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Congress Shows That It CARES About Accounting Rules for Banks and Credit Unions

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On March 27, 2020, President Trump signed into law the Coronavirus Aid, Relief, and Economic Security Act (the "CARES Act"), which provides relief from certain accounting and financial reporting requirements under U.S. GAAP. **Note that until actions are taken by the SEC or the FASB, the provisions of the CARES Act are not amendments to U.S. GAAP.** However, we do expect the CARES Act's passage to trigger actions by the SEC or FASB (or both). Below are some thoughts on what those actions might be within the context of the relief provided.

Deferral of the CECL Standard

Section 4014 of the CARES Act offers optional temporary relief from applying the FASB's current expected credit losses (CECL) standard (ASU 2016-13)[1] only for the following qualifying entities:

- Insured depository institutions,[2] as defined in Section 3 of the Federal Deposit Insurance Act.
- Credit unions regulated by the National Credit Union Administration.

[1] FASB Accounting Standards Update (ASU) No. 2016-13, *Measurement of Credit Losses on Financial Instruments*.

[2] The CARES Act states that the relief applies to an insured depository institution, bank holding company, or any affiliate thereof.

Qualifying entities are not required to comply with the CECL standard during the period beginning on the date of enactment and ending on the earlier of the following:

- The termination date of the national emergency declared by President Trump under the National Emergencies Act on March 13, 2020, related to the outbreak of novel coronavirus disease 2019 (COVID-19).
- December 31, 2020.

Connecting the Dots

We expect that any guidance developed by the SEC or FASB to address the CARES Act's impact on U.S. GAAP would most likely take into account both the scope and length of any optional deferral. For example, the guidance will most likely take into account whether any deferral should apply to all entities that were otherwise required to adopt the CECL standard or limited to qualifying entities specifically included in the CARES Act. In addition, it is possible that guidance from the SEC or FASB would more clearly define the date of adoption if an entity chose the deferral, which could reduce the uncertainty created by the CARES Act by suggesting that the date of adoption would not be based on an announcement that a national emergency has terminated.

Relief From Troubled Debt Restructurings

Section 4103 of the CARES Act provides temporary relief from the accounting and reporting requirements for troubled debt restructurings regarding certain loan modifications related to COVID-19 that are offered by insured depository institutions and credit unions (i.e., the same entities that qualify for the optional deferral of the CECL standard described above).

Specifically, the CARES Act provides that a qualifying financial institution may elect to suspend (1) the requirements under U.S. GAAP for certain loan modifications that would otherwise be categorized as a troubled debt restructuring and (2) any determination that such loan modifications would be considered a troubled debt restructuring, including the related impairment for accounting purposes. The modifications that would qualify for this exception include any modification involving a loan that was not more than 30 days past due as of December 31, 2019, that occurs during the "applicable period,"[3] including any of the following:

- A forbearance arrangement.
- An interest rate modification.
- A repayment plan.
- Any other similar arrangement that defers or delays the payment of principal or interest.

The exception does not apply to any adverse impact on the credit of a borrower that is not related to the COVID-19 pandemic.

Connecting the Dots

On March 22, 2019, a group of banking agencies[4] released an interagency statement[5] that offers some practical expedients for modifications that occur in response to the COVID-19 pandemic. The expedients require a lender to conclude that a borrower is not experiencing financial difficulty if either (1) short-term (e.g., six months) modifications are made, such as payment deferrals, fee waivers, extensions of repayment terms, or other delays in payment that are insignificant related to loans

[3] The applicable period for loan modifications means the period beginning on March 1, 2020, and ending on the earlier of (1) December 30, 2020, or (2) the date that is 60 days after the termination date of the national emergency declared by President Trump under the National Emergencies Act on March 13, 2020, related to the outbreak of COVID-19.

[4] The Board of Governors of the Federal Reserve System, the Federal Deposit Insurance Corporation, the National Credit Union Administration, the Office of the Comptroller of the Currency, the Consumer Financial Protection Bureau, and the State Banking Regulators.

[5] Interagency Statement on Loan Modifications by Financial Institutions Working With Customers Affected by the Coronavirus.

in which the borrower is less than 30 days past due on its contractual payments at the time a modification program is implemented or (2) the modification or deferral program is mandated by the federal government or a state government (e.g., a state program that requires all institutions within that state to suspend mortgage payments for a specified period).

For a loan modification to be considered a troubled debt restructuring in accordance with ASC 310-40,[6] **both** of the following conditions must be met:

- The borrower is experiencing financial difficulty.
- The creditor has granted a concession (except for an insignificant delay in payment).

Accordingly, any loan modification that meets a practical expedient described above would not be considered a troubled debt restructuring because the borrower is not experiencing financial difficulty. However, if a loan modification does not meet the conditions for a practical expedient, the modification is not necessarily a troubled debt restructuring. The creditor must evaluate whether, under ASC 310-40, the borrower is experiencing financial difficulty and whether a concession, other than an insignificant delay in payment, has been made. Note that in the discussion above on short-term modifications, we are not interpreting the meaning of an insignificant delay in payment; ASC 310-40 provides guidance on determining whether a delay in payment is insignificant.

The CARES Act and the interagency statement overlap in many areas, but they are not consistent. For example, the interagency statement requires an evaluation of whether the borrower is less than 30 days past due at the time a modification program is implemented, as opposed to the CARES Act, under which that determination is made as of December 31, 2019. In addition, the CARES Act allows interest rate modifications to occur on the loans, whereas the interagency statement only provides relief for modifications associated with the timing of payments (e.g., deferrals).

As in the case of the optional deferral of the CECL standard discussed above, entities should monitor any guidance issued by the SEC or FASB. We believe that in the absence of any further clarifications, it would be prudent for entities to apply the guidelines established by the interagency statement given that is an interpretation of U.S. GAAP by banking agencies whereas the CARES Act indicates that GAAP can be suspended. In addition, the FASB issued a statement on March 22, 2020, noting that the interagency statement "was developed in consultation with the staff of the FASB who concur with this approach."

[6] FASB Accounting Standards Codification (ASC) Subtopic 310-40, *Receivables: Troubled Debt Restructurings by Creditors*.

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