March 18, 2020

MEMORANDUM TO: Board of Directors

FROM: Doreen R. Eberley, Director

SUBJECT: Regulatory Capital Rule: Money Market Mutual Fund Liquidity Facility

SUMMARY: To provide liquidity to the money market sector to help stabilize the financial system, the Board of Governors of the Federal Reserve System ("FRB") on March 18, 2020, authorized the Federal Reserve Bank of Boston to establish the Money Market Mutual Fund Liquidity Facility ("MMLF"), pursuant to section 13(3) of the Federal Reserve Act. Under the MMLF, the Federal Reserve Bank of Boston will extend non-recourse loans to eligible financial institutions to purchase certain types of assets from money market mutual funds ("MMFs"). To facilitate this Federal Reserve lending program, staff is presenting for approval of the Federal Deposit Insurance Corporation ("FDIC") Board of Directors ("FDIC Board") a request to adopt and publish the attached interagency interim final rule ("interim final rule"), to allow banking organizations to neutralize the regulatory capital effects of participating in the program.

Recommendation: Staff requests that the FDIC Board approve this interagency interim final rule and authorize its publication in the *Federal Register* with an immediate effective date and with a comment period deadline of 45 days after the date of *Federal Register* publication.

Concur:

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Nicholas J. Podsiadly
General Counsel

Discussion:

I. Background

Recent events have significantly and adversely impacted global financial markets. The spread of the Coronavirus Disease 2019 (COVID-2019) has slowed economic activity in many countries, including the United States. In particular, sudden disruptions in financial markets have put increasing liquidity pressure on MMFs. Given these pressures, MMFs have been faced with redemption requests from clients with immediate cash needs. The MMFs may need to sell a significant number of assets to meet these redemption requests, which could further increase market pressures.

In order to prevent the disruption in the money markets from destabilizing the financial system, on March 18, 2020, the FRB, with approval of the Secretary of the Treasury, authorized the Federal Reserve Bank of Boston to establish the MMLF, pursuant to section 13(3) of the Federal Reserve Act.[1] Under the MMLF, the Federal Reserve Bank of Boston will extend non-recourse loans to eligible borrowers to purchase assets from MMFs. Assets purchased from MMFs will be posted as collateral to the Federal Reserve Bank of Boston (eligible collateral). Eligible borrowers under the MMLF include certain banking organizations subject to the agencies' capital rule,[2] such as depository institutions and depository institution holding companies. Eligible collateral under the MMLF includes U.S. Treasuries, fully guaranteed agency securities, securities issued by government-sponsored enterprises, and certain types of commercial paper.

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1 12 U.S.C. § 343(3).

2 See 12 CFR parts 3 (OCC), 217 (Board) and 324 (FDIC).

To facilitate this Federal Reserve lending program, this interim final rule would allow banking organizations to neutralize the effects of purchasing assets through the MMLF on risk-based and leverage capital ratios.

II. The Interim Final Rule

The agencies' capital rule requires banking organizations to comply with risk-based and leverage capital requirements, which are expressed as a ratio of regulatory capital to assets. Risk-based requirements are based on risk-weighted assets, whereas leverage requirements are based on a measure of total consolidated assets or total leverage exposure. Participation in the MMLF will affect the balance sheet of a banking organization because the banking organization must acquire and hold assets (that is, eligible collateral pledged to the Federal Reserve Bank of Boston) on its balance sheet. As a result, a banking organization that participates in the MMLF could realize increased capital requirements.

Staff of the agencies have determined that the current leverage and risk-based capital requirements for the assets acquired by a banking organization as part of the MMLF do not reflect the substantial protections provided to the organization by the Federal Reserve Bank of Boston in connection with the facility. Because of the nonrecourse nature of the FRB's extension of credit to the banking organization, the organization is not exposed to credit or market risk from the assets purchased by the banking organization and pledged to the FRB. Therefore, staff of the agencies believe that it would be appropriate to exclude the effects of purchasing assets through the MMLF from a banking organization's regulatory capital.

Specifically, the interim final rule would permit banking organizations to exclude nonrecourse exposures acquired as part of the MMLF from a banking organization's total leverage exposure, average total consolidated assets, advanced approaches-total risk-weighted assets, and standardized total risk-weighted assets, as applicable.

Conclusion:

Staff requests that the FDIC Board approve this interim final rule and authorize its publication in the *Federal Register* with an immediate effective date and with a comment period deadline of 45 days after the date of *Federal Register* publication.

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