

Clients & Friends Memo

COVID-19 Update: Federal Reserve Announces Municipal Liquidity Facility

April 15, 2020

The Federal Reserve has announced the Municipal Liquidity Facility (the “MLF”) to provide liquidity to state and local governmental authorities affected by the COVID-19 pandemic.¹ The MLF, which is established pursuant to the Federal Reserve’s emergency lending authority under Section 13(3) of the Federal Reserve Act,² will lend up to \$500 billion to “Eligible Issuers” through September 30, 2020, subject to extension.

Under the MLF, a Federal Reserve Bank will commit to lend funds to a special purpose vehicle (the “SPV”), on a full-recourse basis and secured by all assets of the SPV. The SPV will also be funded by the Treasury Department, which will make an initial equity investment of \$35 billion.³ The SPV is permitted to purchase up to \$500 billion of short-term notes directly from states, cities and municipalities upon their issuance.⁴

This memorandum outlines the key terms of the MLF.

Eligible Issuers:

- U.S. states and the District of Columbia (“States”); U.S. cities with populations of at least one million residents (“Cities”), U.S. counties with populations of at least two million residents (“Counties”); or an instrumentality thereof that issues notes on behalf of such State, City or County for the purpose of managing cash flows.⁵

¹ See Federal Reserve Takes Additional Actions to Provide Up to \$2.3 Trillion in Loans to Support the Economy (Apr. 9, 2020), available [here](#); see also [Municipal Liquidity Facility Term Sheet](#) (Apr. 9, 2020), available [here](#).

² Section 13(3) allows the Federal Reserve to take certain emergency actions in “unusual and exigent circumstances,” including by authorizing any Federal Reserve Bank to discount notes in any program or facility with “broad-based eligibility.”

³ The Treasury Department will use funds appropriated pursuant to Section 4027 of the CARES Act to make the equity investment.

⁴ It is not clear whether the MLF contemplates the use of an agent dealer or other institution to assist in purchases.

⁵ Eligible Issuers will be determined using U.S. Census Bureau data.

- Only one issuer per State, City or County is eligible to participate in the MLF.

Eligible Notes:

- Tax anticipation notes, tax and revenue anticipation notes, bond anticipation notes and other similar short-term notes issued by Eligible Issuers.
- Notes must have maturities of 24 months or less from the date of issuance.

Limitations:

- The SPV may purchase Eligible Notes in one or more issuances up to an aggregate amount of 20% of the sum of (1) the general revenue from own sources for fiscal year 2017 and (2) utility revenue of the relevant State, City or County government for fiscal year 2017.
- A State may request the SPV to purchase Eligible Notes in excess of the above limitation in order to provide financial support to political subdivisions and instrumentalities that are not Eligible Issuers.

Use of Proceeds:

- Eligible Issuers may use the proceeds of Eligible Notes to manage (1) reductions in cash flow caused by an extension of an income tax filing deadline, (2) potential reductions of tax and other revenues or increases in expenses related to or resulting from the COVID-19 pandemic, and (3) required payments of principal and interest on obligations of the relevant State, City or County.
- An Eligible Issuer may also use the proceeds of Eligible Notes to purchase similar notes issued by, or otherwise to assist, political subdivisions and instrumentalities of the relevant State, City or County for the purposes enumerated above.

Pricing, Fees and Other Terms:

- Pricing will be based on an Eligible Issuer's rating at the time the SPV purchases the Eligible Notes. The Federal Reserve indicated that further details on the rating point will be provided.
- To participate in the MLF, an Eligible Issuer will pay an origination fee equal to 10 basis points of the aggregate principal amount of the Eligible Notes purchased by the SPV with respect to that Eligible Issuer. The origination fee can be paid from the proceeds of the Eligible Notes.
- Eligible Notes purchased by the SPV are callable by the Eligible Issuer, at par, at any time.

Termination:

- The SPV will not purchase Eligible Notes after September 30, 2020, unless the MLF is extended by both the Federal Reserve and the Treasury Department.
- The Federal Reserve Bank will continue funding the SPV until its underlying assets either mature or are sold.

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