

Office of the Comptroller of the Currency
Minutes of the Meeting of the
Mutual Savings Association Advisory Committee
September 22, 2020

The Mutual Savings Association Advisory Committee (MSAAC) was convened for a meeting at 8:30 a.m. on September 22, 2020. The meeting was conducted via webinar.

In accordance with the provisions of Public Law 92-463, the meeting was open to the public from 8:30a.m. to 10:45a.m.

Advisory Committee Members Present

Ana Babiasz, James Brown, JR Buckner, John Coyne, Tom Fraser, Jim McQuade, Brian North, Dennis Parente, Annette Russell, William White

OCC Staff Attending

Acting Comptroller of the Currency, Brian Brooks, Jason Almonte, Frances Augello, Charlotte Bahin, Michael Brickman, Arnie Cohen, Ralph DeLeon, Danial Grantham, Vicki Hawkins-Jones, Cristina Im, Brian James, Ernie Knott, Kay Kowitt, Karen Marcotte, Sydney Menefee, Michael Moriarty, Andrew Moss, Linda Nichols, John O'Brien, Blake Paulson, James Porreca, Marta Stewart-Bates, Heidi Thomas, Troy Thornton

Public Meeting

Introduction and General Remarks

Michael Brickman, Deputy Comptroller for Thrift Supervision and Special Supervision, welcomed the members of the Advisory Committee. Mr. Brickman gave a brief description of the agenda for the meeting. He explained that the first hour of the meeting would be a roundtable discussion as part of which each of the Committee members would provide information about his or her market. The second hour of the meeting would include supervisory updates from the District Deputy Comptrollers. Mr. Brickman also noted that Senior Deputy Comptroller and Chief Operating Officer Blake Paulson and Acting Senior Deputy Comptroller for Midsize and Community Bank Supervision Sydney Menefee would participate in the both roundtable discussions.

Finally, Mr. Brickman noted that this meeting is the last meeting of the Advisory Committee with this group of members. He described the achievements of this committee, including providing input for the implementation of the Covered Savings Association Act.

Member Roundtable

In preparation for the Member Roundtable portion of the meeting, the Committee members were sent the following examples of possible topics for discussion. The examples were not exclusive, and the Committee members were told that they could raise any topic they wished.

- Local economy, any signs of movement in either direction
- Loan demand, both retail and commercial; are levels of forbearance changing? Are borrowers that are reaching the end of their forbearance period able to return to regular payments?
- For those members with commercial or multifamily loan portfolios, are there any changes? How are small businesses area doing?
- Are you increasing the bank's allowance, has thinking about that changed?
- Many banks are reporting steady or growing customer deposits, have your deposit levels changed?
- Did you participate in any of the programs developed to respond to the pandemic? What was your experience? What were the benefits, if any?
- What proactive steps are you taking to prepare for potential longer-term economic fallout from the pandemic? Are you considering stress scenarios on portfolio performance, are you expanding or limiting lending or deposit operations or strategic plans, have you decided to sell or discontinue any products or loans?
- Have your board or management teams had discussions about expanding or reevaluating your outreach to minority customers or communities in your market? Have you had discussions about access to credit or products offered as a result?

Each of the Committee members highlighted the pandemic's impact on local economies, individual operations and priorities.

The economic impact on the individual market areas generally varied by location, how long the local shutdown had lasted and what industries drive the local economy. Those Committee members who are traditional mortgage lenders generally reported strong mortgage performance with low levels of requested forbearance relative to averages reported for the industry generally and for non depository lenders. Committee members noted that even those customers who had requested forbearance were keeping current with escrow payments. They also reported that delinquencies are at rates similar to those before the pandemic. Several Committee members noted that they have been expecting credit issues resulting from the actions being taken to address counter the pandemic but that they have not materialized.

There was general optimism about mortgage lending in most markets. Several Committee members who are construction lenders reported that the market is thriving. The commercial real estate lenders on the Committee were concerned about whether small businesses would be able to reopen or survive a long-term pandemic. The unemployment levels varied by geographic area. Committee members report that many small businesses were not able to survive the local shutdowns. Those areas dependent on hotels, restaurants and other tourism industries were less optimistic. In particular, the Committee members in markets in which tourism is seasonal, are less optimistic about the general economy. They are concerned about the long-term affects on their geographic areas from travel restrictions and small business shutdowns. Committee members noted that where an employer, group of employers or industry is important to the health of the community, changes in operations or closures, resulting from local shutdowns can have extreme consequences.

The increased level of deposits as a result of the Payroll Protection Plan was discussed by the Committee members who participated in the program. A Committee member noted the affect of the increase in deposits on the institution's leverage ratio and that the change is reflected in discussions about capital at the Board of Directors level. Another Committee member noted that deposits had grown more than at any other time in recent history. Committee members generally expect the deposit levels to get back to pre-pandemic levels in a year to eighteen months. The Committee members noted that having a mutual charter was an advantage in uncertain economic times. They have good capital levels and can take the long view when planning. They can be patient as they work out of the affects of the pandemic. Several Committee members also mentioned that collaboration is an important way that mutuals expand products and services and that it is important for mutuals to consider opportunities. A Committee member noted that there are legislative and regulatory impediments to collaboration that it would be helpful to address.

The Committee members raised several supervisory concerns as they talked about the affects of the pandemic on their local economies. Several Committee members talked about the need for an extension of the troubled debt restructuring guidance. Ms. Menefee asked whether the Committee members are working and communicating with their borrowers. Mr. Paulson told the Committee members that the message to examiners is that they should be patient and not rush to downgrade loans. Loan ratings must accurately reflect the risk and that the opportunity to improve must be given. The future is uncertain but when actions are needed, they should be taken. Examiners are given the message that they should tell bankers to work with borrowers to structure loans.

Several Committee members described their recent examination experience. In each case, the bank had undergone a recent examination and all of the exam, except the exit meeting had been conducted off-site. The Committee members complimented the OCC on how well the off-site examinations went. A Committee member asked that the OCC and the Federal Reserve work together on the rule to implement the Community Reinvestment Act. Mr. Paulson noted that the recently issued advanced notice of proposed rulemaking issued by the Federal Reserve to review the current CRA rule is similar to the OCC's CRA final rule. A Committee member thanked the OCC for the work done to implement the Covered Savings Association Act. Mr. Paulson thanked the Committee members for their contributions on a variety of topics.

District Roundtable

Mr. Brickman introduced the District Deputy Comptrollers who were at the meeting and introduced the topics that would be covered as part of the discussion. Kay Kowitt, Deputy Comptroller for the Western District, Troy Thornton, Deputy Comptroller for the Southern District and Brian James, Deputy Comptroller for the Central District were present, and Michael Moriarty and Linda Nichols represented Beverly Cole the Deputy Comptroller for the Northeastern District. Mr. Brickman described the roundtable topics that would be discussed. They included hearing the district perspective of direct supervision of savings associations and the risk assessments introduced as a result of the pandemic. He noted that the OCC values all feedback on how communication and examinations have continued to be conducted as the agency has shifted to a more virtual environment.

Ms. Kowitt described the OCC's supervisory approach to assessing the impact of the pandemic and provided some early observations. She began with the supervisory approach. She clarified that the OCC's overarching risk-based supervisory philosophy has not changed. In May, the OCC developed an internal plan to guide the supervisory efforts over the next few quarters and beyond, if necessary. The first step in the plan was to conduct a risk assessment across all community banks get a baseline determination of how best to prioritize and allocate resources going forward.

At the conclusion of the assessment, a risk leveling process resulted in changes to supervisory strategies, as appropriate. The execution of the strategies varies by district and field office depending on individual banks, business models and risks. Ms. Kowitt noted that as part of discussions with the appropriate ADC or portfolio manager, bank management should be aware of the bank's supervisory plan and whether it has changed. The focus is on risk management and governance systems that are in place to manage those risks, as well as any proactive measures to respond to the identified risks.

Of particular interest are each bank's credit risk management practices. They are an important foundation to managing the loan portfolio in good times and they are even more critical given the challenges of the pandemic. Areas of focus include everything from MIS monitoring practices, risk ratings, problem loan workout, collateral valuation, stress testing, loan review, and the core fundamental components of a good credit administration program. The supervisory approach needs to remain fluid, the full impact of the pandemic or the duration of the downturn is not known. Ms. Kowitt added that many of the impacts are due to factors outside the control of bank management and it is important that examiners exercise appropriate flexibility.

She noted that the condition of the banking industry was strong at the outset of the pandemic. Most banks had low or manageable problem assets, good capital, and liquidity positions. The negative impact has not really materialized due in part to the government stimulus programs. Loan portfolios so far are generally performing well, as the Committee members noted, but deterioration of asset quality can occur when some borrowers do not recover from the economic impact.

Commercial credit is the primary risk to the banks supervised by the OCC due to the concentrations in vulnerable sectors, for example commercial real estate, hospitality and travel. There are geographic differences in concentrations, for example oil and gas and the agriculture sector can be concentrated in some geographies. There also is some elevated retail risk due to the high unemployment and the expiring stimulus payments and loan modifications.

Ms. Kowitt noted that capital and liquidity are sound. The second quarter data show increased pressure on earnings due to a combination of the prolonged low interest rate environment and the increasing loan loss provision expenses. Other risks include operational risk and compliance risk. Operational risk continues as bank management manages IT systems and cyber security risks in this environment. Compliance risk is important given the rapid implementation of the numerous new rules recently issued by the OCC.

Mr. James echoed Ms. Kowitt's comments about examiners use of reasonable judgment. He noted that he is cautiously optimistic. Earlier in the pandemic, he was more concerned, but now he is optimistic that possibly the downturn will not be as severe as predicted. He agreed that the industry was in good condition going into the pandemic. Asset quality was good and bank management had done a lot of work over the last eight to 10 years to strengthen risk management practices.

Mr. James said that he would focus his remarks on the risk drivers increasing credit risk in institutions, particularly commercial real estate. An example of the risks is a review of multifamily lending to see what types of concentrations there are in the institutions that make multifamily loans. Right now, across the four districts, there are 20 institutions with multifamily concentrations over 200 percent of risk-based capital. When other higher risk areas for commercial real estate are added, for example, office, hotel, and retail lending, 50 institutions have concentrations of over 200 percent of risk-based capital across the four districts. While there are institutions with some risk, the numbers look a little different than what they were going into the last downturn. He acknowledged that some of his optimism results from his review of this information, the types and levels of concentrations are not the same as they were going into the last downturn.

In another area of commercial real estate, construction and development, there are 23 institutions that have construction development concentrations at 100 percent of risk-based capital or above. Most of those are in the Southern District, in the growth markets and on the coast. There are no institutions with construction and development concentrations at 100 percent of risk-based capital in the Central District. C&I lending is another type of commercial lending that over the longer term will be watched to get a better sense of how its performance will impact commercial real estate.

Mr. James noted that prior to the pandemic, from a credit administration perspective, the supervisory focus was on preparing for the next downturn, without knowing when it would happen. The focus at the time was underwriting concentration risk management and problem identification. Since the beginning of the pandemic, as part of the risk assessment, ADCs have talked about their portfolios in each individual market. They generally are optimistic about how the risk management in the institutions is holding up. They give credit for the health of institutions to the quality work that bank management is doing on the risk management side. The ADC group, as they provide feedback, has confidence that things are working well.

As was previously mentioned, the way forward is uncertain. Each market is different because the lockdowns have been of different duration and scope. It is important to understand what the local rules are, what type of moratoriums are in place in each one of the markets. It is a benefit to have local ADCs and local examiners that know those markets. Mr. James reiterated that what cannot be emphasized enough with exam teams is the importance of using good judgment as credit risk management is reviewed. The focus of communications with examiners is that they should be patient and understand that banks are working with borrowers, while also understanding that appropriate identification of the risk in the portfolio is necessary. The troubled debt restructuring discussion should not be the primary discussion, rather it is the identification of the risk.

Mr. James noted that retail credit is not raising a lot of concerns. In the Central District it is not a significant discussion. A lot of people are returning to normal payments, but much of the information is anecdotal. In the second round of discussions with banks, examiners will get a better sense of what retail credit looks like. It is still early, and it will be another quarter or two before there is an understanding of how retail credits are performing because there are so many unknowns. On the retail side, unknowns include whether employment will bounce back.

Mr. Thornton discussed examiner guidance that had been issued. He noted what bank management should be doing or thinking about now to prepare for the longer-term consequences of the pandemic. The inter-agency examiner guidance issued in June (OCC Bulletin 2020-64) provided guidance on assessing safety and soundness considering the effect of the pandemic on financial institutions. The message in the guidance is consistent with the supervisory communications with bank management. The pandemic was not anybody's fault, but the reaction to the increased risk both throughout the system and within each institution is critical. Risk management has never been more important, and the management rating largely will be determined by both management's ability and willingness to take the appropriate actions in response to the stress that is caused by these COVID impacts, and whether the new risk has been managed appropriately.

Mr. Thornton's comments focused on protecting the management rating. The agencies encouraged banks to work with borrowers during this difficult time and community banks, including federal savings associations, rose to the challenge. He advised bank management that working with borrowers is important. He said that it is imperative to understand that working with borrowers does not mean turning a blind eye to risk. Some of the small businesses will not survive and it is up to bank management to identify problems early, to the extent possible, and develop workout plans for problem borrowers, and eventually improve or exit those problems. The loan deferrals are intended to help good borrowers survive the pandemic but given the uncertainty, the expectation is that asset quality will deteriorate over the next few quarters as many businesses will struggle, and some may not survive this downturn.

The pandemic affected some borrowers harder than others. For example, in the commercial real estate market, particularly the hotel, retail, and office sectors have been hit. These sectors are expected to experience the most significant decline given the stay at home orders and the travel restrictions and the transition to a virtual workspace. The rising unemployment rate also is expected to impact some sectors of multifamily, particularly in metropolitan areas with high levels of hospitality, retail, restaurant and entertainment jobs. Construction in some areas is expected to decline as many of the projects are dormant or have been operating with skeleton crews. Concentrations are going to play an important role in determining the significance of the impact.

Mr. Thornton reiterated that not all hospitality, retail, or restaurant loans are going to become problems, and each individual situation needs to be analyzed differently. While the stimulus packages helped some good borrowers survive, the same stimulus packages likely mask problems for some borrowers that may have underlying issues. On a positive note, and consistent with what the Committee members report, Mr. Thornton reported that he had heard on calls with examiners and bank management from several cities in the Southern District that about two

thirds of the loans that had been deferred were now being paid back. Many of the loan customers that requested and were approved for these deferrals did so out of an abundance of caution.

As the pandemic progresses there are things that will not change. The OCC continues to use the rating system that considers a bank's size and complexity and risk profile. The CAMELS system and the risk assessment system will not change, and the focus will be on risk management. Risk management is about how well bank management identifies, measures, monitors, and controls risk. Prior to the pandemic, the message to the industry was focused on preparing for the next downturn. In discussions it might have been called preparing for winter, but for the most part it was about risk control, having good policies to ensure appropriate underwriting, controlling the volume of exceptions, monitoring concentration levels and limits, having good systems in place to identify problems with an emphasis on work of frontline staff, and having strong capital, robust allowance, and good liquidity planning.

As a result, the industry entered the pandemic in a good position. Banks generally had strong capital, good liquidity, good asset quality, and reasonable concentration limits and levels. The industry condition was much better than before the last recession. While controlling risk is important, much of the near-term emphasis shifts to identification and measuring.

Ms. Nichols was participating in the meeting for Deputy Controller for the Northeastern District, Beverly Cole. She reported that the Northeastern District continues to have a large number of mutuals who work with customers. During the pandemic, they have been providing forbearances and a number of mutuals participated in the Paycheck Protection Program. In the Northeastern District there were a little over 1.3 billion PPP loans with an average amount of \$3,000.

Ms. Nichols echoed what has by the District Deputy Comptrollers about the process that was used to develop the COVID action plans and the execution and implementation of the plans. The ADCs and examiners continue to focus on the risk management processes and using guidance that has been reiterated by the District Deputy Comptrollers to take positive steps to work with banker management. The primary risk in the Northeastern District is commercial real estate concentration. There is stress in those portfolios. However, there have not been findings that give rise to making changes in strategies or any changes to resource allocation. Commercial real estate, retail, and hospitality loans in New York have been adversely affected. Many businesses closed or shut down temporarily depending the location. Going forward, the focus is on risk management, having conversations with bank management and continuing to monitor the analytics and the information.

Mr. Brickman asked the Committee Members whether they have any feedback on the interaction with their examiners or ADCs or questions about what the District Deputy Comptrollers talked about. Several Committee members reported that they had recently had examinations or were about to begin an examination. Most of the exams were off-site and although there were challenges, once they were resolved, the exams went well. Some of the challenges were technology or scheduling related as bank management and examination teams adjusted to a virtual work environment. Several Committee members had training teams participating during the examinations and those went well. Ms. Kowitt thanked the Committee members who had

training teams and explained that there are about 100 new examiners who had been hired during the past year and that the OCC had the new experience of training them in a virtual environment.

Several Committee members noted that the communication with the exam teams and the Field Offices has been very helpful. They found that the process the described by the District Deputy comptrollers to be accurate. They appreciated the flexibility and communication. Mr. Brickman noted that the interagency guidance on expectations for how the bank regulators will approach examinations in the pandemic should resonate as being reflective the OCC's culture and mindset. Examination reports and findings will describe the factors that are in the bank's control, for example, identifying the deterioration in the credits, working with borrowers to resolve those concerns, compared with the factors that are not in the bank's control. For example, the mandatory closing of local businesses is not in the bank's control. Some business had to shut down for months at a time.

Mr. Brickman asked whether there were any other questions, comments, or feedback for the District Deputy Controllers. He mentioned that the OCC is formulating its budget for the next strategic and operating plan. There have been cost savings to the agency as a result of the reduction in travel due to the pandemic. The agency has been able to reduce assessments over the last several assessment periods. The assessment model allows the agency to continue to increase fees for banks that deteriorate and become problem institutions, which typically offset the cost of increased supervision. The OCC is considering how to handle assessments, given the ballooning balance sheets a lot of bank have experienced as a result of the inflow of deposits from PPP funds and other deposit increases during the pandemic. The agency elected to maintain the total asset calculation fixed at a point in time preceding the pandemic in order to prevent an undue increase in assessments from banks that are working to benefit their communities by participating in the various programs and/or taking the deposits that arise from some of the benefit programs.

Mr. Brickman asked the Committee members whether there are future initiatives or any other ideas they want to talk about today. Several Committee members had already mentioned the continued focus on collaboration and innovation and reiterated that working with the Committee helped to make some of important connections. In the past, the Committee had discussed the concept of what it would take to charter a new mutual savings association. He asked what other topics or other areas the OCC needs to address to help community banks generally and more specifically mutual savings associations.

A Committee member raised the topic of capital and mutual capital certificates. The Committee member suggested that the Committee work with the ABA or other banking trade organizations to try to determine whether mutuals could safely issue capital certificates to raise capital. Mr. Brickman noted that the topic of the ability to raise capital, particularly using mutual capital certificates and other mechanisms, has been raised several times over the years. The OCC has demonstrated willingness to work with Committee members and to provide feedback on instruments that have been proposed. He noted that the OCC will continue to provide input when proposals are presented. The concept is complicated by changes in Basel capital rules. Further, any time there is a change in administration and a new Comptroller, OCC staff must resurface issues that continue to affect a mutual savings association industry. He said that OCC staff would

be happy to engage in that dialogue to the extent that the Committee members have ideas or suggestions for ways forward. Historically the agency has not been willing to go out with a new regulation or special treatment for mutuals when it came to the Basel capital rules. OCC staff are willing to continue to explore alternatives if this Committee wants to make it a priority in the next term or at one of our meetings in the future.

Committee Update

Mr. Brickman reported that the charter of the Advisory Committee had been renewed. The OCC has solicited for nominations of new members of the Advisory Committee. The nomination period has closed, and Mr. Brickman noted that a number of strong candidates to serve on the Advisory Committee been received. The OCC currently is going through the process of reviewing the nominations.

Public Statements, Wrap up and Adjournment

There were no written statements submitted in advance of the meeting. Members of the public thanked the Committee members for the discussion. A member of the public asked a question about the impact of the pandemic and risk assessments on the calculation of assessments paid by OCC-supervised institutions. The discussion during the Advisory Committee meeting addressed the question.

Mr. Brickman adjourned the meeting at 10:40 a.m.

Certification

/s/

Michael R. Brickman
Designated Federal Officer