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Community Banks and the COVID-19 Crisis: CBLR and CECL

September 10, 2020
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Certain provisions of the CARES Act provided community banks breathing room while they worked to facilitate the badly needed economic recovery, including the following:

- Temporarily reducing the Community Bank Leverage Ratio (CBLR); and
- Delaying the implementation of the current expected credit losses (CECL) methodology for estimating allowances for credit losses.

On August 26, 2020, the Banking Agencies adopted two rules which are substantially similar to rules issued based on these CARES Act provisions.

CBLR

On September 17, 2019, the Banking Agencies issued a new rule to provide a simplified measure of capital adequacy for certain community banking organizations. The rule went into effect on January 1, 2020 and provided that most banks, and bank holding companies with assets of less than $10 billion that have a CBLR of greater than 9%, would be eligible to use the CBLR framework.

The CARES Act temporarily reduced the CBLR to 8% until December 31, 2020 or 60 days after the end of the COVID-19 crisis—whichever is sooner. A community bank that falls below this temporary CBLR was given a reasonable grace period to get back into compliance. The CARES Act CBLR provisions were adopted by the Banking Agencies in April.

Effective October 1, 2020, the final rule makes no change to the interim final rule issued in April. Additionally, the final rule temporarily lowers the community bank leverage ratio threshold and provides a gradual transition back to the prior level. The threshold will be 8% for the balance of 2020, 8.5% for 2021, and 9% beginning January 1, 2022.

The final rule also retains the grace period. A community banking organization that falls below the CBRL will still be deemed to be well capitalized during a two-quarter grace period so long as the banking organization maintains a CBRL of 7% from the second to the fourth quarter of 2020, greater than 7.5% during 2021, and greater than 8% thereafter.

CECL

The Banking Agencies issued an interim final rule on March 27, 2020, allowing banks that were required to adopt the CECL methodology on January 1, 2020 to delay the estimated impact on cumulative regulatory capital for up to two additional years. They also provided a three-year transition period commencing after 2022 to eliminate the capital benefit by phasing it out during the two-year delay mentioned above.

Under Section 4014 of the CARES Act, financial institutions were excused from complying with the current CECL until December 31, 2020 or 60 days after the end of the COVID-19 crisis—whichever is sooner.

The CECL final rule is substantially similar to the March 27 interim final rule. The final rule gives eligible institutions the option to mitigate the estimated capital effects of CECL for two years, followed by a three-year transition period. These measures provide banks with a transition period of up to five years.

In addition, the final rule expands the pool of eligible institutions to include any institution adopting CECL in 2020. The CECL final rule will be effective upon publication in the Federal Register.