



BOARD OF GOVERNORS  
OF THE  
FEDERAL RESERVE SYSTEM  
WASHINGTON, D. C. 20551

OFFICE OF INSPECTOR GENERAL

November 16, 2010

Board of Governors of the Federal Reserve System  
Washington, DC 20551

Dear Members of the Board:

The Office of Inspector General is pleased to present its report on *The Federal Reserve's Section 13(3) Lending Facilities to Support Overall Market Liquidity: Function, Status, and Risk Management*. To respond to the financial crisis, the Board of Governors of the Federal Reserve System (Board), citing "unusual and exigent circumstances," exercised its authority under section 13(3) of the Federal Reserve Act (12 U.S.C. §343) between March and November 2008, to authorize the creation of the following six lending facilities to support overall market liquidity: Term Securities Lending Facility (TSLF) (including the TSLF Options Program), Primary Dealer Credit Facility, Asset-Backed Commercial Paper Money Market Mutual Fund Liquidity Facility, Commercial Paper Funding Facility, Money Market Investor Funding Facility, and Term Asset-Backed Securities Loan Facility. We performed this work to provide an independent review of the six lending facilities' functions, status, and risks.

Our report describes the overall function and status of each lending facility, including how it operated, the financial markets it was intended to support, and the financial utilization of the facility. The report also identifies risks in each lending facility, for the Board's review in exercising its monetary policy function and its general supervision and oversight of the Federal Reserve Banks. To ease financial market conditions and restore economic stability, the six lending facilities were created separately and quickly to respond to severely stressed market conditions, without the opportunity for extensive planning. In addition, the lending facilities were designed to generally encourage broad participation by many borrowers. Thus, implementation of the facilities involved credit and operational risks, which varied by facility. To mitigate risk, the Federal Reserve implemented a number of credit risk management and operational controls. Overall, general indicators of market stress suggest that the lending facilities helped to stabilize financial markets. As of June 30, 2010, the Federal Reserve has reported that the lending facilities have generated approximately \$9.0 billion in interest income and usage fees, and that none of the lending facilities have experienced any financial losses.

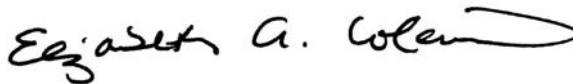
We conducted our review from August 2009 through June 2010, prior to the passage of the Dodd-Frank Wall Street Reform and Consumer Protection Act (the Dodd-Frank Act), which was signed into law on July 21, 2010. The Dodd-Frank Act is a wide-ranging statute that makes numerous substantial changes to the U.S. financial regulatory system. In particular, the Dodd-Frank Act refocuses the Board's authority under section 13(3) of the Federal Reserve Act from discounts to individuals, partnerships, and corporations to discounts to participants in any program or facility with broad-based eligibility. Moreover, the Dodd-Frank Act requires a

Government Accountability Office (GAO) audit of all Federal Reserve emergency lending programs, including those facilities discussed in this report. We will share our report with GAO as it goes forward with its work.

We provided a draft of our report to Board officials in the Division of Reserve Bank Operations and Payment Systems, the Division of Monetary Affairs, and the Legal Division, as well as officials at the Federal Reserve Banks of New York (FRB-NY) and Boston (FRB-Boston), for their review and comment. In their consolidated response, they indicated that our report provides a clear summary of the purpose, implementation, operation, expiration, and key risks associated with each of the six lending facilities.

We appreciate the cooperation that we received from the Board, FRB-NY, and FRB-Boston during our review. We are providing copies of this report to Board management and FRB-NY and FRB-Boston officials. The report will be added to our publicly-available website and will be summarized in our next semiannual report to Congress.

Sincerely,

A handwritten signature in black ink that reads "Elizabeth A. Coleman". The signature is fluid and cursive, with a long horizontal stroke at the end.

Elizabeth A. Coleman  
Inspector General



Board of Governors of the Federal Reserve System

# **The Federal Reserve's Section 13(3) Lending Facilities to Support Overall Market Liquidity:**

**Function, Status, and Risk Management**

Office of Inspector General

November 2010



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