Insights

Financial Services Regulators Respond to COVID-19

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In response to the impact of the coronavirus outbreak ("COVID-19") on our economy and our financial institutions, the FDIC, the Federal Reserve Board and the Office of the Comptroller of the Currency (the "Banking Regulators") have taken a series of steps in the past two weeks to provide financial institutions the flexibility to help affected customers, including (i) modifying the regulatory capital rule as it relates to eligible retained income, (ii) urging banks to use their capital and liquidity buffers in response to COVID-19, and (iii) encouraging banks to work with affected customers and communities, particularly those that are low- and moderate-income.

Eligible Retained Income

The Banking Regulators jointly issued an **interim final rule** to revise the definition of eligible retained income. The purpose of regulatory action is to make any limitations on capital distributions as a result of the current capital rules more gradual.

The Banking Regulators noted the following highlights from this action:

- The interim final rule revises the definition of eligible retained income to the greater of (1) a banking organization's net income for the four preceding calendar quarters, net of any distributions and associated tax effects not already reflected in net income, and (2) the average of a banking organization's net income over the preceding four quarters.
- The revised definition of eligible retained income is intended to strengthen the incentives for banking organizations to use their capital buffers as intended in adverse conditions and serve as a financial intermediary and source of credit to the economy.
- This revision would reduce the likelihood that a banking organization is suddenly subject to abrupt and restrictive distribution limitations in a scenario of lower than expected capital levels. Such a scenario may occur due to the economic disruption caused by COVID-19.

- The revised definition would assist in the ability of S-corporation banks to provide dividends to shareholders in order to meet their pass-through tax liabilities. S-corporation banks should refer to FIL-40-2014 for additional guidance.

Capital and Liquidity Buffers

The Banking Regulators issued **Q&As** related to the Statement Regarding the Use of Capital and Liquidity Buffers dated March 2010. The Banking Regulators noted the following highlights from this action:

- The Banking Regulators are encouraging banking organizations to use their capital and liquidity buffers as they respond to the challenges presented by the effects of COVID-19.
- These capital and liquidity buffers were designed for this purpose to provide banking organizations with the means to support the economy in adverse situations and allow banking organization to continue to serve households and businesses. The Banking Regulators expect banking organizations to continue to manage their capital actions and liquidity risk prudently.
- The Q&As respond to public inquiries from banking organizations regarding the use of their capital and liquidity buffers.

CRA Considerations

The Banking Regulators issued a Joint Statement on **CRA Consideration for Activities in Response to COVID-19** which highlights the following:

- The Banking Regulators recognize that financial institutions working with affected customers during disasters and national emergencies serves the long-term interests of these communities and the financial system, when consistent with safe and sound banking practices and applicable laws, including consumer protection laws.
- Pursuant to the CRA, the agencies will favorably consider retail banking services and retail lending activities in a financial institution's assessment areas that are responsive to the needs of low- and moderate-income individuals, small businesses, and small farms affected by COVID-19 consistent with safe and sound banking practices.
- In light of the declaration of a national emergency, the Joint Statement clarifies that financial institutions will receive CRA consideration for community development (CD) activities.
- Qualifying CD activities include those that help to revitalize or stabilize low- or moderate-income geographies as well as distressed underserved non metropolitan middle income geographies, and that support community

services targeted to low- or moderate-income individuals.

- Favorable consideration will be given to CD activities located in a broader statewide or regional area that includes a bank's CRA Assessment Area and that help to stabilize communities affected by the COVID-19, provided that such institutions are responsive to the CD needs and opportunities that exist in their own assessment area(s).
- The Joint Statement shall be effective through the six-month period after the national emergency declaration is lifted, unless extended by the Banking Regulators.

Additional Guidance Encouraging Financial Institutions to Work With Affected Borrowers

The CFPB, the Conference of State Bank Supervisors, the FDIC, the Federal Reserve Board, the NCUA and the Office of the Comptroller of the Currency (collectively the "Agencies") issued **additional guidance** encouraging financial institutions to work constructively with borrowers impacted by COVID-19 and providing additional information regarding loan modifications.

The guidance provides assurance to financial institutions that the regulators will not criticize institutions for doing so in a safe and sound manner, and will not direct supervised institutions to automatically categorize loan modifications as troubled debt restructurings. The joint statement also provides supervisory views on past-due and nonaccrual regulatory reporting of loan modification programs

The OCC, FDIC, and NCUA have all established COVID-19 resource pages on their websites (available below) that provide further information on the regulatory response to pandemic.

https://www.occ.treas.gov/topics/supervision-and-examination/bank-operations/covid-19-information/convid-19-info-index.html

https://www.fdic.gov/coronavirus/index.html

https://www.ncua.gov/coronavirus

The Krieg DeVault Financial Services team is closely monitoring the regulatory response to the COVID-19 pandemic, and able to assist your institution navigate the myriad of issues this unprecedented crisis presents. As further developments occur, this Alert will be updated.