

PUBLIC FINANCE ADVISORY

The Federal Reserve Announces a New Municipal Liquidity Facility to Provide Cash Flow Relief to State and Local Governments



On April 9, 2020, the Federal Reserve announced a new program to bolster State and local government's cash flow disruptions caused by the COVID-19 pandemic. In its announcement, the Federal Reserve Board disclosed the creation of a new municipal liquidity facility loan program authorized under Section 13(3) of the Federal Reserve Act to provide lending support to the following "Eligible Issuers":

- States;
- The District of Columbia;
- Cities with a population exceeding one million residents; and
- Counties with a population exceeding two million residents.

The new municipal liquidity facility is a loan program and will create a special purpose vehicle (the "SPV"), and one or more of 12 federal reserve banks will lend funds to the SPV on a recourse basis, secured by all SPV assets, and will be authorized to purchase up to \$500 billion in tax, revenue, and/or bond anticipation notes and other short-term notes (the "Eligible Notes") issued by Eligible Issuers. The initial \$35 billion investment in the SPV will be funded by the Economic Stabilization Fund established by the CARES Act.

An Eligible Issuer may use the proceeds to manage cash flow disruptions resulting from (1) income tax deferrals due to filing extensions, and (2) potential reductions of tax or other revenues or increases in expenses relating to or resulting from the COVID-19 pandemic. Additionally, an Eligible Issuer can utilize the proceeds of Eligible Notes for the payment of principal and interest on obligations of the relevant State, city, or county. The SPV will cease purchasing Eligible Notes on September 30, 2020, unless the Treasury Department extends the facility.

The aggregate principal amount of all Eligible Notes issued by an Eligible Issuer is capped at 20% of its general revenue from its own sources and utility revenue for the fiscal year 2017. Eligible Notes will have a maximum maturity of 24 months. The SPV will purchase each Eligible Note at a price based upon the Eligible Issuer's



James Lane
Member
Denver
303.299.8326
[Email](#)



Will Vietti
Associate
Denver
303.299.8016
[Email](#)

credit rating at the time of the purchase, and Eligible Issuers will have the option to redeem the Eligible Notes at par at any time. Each Eligible Issuer that participates in the municipal liquidity facility loan program must pay an origination fee equal to 10 basis points of the principal amount of the obligation. Each Eligible Note will be subject to eligibility review by the Federal Reserve. Additionally, the Federal Reserve will require legal opinions and disclosures prior to the purchase and State law limitations applicable to the incurrence of debt by State and local governments will apply.

An Eligible Issuer will be permitted to use the proceeds of its Eligible Notes purchased by the SPV to either (i) purchase similar notes issued by its political subdivisions and instrumentalities, or (ii) otherwise make funds available for assistance to its constituent political subdivisions. Accordingly, each State could choose to support the same cash flow needs of its local political subdivisions with loans or grants of the proceeds of the eligible loans. Each State will need to determine how much of its proceeds will be shared with local governments and establish procedures for local governments to apply for such available funds. The elected officials of the eligible States will need to act quickly to take advantage of this facility and establish procedures to determine how to equitably share the proceeds with its constituent smaller local governments.

The Federal Reserve has stated that it will continue to closely monitor conditions in the primary and secondary markets for municipal securities and will evaluate whether additional measures are needed to support the flow of credit and liquidity to state and local governments.

For questions regarding the new municipal liquidity facility and its impact, please contact any member of our [Public Finance Group](#).