WEBINAR

Pandemic Preparedness and COVID-19

Presenter: Elizabeth K. Madlem

Associate General Counsel

Agenda

- Disclaimer
- Regulatory Expectations on Financial Institutions
- Pandemic Preparedness
- Assessments to Identify, Quantify and Manage Risks
- Impacts to Contractual Requirements
- Loan Modifications
- Other Considerations

Disclaimer

Today's webinar focuses on the general risks, issues and anticipated responses financial institutions should be considering and addressing during this pandemic accurate as of March 30, 2020.

It is not intended to be all-encompassing.

Definitive guidance should always be coming from your governing regulatory agency, along with the Centers for Disease Control and Prevention, World Health Organization, the U.S. Department of Homeland Security, and other governmental entities.

Refer to your Desktop Manual for a list of additional resources.

Regulatory Expectations on Financial Institutions

- Demonstrated pandemic preparedness plans in place
  - Activated and working

- Topics Include:
  - Market volatility
  - Technology readiness
  - Operations (including products, third parties and employees/remote working)
  - Customer/Investor protections
  - Regulatory compliance
  - Enterprise risk management
  - Supply chain and third-party provider management
  - Contingency planning
  - Cybersecurity services (including fraud and data privacy)
  - Oversight/Surveillance controls
  - Financial impact analysis and capital management
  - Internal Audit
  - Tax efficiency
  - Insurance claims
  - Cost optimization
  - New product development

Regulatory End Goal:
Minimizing adverse impacts to customers and investors through forbearance and disclosure

Key Risks

- Constraints on staffing
- Technology limitations/overloading
- Operations/Facilities
- Supervision of remote employees/locations
- Call center capacity
- Customer/Investor forbearance
- Cybersecurity/fraud threats
- Market volatility
- Reputational Risks

Pandemic Preparedness: Pandemic Planning Policy (PPP)

- Avoid or minimize financial loss to the bank
- Avoid or minimize loss of life or injury
- Continue to serve customers and financial market participants by resuming business operations and activities
- Mitigate the negative effects disruptions can have on a bank's strategic plans, reputation, operations, liquidity, credit quality and market position
- Maintain ability to remain in compliance with applicable laws and regulations

PPP and Coronavirus

March 6, 2020:

FFIEC released a 10-page interagency statement updating the 2007 guidance on how financial institutions should address pandemics in their business continuity plans

Interagency Statement on Pandemic Planning here.

Business Continuity Planning vs. Pandemic Planning

BCP

- Consider effects of natural or man-made disasters with short duration or limited scope
- Malicious activity, technical disruptions, natural/man-made disasters
- Only affect a specific geographic area, facility or system
- Mitigated by focusing on resiliency and recovery considerations

PP

- Undefinable impact due to unknown scale and duration
- No individual or organization is safe from adverse effects
- Pandemics occur in multiple waves
- Impact on delivery of FI's critical financial services

Both traditional business continuity planning and pandemic planning require management to follow a cyclical process of **Planning, Preparing, Responding and Recovering**.

Pandemic Planning requires additional actions to **Identify and Prioritize** essential functions, employees and resources within the institution and across other business sectors.

Not just an Information Technology issue!
PP is an Enterprise-wide Risk

Interagency Update Takeaways - 1

1. **Preventative Program**
   - Reduce likelihood operations will be significantly affected by a pandemic
   - Monitor for potential outbreaks
   - Educate employees (and community at large)
   - Communicate and coordinate with critical service providers/suppliers
   - Provide appropriate hygiene training and tools to employees

Interagency Update Takeaways - 2

2. Documented Strategy

- Develop a strategy for recovering from a pandemic wave
- Scaling of institution's pandemic efforts to a particular stage of pandemic outbreak (i.e. 6 intervals per CDC here)
- Detailed recovery plan from pandemic wave and preparations for following waves
- Outline plan for re-entering personnel into the workplace

Interagency Update Takeaways - 3

3. Comprehensive framework of facilities, systems or procedures

- Define critical operations and employees
- Address staffing and employee protocols addressing any anticipated prolonged periods of staff unavailability
- Considering minimizing staff contact
  - Social distancing
  - Telecommuting/working remotely
  - Redirecting customers from branch to electronic banking services
  - Conducting operations from alternative sites
- Considerations of customer procedures and impact for restrictions of access to facilities
- Systems checks for increased reliance and frequency for online banking, telephone banking, ATMs, and call support services
- Procedures for response to public health and other government authorities mandates that may affect critical business functions

Interagency Update Takeaways - 4

4. Testing Program

- Implement a testing program that ensures pandemic planning practices and capabilities are effective and allow critical operations to continue
- Enterprise-wide in scope with critical functions defined

Interagency Update Takeaways - 5

5. Oversight program to ensure ongoing review and updates

- Steps to update policies, procedures and standards to include up-to-date, relevant information
- Scope includes governmental sources and institution's monitoring program

Board and Senior Management Responsibilities

- Involve senior business management from all functional, business and product areas including:
  - Administrative
  - human resources
  - Legal
  - IT/IS support functions
  - Key product lines
- Board of Directors oversee development of pandemic plan
  - Approves written plan
  - Ensures senior management is investing sufficient resources into planning, monitoring and testing final plan
- Senior Management develops pandemic plan and translates into specific policies, processes and procedures
  - Communicates plan throughout institution to ensure consistency in understanding of key elements and roles and responsibilities
  - Ensures plan is regularly tested and remains relevant

Assessments to Identify, Quantify and Manage Risk

Incorporate Pandemic Risks into Business Impact Analysis

- Define appropriate known risks/key risk indicators
- Analyze loan exposure data/performance indicators
- Define and refine priorities
- Identify other considerations (concentration risks, upstream-downstream)
- Policy Implications
  - Managing concentration risks:
    - Identifying risks
    - Assess limits and determine appropriate risk pricing of loan segments while adjusting risk appetite statements
    - Refine grading models providing updates for dual risk rating systems
    - Capital planning and stress-testing (reevaluating economic capital, regulatory capital requirements, and ALLL/CECL)
    - Business development
      - Identifying safe and sound lending opportunities under times of stress

Impacts to Contractual Requirements

Certain legal doctrines can excuse delay in performance or non-performance of contractual obligations—vary among jurisdictions (federal, state, local or foreign)

- *Force majeure*
- Impracticability/Impossibility of performance
- Frustration of commercial purpose

Interagency Statement on Loan Modifications by Financial Institutions Working with Customers Affected by the Coronavirus

- Encourages financial institutions to work constructively with affected borrowers
- Will not criticize institutions for prudent loan modifications
- Will no direct supervised institutions to automatically categorize COVID-19-related loan modifications as TDRs
- Confirmed with FASB that short-term modifications made on a good faith basis to borrowers who were current prior to any relief are not TDRs
- Modification efforts for borrowers of one-to-four family residential mortgages where loans are prudently underwritten and not past due or carried in nonaccrual status do not result in loans being considered restructured or modified for purpose of respective risk-based capital rules
- Prudent loan modification programs are viewed as positive actions to effectively manage or mitigate adverse impacts and lead to improved loan performance and reduced credit risk

Loan Modifications

- Past due status should be based on the due date stipulated in the legal loan documents as modified within such modification program
- Interagency statement reminds institutions that loans that have been restructured will continue to be eligible as collateral at the FRB's discount window based on the usual criteria

Interagency Statement on Loan Modifications by Financial Institutions Working with Customers Affected by the Coronavirus

Frequently Asked Questions for Financial Institutions Affected by the Coronavirus Disease 2019 (Referred to as COVID-19) – Updated March 19, 2020

FIL-50-2013, Interagency Supervisory Guidance Addressing Certain Issues Related to Troubled Debt Restructurings

Other Considerations - 1

Managing Bank's Communications in Social Media

- Turn off or pause "robots"
- Focus on human interaction and oversight
- Keep communications proactive, simple, direct, honest and empathetic
- Reassess what is in the hopper (removing automated outreach for events, meetings, etc.)
- Remind people of all digital banking options available—online banking, online bill pay, mobile banking, mobile deposits, Zelle, etc.
- Warn and educate consumers on financial scams
- Inform public about steps to alter operations (closure of lobbies or entire branches, extended call center hours, etc.)
- Amplify reach of helpful information from credible sources

Other Considerations - 2

Government & Central Bank Fiscal and Monetary Stimulus Measures (1)

U.S. Federal Reserve has taken a number of significant measures to provide monetary stimulus:

- March 3—unscheduled cut to the Fed Funds Rate
  - Slashed rates by 0.5% (largest cut since 2008 financial crisis)
- March 12—Fed massively expanded reserve repo operations, adding $1.5 trillion of liquidity to the banking system
  - Extended the amount of short term loans to banks to keep money markets stable and allow banks to have more cash on hand
- March 15—Fed set out several pieces of monetary stimulus
  - Cut interest rates by a full percentage point, down to a range of 0.00% to 0.25%
  - Restarted quantitative easing with purchase of $500 billion in treasurys and $200 billion in mortgage-backed securities
  - Lowered the interest rate on the discount window by 1.5% to 0.25% (another way Feds lend to banks)
  - Fed lowered reserve requirements to zero effective March 26th (loosen credit markets)
  - Encouraged banks to use their capital and liquidity buffers to lend (funds kept in reserve for tough times)

Other Considerations - 3

Government & Central Bank Fiscal and Monetary Stimulus Measures (2)

- March 16- Fed Reserve increased reverse repo operations by another $500 billion
- March 17- Fed introduced two new programs to help preserve market liquidity:
  - Commercial Paper Funding Facility (CPFF)—allows Fed to create a corporation which can purchase commercial paper, short-term, unsecured loans made by businesses for every day expenses
  - Primary Dealer Credit Facility (PDCF)—Started March 20 offering short-term loans to banks secured by collateral such as municipal bonds or investment-grade corporate debt; will run for at least 6 months
- March 18- Fed announced Money Market Mutual Fund Liquidity Facility (MMLF) to lend money to banks so they can purchase assets from money market funds (like CPFF)
  - Lending under the program will not effect bank capital requirements
  - Scheduled to run until end of September

Other Considerations

Government & Central Bank Fiscal and Monetary Stimulus Measures (3)

- March 23- Fed Reserve released another raft of monetary stimulus including:
  - Expanding its asset purchases of both treasuries and mortgage backed securities by an additional $625 billion
  - Expanded the scope of what mortgage-backed securities it will purchase, now including agency commercial mortgage-backed securities
  - Established the Primary Market Corporate Credit Facility (PMCCF) to buy bonds and loans banks give to large businesses
  - Established the Secondary Market Corporate Credit Facility (SMCCF) to purchase bonds and ETFs to provide liquidity for the corporate bond market

Other Considerations

Government & Central Bank Fiscal and Monetary Stimulus Measures (4)

- Established the Term Asset-Backed Securities Loan Facility (TALF) to purchase asset-backed securities backed by things such as auto-loans, student loans, or small business loans
- Expanded MMLF to include more different types of money market funds
- Expanded CPFF to include a wider variety of commercial paper assets and a reduction in interest rates for loans from CPFF
- Will be soon rolling out the "Main Street Business Lending Program" to support small and medium businesses

Each will run until September 30, 2020 unless extended

Other Considerations

CARES Act and Paycheck Protection Program (PPP)

- On March 27, 2020, the President signed into law the Coronavirus Aid, Relief, and Economic Security Act (CARES Act) which provides a **$2 trillion stimulus package** in response to the COVID-19 pandemic.

- Section 1102 of the Act creates a new “Paycheck Protection Program” (PPP) to be added to the existing Small Business Act. The Program authorizes the Small Business Administration (SBA) to 100% guarantee all PPP loans. The SBA is required to provide guidance to PPP lenders within 30 days of enactment of the CARES Act.

Other Considerations

Small Business Relief Programs

- FDIC is encouraging banks to work with customers to provide coronavirus-related assistance related to both personal *and* business finances
- U.S. Small Business Administration (SBA) coronavirus resource page offers guidance to small business owners

Other Considerations

Small Dollar Lending (1)

- Statement issued March 26th, 2020 to encourage financial institutions to offer responsible small-dollar loans to both consumers and small businesses.
- Financial institutions currently are allowed to make responsible small-dollar loans—such loans are offered through a variety of loan structures that may include open-end lines of credit, closed-end installment loans, or appropriately structured single payment loans.
- For borrowers who experience unexpected circumstances and cannot repay the loan as structured, financial institutions are encouraged to consider workout strategies designed to help enable borrowers to repay the principal of the loan while mitigating the need to re-borrow.

Other Considerations

Small Dollar Lending

- For all products, financial institutions should offer loans in a manner that is consistent with safe and sound practices, providing fair treatment of consumers, and comply with applicable statutes and regulations, including consumer protection laws.
- Await additional Agency guidance
- Beware of Consumer Advocacy backlash—request for 36% cap

Other Considerations

Labor Laws and Considerations

- DHS/CISA guidance deemed certain workers within the financial services sector "Essential Critical Infrastructure Workers:"
  - Workers who are needed to process and maintain systems for processing financial transactions and services (e.g., payment, clearing, and settlement; wholesale funding; insurance services; and capital markets activities)
  - Workers who are needed to provide consumer access to banking and lending services, including ATMs, and to move currency and payments (e.g., armored cash carriers)
  - Workers who support financial operations, such as those staffing data and security operations centers

- Fair Labor Standards Act (FLSA) and state law requirements
  - Helpful FAQ here.

Questions?

Thank you for your participation!

We hope you found value in today's presentation.

Review your Manual for additional guidance, comments, tools and FAQs.

If you have any additional questions,

contact Compliance Alliance at 888-353-3933 or elizabethm@compliancealliance.com