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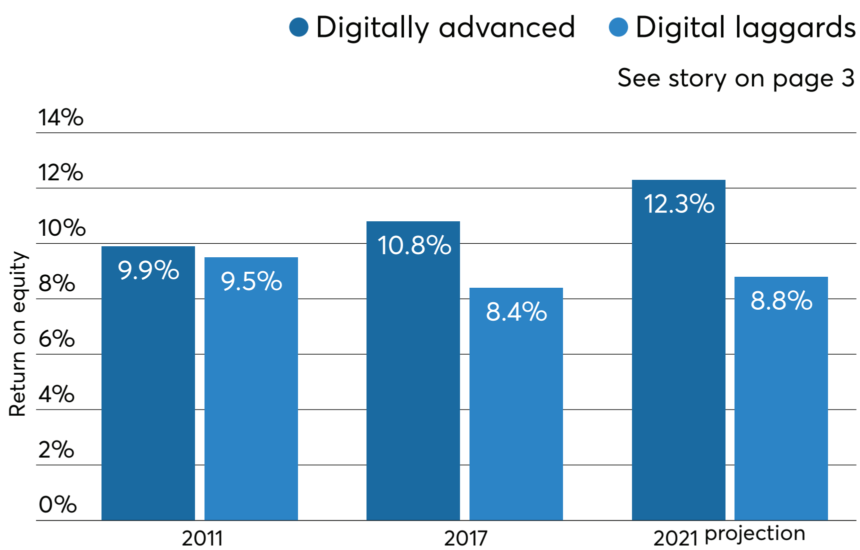
Digital divide

Banks that embraced technology have produced a higher ROE than those that haven't, according to an analysis of 161 banks. The gap is expected to keep widening.



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dailybriefing

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FEDERAL RESERVE

Fed can do only so much to limit pandemic's economic hit: Powell

By Hannah Lang
May 13, 2020

WASHINGTON — Calling the coronavirus crisis "significantly worse than any recession since World War II," Federal Reserve Chairman Jerome Powell warned that the central bank's emergency lending facilities might not be enough to keep businesses afloat if the downturn persists.

The Fed has unveiled roughly a dozen programs under its emergency powers to help boost different segments of the financial markets struggling under the weight of the pandemic, including efforts to backstop corporate and municipal bonds, and help fund the Paycheck Protection Program. Many of the programs are still in the planning stages, such as Main Street Lending Program, through which banks will offer loans to middle-market firms.

But Powell cautioned that the programs are more a short-term defense against liquidity strains than a permanent solution for companies' financial woes.

"A loan from a Fed facility can provide a bridge across temporary interruptions to liquidity, and those loans will help many borrowers get through the current crisis," Powell said in an online video speech for the Peterson Institute for International Economics. "But the recovery may take some time to gather momentum, and the passage of time can turn liquidity problems into solvency problems."

Powell also warned that without more fiscal support from Congress, the economy could face long-term damage and a tougher path to recovery.

"This trade-off is one for our elected representatives, who wield powers of taxation and spending," Powell said. He emphasized that the Fed has the ability to act of its own accord but its mandate is limited to lending powers.

Powell added he didn't believe it was appropriate for the Fed to weigh in on what fiscal measures Congress should consider.

"We don't play a formal role in fiscal policy, meaning that we wouldn't take a position … supporting a particular bill," he said in response to a question from Adam Posen, the president of the Peterson Institute. "It's not our role to supervise Congress; it's actually the other way around."

The speech came as the Fed has been urged to accelerate emergency facilities such as the Main Street Lending Program that were announced but have not gotten off the ground.

The Main Street program will go live in a few weeks, Powell said. He noted that it is different in substance from any of the credit facilities the central bank has stood up before, and is "completely unique in our history."

"We can make loans to solvent borrowers, and to solvent borrowers who don't have access to other private sources of capital," he said. "As I mentioned, the passage of time is really all it takes to turn a liquidity problem into a solvency problem, so we'll be a big help for companies for a while, but over a longer period of time, it may be that more fiscal help is needed."

Powell also said that "avoidable household and business insolvencies can weigh on growth for years to come." If small and medium-sized businesses close permanently, it would hamper job creation, he said.

"A prolonged recession and weak recovery could also discourage business investment and expansion, further limiting the resurgence of jobs as well as the growth of capital stock and the pace of technological advancement," Powell said. "The result could be an extended period of low productivity growth and stagnant incomes."

Already, the job gains the economy enjoyed in the past decade have been erased, making this downturn one "without modern precedent," he said.

The economic slowdown is undoubtedly disproportionately affecting lower-income households. On Thursday the Fed will release survey results showing that about 40% of households earning less than $40,000 a year had experienced job loss in March, Powell said.

"This reversal of economic fortune has caused a level of pain that is hard to capture in words, as lives are upended amid great uncertainty about the future," he said.

And although markets started pricing in the possibility of negative interest rates for the first time last week, Powell effectively ruled out that the Fed would consider lowering the federal funds rate beow zero.

The Federal Open Market Committee's "view on negative rates really has not changed. This is not something that we're looking at," he said, adding that the "evidence on the effectiveness of negative rates is mixed."

"It's an unsettled area, I would call it," said Powell. "For now, it's not something we're considering."

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Powell also appeared to throw cold water on the idea of a quick economic recovery.

Although the U.S. economy has already lost about 20 million jobs since the onset of the coronavirus, Powell said he doesn't believe that unemployment has reached its peak.

"I would say that probably over the course of the next month or so, unemployment will peak" and will likely remain well above the record-high levels of earlier this year, as well as the levels of 2019 and 2018, Powell said. But he also said that returning to those historically high levels of unemployment is not out of the question.

"It'll take some time to get back to where we were," Powell said. "I have every reason to think we can get back where the economy should substantially recover once the virus is under control."

M&A

Goodwill charges emerge amid pandemic

By Jim Dobbs
May 13, 2020

Bankers face a difficult decision about the goodwill sitting on their balance sheets.

The coronavirus pandemic has punished the economy and the stock market, undermining the value of many banks' intangible assets. That convinced a handful of banks, including PacWest Bancorp, Umpqua Holdings and Cadence Bancorp., to take goodwill impairment charges in the first quarter.

Many more will likely do the same this summer, barring a sudden and unexpected reversal of fortune, sending goodwill impairment to levels that haven't been seen since the financial crisis, industry experts said.

The KBW Nasdaq Bank Index has fallen by more than 30% since early March.

"I think the likelihood of more impairments to come is pretty high," said Rick Childs, a partner at the accounting firm Crowe LLP.

Goodwill represents the premium an acquirer pays when buying an asset for more than its actual value. Accounting rules require the buyer to evaluate goodwill annually, though a triggering event such as fallout from the pandemic can also prompt a review.

Banks tend to take impairment charges after concluding that the fair value of an asset — or what it would reasonably fetch in a sale — has declined. Some banks opted to write off goodwill in the first quarter after the value of their stock fell below their tangible book value.

Accounting guidelines call for banks to book goodwill impairments after a "sustained" drop in share price, Childs said. While that leaves banks some leeway on timing, many will face pressure to proceed with charges if bank stocks remain under heavy pressure through June.

Some opted to take their lumps sooner rather than later.

PacWest, of Beverly Hills, Calif., reported a $1.4 billion loss in the first quarter after recording a $1.5 billion goodwill impairment charge. The $26 billion-asset company, a prolific acquirer after the financial crisis, also set aside $112 million to cover potential loan losses stemming from the pandemic.

PacWest faces "bleak economic forecasts," President and CEO Matt Wagner said in the company's quarterly release. He noted that the impairment was a noncash charge that had no impact on regulatory capital, cash flows or the bank's liquidity position.

Aggressive merger activity, and a consistently expanding economy, has created an abundance of goodwill on banks' balance sheets.

Goodwill and other intangible assets at banks increased by nearly 14% over the last five years, totaling $409 billion on Dec. 31, according to data compiled by the Federal Deposit Insurance Corp. It is the industry's largest amount of goodwill since mid-2009, just before the last series of goodwill impairment charges took place.

"It's an incredibly difficult time right now — you could see a lot of this happening again," said Charles Wendel, president of Financial Institutions Consulting.

Goodwill impairments not only make for ugly quarterly losses, Wendel said. They also serve as a leading indicator of profitability challenges, making it more difficult — and more expensive — for banks to raise capital.

Those factors, along with low stock prices, could hamstring acquisitive banks and stunt industrywide consolidation, Wendel said.

Cadence, which is based in Houston, provided a sobering economic outlook after it booked a $412.9 million goodwill impairment charge and a $399 million quarterly loss. The $17 billion-asset company is facing a slump in oil prices that hit its energy portfolio.

"We expect to be dealing with credit stress" resulting from COVID-19 "for a meaningful period of time, and that will be our primary focus," Chairman and CEO Paul Murphy Jr. said during a conference call to discuss quarterly results.

The experience of Umpqua, of Portland, Ore., demonstrates the fluid nature of the downturn.

The $27.5 billion-asset company did not initially book an impairment charge, though it noted in a release announcing a $28 million loss that a review was underway. It disclosed a $1.8 billion write-down two weeks later in its quarterly filing with the Securities and Exchange Commission.

Umpqua wrote off all the goodwill in its wholesale and retail banks, leaving it with $2.7 million tied to its wealth management business.

Market volatility, forecasts of prolonged low interest rates and a drop in Umpqua's stock price informed the assessment, Ron Farnsworth, the company's chief financial officer, told analysts during a quarterly call.

"It's something that just came on so fast late in the quarter," Farnsworth said.

DIGITAL BANKING

Banks tore up digital scripts once pandemic hit

By Allissa Kline
May 12, 2020

When U.S. Bancorp realized this spring that some customers were going to struggle to pay their mortgages, it moved quickly to design and deploy an online forbearance tool. Within a week of launching, the tool was used by more than 50% of customers seeking a temporary halt on payments.

How did the Minneapolis bank move so fast? Chief Digital Officer Derek White said it was "well down the path" of its current technology strategy when the coronavirus pandemic struck.

"The investments we've made in technology positioned us" to be able to react quickly to the situation, White said. "If anything was accelerated, it was the recognition that we need to design the experience around the end human user and understand what they want to be able to do with their money."

Industry experts say that banks with robust technology strategies are well ahead of the competition in the age of the coronavirus. For starters, many were able to transition large swaths of their workforce to remote setups in a matter of weeks, if not days. Then they moved quickly to install online application portals for small-business owners seeking emergency Paycheck Protection Program loans.

Now, several — from the megabank Wells Fargo to the community bank WSFS Financial in Wilmington, Del. — are referring back to their technology road maps, ramping up or refining services such as digital account openings, mobile check deposits and online mortgage deferment tools. Others are introducing digital treasury solutions and expanding onboarding capabilities for new and existing customers.

Brad Smith, managing director of the technology solutions team at Cornerstone Advisors Group, said technology projects with "low or questionable" returns on investments may be put on the back burner, but by most accounts banks are moving forward with — and in some cases expanding — their technology initiatives.

"Banks that have already invested in and transformed their digital channels are just killing it right now," Smith said. "Folks who were really smart to make big bets on digital and contact centers and already had those things in play have seen very little disruption" as a result of the pandemic and economic fallout.

For years, banks have been heavily investing in information technology. According to a June 2019 report from Accenture, the world's retail and commercial banks collectively spent about $1 trillion a year between 2015 and 2018 to reshape their IT capabilities.

Research from Cornerstone, a consulting firm for financial institutions, shows that banks spend roughly $2 million to $3 million on technology per billion dollars in assets, Smith said. That is up 2% since 2017, he said.

The end goal: to create better and faster products and services for customers, which in turn would drive customer growth and, ultimately, revenue growth. There are mixed feelings about whether these efforts are having a big top-line impact, but banks nonetheless continue to "digitize" all kinds of business lines.

In fact, going into 2020, the bulk of the technology spending was centered on digitization, including online account openings, Smith said. In general, banks were either replacing first-generation online account-opening models or adding that capability to their lineup for the very first time, he said.

Now, with so many people staying home and businesses shut down, it has become a critical service.

"That's just going gangbusters," Smith said. "And the vendors are now dealing with a backlog."

At the $12.3 billion-asset WSFS, online account openings are just one part of the bank's technology strategy, according to Chief Technology Officer Lisa Brubaker. The bank initially laid out a five-year, $32 million tech plan, but last year decided to speed up the pace and delivery of the project to three years.

It then spent much of 2019 laying the foundation for its digital overhaul. Today the bank is improving its online and mobile presence, building a digital toolset for employees to better serve clients and opening up its technology infrastructure to partner with fintech and other firms.

Those items were always part of the bank's plans, but now there is a new sense of urgency, Brubaker said.

"I think, if anything, the [crisis] underscores our need to stay the course" on technology, she said. "If we see a need to accelerate in some area, we will because we think it's important to stay ahead."

Wells Fargo, the third-largest bank in the nation, with assets of nearly $2 trillion, recently raised the limits for mobile deposits and wires, launched a new digital mortgage deferment tool and expanded its e-signature capabilities. In an email, Saul Van Beurden, the bank's head of technology, said more than 340,000 Wells customers have enrolled in digital banking in recent weeks, at the same time as there have been significant year-over-year increases in mobile deposits, online sessions and online wires.

Van Beurden said the bank will "keep on investing" in its digital initiatives.

The American Bankers Association, which represents banks of all sizes, could not say how much the banking industry spends on technology. But the organization does not expect a near-term reduction.

"I think technology spending will be an increasing priority at banks across the board," said Rob Morgan, the ABA's senior vice president of innovation and strategy. "That was the case before, and I think it will be the case even more so after. As the economy digitizes, banks will do the same."

At Citizens Financial Group, a "digital transformation" that has been underway for the better part of a year gave the Providence, R.I., company the ability to pivot quickly, Chief Information Officer Michael Ruttledge said. First it focused on transitioning about 70% of its employee base to a work-at-home model in three weeks and then it moved on to building out a PPP loan-processing portal, which it accomplished in just 48 hours.

Now it is turning its attention back to its technology guidebook and asking some key questions: What investments should it be making in technology, and what can it do to accelerate the process?

"I do think it's forcing us to step back and look at our investments and say, 'Are we making investments in the right places?' " Ruttledge said. "We're definitely asking, 'What should we be doing in the digital space?' particularly when you think about managing through a recession and taking care of our clients."

Brian Klock, a managing director who covers midsize banks at Keefe, Bruyette & Woods, said he does not expect banks in general to pull back on their technology budgets this year. Instead, like Citizens, they are likely to think hard about where those investments will be directed.

"I just think they want to make sure the dollars they've investing are working and funneled toward where demand is the highest right now," he said.

CORE SYSTEMS

Bisignano's priorities as Fiserv CEO: Bond with banks, invest in tech

By Penny Crosman
May 13, 2020

Frank Bisignano has his work cut out for him.

Bisignano is set to become CEO of Fiserv, a core banking software company with 12,000 financial institution customers, in July, replacing longtime CEO Jeff Yabuki. Bisignano had been chairman and CEO of First Data, which Fiserv acquired last July, and then became president and chief operating officer of the combined company.

In his new role, Bisignano will need to fulfill the $1.2 billion of cost cuts and $500 million in new revenue streams shareholders have been promised will come from the merger. He will also need to cross-sell Fiserv's bank customers on First Data's payment technology.

Bisignano has been in banking for a few decades. He ran Citigroup's Global Transaction Services unit in the early 2000s. He joined JPMorgan Chase in 2005, and became CEO of its mortgage banking unit in 2011 when it was still recovering from the financial crisis. He rose to co-COO and, before he left for First Data in 2013, was possibly in line to succeed JPMorgan CEO Jamie Dimon.

In an interview, Bisignano responded to questions about the merger, Fiserv's future and what the financial world will look like after the pandemic. He downplayed the pressure to cut costs, emphasizing his track record of producing revenue growth and the company's investments in technology like the point-of-sale system Clover that helps banks compete with Square and other fintechs.

Lately you have been leading Fiserv's coronavirus response. Can you tell me about some of the things you've been doing both internally, setting people up to work from home and such, and to help your clients?

FRANK BISIGNANO: At the end of the day, we're in business to serve our clients and our first and foremost concern is to protect our employees. Those are our two most important constituencies, along with our shareholders. Because we're a global company, we started our pandemic planning at the end of the fourth quarter and early stages of the first quarter. We have more than 40,000 people working remotely. We communicate to our clients every day. We invested heavily in our digital capability to deliver to them along with building a bunch of other tools, trying to help banks and merchants with the Paycheck Protection Program during this difficult time. We galvanized early, instituted our recovery plans, began our remote working and employees who needed to come into the office that needed our production facilities, we gave a 25% pay increase.

Was it a technology challenge to get everybody working from home, or did everyone pretty much have a laptop and the things that they needed to do that?

Getting 44,000 people working from home took a little work, but I wouldn't call it a technology challenge. We're fundamentally a technology company, and we had all the capabilities. I think the team came together. Sometimes in a difficult situation, things can go one way or the other. In our case it was selfless teamwork by all the team members.

Banks' role in the PPP has been pretty controversial. There's been a lot of criticism of banks giving loans to large companies and taking the most profitable route for themselves instead of the route that would help the people in the most difficulty. Do you have any thoughts on how that has gone down?

Our job was to be an enabler of small businesses and banks. We enhanced our technology, both at the point of sale, on our Clover platform, and throughout our community bank network. Our job was an enabler, and we were that for both small businesses directly and for our bank partners across the board. I think our bank clients are very pleased with how we performed.

What kinds of enhancements did you make to Clover?

The ability to interface so merchants could actually apply for PPP. And then we partnered with some [Small Business Administration] banks to get them the loans.

When you think about the Fiserv and First Data merger and what's happened in the wake of that, how do you feel that's been going and what outcomes are you most happy about?

Jeff [Yabuki] and I embarked on this journey months ago, and we've been working side by side. Our leadership teams and executive committees have operated together selflessly during this crisis. Jeff and I have worked very closely together every day, with the objective of having one team and enhancing what we do for clients and ultimately creating unique value for clients and shareholders. In terms of how that's all come together, we raised our revenue synergy targets because the team is working so well together and we're watching enhancements to service along with productivity while talking to our teammates as much as humanly possible. So I think it's going about as well as could be.

Fiserv has said it will obtain "cost synergies" from the First Data acquisition of $1.2 billion. How will you be able to cut $1.2 billion in this environment?

There's the infrastructure of the company — that's everything from data centers to real estate to technology infrastructure. There's procurement spending, which is where we spend with outside providers. That's a very significant number. Then there's corporate overhead. If you think about a merger of this size, that $1.2 billion is 12% of our expense base. And if you think about two big fintechs with corporate overhead, vendor spending and infrastructure, it has nothing to do with anything other than the opportunity to reduce that when we put the companies together.

How many layoffs have there been?

We've been fortunate. We use attrition as our friend. We've always had that philosophy. We also have a large contractor workforce. And we were able to convert some of the them and we've affected some of that in a large way. We've been working very hard on how we've taken expense out and not affecting people in a manner. We've had the benefit of having a lot of outside contractors and having a lot of outside spending. And that's really where our focus has been.

Are you saying there haven't been any layoffs?

We've reduced headcount in some sites where we shut down sites. And we've made changes, but this is not a number that we're counting, to be honest. We're working to get as much of the outside spend out of the company as humanly possible. And of course there's some redundancy when you take two corporate overheads and put them together. We also increased our revenue synergy, and we talked about $500 million in innovation investment spending. So we're reinvesting back in the business, and we're developing talents in the process.

Where is that additional revenue coming from?

It's coming from the combination of our bank partners and our Clover platform, our merchant business, how we take our capabilities and bring them together. We're an excellent partner with banks, and we're bringing them great merchant capabilities through Clover. We have digital innovation in disbursement and areas like how we deliver payments. So payment innovation is at the top of the list.

It probably wouldn't surprise you to hear that when I talk to bankers, they sometimes express frustration with some of the traditional core vendors. Some of them have had these cores for decades and they find when they want to adopt emerging technologies, it's tough. It just doesn't always work. Some of them are thinking about going to a cloud-based core vendor and a pay-as-you-go pricing model. What is your thinking about that?

I have a lot of thoughts about it, so I'll try to synthesize it down for you. We are a strategic partner to our clients, and we're going to continue to work on our engagement model, our service model, our innovation model and how we deliver value-added services that integrate well. We have a privileged position with our clients where we make them the centerpiece of our business. We're going to continue doing that, and we're going to continue working on how to deliver best-in-class service and products to them. The plethora of opportunity we have to help our clients serve their clients better is a very privileged position. This company was built on that, it has a long legacy of that and I believe we will continue exactly in that innovation space to be the best innovator for our clients. And that's why you see Clover and the banking relationships coming together in such a good way.

When you think about innovation, do you think mostly about payments or are there other types of innovation that you're thinking of expanding into as well?

I think innovation is transformational. It's transformational payments, it's transformational digital, it's how do we bring all the data we have inside of this company in a manner that helps clients. If you look at our earnings release, you'll see that we talked about using our SpendTrend product and distributing it to our clients, banks, governments and businesses, small and large. That capability to help them in their decisioning causes us to believe we'll continue to differentiate in the client's office.

What do you think the banking and payments world could look like when things theoretically go back to normal? Are there preferences that are permanently changed, or do you think everything will go back to normal in terms of what consumers want, what businesses want, what bankers need to provide?

I think the speed at which digital is changing things is going to increase — it's increased right now. And I think we're going to define a new normal. Who knows what we thought normal exactly was, because in transformational businesses, you're always recreating a norm. And now we've had an event that has caused us to see many different things. What you can count on from Fiserv is a value in moving information and payments at the speed of light will be what continues through as we go on this journey. We will be part of the digital transformation of our clients.

Do you see any new opportunities for Fiserv when the pandemic is over?

That's what our innovation spending is about. It's about investing in the future, investing in our clients, investing where we believe our clients can benefit most from a highly valued product set. It's the issues that we've talked about multiple times, how are we going to help our clients help their clients, whether that's at the point of sale, in an e-commerce fashion, in a software fashion, in a banking remote deposit fashion. All of those are going to expedite and we're heavily invested in that and we'll continue to heavily invest.

What about things like open banking, virtual assistants and robotic process automation, some of the current newer technologies that people are thinking about?

Virtual assistants have been spread across our whole company. And it's one of these things that are enhancing value and ultimately will bring synergistic revenue opportunities because of the innovative technology. We used RPA and robotics to build engines to help move many things during this pandemic. So we've been heavily invested in RPA. We're heavily invested in artificial intelligence, and we're going to continue to use them to help our clients run their business.

You've been called a Mr. Fix It and a turnaround person in some of your roles at JPMorgan Chase, where you had to relocate a large team when the World Trade Center collapsed on Sept. 11 and where the mortgage business later had to be revived, and at First Data. What are the keys to turning a bad situation into a good one?

My career has been about growing. It was about growing the top line. It was about growing talent. It was about building a team. It was about, how we're going to have market-leading positions through technology, innovation and service. First Data had a bunch of problems and a bunch of CEOs, but ultimately what we did was build technology, grow the top line and delight clients. If you go through my career, that's what you would see. Sometimes it was a problem situation, but many times it was just building a business that continued sustained growth. You would see continued revenue growth, continued business building and strategic investing in innovation. Sometimes it was in a situation that needed more help than others.

Sept. 11 was a crisis. I was a role player and I happened to have 15,000 people. At the time I thought it would be one of the most unfortunate events in my life. Maybe it was. I later got throat cancer, which I thought was a byproduct of that. We're in a pandemic now, and you could say nothing could be worse than what we're seeing for the safety and health of people right now. There are going to be these situations. You need to be able to grow business while servicing clients while delivering shareholder value while building a great team. And we have a great team at Fiserv.

PAYCHECK PROTECTION PROGRAM

SBA backs off legal threat against firms that didn't need PPP loans

By Bloomberg News
May 13, 2020

The Trump administration said firms that took loans that they didn't need from a small-business aid program will be allowed to repay the money without legal consequences, reversing an earlier threat that the government could pursue them criminally.

New guidance issued Wednesday for the Paycheck Protection Program by the Small Business Administration and the Treasury Department also said that companies that took loans of less than $2 million will automatically be determined to have done so in good faith because they're less likely to have access to other resources.

The SBA will review all loans above $2 million to check whether firms properly certified they needed the money. If it determines the company shouldn't have gotten the money, the loan won't be forgiven and if the borrower returns it, no further action will be taken, according to the new guidance.

Assuming that loans of less than $2 million were taken in good faith will allow the SBA to focus its resources on reviewing larger loans given the massive size of the program, the agencies said.

Last month, after a backlash after large firms swooped in and collected millions from the PPP — which was intended to cast a lifeline to small firms that didn't have access to capital markets —Treasury Secretary Steven Mnuchin said that firms could face criminal charges for taking loans they didn't need.

Meanwhile, borrowers who commit fraud in taking relief loans are already being prosecuted. The Justice Department last week brought the first criminal case related to the program when it charged two New England businessmen with fraud and alleged that their applications falsely claimed employees they don't have.

The Paycheck Protection Program allows loans of as much as $10 million that can be become grants if proceeds are spent mostly on payroll for two months after they are received. It's meant to keep workers employed and firms ready to reopen when state stay-at-home orders are lifted.

After organizations such as Shake Shack and the Los Angeles Lakers got loans at the expense of mom-and-pop shops, the SBA and Treasury issued guidance April 23 saying companies with "substantial market value and access to capital markets" would be unlikely to qualify. Borrowers had to certify on their applications that "current economic uncertainty makes this loan request necessary to support the ongoing operations" of the business.

Companies had been given until May 7, later extended to Thursday, to return loans without any penalty. (Shake Shack and the Lakers returned the money.) But there was confusion about eligibility, and some firms said they returned their loans "out of an abundance of caution" even if they believed they qualified for it.

The SBA and Treasury haven't disclosed how many companies have returned or canceled loans and in what amounts. Public companies reported returning 61 loans worth $411 million as of Wednesday morning, according to data compiled by FactSquared.

SMALL BUSINESS LENDING

Community banks call on Congress to rein in credit union regulator

By John Reosti
May 13, 2020

Bankers are stepping up their fight over the National Credit Union Administration's change to how it calculates the low-income designation for credit unions.

Last week the credit union regulator said it would include members who serve in the military when determining an institution's low-income status. A credit union can be designated as low income if its membership meets certain criteria, and the status comes with some advantages, such as being exempt from the member business lending cap.

Bankers have slammed the move, arguing that it's part of a broader pattern of credit unions and their regulator using the coronavirus as cover to overreach on regulatory changes.

"A pandemic and economic crisis should not be an opportunity for credit union powers expansion that does nothing to alleviate the crisis," Rebeca Romero Rainey, president and CEO of the Independent Community Bankers of America, wrote in a letter to members of the Senate Banking Committee.

Quickly linking the decision on service members to the wider MBL issue, Rainey claimed in the May 11 letter that weakening current restrictions on credit union business lending "would exclusively benefit the largest, growth-obsessed credit unions."

More commercial lending by big credit unions would serve to increase the industry's risk profile to the detriment of smaller, more traditional institutions, she wrote, adding, "It warrants mentioning that these very credit unions were shut out of the comment process by their own regulator."

Bankers are objecting more strenuously to the way the NCUA arrived at its decision. Aaron Stetter, the ICBA's executive vice president of policy and political operations, labeled the decision "executive fiat" in an interview Monday. He wouldn't rule out possible litigation over the change, though the group is waiting to see how Congress reacts first.

The NCUA "made an administrative decision benefitting their largest member without any public input," Stetter said. Bankers weren't given a say, to be sure, but the agency "silenced its own industry, as well," Stetter said. "Other credit unions weren't allowed to weigh in on this."

According to Stetter, counting service members as low-income individuals for the purposes the low-income designation makes it inevitable that the $126 billion-asset Navy Federal Credit Union will soon qualify.

"What better example of being a captive regulator than to pave the way for Navy Federal to go out and do this," Stetter said.

Navy Federal and the NCUA both declined to comment.

A 'technical correction'?

Besides unrestricted member business lending, low-income designated credit unions have the ability to accept nonmember deposits and the authority to issue subordinated debt. About half of all credit unions had a low-income designation at the end of 2019, according to NCUA data. The number has more than doubled over the last decade.

Defense Credit Union Council President and CEO Anthony Hernandez said the change amounts to a "technical correction," adding it was within NCUA's discretion to make.

According to Hernandez, the regulation already allows college students to be counted toward the low-income designation. Adding more military members, who frequently fall below the 80% median-income threshold, is hardly a stretch, Hernandez said.

A credit union qualifies for low-income designation if a majority of its members earn 80% or less than the applicable median-family-income or total-median-income.

Specifically, the rule allows all service members to be counted in low-income designation calculations. Previously, only those with physical street addresses could be counted.

"I don't think anything untoward was done," Hernandez said. "Frankly, I'm surprised the rule didn't already address this issue."

Stetter suggested that the NCUA's service-member decision is part of a wider trend of the credit union industry and its regulator using the coronavirus pandemic to dismantle the longstanding congressionally mandated restrictions that limit member business lending by credit unions.

Board members J. Mark McWatters and Todd Harper have called for either increasing or eliminating outright the 12.25% cap on member business lending that applies to non-low-income-designated credit unions. Credit union allies in Congress recently introduced bills that would suspend the cap for a year or raise to 20%.

Michael Emancipator, the community banker group's vice president and regulatory counsel, accused the NCUA of bypassing the Administrative Procedure Act when it announced its service member decision.

"In the past, at least they've paid lip service to the facial requirements of the APA," Emancipator said.

The American Bankers Association, too, promised to fight any bid to weaken limits on credit union member business lending. James Ballentine, the ABA's executive vice president for congressional relations and political affairs, said there's little evidence credit unions need more authority to lend to businesses.

"They have plenty of capacity now," Ballentine argued in a recent interview. "There are only 30 that are near the cap. Using this crisis to expand their business powers doesn't make sense."

"We'll actively oppose any effort to increase the member business loan cap," Ballentine added.

CFPB

CFPB gives credit card issuers flexibility on billing disputes

By Kate Berry
May 13, 2020

The Consumer Financial Protection Bureau issued guidance meant to enable credit card companies to resolve billing disputes tied to businesses affected by the coronavirus pandemic.

Credit card issuers that make a good-faith effort to resolve billing disputes will not receive an enforcement action or be cited in a supervisory exam, the CFPB said Wednesday.

The agency said it wanted to inform creditors of its "flexible supervisory and enforcement approach" as many small businesses hit by the economic fallout of the virus have struggled to keep up with the volume of billing disputes brought by consumers.

Credit card issuers are typically required to acknowledge a merchant billing error notice from a consumer within 30 days. But the guidance means issuers failing to meet that deadline will not be cited by the CFPB.

Lenders generally must investigate and resolve billing errors within two billing cycles but no later than 90 days, according to Regulation Z, which implements the Truth in Lending Act.

The CFPB noted that consumers have been facing long hold times trying to reach both merchants and credit card time, some of which may be closed or operating with reduced staff.

The CFPB said merchants may be having trouble responding to creditors' inquiries, making it hard for creditors to resolve billing disputes swiftly and accurately.

GSEs

FHFA extends Fannie and Freddie mortgage payment deferral program

By Paul Centopani
May 13, 2020

To help keep borrowers with coronavirus-related hardships current on their mortgage payments, the Federal Housing Finance Agency announced a new deferral option starting July 1.

Once able, eligible homeowners can return to paying their prepandemic monthly totals and add up to 12 months of missed payments to the end of their loan term. The deferred sums to be repaid include principal, interest and escrow advances. Borrowers will not have to make the missed payments in a lump sum.

"For homeowners in forbearance due to COVID-19, payment deferral allows them to make up missed forbearance payments when they sell their home or refinance," FHFA Director Mark Calabria said in a press release. “This new forbearance repayment solution responsibly simplifies options for homeowners while providing an additional tool for mortgage servicers. Borrowers who can pay their mortgage should, because missed payments remain an obligation that will ultimately have to be repaid.”

In April, state attorneys general urged the FHFA to expand payment help options. Distressed borrowers bombarded the Consumer Financial Protection Bureau with a record number of complaints during the month in regards to unwanted forbearance plans and refusal of deferments. A recent report showed servicers could have to absorb anywhere from $3 billion to $13 billion per month in the case of payment suspensions.

Fannie Mae and Freddie Mac announced assistance plans shortly after the economic impacts of the virus took hold. However, that was before everyone realized the true vastness of the pandemic.

“Our main focus continues to be finding new and innovative ways to help borrowers and their families during this pandemic,” said Donna Corley, executive vice president and head of Freddie Mac’s single-family business. “Our payment deferral solution adds another tool to our toolbox to help homeowners pick up where they left off once they’ve recovered from a short-term financial hardship.”

Of course, this is all contingent on borrowers’ meeting criteria to qualify for the COVID-19 repayment plans through servicer evaluation.

Dan Berger, president and CEO of the National Association of Federally-Insured Credit Unions, said the new program gives homeowners financial flexibility.

“This policy change would also allow credit unions to preserve liquidity to lend to those in need, instead of being required to buy back loans from the GSEs,” he said. “NAFCU welcomes this policy change as it helps homeowners and preserves the safety and soundness of credit unions and the mortgage industry.”

PAYTHINK

Fintechs must quickly adjust to sustainability and contact

By Pamela Novoa Ralli
May 14, 2020

In the current state of things, no one has a clear understanding of how long coronavirus and its effects will last. This includes economic repercussions, the ways in which companies need to alter their practices and how consumers interact with both corporations and each other. Nearly all interactions will change in the coming months; in fact, many already have — including within the payments and banking industries.

Based on the current environment and the macro developments in the commercial landscape of the U.S. and U.K., the following payments and banking trends are predicted:

Reduction of cash. The World Health Organization is reportedly encouraging people to use as many digital payment options as possible in the wake of the pandemic. Physical means of payments, such as cash and checks, have experienced a significant reduction in both usage and acceptance. During March, cash usage was halved, according to Links, which operates the U.K.’s largest ATM network. Now is the time to promote and design digitization programs for commerce and the economy.

Contactless commerce. The fear of contact has increased the use of contactless payments. Cashiers are being trained not to take cards from customers and to promote the insertion of cards into readers by shoppers as well as talking to customers about in-app purchase while in the store. The impact of local shopkeepers who actively encourage customers to use contactless payments will convert some of the more reluctant users.

Access to digital payments and banking tools. The economic downturn is bringing to the surface a longstanding divide over the cost and accessibility of digital payments. Not everyone has the same level of access to the necessary technologies and tools to achieve full digitalization of their business. Businesses without access to digital payments lose out more as remote buying increases. Now is the time to design setups where all businesses and consumers, irrespective of their demographic, economic situation and education, have access to engage in the new-normal economy.

Security front and center. As the economy starts rebuilding, businesses will want to hurry to onboard new clients, new suppliers and new employees; this will also occur while most businesses are understaffed and their back offices are underinvested. Data security, identity and transaction fraud are likely to experience significant growth during this period, and we expect security services to become critical for the future economic rehabilitation.

A focus on more sustainable business models. The magnitude of COVID-19 is still unclear, but it’s apparent the crisis will continue to have a material impact on M&A activity worldwide; investors are highly likely to lean away from the relatively riskier ventures of investing in startups. Fintech companies should prepare for a less funding-friendly environment in 2020. In this environment, we expect fintech companies to shift focus to a more sustainable business model that isn’t dependent on the constant inflow of external investor money.

Collaboration between big and small. The cashflow and profitability crunch, propelled by the economic downturn, will likely lead to significant changes in the fintech and banking industries. In the post-COVID-19 world, banks will be forced to organize themselves to meet evolving needs of small business and/or retail businesses, particularly as it relates to the rising demand for new digital services. Banks will consider structural moves on the use of cloud-based infrastructure, automation and analysis-driven decisions to reimagine the digital customer experience.

Fintech companies, in turn, will look to take advantage of that new revenue and customer pool. The data interoperability involved is dependent on a new model of collaboration between the financial services companies, fintech companies and regulators. Banks and fintech companies will have to play well together support this new landscape.

This article originally appeared in PaymentsSource.

BANKTHINK

Pandemic makes CRA reform more urgent, not less

By Kenneth H. Thomas
May 13, 2020

The proposal to modernize the Community Reinvestment Act would help low- and moderate-income neighborhoods in New York and our other major cities recover from the coronavirus pandemic.

Unfortunately, the proposal was misunderstood as doing the opposite by a New York congressman, the Consumer Bankers Association and other trade groups and community leaders in the roughly 2,000 comments recently submitted as part of the rulemaking process.

Everyone agreed that the 1977 CRA should be modernized to account for digital banking. The proposed reforms adopted an innovative solution requiring branchless banks to reinvest some of their billions of internet deposits back into the big cities sourcing them, rather than benefiting their credit card friendly "hot spot" home-office cities in Delaware, South Dakota and Utah.

Critics of the proposal wrongly assume the reinvested internet deposits will benefit the affluent people sourcing them in New York and other big cities. The reform, however, would require some of the internet deposits coming from the affluent people and neighborhoods of New York to be reinvested back into community development loans, investments and services benefiting low- and moderate-income (LMI) people and neighborhoods there.

Consider it a CRA "Robin Hood" proposal, where the CRA benefits of deposits from the rich are being used to help the poor. This proposal is consistent with CRA's intent and, in fact, its middle name of "reinvestment."

With this in mind, consider how those internet deposits would benefit the most distressed communities and people in New York, including first responders, hospital workers and other front-line heroes in this pandemic.Furthermore, under this flexible proposal, those same branchless banks, once they have met their LMI reinvestment obligations in New York, have the option of providing CRA benefits to other distressed communities, rural areas and Indian country.

The proposal, however, would expand the original CRA modernization mission, which was remedied with this reinvestment rule, to a total overhaul of the law. That is why most community groups and banks criticized the proposal for not only being unnecessarily complex and costly, but also failing to account for banks of different types and sizes.

It's also a reason that the Federal Reserve did not join the Office of the Comptroller of the Currency and Federal Deposit Insurance Corp. in their joint notice of proposed rulemaking.

The current regulation already allows for six different CRA exam procedures for the nation's more than 5,000 banks. There is a four-ratio streamlined lending test for thousands of small banks; a dual-lending and community-development test for intermediate-sized banks; and separate lending, investment and service tests for hundreds of large banks.

The current CRA requirements also have a straightforward community-development test for limited-purpose and wholesale banks of any size, in addition to an effectively self-regulating "strategic plan" option for any size or type of bank.

The proposal would keep the latter option but eliminate intermediate, limited-purpose and wholesale bank exams. The small bank definition would increase by asset size, and the remaining large banks would be subject to the new formulaic approach.

The Independent Community Bankers of America asked regulators to increase the "small bank" definition from the current $326 million to $5 billion, which is 10 times higher than the $500 million ceiling regulators proposed.

While their proposal would exempt about 600 banks, the ICBA proposal would exempt roughly 1,200 more intermediate and large banks. These exempt banks would no longer be required to provide upward of $50 billion of annual CRA benefits to their local communities, based on past estimates of CRA benefits.

As a CRA bank consultant and having helped work on the 1995 reforms with the OCC, there is a better option called the "75% solution" to CRA reform that should satisfy community groups, the industry and even the regulators.

It provides 75% of all the benefits envisioned by the proposal without incurring any new regulatory burden on 99% of banks, which would continue under the six existing exam procedures. The only banks subject to the proposal would be the 1% of "very large banks," namely 43 banks with $50 billion or more of assets, plus branchless banks subject to the proposed reinvestment rule. Those two groups, representing 75% of bank assets, would have the resources to comply with the new requirements.

The costs and benefits of such a proposal on those very large banks will be evaluated after three years — roughly one examination cycle — to determine the feasibility of applying it to other banks, or reverting to the existing requirements.

Community groups under this proposed concept would continue to benefit from the CRA efforts of the 99% of other banks in their local communities, and should not be concerned with the additional regulatory burden on the too-big-to-fail banks.

In addition, most examiners will not need retraining, since the largest banks already have separate exam teams. The Fed should be willing to accept this compromise, since it is the primary regulator for only 10 of the 43 impacted banks, and just four would have retail operations impacted by the new requirements.

The banking industry should likewise be supportive of this proposal, since 99% of banks continue the status quo, which has a 98% pass rate and a relatively low regulatory burden, ranking just sixth in compliance costs. Also, there would be no disruption to their community development efforts, as there would be under the current regulatory proposal.

Most significantly, with the CRA reform debate off the table, community groups, regulators and especially banks would be able to focus on the critical task of helping communities recover from the coronavirus pandemic, which must remain a top priority.

Kenneth H. Thomas, president of Miami-based Community Development Fund Advisors, was a lecturer in finance at the University of Pennsylvania's Wharton School for over 40 years. ❑