Ask the Regulators®

An Overview of the Emergency Capital Investment Program

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Presenters: Christopher Weaver, David Alexander

Carl White: Good afternoon, everyone, and welcome to another session of Ask the Regulators®. My name is Carl White; I'm senior vice president over Supervision at the Federal Reserve Bank of St. Louis. Today the Federal Reserve System, the FDIC, the OCC, and the NCUA are all coming together for a session with the U.S. Department of Treasury to discuss an overview of the Emergency Capital Investment Program, otherwise known as ECIP.

Some logistics before we get started: The best experience is if you're joining us through the webinar and through the webinar audio. So some of you who are calling in via phone and then maybe watching the webinar on a screen, you might notice a slight delay. One suggestion is to download the presentation and then go through it as you hear the speakers advance the slides. And we'll be very clear on which slide that we're on.

Today we are joined by Christopher Weaver. He is the interim director of the Emergency Capital Investment Program at the U.S. Treasury. We're also joined by David Alexander in the Office of the General Counsel at the U.S. Treasury. And then also on the line to help answer questions are Thomas Fay, senior capital market specialist with the NCUA; Betty Rudolph, national director for Minority and Community Development Banking at the FDIC; and Art Lindo, deputy director for policy, Division of Supervision and Regulation at the Federal Reserve Board of Governors.

So before we turn it over to our speakers, I do need to cover just a few call logistics on Slide 2. First of all, as always, we do record every Ask the Regulators® call, and you get the recording using the exact same link that you used today, or you can just go to our website at www.askthefed.org. And a reminder: The opinions expressed in the presentations are statements of the speaker's opinion, are intended only for informational purposes, and are not formal opinions of—nor binding on—the Federal Reserve Bank of St. Louis, the Board of Governors of the Federal Reserve System, or any of the other agencies on today's call.

Regarding questions: We have received a large number of questions already, but you can still submit questions using either the Ask Question button right there in the webinar, or you can send us an email at asktheregulators@stls.frb.org, and that's right there on the slide, so you can reference that. The agencies represented on this call may use your questions in developing content for future sessions. So as a reminder, institution-specific questions are always best handled by your state or federal regulator or by the examiner in charge for your institution. So if you have a very specific question, we encourage you to reach out to your direct contacts.

Also on Slide 3, please note, and I quote, "The OCC, Federal Reserve Board of Governors, and FDIC issued an interim final rule regarding capital treatment under the ECIP that was published on March 22, 2021, that included a request for public comment through May 21, 2021. Because the comment period on the interim final rule is open, we will not engage with comments on the interim final rule during this discussion."

All right. So we got all that out of the way, so let's go ahead and jump to Slide 4, and we're going to get started. Chris, I'm going to turn it over to you to take it from here.

Christopher Weaver: Thanks, Carl. So good afternoon, everyone. My name is Christopher Weaver. Again, I'm the interim director for the Emergency Capital Investment Program, where I'm leading the team that's helping stand up this recovery program. I'm also joined by my colleague David Alexander, who is in our general counsel's office and is also on detail from the Federal Reserve to help us with the implementation of ECIP.

So we can turn to Slide 5. The Emergency Capital Investment Program was part of the Consolidated Appropriations Act that passed in December of 2020. The ECIP program appropriated $9 billion to Treasury to make investments in CDFIs, banks, credit unions, and holding companies. The primary purpose of the program is to revitalize low-income and minority communities, particularly those that have been disproportionately impacted by the COVID-19 pandemic. The ECIP program is part of a larger focus on CDFIs, where the provisions and statute also include the Rapid Response Program and the Minority Lending Program that either have been rolled out already by the CDFI fund or are in the process of being rolled out. TheThe Treasury Department sees all of these programs together as potentially being transformational for the CDFI industry and are looking forward to the impact that we think we can have on underserved communities.

Can move to Slide 6. TheThe basic eligibility before the program, in order to be eligible, an applicant has to satisfy two criteria. First, the applicant has to be a CDFI or a minority depository institution. So in terms of CDFIs, the applicant has to apply for CDFI status before December 27, 2020, and receive their certification before the date of filing their application. And in terms of the MDIs, that status just has to be present on the date of application. Now, in addition to being a CDFI/MDI, the applicant also has to be either a holding company, an insured depository institution that's not controlled by a holding company, or a credit union. And so if an institution is an insured depository institution that's controlled by a holding company, they must apply at the holding company level and cannot apply at the depository institution level.

Slide 7. TheThere are two categories of institutions that are ineligible according to the statute. Those are institutions in troubled condition by their federal regulator and institutions that are subject to a formal enforcement action for unsafe and unsound lending practices. Because this is mandated by law, Treasury does not have any flexibility to allocate funds to applicants that fall into these two categories.

In terms of the process, the applications will be received by Treasury through the portal. They'll be initially screened for completeness and basic eligibility, and then those applications will be forwarded to the regulators. The regulators will not be making investment decisions, but they will be providing data back to the Treasury Department to help us with the underwriting. And some of that information that we'll be receiving is around these two ineligibility criteria. So if we receive an indication from the regulators that an applicant is ineligible based on any of these two criteria, Treasury will not move forward with the underwriting process, and the applicants won't have an opportunity to refile those applications. So you must make sure that any issues that you have in terms of troubled condition or enforcement actions are resolved before filing the application.

Slide 8. TheThe Treasury investments in CDFIs/MDIs will be in the form of preferred stock or subordinated debt. The subordinated debt is reserved for those institutions that can't issue preferred stock, and those will include the Subchapter S corporations, the mutuals, and credit unions. The maximum amount of investment that any applicant receives is $250 million, but that's further limited based on the total assets of the financial institution. The limitations are 7.5% of assets for institutions with greater than $2 billion in assets, the institutions will be limited to 15% of assets if they have between $500 million and $2 billion in assets, and then 22.5% of assets for institutions with less than $500 million. So it's the lesser of the $250 million or any of those cutoffs based on asset size.

Slide 9. So, again, the preferred stock will be purchased from most institutions with the exception of the S corps, mutuals, and credit unions. The term sheets for the respective institutions are listed on the Treasury website, and you can find the link at the end of this PowerPoint presentation. But just an important thing to note that the term sheets state that the provisions are preliminary and subject to change, and the final terms will be the conditions that are found in the definitive closing documents. Treasury has received a number of comments around the term sheets, and we're still open to questions and recommendations on things that people think we can do to improve those. So you can submit any of those comments to the email that's at the end of this PowerPoint, as well, too. But we continue to work our way through comments on them.

But some of the key terms in the term sheet as it relates to the preferred stock is that it is a perpetual instrument that will receive tier 1 capital treatment. There are no dividend or interest payments in the first 24 months after closing, and the instrument is a non-voting and non-cumulative instrument. So after the first 24 months of no payments, the rate will be based on increases in qualified or deep impact lending that I'll cover in the next slide. But in no event can the rate go above the 2% rate that's required under the statute.

Slide 10. TheThe ECIP statute is designed to increase lending in underserved communities. And Treasury has designed the program, from our perspective, to try to make some distinction between what we determine to be good and what we determine to be great, so that we provide greater incentives for lending in those areas that we think have historically been underserved more so than others. The qualified lending categories that you see on the slide are designed to largely align with what the CDFI fund accepts, except we've broken them down into people, places, businesses, and projects. The qualified lending column, those things will receive dollar-for-dollar credit against the rate reduction. But the deep impact category is where we see double credit. And that's Treasury recognizing that the type of lending that's on the deep impact side in some cases can be time consuming and more costly, and it's our goal to try to more quickly lower the cost of capital for those institutions that focus in these areas. And, again, these guidelines are on our website, and we're still also open to additional suggestions in that area, as well, too.

Slide 11. The rate reduction guidelines are posted on the website. They spell out the methodology that Treasury will use to calculate the dividend or interest rate after year 2. The process goes where Treasury will begin by establishing a baseline that calculates the amount of qualified lending originated by the financial institution in the four quarters leading up to September 30, 2020. And The baseline is our starting point for determining the rate reduction. Then it will have the 24 months that I mentioned earlier, where there will be no dividend or interest payments. And then beginning in the first quarter of year 3, treasury will compare the dollar amount of origination from year 2 to the baseline year. And if the amount of origination has increased by 200% to 400% of the Treasury investment, the rate will be 1.25% for the following year. And if the origination has increased by 400% of the amount of the Treasury investment, the rate will be 0.5%. And again, the deep impact lending will receive double credit towards that rate reduction.

So just a couple of important things to note here about the rate reduction: So first, the baseline calculation is based on originations in the four quarters leading up to September 30 and not the dollar amount of loans on the balance sheet on that date. The same is also true for the comparison year. The baseline and dividend rate reduction are based on originations and not balance sheets. And then the second important thing to note is that the dividend on interest rate calculation is done annually and could increase if the amount of originations fluctuate from year to year, but in no event can the rate ever go above 2%.

Slide 12. Briefly, in terms of the application process, the application portal is the only way applicants can apply for the program. The application window closes on July 6, 2021, and Treasury will not accept applications outside of the portal or after the closing date. And the complete application must have an application form as well as a complete emergency investment lending plan, which I'll cover in the next slide.

Slide 13. The Emergency Investment Lending Plan has four sections. They must all be completed and supported with documentation and data. The first section focuses on the track record of lending by the institution directly to low- to moderate-income and minority borrowers. And it's very important to note that this section focuses on lending directly to individuals as opposed to place-based lending. So this is people focused. This is looking back two years to your track record of lending directly to LMI and minority borrowers. The second section is where the applicant will lay out their business strategy and operating goals. In this section, you should demonstrate an understanding of the target market, and you should have strategies and goals that are tailored to the needs of that community based on your understanding, particularly those impacts that have arisen as a result of the COVID pandemic. So Question 2 should have data about the community, it should have the impact that COVID has had on that community, and it should have a narrowly tailored strategy to meet those needs.

And then in Question 3, there is a two-part question here. The first section of it is identifying the growth strategy for the entity over the 10 years of the program. This is aggregate dollar amount of increased qualified lending that you believe your institution will do, both for people and places, over the 10-year period. But the Question B is more focused, and it focuses on the growth strategy specifically for minority communities. And so that should be your gross strategy and how you have reached those minority communities in section 3b. And then, finally, the last section focuses on the outreach and community plan. All the institutions that are participating in this program should demonstrate that they've engaged with the community and that they've developed an outreach and communication strategy that basically shows that it's been responsive to the needs of that community.

Slide 14. The underwriting process. Again, all decisions around allocation and allocation amounts will be made by the Treasury Department and not the regulators. And The regulators will provide information about financial condition to the Treasury Department, but the Treasury Department has the ultimate responsibility for decisions in the underwriting process. So in terms of the Treasury process, each application will receive both an individual review and then all of the applications will receive a collective assessment.

So in terms of the individual review, there are three components to that.

The first component is the financial condition and the ability to repay the dividends or interest. The financial condition will be mostly based on data that's received from the regulators, but Treasury will also do an assessment to determine whether or not the institutions meet a minimum dividend or interest coverage ratio, and that's directly related to the ability to service the debt.

And then the second component is the capacity to execute on the lending plan. Again, we'll go back to that Question 1 in the lending plan, where we focus on your track record and how well you historically met the needs of both individuals and the target communities. We'll also look at the reasonableness of the plan based on the size and condition of the market. And then, finally, we'll look at the internal capacity of the institution, which would include their staffing and their networks and the ability to execute on a lending plan based on that.

And then, the third component is the responsiveness to community needs. This is very important, because we're trying to make sure that the program is focusing on addressing some of the issues that have arisen as a result of COVID. So this section should demonstrate an understanding of the market, and it should be very data driven. You're looking at the unemployment rates or mortgage defaults. This depends on what your strategy is for addressing that community, but it should be driven by the impact that COVID has had on that particular community, and your plan should be tailored to meeting those needs. And finally, the responsiveness: We'll look, as I mentioned earlier, about the community outreach plan and how you've engaged with the community in making those determinations.

And then once each application has received an individual review, Treasury will conduct a collective review of all the applications. And this is primarily to make sure that both the statutory and policy goals of the Treasury Department are being met. So we will look at the geographic and demographic coverage to make sure that we don't leave any community out, and we will also look at the compliance with the statutory set-asides based on asset size that are required by the law. So this collective review will be very important in the event that we are oversubscribed for this program, because decisions about the amount of allocation or how we reallocate will be based on these criteria.

And then Slide 15. The Emergency Capital Investment Program also has some compliance requirements, but I will say that the program is largely an incentive program, and so it's more carrots than there are sticks. So Treasury has published an IFR that focuses on exec comp buybacks and dividends. Our goal is not to create a parallel or duplicate structure with the regulators, so the IFR largely aligns with the requirements that are required by your primary regulator. But this IFR, from Treasury's vantage point, is applicable during the investment period or until Treasury no longer holds the investment. And then in terms of clients, we'll also have a periodic reporting for qualified lending and deep impact lending in order to first establish the baseline and track the impact of the program. And there will be more released on this, requirements for the reports will be issued at a later date, and Treasury will provide an opportunity to comment on those.

And with that said, we can turn to the final slide around resources. Treasury has a webpage where we're still accepting comments around the term sheets as well as the rate reduction guidelines. Any suggestions or comments that anyone has, the email address there is ECIPInquiries@treasury.gov. Very much interested in hearing feedback. And then the webpage link there is where you can find the term sheets and the rate reduction guidelines. And then finally, and most importantly, the application window closes on July 6, 2021. The ECIP program is not being done on a first-come-first-served basis, and There is no particular advantage for an institution applying early as long as they apply before the application deadline.

And with that, I'll turn it back over to my colleagues in the Federal Reserve.

Carl White: All right, thanks, Christopher. We'll let you grab a drink and pause before we get into questions. The last slide, 17, also just reiterates how you can submit questions. You can email your questions right there to asktheregulators@stls.frb.org, or you can use the Ask the Question button. As I said at the beginning, we've already received quite a few questions, and we're going to get through as many as we can. But that does not prevent you from submitting questions, and we'll make sure that those questions are shared with our presenters today.

One last reminder as we move to questions. I do want to remind you once again that the OCC, the Federal Reserve Board of Governors, and the FDIC issued an interim final rule regarding capital treatment under the ECIP that was published on March 22. That included a request for public comment through May 21. So because the comment period is still open, we will not engage with comments on the interim final rule during this discussion.

All right. So we're going to jump right into the questions. So Christopher, I hope you're ready. The first few I think I'm going to throw your way.

The first one is really tied to what is meant by "troubled conditions." So: If the bank or holding company is currently deemed to be in troubled condition but is likely to have the designation removed over the next couple of months, will the institution be eligible for the ECIP?

Christopher Weaver: So this is one of those categories where Treasury does not have a lot of flexibility. The statute specifically spells out that if the institution is in troubled condition or subject to an enforcement action that addresses unsafe or unsound lending practices, that they are not eligible for the program. So as I stated in my presentation, we will send all the applications over to the regulators, the regulators will make the determination about a troubled condition orwheater or not there's an enforcement action that impacts unsafe and unsound lending. If that communication comes back to the Treasury Department, we will not proceed with the underwriting process. And so from the Treasury perspective, there is no flexibility on this question.

Carl White: All right, thanks, Chris. And I think there was a follow-up question, but I think you pretty much answered that as well, so we'll move on to the next topic.

All right. Another one for you, Christopher. So: What happens if, during the period in which a CDFI is an ECIP participant, that the CDFI's market changes and the bank is no longer CDFI certified? Likewise, if an MDI bank's ownership or management team changes, and it loses its MDI status, what are the implications and, for some debt, for example, would it be put into demand? What would happen to the rate? Would there be a cure period?

So really, the question is: What happens if they're no longer technically a CDFI or MDI after the fact?

Christopher Weaver: The program does require the institutions to maintain their CDFI and MDI status during the investment period. But Treasury recognizes that from time to time, institutions—at least for CDFI purposes—may fall below the 60% threshold. The CDFI fund typically provides an opportunity to cure and Treasury will not take any action during that cure period. If it does go beyond the cure period, Treasury does maintain the right to trigger the noncompliance remedies that are in the term sheets, and that could include restrictions on capital distributions or restrictions on the rate reductions that are available underneath the program. But we tend to have the maximum flexibility around this to give people the opportunity to cure.

Carl White: All right, thanks, Christopher. One more for you, Christopher. So: Treasury has allocated $2 billion to institutions under $500 million and an additional $2 billion to those between $500 million and $2 billion. If there are enough quality applications, could these smaller banks also get some of the remaining $5 billion, or is the $5 billion essentially left just for the bigger banks by virtue of the allocations to the smaller banks?

Christopher Weaver: The answer is that the statute mandates a minimum dollar amount set aside for institutions with less than $2 billion in assets and less than $500 million in assets. There is no minimum set-aside amount for the institutions with more than $2 billion in assets. So in theory, the smaller institutions could receive a piece of the $4 billion that could be perceived as being allocated to the larger institutions. There is no minimum set aside for the larger institutions.

Carl White: Got it. Okay, thanks, Christopher.

So, David, we're going to turn to you now. So: Why is there a mandatory five-year hold period for stock or sub-debt issued under ECIP? Can this be changed? If a bank or holding company wants to redeem an issuance prior to the five-year period, can they do so if their primary regulators approve?

David Alexander: It's a good series of questions. And the term sheets provide a little bit more of the detail on the framework, so I would encourage folks that are interested in this topic to refer back to the term sheets that have been published on the ECIP website.

There is a five-year holding period. And the primary reason for that is that Treasury sought to establish the terms of the preferred stock issued under the program in order to enable the preferred stock to receive tier 1 capital treatment. And it's made the terms of the subordinated debt, to the extent possible, consistent with the terms of the preferred stock that's being issued under the program, which is what the statutory mandate sets out for Treasury.

So going back to the preferred stock term sheet, there's a provision that I would point out, and it's the Change in Law provision. So if there is a change in law after an investment under ECIP has been made that is a final change in law or regulation that could result in a loss of regulatory capital treatment for the investment, the institution can redeem the investment after it has—with the approval of its primary federal regulator. And so this Change in Law provision specifically is a way that an institution can redeem its investment at any time after the investment's been made under the ECIP program. And so I think that's a point of flexibility for capital treatment that people can be aware of. There will be more, again, information on the nuances of these terms when the final instruments are reviewed and executed, but as a general matter, this is the exception to the five-year holding period that firms can be aware of.

Carl White: All right, thanks, David. So, David, so the next is kind of a series of questions related to the excessive or luxury expenditure policy requirement. I'll just try to summarize these, and maybe you can provide some more clarification. The first one states: If a bank already has such a policy in place that's consistent with Treasury's draft policy, do they need to adopt another policy? The second one is: Can any expenditures be excluded? And the example they give would be company cars. And then: Will Treasury approve individual expenditure policies, or should the banks just work with their primary regulators? And then the last couple questions are: What types of spending would be considered excessive? Could you give maybe some specific examples there?

David Alexander: Okay. Well, I'll try to take these questions in turn. I think the first question was, if a bank already has a policy, is the bank required to write a new policy? The answer there is absolutely not. The statute requires Treasury to put forth the regulation, and Treasury has done that. And the regulation has standards for an excessive or luxury expenditures policy, but it doesn't require the establishment of a new policy. If a bank already has an excessive or luxury expenditures policy, what I would recommend is that the bank take a look at the categories that are covered under the Treasury regulation, and if there is language for each of those categories of expenditures in the existing policy, then, you know, the only thing that would need to be done is the compliance component where updates are made. If updates are made, and Treasury is made aware of those updates, there's certification provided on an annual basis that the firm is in compliance with the policy, that's about the extent of it. And then publishing the policy on the website if it's not already published in the website. So it's not a requirement to redo the policy.

Treasury did include a model policy in its regulation. The purpose for doing that was to reduce burden. So for firms that do not have any policy and were wondering how to go about writing a policy, there is a policy example there in the regulation that can be used as a template to create the policy. There are variations of that that firms can adopt for themselves based upon their business needs. And There's flexibility there provided that the general requirements in the regulation, in the IFR that Treasury issued, are covered.

I think the second question was if a bank opts to use the draft policy, can they exclude expenditures that have been approved by their primary federal regulator under the existing policy? Again, under the premise that you can use the existing policy and don't have to replace it, I think that would be a nonissue. If there are any categories of expenditures that are required to be addressed in the policy that are not addressed in the existing policy, then those should be added. But the idea would be that you could build off of—a firm could build off of the existing policy that it has.

The next question was on approval of excessive or luxury expenditure policies, and should the banks work with the primary regulators or with Treasury. So Treasury's requirement under the IFR is to establish a luxury expenditure policy. The policy should cover the items that are in the regulation. The policy needs to be published to the website. The policy needs to be certified as to compliance on an annual basis, but it's not an approval process. Treasury's not intending or expecting to do a case-by-case approval of excessive or luxury expenditure policies for banks that are participating in the program. Banks are expected to develop those policies on their own or in conjunction with their primary federal regulators to the extent that their regulators have requirements for policies and procedures. And then, with respect to Treasury, the expectation is that we would see that those policies are published, and then Treasury would receive the certifications on an annual basis.

The next question was what types of spending would be considered excessive. I think questions that's been presented include things like paying for training for staff, paying for boards of directors training or conferences, renovating bank facilities. So, you know, as could be expected, any expense can be useful and have a valid business purpose and be needed in context of the business goals and objectives of an organization. I think the purpose that was expressed in the regulation and then, I think, as demonstrated in the model policy that Treasury included in the IFRs, is that firms can decide where these quantitative limits should be placed for their organization. In other words, you know, it's really a question of whether expenses are excessive or unnecessary more than a question of, you know, should there be broad prohibitions on categories of expenditures. Now, there may be categories of expenditures that each organization look taking into consideration its business activities or objectives determines are unnecessary. Those are business decisions that would be made by each organization, you know, in the policy as it's approved by the board of directors. And then that is where the responsibility lies for making those assessments of what is or is not an appropriate expenditure.

I think that flows into the next question, which was what types of expenditures are banks required to go to Treasury to get approval for? And the answer is none. Treasury is not going to be looking at applications by banks to make specific expenditures; the purpose of the policy is so that each organization that's participating in the ECIP has its own policy and its own approval processes and standards that have been set out by, you know, management and approved by the board of directors. And that's what would, you know, be expected to be followed for any expenditures that are taken. The answer to that last question is: No, Treasury will not be doing approvals for expenditures for organizations that participate in ECIP.

Carl White: Great. Thanks, David. That was a multipart question. Sorry about that. Those are sometimes kind of difficult, but you covered a lot of detail there. So I appreciate that. The next question is about, you know, how the interim rule addresses executive comp, dividend restrictions, stock buybacks, by saying banks' policies or practices must be reasonable. The question is: What is considered reasonable, and then how will banks know if they're in compliance?

David Alexander: So, in particular, the way that the interim final rule that Treasury published works is that it relies and ties heavily into the requirements that already exist for each institution that have been put forth by its primary federal regulator. In fact, when it comes to the compensation issues, if a firm is in compliance with the requirement that its primary federal regulator has set out, the interim final rule indicates that that's deemed to be compliance with the rule, the interim final rule. The first thing that a bank can do to make sure that it's meeting that reasonable standard for compensation policies and procedures is make sure that it's in compliance with the requirements that are issued by its primary federal regulator. There are probably very few exceptions where it is a possibility that something might raise a question. I think the expectation is that, as a general matter, what we would see is firms that are complying with their primary federal regulator requirements, and that would be the gold standard there.

With respect to payments on dividends and share buybacks, capital distributions, there's really a basic way to approach this. One would be to look at the rule as requiring that before distributions are made to shareholders or to bond holders that are subordinate to Treasury's position, that payments that are due to Treasury are being made to Treasury on time, and that as long as that requirement is in place, there's not going to be any issue there. The other issue is Treasury took a look at the rules that most organizations that would participate in ECIP use whenever they are—well, the rules they're subject to under their primary regulator requirements for making distributions of capital. And the metric that's used in the IFR to measure distributions of capital aligns pretty closely with that requirement. And so as a general matter, if an institution is making distributions of capital that are consistent with the limitations on capital distributions that are issued by its primary federal regulator, that should be sufficient to be in compliance with the Treasury rule. And so, again, there's a theme here, which is that compliance with the requirements of a primary federal regulator will usually steer an institution in the right direction and result in compliance with the Treasury IFR requirements as well.

Carl White: All right, thanks, David. One more for you, and then we'll give you a rest and go back to Chris. So: The current subordinate debt term sheet for sub-S and mutual banks does not provide parity with the preferred stock offering for C-corp banks. The authorizing statute mandated comparable treatment. Can the agencies and Treasury amend the sub-debt term sheet for Sub S and mutual banks to, one, allow tier 1 treatment, two, extend the maturity from 15 to a minimum of 30-plus years, and/or lower the interest rate from 2.5% to 2%?

David Alexander: The first thing I'll say is that, as mentioned earlier, whenever setting these terms for the instruments, Treasury sought to establish the terms of the preferred stock issued in the program in order to enable the preferred stock to receive tier 1 capital treatment. And to the extent possible, the terms of subordinated debt have been made consistent with those terms.

Now, one distinction here is that debt always has to have a term associated with it. With preferred stock, in order to get to tier 1 capital treatment, it's required that preferred stock have a perpetual term. So when you're looking at areas where it would not feasible or possible to make terms align perfectly across instruments, that flexibility that the statute has to make adjustments falls squarely on this issue of how you look at terms for subordinated debt instruments. This is an area where Treasury has sought comment, feedback from the public and continues to do so. And as Chris mentioned previously, Treasury is encouraging participants who have views on this issue, not on the terms, to continue to provide those views, and Treasury will be taking those views into consideration. And that, you know, if there are any potential changes that will be made, they'll be expressed or, you know, it will be reflected in the final terms of instruments that are executed at closing.

Carl White: All right, thanks, David. All right, Christopher, we're going to turn back to you. And the next couple questions have to do with the 30% test. The first question reads: The 30% test presents significant barriers to participation for many. If an applicant submits its CDFI certification status as a proxy but later explains how it is highly effective in serving the types of customers described in the 30%, can it regain competitiveness and its potential for the amount requested in the application?

Christopher Weaver: Let me first walk the listeners through what the 30% test is for those who may not be completely familiar with it. So in the ECIP statute, a lending plan is required to demonstrate that not less than 30% of the lending over the past two years fell into three categories, and that's loans directly to LMI borrowers; loans directly to, essentially other targeted populations, which are minority borrowers according to the CDFI fund; and then loans that create direct benefits for LMI or minority borrowers. And so this is not in the eligibility section of the statute, but it is in the section of the statute that's required to have a complete lending plan. And The statute places a great deal of emphasis on Treasury trying to strike a balance between lending directly to individuals and place-based lending. And so this question here is focused 100% on lending directly to individuals, directly to borrowers.

And so this 30% threshold, we recognize that, for a number of reasons, some institutions may not have definitive data around the demographics of their borrowers. In some cases, that may be for legal or regulatory reasons for fair lending and equal credit issues, and some of it is just in terms of the difficulty in collecting that data. But some other borrowers, especially in the mortgage space and other places, will have access to that data.

So we tried to build into the application some flexibility that would allow borrowers to do one of three ways of demonstrating their responses to this question: They can provide the definitive data on those applications where they have it. The second is that they can use proxies that will indicate a reasonable probability about the demographics of the borrowers. So one of the examples we use is that if you don't have data about the race of the applicant, you could use loans that are made in majority-minority census tracts as a proxy for the race of the borrower. And we've left it to applicants to use any number of proxies, as long as they provide data around why they believe that indicates a reasonable probability about the demographics of that borrower. And then the last option, at least for CDFIs, is they can just rely on their CDFI certification.

But we do state very clearly that simple reliance on the CDFI certification—it will get you a pass for Question 1a, but when it comes to us looking at the track record of institutions, the quality of data that's provided in that section will be scored. And so to the extent that you're able to use more proxies and definitive data, those applications will receive more credit in the scoring. So no institution is going to be deemed ineligible for using any one of the methods, but some of them will receive more weight than others. Applicants can go through and talk about how they believe they can effectively reach the LMI and minority borrowers, but they should try as best as possible to back that up with data and documentation.

Carl White: All right, thanks, Christopher. Okay. I'm going to kind of change things up a little and give David and Christopher a break. I know we have the other agencies on the line as well, so I'm going to throw a few questions at some of our other colleagues who are on the phone.

The first, I think maybe, Art, I'll kick this one to you. So: If a bank holding company receives sub-debt, are there any restrictions on down streaming it to the bank as tier 1 capital? Will bank holding companies for sub-S banks be required to push down ECIP capital to the bank level?

I'll throw that to Art, or maybe, David, you'd like to jump in, as well.

Art Lindo: Thanks. David touched on this a little bit earlier. I mean, Treasury is finalizing what the terms are to this type of debt instrument, and the point being that we have an interim final rule out, so I have to be a little careful about what I say. But given where we are in all of that, the bottom line is what are rules around, if you will, sub-debt type instruments being included in the capital base? And with that said, basically, when you look at that being passed into it, it's not the same as perpetual preferred, so it doesn't get treated exactly the same way. The point would be it wouldn't be tier 1; it would be tier 2.

But when you think about the type of, if you will, the sub-debt, what are the uses, there are other ways that a floating company, a Subchapter S could, in fact, pass funding down to a subsidiary bank. So, you know, through other means, I guess you could say they could put it in in certain ways such as additional paid-incapital, but the idea here being that if it's sub-debt, the characterization of that would have some connotations to the investment, if you will, in the subsidiary entity. As they do pass it down, our goal is to see if, in fact, sustained quality of capital as others.So within our capital rules, without violating, again, the conditions on which I can talk about our rules since it's out for comment, you would look at the treatment of that being it wouldn't be clearly tier 1 in that regard; it would be tier 2. So maybe not the answer that most firms want, but until we get a final rule in place, that's what you have to see, and we have to see the conditions that the Treasury put out in final form.

Carl White: All right, great. Thanks, Art. I don't know, David, if you had anything more to add to that?

David Alexander: One thing I would add to that, in general, about the ECIP program is if, you know, you can look at the program and raise the question, I think this touches on the issue of are there limitations on use? Well, there are some limitations on use of funds in this program, but it's not this type of limitation. Those limitations are the limitations that we just walked through that are issued under the IFR on executive compensation, making sure you have policies and procedures in place so that your compensation's reasonable. That's a limitation on the use of funds. And dividends, distributions, buybacks—those need to be consistent with the requirements of the IFR. But that's really the extent of limitations on the use of funds under the program. The program also includes incentives for the use of funds, which Chris touched on earlier. And that means that you can get the rate reductions that were described under the rate reduction guidelines if the funds are used to expand lending in the ways that are described there. So, you know, in terms of uses of funds and how those are impacted, I would look to the IFR on executive compensation due to the buybacks; limitations on incentives, we'll look to the rate reduction guidelines.

Carl White: All right, great. Thanks, David, for that additional information. So let's go to Tom with the NCUA. So: Will the NCUA wait to contact credit union on their secondary capital plan until the Treasury Department has decided on ECIP amount approved, or will they still abide by the 45-day rule?

Thomas Fay: Thanks for the question. Hi, this is Tom Fay, senior capital market specialist at NCUA. Earlier in February, we did have a webinar with the credit union industry, and we did illustrate, or at least encourage credit unions, upon submitting an ECIP application to Treasury, and we encouraged them, to shortly afterwards, to send their secondary capital plan to the regional director. The reason is that it would give us an opportunity to see both applications concurrently and therefore making our time and approving both as efficiently as possible.

Now, to answer the question, obviously the current regulation is that we would take no more than 45 days to approve a secondary capital plan, and if it should be longer than 45 days, then that plan is essentially automatically approved. So essentially, it's the same as a non-objection or no objection. So, again, you can wait for us to approve of your plan because we will make those recommendations before the 45 days, but if you don't hear from NCUA, then it is automatically approved.

Carl White: Great, thanks, Tom. This next question might be for Betty with the FDIC and also Christopher back from the Treasury. He may want to chime in on this one as well.

So let me read it: The FDIC's capital estimator does not populate the data for newly certified CDFIs since December 2020. The ECIP application portal asks if the applicant has been a certified CDFI since that date. In the FAQs published March 30, Treasury said to be eligible to apply, you must have submitted your application for certification by December 27, 2020, and must be certified by the time you submit your application. Is a CDFI bank or a depository institution holding company that submitted its application for certification prior to December 27, 2020, and certified prior to the opening of the ECIP application on March 4, 2021, eligible to apply?

So a lot there really tied to when are they eligible.

Betty Rudolph: So this is Betty Rudolph with the FDIC, and I'll address that first part with respect to the capital estimator, which is an interagency tool, and the capital estimator captures data on FDIC-insured MDIs and CDFIs quarterly consistent with the Call Report. So we will be updating the estimator over the next week to 10 days to capture changes to the MDI and CDFI bank list between December 31, 2020, and March 31, 2021. And this update will include 29 additional CDFI banks. I would like to note that the capital estimator update process is independent of ECIP eligibility. We include all MDIs and CDFIs on the list as of the quarter-end dates, regardless of their ECIP eligibility. And I'll turn it over to Chris for the remainder of that question.

Christopher Weaver: Sure. So in terms of CDFI certification, the applicant has to have applied for CDFI certification before December 27, 2020, and as long as they have received that certification before they filed for their application, then they are eligible. And so we've already communicated with the CDFI fund, and they either have or will make determinations on all the applications that were filed before December 27, There won't be any that are pending approval when the application window closes.

Carl White: All right, thanks, both of you. So we're going to try to do just a couple more quick ones here. Let's go back to David. So, David: Does ECIP capital have to be repaid to the Treasury after 10 years?

David Alexander: Thanks. That's a good question. The answer to that question is no, it does not have to be repaid to Treasury within 10 years. The 10-year mark has some significance because after 10 years the rate reduction period that is developed under the statute concludes, and there are some significant, I guess, changes in the applicable requirements for the instruments after that time. For example, after 10 years, it could be the shortest period for which the restrictions on executive compensation dividends and share buybacks no longer apply. That period applies for the lesser of the investment period: the period for which Treasury holds its investment or 10 years.

The requirement is effectively that, under the statute, if there are any additional terms that Treasury would seek to apply to an investment after 10 years, those would kick in. And under the program that's been developed, there aren't any significant additional requirements that would apply to an investment after 10 years. And so not a material change in terms of additional requirements or an investment after 10 years, and the durations on subordinated notes and alThe perpetual nature of preferred stock mean that those investments can continue beyond 10 years.

Carl White: Great, thanks, David. All right. Looking at the clock, I think we can get one or two more in. So, Christopher: Are there any restrictions on the use of ECIP funds? What are the implications of not meeting the goals of the lending plan?

Christopher Weaver: So I think we've tackled this one in the presentation that David mentioned that the limited restrictions that there are on the IFR. But in terms of the types of lending and the types of things that the entities can do with the money in terms of investment, the program is all carrots and very few sticks. And so it's very flexible in how they can use the capital.

In terms of what happens if they don't comply with the operating goals that they've laid out in their lending plan, I guess the short answer to that is nothing. And that's why we are screening so heavily in terms of the lending plans to try to make sure we're picking institutions that have a strong track record of meeting the needs of those underserved communities, but we have incentives for people to do the things that we've identified, but there are no penalties for not meeting those operating goals.

Carl White: All right, thanks, Christopher. And I am going to squeeze one more in because I think it's a really good question. Art, I'm going to throw this one to you: Is the Fed treating women-owned or women-led institutions as MDIs? Will they be eligible for ECIP?

Art Lindo: Okay. The Fed's using the definition of MDI it says is based on FIRREA section 308. So that would not include women-owned depositor institutions. The answer is an MDI is currently defined as 51 or 51 or more percent ownership, if you will, by a minority class, if you will. So that would meet the WDI definition, so just to be clear on that. Now, there's been some confusion simply because we put out some guidance that we, at the Federal Reserve, put women-owned depository institutions in a supervisory program with our MDIs, but they are not defined as MDIs for this purpose.

Carl White: All right, great. Thanks, Art, for that clarification. We're going to wrap things up. We're right at the top of the hour. Thank you so much to all our presenters—to Christopher, David, Betty, Tom, and Art for all your work leading up to this session and, obviously, today handling all the questions and doing the presentation. This session will be archived at the exact same link that you used today, or you can just go to the Ask the Fed® website at www.askthefed.org. So you can go back and listen to that whenever you'd like.

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Thank you so much for joining us this afternoon, and we'll talk to you next time.

(END OF RECORDING)