

COVID-19: FEDERAL RESERVE'S COMMERCIAL PAPER FUNDING FACILITY 2020 MAY ENHANCE CONSUMER LENDING AND CORPORATE LIQUIDITY

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"Wishing you a pot o' gold, and all the joy your heart can hold." – traditional St. Patrick's Day greeting

On March 17, 2020, the Federal Reserve Board announced the establishment of the Commercial Paper Funding Facility 2020 ("CPFF"), a leading U.S. government initiative to facilitate the return of capital to the financial system by providing a backstop funding of three-month commercial paper [1]. The CPFF is designed to support the flow of consumer credit by helping stimulate demand for asset-backed commercial paper and to help maintain the crucial role of corporate commercial paper programs as a source of liquidity to help companies meet their operational needs.

The CPFF directly addresses the considerable strain on the commercial paper markets in recent days, as businesses and households face greater uncertainty in light of the COVID-19 contagion crisis. By eliminating much of the risk that eligible issuers will not be able to repay investors by rolling over their maturing commercial paper obligations, the hope is that CPFF will encourage investors to once again engage in term lending in the commercial paper markets during an unprecedented time of fear and economic turmoil.

The United States Federal Reserve Board (the "Fed") is establishing the CPFF program with approval of the Treasury Secretary under Section 13(3) of the Federal Reserve Act. This is the same statutory authority that was used during the 2008 financial crisis to create groundbreaking federal interventions in credit markets with programs such as the Term Asset-Backed Securities Loan Facility -- TALF --, the Term Auction Facility --TAF --, the Primary Dealer Credit Facility -- PDCF -- and the Term Securities Lending Facility --TSLF.

The CPFF will be structured as a committed secured credit facility under which the Federal Reserve Bank of New York ("FRBNY") will make loans to a special-purpose vehicle (the "SPV") to buy three-month commercial paper (including asset-backed commercial paper) at pricing based on the then-current three-month overnight index swap rate plus 200 basis points.

The FRBNY will commit to lend funds to the SPV to purchase eligible commercial paper, with all such loans being secured by all the assets of the SPV. The U.S. Treasury Department will provide the FRBNY with \$10 billion of credit protection for the CPFF from its Exchange Stabilization Fund.

In order to be eligible for purchase by the SPV, commercial paper must meet the following criteria:

- It must have a three-month term;
- It must be issued by a U.S. company (including one with a foreign parent);

- It must be denominated in U.S. dollars;
- It must have a short-term credit rating of at least A-1/P-1/F-1 (or its equivalent) by a major nationally recognized statistical rating organization ("NRSRO") and, if rated by multiple major NRSROs, must be rated at least A-1/P-1/F-1 by two or more major NRSROs, in each case subject to review by the Fed; and
- It must not exceed the issuer limit described below.

The SPV's exposure to any single issuer at any time will be capped at the largest amount of U.S. dollar-denominated commercial paper of that issuer that was outstanding on any day between March 16, 2019 and March 16, 2020 (the "issuer limit"). Furthermore, once an issuer's total outstanding commercial paper (including commercial paper owned by the SPV) equals or exceeds the issuer limit, the SPV may not buy additional commercial paper from that issuer even if the SPV's holding of that issuer's commercial paper is less than the issuer limit.

As the Fed publishes more detailed terms and conditions for the CPFF and an operational calendar, we will assist our clients to determine how they can participate effectively in the benefits this program has to offer them and the market.

[1] Further details of the CPFF are available on the Federal Reserve website:

<https://www.federalreserve.gov/newsevents/pressreleases/monetary20200317a.htm>.

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