

Monthly News Brief

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Legislative Update

21st Century ROAD to Housing Act Returns to the Senate with Community Bank Title Restored

As reported in our March Newsletter, the Senate's version of HR 6644 — the 21st Century ROAD to Housing Act — stripped the community bank title from the bill the House had passed in February. On May 20, the House passed an amended version of the legislation by a vote of 396–13, restoring the community bank provisions as Title IX, Strengthening Community Banks' Role in Housing. Title IX consolidates a dozen separately reported banking measures previously approved by the House Financial Services Committee.

For Subchapter S Bank Association members, the most consequential provisions include clarifying that custodial deposits at smaller institutions are not treated as brokered deposits (Sec. 901), expanding the share of reciprocal deposits that may be excluded from brokered classification (Sec. 902), raising the asset threshold for the extended 18-month examination cycle from \$3 billion to \$6 billion (Sec. 903), and directing the agencies to streamline de novo community bank chartering with a two-year phase-in of capital requirements (Secs. 909 and 910).

The bill now returns to the Senate to reconcile differences between the chambers' versions. The Subchapter S Bank Association continues to support inclusion of the community bank title in any final legislation. The text of the House-amended bill can be found [HERE](#).

House Financial Services Committee Examines Fraud, BSA Modernization, and Bank-Fintech Partnerships

The House Financial Services Committee held a series of hearings and markups in May relevant to community banks. On May 13, the full committee marked up several measures focused on financial fraud and AI-enabled crime, including HR 2152, the AI PLAN Act, which directs a federal strategy against AI-facilitated financial crime, and HR 2978, the GUARD Act, which authorizes state and local law enforcement to use federal grant funds for financial fraud investigations.

On May 19, the Subcommittee on National Security, Illicit Finance, and International Financial Institutions held a hearing titled “Modernizing the BSA for Financial Crime in the 21st Century.” BSA right-sizing has long been a priority for community banks given the disproportionate compliance burden imposed by current reporting thresholds. On May 20, the Subcommittee on Digital Assets, Financial Technology, and Artificial Intelligence held a hearing titled “Partnering for Innovation: How Bank-Fintech Collaborations Enhance Financial Infrastructure.” Committee materials are available [HERE](#).

FFIEC Proposes Comprehensive Overhaul of CAMELS Rating System

On May 19, the Federal Financial Institutions Examination Council issued a notice of proposed rulemaking that would revise the Uniform Financial Institutions Rating System — commonly known as CAMELS — for the first time in approximately 30 years. The proposal would refocus both component and composite ratings on factors that materially affect an institution’s financial condition and risk profile, deemphasizing policies, procedures, and documentation findings unless tied to significant financial risk.

Several elements of the proposal are particularly favorable to community banks. The proposal raises the standard for examiners to downgrade the Management component by requiring a connection to material financial risk; limits the influence of specialty examination findings on composite ratings; removes all references to reputation risk, consistent with the interagency final rule taking effect June 9; and modernizes terminology to align with current accounting practice, including replacing “allowances for loan and lease losses” with “allowances for credit losses.” Comments are due August 17, 2026. The FFIEC release is available [HERE](#).

OCC Continues Effort to Reduce Regulatory Burden on Community Banks

On May 18, the OCC issued News Release 2026-38 summarizing its ongoing reforms to tailor supervision for community banks. Comptroller of the Currency Jonathan Gould stated: *“Community banks are anchors of local economies, providing essential banking services and small business lending that helps power job creation.”*

The release consolidates several previously announced actions — including the examination tailoring guidance effective January 1, the CBLR final rule taking effect July 1 (covered in our April Newsletter), and the revised model risk management guidance from which community bank models are generally excluded — and introduces one new step: examiners are now required to use an updated resource intended to narrow the scope and simplify bank information technology and cybersecurity examinations at community institutions. The release can be found [HERE](#).

OCC Issues Third Quarter 2026 CRA Evaluation Schedule

On May 28, the OCC published its schedule of Community Reinvestment Act evaluations for the third quarter of 2026. The OCC has historically published the CRA schedule two quarters in advance but has temporarily reverted to one quarter at a time while it implements the new community bank CRA scheduling discretion previewed in News Release 2026-38. Member banks under OCC supervision should review the published schedule [HERE](#).

FDIC Releases First Quarter 2026 Banking Profile

On May 27, the FDIC released its Quarterly Banking Profile for the first quarter of 2026. FDIC-insured institutions reported aggregate net income of \$80.5 billion, an increase of 3.6 percent over the prior quarter, and a return on assets ratio of 1.26 percent. Community bank quarterly net income rose 3.9 percent over the prior quarter, and the share of unprofitable community banks declined from 7.4 percent to 4.9 percent. Domestic deposits grew for the seventh consecutive quarter. The Quarterly Banking Profile can be found [HERE](#).

Dividend Flexibility in Subchapter S Banks: Strategic Distribution Planning

Tax-Free Distribution of Earnings

One of the most compelling advantages of Subchapter S banking is the ability to distribute earnings without a second layer of tax. A C corporation bank pays corporate income tax on its earnings whether or not they are distributed, and shareholders are taxed again when those earnings are paid out as dividends. That second layer discourages distributions and can push capital decisions toward minimizing taxes rather than serving the business. S banks face no such constraint. Because income is allocated to shareholders for tax purposes as it is earned, cash distributions from the bank's accumulated adjustments account (AAA) are generally tax-free to shareholders with sufficient stock basis. The board can therefore size distributions around the bank's capital needs, growth opportunities, and shareholder preferences. S banks may distribute all earnings, retain everything for growth, or strike any balance in between without changing the tax result for shareholders.

Cash Flow Planning for Shareholders

The pass-through structure also creates a challenge: shareholders owe tax on their allocable share of bank income whether or not they receive cash. Planning for this phantom income falls on both the bank and its shareholders. A shareholder who owns 10% of an S bank earning \$5 million reports \$500,000 of income and could owe roughly \$185,000 in federal tax at the top 37% marginal rate, even if the bank distributes nothing. To address this, most S banks adopt a regular tax-distribution policy sized to cover shareholders' estimated liability — commonly 40% to 45% of allocated income, to account for combined federal and state tax. Formalizing these distributions in shareholder agreements or a board dividend policy gives shareholders predictability. Boards should also weigh differing shareholder needs — some prefer current income, others long-term value — and communicate distribution policy clearly while balancing those preferences against the bank's capital and regulatory requirements.

Distribution vs. Retained Earnings Strategy

Balancing distributions against retained capital is the central strategic decision for an S bank. Unlike a C corporation, where retained earnings have borne only corporate-level tax, S bank shareholders have already paid personal tax on earnings the bank keeps. That creates an

expectation of some tangible return, so boards must explain why retention — for organic growth, acquisitions, or capital buffers — justifies asking shareholders to reinvest after-tax dollars. Banks with strong growth prospects may retain more after meeting tax distributions, a strategy that works best when they can demonstrate superior returns on that capital. Mature banks in stable markets may instead distribute a larger share, returning capital for shareholders to deploy as they see fit. Capital position also drives the decision: well-capitalized banks have room to distribute generously, while those near regulatory minimums must retain earnings to stay compliant and fund asset growth.

The examples in this article are purely hypothetical and provided for illustrative purposes only. Members should consult qualified tax professionals for guidance specific to their own institutions.

Subchapter S Bank Association 29th Annual Conference

Join us for the Subchapter S Bank Association's 29th Annual Conference on October 22nd and 23rd, 2026 at San Antonio Marriott Rivercenter on the River Walk in beautiful downtown San Antonio!

Listen to the latest in strategies and tactics to improve bank performance and ensure ongoing compliance from the leading professionals in the industry!

Find out more information [HERE!](#)

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