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Understanding the Federal Reserve's New Bank Term Funding Program in Response to Recent Bank Failures

March 16, 2023

On March 12, 2023, in the wake of shutdowns of Silicon Valley Bank and Signature Bank by regulators in their respective states, the Federal Reserve Board announced the creation of a new Bank Term Funding Program ("BTFP") backstopped by up to $25 billion from the U.S. Treasury Department's Exchange Stabilization Fund.

The Federal Reserve also eased conditions for discount window borrowing.

This client alert discusses the terms and implications of the BTFP and the new discount window requirements.

BTFP

The goal of the BTFP is to make available additional funding to eligible depository institutions, to stabilize the banking system and to safeguard deposits and credit. The core feature of the BTFP is the provision of short-term loans to eligible financial institutions in exchange for certain long-term securities pledged as collateral.

The Bank Term Funding Program term sheet is available here.

Borrower Eligibility

To borrow under the BTFP, an institution must be a U.S. federally insured depository institution (including a bank, savings association or credit union) or U.S. branch or agency of a foreign bank and be eligible for primary credit.

Eligible Collateral and Valuation

Eligible collateral includes U.S. treasury securities, agency debt and mortgage-backed securities and certain other qualifying assets. Eligible collateral must be available for purchase by the Federal Reserve in the open market and must have been owned by the borrower as of March 12, 2023.

Under the BTFP, a borrower can borrow up to the value of its eligible collateral. However, for purposes of the BTFP, pledged collateral will be valued at par, and not at its mark-to-market value. This means that the deterioration in value of long-term securities caused by increases in interest rates since 2022 will be ignored by the Federal Reserve for purposes of valuing the collateral.

Economic Terms

Advances can be requested under the BTFP until at least March 11, 2024. The loans will be available for terms of up to one year from the date of the advance.

The interest rate for term advances is the one-year overnight index swap rate plus 10 basis points. Interest rates will be fixed for the term of the advance on the day the advance is made. Borrowers may prepay advances (including for purposes of refinancing) at any time without penalty.

Discount Window

The discount window is a standing loan program available to any U.S. federally insured depository institution (including banks, savings associations or credit unions) that allows such eligible institutions to borrow money from the Federal Reserve against a range of bank-held collateral to meet temporary shortages of liquidity. In general, a pledging institution must have rights in investment grade securities that are sufficient to grant an enforceable and perfectable first-priority security interest to the Federal Reserve Bank. Examples of securities accepted by the Federal Reserve for purposes of the discount window include, but are not limited to, U.S. treasury securities and fully guaranteed agency securities, corporate and municipal bonds, asset-backed securities, collateralized debt and loan obligations and a wide range of commercial, agricultural and industrial loans. A more fulsome list of eligible collateral can be found here.

The core change to the discount window program announced on March 12, 2023 was a switch to the same par valuation for discount window loan collateral, insulating borrowers from the effects of recent interest rate increases under these existing programs, as well as under the BTFP.

What's Next?

The Federal Reserve Board noted that it is carefully and closely monitoring developments and conditions across the financial markets and emphasized that it is prepared to use its full range of tools to support households and businesses. We will continue to monitor additional or modified information about the BTFP and other Federal Reserve action as it becomes available. More information about the receivership of Silicon Valley Bank and Signature Bank is available at our client alert here.

Proskauer's cross-disciplinary, cross-jurisdictional practices have particular expertise with the complexities involved in financing and asset management. We are focused on supporting and addressing client concerns and are prepared to discuss navigating the current situation. If you have any questions, please contact your attorney team at Proskauer.

Related Professionals

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