Potential for Selling Held-to-Maturity Securities for Liquidity Purposes

Many financial institutions are facing numerous requests from both retail and commercial customers seeking to defer scheduled loan payments as these borrowers have been financially impacted by COVID-19. At the same time, there appears to be significant loan demand from small businesses for the new Paycheck Protection Program under the SBA 7(a) Program. These forces could impact overall liquidity and funding positions. While there are plenty of traditional sources of liquidity that banks can access, and a particularly attractive opportunity as detailed in the latest Strategic Insight, a less than obvious source of liquidity may be available because of the current COVID-19 pandemic.

It is normally rare to transfer or sell securities that are classified as Held-to-Maturity (HTM). However, there are certain safe harbor rules available that permit the transfer or sale of HTM securities without tainting the portfolio or one's ability to use this classification going forward. There is also a limited exclusion for certain unusual events. ASC 320-10-25 indicates events that are isolated, nonrecurring, and unusual for the reporting enterprise that could not be reasonably anticipated, however, may cause an enterprise to sell or transfer an HTM security without necessarily calling into question its intent to hold other HTM debt securities to maturity.

On March 27, 2020, the FDIC recently published ***Frequently Asked Questions for Financial Institutions Affected by the Coronavirus Disease 2019 (Referred to as COVID-19)***. A link to the document can be found at https://www.fdic.gov/coronavirus/faq-fi.pdf. A question addressing the subject of selling HTM securities for liquidity purposes is below.

> ***Question: Sales of Held-to-Maturity Securities. If a financial institution affected by the impact of COVID-19 sells investment securities that were classified as HTM to meet its liquidity needs, will that financial institution's intent to hold other investment securities to maturity be questioned?***
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> *Under normal circumstances, the sale of any HTM investment would call into question an institution's intent to hold its remaining HTM investments to maturity. However, ASC Section 320-10-25 indicates that events that are isolated, nonrecurring, and unusual for the reporting enterprise that could not be reasonably anticipated may cause an enterprise to sell or transfer an HTM debt security without necessarily calling into question its intent to hold other HTM debt securities to maturity. ASC Section 320-10-25 specifically states that extremely remote disaster scenarios should not be anticipated by an entity in deciding whether it has the positive intent and ability to hold a debt security to maturity. Accordingly, in this situation, the sale of any HTM investment security would not necessarily call into question the bank's intent to hold its remaining HTM investment securities until maturity.*

Based on this guidance from the FDIC, we believe financial institutions that have been negatively impacted by a reduction of liquidity due to COVID-19 may be able to sell securities classified as HTM without tainting a portfolio or jeopardizing the ability to use this classification in the future. *However, each bank should check with its financial statement auditor for further clarification.* An auditor should also be able to advise whether selling from HTM throughout the duration of the current crisis is allowable, or whether this should be completed in a shorter time period.

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