Financial CP Conduit Proposal

Purpose:
Provide term funding to financial institutions by buying and holding financial CP until the market normalizes to provide such funding.

Basic participants and structure:
An asset manager manages each SPE according to Federal Reserve criteria. Investors would sell CP and CDs of financial firms into the SPE and provide a first loss equity position. The Treasury takes a second-loss preferred equity position and the Federal Reserve lends directly to the SPE through a new 13(3) facility.

Eligible assets:
3 month CP and bank CDs issued by financial firms headquartered in the United States, denominated in U.S. dollars, and considered first tier securities under SEC Rule 2a7. An investor may not sell obligations issued by affiliated parties to the pool.

Pool structure:
A new asset pool in the SPE is created weekly [monthly?] with eligible assets. Minimum asset sale by each investor is $500MM; asset sale must meet diversification requirement below.

Program size:
As much as $50 billion in each pool

Diversification requirement:
Obligations of a single issuer or group of related issuers may not comprise more than 2% of total of each asset pool. No one investor may sell a pool of securities with more than a 10% concentration in one name and an asset manager will be engaged to ensure overall diversification requirements are met.

Sale mechanics:
Fund sells asset to SPE at market value.

Equity structure:
Each investor makes cash-funded equity contribution of 5% of the market value of assets sold. Equity investment could take the form of a discount on the sale price to be recovered at maturity. Sponsor may sell its equity interest to other investors.

Debt structure:
The SPE will issue full recourse secured notes to the Federal Reserve matching the maturity of the underlying assets. The notes will be collateralized by all assets in the SPE.

Rates
Federal Reserve will lend at the 3 month OIS plus 25 bp, and Treasury preferred stock will receive a higher spread of 3 month OIS plus a 200-300 bp spread.

Cash Flows
At maturity of assets in the pool, cash flows are distributed first to repay the Federal Reserve loan, then Treasury's preferred stock, and lastly the equity holders.

Loss waterfall:
Losses on a specific asset first reduce the equity of the investor that sold the asset to the SPE. When the equity of the seller of the asset is exhausted, losses on the asset are absorbed by Treasury's preferred stock. The Federal Reserve has a third-loss position secured by all of the assets in the pool.

Term:
Until relative interest rates make selling assets to the SPE unattractive to investors.

Potential Modifications

- Could alternate weekly to create pools of 3, 6, and/or 9 month paper.