

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

July 25, 2003

**BANKING SUPERVISION AND REGULATION:
GUIDANCE ON APPROPRIATE
USE OF DISCOUNT WINDOW**

To State Member Banks, Bank
Holding Companies, U.S. Branches
and Agencies of Foreign Banks,
and Others Concerned,
in the Twelfth Federal Reserve District

Agencies Release Guidance on Appropriate Use of Discount Window

The federal banking, thrift, and credit union regulatory agencies have issued guidance on the appropriate use of the Federal Reserve's new primary credit discount window program in depository institutions' liquidity risk management and contingency planning. The guidance is attached.

The guidance provides background on the Federal Reserve's discount window programs, including new primary and secondary credit programs introduced this past January. It also reiterates well-established supervisory policies on sound liquidity contingency planning, and discusses sound practices in using primary credit program borrowings in liquidity contingency plans.

Adequate liquidity contingency planning is critical to the ongoing maintenance of the safety and soundness of any financial institution. The guidance notes that sound liquidity contingency plans ensure adequate diversification of the potential sources of funds to be used in a contingency. By enhancing the availability of discount window credit, the Federal Reserve's new primary credit program offers depository institutions an additional source of backup funds for managing short-term liquidity risks and thus can enhance the diversification of contingency funds.

The guidance notes that appropriate use of primary credit for contingency situations requires institutions to ensure that: 1) the necessary documentation and collateral arrangements are in place; 2) primary credit lines are periodically tested; 3) viable take-out or exit strategies exist to replace primary credit borrowings; and 4) appropriate cost/benefit analyses are conducted in light of the cost of primary credit borrowings relative to other sources of short-term contingency funds.

Finally, the guidance notes that occasional use of primary credit for short-term contingency funding should be viewed as appropriate and unexceptional by both management and supervisors. At the same time, the guidance emphasizes that the primary facility is only one of many tools institutions may use in managing their back-up liquidity needs, and that institutions should maintain access to a diversified array of funding sources. The use of primary credit, or any other potential source of contingency funding, is a management decision that must be made in the context of safe and sound management practices.

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Additional Information

All circulars and documents are available on the Internet through the Federal Reserve Bank of San Francisco's Internet site, at <http://www.frbsf.org/banking/letters>. Paper copies of the guidance are available from our Corporate Services Department. To request copies to be sent by mail, please call (415) 974-2060.

For additional information about the appropriate use of the Discount Window, please contact our Banking Supervision and Regulation Department at (415) 974-2974.

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Attachment: [Advisory on the Use of the Federal Reserve's Primary Credit Program in Effective Liquidity Management](#)