

FEDERAL RESERVE BANK OF SAN FRANCISCO  
101 MARKET STREET, SAN FRANCISCO, CALIFORNIA 94105

December 18, 2002

**CREDIT AND RISK MANAGEMENT:  
NEW FEDERAL RESERVE LENDING PROGRAMS**

To the Chief Financial Officer  
of the Institution Addressed

On January 9, 2003, the Federal Reserve will replace two existing discount window programs—adjustment credit and extended credit—with new primary and secondary credit programs. Depository institutions that Reserve Banks deem to be in generally sound financial condition will be eligible for primary credit. Secondary credit will be available to depository institutions not eligible for primary credit. Primary credit normally will be granted on a “no questions asked” basis at a rate that initially will be 100 basis points above the Federal Open Market Committee’s target for the federal funds rate. The rate on secondary credit will be 50 basis points higher than the primary credit rate. Collateral requirements and the seasonal credit program continue unchanged.

This restructuring of the Federal Reserve’s credit programs is designed to improve the functioning of the discount window; it does not represent a change in the stance of monetary policy. The primary credit program will aid the implementation of monetary policy by making discount window credit readily available at a rate above the FOMC’s target, thus limiting how far the actual federal funds rate will rise above the target on days when funding markets are tight. In addition, the new programs will simplify the process of borrowing and promote consistency in the lending function across the Federal Reserve System.

Primary credit will replace adjustment credit as the principal safety valve for ensuring adequate liquidity in the banking system and as a backup source of short-term funds for sound depository institutions. Generally, primary credit will be extended on a very short-term basis, typically overnight. Primary credit may also be extended for up to a few weeks to small institutions in sound financial condition that cannot obtain temporary funds in the market at reasonable terms. Institutions need not seek alternative sources of funds before requesting occasional short-term advances from the primary credit program. There will be no prohibition against using primary credit to fund sales of federal funds. Except in unusual circumstances, depository institutions will not be questioned about the reason for borrowing primary credit. Given the above-market pricing of primary and secondary credit, the Federal Reserve anticipates that depository institutions will not find it advantageous to rely on the discount window as a regular source of funding.

As noted, only institutions that Reserve Banks deem generally sound will be eligible to obtain primary credit. Eligibility is based largely on an institution’s supervisory exam rating and capital status. Supplementary information, such as public debt ratings and information provided by examiners and the market, may also be considered. Generally, institutions with composite CAMEL(S) ratings of 1, 2, or 3 that are at least adequately capitalized will be eligible for primary credit unless supplementary information indicates their condition is not generally sound.<sup>1</sup>

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<sup>1</sup> Foreign Banking Organizations eligible for primary credit would generally have SOSA rankings of 1 or 2 and a ROCA, Combined ROCA, and/or Combined U.S. Operations rating of 1, 2, or 3. Corporate credit unions eligible for primary credit would generally have a CRIS rating of 1, 2 or 3 in both components and meet their minimum capital requirements (varies depending on activities).

Secondary credit is intended for institutions that do not qualify for primary credit. Secondary credit will be extended to institutions primarily to assist in their timely return to a reliance on market funding sources. This program will entail a higher level of Reserve Bank administration and oversight than primary credit. As noted earlier, secondary credit will be extended at a rate 50 basis points above the primary credit rate.

Federal Reserve staff will be holding informational sessions with bank supervisors to explain the new discount window programs. In the view of the Federal Reserve, supervisors should view occasional use of primary credit as appropriate and unexceptional. The discount window web site (<http://www.frbdiscountwindow.org>) contains additional information, including the Board's press release that provides more detail about the new programs, the revised Regulation A, a PowerPoint presentation that summarizes the new programs, and responses to frequently asked questions (FAQs).

### **Additional Information**

If you anticipate an occasional need to borrow from the discount window, or would like to be able to borrow quickly in a contingency, we recommend that you execute and file borrowing documents and preposition collateral. Please contact Mr. Steve Fung, Manager, Discount Window and Collateral at (415) 974-2470, or [steve.fung@sf.frb.org](mailto:steve.fung@sf.frb.org), or me at (415) 974-2974, or [rick.miller@sf.frb.org](mailto:rick.miller@sf.frb.org), if we can answer your questions about the new facilities and the steps involved in setting up borrowing arrangements.

RICK A. MILLER  
Director