Board of Governors of the Federal Reserve System
Federal Deposit Insurance Corporation
Office of the Comptroller of the Currency

Joint Statement on the Interaction of Regulatory Capital Rule: Revised Transition of the CECL Methodology for Allowances with Section 4014 of the Coronavirus Aid, Relief, and Economic Security Act

March 31, 2020

On March 27, 2020, the Board of Governors of the Federal Reserve System, the Federal Deposit Insurance Corporation, and the Office of the Comptroller of the Currency (together, the agencies) issued an interim final rule (IFR) that delays the estimated impact on regulatory capital stemming from the implementation of Accounting Standards Update No. 2016-13, Financial Instruments – Credit Losses, Topic 326, *Measurement of Credit Losses on Financial Instruments* (CECL) for a transition period of up to five years (CECL IFR).[1]

Also on March 27, 2020, the Coronavirus Aid, Relief, and Economic Security Act (CARES Act) was signed into law.[2] The CARES Act provides banking organizations optional temporary relief from complying with CECL (statutory relief) ending on the earlier of (1) the termination date of the current national emergency, declared by the President on March 13, 2020 under the National Emergencies Act[3] concerning the coronavirus disease 2019 (COVID-19), or (2) December 31, 2020 (statutory relief period).

This joint statement clarifies the interaction between the CECL IFR and the CARES Act for purposes of regulatory capital requirements.

The recent disruptions in economic conditions caused by COVID-19 and the uncertainty of its overall effects on the economy have presented significant operational challenges to banking organizations at the same time they have been required to direct significant resources to implement CECL. The goal of the CECL IFR is to provide regulatory relief to banking organizations in order to allow them to better focus on supporting lending to creditworthy households and businesses.[4] Alternatively, banking organizations may use the regulatory capital CECL transition rule issued by the banking agencies in February 2019.[5]

[1] Interagency Press Release: https://www.federalreserve.gov/newsevents/pressreleases/bcreg20200327a.htm

[2] Coronavirus Aid, Relief, and Economic Security Act, Pub. L. No. 116-136, § 4014, 134 Stat. 281 (Mar. 27, 2020).

[3] 50 U.S.C. 1601 et seq.

[4] Banking organizations subject to the agencies' capital rule include national banks, state member banks, state nonmember banks, savings associations, and top-tier bank holding companies and savings and loan holding companies domiciled in the United States not subject to the Board's Small Bank Holding Company Policy Statement (12 CFR part 225, Appendix C), but exclude certain savings and loan holding companies that are substantially engaged in insurance underwriting or commercial activities or that are estate trusts, and bank holding companies and savings and loan holding companies that are employee stock ownership plans.

[5] 84 FR 4222 (February 14, 2019).

The CECL IFR provides banking organizations that are required (as of January 1, 2020) to adopt CECL for accounting purposes under U.S. generally accepted accounting principles (U.S. GAAP) during 2020 an option to delay an estimate of CECL's impact on regulatory capital. The capital relief in the CECL IFR is calibrated to approximate the difference in allowances under CECL relative to the incurred loss methodology for the first two years of the transition period. The cumulative difference at the end of the second year of the transition period is then phased in to regulatory capital over a three-year transition period. In this way, the CECL IFR gradually phases in the full effect of CECL on regulatory capital, providing a five-year transition period.

No banking organization is required to comply with CECL during the statutory relief period in the CARES Act, including banking organizations that otherwise would be required to adopt CECL in 2020 under U.S. GAAP. Such banking organizations may delay compliance with CECL until the statutory relief period expires. Banking organizations that elect to use the statutory relief may also elect the regulatory capital relief provided under the CECL IFR after the expiration of the statutory relief period.

A banking organization may choose to apply CECL pursuant to U.S. GAAP in 2020. If it does, it may elect to obtain the full benefit from the regulatory capital relief provided under the CECL IFR.

A banking organization's five-year transition period under the CECL IFR begins on the date it would have been required to adopt CECL under U.S. GAAP, regardless of whether the banking organization uses the statutory relief. For a banking organization that uses the statutory relief, and subsequently opts to use the relief provided in the CECL IFR, the initial two-year transition period would be reduced by the number of quarters during which the banking organization uses the statutory relief.

The following examples illustrate different scenarios of how the CARES Act and the CECL IFR interact (assuming the statutory relief period remains in effect through December 31, 2020).

Banking organization using the statutory relief starting in the first quarter of 2020:

- A banking organization required under U.S. GAAP to adopt CECL on January 1, 2020, elects to use the statutory relief during the first three quarters of 2020, and then files reports using CECL starting in the fourth quarter of 2020, would have the option under the CECL IFR to delay the estimated effect of CECL on regulatory capital over a period of five quarters (starting in the fourth quarter of 2020) along with its day-one CECL transition amount. This period would be followed by a three-year transition period to phase out the aggregate amount of such capital benefit.

Banking organization (with a calendar year fiscal year) that does not use the statutory relief:

- A banking organization that is required to implement CECL starting January 1, 2020, under U.S. GAAP, and does not opt to use the statutory relief, could make use of the CECL IFR's transitional amounts in regulatory capital for eight quarters, followed by a three-year transition period to phase out the aggregate amount of such capital benefit.

Banking organization (with a non-calendar year fiscal year) that does not use the statutory relief:

- A banking organization with a fiscal year starting after January 1, 2020 that is required to implement CECL under U.S. GAAP in 2020, and does not opt to use the statutory relief, could also make use of the CECL IFR's transitional amounts in regulatory capital for eight quarters, followed by a three-year transition period to phase out the aggregate amount of such capital benefit.

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