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# Federal Reserve Announces the Creation of the Term Asset-Backed Securities Loan Facility

Federal Reserve System: Board of Governors

# Press Release

November 25, 2008

## Federal Reserve announces the creation of the Term Asset-Backed Securities Loan Facility (TALF)

For release at 8:15 a.m. EST

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The Federal Reserve Board on Tuesday announced the creation of the Term Asset-Backed Securities Loan Facility (TALF), a facility that will help market participants meet the credit needs of households and small businesses by supporting the issuance of asset-backed securities (ABS) collateralized by student loans, auto loans, credit card loans, and loans guaranteed by the Small Business Administration (SBA).

Under the TALF, the Federal Reserve Bank of New York (FRBNY) will lend up to $200 billion on a non-recourse basis to holders of certain AAA-rated ABS backed by newly and recently originated consumer and small business loans. The FRBNY will lend an amount equal to the market value of the ABS less a haircut and will be secured at all times by the ABS. The U.S. Treasury Department--under the Troubled Assets Relief Program (TARP) of the Emergency Economic Stabilization Act of 2008--will provide $20 billion of credit protection to the FRBNY in connection with the TALF. The attached terms and conditions document describes the basic terms and operational details of the facility. The terms and conditions are subject to change based on discussions with market participants in the coming weeks.

New issuance of ABS declined precipitously in September and came to a halt in October. At the same time, interest rate spreads on AAA-rated tranches of ABS soared to levels well outside the range of historical experience, reflecting unusually high risk premiums. The ABS markets historically have funded a substantial share of consumer credit and SBA-guaranteed small business loans. Continued disruption of these markets could significantly limit the availability of credit to households and small businesses and thereby contribute to further weakening of U.S. economic activity. The TALF is designed to increase credit availability and support economic activity by facilitating renewed issuance of consumer and small business ABS at more normal interest rate spreads.

TALF Terms and conditions

Last Update: November 25, 2008

**Term Asset-Backed Securities Loan Facility (TALF)**
**Terms and Conditions**[1]

## *Facility*

The TALF will be a Federal Reserve credit facility authorized under section 13(3) of the Federal Reserve Act. The TALF is intended to assist the credit markets in accommodating the credit needs of consumers and small businesses by facilitating the issuance of asset-backed securities (ABS) and improving the market conditions for ABS more generally.

The Federal Reserve Bank of New York (FRBNY) will make up to $200 billion of loans under the TALF. TALF loans will have a one-year term, will be non-recourse to the borrower, and will be fully secured by eligible ABS. The U.S. Treasury Department will provide $20 billion of credit protection to the Federal Reserve in connection with the TALF, as described below.

## *Eligible Collateral*

Eligible collateral will include U.S. dollar-denominated cash (that is, not synthetic) ABS that have a long-term credit rating in the highest investment-grade rating category (for example, AAA) from two or more major nationally recognized statistical rating organizations (NRSROs) and do not have a long-term credit rating of below the highest investment-grade rating category from a major NRSRO.

All or substantially all of the credit exposures underlying eligible ABS must be newly or recently originated exposures to U.S.-domiciled obligors. The underlying credit exposures of eligible ABS initially must be auto loans, student loans, credit card loans, or small business loans guaranteed by the U.S. Small Business Administration. The set of permissible underlying credit exposures of eligible ABS may be expanded later to include commercial mortgage-backed securities, non-Agency residential mortgage-backed securities, or other asset classes. The underlying credit exposures must not include exposures that are themselves cash or synthetic ABS.

Originators of the credit exposures underlying eligible ABS (or, in the case of SBA-guaranteed loans, the ABS sponsor) must have agreed to comply with, or already be subject to, the executive compensation requirements in section 111(b) of the Emergency Economic Stabilization Act of 2008.

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[1] The Federal Reserve reserves the right to review and make adjustments to these terms and conditions – including size of program, pricing, loan maturity, and asset and borrower eligibility requirements – consistent with the policy objectives of the TALF.

Eligible collateral for a particular borrower must not be backed by loans originated by the borrower or by an affiliate of the borrower.

### *Eligible Borrowers*

All U.S. persons that own eligible collateral may participate in the TALF. A U.S. person is a natural person that is a U.S. citizen, a business entity that is organized under the laws of the United States or a political subdivision or territory thereof (including such an entity that has a non-U.S. parent company), or a U.S. branch or agency of a foreign bank.

### *Transaction Structure*

Credit extensions under the TALF will be in the form of non-recourse loans secured by eligible collateral. Substitution of collateral during the term of the loan will not be allowed. TALF loans will have a one-year term, with interest payable monthly. The term of TALF loans may be lengthened later if appropriate. TALF loans will not be subject to mark-to-market or re-margining requirements.

Any remittance of principal or interest on eligible collateral must be used immediately to pay interest due on, or reduce the principal amount of, the TALF loan.

### *Haircuts*

Collateral haircuts will be established by the FRBNY for each class of eligible collateral. Haircuts will be determined based on the price volatility of each class of eligible collateral.

### *Pricing and Allocation*

The FRBNY will offer a fixed amount of loans under the TALF on a monthly basis. TALF loans will be awarded to borrowers each month based on a competitive, sealed bid auction process. Each bid must include a desired amount of credit and an interest rate spread over one-year OIS. The FRBNY will set minimum spreads for each auction.

The FRBNY will reserve the right to reject or declare ineligible any bid, in whole or in part, in its discretion. In this regard, the FRBNY will develop and implement procedures to identify for further scrutiny potentially high-risk ABS that a borrower proposes to pledge to the FRBNY under the TALF.

The FRBNY will assess a non-recourse loan fee at the inception of each loan transaction.

### *Roles of Primary Dealers and Clearing Banks*

Each borrower must use a primary dealer, which will act as agent for the borrower, to access the TALF and must deliver eligible collateral to a clearing bank.

### *Role of the U.S. Treasury Department*

The FRBNY will create an SPV to purchase and manage any assets received by the FRBNY in connection with any TALF loans. The FRBNY will enter into a forward purchase agreement with the SPV under which the SPV will commit, for a fee, to purchase all assets securing a TALF loan that are received by the FRBNY at a price equal to the TALF loan amount plus accrued but unpaid interest. The U.S. Treasury's Troubled Assets Relief Program (TARP) will purchase subordinated debt issued by the SPV to finance the first $20 billion of asset purchases. If more than $20 billion in assets are purchased by the SPV, the FRBNY will lend additional funds to the SPV to finance such additional purchases. The FRBNY's loan to the SPV will be senior to the TARP subordinated loan, with recourse to the SPV, and secured by all the assets of the SPV. All cash flows from SPV assets will be used first to repay principal and interest on the FRBNY senior loan until the loan is repaid in full. Next, cash flows from assets will be used to repay principal and interest on the TARP subordinated loan until the loan is repaid in full. Residual returns from the SPV will be shared between the FRBNY and the U.S. Treasury.

### *Executive Compensation Requirements*

Originators of the credit exposures underlying eligible ABS (or, in the case of SBA-guaranteed loans, the ABS sponsor) must have agreed to comply with, or already be subject to, executive compensation standards consistent with the U.S. Treasury's TARP guidelines applicable to its Capital Purchase Program.

### *Termination Date*

The facility will cease making new loans on December 31, 2009, unless the Board agrees to extend the facility.