The Third Report of the Congressional Oversight Commission

July 20, 2020

<u>Commission Members</u>
U.S. Representative French Hill
Bharat Ramamurti
U.S. Representative Donna E. Shalala
U.S. Senator Pat Toomey

TABLE OF CONTENTS

Introduction 1

Executive Summary 6

Treasury and Federal Reserve Recent Developments 17

Appendix A: Letter from Congressional Oversight Commission to Treasury Secretary Steven Mnuchin and Federal Reserve Chair Jerome Powell, dated May 29, 2020

Appendix B: Letter from Treasury Secretary Steven Mnuchin and Federal Reserve Chair Jerome Powell to Congressional Oversight Commission, dated June 8, 2020

Appendix C: Letter from Treasury Secretary Steven Mnuchin and Federal Reserve Chair Jerome Powell to Congressional Oversight Commission, dated June 29, 2020

INTRODUCTION

This is the third report of the Congressional Oversight Commission (the "Commission") created by the CARES Act. The Commission's role is to conduct oversight of the implementation of Division A, Title IV, Subtitle A of the CARES Act ("Subtitle A") by the Treasury Department (the "Treasury") and the Board of Governors of the Federal Reserve System (the "Federal Reserve"). Subtitle A provided $500 billion to the Treasury for lending and other investments "to provide liquidity to eligible businesses, States, and municipalities related to losses incurred as a result of coronavirus."[1]

Of this amount, $46 billion is set aside for the Treasury itself to provide loans or loan guarantees to certain types of companies. Up to $25 billion is available for passenger air carriers, eligible businesses certified to perform inspection, repair, replace, or overhaul services, and ticket agents. Up to $4 billion is available for cargo air carriers, and up to $17 billion is available for businesses "critical to maintaining national security."[2] Any unused portions of this $46 billion, and the remaining $454 billion, may be used to support emergency lending facilities established by the Federal Reserve.

At this time, the emergency lending facilities established by the Federal Reserve that are receiving CARES Act funds are:

- The Primary Market Corporate Credit Facility (PMCCF) and Secondary Market Corporate Credit Facility (SMCCF): The Treasury has announced it intends to make a total equity investment of $75 billion in these facilities. The SMCCF buys previously issued corporate bonds and exchange-traded funds (ETFs) that invest in corporate bonds. The PMCCF will purchase newly issued corporate bonds and portions of syndicated loans. Collectively, these facilities can support up to $750 billion in purchases.[3] As of July 15, 2020, the Treasury has invested $37.5 billion in the special purpose vehicle

[1] CARES Act, Pub. L. No. 116-136, § 4003(a), 134 Stat. 281 (2020).
[2] *Id* at § 4003(b). In addition, Division A, Title IV, Subtitle B of the CARES Act ("Subtitle B") authorized the Treasury to provide up to $32 billion in financial assistance to passenger air carriers, cargo air carriers, and certain airline industry contractors that must be exclusively used for the continuation of payment of employee wages, salaries, and benefits. Of this amount, up to $25 billion is available for passenger air carriers; up to $4 billion is available for cargo air carriers; and up to $3 billion is available for certain airline industry contractors. The Treasury has begun to provide some of this financial assistance. Subtitle B is not within the jurisdiction of the Congressional Oversight Commission (the "Commission").
[3] Board of Governors of the Federal Reserve System, *Primary Corporate Credit Facility Term Sheet,* Apr. 9, 2020, https://www.federalreserve.gov/newsevents/pressreleases/files/monetary20200409a5.pdf.

(SPV) it uses for the PMCCF and SMCCF.[4] As of July 15, the SMCCF has purchased $11.4 billion of bond ETFs and individual corporate bonds.[5] The Federal Reserve has not announced that the PMCCF has purchased any bonds or syndicated loans.

- The Main Street Lending Program (MSLP): The Treasury has announced it intends to make an equity investment of $75 billion in this program, which backs loans to small and medium-sized businesses with up to 15,000 employees. The Federal Reserve has decided to expand this program to include certain nonprofit organizations. The MSLP can support up to $600 billion in lending.[6] As of July 15, 2020, the Treasury has invested $37.5 billion in this program.[7] The MSLP is operational and able to purchase eligible loans submitted by lenders registered to participate in the program. There are approximately 300 lenders that have registered or are in the process of registering,[8] though only 130 of them have publicized that they are accepting loan applications from new customers.[9] As of July 15, 2020, the MSLP has purchased a single $12 million loan.[10]

- The Municipal Liquidity Facility (MLF): The Treasury has announced it intends to make an equity investment of $35 billion in this facility, which purchases short-term notes issued by state and local governments. The MLF can provide up to $500 billion in

---

[4] Board of Governors of the Federal Reserve System, Statistical Release H.4.1, *Factors Affecting Reserve Balances of the Depository Institutions and Condition Statement of Federal Reserve Banks*, July 16, 2020, https://www.federalreserve.gov/releases/h41/ (to access click on hyperlink for July 16, 2020 release). The SPV for the PMCCF and SMCCF is Corporate Credit Facilities LLC (CCFL). Footnote 14 to table 1 in the H.4.1 statistical release dated July 16, 2020 indicates that the Treasury has made a $37.5 billion equity investment in the CCFL.
[5] *Id*. at Table 4.
[6] Board of Governors of the Federal Reserve System, *Main Street New Loan Facility Term Sheet,* June 8, 2020, https://www.federalreserve.gov/newsevents/pressreleases/files/monetary20200608a1.pdf.
[7] Board of Governors of the Federal Reserve System, Statistical Release H.4.1, *Factors Affecting Reserve Balances of the Depository Institutions and Condition Statement of Federal Reserve Banks*, July 16, 2020, https://www.federalreserve.gov/releases/h41/ (to access click on hyperlink for July 16, 2020 release). The SPV for the MSLP is MS Facilities LLC (MSFL). Footnote 14 to table 1 in the H.4.1 statistical release dated July 16, 2020 indicates that the Treasury has made a $37.5 billion equity investment in the MSFL.
[8] U.S. House Committee on Financial Services hearing on Coronavirus and the CARES Act, 116th Cong. (June 30, 2020) (statement of Jerome Powell, Chair, Board of Governors of the Federal Reserve).
[9] Federal Reserve Bank of Boston, *Listing of Lender Accepting New Business Customers,* Information for Borrowers, https://www.bostonfed.org/supervision-and-regulation/supervision/special-facilities/main-street-lending-program/information-for-borrowers.aspx (last visited on July 19, 2020).
[10] *Id*. at Table 4; U.S. House Small Business Committee hearing on Oversight of the Small Business Administration and Department of Treasury Pandemic Programs, 116th Cong. (July 17, 2020) (statement of Steven Mnuchin, Secretary, U.S. Department of the Treasury).

lending.[11] As of July 15, 2020, the Treasury has invested $17.5 billion in this facility.[12] The MLF has made a single purchase of $1.2 billion in notes from the state of Illinois, as of July 15, 2020.[13]

- The Term Asset-Backed Securities Loan Facility (TALF): The Treasury has announced it intends to make an equity investment of $10 billion in this facility, which will make loans to companies secured by consumer or business loans. The TALF can provide up to $100 billion in lending.[14] As of July 15, 2020, the Treasury has invested $10 billion in this facility.[15] The TALF has lent $937 million, as of July 15, 2020.[16]

The CARES Act charges the Commission with submitting regular reports to Congress on:

- The use by the Federal Reserve of authority under Subtitle A, including with respect to the use of contracting authority and administration of the provisions of Subtitle A.

- The impact of loans, loan guarantees, and investments made under Subtitle A on the financial well-being of the people of the United States and the U.S. economy, financial markets, and financial institutions.

- The extent to which the information made available on transactions under Subtitle A has contributed to market transparency.

---

[11] Board of Governors of the Federal Reserve System, *Municipal Liquidity Facility Term Sheet,* June 3, 2020, https://www.federalreserve.gov/newsevents/pressreleases/files/monetary20200603a1.pdf; Federal Reserve Bank of New York, *FAQs: Municipal Liquidity Facility,* June 3, 2020, https://www.newyorkfed.org/markets/municipal-liquidity-facility/municipal-liquidity-facility-faq.

[12] Board of Governors of the Federal Reserve System, Statistical Release H.4.1, *Factors Affecting Reserve Balances of the Depository Institutions and Condition Statement of Federal Reserve Banks*, July 16, 2020, https://www.federalreserve.gov/releases/h41/ (to access click on hyperlink for July 16, 2020 release). The SPV for the MLF is the Municipal Liquidity Facility LLC (MLFL). Footnote 14 to table 1 in the H.4.1 statistical release dated July 16, 2020 indicates that the Treasury has made a $17.5 billion equity investment in the MLFL.

[13] *Id*. at Table 4; Shruti Singh & Amanda Albright, *Illinois Becomes First to Tap Fed Loans After Yields Surge,* Bloomberg, June 2, 2020, https://www.bloomberg.com/news/articles/2020-06-02/illinois-becomes-first-to-tap-fed-loans-after-bond-yields-surge.

[14] Board of Governors of the Federal Reserve, *Term Asset-Backed Securities Loan Facility,* May 12, 2020, https://www.federalreserve.gov/newsevents/pressreleases/files/monetary20200512a1.pdf.

[15] Board of Governors of the Federal Reserve System, Statistical Release H.4.1, *Factors Affecting Reserve Balances of the Depository Institutions and Condition Statement of Federal Reserve Banks*, July 16, 2020, https://www.federalreserve.gov/releases/h41/ (to access click on hyperlink for July 16, 2020 release). The SPV for the TALF is TALF II LLC. Footnote 14 to table 1 in the H.4.1 statistical release dated July 16, 2020 indicates that the Treasury has made a $10 billion equity investment in the TALF II LLC.

[16] *Id*. at Table 4.

- The effectiveness of loans, loan guarantees, and investments made under Subtitle A in minimizing long-term costs to the taxpayers and maximizing the benefits for taxpayers.[17]

In its first report to Congress on May 18, 2020, the Commission stated that it is responsible for answering two basic questions:

- What are the Treasury and the Federal Reserve doing with $500 billion of taxpayer money?

- Who is that money helping?[18]

That first report posed some preliminary questions the Commission had about the initial actions of the Treasury and the Federal Reserve in implementing Subtitle A. On May 29, 2020, the Commission sent a letter to Treasury Secretary Steven Mnuchin and the Federal Reserve Chair Jerome Powell asking them to provide answers to those questions.[19] The letter divided the questions into two tiers. The Commission requested that the Treasury and the Federal Reserve provide answers to the tier 1 questions by June 8, 2020 and answers to the tier 2 questions by June 29, 2020.

On June 8, the Treasury and the Federal Reserve sent a response letter to the Commission that provided answers to the tier 1 questions.[20] The Commission's second report to Congress on June 18, 2020 discussed those answers.[21] On June 29, 2020, the Treasury and the Federal Reserve sent a response letter to the Commission that provided answers to the tier 2 questions.[22]

The Commission's letter of May 29, 2020 also requested a meeting between the Commission and Secretary Mnuchin and Chair Powell. On June 24, 2020, the Commission met with Secretary Mnuchin and Chair Powell on Capitol Hill. The conversation, which focused on the Treasury and the Federal Reserve's design and implementation of emergency lending programs, was frank, productive, and thoughtful.

---

[17] CARES Act, Pub. L. No. 116-136, § 4020, 134 Stat. 281 (2020).
[18] Congressional Oversight Commission, Questions About the CARES Act's $500 Billion Emergency Economic Stabilization Funds, May 18, 2020, at 5, https://www.toomey.senate.gov/files/documents/COC%201st%20Report_05.18.2020.pdf.
[19] Appendix A of this report contains a copy of the Commission's letter of May 29, 2020.
[20] Appendix B of this report contains a copy of the Treasury and the Federal Reserve's letter of June 8, 2020.
[21] Congressional Oversight Commission, The Second Report of the Congressional Oversight Commission, June 18, 2020, https://www.toomey.senate.gov/files/documents/Congressional%20Oversight%20Commission%20Report%20(June%2018,%202020).pdf.
[22] Appendix C of this report contains a copy of the Treasury and the Federal Reserve's letter of June 29, 2020.

The CARES Act empowers the Commission to hold hearings as part of its oversight work.[23] In the coming weeks, the Commission plans to hold a hearing about the MSLP, which backs loans to small and medium-sized businesses with up to 15,000 employees.

In this report, we describe recent key actions the Treasury and the Federal Reserve have taken under Subtitle A and list and discuss the current status and effects of the Treasury and the Federal Reserve's emergency lending programs.

[23] CARES Act, Pub. L. No. 116-136, § 4020(e)(1), 134 Stat. 281 (2020).

EXECUTIVE SUMMARY

The Treasury and the Federal Reserve have announced how they plan to use $195 billion of the $454 billion Congress allocated in the CARES Act to support emergency lending facilities established by the Federal Reserve. As of July 15, 2020, these facilities have made a total of $13.6 billion in purchases and loans,[24] up from a total of $6.7 billion in purchases as of our last report on June 18, 2020. Since our last report, the Treasury has also made one loan, totaling $700 million, to a business it decided was critical to maintaining national security.[25] As of today, all of the Federal Reserve facilities funded by the CARES Act are operational.

Larger Businesses with Access to the Capital Markets

The Commission's last report noted that the Federal Reserve's mere announcement that it was establishing emergency facilities improved market function, enabling certain larger companies to access credit through the debt capital markets to help fund their operations at rates lower than those available when the market was severely stressed. Since the last report, the Federal Reserve has increased its presence in these markets, including by purchasing individual corporate bonds for the first time.

These interventions can help stabilize the economy and support employment. According to the Treasury and Federal Reserve, "[c]orporate bonds support the operations of companies with more than 17 million employees based in the United States . . . . If companies are unable to issue corporate bonds, they may be unable to invest in inventory and equipment, meet current liabilities, or pay employees."[26] The evidence available to the Commission suggests that while some companies that have been able to borrow through the capital markets are using the funds to maintain or even expand payroll, other companies have cut payroll while continuing to issue dividends to shareholders.[27] It is also clear that some of the companies that have been able to borrow since the announcement of these facilities were in strong financial condition.[28]

---

[24] Board of Governors of the Federal Reserve System, Statistical Release H.4.1, *Factors Affecting Reserve Balances of the Depository Institutions and Condition Statement of Federal Reserve Banks*, June 16, 2020, https://www.federalreserve.gov/releases/h41/ (to access click on hyperlink for June 16, 2020 release).

[25] U.S. Department of the Treasury, *Treasury to Provide Loan to YRC Worldwide*, July 1, 2020, https://home.treasury.gov/news/press-releases/sm1049.

[26] Appendix B at 3.

[27] Bob Ivry, et al., *Fed Vow Boosts Debt Binge as Borrowers Cut Thousands of Jobs*, Bloomberg, June 5, 2020, at https://www.bloomberg.com/news/articles/2020-06-05/fed-vow-boosts-debt-binge-while-borrowers-cut-thousands-of-jobs.

[28] Joy Wiltermuth, *Apple borrows $8.5 billion, joins record corporate debt borrowing spree*, May 4, 2020, https://www.marketwatch.com/story/apple-pulls-in-pricing-joins-record-corporate-debt-borrowing-spree-2020-05-04.

Given the powerful impact the announcement of these facilities had on market function, our last report questioned whether the Federal Reserve should even continue its secondary market corporate bond-buying activity activities. Chair Powell addressed this issue in his testimony before the U.S. Senate Banking Committee (the "Senate Banking Committee") and U.S. House of Representatives Financial Services Committee (the "House Financial Services Committee") in June. He testified that "markets are functioning pretty well" and "as those markets continue to normalize, our purchases will decline."[29] But he noted that if market function deteriorated, the SMCCF's purchases would increase.[30] In addition, Chair Powell said that even though the corporate bond market is currently functioning well, the Federal Reserve decided to begin buying individual corporate bonds with the SMCCF, in part, in order to maintain its credibility with market participants by following through on its previously announced plan to buy such bonds.[31] At our June 24, 2020 meeting, Chair Powell reiterated that the Federal Reserve's credibility is key and that to maintain it, the Federal Reserve needed to follow through on its announcement.

We recognize the importance of the Federal Reserve following through on its commitments. At the same time, the secondary market for corporate bonds is functioning well already and continued Federal Reserve intervention can have distortionary effects in both the short term and the long term. Moreover, the Federal Reserve has the PMCCF as a tool to help individual companies that may be struggling to borrow money to finance their operations. We will continue to closely monitor the corporate bond markets and the operation of these facilities.

Small and Medium-Sized Businesses

Our last report noted that there was less evidence, so far, that the actions of the Treasury and the Federal Reserve have been as beneficial for small and medium-sized businesses as they have been for larger companies that can access the capital markets. The lending facility intended to support credit to these companies—the MSLP—became fully operational only on July 6, 2020, more than three months after the Federal Reserve announced that it would be establishing the facility. The length of time it took to establish and launch this facility has been an understandable source of frustration for some small and medium-sized businesses interested in the program.

At our June 24, 2020 meeting and in a June 29, 2020 letter to the Commission, Secretary Mnuchin and Chair Powell explained that providing support to small and medium-sized businesses is new territory for the Federal Reserve and very complex because these businesses are a "broad and heterogeneous class of borrowers" with diverse needs.[32] They indicated the

---

[29] U.S. House Financial Services Committee hearing on Monetary Policy and the State of the Economy, 116th Cong. (June 17, 2020) (statement of Jerome Powell, Chair, Board of Governors of the Federal Reserve).
[30] U.S. Senate Banking, Housing, and Urban Affairs Committee hearing on the Quarterly CARES Act Report to Congress, 116th Cong. (June 16, 2020) (statement of Jerome Powell, Chair, Board of Governors of the Federal Reserve).
[31] *Id*.
[32] Appendix C at 10.

Federal Reserve had to develop a standardized process for the MSLP and "leverage existing channels of bank lending."[33] In contrast, the agencies noted that the "highly-developed and standardized bond market utilized by larger companies" provided them with "an established and effective mechanism for the Federal Reserve to alleviate dislocations in the large corporate credit markets."[34] While the Commission acknowledges the complexity involved in establishing the MSLP, we expect the Treasury and the Federal Reserve to act more swiftly in the future if adjustments need to be made to the MSLP to improve its effectiveness.

If credit is unavailable through other means, the MSLP has the potential to benefit small and medium-sized businesses that employ millions of workers in the U.S. According to one economic study, an estimated 45 million employees, or almost 40% of all private-sector workers, are employed by a business eligible for the MSLP.[35] However, we do not know how many eligible businesses are actually in need of credit from the MSLP. As of July 15, 2020, the facility has purchased one $12 million Main Street loan from a lender in Wisconsin. While information about this loan was provided by Secretary Mnuchin at a July 17, 2020 hearing of the U.S. House of Representatives Small Business Committee, real-time reporting about the MSLP is unavailable, as the Federal Reserve usually releases detailed disclosures about programs like the MSLP on a monthly basis.

We raised questions about the utilization of the MSLP at our June 24, 2020 meeting with Secretary Mnuchin and Chair Powell. We asked them whether low utilization of the MSLP would reflect that businesses do not need credit or have obtained it elsewhere, or that the program is not designed properly to provide assistance to businesses that need it. In response, they noted that low utilization of a program does not necessarily indicate a problem with its design. For example, they noted that the PMCCF had not been used by any businesses. In their view, the lack of utilization of the PMCCF is not a design flaw, but a result of the fact that the corporate bond market is functioning well and businesses are accessing credit through that market.

Secretary Mnuchin and Chair Powell believe, based on feedback they have received from lenders, there is currently a fair to modest amount of interest from businesses in the MSLP. They think this sentiment may reflect the fact that some businesses have been able to obtain credit by drawing down on existing lines of credit or by getting Paycheck Protection Program (PPP) loans backed by the Small Business Administration (SBA). Furthermore, it is possible some small and medium-sized businesses are finding financing from other non-bank lenders sufficient to meet

---

[33] *Id.*
[34] *Id.* at 2.
[35] Nick Timiaraos & Kate Davidson, *Fed, Treasury Disagreements Slowed Start of Main Street Lending Program*, Wall Street Journal, July 12, 2020, https://www.wsj.com/articles/fed-treasury-disagreements-slowed-start-of-main-street-lending-program-11594558800.

their needs.[36] Our initial reaction is that a purchase of one $12 million loan over a week and one-half seems like a small amount, given the economic challenges facing some small and medium-sized businesses. Chair Powell and Secretary Mnuchin told us that demand for Main Street loans may increase over time because bank lending in the middle market has tightened and, as a result, businesses may have less credit to draw on from banks going forward.

Fundamentally, the MSLP is intended to ensure that these businesses can access credit, but there are indications that at least some small businesses do not need credit or they are able to obtain it from sources other than the MSLP. The widely followed monthly National Federation of Independent Business (NFIB) survey of small businesses found that only 3% of business owners reported that all their borrowing needs were not satisfied in June 2020, and only 1% reported that financing was their top business problem (down 1% from May 2020). In contrast, 34% of owners reported all their credit needs were met, and 54% said they were not interested in a loan. The average rate paid on short maturity loans by businesses was 4.5% (down 1.3% from March and April 2020 and down 1% from June 2020). According to the NFIB, "[h]istorically, loans have never been cheaper."[37] What the MSLP cannot do, as a result of the Federal Reserve's statutory and regulatory obligations,[38] is help businesses facing serious declines in revenue that cannot take on additional debt to address that problem.

At our June 24, 2020 meeting, we also raised with Secretary Mnuchin and Chair Powell the issue of creditworthy businesses that may be falling in the gaps between the federal government's assistance programs for businesses. Currently, a business's eligibility for the MSLP is based, in part, on its adjusted 2019 earnings before interest, taxes, depreciation, and amortization (EBITDA). There are some businesses, such as those with a real estate focus, retail businesses with large amounts of inventory, and new and growing businesses, that do not meet the MSLP's EBITDA standards and are too large to qualify for PPP loans but nonetheless are creditworthy because they have substantial assets. These businesses may have low or weak cash flow but possess a favorable loan-to-value or loan-to-cost ratio. At our meeting, Secretary Mnuchin indicated they are looking at options to potentially address this situation, including a possible asset-based lending facility established by the Federal Reserve. As the Treasury and the Federal Reserve are considering such options, the Commission would also recommend they consider

---

[36] One data set that is helpful for determination of small and medium-sized business access to credit is bankruptcy filings. While commercial chapter 11 bankruptcy reorganization filings increased for the first six months of 2020 over the same period for 2019, the total commercial bankruptcy filings across all chapters fell. American Bankruptcy Institute, *Commercial Chapter 11 Filings Increase 26 Percent in First Half of 2020 over Last Year, Total Filings Drop 23 Percent*, July 7, 2020, https://www.abi.org/newsroom/bankruptcy-headlines/commercial-chapter-11-filings-increase-26-percent-in-first-half-of.

[37] William C. Dunkelberg & Holly Wade, *NFIB Small Business Economic Trends*, June 2020, https://assets.nfib.com/nfibcom/SBET-June-2020.pdf.

[38] 12 U.S.C. § 343(3) (Section 13(3) of the Federal Reserve Act); 12 C.F.R. Part 201 (Federal Reserve's Regulation A).

whether it would be appropriate for the MSLP to provide second lien lending to creditworthy businesses with reasonable cash flow and valued collateral.

In addition, the Commission questioned Secretary Mnuchin and Chair Powell about the MSLP payroll conditions. The term sheets for the MSLP state that a business participating in the program "should make commercially reasonable efforts to maintain its payroll and retain its employees during the time [its Main Street loan] is outstanding,"[39] a point reiterated in the Treasury-Federal Reserve letter to the Commission dated June 8, 2020.[40] They also noted that they "will monitor the program's impact on the economic recovery and employment broadly, rather than on a borrower-by-borrower basis."[41]

During our meeting, Secretary Mnuchin and Chair Powell addressed how they view this "commercially reasonable efforts" standard, whether it is sufficient to get businesses to maintain payrolls, and how they plan to monitor compliance with this standard. They indicated businesses that participate in the MSLP are not required to attest in their loan documents that they will use "commercially reasonable efforts" to maintain payrolls. Instead, as Chair Powell described it, the "commercially reasonable efforts" standard is "hortatory"—meaning it is voluntary, not required. In his view, it is not beneficial for the health of a business to require it to borrow money to pay workers who cannot work.[42] Secretary Mnuchin and Chair Powell noted that the CARES Act was the product of careful bipartisan negotiations in Congress, and the legislation does not require businesses participating in lending programs established by the Federal Reserve to maintain payrolls. They indicated they are focused on implementing the law as it was written by Congress, not rewriting the law. Finally, they confirmed that they will not monitor whether individual businesses that receive Main Street loans are making "commercially reasonable efforts" to maintain payroll, but rather will monitor the MSLP's impact on the economic recovery and employment broadly.

Given these statements by Chair Powell and Secretary Mnuchin, it is clear to the Commission they are not going to impose mandatory payroll requirements on businesses that borrow through

---

[39] *See, e.g.*, Board of Governors of the Federal Reserve System, Main Street New Loan Facility Term Sheet, June 8, 2020, https://www.federalreserve.gov/newsevents/pressreleases/files/monetary20200608a1.pdf.

[40] In the letter, the Treasury and the Federal Reserve stated that the MSLP "expects borrowers to make commercially reasonable efforts to maintain payrolls." Appendix B at 10.

[41] *Id.*

[42] Former Federal Reserve officials have also made this same point. Jeremy Stein, chairman of the Harvard University economics department and a former Federal Reserve governor, stated, "You can't expect companies to borrow to pay employees." Similarly, Mark Carey, a former Federal Reserve staff member, has stated, "To go to great lengths to make companies keep employees that they don't need, in light of new expectations that economic activity will remain below pre-Covid levels for a long while, doesn't make sense." Bob Ivry, et al., *Fed Vow Boosts Debt Binge as Borrowers Cut Thousands of Jobs*, Bloomberg, June 5, 2020, at https://www.bloomberg.com/news/articles/2020-06-05/fed-vow-boosts-debt-binge-while-borrowers-cut-thousands-of-jobs.

the MSLP unless Congress mandates it in new legislation. Congress previously considered but chose not to require the Treasury and the Federal Reserve to impose such requirements on the Federal Reserve's lending facilities as part of the CARES Act. For example, Section 4003(c)(3)(D) of the CARES Act describes a potential lending facility to mid-sized businesses that would impose payroll requirements.[43] Congress did not require the Federal Reserve to establish this facility. In contrast, Congress did mandate that certain Treasury and SBA grant and loan programs established by the CARES Act impose payroll requirements on businesses.

The Commission will continue to closely monitor this facility and seek to gather additional information about the credit needs of small and medium-sized businesses. In the coming weeks, the Commission plans to hold a hearing about the MSLP, at which we intend to inquire about the efficacy and utilization of the facility.

State and Local Governments

As with small and medium-sized businesses, our last report noted there was less evidence, so far, that the actions of the Treasury and the Federal Reserve have been as beneficial for state and local governments as they have been for larger companies that can access the capital markets. As of July 15, 2020, the facility intended to help state and local governments manage cash flow problems relating to the COVID-19 crisis—the MLF—has made a single purchase of $1.2 billion in notes from Illinois. However, at least two other states—New Jersey and Hawaii—are reportedly planning to utilize the MLF.[44] Some commentators have attributed the current low utilization of the MLF to the fact that it often charges interest rates above rates currently available in the municipal bond market, and it does not purchase notes with maturities greater than three years. One analysis of the potential value of the MLF to New Jersey found the facility could provide the state with significantly more capacity to borrow and spend if its repayment term were longer than three years.[45]

In their written answers to the Commission's questions, the Treasury and Federal Reserve provided their rationale for the design of this facility. They stated the "Federal Reserve established the MLF in response to rapid deterioration in the municipal securities market at a time when it appeared unlikely that the short-term municipal securities market could fully meet

[43] CARES Act, Pub. L. No. 116-136, § 4003(c)(3)(D), 134 Stat. 281 (2020).
[44] Karen Pierog, *Cash-strapped New Jersey to borrow up to $9.9 billion under deal*, Reuters, July 10, 2020, https://www.reuters.com/article/us-health-coronavirus-newjersey-debt/cash-strapped-new-jersey-to-borrow-up-to-9-9-billion-under-deal-idUSKBN24B307; Kevin Dayton, *Gov. Ige warns that without more federal aid, Hawaii public worker pay cuts or furloughs are inevitable*, Honolulu Star Advertiser, July 5, 2020, https://www.staradvertiser.com/2020/07/05/hawaii-news/gov-ige-warns-that-without-more-federal-aid-public-worker-pay-cuts-or-furloughs-are-inevitable/.
[45] Gregg Mennis & Ben Henken, *New Jersey Considers Tapping New Fed Borrowing Program to Meet Pension Contributions,* Pew Charitable Trusts, July 15, 2020, https://www.pewtrusts.org/en/research-and-analysis/articles/2020/07/15/new-jersey-considers-tapping-new-fed-borrowing-program-to-meet-pension-contributions.

the demand for short-term municipal note issuance."[46] According to the agencies, the "MLF was designed as a short-term lending program to provide bridge financing to states, localities, and their subdivisions or other governmental entities facing sudden disruptions in their short-term cash flows as a result of the COVID-19 pandemic."[47] In their view, it "was not designed to provide long-term financing for capital infrastructure projects because the long-term municipal capital markets appear to have been disrupted for only a relatively short period."[48]

At our June 24, 2020 meeting, the Commission also questioned Secretary Mnuchin and Chair Powell about the design of the MLF and its low utilization among state and local governments. Their responses were consistent with the written answers they later provided to us in their June 29, 2020 letter. They emphasized that the goal of the MLF is only to provide short-term liquidity for state and local governments, not to fund their long-term spending. As to the facility's low utilization, they pointed to the fact that conditions in the municipal bond market have improved significantly, and Illinois, in fact, was able to obtain most of its financing in that market. They also noted they are not trying to compete with the municipal bond market in terms of interest rates. In their view, the MLF is a backstop and a lender of last resort if the municipal bond market is not functioning. If the market improves, in part because of the backstop the MLF provides, and state and local governments can access credit through the market, they do not view it as a problem that the MLF has a low utilization.

There is evidence that the Federal Reserve's actions, including the announcement of the MLF, have helped to improve conditions in the municipal bond market. In a recent report, economists at the Federal Reserve Bank of New York concluded that market conditions for municipal securities have improved significantly in the wake of the Federal Reserve's actions: "[Y]ields for most issuers have receded to below pre-pandemic levels, outflows from municipal bond mutual funds have turned into inflows, and issuance has picked up."[49] In fact, the $48.6 billion in new municipal bonds issued in June 2020 was the highest monthly municipal bond issuance in eight months and was a 63% increase over issuance in May 2020.[50]

The report also noted that "improvements in muni debt markets are not necessarily sufficient to induce willingness to spend at the local level." [51] The economists noted that, unlike corporations, state and local governments "typically operate under balanced budget requirements, which

---

[46] Appendix C at 15.
[47] *Id.*
[48] *Id.*
[49] Marco Cipriani, et al., *Municipal Debt Markets and the COVID-19 Pandemic*, Liberty Street Economics, June 29, 2020, https://libertystreeteconomics.newyorkfed.org/2020/06/municipal-debt-markets-and-the-covid-19-pandemic.html.
[50] Securities Industry and Financial Markets Association, *US Municipal Issuance*, July 2, 2020, https://www.sifma.org/wp-content/uploads/2017/06/municipal-us-municipal-issuance-sifma.xls.
[51] Marco Cipriani, et al., *Municipal Debt Markets and the COVID-19 Pandemic*, Liberty Street Economics, June 29, 2020, https://libertystreeteconomics.newyorkfed.org/2020/06/municipal-debt-markets-and-the-covid-19-pandemic.html.

constrain or even prohibit the financing of deficits across fiscal years."[52]As a result, the report noted that "[h]istorically, state and local governments respond to recessions by drawing down on rainy day reserves, cutting expenses, and temporarily raising revenues" and that such steps "reflect sound fiscal policies" even though they are "contractionary from a macroeconomic perspective."[53] The report also indicated that the federal government has responded "with significant fiscal support for state and local governments" during the COVID-19 crisis, including $150 billion by way of the Coronavirus Relief Fund, established through the CARES Act.[54] Still, it noted that "[m]ost state and local governments are currently developing their 2021 budgets with the expectation of additional federal fiscal support that would limit the extent of budgetary retrenchment and deficit borrowing."[55] The report also concluded that "conditions remain strained relative to the start of the year, especially given the uncertainty about the path of the COVID-19 pandemic, its impact on economic recovery, and the degree of fiscal support from the federal government following the significant revenue losses experienced by state and local governments."[56]

As the Treasury and the Federal Reserve have made clear, the MLF is intended to help state and local governments with temporary cash flow needs and not longer-term financing problems that might arise from the impact of COVID-19 on the economy or from some governments' long-standing precarious financial situations. While there is mixed evidence about the severity of those longer-term financing problems,[57] many local governments have built up reserves they could draw upon now,[58] and Congress has already provided some federal aid to state and local governments (including, but not limited to, the $150 billion Coronavirus Relief Fund and $121 billion in various other programs),[59] it is evident the MLF, as currently designed, is not a tool for

---

[52] *Id.*
[53] *Id.*
[54] *Id.*
[55] *Id.*
[56] *Id.*
[57] Marco Cipriani, et al., *Municipal Debt Markets and the COVID-19 Pandemic*, Liberty Street Economics, June 29, 2020, https://libertystreeteconomics.newyorkfed.org/2020/06/municipal-debt-markets-and-the-covid-19-pandemic.html.
[58] A recent report noted: "Fortunately, many local governments have used the last decade to slowly build up reserves and rainy day funds, and have access to a pool (but often still limited) of capital. As of 2019, according to Moody's [Municipal Finance Ratio Analysis (MFRA)], the median US County's unreserved, undesignated operational fund balance covered 39% of revenues, a multi-decade historical high." JP Morgan, *Municipal Markets Weekly*, June 12, 2020, at 13.
[59] The CARES Act provided state and local governments $150 billion for the Coronavirus Relief Fund, $30 billion for education, $25 billion for public transportation, $11 billion for COVID-19 testing, and $5 billion for community development grants. The Families First Coronavirus Response Act, which was enacted on March 18, 2020, increased federal Medicaid funding for states by an estimated $50 billion. Pub. L. No. 116–127, 134 Stat. 178 (2020); Letter from Phillip L. Swagel, Director, Congressional Budget Office to U.S. Representative Nita Lowey, Apr. 2, 2020, https://www.cbo.gov/system/files/2020-04/HR6201.pdf.

addressing longer-term state and local government financing issues stretching beyond three years.

Airline Industry and National Security Businesses

At the time of our last report, the Treasury had not made any loans to the airline industry or businesses critical to maintaining national security under Subtitle A. In response to the Commission's questions, the agencies have indicated that, as of June 16, 2020, the Treasury has received 190 applications for such airline industry loans. They also indicated that, as of June 17, 2020, the Treasury has "received 70 applications for the national security loan program, 25 of which meet one of the two national security eligibility criteria established by Treasury," although one of those applications has been withdrawn.[60]

The most significant development with this lending program is the Treasury loan of $700 million to YRC Worldwide Inc. (YRC) under the national security loan program. In the third section of this report, we describe the terms of the loan and provide detailed information about YRC. In short, YRC provides transportation and logistics services, including to the U.S. Department of Defense (the "Defense Department").[61] The company specializes in less-than-truckload (LTL) shipping where smaller cargos from multiple customers are combined on one trailer.[62] According to the Treasury, YRC "provides 68% of less-than-truckload services to the Defense Department."[63]

The Treasury has defined a "business critical to maintaining national security" as a business that is at the time of its application performing under a defense contract of the highest national priority or operating under a top secret facility security clearance.[64] YRC apparently did not meet either of the two national security eligibility criteria. However, YRC qualified for the program under a catch-all provision created by the Treasury allowing it to determine if a business is critical to maintaining national security based solely on a recommendation and certification from the Secretary of Defense or the Director of National Intelligence.

---

[60] Appendix C at 16.

[61] YRC and its operating companies employ 30,000 people, including 24,000 members of the International Brotherhood of Teamsters. YRC Worldwide Inc., *YRC Worldwide Expects To Receive $700 Million CARES Act Loan from U.S. Treasury*, July 1, 2020, http://investors.YRC.com/news-releases/news-release-details/yrc-worldwide-expects-receive-700-million-cares-act-loan-us.

[62] YRC Worldwide Inc., *Annual Report (Form 10-K)*, March 11, 2020, http://investors.YRC.com/static-files/8092f183-eb4b-4ba7-bae2-fb4afc4f3e25.

[63] U.S. Department of the Treasury, *Treasury to Provide Loan to YRC Worldwide*, July 1, 2020, https://home.treasury.gov/news/press-releases/sm1049.

[64] U.S. Department of the Treasury, *Q&A: Loans to Air Carriers and Eligible Businesses and National Security Businesses,* Apr. 10, 2020, https://home.treasury.gov/system/files/136/CARES-Airline-Loan-Support-Q-and-A-national-security.pdf; Defense Contract Management Agency, *Defense Priorities & Allocations System (DPAS),* May 7, 2019, https://www.dcma.mil/DPAS/ ("A DX rating is assigned to those programs of the highest national priority").

The Commission has questions about the decision to deem YRC a business critical to maintaining national security and the process for reaching that conclusion. Secretary Mnuchin has publicly stated that the national security loan program was developed with the thought that Boeing and General Electric might need loans.[65] Given the types of sophisticated services and products these two companies provide for our national defense, it is not hard to argue that they are critical to maintaining national security. It is far from clear that the fourth-largest LTL shipping company in the United States is critical to maintaining national defense because it reportedly delivers "food, electronics and other supplies to military locations around the country."[66] The Commission intends to conduct further oversight of this decision.

The Commission intends to explore the decision to designate YRC as critical to maintaining national security, in part, because the risk of loss of U.S. taxpayer money on this loan appears high. In fact, the Commission notes that the level of risk taken in the loan to YRC appears strikingly higher than the risks associated with the other facilities over which the Commission has oversight. YRC has been rated non-investment grade for over a decade, struggled financially for years before the COVID-19 crisis, and was at risk of bankruptcy before it obtained a loan from the Treasury.[67] Under the CARES Act, a Treasury loan like this one is supposed to be "sufficiently secured" or "made at a rate" that "reflects the risk of the loan" and "is to the extent practicable, not less than an interest rate based on market conditions for comparable obligations prevalent prior to the outbreak of the coronavirus disease 2019 (COVID–19)."[68] It is questionable whether the loan to YRC meets these standards. The interest rate on YRC's loan from the Treasury is 4% lower than the interest rate on the company's most recent debt financing, which was a five-year, $600 million term loan that YRC obtained in September 2019 before the COVID-19 crisis.[69] As part of the loan agreement, the Treasury has obtained a 29.6% equity stake in YRC to reportedly provide "appropriate taxpayer compensation" for the loan.[70] But given the company's long-term non-investment grade rating and previous close calls with

---

[65] Saleha Mohsin, *Mnuchin May Ease Rules for $17 Billion Security Funds,* Bloomberg, June 11, 2020, https://www.bloomberg.com/news/articles/2020-06-11/mnuchin-says-he-may-ease-rules-for-17-billion-security-stimulus.

[66] Kate Davidson & Jennifer Smith, *U.S. Treasury to Lend $700 Million to Trucking Firm YRC Worldwide*, Wall Street Journal, July 1, 2020, https://www.wsj.com/articles/u-s-treasury-to-loan-700-million-to-trucking-firm-yrc-worldwide-11593602409.

[67] Moody's Investors Services, YRC Worldwide Inc. Ratings, https://www.moodys.com/credit-ratings/YRC-Worldwide-Inc-credit-rating-834015 (last visited July 14, 2020); Jennifer Smith, *Truckers Cut Spending as Factory Slowdown Weighs on Operators*, Wall Street Journal, April 7, 2020, https://www.wsj.com/articles/truckers-cut-spending-as-factory-slowdown-weighs-on-some-operators-11586295247; Standard & Poor's, *U.S.-Based YRC Worldwide Inc. Downgraded To 'CCC' On Anticipated Covenant Violation, Outlook Negative*, May 28, 2020, https://www.standardandpoors.com/en_US/web/guest/article/-/view/type/HTML/id/2450913.

[68] CARES Act, Pub. L. No. 116-136, § 4003(c)(2)(C), 134 Stat. 281 (2020).

[69] YRC Worldwide Inc., *Current Report (Form 8-K)*, Sept. 11, 2019, http://investors.YRC.com/static-files/14d3a39a-13af-4e5f-80fc-bcad38b120f2.

[70] U.S. Department of the Treasury, *Treasury to Provide Loan to YRC Worldwide*, July 1, 2020, https://home.treasury.gov/news/press-releases/sm1049.

bankruptcy over the years, it is not clear that an equity stake in YRC will provide much, if any, compensation or protection to taxpayers.[71]

This loan may indicate that the Treasury believes the national security designation permits a much higher risk tolerance to provide relief to firms that were struggling well before the COVID-19 pandemic. If that is the case, the Commission would like to better understand the rationale for this risk tolerance, especially in light of the statutory restrictions on national security loan terms and the fact that the single such loan the Treasury has made—to date—is to a company that may not be critical to maintaining national security.

---

[71] David Twiddy, *YRC Worldwide misses restructuring milestone, warns of bankruptcy potential*, Kansas City Business Journal, March 15, 2011, https://www.bizjournals.com/kansascity/news/2011/03/15/yrc-worldwide-misses-restructuring.html; David Twiddy, *YRC Worldwide bondholders approve debt-for-equity swap*, Kansas City Business Journal, Dec. 31, 2009, https://www.bizjournals.com/kansascity/stories/2009/12/28/daily22.html.

TREASURY AND FEDERAL RESERVE RECENT DEVELOPMENTS

In June and July 2020, the Treasury and the Federal Reserve took a number of actions under Division A, Title IV, Subtitle A of the CARES Act. We describe the key recent developments below.

Primary Market Corporate Credit Facility (PMCCF)

The PMCCF is intended to support credit to businesses by serving as a "funding backstop" for corporate debt.[72] The Federal Reserve, through a special purpose vehicle (SPV), will be the sole purchaser of newly issued corporate bonds or purchase portions of bonds or syndicated loans, at issuance, from corporations rated investment grade as of March 22, 2020 that maintain at least a BB-/Ba3 rating.[73] The Treasury intends to make a total equity investment of $75 billion in the PMCCF and the SMCCF, which can support up to $750 billion in purchases through both facilities.[74] As of July 15, 2020, the Treasury has invested $37.5 billion in the SPV it uses for the PMCCF and SMCCF.[75]

On June 29, 2020, the PMCCF became operational and available for use by eligible businesses.[76] That same day the Federal Reserve Bank of New York released an updated term sheet for the PMCCF and several forms eligible businesses must complete to borrow under the PMCCF, including forms to certify compliance with the CARES Act's U.S. business and conflict of interest requirements.[77]

Two weeks before the PMCCF became operational, on June 16, 2020, Chair Powell told the Senate Banking Committee that "so far" the Federal Reserve had seen "no demand" for the

---

[72] Board of Governors of the Federal Reserve System, *Primary Market Corporate Credit Facility Term Sheet*, Apr. 9, 2020, https://www.federalreserve.gov/newsevents/pressreleases/files/monetary20200409a5.pdf.
[73] *Id.*
[74] *Id.*
[75] Board of Governors of the Federal Reserve System, Statistical Release H.4.1, *Factors Affecting Reserve Balances of the Depository Institutions and Condition Statement of Federal Reserve Banks*, July 16, 2020, https://www.federalreserve.gov/releases/h41/ (to access click on hyperlink for July 16, 2020 release). The SPV for the PMCCF and SMCCF is Corporate Credit Facilities LLC (CCFL). Footnote 14 to table 1 in the H.4.1 statistical release dated July 16, 2020 indicates that the Treasury has made a $37.5 billion equity investment in the CCFL.
[76] Federal Reserve Bank of New York, *New York Fed Announces Primary Market Corporate Credit Facility Launches on June 29*, June 29, 2020, https://www.newyorkfed.org/newsevents/news/markets/2020/20200629.
[77] Federal Reserve Bank of New York, *New York Fed Announces Primary Market Corporate Credit Facility Launches on June 29*, June 29, 2020, https://www.newyorkfed.org/newsevents/news/markets/2020/20200629.

PMCCF.[78] He attributed the lack of demand to the fact that market functioning in the corporate bond market "has improved really substantially."[79] As of July 15, 2020, the Federal Reserve had not announced that the PMCCF had actually purchased any bonds or syndicated loans.

Secondary Market Corporate Credit Facility (SMCCF)

The SMCCF is intended to support credit to businesses by providing liquidity to the market for outstanding corporate bonds. The Federal Reserve, through an SPV, purchases on the secondary market individual corporate bonds issued by corporations rated investment grade as of March 22, 2020 that maintain at least a BB-/Ba3 rating, as well as U.S.-listed exchange-traded funds (ETFs) that themselves invest in a broad range of corporate bonds. As mentioned, the Treasury intends to invest a total of $75 billion in the PMCCF and the SMCCF, which can support up to $750 billion in purchases.

The SMCCF began purchasing bond ETFs on May 12, 2020 and, on June 16, 2020, the SMCCF began purchasing *individual* corporate bonds, which the Federal Reserve considers a better tool for fulfilling the facility's goals.[80] The Federal Reserve has stated the SMCCF is initially purchasing individual "corporate bonds to create a corporate bond portfolio that is based on a broad, diversified index of U.S. corporate bonds."[81] According to the Federal Reserve, this "indexing approach will complement the [SMCCF's] current purchases of [ETFs]."[82] In the future, the SMCCF may purchase individual corporate bonds using other methodologies.[83]

---

[78] U.S. Senate Banking, Housing, and Urban Affairs Committee hearing on the Quarterly CARES Act Report to Congress, 116th Cong. (June 16, 2020) (statement of Jerome Powell, Chair, Board of Governors of the Federal Reserve).
[79] *Id.*
[80] Federal Reserve Bank of New York, *New York Fed Announces Start of Certain Secondary Market Purchases on May 12,* May 11, 2020, https://www.newyorkfed.org/newsevents/news/markets/2020/20200511; Board of Governors of the Federal Reserve System, *Federal Reserve Board announces updates to Secondary Market Corporate Credit Facility (SMCCF), which will begin buying a broad and diversified portfolio of corporate bonds to support market liquidity and the availability of credit for large employers*, June 15, 2020, https://www.federalreserve.gov/newsevents/pressreleases/monetary20200615a.htm.
[81] Board of Governors of the Federal Reserve System, *Federal Reserve Board announces updates to Secondary Market Corporate Credit Facility (SMCCF), which will begin buying a broad and diversified portfolio of corporate bonds to support market liquidity and the availability of credit for large employers*, June 15, 2020, https://www.federalreserve.gov/newsevents/pressreleases/monetary20200615a.htm.
[82] Board of Governors of the Federal Reserve System, *Federal Reserve Board announces updates to Secondary Market Corporate Credit Facility (SMCCF), which will begin buying a broad and diversified portfolio of corporate bonds to support market liquidity and the availability of credit for large employers*, June 15, 2020, https://www.federalreserve.gov/newsevents/pressreleases/monetary20200615a.htm.
[83] Federal Reserve Bank of New York, *FAQs: Primary Market Corporate Credit Facility and Secondary Market Corporate Credit Facility,* June 29, 2020, https://www.newyorkfed.org/markets/primary-and-secondary-market-faq/corporate-credit-facility-faq.

On June 17, 2020, Chair Powell testified before the House Financial Services Committee about the SMCCF's bond buying. He stated that purchasing individual corporate bonds is "going to form the primary mode of support over time . . . by which we support market function."[84] He stated that "[o]ver time, we'll gradually move away from ETFs." According to Chair Powell, buying individual corporate bonds is "a better tool ultimately for supporting liquidity and market function." He stated that "markets are functioning pretty well" and "as those markets continue to normalize, our purchases will decline." The day before, on June 16, 2020, Chair Powell stated at a Senate Banking Committee hearing that if there was a deterioration in market functioning, the SMCCF's purchases would increase.[85] In addition, he noted that even though the corporate bond market is currently functioning pretty well, the Federal Reserve decided, in part, to begin buying individual corporate bonds with the SMCCF in order to maintain its credibility with market participants by following through on its previously announced plan to buy such bonds.[86]

Since May 12, 2020, the Federal Reserve has submitted three periodic reports about the SMCCF to the Senate Banking Committee and the House Financial Services Committee that disclose details about the facility's purchases of bond ETFs and individual corporate bonds.[87] Our analysis of these reports shows that from May 12, 2020, when the SMCCF began purchasing bond ETFs, through June 15, 2020, the day before the SMCCF began purchasing individual corporate bonds, the SMCCF purchased an average of $273 million of bond ETFs per day. During that time period, the highest daily purchase amount was $365 million on June 12, 2020, and the lowest daily purchase amount was $190 million on May 19, 2020. Since the SMCCF began purchasing individual bonds on June 16, 2020 through June 29, 2020, the facility's average daily amount of bond ETF purchases declined to $134 million. The lowest daily purchase amount during that period was $67 million on June 29, 2020 and the highest daily purchase amount was $207 million on June 19, 2020.[88]

Consistent with Chair Powell's testimony, these reports show the SMCCF has begun to shift its bond buying from ETFs to individual corporate bonds. From June 16, 2020 through June 29, 2020, the SMCCF purchased an average of $165 million of individual corporate bonds per day. During that time period, the highest daily purchase amount of individual bonds was $227 million

---

[84] U.S. House Financial Services Committee hearing on Monetary Policy and the State of the Economy, 116th Cong. (June 17, 2020) (statement of Jerome Powell, Chair, Board of Governors of the Federal Reserve).
[85] U.S. Senate Banking, Housing, and Urban Affairs Committee hearing on the Quarterly CARES Act Report to Congress, 116th Cong. (June 16, 2020) (statement of Jerome Powell, Chair, Board of Governors of the Federal Reserve).
[86] *Id.*
[87] Board of Governors of the Federal Reserve System, *Periodic Report: Update on Outstanding Lending Facilities Authorized by the Board under Section 13(3) of the Federal Reserve Act,* May 28, 2020, https://www.federalreserve.gov/files/pmccf-smccf-talf-5-29-20.pdf#page=2.
[88] This analysis is based on the Federal Reserve's July 10, 2020, June 28, 2020, and May 29, 2020 transaction-specific disclosures for the SMCCF, which are available at https://www.federalreserve.gov/publications/reports-to-congress-in-response-to-covid-19.htm.

on June 16, 2020 and the lowest daily purchase amount was $155 million on June 19, 2020. The total average daily purchase amount of both bond ETFs and individual corporate bonds during that period was $310 million.[89]

On July 8, 2020, the Executive Vice President of the Federal Reserve Bank of New York, Daleep Singh, stated the SMCCF has "slowed the pace of purchases, from about $300 million per day to a bit under $200 million a day."[90] To put the size of those purchases into context, he noted that "$300 million of ETF purchases a day represented about 10 percent of average daily volumes for ETFs that were eligible for purchase at the time."[91] Similarly, he stated that the SMCCF's daily purchases of "a bit under $200 million a day across ETFs and cash bonds" represent "around 5 percent of the average daily volume of eligible cash bonds, and less than 1 percent of ETF average daily volume."[92] Like Chair Powell, Mr. Singh stated: "If market conditions continue to improve, Fed purchases could slow further, potentially reaching very low levels or stopping entirely. This would not be a signal that the SMCCF's doors were closed, but rather that markets are functioning well. Should conditions deteriorate, purchases would increase."[93]

As of June 29, 2020, the SMCCF had purchased more than 500 individual corporate bonds from more than 300 different issuers. The purchase amount for these bonds was $1.76 billion.[94] The chart below lists the SMCCF's ten largest individual bond holdings by issuer, as of June 29, 2020.[95] The bonds of these ten issuers make up 13% of the SMCCF's total individual bond holdings.

---

[89] *Id.*

[90] Daleep Singh, *The Fed's Emergency Facilities: Usage, Impact, and Early Lessons,* remarks at Hudson Valley Pattern for Progress, July 8, https://www.newyorkfed.org/newsevents/speeches/2020/sin200708.

[91] *Id.*

[92] *Id.*

[93] *Id.*

[94] Board of Governors of the Federal Reserve System, *Periodic Report: Update on Outstanding Lending Facilities Authorized by the Board under Section 13(3) of the Federal Reserve Act (Transaction-specific Disclosures),* June 28, 2020, https://www.federalreserve.gov/publications/files/smccf-transition-specific-disclosures-6-28-20.xlsx; Board of Governors of the Federal Reserve System, *Periodic Report: Update on Outstanding Lending Facilities Authorized by the Board under Section 13(3) of the Federal Reserve Act (Transaction-specific Disclosures),* July 10, 2020, https://www.federalreserve.gov/publications/files/smccf-transaction-specific-disclosures-7-10-20.xlsx.

[95] This chart was compiled using data in the Federal Reserve's June 28, 2020 and July 10, 2020 transaction-specific disclosures for the SMCCF. Board of Governors of the Federal Reserve System, *Periodic Report: Update on Outstanding Lending Facilities Authorized by the Board under Section 13(3) of the Federal Reserve Act (Transaction-specific Disclosures),* June 28, 2020, https://www.federalreserve.gov/publications/files/smccf-transition-specific-disclosures-6-28-20.xlsx; Board of Governors of the Federal Reserve System, *Periodic Report: Update on Outstanding Lending Facilities Authorized by the Board under Section 13(3) of the Federal Reserve Act (Transaction-specific Disclosures),* July 10, 2020, https://www.federalreserve.gov/publications/files/smccf-transaction-specific-disclosures-7-10-20.xlsx.

Issuer	Sector	Par Value of Bonds (U.S. $)	Percentage of SMCCF's Individual Bond Holdings (as of 6/29/20)
AT&T Inc.	Communications	$30,500,000	1.85%
Volkswagen Group America	Consumer Cyclical	$26,500,000	1.61%
Verizon Communications	Communications	$25,000,000	1.52%
Apple Inc.	Technology	$25,000,000	1.52%
General Electric Co.	Capital Goods	$24,000,000	1.46%
Toyota Motor Credit Corp.	Consumer Cyclical	$24,000,000	1.46%
Daimler Finance NA LLC	Consumer Cyclical	$23,000,000	1.40%
General Motors Financial Co.	Consumer Cyclical	$22,000,000	1.33%
Comcast Corp.	Communications	$20,000,000	1.21%

As of June 29, 2020, the SMCCF had purchased close to 107 million shares in sixteen ETFs, of which eleven were investment grade ETFs and six were non-investment grade ETFs. Of these shares, 12.9% were in non-investment grade ETFs and 86.1% were in investment grade ETFs. The market value of these shares was $8 billion as of June 29, 2020.[96] We calculate the SMCCF had an unrealized gain of $74 million on its ETF purchases as of that date.

The chart below lists the names of the bond ETFs that the SMCCF has purchased, the number of shares purchased, and the market value of those shares as of June 29, 2020.[97]

Name of ETF	Shares Purchased (as of 6/29/20)	Cost Basis (U.S. $)	Market Value as of 6/29/20 (U.S. $)
iShares iBoxx US Dollar Investment Grade Corporate Bond ETF (LQD)	16,965,351	$2,227,773,016	$2,275,392,876
Vanguard Short-Term Corporate Bond ETF (VCSH)	18,007,435	$1,475,086,310	$1,487,414,131
Vanguard Intermediate-Term Corporate Bond ETF (VCIT)	13,102,944	$1,220,988,700	$1,244,124,532
iShares Short-Term Corporate Bond ETF (IGSB)	12,218,042	$662,449,950	$668,571,258
SPDR Portfolio Intermediate Term Corporate Bond ETF (SPIB)	13,045,200	$468,458,987	$475,627,992
SPDR Bloomberg Barclays High Yield Bond ETF (JNK)	4,644,986	$468,180,579	$465,102,448

[96] Board of Governors of the Federal Reserve System, *Periodic Report: Update on Outstanding Lending Facilities Authorized by the Board under Section 13(3) of the Federal Reserve Act (Transaction-specific Disclosures),* July 10, 2020, https://www.federalreserve.gov/publications/files/smccf-transaction-specific-disclosures-7-10-20.xlsx.
[97] *Id.*

Name of ETF	Shares Purchased (as of 6/29/20)	Cost Basis (U.S. $)	Market Value as of 6/29/20 (U.S. $)
iShares Intermediate-Term Corporate Bond ETF (IGIB)	7,229,491	$428,127,220	$434,492,409
iShares iBoxx High Yield Corporate Bond ETF (HYG)	3,434,502	$278,160,583	$277,782,521
SPDR Portfolio Short Term Corporate Bond ETF (SPSB)	8,831,593	$275,314,736	$276,605,492
iShares Broad US Dollar Investment Grade Corporate Bond ETF (USIG)	2,719,912	$160,266,222	$163,738,702
Xtrackers US Dollar High Yield Corporate Bond ETF (HYLB)	1,435,025	$66,888,341	$66,412,957
iShares Broad US Dollar High Yield Corporate Bond ETF (USHY)	1,387,688	$52,696,559	$52,426,852
iShares 0-5 Year Investment Grade Corporate Bond ETF (SLQD)	841,975	$43,490,249	$43,866,897
SPDR Bloomberg Barclays Short Term High Yield Bond ETF (SJNK)	1,220,506	$31,065,310	$30,463,829
VanEck Vectors Fallen Angel High Yield Bond ETF (ANGL)	1,057,195	$29,314,191	$29,918,618
iShares 0-5 Year High Yield Corporate Bond ETF (SHYG)	606,927	$25,693,745	$25,782,258

The Federal Reserve also provides weekly disclosures of the value of the bond ETFs and individual corporate bonds owned by the SPV for the SMCCF and PMCCF. The most recent disclosure indicates that SPV owns $11.4 billion worth of bond ETFs and individual corporate bonds as of July 15, 2020.[98]

<u>Main Street Lending Program (MSLP)</u>

The MSLP is intended to facilitate lending by banks to small and medium-sized businesses. Businesses with up to 15,000 employees or up to $5 billion in 2019 annual revenues are eligible to receive loans under this program. The MSLP currently consists of three facilities: the Main Street New Lending Facility (MSNLF), the Main Street Priority Loan Facility (MSPLF), and the Main Street Expanded Loan Facility (MSELF). The Federal Reserve has decided to expand the MSLP to include two facilities to provide loans to certain nonprofit organizations. The Treasury

---

[98] Board of Governors of the Federal Reserve System, Statistical Release H.4.1, *Factors Affecting Reserve Balances of the Depository Institutions and Condition Statement of Federal Reserve Banks*, July 16, 2020, at Table 4, https://www.federalreserve.gov/releases/h41/ (to access click on hyperlink for July 16, 2020 release).

has announced it intends to make an equity investment of $75 billion in the MSLP. Collectively, the facilities can support up to $600 billion in lending.[99]

On June 15, 2020, the Federal Reserve Bank of Boston, which administers the MSLP, began accepting applications from lenders to participate in the program and announced that the program would begin buying loans soon.[100] On June 19, 2020, the president of the Federal Reserve Bank of Boston, Eric Rosengren, stated that more than 200 lenders had begun the registration process.[101] He also stated that interest in the MSLP from businesses was "tremendous" and that he "anticipate[d] plenty of borrowers and plenty of banks participating in the program as it continues to roll out."[102]

Later in the month, on June 30, 2020, Chair Powell testified before the House Financial Services Committee that approximately 300 lenders had registered or were in the process of registering to participate in the MSLP.[103] He also stated that banks were telling the Federal Reserve that they were "not getting a ton of interest from borrowers" for the MSLP. However, he noted that many banks have told the Federal Reserve that they expect that will change "over the course of the next few months" and that "demand from borrowers will . . . increase."[104] Chair Powell stated that as the MSLP "fully comes online" the Federal Reserve would continue "to look to see whether there are ways that we can improve it" and that it was "open to . . . making adjustments going forward."[105]

On July 1, 2020, after receiving a request from the Commission, the Federal Reserve released over one thousand pages of public comments it received from April 9, 2020 through April 30, 2020 regarding the MSNLF and the MSELF. These comments, which are available on the Federal Reserve's website, come from a range of interested stakeholders, including lenders and borrowers.[106]

---

[99] Board of Governors of the Federal Reserve System, *Main Street New Loan Facility Term Sheet,* June 8, 2020, https://www.federalreserve.gov/newsevents/pressreleases/files/monetary20200608a1.pdf.

[100] Federal Reserve Bank of Boston, *Federal Reserve's Main Street Lending Program opens for lender registration*, June 15, 2020, https://www.bostonfed.org/news-and-events/press-releases/2020/federal-reserves-main-street-lending-program-opens-for-lender-registration.aspx.

[101] Christopher Condon & Catarina Saraiva, *Fed's Rosengren Expects Main Street Program to Build Over Time*, Bloomberg, June 19, 2020, https://www.bloomberg.com/news/articles/2020-06-19/fed-s-rosengren-outlines-dark-forecast-with-warning-over-virus?sref=hKSAni5g.

[102] *Id.*

[103] U.S. House Committee on Financial Services hearing on Coronavirus and the Cares Act, 116th Cong. (June 30, 2020) (statement of Jerome Powell, Chair, Board of Governors of the Federal Reserve).

[104] *Id.*

[105] *Id.*

[106] Ann Saphir, et al., *Fed deluged by letters from needy over U.S. loan program*, Reuters, July 1, 2020, https://www.reuters.com/article/us-usa-fed-mainstreet/fed-deluged-by-letters-from-needy-over-u-s-loan-program-idUSKBN242782. The comments are available on the Federal Reserve's website at https://www.federalreserve.gov/monetarypolicy/mainstreetlending.htm.

On July 6, 2020, the Federal Reserve Bank of Boston announced the MSLP was fully operational and ready to purchase eligible loans submitted by lenders registered to participate in the program.[107] Two days later, on July 8, 2020, the Federal Reserve Bank of Boston began listing on its website the names of certain registered lenders in the program. This list, which continues to be updated, reflects registered lenders by state "who are accepting [Main Street loan] applications from new business customers, in addition to existing ones; and also elect to be listed."[108] As of July 19, 2020, this list includes 130 lending institutions.[109] The Federal Reserve has not released the names of registered lenders who are accepting Main Street loan applications only from existing business customers.

The number of registered lenders on the Federal Reserve's list varies by state. As of July 19, Texas has the highest number of lenders on the list, with 18 lenders, and Florida, Illinois, Michigan, and New Jersey all tie for second, with 13 lenders each.[110] Hawaii and Puerto Rico each only have one lender listed. Among the nation's four largest banks, Bank of America is the only one included in the Federal Reserve's list. It is accepting applications from new business customers in all fifty states and the District of Columbia. The nation's three other largest banks—JPMorgan Chase, Wells Fargo, and Citigroup—have publicly indicated they have registered or plan to register for the program.[111] However, Citigroup has stated it will accept applications only from existing business customers.[112]

On July 17, 2020, the Federal Reserve announced that it was expanding the MSLP by establishing two facilities intended to support lending by banks to certain small and medium-sized nonprofit organizations.[113] These facilities—the Nonprofit Organization New Loan Facility (NONLF) and Nonprofit Organization Expanded Loan Facility (NOELF)—are available to certain nonprofit organizations with up to 15,000 employees or up to $5 billion in 2019

---

[107] Federal Reserve Bank of Boston, *Boston Fed announces Main Street Lending Program is Fully Operational,* July 6, 2020, https://www.bostonfed.org/news-and-events/press-releases/2020/boston-fed-announces-main-street-lending-program-is-fully-operational.aspx?utm_source=email-alert&utm_medium=email&utm_campaign=mslp&utm_content=pr-nc-200706.

[108] Federal Reserve Bank of Boston, *Information for Business Borrowers,* https://www.bostonfed.org/supervision-and-regulation/supervision/special-facilities/main-street-lending-program/information-for-borrowers.aspx (last visited on July 19, 2020).

[109] Federal Reserve Bank of Boston, *Information for Business Borrowers,* https://www.bostonfed.org/supervision-and-regulation/supervision/special-facilities/main-street-lending-program/information-for-borrowers.aspx (last visited on July 19, 2020).

[110] *Id.*

[111] Rachel Siegel, *Fed's Main Street lending program doesn't have many large banks making loans to new customers,* Washington Post, July 8, 2020, https://www.washingtonpost.com/business/2020/07/08/fed-main-street/.

[112] *Id.*

[113] Board of Governors of the Federal Reserve System, *Federal Reserve Board modifies Main Street Lending Program to provide greater access to credit for nonprofit organizations such as educational institutions, hospitals, and social service organizations*, July 17, 2020, https://www.federalreserve.gov/newsevents/pressreleases/monetary20200717a.htm.

revenues.[114] A month earlier, on June 15, the Federal Reserve had announced that it was seeking public feedback, until June 22, 2020, on its draft loan terms for these facilities.[115] Based on the public feedback the Federal Reserve received, it modified the terms of these facilities, including reducing the minimum employee size threshold for nonprofits from 50 employees to ten, and adjusting several financial eligibility criteria "to accommodate a wider range of nonprofit operating models."[116]

In general, the loan terms for the Main Street loans for nonprofit organizations are similar to those for Main Street loans for businesses, including the interest rate, principal and interest payment deferral, five-year loan term, and minimum and maximum loan sizes. Only a nonprofit organization that is a tax-exempt organization under section 501(c)(3) or 501(c)(19) of the Internal Revenue Code are eligible for NONLF and NOELF.[117] However, at the discretion of the Federal Reserve, "other forms of organization may be considered for inclusion as a Nonprofit Organization" under the facilities.[118]

The chart below shows the current key terms and conditions of the Main Street nonprofit organization facilities, as amended by the Federal Reserve's July 17, 2020 announcement.

---

[114] Board of Governors of the Federal Reserve System, *Nonprofit Organization New Loan Facility Term Sheet*, July 17, 2020, https://www.federalreserve.gov/newsevents/pressreleases/files/monetary20200717a2.pdf; Board of Governors of the Federal Reserve System, *Nonprofit Organization Expanded Loan Facility Term Sheet*, July 17, 2020, https://www.federalreserve.gov/newsevents/pressreleases/files/monetary20200717a1.pdf.
[115] Board of Governors of the Federal Reserve System, *Federal Reserve Board announces it will be seeking public feedback on proposal to expand its Main Street Lending Program to provide access to credit for nonprofit organizations*, June 15, 2020, https://www.federalreserve.gov/newsevents/pressreleases/monetary20200615b.htm.
[116] *Id*.
[117] Board of Governors of the Federal Reserve System, *Nonprofit Organization Expanded Loan Facility Draft Term Sheet*, June 15, 2020, https://www.federalreserve.gov/newsevents/pressreleases/files/monetary20200615b1.pdf.
[118] *Id*.

Proposed Main Street Nonprofit Loan Options	NONLF	NOELF
Type of Loan	New loans to borrowers	Expanded loans to existing borrowers
Term	5 years	
Minimum Loan Size	$250,000	$10 million
Endowment Cap	$3 billion	
Years in Operation	At least 5 years	
Eligibility Criteria	• Minimum number of employees 10 (previously 50) • Total non-donation revenues equal to or greater than 60% of expenses for the period from 2017 through 2019 (previously 70% of revenues) • 2019 operating margin of 2% or more (previously 5%) • Current days cash on hand 60 days (previously 90 days) • Current debt repayment capacity—ratio of cash, investments and other resources to outstanding debt and certain other liabilities—of greater than 55% (previously 65%)	
Maximum Loan Size	The lesser of $35 million, or the borrower's average 2019 quarterly revenue	The lesser of $300 million, or the borrower's average 2019 quarterly revenue
Lender's Risk Retention in Loan	5%	5%
Facilities Risk Retention in Loan	95%	95%
Principal Repayment Schedule	Principal deferred for 2 years. 15%, 15% and 70% principal repayment due in years 3, 4 and 5, respectively.	
Deferral of Interest Payments	Interest payments deferred for one year	
Loan Rate	London Interbank Offered Rate (LIBOR) + 3%	

As of July 15, 2020, the MSLP has purchased a single $12 million loan.[119] According to Secretary Mnuchin, this loan was "to doctors' offices consisting of 15 practices in Wisconsin."[120]

[119] Board of Governors of the Federal Reserve System, Statistical Release H.4.1, *Factors Affecting Reserve Balances of the Depository Institutions and Condition Statement of Federal Reserve Banks*, July 16, 2020, https://www.federalreserve.gov/releases/h41/ (to access click on hyperlink for July 16, 2020 release). The SPV for the MSLP is MS Facilities LLC (Main Street Lending Program); U.S. House Small Business Committee hearing on Oversight of the Small Business Administration and Department of Treasury Pandemic Programs, 116th Cong. (July 17, 2020) (statement of Steven Mnuchin, Secretary, U.S. Department of the Treasury).

[120] U.S. House Small Business Committee hearing on Oversight of the Small Business Administration and Department of Treasury Pandemic Programs, 116th Cong. (July 17, 2020) (statement of Steven Mnuchin, Secretary, U.S. Department of the Treasury).

The lender was a family-owned community bank.[121] Secretary Mnuchin also stated there's a $50 million construction loan "in the working" under the MSLP.[122]

Municipal Liquidity Facility (MLF)

The MLF is intended to help state and local governments manage cash flow problems relating to the COVID-19 crisis. The Federal Reserve, through an SPV, will purchase notes from U.S. states, including the District of Columbia, U.S. counties with a population of at least 500,000 residents, U.S. cities with a population of at least 250,000, and certain multistate entities. States may use the proceeds for the sales of these notes to support counties and cities. The Treasury has announced it intends to make an equity investment of $35 billion in this facility. The MLF can purchase up to $500 billion in notes.[123]

On May 19, 2020, Chair Powell testified before Congress that he expected the MLF to be operational by the end of May or the beginning of June.[124] The MLF became operational on May 26, 2020.[125]

On June 5, 2020, Illinois borrowed $1.2 billion from the MLF through the sale of one-year notes, making it the facility's first participant.[126] Illinois will pay an interest rate of 3.82% on these notes, which is more than a full percentage point less than the 4.875% interest rate it paid on comparable short-term notes during a public market sale in mid-May 2020.[127]

On June 29, 2020, economists at the Federal Reserve Bank of New York released a report concluding that "conditions in the municipal markets have improved significantly, in part [as] a result of the announcement and implementation" of several emergency lending facilities

---

[121] *Id.*
[122] *Id.*
[123] Board of Governors of the Federal Reserve, *Municipal Liquidity Facility Term Sheet,* June 3, 2020, https://www.federalreserve.gov/newsevents/pressreleases/files/monetary20200603a1.pdf; Federal Reserve Bank of New York, *FAQs: Municipal Liquidity Facility Term Sheet,* June 3, 2020, https://www.newyorkfed.org/markets/municipal-liquidity-facility/municipal-liquidity-facility-faq.
[124] U.S. Senate Banking, Housing, and Urban Affairs Committee hearing on the Quarterly CARES Act Report to Congress, 116th Cong. (May 19, 2020) (statement of Jerome Powell, Chair, Board of Governors of the Federal Reserve).
[125] Federal Reserve Bank of New York, *FAQs: Municipal Liquidity Facility*, June 3, 2020, https://www.newyorkfed.org/markets/municipal-liquidity-facility/municipal-liquidlity-facility-faq.
[126] Shruti Singh & Amanda Albright, *Illinois Becomes First to Tap Fed Loans After Yields Surge,* Bloomberg, June 2, 2020, https://www.bloomberg.com/news/articles/2020-06-02/illinois-becomes-first-to-tap-fed-loans-after-bond-yields-surge.
[127] *Id.; State of Illinois, General Obligation of Bonds, Series of May 2020,* May 2020, https://www2.illinois.gov/sites/capitalmarkets/Documents/Official%20Statements/2020/State%20of%20Illinois-General%20Obligation%20Bonds%20Series%20of%20May%202020-Official%20Statement.pdf.

established by the Federal Reserve, including the MLF.[128] The report notes that "both the primary and secondary markets for municipal securities underwent considerable stress during the early stages of the COVID-19 pandemic," including increased yields on bonds, significant outflows from municipal bond mutual funds, and decreased issuance of new municipal bonds.[129] In the wake of the Federal Reserve's actions, including the announcement of the MLF, the report concludes that "[m]arket conditions for municipal securities have improved significantly since then: yields for most issuers have receded to below pre-pandemic levels, outflows from municipal bond mutual funds have turned into inflows, and issuance has picked up."[130] According to the report, "[t]hese improvements in municipal market conditions help ensure that state and local governments have better access to funding."[131] Moreover, the report noted that "improvements in muni debt markets are not necessarily sufficient to induce willingness to spend at the local level." The economists noted that, unlike corporations, state and local governments "typically operate under balanced budget requirements, which constrain or even prohibit the financing of deficits across fiscal years."[132]

On July 5, 2020, the *Honolulu Star Advertiser* reported that Hawaii Governor David Ige stated his new financial plan for Hawaii, in response to the COVID-19 crisis, includes borrowing $750 million from the MLF, but that he is wary of borrowing more than that amount.[133] He noted that the cost of borrowing under the MLF "is very low" but said "once you get over $1 billion, it really is not that helpful because we've got to pay it back in such a short interval."[134]

On July 10, 2020, New Jersey Governor Phil Murphy announced that he had reached an agreement with New Jersey legislative leaders on a bill that if enacted would allow the state to issue up to $9.9 billion in bonds through the MLF or the public capital markets in response to the COVID-19 crisis.[135] He signed the bill into law on July 16, 2020.[136] According to Governor

---

[128] Marco Cipriani, et al., *Municipal Debt Markets and the COVID-19 Pandemic*, Liberty Street Economics, June 29, 2020, https://libertystreeteconomics.newyorkfed.org/2020/06/municipal-debt-markets-and-the-covid-19-pandemic.html.

[129] *Id.*

[130] *Id.*

[131] *Id.*

[132] *Id.*

[133] Kevin Dayton, *Gov. Ige warns that without more federal aid, Hawaii public worker pay cuts or furloughs are inevitable*, Honolulu Star Advertiser, July 5, 2020, https://www.staradvertiser.com/2020/07/05/hawaii-news/gov-ige-warns-that-without-more-federal-aid-public-worker-pay-cuts-or-furloughs-are-inevitable/.

[134] *Id.*

[135] Karen Pierog, *Cash-strapped New Jersey to borrow up to $9.9 billion under deal*, Reuters, July 10, 2020, https://www.reuters.com/article/us-health-coronavirus-newjersey-debt/cash-strapped-new-jersey-to-borrow-up-to-9-9-billion-under-deal-idUSKBN24B307.

[136] Stacey Barchenger & Dustin Racioppi, *Murphy approves $9.9B borrowing plan that taxpayers could be repaying for 35 years*, NorthJersey.com, July 16, 2020, https://www.northjersey.com/story/news/2020/07/16/nj-lawmakers-vote-billion-borrowing-plan-phil-murphy-backed/5436239002/.

Murphy's office, the MLF is "an option for a significant portion of the borrowing" authorized by the bill.[137] Governor Murphy has previously stated the MLF "is very attractive" for New Jersey."[138] On July 15, 2020, the Pew Charitable Trusts (Pew) released an article indicating the New Jersey legislature had asked Pew to conduct an analysis of the MLF and its potential value to New Jersey.[139] In that analysis, Pew found that "[h]igh borrowing costs, which include the [MLF's] penalty rate above the typical market rate, may limit widespread use of the MLF as anything other than a last resort." However, Pew reported that the "MLF pricing as of early July is favorable for New Jersey and Illinois, the two states with the lowest credit ratings and largest unfunded pension liabilities per capita."[140] Pew's analysis estimated that the MLF could provide New Jersey "additional budget capacity of approximately $1.4 billion under the current terms of the program, and up to $4.5 billion if terms were extended to allow for borrowing over five years instead of three."[141]

As of July 15, 2020, the MLF has made no additional loans beyond its $1.2 billion loan to the state of Illinois.[142]

Term Asset-Backed Securities Loan Facility (TALF)

The TALF is intended to facilitate the provision of credit to consumers and businesses by enabling the issuance of asset-backed securities (ABS) "backed by private student loans, auto loans and leases, consumer and corporate credit card receivables, certain loans guaranteed by the Small Business Administration (SBA), and certain other assets."[143] The Federal Reserve, through an SPV, will "make loans to U.S. companies secured by certain AAA-rated asset-backed securities (ABS) backed by recently originated consumer and business loans."[144] The Treasury

---

[137] *Id*.
[138] Office of New Jersey Governor Phil Murphy, *Transcript: May 1st, 2020 Coronavirus Briefing,* May 1, 2020, https://www.nj.gov/governor/news/news/562020/20200501e.shtml.
[139] Gregg Mennis & Ben Henken, *New Jersey Considers Tapping New Fed Borrowing Program to Meet Pension Contributions,* Pew Charitable Trusts, July 15, 2020, https://www.pewtrusts.org/en/research-and-analysis/articles/2020/07/15/new-jersey-considers-tapping-new-fed-borrowing-program-to-meet-pension-contributions.
[140] *Id*.
[141] *Id*.
[142] Board of Governors of the Federal Reserve System, Statistical Release H.4.1, *Factors Affecting Reserve Balances of the Depository Institutions and Condition Statement of Federal Reserve Banks*, July 16, 2020, https://www.federalreserve.gov/releases/h41/ (to access click on hyperlink for July 16, 2020 release).
[143] Board of Governors of the Federal Reserve System, *Periodic Report Update on Outstanding Lending Facilities Authorized by the Board under Section 13(3) of the Federal Reserve Act*, May 28, 2020, https://www.federalreserve.gov/files/pmccf-smccf-talf-5-29-20.pdf#page=3.
[144] *Id*.

has announced it intends to make an equity investment of $10 billion in this facility. The TALF can provide up to $100 billion in lending.[145]

The TALF made its first loan on June 25, 2020.[146] On June 30, 2020, Chair Powell testified before the House Financial Services Committee that since the TALF was announced on March 23, 2020, "ABS spreads have contracted significantly."[147] As a result, he noted the TALF "might be used relatively little and mainly serve as a backstop, assuring lenders that they will have access to funding and giving them the confidence to make loans to households and businesses."[148]

The Federal Reserve submitted a periodic report about the TALF to the Senate Banking Committee and the House Financial Services Committee on July 10, 2020 that disclosed details about the facility's initial loans.[149] As of June 30, 2020, the TALF has made 19 loans totaling $252 million to five different borrowers.[150] Those five borrowers are: BlackRock Securitized Investors, LP; HVS XXVI LLC; MacKay Shields TALF 2.0 Opportunities Master Fund LP; Palmer Square TALF Opportunity Sub LLC; and TOCU IX LLC.[151] Of the 19 loans, 17 support the commercial mortgage sector, while one supports the small business sector and another supports the insurance premium finance sector.[152] Each loan was originated on June 25, 2020 and matures on June 26, 2023, and has a fixed interest rate of 1.3%.[153]

As of July 15, 2020, the TALF has made $937 million in loans to eligible borrowers.[154]

---

[145] Board of Governors of the Federal Reserve System, *Term Asset-Backed Securities Loan Facility,* May 12, 2020, https://www.federalreserve.gov/newsevents/pressreleases/files/monetary20200512a1.pdf.
[146] U.S. House Committee on Financial Services hearing on Coronavirus and the Cares Act, 116th Cong. (June 30, 2020) (statement of Jerome Powell, Chair, Board of Governors of the Federal Reserve), https://www.federalreserve.gov/newsevents/testimony/powell20200630a.htm.
[147] *Id*.
[148] *Id*.
[149] Board of Governors of the Federal Reserve System, *Periodic Report: Update on Outstanding Lending Facilities Authorized by the Board under Section 13(3) of the Federal Reserve Ac (Transaction-specific Disclosures),* July 10, 2020, https://www.federalreserve.gov/publications/files/talf-transaction-specific-disclosures-7-10-20.xlsx.
[150] *Id*.
[151] *Id*.
[152] *Id.*
[153] *Id.*
[154] Board of Governors of the Federal Reserve System, Statistical Release H.4.1, *Factors Affecting Reserve Balances of the Depository Institutions and Condition Statement of Federal Reserve Banks*, July 16, 2020, https://www.federalreserve.gov/releases/h41/ (to access click on hyperlink for July 16, 2020 release). The SPV for the TALF is TALF II LLC.

Treasury Loans for the Airline Industry and National Security Businesses

The Treasury has available $17 billion to make loans to businesses critical to maintaining national security under Subtitle A. To date, it has entered into one agreement to provide such a loan.

On July 1, 2020, the Treasury announced that it intended to provide a $700 million loan to YRC Worldwide Inc. (YRC).[155] The loan agreement between the Treasury and YRC was finalized on July 8.[156] YRC is a holding company that provides transportation and logistics services throughout North America via its operating companies, including to the Defense Department. YRC and its operating companies employ 30,000 people, including 24,000 members of the International Brotherhood of Teamsters.[157] The company specializes in LTL shipping where smaller cargos from multiple customers are combined on one trailer.[158] Based on 2019 revenue, YRC is the fifth-largest U.S. trucking company and the fourth-largest LTL shipping provider.[159] According to the Treasury, YRC "provides 68% of less-than-truckload services to the Department of Defense."[160] The company reportedly delivers "food, electronics and other supplies to military locations around the country."[161]

The Treasury has defined a "business critical to maintaining national security" as a business that is at the time of its application performing under a defense contract of the highest national priority or operating under a top secret facility security clearance.[162] Even if a business does not

---

[155] U.S. Department of the Treasury, *Treasury to Provide Loan to YRC Worldwide*, July 1, 2020, https://home.treasury.gov/news/press-releases/sm1049.

[156] U.S. Department of the Treasury, *Loans to Air Carriers, Eligible Businesses, and National Security Businesses*, https://home.treasury.gov/policy-issues/cares/preserving-jobs-for-american-industry/loans-to-air-carriers-eligible-businesses-and-national-security-businesses (last visited July 17, 2020).

[157] YRC Worldwide Inc., *YRC Worldwide Expects To Receive $700 Million CARES Act Loan from U.S. Treasury*, July 1, 2020, http://investors.YRC.com/news-releases/news-release-details/yrc-worldwide-expects-receive-700-million-cares-act-loan-us.

[158] YRC Worldwide Inc., *Annual Report (Form 10-K)*, March 11, 2020, http://investors.YRC.com/static-files/8092f183-eb4b-4ba7-bae2-fb4afc4f3e25.

[159] Jennifer Smith, *Trucker YRC Seeks to Defer Millions in Benefits Payments*, Wall Street Journal, June 18, 2020, https://www.wsj.com/articles/trucker-yrc-seeks-to-defer-millions-in-benefits-payments-11592508252.

[160] U.S. Department of the Treasury, *Treasury to Provide Loan to YRC Worldwide*, July 1, 2020, https://home.treasury.gov/news/press-releases/sm1049.

[161] Kate Davidson & Jennifer Smith, *U.S. Treasury to Lend $700 Million to Trucking Firm YRC Worldwide*, Wall Street Journal, July 1, 2020, https://www.wsj.com/articles/u-s-treasury-to-loan-700-million-to-trucking-firm-yrc-worldwide-11593602409.

[162] U.S. Department of the Treasury, *Q&A: Loans to Air Carriers and Eligible Businesses and National Security Businesses*, April 10, 2020, https://home.treasury.gov/system/files/136/CARES-Airline-Loan-Support-Q-and-A-national-security.pdf; Defense Contract Management Agency, *Defense Priorities & Allocations System (DPAS)*, May 7, 2019, https://www.dcma.mil/DPAS/ ("A DX rating is assigned to those programs of the highest national priority").

satisfy either of these two criteria, it may be considered for loans if the Treasury Secretary determines that the business is critical to maintaining national security, based on a recommendation and certification by the Secretary of Defense or the Director of National Intelligence that it is.[163] In YRC's case, the Treasury determined that it was critical to maintaining national security based on a certification by the Secretary of Defense.[164] It is unclear how the Treasury and the Defense Department reached their decisions.

YRC's most recent quarterly report reveals that it had significant liquidity issues. As of March 31, 2020, the company had $879.9 million in total debt and only $118 million in liquidity.[165] It has stated that "[i]n response to the uncertainty related to cash flows associated with COVID-19, [it] began taking liquidity preservation efforts late in the first quarter of 2020."[166] These efforts included, among other things, "the reduction of capital expenditures, temporary deferrals of operating lease payments, union health & welfare payments, [and] contributions to our non-union and multi-employer pension plans."[167] YRC's operating companies contribute to 33 multi-employer pension plans that cover approximately 79% of YRC's 30,000 employees.[168]

The Treasury's loan to YRC contains two parts (i.e., tranches) that mature on September 30, 2024.[169] The first tranche of $300 million (tranche A) has an interest rate of London Inter-bank Offered Rate (LIBOR) +3.50%.[170] YRC will use these funds to cover, among other things, healthcare and pension liabilities, real estate and equipment leases, and interest payments on debt.[171] The second tranche of $400 million (tranche B) also has an interest rate of LIBOR +3.50%. YRC will use these funds to finance the purchase of tractors and trailers in accordance with the company's capital expenditures plan that must be submitted to, and approved by, the Treasury.[172]

---

[163] U.S. Department of the Treasury, *Q&A: Loans to Air Carriers and Eligible Businesses and National Security Businesses,* Apr. 10, 2020, https://home.treasury.gov/system/files/136/CARES-Airline-Loan-Support-Q-and-A-national-security.pdf.
[164] *Id.*
[165] YRC Worldwide Inc., *Quarterly Report (Form 10-Q)*, May 11, 2020, http://investors.YRC.com/static-files/a46b9f22-71b7-4bd8-acf6-b12aabb24bf5.
[166] *Id.*
[167] *Id.*
[168] YRC Worldwide Inc., *Annual Report (Form 10-K)*, March 11, 2020, http://investors.YRC.com/static-files/8092f183-eb4b-4ba7-bae2-fb4afc4f3e25.
[169] U.S. Department of the Treasury, *Transaction Summary*, July 8, 2020, https://home.treasury.gov/system/files/136/YRC-Transaction-Summary.pdf.
[170] *Id.*; U.S. Department of the Treasury, *Transaction Documentation*, July 8, 2020, https://home.treasury.gov/system/files/136/YRC-Documentation.pdf.
[171] U.S. Department of the Treasury, *Transaction Documentation*, July 8, 2020, https://home.treasury.gov/system/files/136/YRC-Documentation.pdf.
[172] U.S. Department of the Treasury, *Transaction Summary*, July 8, 2020, https://home.treasury.gov/system/files/136/YRC-Transaction-Summary.pdf; U.S. Department of the Treasury, *Transaction Documentation*, July 8, 2020, https://home.treasury.gov/system/files/136/YRC-Documentation.pdf.

Before YRC obtained this loan, it deferred millions of dollars of pension and healthcare payments for its largely unionized workforce for March, April, and May 2020.[173] In April 2020, YRC "told a large multiemployer health-care fund that the missed contributions would be paid once YRC received" a loan from the Treasury.[174] On July 1, 2020, YRC's Chief Executive Darren Hawkins stated that the funds from the Treasury will allow the company to pay off three months of missed pension and healthcare payments, which were "roughly $40 million a month."[175] On or around July 2, 2020, after Treasury announced its intent to provide a loan to YRC, the company began to repay some of these missed payments.[176]

Both tranches will be secured by a combination of a first-priority security interest in certain escrow accounts, a third-priority security interest in YRC's personal property, a third-priority mortgage or deed on certain real property, and a third-priority pledge of YRC's equity interests.[177] In addition, both tranches are subject to financial covenants that require the company to maintain certain minimum liquidity and earnings before interest, taxes, depreciation, and amortization (EBITDA) standards.[178] The covenants also require YRC to comply with the CARES Act's direct lending restrictions on employee compensation, stock repurchases, dividends, and reductions in employment levels.

In connection with the loan, YRC will issue almost 16,000,000 shares of common stock to the Treasury, which is equivalent to 29.6% of the company's fully diluted outstanding stock.[179] To comply with the CARES Act's requirement that the Treasury "shall not exercise voting power with respect to any shares of common stock," the Treasury will hold its shares of YRC's common stock through a voting trust, which will be required to vote the shares in the same proportion that all other unaffiliated shares of YRC's common stock are voted.[180]

---

[173] Jennifer Smith, *Trucker YRC Seeks to Defer Millions in Benefits Payments*, Wall Street Journal, June 18, 2020, https://www.wsj.com/articles/trucker-yrc-seeks-to-defer-millions-in-benefits-payments-11592508252.
[174] *Id.*
[175] Kate Davidson & Jennifer Smith, *U.S. Treasury to Lend $700 Million to Trucking Firm YRC Worldwide*, Wall Street Journal, July 1, 2020, https://www.wsj.com/articles/u-s-treasury-to-loan-700-million-to-trucking-firm-yrc-worldwide-11593602409.
[176] Brian Kaberline, *YRC makes partial payment to employee health funds*, Kansas City Business Journal, July 6, 2020, https://www.bizjournals.com/kansascity/news/2020/07/06/yrc-makes-partial-payment-to-employee-health-funds.html.
[177] U.S. Department of the Treasury, *Transaction Documentation*, July 8, 2020, https://home.treasury.gov/system/files/136/YRC-Documentation.pdf.
[178] *Id.*
[179] *Id.*
[180] CARES Act, Pub. L. No. 116-136, § 4003(d)(2)(B), 134 Stat. 281 (2020); YRC Worldwide Inc., *Current Report (Form 8-K)*, June 30, 2020, http://investors.YRC.com/static-files/aac3d537-bae1-4f0c-b0ef-99269b0d0b53; YRC Worldwide Inc., *YRC Worldwide Expects To Receive $700 Million CARES Act Loan from U.S. Treasury*, July 1, 2020, http://investors.YRC.com/news-releases/news-release-details/yrc-worldwide-expects-receive-700-million-cares-act-loan-us.

Notably, the interest rate on YRC's loan from the Treasury is 4% lower than the interest rate on its most recent debt financing, which was a five-year, $600 million term loan that YRC obtained in September 2019 before the COVID-19 crisis.[181] YRC has been rated non-investment grade for over a decade.[182] On April 6, 2020, a research report by investment bank Stephens Inc. indicated that YRC might be at risk of a "potential bankruptcy."[183] One month later, on May 11, 2020, YRC stated there was "substantial doubt" about its ability to continue to operate as a going concern without "governmental assistance or a meaningful stabilization of the economy in the near-term."[184] On May 28, 2020, Standard & Poor's (S&P) downgraded YRC from CCC+ to CCC after the company announced it did not believe it would be able to comply with the financial covenant under its term loan agreement.[185] In its downgrade report, S&P stated it believed that YRC's "capital structure will be unsustainable over the long term," in part due its heavy pension burden.[186]

After YRC entered its loan agreement with the Treasury, which improved the company's liquidity position, S&P upgraded the company only one notch to CCC+.[187] S&P noted, among other things, that it "believe[d] the company will remain highly leveraged given its contingent exposure to substantially underfunded Teamster multiemployer pension plans (MEPPs)," which includes "about $8 billion of contingent obligations related to MEPPs."[188]

The Treasury has available $29 billion to make loans to the airline industry under Subtitle A. To date, it has not entered into any agreements to provide such loans. However, the Treasury has signed letters of intent with ten passenger air carriers that set out the terms on which the Treasury is prepared to extend loans to these carriers.[189] It has not released the details of these terms.

---

[181] YRC Worldwide Inc., *Current Report (Form 8-K)*, Sept. 11, 2019, http://investors.YRC.com/static-files/14d3a39a-13af-4e5f-80fc-bcad38b120f2.
[182] Moody's Investors Services, YRC Worldwide Inc. Ratings, https://www.moodys.com/credit-ratings/YRC-Worldwide-Inc-credit-rating-834015 (last visited July 14, 2020).
[183] Jennifer Smith, *Truckers Cut Spending as Factory Slowdown Weighs on Operators*, Wall Street Journal, April 7, 2020, https://www.wsj.com/articles/truckers-cut-spending-as-factory-slowdown-weighs-on-some-operators-11586295247.
[184] YRC Worldwide Inc., *Quarterly Report (Form 10-Q)*, May 11, 2020, http://investors.YRC.com/static-files/a46b9f22-71b7-4bd8-acf6-b12aabb24bf5.
[185] Standard & Poor's, *U.S.-Based YRC Worldwide Inc. Downgraded To 'CCC' On Anticipated Covenant Violation, Outlook Negative*, May 28, 2020, https://www.standardandpoors.com/en_US/web/guest/article/-/view/type/HTML/id/2450913.
[186] *Id.*
[187] Standard & Poor's, *YRC Worldwide Inc. Upgraded To 'CCC+' On Improved Liquidity; Outlook Stable*, July 9, 2020, https://www.standardandpoors.com/en_US/web/guest/article/-/view/type/HTML/id/2475963.
[188] *Id.*
[189] U.S. Department of the Treasury, *Statement from Secretary Steven T. Mnuchin on CARES Act Loans to Major Airlines*, July 2, 2020, https://home.treasury.gov/news/press-releases/sm1054.

On July 2, 2020, the Treasury announced that five passenger air carriers—American Airlines, Frontier Airlines, Hawaiian Airlines, Sky West Airlines, and Spirit Airlines—had signed letters of intent for loans under Subtitle A.[190] The next week, on July 7, 2020, the Treasury announced that five additional passenger air carriers—Alaska Airlines, Delta Air Lines, JetBlue Airways, United Airlines, and Southwest Airlines—also had signed such letters of intent.[191]

On July 9, 2020, Secretary Mnuchin stated during a television interview that he thought "many of these airlines aren't going to need to use [Subtitle A loans] and we'll finance them in the capital markets. But we wanted to make sure that the airlines had backstops so that they had liquidity."[192]

To date, the Treasury has not announced loan agreements with any airline industry businesses for loans under Subtitle A.

---

[190] U.S. Department of the Treasury, *Treasury and Five Major Airlines Agree on Loan Terms*, July 2, 2020, https://home.treasury.gov/news/press-releases/sm1050.

[191] U.S. Department of the Treasury, *Statement from Secretary Steven T. Mnuchin on CARES Act Loans to Major Airlines*, July 2, 2020, https://home.treasury.gov/news/press-releases/sm1054.

[192] CNBC, *CNBC Transcript: Treasury Secretary Steven Mnuchin Speaks with CNBC's "Squawk on the Street" Today*, July 9, 2020, https://www.cnbc.com/2020/07/09/cnbc-transcript-treasury-secretary-steven-mnuchin-speaks-with-cnbcs-squawk-on-the-street-today.html.

APPENDIX A

May 29, 2020

The Honorable Steven T. Mnuchin
Secretary
U.S. Department of the Treasury
1500 Pennsylvania Avenue, NW
Washington, D.C. 20220

The Honorable Jerome H. Powell
Chairman
Board of Governors of the Federal Reserve
20th Street and Constitution Avenue, NW
Washington, D.C. 20551

Dear Secretary Mnuchin and Chairman Powell:

We write as members of the Congressional Oversight Commission (the "Commission") created by the CARES Act. The Commission's role is to conduct oversight of the implementation of Division A, Title IV, Subtitle A of the CARES Act ("Subtitle A") by the Treasury Department (the "Treasury") and the Federal Reserve. On May 18, the Commission issued its first report, outlining, among other things, some preliminary questions we have about the actions of the Treasury and the Federal Reserve in implementing Subtitle A so far. The Commission is required by statute to issue a report every thirty days.

As we carry out our responsibilities and prepare for future reports, we request your assistance in two ways. First, we ask that you provide answers to the questions that we posed in our May 18 report. Second, we ask that you meet with us to discuss the Treasury and Federal Reserve's implementation of Subtitle A and that the meeting be held promptly.

We have broken down the questions we asked in our May 18 report into two tiers, which are identified in the appendix to this letter. We request that you provide answers to the tier 1 questions by June 8. We request that you provide answers to the tier 2 questions by June 29. We look forward to receiving your answers in writing or through conversations with our staff.

Thank you for your attention to this matter.

Sincerely,

/s/
French Hill
Member of Congress

/s/
Bharat Ramamurti
Commissioner

/s/
Donna E. Shalala
Member of Congress

/s/
Pat Toomey
U.S. Senator

Enclosure: Appendix

APPENDIX

TIER 1 QUESTIONS

I. General Questions

1. How will the Treasury and the Fed (the "agencies") assess the success or failure of this program?

2. The agencies are supposed to use this program to stabilize the economy and help companies and municipalities with liquidity issues stemming from the COVID-19 crisis. How will the agencies attempt to achieve this goal while protecting taxpayer dollars? Are the agencies prepared to lose taxpayer dollars in an effort to facilitate more lending and support to a broader set of entities?

II. Program and Facility-Specific Questions

Primary Market Corporate Credit Facility (PMCCF)

1. How did the agencies determine the eligible assets for purchase by this facility?

2. Why did the agencies require an issuer to be rated investment grade by the credit rating agencies as of March 22, 2020 to be an eligible issuer for this facility? What would be the implications of broadening eligibility to this facility to issuers rated non-investment grade?

3. Why did the agencies choose March 22, 2020 as the cutoff date for an issuer to be rated investment grade to be an eligible issuer for this facility? How will this date selection impact the ability of issuers that have been downgraded from investment grade to non-investment grade to access capital through this facility?

4. Why did the agencies limit eligible issuers to those rated by a major nationally recognized statistical rating organization (NRSRO) as opposed to issuers rated by other credit rating organizations?

Secondary Market Corporate Credit Facility (SMCCF)

1. Is there a concern that changes in secondary market bond prices will reduce the flow of credit to households and businesses or create risk to the financial system? If so, how and what is the strategy for using this facility to address that concern?

2. On May 4, the Federal Reserve Bank of New York announced that it plans to use this facility to purchase Exchange Traded Funds (ETFs) that may own bonds rated below investment grade. How did the Fed reach this decision, and how does it measure the trade-offs of purchasing such ETFs?

3. The Fed has hired the firm Blackrock to serve as an investment manager for this facility. How is the Fed ensuring Blackrock is acting in the best interest of the Fed and the public?[1]

4. Does Blackrock have a duty of best execution to the Fed?

5. BlackRock has entered into a contract with the New York Federal Reserve Bank to provide management and advisory services to the facility. In that role, BlackRock employees will have access to material non-public information. Per the contract, certain BlackRock executives with access to that information will have the ability to provide "investment management, trading, and/or advisory services to other clients with respect to securities other than corporate bonds, ETFs, equity securities, or derivatives the value of which are tied to such instruments, including providing general market views and market views related to securities other than corporate bonds, ETFs, equity securities, or derivatives the value of which are tied to such instruments." They are also permitted to provide "investment management, trading or advisory services" in any asset class and to purchase investments for themselves in any asset class after a two-week cooling-off period.

    a. Why is two weeks an appropriate cooling-off period?

    b. How will any breaches of the non-public information be reported? What will be the discipline for such breaches?

Main Street Lending Program

1. Why did the agencies choose the 85% and 95% purchase rates for the SPVs in this program?

2. Why did the agencies choose the employee-size and annual revenue criteria that determine which businesses are eligible for this program?

3. How did the agencies choose the minimum loan sizes for the facilities in this program?

4. Why did the agencies decide not to create the mid-sized business lending facility that is described but not mandated in Section 4003(c)(3)(D) of the CARES Act?

5. What is the agencies' rationale for the adjusted earnings before interest, taxes, depreciation, and amortization (EBITDA) and leverage standards for loans in this program?

6. Between the initial announcement of the Main Street facilities on April 9 and the modifications to the facilities the Fed announced on April 30, the Fed reportedly received more than 2,200 comments from experts, industry groups, and others. Will the Fed release those comments so the public can review them?

---

[1] This question about BlackRock was in the Commission's May 18 report. However, the two questions about BlackRock that follow (questions #4 and #5) were not.

7. As part of its April 30 revisions to the facility term sheets for this program, the agencies removed the requirement that companies attest that they require financing "due to the exigent circumstances presented by the coronavirus disease."

    a. Why did the agencies remove that requirement?

    b. Without this requirement, how will the agencies ensure they are providing liquidity "to eligible businesses, [s]tates, and municipalities *related to losses incurred as a result of coronavirus*"?

8. As part of its April 30 revisions to the facility term sheets for this program, the agencies eliminated the requirement that firms attest to making "reasonable efforts" to maintain payroll and retain employees during the term of the loan and replaced it with a requirement that firms should make "commercially reasonable efforts" to maintain payroll.

    a. Why did the agencies remove the original attestation requirement?

    b. How do the agencies define "commercially reasonable efforts"?

    c. How will the agencies enforce this requirement?

Municipal Lending Facility

1. How did the agencies decide which municipalities to include in this facility?

2. What is the rationale for the population-size criteria that determine the cities and counties eligible for this facility? What are the concerns, if any, about purchasing notes from cities or counties smaller than the thresholds established?

3. Why were U.S. territories excluded from this facility?

TIER 2 QUESTIONS

I. General Questions

1. If the agencies use economy-wide metrics, like GDP growth, unemployment rates, or wage growth, to assess the success or failure of this program how will they isolate the effects of this program from other factors, including other federal and state relief measures?

2. If the agencies use more narrow metrics, like bond spreads, to assess the success or failure of this program how will they assess how changes in those metrics affect the broader economy, including the financial well-being of the people of the United States?

3. Do the agencies believe the Fed's emergency lending programs are better suited to assist bigger companies that can access the capital markets than smaller firms that cannot? If not, why not? If so, what are the agencies doing to counteract that issue?

4. Will the agencies faithfully follow the statutory requirements of Subtitle A when implementing the lending programs and facilities?

5. How can the agencies best determine the lending capacity of, and Treasury investment into, each Fed lending facility under Subtitle A in order to help support and stabilize the economy?

6. How can the agencies best determine how much of the Treasury's $454 billion in CARES Act funds to allocate among Fed lending facilities and when to allocate such funds in order to help support and stabilize the economy?

7. How can the agencies best estimate the risk of loss to taxpayer funds in each Fed lending facility?

8. How will the Fed ensure it complies with all restrictions to emergency lending under Section 13(3) of the Federal Reserve Act, including those prohibiting lending to insolvent borrowers?

9. How can the agencies best monitor compliance with and enforce the conflict of interest rules governing the agencies' lending programs and facilities?

10. How can the agencies best enforce the statutory terms and conditions for borrowers under their lending programs and facilities under Subtitle A, including the condition that borrowers are U.S. businesses, as defined by the CARES Act?

11. How will loans under these programs and facilities comply with Bank Secrecy Act (BSA) and the Anti-Money Laundering (AML) rules?

12. How will the agencies decide when to hire third parties to help manage the program or specific facilities? How will the agencies mitigate conflicts of interest these third parties might have?

13. Regarding outside services to assist the agencies to manage the programs and facilities, what is the competitive selection process for custody and fund management services? How are conflicts of interest mitigated?

14. The agencies' emergency lending programs and facilities provide lending directly through government loans and indirectly through banks and other qualified lenders. What are the trade-offs involved with these different delivery mechanisms?

15. While quickly providing lending to borrowers may result in more fraud and abuse, it may also assist many eligible borrowers that need money quickly. How should the agencies balance these trade-offs?

16. The Congressional Budget Office (CBO) recently published its preliminary estimate of the budgetary effects of the CARES Act. CBO's estimate concludes that "the income and the costs stemming from" the Fed's emergency lending facilities funded by the CARES Act "are expected to roughly offset each other." CBO notes that the Fed did "not sustain losses on similar lending . . . [d]uring the financial crisis of 2008 and 2009."[2] Do you believe CBO is correct in its assumptions of a no net cost result? In order to accomplish the goal of economic stabilization and return to economic growth, is this a reasonable assumption?

17. How can the agencies best incentivize private-sector financial institutions to help facilitate the Treasury and the Fed's lending programs and facilities to ensure credit gets to American households and businesses, while ensuring that taxpayer dollars are well spent?

18. How can the agencies best set rates and fees for the Treasury and the Fed's lending programs and facilities under Subtitle A to ensure their workability and that the federal government remains the lender of last resort?

19. What will the effect of Treasury and Fed lending be on overall employment?

20. Do the agencies believe it is appropriate to modify the facilities to ensure specific companies or industries have access to some or all of the funds? If so, how are those modifications being considered in a manner that also addresses all industries and sectors?

II. Program and Facility-Specific Questions

Primary Market Corporate Credit Facility (PMCCF)

1. Through this facility, the Fed, through an SPV, will be purchasing new bonds from companies. Do the agencies intend to place limitations or parameters around companies receiving this support, or use of proceeds? Are such limitations workable in capital markets transactions? Do the agencies believe the proceeds of bond purchases will help stabilize the economy regardless of how the proceeds are used?

2. The Federal Reserve Bank of New York, which is implementing this facility, recently stated that a U.S. subsidiary of a foreign company can qualify for support through the facility. How does the Federal Reserve Bank of New York plan on enforcing its requirement that proceeds derived from participation in the facility may only be used for the benefit of the U.S. subsidiary issuer, its consolidated U.S. subsidiaries, and affiliates of the U.S. subsidiary issuer that are U.S. businesses, rather than for the benefit of its foreign affiliates?

Main Street Lending Program

1. Do the agencies plan to expand eligible lenders in this program beyond depository institutions? Why or why not?

---

[2] Letter from Phillip L. Swagel, Director, Congressional Budget Office to U.S. Senator Mike Enzi, Apr. 27, 2020, https://www.cbo.gov/system/files/2020-04/hr748.pdf.

Municipal Lending Facility

1. What conditions, if any, including those related to policies, will the agencies impose on states and municipalities that receive funding under this facility?

2. What is the rationale for the three-year repayment terms under this facility?

3. Will the agencies disclose information about any states, counties, and cities whose applications for loans from this facility are denied?

Loans for the Airline Industry and National Security Businesses Under Subtitle A

1. How many applications has the Treasury received for loans under Subtitle A?

2. How is the Treasury measuring and evaluating any proposals that loan applicants submit "on the form and amount of taxpayer protections they propose to provide" as part of their loan agreements, such as a warrant or equity instrument in an applicant's business?

3. When does the Treasury anticipate approving and disbursing these loans?

4. Under Subtitle A, the Treasury's loan agreements with the airline industry and businesses critical to maintaining national security must require a borrower to "not reduce its employment levels by more than 10 percent from the levels" as of March 24, 2020. How does Treasury intend to faithfully apply this statutory requirement?

APPENDIX B

June 8, 2020

The Honorable French Hill
U.S. House of Representatives
Washington, DC 20515

The Honorable Donna E. Shalala
U.S. House of Representatives
Washington, DC 20515

Mr. Bharat Ramamurti
Commissioner
Washington, DC 20515

The Honorable Pat Toomey
United States Senate
Washington, DC 20510

Dear Members of the Congressional Oversight Commission:

Thank you for your letter dated May 29, 2020, regarding the actions of the Department of the Treasury and the Board of Governors of the Federal Reserve System under Division A, Title IV, Subtitle A of the CARES Act. We look forward to working with the Commission to ensure that implementation of the CARES Act is carried out consistent with the statute's text and purpose.

Please find attached answers to the Tier 1 questions posed by the Commission in your correspondence.

Sincerely,

Steven T. Mnuchin
Secretary
U.S. Department of the Treasury

Jerome H. Powell
Chair
Board of Governors of the
Federal Reserve System

Enclosure

<u>Congressional Oversight Commission: Answers to Tier 1 Questions</u>

I. General Questions

1. *How will Treasury and the Fed ("the agencies") assess the success or failure of this program?*

The Board of Governors of the Federal Reserve System (the "Board"; together with the Federal Reserve Banks, the "Federal Reserve") with the support and approval of the Department of the Treasury ("Treasury"; together with the Federal Reserve, the "agencies") has established a set of lending facilities pursuant to the Coronavirus Aid, Relief, and Economic Security Act ("CARES Act") and under section 13(3) of the Federal Reserve Act (the "13(3) facilities"). The agencies created the 13(3) facilities in response to the unprecedented financial and economic strains imposed by the COVID-19 pandemic and by the public health measures employed in response. The agencies monitor a broad range of economic and financial indicators to judge economic activity, credit flows, and market functioning as a whole. The Federal Reserve designed the facilities to work together to protect financial stability and support achievement of its dual mandate of full employment and price stability.

Broadly speaking, the 13(3) facilities established with the support and approval of Treasury using funds made available by the CARES Act—the corporate credit facilities (the Primary Market Corporate Credit Facility ("PMCCF") and Secondary Market Corporate Credit Facility ("SMCCF")), the Main Street Lending Program (the Main Street New Loan Facility ("MSNLF"); the Main Street Priority Loan Facility ("MSPLF"); and the Main Street Expanded Loan Facility ("MSELF")); the Term Asset-Backed Securities Loan Facility ("TALF"); and the Municipal Liquidity Facility ("MLF")—have as their immediate goal the promotion of the flow of credit to businesses, households and state and local governments. The effectiveness of all these facilities is generally best measured by the degree to which the targeted market or area of the economy recovers by having the program present.

As noted, the agencies monitor a variety of indicators to assess the performance of the 13(3) facilities. With respect to short-term funding markets, among other indicators, we monitor issuance, maturity, outstandings and spreads for a range of money market instruments, including repurchase agreements, commercial paper, certificates of deposit, and variable-rate demand notes. We also measure pressures on key institutions and intermediaries in these markets, which include, but are not limited to, money market funds, commercial banks and dealers. Finally, we monitor the volume and key features of assets pledged to, or purchased by, these facilities as well as the counterparties to these transactions.

When judging the flow of credit to households, businesses, and state and local governments, we use similar metrics. Among these, we monitor the issuance, maturity, outstandings, and spreads for a wide range of debt instruments, including auto, credit card, and other consumer loans; loans to small businesses; syndicated loans; corporate bonds; municipal notes and bonds; and asset-backed securities. We also monitor measures of market functioning, such as bid-ask spreads, trading costs, order book depth, trading volumes, and price volatility. Moreover, the agencies monitor the health of key institutions and intermediaries in these credit markets, which include, but are not limited to, open-end mutual funds, commercial banks, and dealers. Finally,

as these facilities come to operational readiness, we monitor the volume and key characteristics of loans made (or assets purchased) by these facilities, as well as the set of businesses and governmental entities (e.g., states and municipalities) using the facilities.

2. *The agencies are supposed to use this program to stabilize the economy and help companies and municipalities with liquidity issues stemming from the COVID-19 crisis. How will the agencies attempt to achieve this goal while protecting taxpayer dollars? Are the agencies prepared to lose taxpayer dollars in an effort to facilitate more lending and support to a broader set of entities?*

In implementing the 13(3) facilities using the authority provided by the CARES Act, and under the Federal Reserve Act, the agencies are committed to addressing the severe economic dislocations that have occurred as a result of the impact of COVID-19. We have designed the 13(3) facilities to provide liquidity to solvent borrowers—businesses and states and municipalities—to better enable these organizations to either rehire their workers when the economy reopens or keep them on board. Consistent with the CARES Act, these facilities also are designed and implemented in compliance with section 13(3) of the Federal Reserve Act, which provides that the Federal Reserve is restricted to making loans that are secured to the satisfaction of the lending Reserve Bank and that carry sufficient credit protections to protect taxpayers from losses. Equity investments provided by Treasury, including equity investments made by Treasury using funds appropriated by Congress under the CARES Act, are designed to cover losses on loans made by the facility, including in downside economic scenarios—and thus inherently may take loss. Treasury accepts the possibility that losses may occur with respect to the funds it has committed, and believes that the terms and conditions of the 13(3) programs to which it has committed funds appropriately balance the interests of taxpayer protection and program efficacy.

We have focused to date on the most pressing needs for liquidity support in the U.S. economy. We are willing to adapt and extend these programs—or adopt additional programs—if appropriate to address the economy's evolving needs or our evolving understanding of its needs. The Federal Reserve expects that its loans made to fund the 13(3) facilities will be fully repaid under a very broad range of economic outcomes. The performance of Treasury equity investment in the 13(3) facilities will depend on program features and future economic conditions.

II. Program and Facility-Specific Questions

Primary Market Corporate Credit Facility (PMCCF)

1. *How did the agencies determine the eligible assets for purchase by this facility?*

Under the PMCCF term sheet, there are two groups of eligible assets. First, the PMCCF may purchase eligible corporate bonds as the sole investor in a bond issuance. Second, the PMCCF may purchase portions of syndicated loans or bond issuances of eligible issuers at

issuance; the PMCCF may purchase no more than 25 percent of any such loan syndication or bond issuance.

The agencies established the PMCCF to ensure that creditworthy companies that rely on capital markets to fund their operations have access to credit during the current unusual and exigent circumstances in which financial markets are experiencing extraordinary disruptions, volatility, and illiquidity. Corporate bonds support the operations of companies with more than 17 million employees based in the United States, and these bonds are key investment assets for retirees and pension funds. If companies are unable to issue corporate bonds, they may be unable to invest in inventory and equipment, meet current liabilities, or pay employees. The PMCCF seeks to ensure that creditworthy companies with maturing capital markets instruments (namely, syndicated loans and corporate bonds) retain the ability to refinance debt as well as access additional credit to ensure liquidity through this unprecedented period of COVID-19-related disruption.

Since the PMCCF's goal is to provide general support to creditworthy companies, and not to select among different industries and companies, the PMCCF utilizes a broad, transparent and simple ratings-based eligibility standard. In addition, since depository institutions and depository institution holding companies have access to other sources of support, their debt instruments are excluded from eligibility, as are companies that received specific lending support from Treasury under the CARES Act. Finally, because the equity provided to the PMCCF by the Treasury includes funds appropriated under the CARES Act, companies that participate in the PMCCF must comply with the U.S. business, conflict company, and other applicable CARES Act requirements.

2. *Why did the agencies require an issuer to be rated investment grade by the credit rating agencies as of March 22, 2020, to be an eligible issuer for this facility? What would be the implications of broadening eligibility to this facility to issuers rated non-investment grade?*

The PMCCF seeks to support creditworthy companies that rely on capital markets to fund their operations during unusual and exigent circumstances. Section 13(3) of the Federal Reserve Act and the Board's Regulation A require that a lending Reserve Bank secure itself to its satisfaction and ensure protection of the taxpayer. A historical investment-grade rating reflects positively on the creditworthiness of a firm prior to the unprecedented period of COVID-19-related disruption. Issuers that are rated investment grade have historically realized default rates that are significantly lower than issuers rated non-investment grade. Therefore, acquiring capital markets instruments of investment-grade issuers provides greater security than acquiring capital markets instruments of non-investment-grade issuers.

If the eligibility criteria of the PMCCF were broadened to include issuers that were not rated investment grade as of March 22, 2020, the number of companies eligible to obtain credit from the PMCCF would increase. Such an expansion, however, would increase the credit risk to the PMCCF at a rate greater than the proportionate increase in potential borrowers, due to the higher leverage and default risk of high-yield borrowers.

3. *Why did the agencies choose March 22, 2020, as the cutoff date for an issuer to be rated investment grade to be an eligible issuer for this facility? How will this date selection impact the ability of issuers that have been downgraded from investment grade to non-investment grade to access capital through this facility?*

The two corporate credit facilities were initially authorized by the Board and approved by the Secretary of the Treasury on March 22, 2020. That cut-off date was chosen for the ratings criteria in order to extend the reach of the facilities to include all companies eligible at the announcement date, regardless of how long it would take to operationalize the facilities.

Issuers that were investment grade prior to March 22, 2020, but were subsequently downgraded, may still be eligible to access the PMCCF. They must be rated at least BB-/Ba3 as of the date on which the PMCCF makes a purchase. If rated by multiple major NRSROs, such issuers must be rated at least BB-/Ba3 by two or more NRSROs at the time the PMCCF makes a purchase.

4. *Why did the agencies limit eligible issuers to those rated by a major nationally recognized statistical rating organization (NRSRO) as opposed to issuers rated by other credit rating organizations?*

The PMCCF uses ratings to evaluate the credit quality of companies in order to determine whether they may access the facility. To enable a quick launch, the PMCCF originally relied on the three NRSROs that the largest number of investors rely on. After conducting additional analysis, the facility recently added another three rating agencies to the list of eligible NRSROs. In assessing which rating agencies to deem eligible, the agencies analyzed a wide range of factors, including the extent to which an individual rating agency is relied upon by private-sector investors with respect to the relevant asset classes.

Secondary Market Corporate Credit Facility (SMCCF)

1. *Is there a concern that changes in secondary market bond prices will reduce the flow of credit to households and businesses or create risk to the financial system? If so, how and what is the strategy for using this facility to address that concern?*

Since the onset of the COVID-19 pandemic, the corporate bond market has experienced significant dislocations. By facilitating market functioning, the SMCCF is intended to reduce the risk that secondary market prices for corporate bonds become subject to fire sales or price dislocations. These price dislocations are important because they affect the primary markets for American companies to access capital. Potential buyers may purchase bonds sold at distressed prices in the secondary market rather than buying newly issued bonds directly from companies, reducing the availability of new credit to fund companies. By providing support to the secondary market, the SMCCF reduces the cost of credit and increases the availability of credit to borrowers who might otherwise not be able to access the market with new corporate bond issuances at reasonable rates. In addition, there is a direct relationship between the secondary market and the primary market, as most new corporate bond prices are set based on secondary market spreads.

2. *On May 4, the Federal Reserve Bank of New York announced that it plans to use this facility to purchase exchange-traded funds (ETFs) that may own bonds rated below investment grade. How did the Fed reach this decision and how does it measure the trade-offs of purchasing such ETFs?*

Market functioning in the corporate credit market has been impaired based on metrics such as prices, bid ask spreads, trading volumes, and price volatility as well as limited primary market issuance from high-yield issuers. By purchasing ETFs that have exposure to high-yield issuers, the SMCCF seeks to provide support to the more dislocated segments of the corporate bond market and to limit discontinuities between the different segments of the market. Such discontinuities can lead to extreme outcomes where companies downgraded a single notch—from low investment-grade to the upper end of high-yield—find themselves facing sharply higher funding costs and thus are under increased pressure to cut costs, including by reducing their workforces. The increased risk associated with acquiring instruments issued by high-yield companies is managed by investing through instruments that allow for the creation of a diversified portfolio and by the increased amount of Treasury's equity allocated to support these purchases. The agencies also limit the amount of risk to the SMCCF from purchases of high-yield ETFs by ensuring that the large majority of ETF purchases target the investment-grade corporate bond market.

3. *The Fed has hired the firm Blackrock to serve as an investment manager for this facility. How is the Fed ensuring Blackrock is acting in the best interest of the Fed and the public?*

On May 11, 2020, Corporate Credit Facilities LLC ("CCF"), a special purpose vehicle created to facilitate the operations of SMCCF, entered into an Investment Management Agreement ("IMA") with BlackRock Financial Management, Inc. ("BlackRock"). The Federal Reserve Bank of New York ("FRBNY") is the sole managing member of the CCF.

Pursuant to the IMA, BlackRock acts as a fiduciary to the CCF in performing investment management services. In order to best advance the CCF's objectives as a fiduciary, BlackRock is required to follow FRBNY's specific and detailed investment guidelines and to buy and sell corporate bonds, corporate loans, and corporate bond ETFs on a best execution basis. BlackRock is required to communicate with the CCF on a daily basis regarding its planned purchase activity for the day and respond to requests for updates from the CCF on market functioning and asset purchases.

The IMA imposes stringent requirements on BlackRock to protect confidential information and to mitigate conflicts of interest. Confidential information gained by BlackRock or its affiliates or their respective directors, officers, or employees in the course of this engagement may not be leveraged for matters unrelated to the CCF. BlackRock's compliance with the rigorous information barrier and conflict of interest mitigation provisions the Federal Reserve has imposed under the IMA is subject to audit and review by FRBNY, the Board, and other governmental authorities with oversight responsibilities under applicable law.

These are select examples of provisions relating to the Federal Reserve's efforts to ensure that Blackrock is acting in the best interest of the public. The IMA, including the investment guidelines, is available in full on the FRBNY website. *See* https://www.newyorkfed.org/medialibrary/media/markets/SMCCF_Investment_Management_Agreement.pdf.

4. *Does Blackrock have a duty of best execution to the Fed?*

Yes. The Operating Guidelines set out in the IMA provide that "[a]ll transactions in Eligible ETFs will be effected through Eligible Sellers at market prices on a best execution basis in accordance with [the IMA], whether in the secondary market or via primary creations and redemptions."

5. *BlackRock has entered into a contract with the New York Federal Reserve Bank to provide management and advisory services to the facility. In that role, BlackRock employees will have access to material non-public information. Per the contract, certain BlackRock executives with access to that information will have the ability to provide "investment management, trading, and/or advisory services to other clients with respect to securities other than corporate bonds, ETFs, equity securities, or derivatives the value of which are tied to such instruments, including providing general market views and market views related to securities other than corporate bonds, ETFs, equity securities, or derivatives the value of which are tied to such instruments." They are also permitted to provide "investment management, trading or advisory services" in any asset class and to purchase investments for themselves in any asset class after a two-week cooling-off period.*

a. *Why is two weeks an appropriate cooling-off period?*

b. *How will any breaches of the non-public information be reported? What will be the discipline for such breaches?*

The IMA provides stringent requirements to protect confidential information and to mitigate conflicts of interest. Confidential information gained by BlackRock or its affiliates or their respective directors, officers, or employees in the course of this engagement may not be leveraged for matters unrelated to the CCF. This restriction prohibits, without limitation, use of any confidential information for the benefit of BlackRock, for the benefit of any other BlackRock client, or to inform any financial transaction, render any advice or recommendation, or attempt to influence any market or transaction for the benefit of any individual or entity other than the CCF. This obligation survives the termination or expiration of the IMA.

The "two-week cooling off period" relates to the information wall between BlackRock employees who are involved in providing investment management, trading, and/or advisory services to the CCF or FRBNY and other BlackRock employees. BlackRock employees providing such services to the CCF or FRBNY—for the duration of when they have access to material nonpublic information plus a two week cooling off period—are prohibited from providing investment management, trading, or advisory services to anyone other than the CCF in any of the asset classes held by BlackRock and must also refrain from purchasing for him/herself

investments in any of the asset classes held by BlackRock, unless authorized by the Chief Compliance Officer of FRBNY. The two-week period is intended to ensure that material nonpublic information loses its value in the market. To be clear, even after the two-week cooling off period, material nonpublic information may not be leveraged for matters unrelated to the CCF. Additional information is available in Exhibit G to the IMA, which sets forth the Information Barrier and Conflicts of Interest Mitigation Procedures. *See* https://www.newyorkfed.org/medialibrary/media/markets/SMCCF_Investment_Management_Agreement.pdf.

The IMA requires that breaches of confidential information be reported promptly. Should a breach occur, FRBNY will respond with diligence and promptness. Consequences for any breach will be determined by the Federal Reserve.

Main Street Lending Program

1. *Why did the agencies choose the 85% and 95% purchase rates for the SPVs in this program?*

The Main Street SPV will purchase participations in MSNLF loans, MSPLF loans, and MSELF upsized tranches. The agencies considered several factors in sizing participations in Main Street eligible loans and upsized tranches. The agencies created Main Street facilities that purchase sizable (but less than 100 percent) participations in loans in order to maintain a level of risk sharing that limits downside risk and creates balance sheet capacity for eligible lenders, while at the same time ensuring eligible lenders have a strong incentive to apply prudent underwriting and risk management standards. Upon full consideration of the relevant factors, the agencies believe that a 95 percent participation provides an appropriate balance of these considerations for all three Main Street facilities. Accordingly, on June 8 the Board issued revised term sheets that, among other changes, specify a 95% participation percentage for MSPLF loans (up from 85%), while maintaining the 95% participation percentage for MSNLF and MSELF loans.

2. *Why did the agencies choose the employee-size and annual revenue criteria that determine which businesses are eligible for this program?*

Employee size and annual revenue criteria are used for the Small Business Administration's (SBA) 7(a) program and Payroll Protection Program ("PPP") and are commonly used to measure the footprint of a business. The adoption of such metrics was considered prudent, because the program is designed to support small and medium-sized businesses that are unable to receive sufficient assistance through other programs, such as the SBA's PPP, and that lack access to the Federal Reserve's Primary and Secondary Market Corporate Credit Facilities. The agencies set the employee and revenue criteria for the Main Street Lending Program to provide broad access to companies that lack access to or sufficient support from other existing programs and were otherwise in sound financial condition prior to the crisis.

The agencies have not set a lower bound "floor" for borrower size under the program, thereby providing access to small businesses that met other program criteria. The upper bounds for the employee-size and annual revenue criteria were raised from 10,000 employees or $2.5

billion in revenues to 15,000 employees or $5 billion in revenues in response to public feedback that the lower levels initially proposed would have scoped out businesses that could benefit from Main Street loans. The changes were also intended to provide a better congruence with the PMCCF and SMCCF by capturing a wider swath of companies that may not have reached the scale needed to issue the kinds of capital market instruments that would be purchased under the PMCCF and SMCCF.

3. *How did the agencies choose the minimum loan sizes for the facilities in this program?*

The agencies considered several factors in determining minimum loan sizes. Consistent with the desire to assist companies that may have received insufficient support through the PPP or that are unable to receive support through the PMCCF or SMCCF, the Main Street Lending Program targeted a minimum loan size that would be attractive to a broad range of small and medium-sized businesses that may not have been able to receive support from these other programs. The agencies also had a desire to maintain sufficient overlap with the upper bound of the PPP in order to avoid excluding inadvertently a set of businesses from assistance. The agencies considered public feedback received and, in the revised term sheets issued on June 8, have selected $250,000 (lowered from $500,000) as the minimum loan size for the MSNLF and MSPLF in an effort to make the Main Street Lending Program accessible to as many borrowers as possible, while ensuring the program is feasible from an operational perspective.

The minimum loan size of the MSELF, at $10 million, was set significantly higher than that of the MSNLF or MSPLF because MSELF upsized tranches are likely more attractive to larger, more sophisticated borrowers with more complex funding structures.

4. *Why did the agencies decide not to create the mid-sized business lending facility that is described but not mandated in Section 4003(c)(3)(D) of the CARES Act?*

The agencies designed the Main Street Lending Program to meet the needs of small and medium-sized businesses as effectively and efficiently as possible, while protecting taxpayer funds. The program is designed within the parameters of Section 13(3) of the Federal Reserve Act, the CARES Act, and the Board's Regulation A, and includes CARES Act restrictions on executive compensation, capital distributions, and equity repurchases. The program includes a number of features that are designed to be attractive to small and medium-sized businesses, including deferral of interest payments for one year and deferral of repayment of principal for two years.

5. *What is the agencies' rationale for the adjusted earnings before interest, taxes, depreciation, and amortization (EBITDA) and leverage standards for loans in this program?*

Fundamentally, the agencies decided to use a leverage test based on EBITDA as the key parameter to govern the credit risk assumed by the Main Street Lending Program. The use of EBITDA and leverage requirements is standard industry practice in evaluating a potential borrower's creditworthiness for cash flow-based lending. Lenders and borrowers regularly agree to adjust a borrower's EBITDA to accommodate differences in business models across industries and to accommodate one-time events that may positively or negatively impact a borrower's

earnings. When applied prudently, these adjustments provide a lender with a more accurate representation of a business's earnings capacity over time.

Allowing for leverage of 4x or 6x adjusted EBITDA is within the normal range of practice across the banking industry. The agencies determined that leverage of 4x adjusted EBITDA is reasonable for the MSNLF given the parameters of MSNLF Loans, but they allowed for greater leverage within the MSELF and MSPLF because other risk mitigating features and protections exist in those facilities, such as the additional security required in the MSELF and the larger risk retention requirement in the MSPLF.

6. *Between the initial announcement of the Main Street facilities on April 9 and the modifications to the facilities the Fed announced on April 30, the Fed reportedly received more than 2,200 comments from experts, industry groups, and others. Will the Fed release those comments so the public can review them?*

The agencies received more than 2,200 comments from small and medium-sized business owners, industry groups, nonprofit organizations, and lenders between April 9 and April 30. After reviewing the comments received, the agencies expanded many aspects of the Main Street Lending Program to make credit available to a greater number of small and medium-sized businesses across the country. We are in the process of preparing the comments received for public release by removing certain proprietary commercial and personally identifiable information. We anticipate releasing the comments to the public by the end of the month.

7. *As part of its April 30 revisions to the facility term sheets for this program, the agencies removed the requirement that companies attest that they require financing "due to the exigent circumstances presented by the coronavirus disease."*

a. *Why did the agencies remove that requirement?*

b. *Without this requirement, how will the agencies ensure they are providing liquidity "to eligible businesses, [s]tates, and municipalities related to losses incurred as a result of coronavirus"?*

Nearly all sectors of the U.S. economy have been affected directly or indirectly by the exigent circumstances presented by the coronavirus pandemic. As adopted following the expiration of the public comment period, the Main Street Lending Program includes key features that more directly and effectively target credit to borrowers that have experienced a change in circumstances over the past several months. For example, while an eligible borrower's loans outstanding with the eligible lender must have received an internal risk rating that is equivalent to a "pass" rating used by supervisors, the term sheets intentionally specify that the relevant "as of" date for assignment of that rating is December 31, 2019—a date that precedes the onset of the COVID-19 disruption in the United States. In similar fashion, the mandatory Main Street borrower certification requires borrowers to attest that they (i) had generally been paying their undisputed debts due during the 90 days preceding the Main Street loan (unless the borrower is behind on its obligations because of disruptions to its business caused by the COVID-19 pandemic), and (ii) will be in a position following receipt of the Main Street loan to bring current

any debts that have fallen into arrears during the period of COVID-19 disruption. These program features are designed to make Main Street funding available to businesses that were in sound financial condition prior to the onset of the pandemic, but that may need additional financing to support operations until conditions normalize.

8. *As part of its April 30 revisions to the facility term sheets for this program, the agencies eliminated the requirement that firms attest to making "reasonable efforts" to maintain payroll and retain employees during the term of the loan and replaced it with a requirement that firms should make "commercially reasonable efforts" to maintain payroll.*

a. Why did the agencies remove the original attestation requirement?

The agencies revised the language regarding "reasonable efforts" to remove ambiguity and clarify that such efforts should be commercially reasonable—that is, that such efforts should be within the range that contribute to the health of the business and its ability to support employment over the longer term. More precisely, the goal of the program is to support the health of businesses through this difficult period so they are able to contribute to a robust economic recovery. Employees are critical contributors to the success of a business, and commercially reasonable efforts to maintain employment contribute to a faster recovery and to the health of a business in the long run.

b. How do the agencies define "commercially reasonable efforts"?

"Commercially reasonable efforts" is a standard defined in contract law. The application of such a standard in this context means that businesses that participate in the program are expected to make good-faith efforts to maintain payroll and retain employees in light of their respective capacities, economic environment, available resources, and business need for labor.

c. How will the agencies enforce this requirement?

The program expects borrowers to make commercially reasonable efforts to maintain payrolls. Such efforts may take different forms across the broad range of businesses eligible for the program. Because of the variety of approaches we expect from borrowers, the agencies will monitor the program's impact on the economic recovery and employment broadly rather than on a borrower-by-borrower basis. We expect to make adjustments to the Main Street Lending Program as needed to ensure the program contributes to robust economic recovery and employment gains.

Municipal Lending Facility

1. *How did the agencies decide which municipalities to include in this facility?*

The agencies determined eligibility criteria for the MLF with the aim of providing access to credit through the facility to as many municipalities as possible in the shortest timeframe possible. The municipal securities market involves upwards of 50,000 individual issuers, and it would not be logistically feasible for the MLF to stand ready to quickly undertake the diligence

reviews and otherwise work with borrowers in order to directly purchase notes from all municipal issuers. Initial direct eligibility was therefore limited to U.S. states and a number of large jurisdictions, while smaller jurisdictions were made eligible to issue notes to the MLF indirectly through another eligible state or municipality.

The agencies have subsequently expanded the facility to include multi-state entities, revenue bond issuers, and a broader range of municipalities, in response to feedback identifying legal barriers that would frustrate indirect participation by previously ineligible entities. The agencies also have amended the terms of the MLF to allow more than one issuer per eligible state, city, or county in order to facilitate the provision of assistance to smaller political subdivisions or other government entities. The MLF continues to encourage large eligible issuers to permit indirect participation by their political subdivisions or other governmental entities, however, because it remains logistically infeasible for the Federal Reserve to purchase notes directly from all U.S. municipalities for the reasons described above.

2. *What is the rationale for the population-size criteria that determine the cities and counties eligible for this facility? What are the concerns, if any, about purchasing notes from cities or counties smaller than the thresholds established?*

As described above, the population-size criteria for the MLF were selected to enable that the limited number of feasible issuers be allocated to entities serving the greatest number of people in the shortest timeframe possible. It would not be logistically feasible to purchase notes directly from all U.S. cities and counties, and smaller cities and counties have therefore been limited to indirect participation in the MLF through their respective states. Further, all cities and counties—even those ineligible to directly participate in the facility—have benefited from improving market conditions that have resulted from the presence of the MLF as a backstop to the short-term municipal securities market. By addressing the liquidity needs of larger cities and counties, the MLF frees up credit from private market sources to address the needs of smaller cities and counties. This is already evidenced by the significant increase in bank lending agreements that have been filed with EMMA, the Municipal Securities Rulemaking Board's online disclosure portal, since early April.

3. *Why were U.S. territories excluded from this facility?*

The MLF is open only to entities that were rated investment grade as of the facility's announcement to ensure compliance with provisions of the Federal Reserve Act, the Board's Regulation A, and the CARES Act. For example, under the Federal Reserve Act, FRBNY must assign a lendable value, consistent with sound risk management practices, to all collateral for a loan extended under section 13(3). The security for any loan under the MLF also must protect the taxpayer from losses. Both requirements are furthered by lending only to investment grade borrowers. The CARES Act also provides that the principal amount of any obligation issued by a State or municipality under a facility authorized by section 4003(b) of the Act shall not be reduced through loan forgiveness. This provision substantially restricts the MLF's ability to work out or resolve defaulting notes or other obligations that it has purchased. Restricting access to investment-grade issuers furthers compliance with this restriction by reducing the likelihood that the facility will hold debt that falls into default. Moreover, given the large number and

heterogeneous nature of issuers of municipal debt, it can be difficult to assess and compare their creditworthiness. Credit ratings provide an objective, transparent, and efficient means by which the agencies can assess the risk associated with lending to an issuer.

No U.S. territory is rated investment grade. Given their financial circumstances, additional debt that cannot be forgiven is unlikely to provide U.S. territories with substantial relief. Further, Puerto Rico is in default on its general obligation debt and would therefore be prohibited from accessing the Facility by the Board's Regulation A. Puerto Rico is the only U.S. territory with independent local governments, and the Federal Reserve is not aware of any local Puerto Rican government that carries an investment-grade rating. After Hurricanes Irma and Maria, the U.S. Virgin Islands and its power authority borrowed approximately $300 million from Federal Emergency Management Agency ("FEMA") through its Community Disaster Loan Program and have already sought loan forgiveness for such loans from FEMA because of their limited debt repayment capacity.

APPENDIX C

June 29, 2020

The Honorable French Hill
U.S. House of Representatives
Washington, DC 20515

The Honorable Donna E. Shalala
U.S. House of Representatives
Washington, DC 20515

Mr. Bharat Ramamurti
Commissioner
Washington, DC 20515

The Honorable Pat Toomey
United States Senate
Washington, DC 20510

Dear Members of the Congressional Oversight Commission:

We write in further response to your letter dated May 29, 2020, regarding the actions of the Department of the Treasury and the Board of Governors of the Federal Reserve System under Division A, Title IV, Subtitle A of the CARES Act. Please find attached answers to the Tier 2 questions posed by the Commission in your correspondence.

Sincerely,

Steven T. Mnuchin
Secretary
U.S. Department of the Treasury

Jerome H. Powell
Chair
Board of Governors of the
Federal Reserve System

Enclosure

Congressional Oversight Commission: Answers to Tier 2 Questions

I. General Questions

1. *If the agencies use economy-wide metrics, like GDP growth, unemployment rates, or wage growth, to assess the success or failure of this program how will they isolate the effects of this program from other factors, including other federal and state relief measures?*

The lending facilities put in place by the Board of Governors of the Federal Reserve System (the "Board"; together with the Federal Reserve Banks, the "Federal Reserve") with the support and approval of the Department of the Treasury ("Treasury"; together with the Federal Reserve, the "agencies") pursuant to the Coronavirus Aid, Relief, and Economic Security Act ("CARES Act") and under section 13(3) of the Federal Reserve Act (the "13(3) facilities") have two main goals—restoring financial market functioning and access to short-term funding markets and supporting the flow of credit to households, businesses, and communities. By doing so, these facilities will provide significant support for economic growth and employment. It is difficult to identify the causal effect of these government programs on macroeconomic aggregates isolated from other factors. Given the difficulty of measuring these impacts in real time, we monitor a variety of indicators to assess the effect of the facilities on a targeted market or area of the economy, as noted in our previous response to the Tier 1 questions. That being said, the agencies intend to explore in the longer-term a variety of techniques that have been successfully employed in economics and finance literature to isolate the effect of government programs.

2. *If the agencies use more narrow metrics, like bond spreads, to assess the success or failure of this program how will they assess how changes in those metrics affect the broader economy, including the financial well-being of the people of the United States?*

As noted in our previous response to the Tier 1 questions, the agencies will assess the performance of the 13(3) facilities by monitoring a wide range of indicators, such as issuance, maturity, outstandings, transaction costs, and spreads in a variety of debt and money market instruments. While it is difficult to directly measure how much improvements in these metrics will impact the broader economy or employment, these indicators can demonstrate the effectiveness of a specific facility on a targeted market or area of the economy.

For example, the Federal Reserve established the Primary Market Corporate Credit Facility ("PMCCF") and Secondary Market Corporate Credit Facility ("SMCCF") to backstop issuance and liquidity for corporate bonds and syndicated loans of issuers who were rated investment grade prior to the announcement of the facilities and maintain at least a BB-/Ba3 rating. Key indicators we monitor in the corporate credit markets include spreads on investment-grade debt, levels of issuance, bid-ask spreads, and dislocations between the investment-grade and high-yield markets. As noted by the Federal Reserve Bank of New York ("FRBNY"), the announcement of the PMCCF and SMCCF had a positive impact on these indicators.[1] These indicators have continued to show improved functionality in the corporate credit markets over

[1] Federal Reserve Bank of New York, *The Primary and Secondary Market Corporate Credit Facilities* https://libertystreeteconomics.newyorkfed.org/2020/05/the-primary-and-secondary-market-corporate-credit-facilities.html

the past few months. Improvements in these indicators can help to establish that the facilities have supported the flow of credit to businesses, thus allowing them to continue to operate, provide employment, and support the growth of the economy.

3. *Do the agencies believe the Fed's emergency lending programs are better suited to assist bigger companies that can access the capital markets than smaller firms that cannot? If not, why not? If so, what are the agencies doing to counteract that issue?*

The agencies have established eleven emergency lending facilities, which are each targeted at providing liquidity to a segment of the economy or financial markets. The overall intent of the facilities is to address the severe economic dislocations suffered by communities, households, and businesses of all sizes as a result of the COVID-19 pandemic and efforts to contain its spread.

The Federal Reserve and Treasury have worked to develop facilities that can provide assistance to both larger and smaller firms. The highly-developed and standardized bond market utilized by larger companies provides an established and effective mechanism for the Federal Reserve to alleviate dislocations in the large corporate credit markets, while the provision of corresponding support to small and medium-sized businesses has required the development of lending programs that make use of depository institutions as intermediaries to reach a broader and much more numerous universe of borrowers.

With regard to smaller and mid-sized businesses, the agencies have established the Main Street Lending Program (the Main Street New Loan Facility ("MSNLF"); the Main Street Priority Loan Facility ("MSPLF"); and the Main Street Expanded Loan Facility ("MSELF")). The Main Street Lending Program aims to provide credit to small businesses that have been impacted by the decline in economic activity and rely on banks to originate loans.[2]

The Federal Reserve's Term Asset-Backed Securities Loan Facility ("TALF") will provide additional support to small businesses by enabling the issuance of asset-backed securities backed by loans guaranteed by the SBA and certain other assets.

The Federal Reserve is actively engaged in conversations with small businesses and monitoring small business conditions, such as borrowing and lending. In addition, Federal Reserve staff are reaching out to banks, credit unions, community development financial institutions, other non-profit lenders, and small business groups to gather insights on the financial challenges of small businesses and the appropriate public policy response.

---

[2] In addition, with the approval of the Secretary of the Treasury, the Federal Reserve has established the Paycheck Protection Program Liquidity Facility ("PPPLF"). The PPPLF helps ensure that any limits on the balance-sheet capacity of a lender do not unduly curtail its ability to lend under the Paycheck Protection Program implemented by the Small Business Administration ("SBA") with support from Treasury. Treasury has not provided financial support for the PPPLF using funds made available under Division A, Title IV, Subtitle A of the CARES Act or otherwise.

4. *Will the agencies faithfully follow the statutory requirements of Subtitle A when implementing the lending programs and facilities?*

Yes. The statutory requirements applicable to Treasury's investments are incorporated into the fundamental structure and terms of the facilities as set forth in the governing term sheets, frequently asked questions, required certifications and transaction documentation published for each facility. As discussed further below and as provided in the program documentation, participants in the facilities are required to make representations and warranties and submit certifications and undertakings as to compliance with relevant statutory requirements. In addition, the Board has complied with its obligation to regularly report to Congress on the facilities and has gone beyond statutory requirements to voluntarily provide enhanced public disclosure with respect to each of the 13(3) facilities that makes use of CARES Act funding. The agencies recognize the important public policy objectives behind these statutory requirements, which align with the agencies' goals of targeting the provision of credit to those employers, consumers, and municipalities in need of support during this extraordinary period.

5. *How can the agencies best determine the lending capacity of, and Treasury investment into, each Fed lending facility under Subtitle A in order to help support and stabilize the economy?*

In establishing each of the 13(3) facilities that involve a Treasury investment of funds authorized under the CARES Act, a determination is made jointly by the agencies regarding the maximum amount of Federal Reserve lending that will be supported by a given investment of Treasury loss-absorbing capital. This ratio constitutes the "gearing ratio" for the overall facility, and in certain cases is arrived at by the specification of individual gearing ratios for particular classes of credit exposure to be assumed by the facility. Consistent with section 13(3) of the Federal Reserve Act, the agencies establish the gearing ratio for a particular facility to ensure that the Federal Reserve is unlikely to suffer losses on its lending, even in downturn scenarios.

For instance, the SMCCF will leverage Treasury equity at 10 to 1 when acquiring corporate bonds of issuers that are investment grade at the time of purchase and when acquiring ETFs whose primary investment objective is exposure to U.S. investment-grade corporate bonds. The SMCCF will leverage Treasury equity at 7 to 1 when acquiring corporate bonds of issuers that are rated below investment grade at the time of purchase and in a range between 3 to 1 and 7 to 1, depending on risk, when acquiring any other type of eligible asset. Correspondingly, the PMCCF will leverage Treasury equity at 10 to 1 when acquiring corporate bonds or syndicated loans from issuers that are investment grade at the time of purchase. The PMCCF will leverage its equity at 7 to 1 when acquiring any other type of eligible asset. Thus, given the initial allocation of $25 billion in Treasury equity to the SMCCF and $50 billion to the PMCCF, the maximum potential combined size of the two facilities is $750 billion assuming that the maximum 10 to 1 gearing ratio is applicable to all facility exposures. However, the facilities stand ready to assume (and in the case of the SMCCF have already assumed) non-investment grade exposures that correspond to a lower gearing ratio in view of their higher level of underlying credit risk. So the ultimate maximum size of each corporate credit facility will depend on the nature—and associated gearing ratio—of the exposures assumed.

The agencies monitor facility usage on an ongoing basis, including asset composition and associated underlying gearing ratios where relevant. Using the authority provided by the CARES Act, Treasury stands ready to allocate further equity contributions to existing or new 13(3) facilities where warranted in order to support U.S. economic recovery.

6. *How can the agencies best determine how much of the Treasury's $454 billion in CARES Act funds to allocate among Fed lending facilities and when to allocate such funds in order to help support and stabilize the economy?*

In the evolving context of the COVID-19-related economic disruption, the current set of CARES-funded 13(3) facilities—supported by $195 billion out of the total $454 billion authorized amount of CARES Act funds—represents the agencies' best judgment as to a broad-based and effective initial set of lending measures to support U.S. economic activity and employment under the severe strains presented by the pandemic. These facilities cover a broad spectrum of U.S. economic activity and funding markets—including states and municipalities, small to medium-sized businesses, large corporate issuers, and market-based finance supporting auto loans, student loans, credit card funding, equipment loans and leases, commercial mortgages and small business loans guaranteed by the SBA.

As indicated most recently by the proposed expansion of the Main Street Lending Program to cover non-profit borrowers, the agencies have exhibited a continuous willingness to expand existing facilities or introduce new facilities where an unaddressed need for liquidity presents itself. As the full set of these introduced facilities achieves operational functionality, the agencies will rigorously assess the adequacy and appropriateness of the 13(3) facilities' coverage and the corresponding allocations of CARES Act funds.

Where readjustment or increased commitment is necessary, the agencies stand ready to act using the full scope of authority provided by section 13(3) of the Federal Reserve Act and CARES Act appropriations.

7. *How can the agencies best estimate the risk of loss to taxpayer funds in each Fed lending facility?*

In accordance with the statutory and regulatory requirements applicable to Federal Reserve lending under section 13(3) of the Federal Reserve Act—and consistent with statements in its regular periodic reports to Congress—the Federal Reserve does not expect to incur losses with respect to the loans it has extended as part of any of its currently authorized and outstanding 13(3) facilities. For 13(3) facilities that are supported by Treasury's investments of capital using funds appropriated under the CARES Act, such equity contributions function as credit protection for the Federal Reserve and are inherently exposed to loss. Whether any loss in respect of Treasury funds will ultimately be sustained in a given facility depends on a number of factors relating to future U.S. economic conditions as well as the future operational performance of the facilities.

In coordination with the Office of Management and Budget and applying relevant provisions of the Federal Credit Reform Act of 1990, Treasury has modeled the estimated lifetime cost of

its investment in each facility to which it has committed funds appropriated by the CARES Act. This modeling, based on estimated expected cash flows on a net present value basis, takes into account a range of possible future economic scenarios. The ultimate loss or gain on Treasury's investment will depend, among other things, on the future path of U.S. economic and financial market performance. Overall, the terms and conditions of each facility involving CARES Act funds have been set by the agencies with a view toward achieving an appropriate balance between taxpayer protection and the achievement of program policy goals.

8. *How will the Fed ensure it complies with all restrictions to emergency lending under Section 13(3) of the Federal Reserve Act, including those prohibiting lending to insolvent borrowers?*

Section 13(3) of the Federal Reserve Act and the Board's Regulation A allow the Board to authorize a Reserve Bank to extend credit under certain conditions, including that the circumstances are "unusual and exigent," that the facility is "broad-based," that the borrower lacks adequate credit accommodations but is not "insolvent," that the facility protects taxpayers from loss, and that the facility charges an interest rate that is set at a premium to normal market conditions. In determining whether to authorize a facility under Section 13(3), the Board considers a range of economic and financial information, including data such as yields or spreads on debt, to reach the determination that circumstances are unusual and exigent. The Board also carefully sets the features of the proposed facility to ensure that the program is broad-based, that taxpayers are well protected, and that the interest rate charged to borrowers is set at a premium to normal market conditions. The Federal Reserve ensures compliance with statutory provisions related to borrower insolvency and availability of adequate credit accommodations by requiring borrowers to provide certifications regarding their solvency and the availability of adequate credit accommodations.

9. *How can the agencies best monitor compliance with and enforce the conflict of interest rules governing the agencies' lending programs and facilities?*

Section 4019 of the CARES Act requires entities that seek to enter into a transaction with a facility under Section 4003 to certify that they comply with the Act's conflict of interest requirements. The Federal Reserve mandates that participants submit these certifications to the Federal Reserve as part of the participant eligibility process. Participants are required to maintain a file documenting the basis for each certification submitted to the Federal Reserve. The files are subject to auditor attestation or direct inspection by the Federal Reserve to check their accuracy.

In addition, the Federal Reserve and Treasury monitor and enforce conflict of interest rules applicable to their employees. Federal Reserve and Treasury employees are subject to 18 U.S.C. § 208. Section 208, in relevant part, prohibits Federal Reserve and Treasury employees from participating personally and substantially in matters in which, to the employee's knowledge, the employee or certain related parties has a financial interest directly and predictably affected by the matter. Federal Reserve Banks also share a common Code of Conduct that incorporates the requirements of Section 208 and additionally instructs employees to avoid any situation that might create an appearance of a conflict of interest.

The Federal Reserve also imposes substantial conflicts of interest restrictions on the vendors it employs to administer its emergency lending facilities. *See, e.g.*, BlackRock Investment Management Agreement (https://www.newyorkfed.org/medialibrary/media/markets/SMCCF_Investment_Management_Agreement.pdf).

10. *How can the agencies best enforce the statutory terms and conditions for borrowers under their lending programs and facilities under Subtitle A, including the condition that borrowers are U.S. businesses, as defined by the CARES Act?*

The agencies have incorporated applicable provisions of the CARES Act directly into the terms of the facilities and require borrowers and counterparties to execute certifications regarding CARES Act eligibility requirements prior to participating in the 13(3) facilities. The methods differ depending on the facility structure.

With respect to the U.S. business requirement in particular, there are common elements of the certifications across each facility. Where certifications are required, they must be made in writing by the applicable institution's chief executive officer and chief financial officer, or individuals performing similar functions. If the certifying entity no longer meets the U.S. business test, the institution must immediately notify the Reserve Bank. If the certification is found to have included a knowing material misrepresentation, the Board or the Reserve Bank will promptly refer the matter to appropriate law enforcement authorities. There may be other consequences as well. For example, under PMCCF and the Main Street Lending Program, the extension of credit will also become immediately due and payable. Under the TALF, the facility's loan to the borrower automatically converts from a limited recourse loan into a recourse loan.

11. *How will loans under these programs and facilities comply with Bank Secrecy Act (BSA) and the Anti-Money Laundering (AML) rules?*

The Federal Reserve and Treasury place a high priority on compliance with the Bank Secrecy Act and anti-money laundering ("BSA/AML") requirements and on preventing illicit financial activity from occurring within the Federal Reserve lending facilities supported by Treasury equity investments under section 4003(b) of the CARES Act. Although under U.S. law Federal Reserve entities are not explicitly subject to BSA/AML rules, for those Federal Reserve facilities that are intermediated through banks and other U.S. financial institutions, including the CARES Act facilities, the participating institution is required to apply its BSA/AML policies and procedures to its customers.

Under the Main Street Lending Program, the eligible lenders that originate the Main Street loans are banking organizations, all of which are subject to extensive BSA/AML requirements, including the requirement to maintain an adequate BSA/AML compliance program, customer due diligence (CDD) program, and suspicious activity transaction monitoring program. Likewise, under the TALF, each eligible borrower is required to establish an account with a "TALF Agent"—a financial institution specially designated by FRBNY, and currently comprised

of primary dealers who also serve the Federal Reserve as counterparties in its open market operations. TALF Agents are required to subject all prospective borrowers to their BSA/AML compliance programs and to report suspicious activity to law enforcement as required by law.

The CARES Act corporate credit facilities, the PMCCF and the SMCCF, also are structured to minimize risk of financial fraud. Generally speaking, these facilities involve relatively low BSA/AML risk, as they are mostly limited to purchasing U.S. corporate bonds of issuers with investment-grade credit ratings as of the day before announcement of the facility, as well as U.S.-listed bond ETFs. More specifically, the Investment Manager for the facilities is obligated to, among other things, manage the facilities in accordance with all laws and regulations applicable to it, including BSA/AML requirements.

Finally, the Municipal Lending Facility ("MLF") likewise entails relatively low BSA/AML risk, since it mostly involves the purchase of investment-grade notes issued by a U.S. state or local governmental authority. Nevertheless, an affiliate of Bank of New York Mellon, which provides, among other things, settlement services for the facility, must comply with applicable BSA/AML rules.

12. *How will the agencies decide when to hire third parties to help manage the program or specific facilities? How will the agencies mitigate conflicts of interest these third parties might have?*

The Federal Reserve balances various factors when evaluating whether and when to hire third parties to help manage the emergency lending programs and facilities. Some key considerations include expertise and timing. The Federal Reserve often needs specialized knowledge and expertise possessed by third parties, which can be leveraged to establish and operate the programs and facilities in an effective and timely manner. On timing and duration, the Federal Reserve considers how quickly and urgently the program or facility needs to become operational, as well as the expected duration of the program or facility. Third parties are often the most effective option to support the robust establishment of programs and facilities while mitigating potential delays and unnecessary costs.

In agreements with third-party vendors, the Federal Reserve has incorporated contractual terms to mitigate conflicts of interest. Examples of provisions include, but are not limited to:

- Requirements to maintain the confidentiality of non-public information;
- Prohibitions against use of non-public information for vendor's own benefit or the benefit of another client;
- Requirements to wall-off particular staff members from other members of the firm, when appropriate;
- Requirements for adequate information barrier procedures and training on those procedures;
- Requirements for acceptable processes to identify, escalate and remediate conflicts of interest; and

- Requirements to comply with reviews and audits by Federal Reserve and other appropriate oversight bodies.

The Federal Reserve has published program and facility-related contracts, including vendor contracts. Those contracts are available here:

- https://www.newyorkfed.org/aboutthefed/vendor_information.html; and
- https://www.bostonfed.org/supervision-and-regulation/supervision/special-facilities/main-street-lending-program/vendors.aspx.

Additionally, the Federal Reserve has established hotlines for members of the public to make anonymous reports on any illicit or unethical behavior in connection with any of the facilities (FRBNY Integrity Hotline: 877-52-FRBNY (877-523-7269) or https://secure.ethicspoint.com/domain/media/en/gui/58813/index.html).

13. *Regarding outside services to assist the agencies to manage the programs and facilities, what is the competitive selection process for custody and fund management services? How are conflicts of interest mitigated?*

The Federal Reserve employed a competitive selection process when engaging outside services relating to custody and fund management services, unless it determined that an exception was appropriate due to an urgent and exigent need to expeditiously support financial markets. As part of the competitive selection process, the Federal Reserve issued Requests for Proposals ("RFPs") and evaluated potential vendors based on quantitative and qualitative criteria the Federal Reserve deemed relevant for the particular program or facility. The contracts for vendors engaged without an RFP process are for a limited duration. For those contracts, the Federal Reserve anticipates engaging in a competitive selection process once economic circumstances permit, if the need for the outside service persists.

The application of these principles to each facility is outlined below.

- Main Street Lending Program: An RFP was issued for custodian and accounting administration services. This RFP considered implementation and operational capabilities, as well as overall qualifications needed to support the program. A separate RFP was issued for a vendor to provide asset purchase intake and due-diligence as well as credit administration services for this facility. This second RFP considered technological and operational capabilities, the ability to deliver a control environment across an integrated solution, and technical expertise needed to execute the defined services.
- Municipal Liquidity Facility: A vendor was selected through an RFP process to serve as the custodian and administrator. This RFP focused chiefly on operational capabilities.
- Primary Market and Secondary Market Corporate Credit Facilities: A separate RFP was issued for each of custody services and fund management services. The RFPs considered implementation and operational capabilities, as well as overall qualifications needed to support the facility.

- Term Asset-Backed Securities Loan Facility: Given the urgent and exigent need to expeditiously support financial markets, FRBNY authorized an exception to the competitive bidding process. The custodian/administrator and collateral monitor were both selected on a short-term basis after considering the custodian/administrator's operational and technological capabilities and the collateral monitor's knowledge and experience in the asset-backed securities market, as well as both agents' prior experience with TALF, which have allowed for a quick time to market.

Federal Reserve employees are subject to 18 U.S.C. § 208. Section 208, in relevant part, prohibits Federal Reserve employees from participating personally and substantially in matters in which, to the employee's knowledge, the employee or certain related parties has a financial interest directly and predictably affected by the matter. Federal Reserve Banks also share a common Code of Conduct that incorporates the requirements of Section 208 and additionally instructs employees to avoid any situation that might create an appearance of a conflict of interest.

In connection with the programs and facilities, Federal Reserve employees who personally and substantially participate in the vendor selection process certify that they have no conflicts with any of the prospective vendors involved in the selection process. If a particular conflict of interest cannot be resolved in consultation with Federal Reserve compliance staff, that individual is recused from the selection process.

Contracts with prospective vendors are carefully reviewed by Federal Reserve staff. In contract negotiations with each vendor, Federal Reserve staff ensure that the agreements contain appropriate contract language regarding identification and mitigation of conflicts. Staff also review the vendors' conflict of interest policies and procedures, and help resolve potential conflicts highlighted by vendors.

The Federal Reserve has published program and facility related contracts, including vendor contracts. Those contracts are available at the links provided above.

14. *The agencies' emergency lending programs and facilities provide lending directly through government loans and indirectly through banks and other qualified lenders. What are the trade-offs involved with these different delivery mechanisms?*

The agencies have designed each facility to provide credit to a particular market or class of borrower in the most efficient and effective manner possible. Where it has made sense to do so, the agencies have used existing lending channels to provide support to the economy.

In the case of several facilities that have been established to support access to credit via securities and capital markets, including the PMCCF, SMCCF, and MLF, the facilities are able to acquire bonds from issuers and market participants directly, relying significantly on external credit ratings in the evaluation of credit quality. In designing and implementing these facilities, the agencies have chosen to make use of existing modes of debt capital markets financing in order to maximize the effectiveness of the facilities in achieving policy aims. Reflecting existing securities market financing techniques, the PMCCF may acquire bonds not only as the sole

investor but may also acquire a portion of a syndicated bond issue. Further, recognizing that corporate borrowers rely not only on bond issuance but also on bank lending, the agencies have provided that the PMCCF may also purchase portions of a syndicated bank loan at issuance. Likewise, the SMCCF leverages existing market infrastructure by not only acquiring individual corporate bonds from primary dealers that have qualified as eligible sellers, which specialize in making markets in such debt, but also by acquiring shares of U.S.-listed ETFs whose investment objective is to provide broad exposure to the market for U.S. corporate bonds. This, along with the facility's purchases of individual bonds to track a broad, diversified market index developed by the Federal Reserve, represents a particularly efficient way to provide broad support for the corporate bond market.

In the case of the Main Street Lending Program, which provides financing to small and medium-sized businesses, the agencies will leverage existing channels of bank lending by acquiring participations in loans extended to borrowers by financial institutions. The loans in which the facility will acquire participations and associated documentation must contain specific terms that incorporate applicable CARES Act requirements and restrictions. Relying on bank intermediation as a central element of the Main Street Lending Program allows the agencies to take advantage not only of lending institutions' existing customer relationships but also their underwriting expertise to reach a broad and heterogenous class of borrowers that generally lack the external ratings or public credit standing necessary to access the securities markets.

With the establishment of the TALF, the agencies are supporting the securitization markets that fund a substantial share of credit to consumers and businesses. The TALF is designed to increase credit availability for businesses and consumers by facilitating the issuance of ABS backed by loans to consumers and businesses at more normal interest rate spreads. In providing credit to borrowers that acquire securities backed by consumer receivables and other such assets, the TALF is able to provide support to the consumers to whom it would be impractical to lend directly and to provide another means of support to businesses beyond what is available under the PMCCF, SMCCF and the Main Street Lending Program.

15. *While quickly providing lending to borrowers may result in more fraud and abuse, it may also assist many eligible borrowers that need money quickly. How should the agencies balance these trade-offs?*

The agencies have worked hard to establish and implement the 13(3) facilities as quickly as possible given the urgent need to support market functioning and economic activity. However, in doing so, the agencies have also sought to ensure that the facilities are being used appropriately by eligible parties.

In addition to required certifications related to CARES Act eligibility requirements, discussed above, mandatory certifications required in order to participate in the CARES Act 13(3) facilities also cover restrictions and eligibility requirements imposed by section 13(3) of the Federal Reserve Act and the Board's Regulation A, particularly the requirements that (i) credit not be provided to an entity that is insolvent and (ii) participants in the facility must be unable to secure adequate credit accommodations from other banking institutions. If the facility participant includes a knowing material misrepresentation in its certification, all extensions of

credit made by the facility to the participant would become immediately due and payable. The participant would also be referred to the relevant law enforcement authorities for investigation. In addition, the Main Street facilities' reliance on bank lending channels will help reduce borrower fraud and abuse.

16. *The Congressional Budget Office (CBO) recently published its preliminary estimate of the budgetary effects of the CARES Act. CBO's estimate concludes that "the income and the costs stemming from" the Fed's emergency lending facilities funded by the CARES Act "are expected to roughly offset each other." CBO notes that the Fed did "not sustain losses on similar lending . . . [d]uring the financial crisis of 2008 and 2009." Do you believe CBO is correct in its assumptions of a no net cost result? In order to accomplish the goal of economic stabilization and return to economic growth, is this a reasonable assumption?*

The CBO prepares its estimates under its own statutory mandate and in a manner that is separate and independent from the agencies' administration of the 13(3) facilities. Consequently, the agencies do not believe it would be appropriate to directly comment on the assumptions or conclusions CBO has arrived at in fashioning its published estimate.

As noted above in response to Question 7, the Federal Reserve does not expect to incur loss with respect to the loans it has extended as part of any of its currently authorized and outstanding 13(3) facilities. For 13(3) facilities that are supported by Treasury's investment of loss-absorbing capital using funds appropriated under the CARES Act, such equity contributions function as credit protection for the Federal Reserve and are inherently exposed to loss. Whether any loss in respect of Treasury funds will ultimately be sustained in a given facility depends on a number of factors relating to future U.S. economic conditions as well as the future operational performance of the facilities.

17. *How can the agencies best incentivize private-sector financial institutions to help facilitate the Treasury and the Fed's lending programs and facilities to ensure credit gets to American households and businesses, while ensuring that taxpayer dollars are well spent?*

As discussed above, the agencies have structured the facilities to take advantage of, when appropriate, existing lending channels to increase efficiency and the provision of credit. In particular, the agencies have structured the TALF and the Main Street Lending Program in a way that leverages existing financing structures. Under the TALF, the facility provides credit to borrowers to permit them to acquire ABS, CMBS, and CLOs that are in turn pledged as collateral for the loan. Lending is conducted by the facility at a premium to normal market rates, in accordance with section 13(3) of the Federal Reserve Act and Regulation A, which helps ensure that the facility appropriately functions as a funding backstop that will naturally lose economic appeal as private funding markets return to a more normalized condition over time.

The Main Street Lending Program's purchase of 95 percent participations will make it easier for financial institution lenders to extend credit during the current challenging environment. At the same time, the lenders must agree to certain covenants that are intended to preserve the credit position of the Main Street facility against certain actions that lenders might otherwise be incentivized to take. Specifically, lenders must commit that they will not request that the

borrower repay debt extended by the lender to the borrower or pay interest on such outstanding obligations until the Main Street loan is repaid in full, unless the debt or interest payment is mandatory and due or in the case of default and acceleration. Each lender also must commit that it will not cancel or reduce any existing committed lines of credit to the borrower, except in an event of default.

18. *How can the agencies best set rates and fees for the Treasury and the Fed's lending programs and facilities under Subtitle A to ensure their workability and that the federal government remains the lender of last resort?*

Under section 13(3) of the Federal Reserve Act and the Federal Reserve's Regulation A, the interest rates and fees payable by borrowers under a 13(3) facility must be set at levels generally higher than the rates that would have been paid by such borrowers under the normal market conditions that prevailed prior to the onset of the "unusual and exigent circumstances" that gave rise to the 13(3) authorization. By setting rates that meet that standard—but that are nonetheless lower than rates that might prevail in highly disrupted, poorly functioning markets adversely affected by the COVID-19 disruption—the pricing terms of the facilities can be set in a manner that enables the facility to function as an effective lending backstop while still properly conforming to a "lender of last resort" role that limits overreliance on public sector credit.

19. *What will the effect of Treasury and Fed lending be on overall employment?*

The Federal Reserve and the Treasury have designed the 13(3) facilities to improve the functioning of financial markets and improve economic conditions broadly, including, in particular, overall employment. As we noted in our response to Question 1, it is difficult to identify the causal effect of government programs on macroeconomic aggregates. A variety of techniques have been successfully used in the economics and finance literature. For example, there is a substantial amount of evidence that financial conditions impact real economic activity. More generally, if firms, states, and localities were to be shut out of credit markets, many would be pressured to slash payrolls to control costs. Some might shut down completely. Our section 13(3) facilities help alleviate those pressures by supporting the flow of credit. However, making precise estimates in real time is a significant challenge.

To meet this challenge, we monitor a variety of market and economic indicators to assess the performance of the facilities as noted in our previous response to Tier 1 questions.

20. *Do the agencies believe it is appropriate to modify the facilities to ensure specific companies or industries have access to some or all of the funds? If so, how are those modifications being considered in a manner that also addresses all industries and sectors?*

The lending facilities that the agencies have established using CARES Act authority and section 13(3) of the Federal Reserve Act are, individually and collectively, broad-based programs that are intended to support liquidity and economic activity across a wide range of industries and business sectors, including the state and municipal sectors. The agencies are committed to continuous evaluation of these programs to identify and fill any unwarranted gaps in the scope of the facilities. The agencies have demonstrated—and will continue to

demonstrate—willingness to adjust the terms and scope of programs to address the liquidity needs of additional broad classes of borrowers whose inclusion would further program goals.

II. Program and Facility-Specific Questions

Primary Market Corporate Credit Facility (PMCCF)

1. *Through this facility, the Fed, through an SPV, will be purchasing new bonds from companies. Do the agencies intend to place limitations or parameters around companies receiving this support, or use of proceeds? Are such limitations workable in capital markets transactions? Do the agencies believe the proceeds of bond purchases will help stabilize the economy regardless of how the proceeds are used?*

The purpose of the PMCCF is to ensure that creditworthy companies that rely on capital markets to fund their operations have access to credit during the current unusual and exigent circumstances. The PMCCF offers terms, conditions, and pricing that are intended to support companies in times of stress but discourage use of the facility as economic conditions improve.

While the CARES Act applies capital distribution and executive compensation restrictions to programs or facilities that provide direct loans, Congress explicitly exempted securities and capital markets transactions, as well as syndicated loans, from these provisions. Because the PMCCF purchases bonds, which are securities and capital markets transactions, and participates in syndicated loans, the CARES Act direct loan provisions do not apply to the PMCCF. The PMCCF complies with all requirements of the CARES Act that apply, including the U.S. business and conflict of interest provisions.

The agencies have designed the PMCCF to charge an interest rate that is a premium to normal market conditions and to impose use of proceeds restrictions on participants that are U.S. subsidiaries of foreign companies, but otherwise to impose contractual obligations that mirror standard market terms. The PMCCF's requirement that the proceeds of bond purchases from, or loans made to, U.S. subsidiaries of foreign companies are used in the United States is consistent with the U.S business requirement in the CARES Act. The PMCCF's premium interest rate is consistent with the Board's emergency lending regulation and long-standing policies. Imposing additional restrictions on capital markets transactions that are not consistent with standard market terms could limit the PMCCF's ability to support the corporate credit markets and could, therefore, reduce the ability of U.S. companies to preserve their operations and maintain payrolls.

There is a substantial amount of evidence that financial conditions impact real economic activity. Difficulties in accessing debt at rates and in quantities consistent with typical market functioning negatively affect the economy and increase the probability of very severe recessions. Bond purchase programs, such as the PMCCF, help to ensure that corporations have access to sufficient credit at rates that are not as high as they might otherwise be during an unprecedented period of financial market disruption and economic uncertainty. This economic benefit could derive less from actual PMCCF purchases, which may turn out to be small, than from its presence as a backstop, which reduces uncertainty and bolsters confidence that credit

markets will continue to function rather than exacerbate economic difficulties. By improving the cost of and access to credit, PMCCF potential and actual bond purchases help to ensure that corporations can maintain existing operations and continue to invest in the U.S. economy. In turn, this helps to stabilize the economy.

2. *The Federal Reserve Bank of New York, which is implementing this facility, recently stated that a U.S. subsidiary of a foreign company can qualify for support through the facility. How does the Federal Reserve Bank of New York plan on enforcing its requirement that proceeds derived from participation in the facility may only be used for the benefit of the U.S. subsidiary issuer, its consolidated U.S. subsidiaries, and affiliates of the U.S. subsidiary issuer that are U.S. businesses, rather than for the benefit of its foreign affiliates?*

The Federal Reserve is requiring that issuers that are U.S. subsidiaries of foreign companies use any PMCCF borrowings to support their U.S. businesses and U.S. employees. This is a requirement that goes beyond what the law mandates.

Specifically, provided that other requirements are met, an issuer to the PMCCF must be created or organized in the United States or under the laws of the United States. An issuer may be a subsidiary of a foreign company, provided that (i) the issuer itself is created or organized in the United States or under the laws of the United States, and (ii) the issuer on a consolidated basis has significant operations in and a majority of its employees based in the United States. An issuer in the PMCCF that is a U.S. subsidiary of a foreign company must use the proceeds derived from participation in the PMCCF only for the benefit of the issuer, its consolidated U.S. subsidiaries, and other affiliates of the issuer that are U.S. businesses, and not for the benefit of its foreign affiliates.

Additional protection is offered by the fact that the CEO and CFO (or the individuals performing similar functions) of the issuer must certify to compliance with this requirement in order to borrow from the PMCCF. The issuer will be required to keep records of its certification process and underlying due diligence. These records will be available to the Federal Reserve upon request. A knowing material misrepresentation in these certifications would provide a basis for the Federal Reserve to refer the matter to law enforcement authorities.

In addition, the issuer will be contractually bound. The standard form PMCCF transaction documents require that the issuer ensure that funds will not be used for the benefit of foreign affiliates, and require immediate repurchase of the bond if this requirement is violated.

Main Street Lending Program

1. *Do the agencies plan to expand eligible lenders in this program beyond depository institutions? Why or why not?*

A wide range of financial institutions are eligible to participate in the Main Street Lending Program. Eligible Lenders include U.S. federally insured depository institutions (banks, savings associations, and credit unions), U.S. branches or agencies of foreign banks, U.S. bank holding

companies, U.S. savings and loan holding companies, U.S. intermediate holding companies of foreign banking organizations, or any U.S. subsidiary of any of the foregoing.

Recognizing that small and medium-sized businesses often access credit through a variety of sources and types of institutions, the Federal Reserve is studying the feasibility of expanding the scope of eligible lenders in the future.

Municipal Lending Facility

1. *What conditions, if any, including those related to policies, will the agencies impose on states and municipalities that receive funding under this facility?*

The MLF imposes no policy conditions on eligible issuers other than restrictions on the use of note proceeds. An eligible issuer may use the proceeds of notes purchased by the MLF to help manage the cash flow impact of income tax deferrals resulting from an extension of an income tax filing deadline, deferrals or reductions of tax and other revenues or increases in expenses related to or resulting from the COVID-19 pandemic, and requirements for the payment of principal and interest on obligations of the issuer or its political subdivisions or other governmental entities. An eligible State, City, or County issuer also may use the proceeds of the notes purchased by the MLF to purchase similar notes issued by, or otherwise to assist, political subdivisions and other governmental entities of the issuer for the purposes enumerated in the prior sentence.

2. *What is the rationale for the three-year repayment terms under this facility?*

The MLF was designed as a short-term lending program to provide bridge financing to states, localities, and their subdivisions or other governmental entities facing sudden disruptions in their short-term cash flows as a result of the COVID-19 pandemic. The Federal Reserve established the MLF in response to rapid deterioration in the municipal securities market at a time when it appeared unlikely that the short-term municipal securities market could fully meet the demand for short-term municipal note issuance. The MLF was not designed to provide long-term financing for capital infrastructure projects because the long-term municipal capital markets appear to have been disrupted for only a relatively short period. A relatively short repayment term is also consistent with the Federal Reserve's mandate under section 13(3) and the Board's Regulation A to design facilities that provide credit in unusual and exigent circumstances, but encourage repayment of the credit and disuse of the facility as the unusual and exigent circumstances recede. Short repayment terms also allow the agencies to buy and hold municipal securities and passively exit the market without causing significant disruption as market conditions normalize.

The facility was initially announced with a two-year repayment term. After the initial announcement of the facility, the agencies extended the maximum repayment term to three years based on feedback from states and municipalities. The longer term was intended to provide more flexibility for issuers to manage their cash flow and liquidity challenges through the COVID-19 pandemic and uncertain economic recovery and provide more time for fiscal recovery and repayment or refinancing of the notes.

3. *Will the agencies disclose information about any states, counties, and cities whose applications for loans from this facility are denied?*

The agencies do not expect to deny applications to issue notes to the facility because the MLF does not make individualized credit determinations for entities seeking to issue notes to the facility. Instead, the MLF's eligibility and pricing are based upon objective, transparent criteria. For example, the most recent MLF term sheet includes a list of eligible issuers, maximum borrowing amounts, use of proceeds limitations, and credit ratings-based eligibility and pricing criteria. Applications that meet these public criteria will be approved. If these criteria are not met, the issuer would know in advance and would be unlikely to apply.

The MLF is committed to transparency and will fully meet its disclosure obligations pursuant to section 13(3) of the Federal Reserve Act, the Board's Regulation A, and the CARES Act.

Loans for the Airline Industry and National Security Businesses Under Subtitle A

1. *How many applications has the Treasury received for loans under Subtitle A?*

The CARES Act provides funding for up to $46 billion in loans to provide liquidity to certain eligible businesses related to losses incurred as a result of coronavirus. Eligible businesses include air carriers and related U.S. businesses that have not otherwise received adequate economic relief in the form of loans or loan guarantees provided under the CARES Act and businesses critical to maintaining national security.

Specifically, $25 billion is available for loans to passenger air carriers; eligible businesses that are certified under 14 CFR Part 145 and approved to perform inspection, repair, replace, or overhaul services ("Part-145 certified repair station operators"); and ticket agents as defined in 49 U.S.C. § 40102. In addition, $4 billion is available for loans to cargo air carriers, and $17 billion is available for loans to businesses critical to maintaining national security.

Treasury has released guidance and application materials and, as of June 16, 2020, has received 190 applications from air carriers, Part-145 certified repair station operators, and ticket agents. As of June 17, 2020, Treasury has received 70 applications for the national security loan program, 25 of which meet one of the two national security eligibility criteria established by Treasury, although one of those has been withdrawn.

2. *How is the Treasury measuring and evaluating any proposals that loan applicants submit "on the form and amount of taxpayer protections they propose to provide" as part of their loan agreements, such as a warrant or equity instrument in an applicant's business?*

Section 4003(d) of the CARES Act generally requires that Treasury receive a warrant or equity instrument in the borrower if the borrower is a public company, or a warrant, equity instrument, or senior debt instrument if the borrower is a private company. Applicants were invited to submit proposals on the form and amount of taxpayer protections they proposed to

provide. Together with the other data and information provided in the applications, Treasury will develop standards for adequate and appropriate taxpayer protections.

Treasury has not yet determined the final form of taxpayer protection that will be required, but anticipates applying a uniform standard that satisfies the requirements of Section 4003(d).

3. *When does the Treasury anticipate approving and disbursing these loans?*

Treasury is continuing to review loan applications in accordance with its statutory obligations, communicate with applicants as appropriate, and make determinations regarding the timing of loan approvals and disbursements. Treasury anticipates approving and disbursing loans in the near future.

4. *Under Subtitle A, the Treasury's loan agreements with the airline industry and businesses critical to maintaining national security must require a borrower to "not reduce its employment levels by more than 10 percent from the levels" as of March 24, 2020. How does Treasury intend to faithfully apply this statutory requirement?*

Treasury intends to include this statutory requirement as a covenant in the loan agreements between Treasury and each borrower. Specifically, to receive a loan, a borrower must agree that, until September 30, 2020, it will maintain employment levels as of March 24, 2020 to the extent practicable, and in any case not reduce its employment levels by more than 10 percent from the levels on such date.