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Bipartisan Bill to Include U.S. Munis as High-Value Assets Introduced.

May 4 (Reuters) – A bipartisan group of U.S. lawmakers has introduced legislation that would require federal regulators to allow banks to include muni bonds as liquid assets, an issue that cities and states say could increase their borrowing costs.

In September, U.S. regulators tightened rules on which assets banks can sell in the event of a credit crunch. They also excluded debt issued by U.S. states and cities from banks' high-quality liquid assets, or HQLA.

Since then, many municipalities lobbied against the decision, arguing that if municipal debt is no longer considered a high-liquid asset, banks will have less incentive to buy their bonds, hiking borrowing costs.

On Friday, a group of five Republicans and five Democrats on the House Financial Services Committee introduced a bill that would require regulators to treat munis that are investment grade, liquid and readily marketable as a "2A" high-liquid asset.

The legislation was introduced by Republican Luke Messer from Indiana and New York Democrat Carolyn Maloney.

"We shouldn't allow Federal bureaucrats to promote policies that disincentivize investment in our local communities," Messer said in a statement.

Maloney said: "States and cities rely on municipal bonds to finance critical infrastructure, build schools, and pave roads. This important legislation ensures that municipal bonds, which are among the safest investments available, are treated fairly by the regulators."

The bill appears to have a good chance of passage out of the committee and onto the floor of the House of Representatives for a full vote, given that Maloney and another of the bill's co-sponsors, veteran Republican Peter King, are highly ranked.

Without legislation, there appears little prospect of regulators reversing course on the rule. A rule change would require agreement of three bank regulators: the Office of the Comptroller of the Currency (OCC); the Federal Deposit Insurance Corporation (FDIC); and the Federal Reserve.

The Fed has publicly said it wants to amend the rule to include munis, while the OCC appears most opposed to a rule change.

Retail investors are the largest holders in the $3.7 trillion municipal bond market. Households hold about 40 percent of all outstanding municipal bonds, $1.5 trillion, while banks hold about $485 billion, or around 12 percent, according to Federal Reserve data.

BY TIM REID

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