Community Bankers of Michigan Regulatory Dispatch

April 26, 2023

Timely news and resources community bankers can use

to better stay on top of a rapidly changing world.

Interagency Policy Statement on Allowances for Credit Losses

SUMMARY: The federal financial institution regulatory agencies have jointly issued the attached Interagency Policy Statement on Allowances for Credit Losses (statement revised April 2023). The agencies issued this revised statement in response to changes in the accounting guidance for troubled debt restructurings (TDRs) by creditors under U.S. generally accepted accounting principles (U.S. GAAP).

Comment: Community banks must evaluate modified loans and investment securities held-to-maturity and available-for-sale for impairment under FASB Accounting Standards Update (ASU) 2022-02.

CBM Insights

Q. Are we required to have 'builders' risk' insurance at closing for a construction loan? If the borrower pays for it after closing, how do we disclose that on the Closing Disclosure?

A. When 'builders' risk' insurance is required is as much a matter of bank policy as a regulatory requirement. Banks usually require 'builders' risk' insurance as a requirement of an acceptable construction loan contract with the builder.

Typically, 'builders' risk' insurance is not written with the borrower as an insured party. That is an important consideration especially when contemplating flood insurance requirements. The FDPA does not require flood insurance be in place at closing on a construction loan, just that it be in place '…before the lender disburses funds to pay for building construction (except as necessary to pour the slab or perform preliminary site work, such as laying utilities, clearing brush, or the purchase and/or delivery of building materials) on the property securing the loan.

If the property is not in a flood zone, you would still want 'builders' risk' insurance in place before advancing funds to begin actual construction for safety & soundness reasons. Having it in place at closing just means that you don't have to 'adequate internal controls in place' to ensure it is obtained before funding.

As far as the Closing Disclosure and 'builders' risk' insurance, it would be disclosed in Section H if it is required to have been paid or is to be paid from closing funds.

If it is paid after closing, it would not be disclosed on the Closing Disclosure. Oddly enough, the CFPB added specific requirements for an addendum for post-consummation construction loan inspection fees in TRID 2.0, but that did not address post-consummation payment of 'builders' risk' insurance premiums.

Items of Interest

Bank Management

OCC Acting Comptroller Discusses Open Banking (04/19/2023) - WASHINGTON—Acting Comptroller of the Currency Michael J. Hsu discussed the Office of the Comptroller of the Currency's (OCC) approach to open banking in remarks at FDX Global Summit Spring 2023 in Raleigh, N.C.

In his remarks, the Acting Comptroller highlighted the evolution of open banking and its potential impact on the OCC's supervision in the context of liquidity, operational, third-party, and compliance risks. He also discussed the importance of data, and the relationship of banking and commerce, in the development of open banking to build trust among consumers and the public.

Comment: Open banking describes the process of banks and other traditional financial institutions giving customers and third parties easy digital access to their financial data. While data portability will likely be empowering for consumers, it could also increase the liquidity risk of retail deposits for community banks, said acting Comptroller of the Currency Michael Hsu.

FRB Beige Book (04/19/2023)

- Federal Reserve Bank of Boston
- Federal Reserve Bank of New York
- Federal Reserve Bank of Philadelphia
- Federal Reserve Bank of Cleveland
- Federal Reserve Bank of Richmond
- Federal Reserve Bank of Atlanta
- Federal Reserve Bank of Chicago
- Federal Reserve Bank of St. Louis
- Federal Reserve Bank of Minneapolis
- Federal Reserve Bank of Kansas City
- Federal Reserve Bank of Dallas
- Federal Reserve Bank of San Francisco

Overall Economic Activity:
Overall economic activity was little changed in recent weeks. Nine Districts reported either no change or only a slight change in activity this period while three indicated modest growth. Expectations for future growth were mostly unchanged as well; however, two Districts saw outlooks deteriorate. Consumer spending was generally seen as flat to down slightly amid continued reports of moderate price growth. Auto sales remained steady overall, with only a couple of Districts reporting improved sales and inventory levels. Travel and tourism picked up across much of the country this period. Manufacturing activity was widely reported as flat or down even as supply chains continued to improve. Transportation and freight volumes were also flat to down, according to several Districts. On balance, residential real estate sales and new construction activity softened modestly. Nonresidential construction was little changed while sales and leasing activity was generally flat to down. Lending volumes and loan demand generally declined across consumer and business loan types. Several Districts noted that banks tightened lending standards amid increased uncertainty and concerns about liquidity. The majority of Districts reported steady to increasing demand and sales for nonfinancial services. Agriculture conditions were mostly unchanged in recent weeks while some softening was reported in energy markets.

Labor Markets:
Employment growth moderated somewhat this period as several Districts reported a slower pace of growth than in recent Beige Book reports. A small number of firms reported mass layoffs, and those were centered at a subset of the largest companies. Some other firms opted to allow for natural attrition to occur, and to hire only for critically important roles. Contacts reported the labor market becoming less tight as several Districts noted increases to the labor supply. Additionally, firms benefited from better employee retention, which allowed them to hire for open roles while not constantly trying to back-fill positions. Wages have shown some moderation but remain elevated. Several Districts reported declining needs for off-cycle wage increases compared to last year.

Prices:
Overall price levels rose moderately during this reporting period, though the rate of price increases appeared to be slowing. Contacts noted modest-to-sharp declines in the prices of nonlabor inputs and significantly lower freight costs in recent weeks. Nevertheless, producer prices for finished goods rose modestly this period, albeit at a slightly slower pace. Selling price pressures eased broadly in manufacturing and services sectors. Consumer prices generally increased due to still-elevated demand as well as higher inventory and labor costs. Prices for homes and rents leveled out in most Districts but remained at near record highs. Contacts expected further relief from input cost pressures but anticipated changing their prices more frequently compared to previous years.

Dallas:
Modest growth continued, with steady gains in service sector activity and a pickup in home sales and manufacturing output. Job growth was modest, though hiring slowed sharply in services. The pace of price increases slowed. Outlooks were largely negative, and contacts voiced concern about weakening demand, a potential recession, and the spillover effects of the recent bank failures on the broader economy.

FDIC Releases Semiannual Update on the Deposit Insurance Fund Restoration Plan (04/18/2023) - WASHINGTON – The Board of Directors of the Federal Deposit Insurance Corporation (FDIC) released its semiannual update on the Restoration Plan for the agency's Deposit Insurance Fund (the Fund).

FDIC Chairman Martin J. Gruenberg said, "The bottom line to this update is that even with increased uncertainty in the banking industry and the recent failure of two large banks, staff project that the losses from the two failures are not expected to have a material effect on the projected timeline for reaching the statutory minimum reserve ratio of 1.35 percent. The reserve ratio is expected to reach the minimum ahead of the statutory deadline of September 30, 2028, and staff recommend no changes to the Amended Restoration Plan at this time."

The FDIC estimates that the two recent failures of Silicon Valley Bank and Signature Bank resulted in losses of approximately $22.5 billion, of which $19.2 billion is attributable to the protection of uninsured depositors under the Systemic Risk Exception. Federal law requires that any losses to the FDIC's Deposit Insurance Fund related to this action be repaid by a special assessment on banks. Only the remaining $3.3 billion in losses will directly impact the DIF balance and is not expected to have a material effect on the projected timeline for reaching the statutory minimum reserve ratio.

Background:
The Federal Deposit Insurance Act (FDI Act) requires that the FDIC's Board of Directors adopt a restoration plan when the Fund's reserves fall below 1.35 percent of all insured deposits held in FDIC-insured financial institutions. Extraordinary deposit growth during the first and second quarters of 2020 caused the Fund's reserve ratio to decline below this statutory minimum. On September 15, 2020, the FDIC established a plan to restore the Fund's reserves to at least 1.35 percent by September 30, 2028, while maintaining the assessment rate schedule in place at the time.

	On June 21, 2022, the FDIC Board of Directors approved an amendment to the agency's Restoration Plan and proposed to increase deposit insurance assessment rates by two basis points for all insured depository institutions. On October 18, 2022, the FDIC Board adopted a final rule to increase initial base deposit insurance assessment rate schedules by two basis points beginning in the first quarterly assessment period of 2023. ***Comment: While community banks will be happy to hear that this particular update on the DIF restoration plan will not result in increased deposit insurance assessments…yet. There are discussions on how to recoup the costs of the systemic risk exception coverage of uninsured deposits in March resulting from Silicon Valley Bank and Signature Bank failures.***
	FRB Considerations for a Central Bank Digital Currency Governor Michelle W. Bowman (04/18/2023) - *In broad terms, a CBDC is simply a new form of digital liability of a central bank. Because it is issued by a central bank, CBDC is typically thought of as being denominated in the currency of that central bank. One could imagine a digital U.S. dollar, a digital euro, or a digital pound. Beyond this baseline definition though, "what is a CBDC" defies a simple definition. A CBDC built on distributed ledger technology offers a wide range of design and potential use options, as well as potential risks. This variability complicates any discussion of a CBDC simply because we may not be talking about the same thing.* *There are two threshold questions that a policymaker needs to ask before any decision to move forward with a CBDC. First, what problem is the policymaker trying to solve, and is a CBDC a potential solution? Second, what features and considerations--including unintended consequences--may a policymaker want to consider in deciding to design and adopt a CBDC? While it would be impossible for me to provide a comprehensive analysis of every issue surrounding CBDC, my goal today is to offer a perspective on these two threshold questions and to conclude with some thoughts about the imperative for future research on CBDCs and the potential future of CBDCs in the United States.* *What Problem Could a CBDC Solve?* *In my view, the fundamental question is: what problem could a CBDC solve?* ***Comment: Bowman noted "the risk that a [central bank digital currency] would provide not only a window into, but potentially an impediment to, the freedom Americans enjoy in choosing how money and resources are used and invested."***

BSA / AML

	FinCEN Renews and Expands Real Estate Geographic Targeting Orders (04/21/2022) - WASHINGTON—The Financial Crimes Enforcement Network (FinCEN) announced the renewal and expansion of its Geographic Targeting Orders (GTOs) that require U.S. title insurance companies to identify the natural persons behind shell companies used in non-financed purchases of residential real estate. The terms of the GTOs are effective beginning April 25, 2023 and ending on October 21, 2023. The GTOs continue to provide valuable data on the purchase of residential real estate by persons possibly involved in various illicit enterprises. Renewing the GTOs will further assist in tracking illicit funds and other criminal or illicit activity, as well as continuing to inform FinCEN's regulatory efforts in this sector. FinCEN renewed the GTOs that cover certain counties within the following major U.S. metropolitan areas: Boston; Chicago; Dallas-Fort Worth; Houston; Laredo; Las Vegas; Los Angeles; Miami; New York City; San Antonio; San Diego; San Francisco; Seattle, the District of Columbia, Northern Virginia, and Maryland

	(DMV) area; as well as the City and County of Baltimore, the County of Fairfield, Connecticut, and the Hawaiian islands of Honolulu, Maui, Hawaii, and Kauai. FinCEN, working in conjunction with our law enforcement partners, identified additional regions that present greater risks for illicit finance activity through non-financed purchases of residential real estate. Accordingly, today, FinCEN expanded the geographic coverage of the GTOs to Litchfield County in Connecticut and Adams, Arapahoe, Clear Creek, Denver, Douglas, Eagle, Elbert, El Paso, Fremont, Jefferson, Mesa, Pitkin, Pueblo, and Summit counties in Colorado. The effective period of the GTOs for purchases in these newly added areas begins on May 24, 2023. The purchase amount threshold remains $300,000 for each covered metropolitan area, with the exception of the City and County of Baltimore, where the purchase threshold is $50,000. ***Comment: Residential real estate transactions covered by the GTOs include transactions made with cashier's checks, certified checks, traveler's checks, personal checks, business checks, money orders, funds transfers, or virtual currency. Michigan is not currently covered under a GTO.***
	CSBS Model Money Transmission Modernization Act (04/21/2023) - The Model Money Transmission Modernization Act, also known as the Money Transmitter Model Law, is a single set of nationwide standards and requirements created by industry and state experts. The law was approved in full by the CSBS Board of Directors in August 2021. As we move forward, CSBS will work to ensure that implementation among states is as uniform as possible, as states may require legislation, regulation or guidance changes to adopt the provisions contained in the law. ***Comment: The act, also referred to as the Money Transmitter Model Law, is intended to replace 50 sets of state-specific money transmitter laws and rules with a single set of nationwide standards and requirements designed by state and industry experts.***

Deposit / Retail Operations

	No news to report this week.

Human Resources

	No news to report this week.

Lending

	CFPB Provides Additional SBL Sample Data Collection Form File Formats (04/17/2023) - The CFPB has provided additional file formats of the small business lending rule sample data collection form, including sample code to create web versions. You can access the additional formats of the form here: www.consumerfinance.gov/compliance/compliance-resources/small-business-lending-resources/small-business-lending-collection-and-reporting-requirements/. ***Comment: The sample code to create a web version of the data collection form will be particularly helpful for online business applicants. This information can be found on our website www.cbofm.org.***

Technology / Security

	CISA Cyber Experts Talk Shop on the Need for Safer Tech (04/20/2023) - Last week, CISA and 9 U.S. and international cybersecurity agencies released a whitepaper titled "Shifting the Balance of Cybersecurity Risk: Principles and Approaches for Security-by-Design and Default." For those of you playing along at home, 10 agencies signing onto a document is a record number for us at CISA. The document argues that we need to significantly reshape the way software is created to prioritize safety as a non-negotiable foundation. That is, we need to bake security into product development. This is directly in line with the vision laid out in the recently-released National Cybersecurity Strategy, which states that “Today, end users bear too great a burden for mitigating cyber risks” and that “we must ask more of the most capable and best-positioned actors.” When we released the paper a number of prominent tech companies, think tanks and analysts agreed that the burden of cybersecurity is placed too much on the user and believe this whitepaper is a step in the right direction to solving the problem. Others pointed out that while techniques for developing secure by design software exist, they have not been widely adopted.

Selected federal rules – proposed

Proposed rules are included only when community banks may want to comment. Date posted may not be the same as the Federal Register Date.

PROPOSED RULE WITH REQUEST FOR PUBLIC COMMENT

02.01.2023 CFPB Credit Card Penalty Fees (Regulation Z) The Consumer Financial Protection Bureau (Bureau) proposes to amend Regulation Z, which implements the Truth in Lending Act (TILA), to better ensure that the late fees charged on credit card accounts are “reasonable and proportional” to the late payment as required under TILA. The proposal would (1) adjust the safe harbor dollar amount for late fees to $8 and eliminate a higher safe harbor dollar amount for late fees for subsequent violations of the same type; (2) provide that the current provision that provides for annual inflation adjustments for the safe harbor dollar amounts would not apply to the late fee safe harbor amount; and (3) provide that late fee amounts must not exceed 25 percent of the required payment. **Comments should be received on or before May 3, 2023.**