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Federal Reserve's Municipal Liquidity Facility: Arizona Impact - Ballard Spahr

On April 9, 2020, the Municipal Liquidity Facility (MLF) was established pursuant to Section 13(3) of the Federal Reserve Act to assist States and certain local governments with their increased liquidity needs due to the coronavirus pandemic. In general, the MLF provides for the establishment of a special purpose entity to purchase up to $500 billion of short-term securities (Eligible Notes) from U.S. states, counties with populations in excess of 500,000 and cities with populations in excess of 250,000 (referred to as Eligible Issuers) whose general obligations or issuer credit were rated, as of April 8, 2020, at least BBB/Baa3 by two or more major nationally-recognized statistical rating organizations. Eligible Notes are tax anticipation notes, tax and revenue anticipation notes, bond anticipation notes and other short-term notes issued by Eligible Issuers, provided that the notes mature no later than 36 months from the date of issuance.

In Arizona, Eligible Issuers are the State, Maricopa and Pima Counties and the Cities of Phoenix, Tucson, Mesa, Chandler, Scottsdale and Glendale. And, for the purposes of the MLF, Eligible Notes would generally be tax anticipation notes issued by the State of Arizona pursuant to Article 1, Chapter 3, Title 35 of the Arizona Revised Statutes and tax anticipation notes, grant anticipation notes and revenue anticipation notes issued by a county or city pursuant to Articles 3.1, 3.2 and 3.3, respectively, of Chapter 3, Title 35 of the Arizona Revised Statutes.

State tax anticipation notes may be issued for a term of six months in an aggregate principal amount not exceeding 50 percent of the ad valorem taxes and 50 percent of the excise taxes not expected to be collected during the current fiscal year at an interest rate not exceeding 9 percent per annum.

In the case of tax anticipation notes of a county or city which is an Eligible Issuer, the principal amount of the notes cannot exceed 90 percent of the taxes that are not expected to be collected in the current year (for whatever reason), taxes thereafter received must be applied to pay down the note and the notes must mature on or before July 31 following the fiscal year in which they are issued.

Revenue anticipation notes may be issued and sold in advance of the receipt of revenues by a county or city which is an Eligible Issuer (other than ad valorem property taxes, grants, sales taxes, or transaction privilege taxes or State or restricted revenues) provided that the notes must mature not later than the fiscal year in which issued.

In addition, the MLF would permit Eligible Issuers to borrow funds to purchase similar notes from subordinate political subdivisions or other governmental entities in order to assist those entities with their liquidity needs. Although the State of Arizona has announced its own AZCares Fund, this represents a decision by the State to make $441 million of the $1.86 billion it received in Federal coronavirus relief funding available to some Arizona municipalities which do not qualify as Eligible Issuers.

The Federal Reserve Bank of New York has established the Municipal Liquidity Facility LLC, a

Delaware limited liability company, as the special purpose purchaser of the notes. The LLC has issued a term sheet and FAQs here. An Eligible Issuer can indicate its desire to participate in the MLF by filing a “Notice of Interest” with the Federal Reserve Bank of New York. The Notice of Interest can be found here.

The Federal Reserve, and most commentators, regard the MLF as a lender of last resort, intended to fund Eligible Issuers that might not otherwise have access to the credit markets. Notably, the published interest rates at which the LLC will purchase Eligible Notes are based on a comparable maturity overnight index swap plus an applicable spread based on the rating of the Eligible Notes being purchased. For example, in the case of AAA/Aaa-rated Eligible Notes, the spread is 150 basis points; in the case of A+/A1-rated Eligible Notes, the spread is 240 basis points; and in the case of BBB/Baa3-rated Eligible Notes, the spread is 380 basis points.

For further information or assistance in analyzing or accessing the MLF, please contact Bill Hicks (602-798-5423), Michele Bax (602-708-5483), or Tyler Cobb (602-798-5420).

by the Public Finance Group

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