FedFin Daily Briefing

Tuesday, December 22, 2020

New PPP: A Whole Lot More Generous Than the Old PPP

As noted, the new, sweeping COVID-stimulus measures include renewed PPP lending and, finally, a one-page forgiveness process for loans of less than $150,000. Most notably for lenders, the measure not only increases PPP guaranteed amounts by another $284 billion, but also expands the expenses small-businesses may offset via forgivable loan balances. This, combined with a provision allowing eligible small businesses with outstanding PPP loans to get additional loans if they can demonstrate revenue loss, should significantly increase borrower demand and loan size. These provisions may also facilitate a new round of lending to very small and minority borrowers, reaching unmet needs and allowing banks to serve new customers as well as the existing ones they initially targeted due to continuing KYC requirements. Importantly, the new measure also provides expansive "hold-harmless" provisions for lenders under both these new loans and those under prior PPP provisions. Regulators are also barred from enforcement actions if lenders act in good faith and rely on appropriate borrower certifications and attestations.

The bill also requires the SBA to promulgate implementing rules no later than ten days after enactment. This seems unlikely. However, should SBA meet this deadline, the rules are likely to be as hastily designed as during the March CARES launch, possibly leading to renewed confusion and more challenges for PPP lenders. Forgiveness-related rules are due 24 days after enactment, but even then it may be difficult to determine forgivable loan amounts because many of the new expenses now eligible for PPP loans (e.g., PPE, IT infrastructure) are not comparable to past expenses in 2019 nor may have been undertaken in 2020 due to the absence of the funds necessary to acquire them. Further, loans made prior to enactment in which borrowers have or may now claim newly-eligible expenditures are also forgivable up to and including these expenses. Again, this raises complexities and may in practice mean that prior loans now eligible for simplified forgiveness are wholly forgiven even if some expenditures were not previously eligible or may even now be questionable. Borrowers must, however, retain records to document assertions made in forgiveness applications.

FSB Advances Climate-Risk Disclosures

The FSB today responded to the IFRS Foundation's September sustainability-reporting consultation, now making clear that global regulators support the Foundation's approach and encouraging it to use the FSB Task Force on Climate-related Financial Disclosures 2017 recommendations for this sector. These have already been voluntarily implemented in some jurisdictions, with FSB noting significant growth in industry support for the recommendations. However, minimum-disclosure standards should be internationally-agreed upon to promote consistency even as they allow for additional national standards. The FSB also encourages the Foundation to consider whether IASB can strengthen its existing IFRS standards and forthcoming management commentary to capture financially-material information. FSB will report to the G20 finance ministers and central bank governors in July on more ways to promote climate-risk disclosure global coordination.

Agencies Give Conditional Relief for Asset-Management Ownership Stakes, More Rules to Come

Reflecting the huge market power of mutual funds, ETFs, and the asset managers that sponsor them, the federal banking agencies today issued a supervisory letter absolving asset managers of control presumptions when holding large positions in a banking organization as long as banks and asset managers satisfy conditions showing that the asset manager in fact does not exercise control over the bank. However, this relief is solely for temporary enforcement purposes; the agencies are planning a regulation to take on this question in more detail at a time not stated in the supervisory letter. It is unclear if this rule would be freestanding or come in concert with the broader review we expect shortly from the FRB and FSOC of bank/asset-management interconnectivity concerns laid out in a 2015 FSOC request for comment (see FSM Report **SYSTEMIC75**) and revisited with still more urgency in the FSB's holistic review of NBFIs (see *Client Report* **NBFI**).

Fed Recasts Interest on Reserves to Recognize QE

Modernizing its reserve requirements to reflect their far different configuration due to quantitative easing, the Federal Reserve today formalized an interim final rule setting transaction-account reserves at zero and proposed to simplify the terminology for interest on excess reserves, now using the terminology "interest on reserve balances" or IORB. This reflects that there is no longer anything "excess" about the reserves that earn interest from the Fed. The proposal also simplifies the way master accounts may transmit interest to correspondent banks via pass-through accounts. Nothing in the NPR addresses broader questions about interest payments, how these are calculated, and the role they play in Fed policy and the economy as a whole. Although these have been a significant GOP concern (see *Client Reports* in the **IOER** series), interest on Fed balances has become an accepted aspect of unconventional policy and, absent a significant change in how the FOMC sets this rate, we do not expect serious challenge to it in the next Congress.

FHFA Moves on from GSE Capital, Liquidity to Orderly Resolution

Today, FHFA continued fast-paced action to craft a new regulatory framework for the GSEs in conservatorship and beyond. Moving from its complex and controversial capital rule and last week's liquidity proposal, the agency today added a proposed approach to GSE resolution planning. This meets the agency's commitments under the 2019 reform plan with the Trump Administration (see Client Report **GSE143**) and FSOC's 2020 report. The proposal also lays out FHFA's thinking on the rules the Fed would need to promulgate if, as we expect, Fannie and Freddie are designated as SIFIs when Janet Yellen takes over.

FHFA says its rule is similar to the living-will requirements mandated by the FRB and FDIC (see *Client Reports* in the **LIVINGWILL** series). However, the GSEs are different than large banks and GSIBs in that they have an implicit federal guarantee considered still more binding in conservatorship. This resolution framework may thus have sweeping structural impact based on the extent to which it forces the GSEs to stand firm without resort to a federal backstop via infrastructure resilience, indemnification provisions, and measures to continue operations safeguarding U.S. housing finance without establishment of a receivership

Recent Files Available for Downloading

The following reports and analyses have been sent to retainer clients recently. Copies are also available to retainer clients on the Archives section of Federal Financial Analytics' website: www.fedfin.com or clients may obtain the reports/analyses by e-mailing requests@fedfin.com giving the requested item name, firm, and e-mail address. To learn more about GSE Activity Reports, click: http://www.fedfin.com/index.php?option=com_content&view=article&id=18&Itemid=18

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- **FEDERALRESERVE59**: It's hard to envision a Federal Reserve still more central to every aspect of U.S. macroeconomic, financial, and fiscal policy, but that's what FedFin forecasts for 2021.

- **ILC15:** Setting the stage for new charters and legislative battles in 2021, the FDIC has finalized a controversial proposal addressing source-of-support and certain other obligations for the parent companies of some industrial banks and industrial loan companies (ILCs).

- **GSE122120:** As previously noted, FHFA late last week issued a long-promised proposal implementing LCR- and NSFR-like – but not light – rules for Fannie Mae and Freddie Mac.

- **CONSUMER36**: On Monday, the Biden transition released a readout of a meeting between Treasury nominees Janet Yellen and Wally Adeyemo with various racial-equity associations, reinforcing the importance this issue will have in crafting financial regulation in the Biden Administration.

- **GSE121720**: FHFA's controversial capital rule is in today's *Federal Register*, setting an effective date of February 16.

- **GSE-121620**: Secretary Mnuchin's comments yesterday make it clear – at least mostly – that Fannie and Freddie will remain in conservatorship as the Biden Administration takes charge.

- **REFORM200**: In this report, we continue our 2021 forecasts, moving from our assessment of digital finance (see Client Report **DIGITAL6**) and asset-management regulation (see Client Report **RECOURSE6**) to an assessment of the U.S. capital and liquidity framework for large banks and FBOs.

- **RECOURSE6**: In this report, we assess the regulatory consequences of one of the ironies of March's market turmoil: among the reasons it was not worse is because some large banks stepped in and backed customers or investors despite the lack of any legal obligation to do so.

- **CHARTER28:** Continuing Acting Comptroller Brooks' policy of considering precedent-breaking applications and charters, the agency has received a controversial application from Figure to establish a national bank that, by virtue of this charter, would also be a Fed member.

- **GSE-120720:** The last Trump FSOC annual report reiterates 2019's findings: nonbank originators and servicers are weak and interconnected, thus posing systemic risk.

- **DIGITAL6:** Even though 2020 was of course preoccupied by the pandemic, there was no scarcity of the oft-repeated nostrum that law and rule must define the future of digital finance.

- **CHARTER27**: In conjunction with a wide-open request for views on ways to increase the innovativeness of national banks and federal savings associations (FSAs), the OCC has finalized a significant rewrite of their more traditional powers and activities.

- **GSE-120220**: Today's House Financial Services session with Mnuchin and Powell shed just a bit more light – or provided still more uncertainty – on the critical question of whether Treasury will work with FHFA to end the conservatorships before the Biden Administration surely keeps them for a long, long time.

- **GSE-120120A**: At today's Senate Banking hearing on the CARES-funding fracas, Secretary Mnuchin told Sen. Rounds (R-SD) that the GSEs should be quickly brought out of conservatorship but that they will not be let out without sufficient capital.

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- **GSE-120120**: Given the high confirmation odds for Janet Yellen as the nation's next Treasury Secretary, we here assess her impact on the future of U.S. housing finance.

- **ESG3**: Following through on one of his pledges, Acting Comptroller Brooks' agency has issued a controversial proposal to prevent large banks and perhaps all federally-chartered ones from deciding whether or not to grant credit on grounds other than clear, quantitative indicators of ability to repay.

- **GSE-112420**: Building on our analysis of the overall final FHFA capital rule, we turn here to an assessment of the rule's strategic impact.

- **GREEN5**: In its latest report on climate risk, the Financial Stability Board reiterates the complexity of measuring financial-system climate risk, continuing its work to enhance the ability of regulators and financial institutions to do so due to the magnitude both physical and transition risks are likely to pose.

- **GSE-112320: I**n this report, we build on our initial summary of FHFA's final capital construct to assess one of the most important issues on which FHFA made at least some concessions.

- **GSE-111920**: On Monday, we reiterated our call that FHFA would move the capital rule ASAP and then end the conservatorship as quickly as possible under terms and conditions designed to make it challenging for the Biden Administration to unravel a fait accompli.

- **GSE-111820**: In its 2020 systemic-risk assessment, the Office of Financial Research takes unusual issue with GSE CRT transactions.

- **SYSTEMIC90**: The Office of Financial Research's latest systemic-risk assessment reiterates much of the market analysis in the FRB's recent report (see Client Report **SYSTEMIC89**), the FSB's analysis (see Client Report **NBFI**), and the OCC's risk matrix.

- **NBFI**: As promised again just last week, the Financial Stability Board today released a "holistic" plan for dealing with NBFIs along with an ambitious agenda for global standards as soon as next year.

- **GSE-111620**: Responding to your requests, this report summarizes and expands on the post-election outlook for U.S. housing policy we've also discussed with many of you since November 3.

- **RESCUE78**: Today's HFSC hearing with federal regulators addressed some of the same ground as the Senate's session earlier this week (see Client Report **RESCUE77**), although Acting Comptroller Brooks did not come in for the shellacking on his innovative charters delivered by Senate Democrats

- **RESCUE77:** At its first hearing following last week's election, Senate Banking today heard testimony from the federal prudential regulators which largely covered ongoing efforts to combat the COVID pandemic's impacts on the financial system.

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