December 9, 2024

Via Electronic Mail

Ann E. Misback, Secretary
Board of Governors of the Federal Reserve System
Mailstop M–4775, 2001 C St. NW
Washington, D.C. 20551

Re: Request for Information and Comment on Operational Aspects of Federal Reserve Bank Extensions of Discount Window and Intraday Credit (Docket No. OP-1838)

Ladies and Gentlemen:

The Bank Policy Institute[1] appreciates the opportunity to comment on the Request for Information[2] issued by the Board of Governors of the Federal Reserve System seeking public input on the operational aspects of Federal Reserve Bank extensions of discount window and intraday credit.

BPI strongly supports the effort being undertaken to examine the operational effectiveness of present-day discount window infrastructure and believes it is crucial to identify opportunities for improvement and modernization so that the discount window can be optimally positioned, as an operational matter, to perform its important function. The events of spring 2023 highlighted the need for such operational improvements, particularly to the discount window's ability to respond swiftly to liquidity needs that may arise abruptly in an increasingly digital environment. Furthermore, as one element of any future revisions to prudential liquidity standards, we believe it is critical that the Federal Reserve Board and other banking agencies take due account of discount window availability in setting quantitative liquidity requirements, such as the liquidity coverage ratio, and in conducting supervisory assessments of liquidity risk management and contingency funding plans more broadly, including internal liquidity stress tests.

To improve the efficiency and effectiveness of the discount window, we believe the Federal Reserve System should focus broadly on four objectives: (1) harmonizing operational practices across Reserve Banks; (2) improving transparency with respect to determinations around collateral eligibility, valuation and

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1 The Bank Policy Institute is a nonpartisan public policy, research and advocacy group that represents universal banks, regional banks, and the major foreign banks doing business in the United States. The Institute produces academic research and analysis on regulatory and monetary policy topics, analyzes and comments on proposed regulations, and represents the financial services industry with respect to cybersecurity, fraud, and other information security issues.

2 Federal Reserve, *Request for Information and Comment on Operational Aspects of Federal Reserve Bank Extensions of Discount Window and Intraday Credit*, 89 Fed. Reg. 73,415 (Sept. 10, 2024) [hereinafter, *RFI*].

haircuts; (3) modernizing operational processes; and (4) encouraging readiness on the part of banks[3] to borrow from the discount window. Although the RFI does not directly deal with the issue of discount window stigma, we believe that efforts to enhance the operational effectiveness of the discount window should be complemented by measures aimed at reducing the reluctance of banks to use the discount window. Ultimately, banks must be both readily able, and willing, to borrow from the discount window in order for the discount window to serve its critical function.

With respect to the need for harmonization of operational practices across the Federal Reserve System, the current administration of the discount window across twelve separate Reserve Banks has resulted in district-by-district variations in borrowing procedures and approaches to collateral, including determinations around collateral eligibility, valuation and haircuts. These variations do not appear to be inherently related to underlying risk considerations and can result in uneven treatment of similarly situated banks pledging similar collateral. Critically, such differences are often difficult to ascertain from published sources, and the resultant uncertainty may contribute to reluctance among banks to pledge collateral to the window, and ultimately to borrow.

In addition to necessary harmonization of discount window administration across the Federal Reserve System, there is a critical need for greater transparency as to how key determinations (*e.g.*, application of specific haircuts within a broad published range, specific determinations regarding collateral eligibility, etc.) are made. Improving transparency through the publication of clear and uniform guidance, readily accessible on a central website, would reduce operational burden for banks that pledge collateral by reducing the need to engage, as is often the case currently, in prolonged and non-transparent consultation with individual Reserve Bank staff, which can result in inconsistent responses.

Compounding current operational frictions are certain infrastructure elements that are outdated and not aligned with modern industry standards, which likewise can reduce industry willingness to maintain collateral at the discount window as opposed to alternative venues such as the Federal Home Loan Bank System. Adopting process modernization measures—such as updating and harmonizing the process for submitting discount window borrower documents; providing banks with the ability to adjust their Official Authorization Lists (OALs) through an online portal (as is commonly done within the FHLB System currently); and enhancing banks' operational ability to transfer collateral across the discount window and other monetization venues such as the Standing Repo Facility, Triparty Repo and the FHLB System—would help improve overall user experience and operational efficiency.

Efforts to promote harmonization, transparency and modernization could work in tandem to promote ultimate willingness to use the discount window when appropriate. The Federal Reserve Board and other relevant banking agencies should accord appropriate recognition, for all applicable liquidity requirements, of available discount window borrowing capacity. Such recognition would not only be substantively appropriate in terms of the objectives of liquidity regulation, it would also help to reduce stigma around use of the discount window. Reducing such stigma is itself a key factor in achieving operational effectiveness in performance of the discount window's core function.

Below, we elaborate on specific recommendations to achieve the overarching objectives described above. Although our comments focus primarily on improvements to discount window operations, we also provide certain recommendations on how the Federal Reserve can improve its operational administration of intraday credit. Finally, we briefly highlight certain recommendations and considerations related to

[3] This letter uses the terms "banks" and "institutions" to refer to all depository institutions that are eligible to borrow from the discount window, including U.S. branches and agencies of foreign banks.

reducing discount window stigma, an issue which we believe will require ongoing attention even as operational improvements to discount window functioning are achieved and deserves to be further considered by the Federal Reserve as a separate policy matter.

I. Recommendations for Discount Window Operations

Currently, certain operational frictions and inefficiencies exist with respect to each of the discount window operational processes identified by the RFI: (A) submitting legal documents to a Reserve Bank; (B) pledging or withdrawing securities as collateral; (C) pledging or withdrawing loans as collateral; (D) requesting discount window advances and receiving proceeds; (E) repaying discount window advances before their full maturity; and (F) using the Discount Window Direct online portal.[4] Of particular concern for banks that are also FHLB members is the need to diminish operational frictions associated with transferring collateral between the discount window and the FHLB System. Below we set forth certain recommendations to help address these issues and to maximize the effectiveness of each of the operational steps highlighted by the RFI.

A. The Federal Reserve System should reduce operational burden associated with the process by which banks submit legal documents by updating and standardizing certain requirements.

To improve operational efficiency, the Federal Reserve System should implement uniform processes and requirements for the submission of all required discount window documents to Reserve Banks. As a starting point, Reserve Banks should permit borrowers to complete, sign, submit and update discount window documents entirely electronically. Consistent with current efforts by the Federal Reserve to implement a standardized e-signature process for OALs and other Federal Reserve account documentation unrelated to the discount window,[5] efforts to enable the electronic completion, execution and submission of all discount window documents as well would help modernize and improve the overall user experience of discount window participants.

To further reduce uncertainty around the borrowing process, the Federal Reserve should ensure that Reserve Banks have uniform practices not only in terms of *how* required borrowing documents are submitted but also *when*. For example, Reserve Banks accept pledges of loan collateral from banks to secure discount window advances, or for payment system risk purposes, under the borrower-in-custody (BIC) program. Banks participating in the BIC program are required to complete a certification that attests to the controls and other procedures such participant has in place to safeguard the pledged loans and related documentation. Banks are required to complete and submit an initial BIC certification and, thereafter, updated certifications on a periodic schedule that varies across Reserve Banks. For example, the Federal Reserve Bank of New York requires an updated BIC Certification to be submitted by BIC participants every 12 months, whereas the Federal Reserve Bank of Minneapolis only requires the same update every 18 months.[6]

Where appropriate, the Federal Reserve should draw upon industry best practices as a model. For

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4 *RFI*, at 73,417.

5 Federal Reserve, *Docusign and ID.me Resources for Forms*, https://www.frbservices.org/resources/financial-services/accounting/docusign-idme-resources-for-forms (last visited Nov. 18, 2024).

6 *See* Federal Reserve Bank of Minneapolis, *Borrower-in-Custody Collateral Program*, at 5 (June 20, 2024) [hereinafter *Minneapolis BIC Program*]; Federal Reserve Bank of New York, *Borrower-in-Custody Collateral Program Requirements*, at 6 (revised Mar. 2022) [hereinafter *New York BIC Program*].

example, banks are required to maintain on file with the Federal Reserve OALs that establish the identity and authority of the individuals able to take actions that bind a bank in relation to its use of particular Federal Reserve services. If a bank wishes to update the OAL that is maintained specifically for discount window purposes, it must submit a new OAL signed both by an officer identified by title in its previously furnished authorizing resolutions as well as all authorized individuals (both existing authorized individuals and any new individuals to be added). Reserve Banks should provide banks with the ability to adjust their OAL via an online portal, rather than require the submission of a new OAL whenever changes need to be made to the list of individuals authorized to request advances or pledge collateral. This approach is consistent with operational practices adopted within the FHLB System and would build upon efforts that are currently underway by the Federal Reserve to digitalize the execution of OALs that are maintained for other purposes. With respect to recurring required submissions, such as BIC certifications, the Federal Reserve should consider requiring banks to submit updated documents only when there are changes to the previously furnished information. Where no such changes have occurred since the last reporting period, Banks could instead be asked to provide a digital attestation that the information contained in its previous submission remains complete and accurate in all respects.

B. Reserve Banks should ensure the timely assignment of lendable value to newly pledged securities and adopt measures to enable more efficient movement of securities collateral between the discount window and other potential monetization venues such as the FHLB System.

Banks frequently experience delays in the assignment of lendable value to newly pledged securities, with Reserve Banks often taking lengthy and varied periods of time to assign actual or estimated market prices to newly pledged securities. During this interim period between completion of the pledge and assignment of a valuation to the pledged securities, securities for which valuation is still pending receive zero lendable value, which results in a corresponding delay in the availability of executable borrowing capacity.

To address this issue, Reserve Banks should upgrade where necessary the valuation services they contract for, in order to obtain more timely valuation information in relation to comparatively less-liquid securities for which assignments of lendable value can currently lag.[7] We propose that assignments of lendable value should take no longer than three business days. As a complementary measure, Reserve Banks should provide pledging banks with automated alerts listing each pledged security by CUSIP, with an estimate of the time remaining until the assignment of pricing/lendable value for each, based upon the expected turnaround times for assigning value to such security as agreed between the Reserve Banks and their third-party vendors pursuant to applicable service-level agreements. In the use of such third-party valuation services, and in other respects, the valuation protocols applied by Reserve Banks to pledged collateral should consider and, where applicable, be conformed to, current industry standards and best practices, such as those adopted within the triparty repo market. Examples include: committing to the assignment of lendable value within specified periods (*e.g.*, within three business days); aligning the valuation timeline for loan collateral with that for securities collateral—where possible, both processes should be completed concurrently for collateral pledged on the same day—in order to minimize bottlenecks and enable quicker access to overall liquidity; and establishing a standardized communication protocol to provide status updates on progress in assigning lendable value. These revisions, if adopted, would support transparency in the pledging process and reduce uncertainty during the waiting period before lendable value

[7] Banks have reported wide ranges with respect to the time it takes for valuations to be assigned to certain comparatively less-liquid securities, including collateralized loan obligations, asset-backed securities and municipal bonds, with assignments of lendable value sometimes taking upward of several weeks. Valuation times can also vary across Reserve Banks for similar securities collateral.

is assigned, particularly in the event of unexpected delays.

To further reduce uncertainty around the ultimate assignment of lendable value for pledged securities, the Federal Reserve System should (i) enhance transparency by providing banks with more detailed instructions and guidance on its requirements and expectations with respect to the pledging of securities and (ii) build a central online tool that allows banks to review, by CUSIP,[8] the eligibility of particular securities and the relevant margins to be applied to such securities. Crucially, Reserve Banks should maintain sufficient operational capacity to timely accept pledges in substantial volume from multiple banks at the same time without creating additional delays in assigning lendable value.

With respect to withdrawals of securities collateral, effective execution of a liquidity strategy—particularly during a crisis—requires the ability to move securities in and out of the discount window quickly. We believe this is currently unnecessarily inhibited by certain transfer size limits that are imposed as a matter of practice on Fedwire Securities Service transfers of book entry securities. We note that although Section 11.2.2(c) of Operating Circular 7 appears to apply a $1 billion transfer limit on transfers to or from a restricted securities account (such as are used for pledging securities maintained on the Federal Reserve's book-entry system to the discount window), banks have reported receiving error messages with respect to such transfers that subject them to a significantly lower $50 million transfer limit that does not appear intended to apply in such circumstances as a matter of policy.[9] The Federal Reserve System should resolve this issue by aligning actual Fedwire Securities Service operations with the stated terms of Operating Circular 7, which would help reduce the number of transactions a bank must carry out in order to effectuate a given pledge. In addition, the Federal Reserve System should upgrade its infrastructure to more readily enable the movement of securities collateral across the full range of relevant venues for potential monetization: the discount window, the FHLB System, the Standing Repo Facility, and triparty repo custody. To operationally support such collateral movement to and from the discount window in a manner that is interoperable and interconnected with other standard venues for maintaining collateral, the Federal Reserve System should develop and maintain an online tool that would allow banks to move securities collateral between the discount window and such venues in a streamlined and automated fashion. In contrast to current operational arrangements, the envisioned online tool should enable the efficient upload of bulk collateral data using Excel/CSV files with practical file size limits (as opposed to the current reliance on email and FRSecure) and include easy-to-use templates to direct commonly requested types of collateral movement in a manner that can be processed quickly. Availability of such online capabilities would enhance the ability of banks to interact effectively with the discount window in periods of market stress, when it is most needed.

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[8] BPI wishes to underscore the broad importance and utility of the CUSIP identifier for this and a broad range of other purposes within the U.S. financial system. As detailed in BPI's recent comment letter in relation to the ongoing interagency rulemaking under the Financial Data Transparency Act, we are concerned both substantively and procedurally that the proposal to establish the Financial Instrument Global Identifier (FIGI) as the common financial instrument identifier—while excluding more widely adopted standards such as the Committee on Uniform Security Identification Procedures (CUSIP) and the International Securities Identification Number (ISIN)—would introduce broad disruption to global markets. *See* Bank Policy Institute, *Comment Letter Re: Financial Data Transparency Act Joint Data Standards (Docket No. R—1836, RIN 7100–AG–79*) (Oct. 21, 2024).

[9] The Federal Reserve Policy on Payment System Risk states that "[a]lso exempt [from the $50 million transfer size limit] are pledges of securities to a Reserve Bank as principal (for example, discount-window collateral)." Federal Reserve, *Federal Reserve Policy on Payment System Risk* at 32 (effective Mar. 24, 2011).

C. The Federal Reserve System should streamline operational requirements associated with pledging and withdrawing loan collateral, and provide greater overall transparency around this process.

As with the pledging and withdrawal of securities collateral, the Federal Reserve System should harmonize discount window practices with respect to the acceptance and assignment of lendable value to loan collateral across the twelve districts. Currently, Reserve Banks differ in how they determine eligibility and assign lendable value to a range of loan types commonly offered for pledging. Consequently, a bank based in one Federal Reserve district that acquires a portfolio of loans from a bank in another Federal Reserve district may face challenges in obtaining the same lendable value that the selling institution had previously been assigned by its Reserve Bank. There is also a critical lack of transparency regarding how relevant Reserve Banks arrive at such lendable value determinations because the detailed standards that individual Reserve Banks apply to such questions often are not published online or otherwise easily determined. Additionally, certain aspects of the process for pledging and withdrawing loan collateral are not aligned with modern industry practice, which may result in operational inefficiencies.

(1) *Ensure greater consistency and transparency in the collateral pledging process*

The Federal Reserve System should work to harmonize determinations of collateral eligibility and lendable value across Reserve Banks. At a minimum, where differences in practice exist among Reserve Banks with respect to collateral eligibility, they should be highlighted in a transparent manner, with the rationale behind such differences explained, in order to permit forward planning by banks. Ideally, the Federal Reserve System should strive to achieve a sufficient degree of harmonization such that two similarly situated banks pledging identical loan portfolios would receive equivalent treatment at the discount window irrespective of district. Consistency and transparency would be fostered by the Federal Reserve making available a central FAQ system that addresses, on a System-wide basis across all Federal Reserve districts, commonly asked questions about collateral eligibility and the pledging process. As an in-person complement to such online information, the Federal Reserve should consider providing "office hours" or some similar form of regular access to subject-matter experts with whom banks can discuss the collateral pledging process—for instance, by establishing a System-wide hotline through which questions can be addressed. The additional support provided by these measures could help improve banks' understanding of the pledging process and their overall user experience. Currently, banks that interact with the discount window are overly reliant on their relationship manager at a given Reserve Bank, which can result in unnecessary burdens and inefficiencies as such managers at individual Reserve Banks may not necessarily be in possession of all the relevant information needed to resolve the questions posed.

Greater harmonization and transparency are also needed with respect to the process by which Reserve Banks assign market value to pledged collateral and apply haircuts to arrive at lendable value. As a result of district-by-district variations in haircut practices, banks cannot readily and accurately ascertain the lendable value that will be assigned to a given item of loan collateral until such collateral is pledged to the Reserve Bank in question. To facilitate more informed planning on the part of discount window participants, the Federal Reserve System should seek to provide greater clarity with respect to what haircuts—within current broadly specified ranges—will be applicable to various forms of loan collateral. To the extent that the wide ranges currently published for particular forms of collateral are meant to afford latitude for disparate haircut determinations among Reserve Banks, both substantive harmonization and greater transparency are called for.

Once collateral is pledged, the statements made available by the Reserve Banks currently only permit the pledging institution to see the current outstanding balance of the pledged asset and the bottom-

line lendable value assigned to such asset. That is, pledgors are not afforded any visibility into the two distinct components of lendable value: the assigned market value and the haircut applied to such market value. At a minimum, post-pledge transparency should be provided by Reserve Banks as to both components.

Finally, at a granular level, the Federal Reserve should make transparent the content of the specific automated tests that are applied by Reserve Banks in connection with the initial review of the files that pledging institutions submit with respect to items of collateral submitted for pledging. Specifically, greater transparency would be beneficial in relation to the specific tests that are used to trigger collateral-related Exception Reports of the following three types: Error Exceptions; Suspect; and Informational. In particular, banks would benefit from insight into the specific content of the logical tests applied to collateral data submitted by a pledging bank that can generate Error Exceptions in relation to particular collateral items submitted by such bank, as such exceptions result in zero lendable value being assigned to pledged collateral when they occur. Reserve Banks should also make transparent the set of critical data fields with respect to a submitted item of collateral that could result in an Error Exception (*i.e.*, the list of specific fields that, if left blank or found to be inaccurate, would result in an item of collateral being assigned zero lendable value).

(2) *Align pledging process with modern industry practices*

With respect to BIC collateral, the Federal Reserve should update the currently applicable standards for acceptance of pledged loans that are maintained by the pledgors in imaged form (rather than as originals) to reasonably accommodate modern-day industry practices. In order for loans maintained by the pledging institution in imaged form to be accepted as valid BIC collateral, some Reserve Banks require the pledging institution to certify that the original signed copy of the loan instrument has been either (i) destroyed or (ii) securely retained by the pledging institution.[10] Such Reserve Banks should, for instance, account for the fact that a bank that is not the administrative agent for a syndicated loan would not generally be in possession of original physical copies of the loan documents they maintain in scanned form and, consequently, is not in a position to destroy or physically store such documents. The eligibility of such loan collateral should therefore not be dependent on certifications of this nature. To relieve unnecessary burden with respect to other aspects of BIC collateral maintenance, the Federal Reserve System should consider removing the current requirement that loan collateral be conspicuously labeled as being pledged to a Reserve Bank and, in the case of loans that are in tangible form, physically segregated from other loan documents. Banks have policies and procedures for establishing secure custody of pledged loan documentation, which are subject to supervisory oversight and review; consequently, these detailed requirements do not necessarily provide any incremental operational benefit (*e.g.*, facilitate retrieval, prevent loss/misuse or enhance security). Against this factual backdrop, continued imposition of such requirements creates ongoing administrative burdens without material corresponding benefit.

Drawing on a practice currently employed by FHLBs as a streamlined option for assigning lendable value to pledged collateral, the Federal Reserve System should permit banks to pledge new loan portfolios on a "blanket lien" basis. FHLBs generally permit the pledging of new loan portfolios on a grouped "blanket lien" basis (*e.g.*, by permitting loan collateral to be itemized according to broad call report categories) as opposed to a process, such as that currently employed by the discount window (and also offered as an available alternative at FHLBs), that involves a more granular assignment of specific lendable values on a loan-by-loan basis. The discount window should offer a similar approach as a less administratively

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[10] *See*, *e.g.*, Federal Reserve Bank of Cleveland, *Borrower-in-Custody Collateral Program*, at 10 (revised July 2024); *New York BIC Program*, at 12.

burdensome optional alternative to the current mode of pledging, even if (as is generally the case in the FHLB system) such streamlined "blanket lien" pledging would generally result in somewhat lower lendable value ultimately being assigned to a given loan portfolio than would be assigned under the more granular "listing" form of collateral review. If transparently and uniformly administered, offering this mode of pledging as a newly available alternative would help reduce administrative burden resulting from the need to perform valuation and haircut analyses on a loan-by-loan basis and provide for quicker assignment of lendable value to the overall portfolios being pledged. As noted, collateral valuations and haircuts are currently assigned in a non-uniform manner across Reserve Banks, so an approach that looks at the full stock of collateral pledged by a bank more holistically and takes into consideration the overall lending practices of pledgors in relation to such collateral could reduce administrative burden and enhance efficiency for banks and the Federal Reserve System alike. We acknowledge that the successful adoption of blanket lien pledging at the discount window would require careful examination of how such an approach might interact with similar pledging arrangements at FHLBs, and encourage Reserve Banks to work closely together with FHLBs to consider how such an approach can be effectively operationalized at the discount window in practice.

Banks that pledge loans under the BIC program are currently required to submit monthly reports detailing all loans pledged at the applicable Reserve Bank along with their corresponding outstanding balances. Interim updates are also required on an intra-month basis if the total outstanding balance of pledged loans decreases by ten percent or more as compared to the most recent monthly report. Upon such decrease, BIC participants must promptly submit an interim collateral schedule with an explanation of the cause of the decrease in total outstanding balance. For banks that participate in the BIC program, such interim updates—and associated intra-month monitoring of total outstanding balance of the pledged loans—are required even if no discount window advances are currently outstanding. A related issue is that banks may be required to perform such intra-month monitoring on periodic schedules that vary depending on the applicable Reserve Bank, some of which require daily monitoring. To appropriately calibrate the administrative burden associated with the BIC program, (i) monitoring requirements should be made consistent across Reserve Banks and (ii) a bank should only be required to monitor BIC collateral value on an intra-month basis when discount window balances are outstanding that encumber such collateral. In ordinary circumstances where banks do not have discount window advances outstanding that encumber pledged BIC collateral, requiring that such monitoring occur on a monthly basis in connection with submission of the monthly BIC update reports would achieve a better balance of administrative burden relative to the underlying goal of ensuring the maintenance of previously reported collateral value.

Finally, the Federal Reserve should examine whether any data from existing regulatory reports submitted by banks, such as in the FR 2052a or FR-14M/Q forms, overlaps with informational items required by the discount window and, if so, whether such information can be made readily available to the discount window. To the extent that overlapping information could be readily identified and incorporated into the pledging process in an efficient manner, the Federal Reserve System could generate operational efficiencies by reducing duplicative reporting and review.

D. The Federal Reserve System should consider establishing the capability for institutions to access, in immediate and automated fashion, some portion of their available discount window borrowing capacity in appropriate circumstances.

Banks with available borrowing capacity based on the lendable value of pledged collateral should be able to receive discount window loans immediately and automatically upon request, at least up to a pre-specified threshold amount. Reserve Banks could retain a non-automated approval process for amounts above such threshold. Automating the process for requesting advances and receiving proceeds, at least up to some pre-defined level, would result in greater lending efficiency and enable firms to monetize pledged

collateral more readily, which could prove to be vitally important during a crisis.

E. Reserve Banks should provide for same-day release of collateral upon repayment of discount window advances.

Currently, West Coast-based banks may not be able to reallocate collateral the same day they repay discount window advances due to misalignments between the operating hours of the Fedwire Securities Service (which are specified by reference to Eastern Time) and the operating hours of Reserve Banks on the West Coast. The Federal Reserve System should ensure that collateral that has become unencumbered as a result of the repayment of a discount window advance is released on the same day as that repayment, irrespective of any time zone differences.

In addition, the operating hours of the discount window should be extended to 24 hours a day, every day of the year.[11] All functions of Discount Window Direct should similarly be extended to 24 hours a day. While Discount Window Direct is generally accessible at all hours, discount window advance and payment requests submitted via Discount Window Direct can still only be operationally processed and effectuated during the local Reserve Bank's standard business hours. In other words, the discount window lending and payment function of Discount Window Direct is currently effectively closed during non-business hours as a practical matter, even while its online functionality to receive instructions remains active and available.

F. The Federal Reserve System should expand and improve the functionality of Discount Window Direct.

The introduction of Discount Window Direct has improved the overall user experience for discount window participants and represents a positive initial step toward overall operational modernization of the discount window. However, several operational aspects of Discount Window Direct need to be upgraded or expanded in order for Discount Window Direct to achieve its full promise. In particular, Discount Window Direct is currently accessed through FedLine, which requires a user at the relevant bank to be in possession of a physical Fed Token in order to gain the online access necessary to view pledging and borrowing activity. While BPI appreciates the need for effective cybersecurity around the pledging and borrowing process, the requirement that a user be in possession of a physical token could create operational obstacles during a stress event should such token prove to not be readily accessible. Given the widespread use of dual-factor authentication measures in the banking space that are not reliant on the use of a physical token, the Federal Reserve System could consider adopting some alternative form of dual-factor authentication as a more effective means of maintaining security while enabling operationally necessary accessibility. In addition, the Federal Reserve should reduce the operational complexity and burdens associated with obtaining FedLine access for employees of the bank located at overseas branches, who are currently treated in a manner functionally equivalent to employees of third-party legal entities. Simplifying the process required for overseas employees of the bank entity to access Fedline would improve banks' operational ability to interact effectively with the discount window. Finally, Discount Window Direct could also benefit from the addition of a chat box feature or other online customer service interface to provide users with answers to questions in real time. Currently, such questions must generally be addressed using telephone-based customer

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[11] As noted in other industry comment letters, if Fedwire Funds Service operating hours are expanded to include weekends and holidays, it is important that discount window operating hours be similarly expanded to ensure that banks have corresponding access to liquidity during weekends and holidays. *See, e.g.*, The Clearing House, *Comment Letter Re: Expansion of Fedwire Funds Service and National Settlement Service Operating Hours (Docket No. OP–1831)*, at 7 (Sept. 4, 2024).

service, which can be a source of delay.

G. The Federal Reserve System should provide for greater portability of loan collateral between Reserve Banks and the FHLB System.

Operational challenges experienced by banks in repositioning loan collateral between the discount window and the FHLB System are a key concern that should be reviewed and addressed by the Federal Reserve System in connection with its effort to modernize discount window operations. Such review should be undertaken in collaboration with the FHLB System and should be directed toward enabling the smooth transfer of collateral pledges across these two critical venues. Operational improvements to enable such collateral portability would help banks maximize borrowing flexibility and the overall efficacy of contingent funding capabilities. Achieving smoother portability of collateral between Reserve Banks and the FHLB System may, among other benefits, increase willingness on the part of FHLB members to pledge collateral to the discount window in the first instance.

Relatedly, FHLB members can encounter circumstances in which certain collateral items pledged at the FHLB fall out of eligibility for FHLB lending but, due to operational impediments, prove not to be readily transferable to the discount window, despite such items clearly satisfying the discount window's eligibility requirements. Operational impediments in this circumstance can include difficulties in obtaining the release of collateral from the FHLB blanket lien and effectuating the follow-on pledge at the discount window. This fact pattern is particularly prevalent with respect to real estate loan collateral.

To achieve operationally effective portability of collateral, the Federal Reserve should establish a form of standardized intercreditor agreement as a basis upon which Reserve Banks and FHLBs can more efficiently recognize transfers of pledged loan collateral. Given the key role played by the FHLBs as business-as-usual sources of funding backed by substantial pledges of loan collateral—and the view recently underscored by the Federal Housing Finance Agency that it is not within the mandate of the FHLB System to perform the role of lender-of-last-resort[12]—achieving enhancements to the movement of collateral from the FHLBs to the discount window is particularly crucial. This would be a key step toward enhancing industry-wide flexibility in the deployment of collateral and the maintenance of contingent funding capacity.

H. The Federal Reserve Board and other banking agencies should accord appropriate recognition to operationally available discount window capacity for purposes of the liquidity coverage ratio and other liquidity-related elements of the prudential framework, including internal liquidity stress testing.

The Federal Reserve's updated FAQs on Regulation YY[13] took a step in the right direction by clarifying that banks are permitted to incorporate the discount window (as well as the standing repo facility and FHLB borrowing capacity) as potential options through which to monetize their liquidity buffers. The FAQ is clear, however, that a bank cannot receive credit for discount window capacity that is collateralized by loans or securities that do not qualify as highly liquid assets (HLA).[14] To further encourage pre-positioning of

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12 *See* Federal Housing Finance Agency, *FHLBank System at 100: Focusing on the Future*, at 32 (last visited Nov. 19, 2024).

13 Federal Reserve, *Frequently Asked Questions about Regulation YY: Enhanced Prudential Standards*, https://www.federalreserve.gov/supervisionreg/legalinterpretations/reg-yy-frequently-asked-questions.htm (last updated Aug. 13, 2024).

14 *Id.*

collateral (particularly non-HLA collateral), reduce stigma, and improve the resiliency of the banking system, the Federal Reserve should accord appropriate recognition, for all applicable liquidity requirements, of available discount window borrowing capacity. This would encourage ordinary course operational utilization of the discount window and promote overall readiness to borrow. Such recognition would not only be substantively appropriate in terms of the objectives of liquidity regulation, it would also help to reduce stigma around ultimate use of the discount window, which itself is a key to operational effectiveness.[15]

II. Recommendations with Respect to Operational Aspects of Intraday Credit

In this section, we detail two recommendations we believe would help improve the operational administration of access to intraday credit.

A. The Federal Reserve should consider enabling banks to opt in to an operational arrangement in which any end-of-day shortfall that would otherwise result in an overnight overdraft will be deemed to constitute an automatically granted request for a discount window advance secured by available collateral.

To streamline the process for requesting a discount window loan further, banks that are eligible for primary credit should be given the option of having any end-of-day overdraft automatically converted into an overnight discount window loan up to the unencumbered lendable value of pledged collateral. Such automatic conversion would be consistent with the objective of primary credit, which was intended to reduce the administrative burden of receiving a discount window loan.[16]

B. The Federal Reserve System should modestly extend the required renewal date for board resolutions approving a bank's intraday credit limit or "net debit cap."

Under the Federal Reserve Board's Payment System Risk Policy on Intraday Credit, the required renewal date for the board resolutions approving a bank's intraday credit net debit cap currently arises exactly one year after the applicable Reserve Bank approves such bank's net debit cap.[17] If new resolutions are not received by the Reserve Bank before this one-year expiration date, the bank may be assigned a zero cap, which prohibits the institution from using any Federal Reserve intraday credit.[18] As an operational complication that appears to be at variance with the stated policy, we understand that some banks have been informed by Reserve Banks that their intraday credit net debit cap expires one year after the date on

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15 *See* Bill Nelson, *Lender of Last Resort: Issues with the Fed Discount Window and Emergency Lending*, Testimony Before the U.S. House Financial Services Committee, Subcommittee on Financial Institutions and Monetary Policy (Feb. 15, 2024); *see also* Bill Nelson, Bank Policy Institute, *Give Banks Credit for Robust Contingent Liquidity Arrangements* (last visited Nov. 19, 2024); Susan McLaughlin, Yale School Of Management Program on Financial Stability, *Discount Window Stigma: What's Design Got To Do With It?* (Apr. 2, 2024); Bill Nelson, Bank Policy Institute, *Is it Time for a Holistic Review of Liquidity Requirements?* (Feb. 23, 2023); Bill Nelson, Bank Policy Institute, *Discount Window Stigma: We Have Met the Enemy, and He Is Us* (Aug. 10, 2021).

16 *See* Brian F. Madigan & William R. Nelson, *Proposed Revision to the Federal Reserve's Discount Window Lending Programs* (July 2022).

17 Federal Reserve, *Guide to the Federal Reserve's Payment System Risk Policy on Intraday Credit* at 19–20 (effective July 20, 2023).

18 An institution with a de minimis cap must renew its cap resolution annually by submitting a new resolution to its Reserve Bank. An institution with a self-assessed cap must perform a self-assessment annually and submit an updated cap resolution to its Reserve Bank. *Id.* at 20.

which the applicable board resolutions were adopted, rather than one year after the date on which the applicable Reserve Bank approves such net debit cap (the standard articulated in the Guide to the Federal Reserve's Payment System Risk Policy on Intraday Credit). As an initial matter, the Federal Reserve System should ensure that Reserve Bank practices are aligned with the stated requirements in the Guide. Further, the Federal Reserve System should provide a modest degree of additional flexibility by extending the expiration of a bank's net debit cap board resolutions to the end of the month in which the one-year expiration date falls. To illustrate, if a Reserve Bank approved a bank's net debit cap resolutions on July 6, 2024, the Payment System Risk Policy on Intraday Credit would consider such resolutions to require renewal by July 6, 2025.[19] In view of the practical consideration that board meeting routines are generally tied more to particular calendar months as opposed to particular dates within a calendar month, we recommend that the Payment System Risk Policy on Intraday Credit require new resolutions to be received by the Reserve Bank by month-end (in this example, July 31, 2025), rather than by the exact one-year anniversary date (in this example, July 6, 2025). This would better accommodate board meeting schedules and prevent undue complication as a bank approaches the expiration of previously adopted resolutions. Finally, Reserve Banks should more expeditiously approve net debit caps upon receipt of a bank's board resolutions, including committing to a standard maximum time for review.

III. Recommendations for the Provision of Information to the Public

As described above, there is an overall need for clearer and more uniform guidance on various aspects of discount window operations. In this concluding portion of the letter we underscore a set of recommendations on how the Federal Reserve can improve its communications around determinations regarding collateral eligibility and lendable value, and conclude with recommendations aimed at reducing the persistent problem of discount window stigma.

A. The Federal Reserve System should harmonize and improve communications with respect to key operational aspects of the discount window.

Banks have experienced inconsistent and opaque communication regarding important questions relating to collateral valuation and determinations with respect to the eligibility of particular types of loans and securities as collateral. Furthermore, information provided by each Reserve Bank regarding the eligibility standards or valuation criteria they apply can vary significantly. In certain districts such information is highly detailed and specific in conveying the Reserve Bank's expectations, while in other districts it is not. This inconsistent messaging and lack of clarity on practical questions relating to eligibility, valuation and applicable haircuts make it difficult for banks to determine, for example, whether to purchase a given loan portfolio or whether the required legal documents relating to such loan collateral are structured properly. More comprehensive and uniform efforts by the Federal Reserve System to make consistent information and guidance publicly available across districts—as well to administer eligibility, valuation and haircut standards in a uniform fashion—would greatly improve the efficiency of discount window operations overall. The increased certainty in outcome that would be provided by more uniform standards and transparent guidance would facilitate forward planning regarding available sources of contingent liquidity. Ultimately, improving overall predictability, transparency and market understanding with respect to discount window operations could promote increased pledging of collateral to the discount window and diminish stigma around its ultimate use.

In addition, the Federal Reserve System should provide greater clarity and guidance regarding

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19 *Id.*

specifically when repayment of a discount window advance is given effect when made within the 7 A.M. repayment window. Specifically, Reserve Banks should inform banks when repaid discount window advances are debited back and provide any other material information related to such debit (if not otherwise already available). Finally, the Federal Reserve System should provide written guidance that clearly articulates whether instructions to carry out the pledging of collateral must be conveyed specifically by an officer of the pledging bank, or whether it is permissible for a non-officer with power of attorney to pledge collateral.

B. Changes to Reserve Bank-specific disclosures on the Federal Reserve's weekly H.4.1 report could help reduce stigma associated with discount window borrowing.

Public disclosures contained in the weekly Federal Reserve H.4.1 report currently list certain detailed balance sheet information on a Reserve Bank-by-Reserve Bank basis that can inadvertently foster stigma with respect to discount window borrowers when borrowing activity increases appreciably within a given district. Based on such reporting, it is possible for analysts to infer on the basis of week-to-week fluctuations in reported Reserve Bank assets which Reserve Banks may be extending discount window loans in size.[20] This may lead market participants to draw adverse conclusions about particular banks located in the affected Reserve Bank district based on inferences which may or may not be accurate about the likely identity of the institutions engaged in borrowing within that district.

To address this issue, the Federal Reserve should consider the desirability, as a policy matter, of (i) eliminating Reserve Bank-by-Reserve Bank disclosure on the weekly H.4.1. Report or (ii) aggregating into a single line item all currently reported line-item details about particular asset types held by the Reserve Banks. Either of these changes would reduce the practical ability of outside observers to infer the geographic characteristics of week-to-week discount window activity. To the extent that targeted legislative amendments would be helpful in achieving the reduction of stigma associated with these existing disclosures, BPI would be supportive of such efforts.

Mandatory Dodd-Frank Act disclosure, with a two-year lag, of the specific identity of discount window borrowers (and associated amounts borrowed), may also reinforce reluctance to borrow from the discount window in the event of stress by ensuring the ultimate public identification of individual banks that have made use of the discount window. Although it occurs with a two-year lag, such disclosure can lead to negative repercussions for such banks well after the fact, reinforcing the effect of stigma at the time borrowing is originally considered.

Against this backdrop, we recommend that the Federal Reserve do as much as it can do to provide supportive messaging to banks and the public during normal business-as-usual conditions to reinforce that the discount window plays an important and constructive role as an underpinning of systemic stability within the banking system as it simultaneously pursues the operational enhancements described above.

BPI looks forward to continued engagement on these important, and complementary, topics as the Federal Reserve's process of discount window modernization moves forward.

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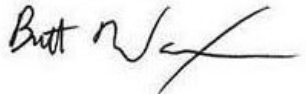
[20] *See* Steven Kelly, Yale School of Management Program on Financial Stability, *Weekly Fed Report Still Drives Discount Window Stigma* (Apr. 3, 2024).

The Bank Policy Institute appreciates the opportunity to comment on the operational aspects of Federal Reserve Bank extensions of discount window and intraday credit. If you have any questions, please contact the undersigned by email at Brett.Waxman@bpi.com.

Respectfully submitted,



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cc: Michael Gibson
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Board of Governors of the Federal Reserve System