our rules also are designed to elicit disclosure tailored to each company's particular industry and business model while being flexible enough to continue to allow for fulsome disclosure as businesses evolve in the future.

Jay Clayton

Former Chairman of the U.S. Securities and Exchange Commission

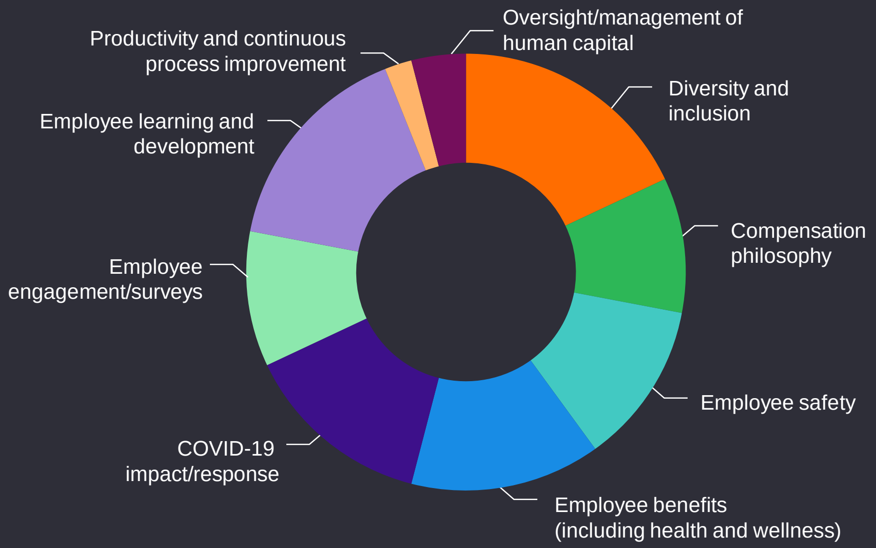
EY

What did companies disclose?

Early findings from 10-K human capital disclosures

- We observed a wide range in the length of human capital disclosures, from a single paragraph to multiple pages.
- The majority of companies employed mostly qualitative disclosure, describing how they considered human capital, including metrics to underscore and explain points.
- Approximately two-thirds of companies included at least one specific figure or metric in addition to the number of employees.

Frequency of disclosure themes discussed in 10-Ks



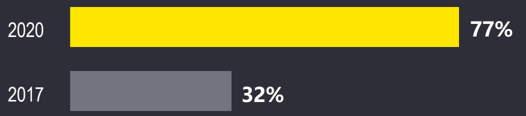
Based on a review of 143 S&P 500 companies that filed 10-Ks through February 15, 2021. Source: How do you value your social and human capital?, EY, March 2021.

Proxy disclosures also highlight human capital

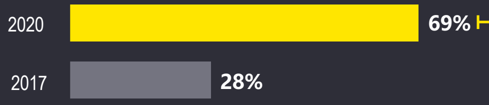
Demonstrate responsiveness to investor focus on workforce issues

- The percentage of Fortune 100 companies voluntarily highlighting human capital initiatives and commitments in their proxy statements and assigning board or committee oversight of human capital has grown exponentially in recent years, and is expected to increase in 2021.

Proxy disclosures that highlighted company initiatives and commitments regarding human capital
(% Fortune 100)



Proxy disclosures that assigned board or committee oversight of human capital
(% Fortune 100)



Oversight is most often assigned to the compensation committee (37% of companies), followed by the full board (23%) or another committee (9%). In most cases disclosures indicate that oversight is inclusive of overall management of, and strategies related to, human capital. However, around a third of disclosures leave unclear whether the board or committee is overseeing a spectrum of human capital factors or just one or two specific components, e.g., workforce diversity or culture.

Top five human capital topics addressed
(% Fortune 100 companies)

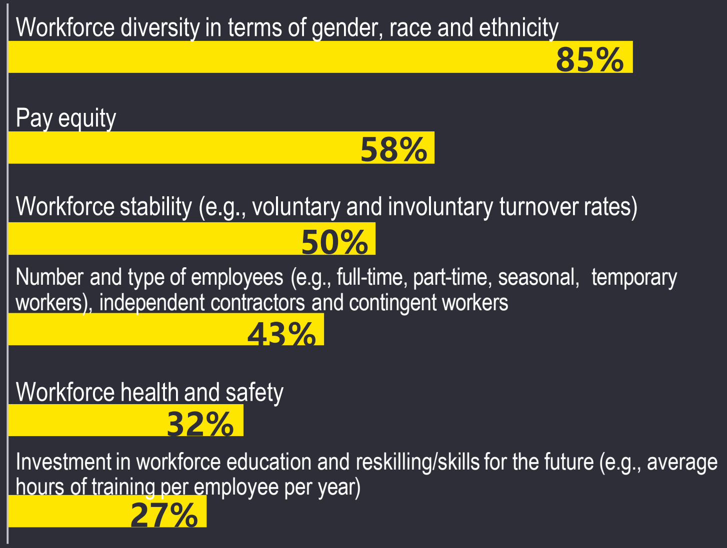
Based on a review of 78 Fortune 100 companies that filed proxy statements as of June 15, 2020. Source: Four ESG highlights from the 2020 proxy season, EY, July 2020.

Which human capital disclosures do investors want?

Diversity a top 2021 investor engagement priority

- In the fall of 2020, the EY Center for Board Matters had conversations with more than 60 institutional investors representing over US$38 trillion in assets under management.
- Around two-thirds of investors surveyed said they will press for robust workforce and board diversity disclosures in 2021, making diversity a top engagement priority this year.
  - Regarding the workforce, most investors want disclosure of diversity data aligned to EEO-1 data
- Other key themes from our discussions included pay equity, workforce stability, company relationships to independent contractors and workforce reskilling and development.

Which three to five of the following disclosures would be of greatest value to you as you assess human capital management?



Source: What investors expect from the 2021 proxy season, EY, February, 2021.

EY

Six ways companies can enhance ESG reporting

Key enhancements investors want to see

1. Focus on what is material and the connection to strategy
2. Align disclosures to external frameworks
3. Disclose metrics, performance and goals
4. Consider integrating material ESG disclosures alongside traditional financial metrics
5. Enhance data credibility through assurance
6. Make sure company disclosures are picked up by third-party data aggregators

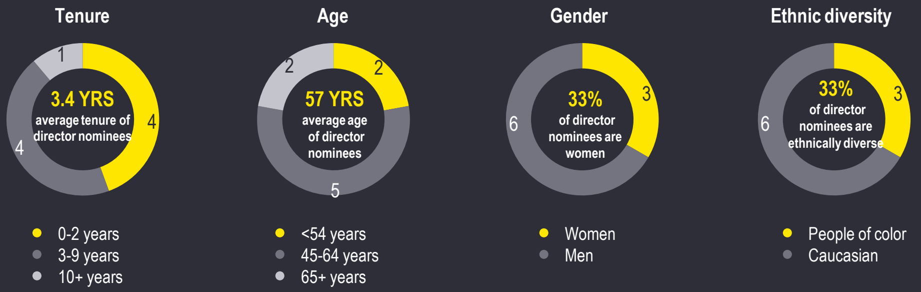
Enhancing governance disclosures

Proxy disclosure trends related to the G of ESG

- Highlight board diversity across skills, tenure and personal characteristics through the use of graphics and a skills matrix.
- Discuss how the board is approaching director succession planning and board education.
- Discuss the board assessment process and key outcomes.
- Include a letter from the board or lead independent director highlighting governance developments and areas of focus.

Skills and expertise

Experience	Director 1	Director 2	Director 3	Director 4	Director 5	Director 6	Director 7	Director 8	Director 9
Senior leadership	●	●	●	●	●		●	●	●
Global/international	●		●	●		●	●	●	●
Industry and IT/technical	●	●	●	●		●		●	
Financial experience							●	●	●
Human capital	●			●	●		●	●	●
Operating and manufacturing	●			●			●	●	
Sales, marketing and brand management	●		●	●	●				
Emerging technologies and business models	●	●	●	●		●	●	●	●
Business development and M&A	●	●		●		●	●	●	●
Cybersecurity/information security	●	●	●				●	●	
Government, legal and regulatory					●				
Public company board	●	●		●	●	●	●	●	●



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Future considerations

How can we maximize the impact of our human capital management and other ESG reporting and processes?

How can we consider and optimize the impact on our brand and reputation with key stakeholders, including investors and prospective employees?

How can we ensure consistency of messaging in IR decks, social media, website, Corporate Sustainability Report, 10-K and the Proxy?

How can we better understand how key shareholders view our disclosures and practices?

More from the EY Center for Board Matters

For more insights, including access to Better Questions for Boards webcasts or to subscribe to our mailing list, please visit **ey.com/us/boardmatters**.

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The SEC Under the New Administration and mREITs: What to Expect

What to expect

- Gensler's tenure at the CFTC was marked by very active rulemaking—the CFTC rolled out a flurry of rules to implement the Dodd-Frank Title VII mandate for swap dealers, many of which later had to be "right-sized" or adjusted—and stepped up enforcement
- Also during his time at the CFTC, Gensler focused on "innovation" at the agency, including the agency's focus on fintech
- So, what can we expect from SEC Chair Gensler?

What to expect *(cont'd)*

- Corporation Finance agenda
    - Revisiting the accredited investor definition
    - Revisiting the exemption from Sarbanes-Oxley Section 404 attestation
    - Climate change disclosure standards that are prescriptive
    - Human capital and diversity disclosures that are prescriptive
    - Political spending disclosures

What to expect *(cont'd)*

- Corporation Finance agenda
  - "Good Corporate Hygiene"—essentially a continuation of the Clayton regime
  - This encompasses reviewing and proposing changes to:
    - Rule 10b-18 (company repurchases)—long a focus for Democrats
    - Rule 10b5-1
    - Rule 13(d)—ownership reporting—taking up the Brokaw Act
    - Address disclosures of short positions

What to expect *(cont'd)*

- Enforcement agenda
  - Continuing the focus on "corporate hygiene"—insider trading violations; use of material nonpublic information by insiders; failure to adopt appropriate safeguards and controls relating to corporate repurchase programs; 10b5-1 plan violations; Regulation FD violations
  - Non-GAAP and other financial reporting issues
  - Whistleblower program reform
  - Enforcement of Regulation BI
  - More active broker-dealer enforcement—Volcker Rule and other violations
  - Addressing market integrity issues

Other Mortgage-Related Policy Issues We’re Watching

SEC Report

- SEC Report released in October 2020: "U.S. Credit Markets: Interconnectedness and the Effects of the COVID-19 Economic Shock"
  - Report focuses on the repurchase agreement (repo) market and short-term wholesale funding market generally, as well as on mortgage market
  - "A risk in the residential mortgage market worthy of continued monitoring is its reliance on short-term funding from certain nonbanks, including mREITs, government MMFs, and the FHLB system. Nonbanks originate 70% and service 50% of all mortgages. Government MMFs have increasingly funded FHLBs, who lend to their member institutions. mREITs finance their MBS portfolios mostly in the repo market."
  - The SEC held a roundtable in October 2020 to discuss the report and focused on leverage and reliance on repo

FSOC Report

- The FSOC's annual report (December 2020) focuses on short-term wholesale funding and need to regulate
  - "Liquidity demand from leveraged participants, such as…mREITs using agency MBS collateral, may have also played a significant role in the recent market volatility. Some of these leveraged participants are vulnerable to funding risks because of their reliance on funding in repurchase agreement (repo) markets"
  - The Council recommends that regulators review these structural vulnerabilities, especially the use of leverage
  - This was followed by SEC Chair Clayton's speech and by banking agency heads' speeches on the need for regulation of repo market