Issues & Answers

February 2023

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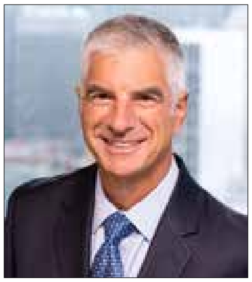
Three Things to do for a More Successful 2023



By Glen Simecek, President and CEO, Washington Bankers Association

All readers of Golf Digest eventually learn to take articles with titles like "Three simple tips to cure your slice!" or "Five easy drills to ensure you never miss a green!" with a grain of salt. For one thing, the tips are never as simple or as easy as advertised. For another, this month's tip all too often is the exact opposite of one they published six months ago. So, it's understandable if the reader is skeptical about golf advice.

In contrast, I'm about to offer you three simple, can't-miss steps to help make you and your bank more successful in 2023 and the years to come.

First, you and key leadership team members should strongly consider joining the Society of Bank Executives. The Society is a relatively new program that provides senior bank executives with opportunities to enhance their leadership skills and build a valuable and vibrant network of peers, not just here in Washington but also across the country. All banks face serious challenges – from economic uncertainty to increased competition to technological upheaval –and the ability to exchange ideas with your peers can help you thrive in the unique and rapidly changing banking landscape.

The feedback we received from last year's pre-session launch was extremely positive. The program includes a mix of virtual and in-person sessions. While the first one has already been held, you can join at any point in the series. To learn more, go to www.executives.bank/home.

The second step you should take is to make plans to attend our first-ever Engage Conference, which will be held May 4-5 at the Washington Athletic Club

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Issues & Answers – February 2023

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Call us at (206) 447-1700 and visit us on the web at www.wabankers.com.

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On the Cover

Sail boats participate in an annual regatta around the San Juan Islands, as seen from the southern tip of the Island, featuring Cattle Point Lighthouse.

Photo by Megan Managan

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in Seattle. This conference will combine elements of our Education/Human Resources Conference and our Retail Sales & Leadership Conference into one larger event, bringing together more bankers dealing with similar workplace issues.

The conference will offer breakout tracks focused on each audience segment, including retail bank management, human resource directors, and training and education coordinators, ensuring that all attendees will still receive the kind of customized information they've come to expect from our events.

Lisa Fain, the CEO of the Center for Mentoring Excellence, is one of our keynote speakers and will be covering mentorship programs – how to establish them and enhance their effectiveness. It's a message that will be valuable to line managers and HR professionals alike. For more details, visit www.wabankers.com/engage.

You might be interested to note that we're doing something similar in the fall with the Credit & Lending Conference, expanding the audience to include credit administrators and lenders. Look for more details on that conference coming soon.

Finally, you register now to attend our annual Convention (www.wabankers.com/convention/), which will be held in Sunriver, Oregon, on June 26-28. Once again, WBA members will join banking colleagues from the Idaho, Nevada, and Oregon Banking Associations. Your 2023 dues include complimentary registration for the Convention. WBA bank members get complimentary registration that was included in their 2023 dues. It's a great event that provides timely information and fosters stronger connections among bankers throughout the West, and we hope to see you there.

Last year's Convention demonstrated how strongly bankers want to attend WBA events in person. So, our goal this year is to deliver as many events as possible in person, even if they look a little different than pre-COVID. No matter how our professional development and conference programs continue to evolve, we will always be working to maximize the benefits they provide for our members.

Not unlike those golfers working on their games.

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Beating Back a Bad Idea: How Bankers United to Play Defense Against Durbin Expansion

By Rob Nichols, President & CEO, American Bankers Association

There's a saying that "everything old is new again," and that's certainly an adage you can bank on in Washington, D.C.—especially when it comes to poor public policy proposals.

A textbook example of this unfolded during the 117th Congress, when our industry found itself once again facing a bad idea that we thought had been soundly defeated: placing restrictive routing mandates on credit cards, like those imposed on debit cards by the Durbin Amendment over a decade ago. The idea came in the form of a bipartisan bill—the so-called Credit Card Competition Act—introduced in the Senate by Sens. Dick Durbin (D-Ill) and Roger Marshall (R-Kan.) and in the House by Reps. Peter Welch (D-Vt.) and Lance Gooden (R-Texas).

Bankers know all too well that the 2010 Durbin Amendment had disastrous consequences for banks and their customers: it increased the costs of checking accounts and debit cards and ultimately led to the elimination of popular debit card rewards programs. The Durbin Amendment's most damaging provisions apply to banks of all sizes, causing a nearly 25% cut in the per-transaction debit card revenue earned by banks with under $10 billion in assets. At the same time, it helped line the pockets of large retailers who talked a big game about passing savings on to consumers—but 10 years' worth of data tells us that simply isn't what happened. In fact, the Federal Reserve published a study finding that only 1% of merchants lowered prices for consumers since the Durbin price controls took effect.

What's more, the Credit Card Competition Act also goes several steps further than the Durbin amendment—not only would it require banks to add a second network to their customers' cards, but it would limit them to options set by the Fed, unlike the Durbin Amendment, which allowed banks to choose between any two unaffiliated networks. The Credit Card Competition Act also requires banks to accept virtually any kind of transaction—functionally requiring them to onboard potentially many more than two networks, even networks that don't meet basic data security standards.

Given the potentially catastrophic effect the bill could have on community banks and bank customers—while providing no tangible cost savings or benefits for consumers—the industry sprang into action to set the record straight.

Immediately following the bill's introduction, ABA led a coalition of eight national financial services trade groups in issuing a statement of strong opposition to the bill. We then followed

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Help Managers Grow Careers & Knowledge with Management Development Program

If retaining and recruiting top employees are the industry's biggest challenges this year, the WBA's 2023 **Management Development Program** can be a solution in your toolbox.

Helping managers grow their understanding of their role within the organization and their leadership skills will help the organization attract and retain the talent needed to be successful. The Management Development Program begins in April and features six sessions on various topics important to managers.

The program covers the current state of the banking environment and why managers need to understand the larger picture, the importance of emotionally intelligent leadership, performance management to develop, train and retain future leaders, effective interpersonal conflict and negotiation, and communication for results and employee engagement.

The MDP will begin in April and features in-person and virtual sessions.

WBA will also offer the **Credit Analyst Development Program** and **Retail Branch Manager Development Program** beginning in the fall.

On the conference side of WBA's educational events, the **2023 Northwest Compliance Conference** will be held March 16-17 at the DoubleTree Hotel, Seattle Airport. This two-day event focuses on all that compliance professionals need to know about changes in the industry.

Also, on March 17, the V**irtual Northwest Bank Directors Series** will begin. This program, offered by the Oregon Bankers Association, provides new and experienced bank directors with continuing education and updates on the latest industry trends. Directors can register for the entire nine-session program or pick and choose the sessions.

This year, WBA is again co-sponsoring the A**merican Mortgage Conference**, hosted by the North Carolina Bankers Association and the ABA on May 1-3 at Wild Dunes Resort on Isle of Palms in South Carolina. This conference is the premier event for the mortgage industry in the country. It brings together leaders from banking, mortgage, policymakers, and investors to share information about the latest issues, analyze changes, and more.

On May 4-5, WBA will host the newly revamped **Engage: Retail Banking, Training, and Engagement Conference** at the Washington Athletic Club in Seattle. This conference will include tracks focused on each bank area. The combined conference will also bring together bankers who often work closely together daily. The agenda will consist of Lisa Fain, CEO of The Center for Mentoring Excellence, with a 90-minute workshop on mentoring.

On May 11-12, the WBA is co-sponsoring the Idaho and Oregon Bankers Association **Annual Agriculture Conference**. The 2023 event features Dr. David Kohl, a nationally-regarded speaker on agriculture banking topics, and Mike Pearson, the host of Agriculture of America!, a weekly show about all things agriculture.

Moving into autumn, WBA will also host the **Credit and Lending Conference** on September 7-8 at the Washington Athletic Club. Previously the Senior Credit Conference, this event has been expanded to include lenders and will cover topics relating to the economy, current credit, lending regulations, and more.

In honor of Cybersecurity Awareness Month in October, we will host the **Virtual Financial Technology and Security Conference** on October 23-24, co-sponsored by the New Jersey and North Carolina Bankers Association. This event brings IT, operations, and security professionals from across the industry to discuss innovation and learn about the latest in the industry.

Please visit the WBA website at www.wabankers.com for more information about registration for our upcoming programs.

Registration is Now Open for 2023 Annual Convention

Registration for the 2023 Annual Convention, co-sponsored by the Idaho, Nevada, Oregon, and Washington Bankers Associations, is now open!

This year's event will be held June 26-28 at the gorgeous Sunriver Resort in Sunriver, Ore., and brings together bankers from throughout the Western U.S. to learn about the latest in the industry.

Last year's event sold out, so don't miss out on your opportunity to secure a spot early. Learn more and register online at www.wabankers.com/convention.

Events Calendar

March 16-17 – 2023 NW Compliance Conference, DoubleTree Hotel, Seattle Airport

May 4-5 – Engage: Retail Banking, Training & Engagement Conference, Washington Athletic Club

April 13 – Management Development Program

May 1-3 – American Mortgage Conference, South Carolina

May 11-12 – IBA, OBA, WBA Agricultural Banker Conference

June 26-28 – 2023 Annual Convention, Sunriver Resort

Sept. 7-8 – Credit & Lending Conference, Washington Athletic Club

October 23-24 – Virtual Financial Technology & Security Conference

To register or to learn more about any of the listed events, please visit www.wabankers.com/calendar.

Bankers Day on the Hill Returns to Capitol Campus

WBA Advocacy

In late January, 50 bankers gathered in Olympia for the first in-person Bankers Day on the Hill since early 2020, before the beginning of the pandemic.

During the event, bankers spent part of the morning learning about the legislative process and the banking industry's top issues. Following the briefing, the attendees headed to the Legislative offices, where they met with their local representatives and senators, discussing issues related to lien priority, first mortgage interest deduction, and more.

Attendees were also encouraged to share with lawmakers their work in their community and showcase how connected the banking industry is to their local economies. Both bankers and lawmakers were excited to meet again in person, and a quieter than normal Capital Campus,\ provided the bankers with ample face time to discuss banking issues.

Thank you to all of the bankers who participated in this year's event and for continuing to advocate on behalf of the industry. The WBA will continue providing its' Legislative Update weekly email throughout the Legislative Session and will be hosting Legislative Roundtables in the fall to again meet with lawmakers.

If you want to learn more about WBA Advocacy or how to participate, please reach out to Megan at megan@wabankers.com.

WBA Member News

Bankers Care

Olympia Federal Savings Participates in Homes First Purchase

At the end of 2022, Olympia Federal Savings was one of several organizations which helped Homes First make a third purchase of a local home.

The property, which will be used for three adults with developmental disabilities, was made possible by various partnerships, including the Washington State Department of Commerce Housing Trust Fund, Thurston County Public Health, the City of Olympia, and Olympia Federal Savings.

First Financial Northwest Bank Donates to The Salvation Army Renton Corps

In late 2022, First Financial Northwest Bank announced it made a $600 donation to The Salvation Army Renton Corps as part of the two organization's 53-year partnership.

HomeStreet Bank Donates to Low-Income Housing Institute

As part of HomeStreet Bank's program to honor volunteer work by employees, the bank announced a $2,500 donation to the Low Income Housing Institute (LIHI)

Zsuzsanna Larson regularly volunteers with the organization, which develops, owns, and operates housing to benefit low-income, homeless, and formerly homeless people in the state. LIHI also advocates for housing policies at the local and national levels and administers a range of supportive service programs to help those in need maintain stable housing.

Liberty Bank Hosts Food and Toy Drive for Pets During Holidays

During the holiday season, Liberty Bank hosted a pet supply drive, collecting food, treats, and toys for local animals in need.

The supplies were donated to Fishline, the area's local

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food bank, to be distributed in the community.

The bank also hosted its annual ugly sweater contest in honor of the season.

Olympia Federal Savings Donates to Thurston County Food Bank

In December, the Olympia Federal Savings Two-Cent program partner was the Thurston County Food Bank.

At the end of the month, the bank donated $2,850 to the organization to help local neighbors eliminate hunger within the community.

Washington Trust Bank Participates in Clothing Drive

At the Washington Trust Bank's Smokey Point branch, Melissa Cox, the branch manager, is a regional board member for Housing Hope. During the holidays, the branch hosted a clothing drive to help local families in need.

Over 250 boxes of clothing were donated this winter to the organization, which serves and operates over 500 affordable housing units in Snohomish County and Camano Island.

Columbia Bank Raises $277,000 During Warm Hearts Winter Drive

This winter, Columbia Bank hosted its eighth annual Warm Hearts Winter Drive, collecting donations of money and items to be given to local homeless shelters.

In total, the bank raised $277,817 for local shelters and has raised more than $2 million throughout the program's eight years.

Cashmere Valley Bank Donates to Spirit Therapeutic Riding Center

The Cashmere Valley Bank Ellensburg branch, recently donated to Spirit Therapeutic Riding Center in Ellensburg, donating funds raised through the ban's denim fund.

Every Friday, the team at CVB can wear jeans for a $1 donation to the branch's denim fund. Throughout the year, the branch chooses where to donate the money raised, and the bank matches the amount.

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Industry News

New Hires

Sarah Avery
Corporate & Institutional Banking, Washington State at PNC Bank

Matt Johnson
Senior Loan Officer at 1st Security Bank of Washington

Amy Currie
Loan Officer and Production Partner at 1st Security Bank of Washington

Diana Meacham
Mortgage Loan Officer at Banner Bank

James Hoyt
Relationship Banking Assistant at Heritage Bank

Sheila Ponder
Accountant Assistant at Olympia Federal Savings

Kendall Thompson
Universal Operations Assistant at Olympia Federal Savings

Art Drayton
Universal Banker at Olympia Federal Savings

Kelsey Cooper
Loan Closer at Olympia Federal Savings

Taryn Paulsen
Residential Loan Officer at Banner Bank

Kerri Schroeder
Managing Director and Region Manager at JPMorgan Chase

Bryan Dent
Vice President and Relationship Manager at Washington Trust Bank

Mario Zink
Business Banking Team Leader at Columbia Bank

James Miller
Vice President and Commercial Banking Officer at Commencement Bank

David Evans
Vice President and Commercial Banking Officer at Commencement Bank

Amanda Bowes
Assistant Vice President and Senior Loan Administrator at Commencement Bank

Kevin Bedlington
Vice President and Relationship Manager at Washington Trust Bank

Promotions

Jason Morgan
Assistant Branch Manager at Kitsap Bank

Matt Ray
Executive Vice President and Chief Lending Officer at Heritage Bank

Amy Curran
Executive Vice President and Director of Commercial Banking at Heritage Bank

Kelli Wilson
Executive Vice President and Chief Banking Officer at Heritage Bank

Sabrina Robison
Executive Vice President and Chief Human Resources Officer at Heritage Bank

Tyson Romanick
Vice President at Baker Boyer Bank

Matt Sursely
Vice President at Baker Boyer Bank

John Adams
Assistant Vice President at Baker Boyer Bank

Amanda Anderson
Assistant Vice President at Baker Boyer Bank

Eric Denney
Assistant Vice President at Baker Boyer Bank

Elise Joblonski
Assistant Vice President at Baker Boyer Bank

Becky Kettner
Assistant Vice President at Baker Boyer Bank

Molly Neal
Assistant Vice President at Baker Boyer Bank

Nick Punch
Assistant Vice President at Baker Boyer Bank

Dan Gaulke
Executive Vice President and Treasurer at Yakima Federal Savings & Loan

Kyle Harrington
Vice President and Accounting Manager at Yakima Federal Savings & Loan

Lotti Biehl
Assistant Vice President and Branch Manager at Yakima Federal Savings & Loan

Tony Mayorga
Assistant Vice President and Branch Manager at Yakima Federal Savings & Loan

Erin Thierolf
Assistant Vice President and Human Resource Generalist at Yakima Federal Savings & Loan

Paul Crawford
Assistant Vice President and Marketing Manager at Yakima Federal Savings & Loan

Paul Crawford
Commercial Relationship Manager at Heritage Bank

Board of Directors

Lynn Terwoerds
First Fed Bank

Have Industry News to share with WBA? Email megan@wabankers.com or call (206) 344-3472.

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The Riding Center provides equine-assisted activities to individuals with physical, emotional, and learning disabilities, senior citizens, and challenged learners.

HomeStreet Bank Donates to Mukilteo Youth Soccer Club

HomeStreet Bank announced a $500 donation to the Mukilteo Youth Soccer Club.

The donation was made in honor of employee Amy Myhre who volunteered 31 hours with the club.

North Cascades Bank Hosts Winter Gear for Kids Drive

The North Cascades Bank Grand Coulee branch recently hosted a Winter Gear for Kids Drive, collecting warm gear for local children.

The pile of donated items was delivered to the Grand Coulee Dam School District to be distributed to anyone in need this winter.

Commencement Bank Hosts Donation Drives in December

Throughout December, Commencement Bank branches hosted several donation drives, collecting food and pet supplies at various branches.

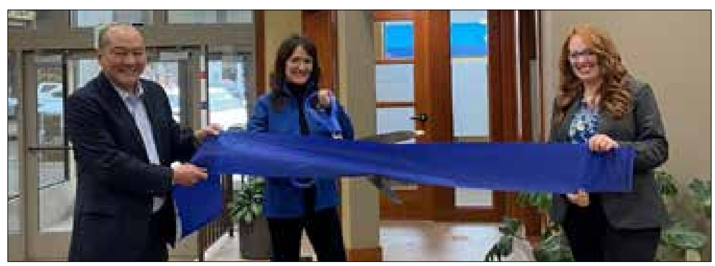
"Whether it was one can of soup or the whole kitchen pantry, you helped to support our local communities, and we are so grateful," the bank said online. "Thank you for helping us make a difference this holiday season."

U.S. Bank Employee Volunteers on Martin Luther King Jr. Day

A Seattle area U.S. Bank team member spent Martin Luther King Jr. Day volunteering with his family in King County.

The bank provides time for employees to volunteer and serve the local community, which Shad Bris' family did at a local elementary school.

The group of over 250 volunteers, which included volunteers from City Year and Starbucks, painted murals at the school.



Baker Boyer Bank Becomes Blue Zone Certified Workplace

In early 2023, Baker Boyer Bank announced that it had become a Blue Zone-certified workplace.

The Blue Zones Project is a community well-being improvement initiative to change the change people experience the world around them.

Walla Walla is the first community in Washington to participate in the program.

PNC and Mariners Participant in Event at Elementary School

The Seattle PNC team and Seattle Mariners Dream Team recently participated in an assembly at Evergreen Heights Elementary with the Mariners Moose.

The team talked to students about the importance of the DREAM principles, which include drug-free, respect for yourself and others, education, attitude, and

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motivation to help them achieve their dreams.
PNC sponsors the program throughout the year.

1st Security Bank of Washington Employee Volunteers with Washington Therapy Doodles

1st Security Bank of Washington employee Kheesha recently volunteered with the Washington Therapy Doodles during their #12DayofGoodness with the Seattle Seahawks.

The dogs and organization worked to spread joy and positivity throughout the community.

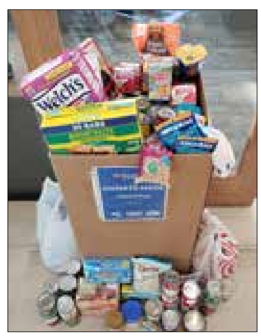
HomeStreet Bank Donates $1,000 to Ballard Food Bank

HomeStreet Bank donated $1,000 to the Ballard Food Bank in honor of a volunteer from the bank.

The donation was made in honor of Nathan Messerschmidt, who regularly volunteers at the food bank.

Peoples Bank Named Business of the Year by Mount Vernon Chamber

In January, the Mount Vernon Chamber of Commerce named Peoples Bank the Business of the Year.



Yakima Federal Savings Hosts January Food Drive

Throughout January, Yakima Federal Savings hosted a food drive benefiting Northwest Harvest and Second Harvest.

The bank collected food items at all branches to help the community in need.

1st Security Bank of Washington Donates to Port Townsend Food Bank

1st Security Bank of Washington donated $6,393 and a large bin of food items to the Port Townsend Food Bank earlier this year.

As part of the bank's annual food drive, customers and community partners provided donations to help local residents in need.

If you have WBA member news to share about work being done in your local community, please send it to Megan Managan at megan@wabankers.com.

Tax Time Turbulence: How Families and Banks Can Manage Tax Refunds

By Chris Phelan, Director Sales Strategy and Analytics, Vericast

Taxes are one of life's few certainties. It is that time of the year again. The tax filing season starts sometime in late January and lasts till the 18th of April. Most American households will be eligible for refunds, and if you are early in filing your taxes, you might receive your tax refund as early as mid-Februrary.

Tax refunds amount to six weeks' take-home pay for the average family receiving them. That's a considerable amount that can reset a family's spending level by creating a savings buffer that the family can rely on for the rest of the year.

Typically, banks and credit unions find themselves flushed with cash once tax refunds start flowing in. However, this year might be different as tax refunds are expected to be smaller in 2023 because there were no federal stimulus payments in 2022.

This is going to coincide with the highest inflation rate in a generation and possible recession. Consumers are going to be feel the squeeze, and every dollar, or the lack of it, counts in such challenging times.

For banks and credit unions, tax refund season presents an opportunity to educate their customers and help them better plan their spending to improve their savings and credit history.

Here is how Financial Institutions can help people make better financial decisions this tax refund season:

Highlight Savings

Savings is the buzzword. The pandemic made people realize the frailty of living paycheck to paycheck. So the desire to save is back in vogue.

Considering the last recession, which was ended in 2009, a study by the National Retail Federation stated that 48% of consumers surveyed planned to use their refund to pay down debt, whereas 39% planned to use it to build their savings. Moreover, even during the pandemic, i.e., between 2020 and 2022, the most popular use of refunds was to build savings (50% in 2020, 54% in 2021, and 51% in 2022).

While many previously used tax refunds to bulk up savings, this year might be different. Though people want to save, they might not be able to save owing to the current economic scenario and looming rate hikes by the fed to tamper spending in the coming three quarters.

In 2023, tax refunds may be used to pay off existing debt and to meet day-to-day expenses to offset rising prices.

This is the time to show people how to save using innovative methods. Banks and credit unions can highlight savings by educating their customers to refinance their credit card debt, to seek out ways to earn interest on their cash balance, to avoid interest where they can by pre-paying their loan or paying their credit card bills on time, etc.

It is important to note that thisis more than just saving dollars and cents. FIs should connect personally to explain what each extra dollar saved would mean for their family and its future. This will motivate customers to save even by foregoing certain expenses.

Incentivize Customers

People are looking to minimize their cost of living by downsizing and looking for deals and discounts to save money. Some are purchasing smaller cars and homes, are looking for used items and second-hand consumer durables when they usually would have bought new goods. The public may be willing to forego brand order to find the most cost-effective deal for a product or service.

In this economic scenario, it is essential to incentivize consumers to increase account usage and to motivate them to stay loyal to your establishment. FIs have tried including cash-bonus upgrades, cross-selling, referral offers and incentives, etc., to incentivize customers. Banks have linked individual transactions to vari-

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Preparing Your Bank to Manage Loan Workouts, Loan Modifications

By Mary Ellen Biery and Kylee Wooten, Abrigo

Now's the time to prepare for managing increased loan workouts and loan modifications.

Loan performance since the pandemic has remained strong across many U.S. financial institutions in recent quarters, but banks and credit unions are boosting provisions for credit losses in anticipation of tougher times ahead.

In addition, prudential regulators have repeatedly encouraged financial institutions to include loan modifications in their actions to mitigate adverse effects on borrowers resulting from extreme weather, COVID-19, rising interest rates, inflation, or other conditions. They've highlighted specific concerns about credit risk management practices, particularly for commercial real estate (CRE).

Below are several tips for banks and credit unions looking to get ready to handle potential loan modifications or even loan workouts so they can maintain strong credit risk management.

Workout volumes are low now, but indicators point to more ahead

Despite the low volume of modifications at many institutions since the pandemic began, signs point to increased activity in the quarters ahead.

Overall, FDIC-insured commercial banks and savings institutions aren't seeing dramatic increases in net charge-offs (Chart 1) or rates related to declining asset quality (Chart 2), such as past-due rates and rates for non-current loans. However, institutions in recent quarters are seeing some indicators of weakening asset quality.

What's behind the loan modification outlook?

"Right now… most institutions aren't seeing increased charged-off loans," said Abrigo Advisory Consultant Zach Englert. "The only real deterioration we're starting to see is in subprime auto and credit card portfolios." Even as news headlines announce that "the sky is falling," many Abrigo clients are relaying they can count only six or seven charge-offs since 2015 or so, he added.

Nevertheless, some clients have said they recognize that more loan workouts could be on the horizon. Among the factors behind these concerns are:

- inflation's impact on costs
- higher interest rates
- labor shortages resulting in the use of higher-cost, outsourced labor
- proactive hedging on supplies that can put stress on liquidity.

Earnings reports also point to some deterioration in asset quality. Several institutions in recent weeks have reported that third-quarter non-performing loan rates ticked higher this year, despite being flat or in some cases below rates from a year earlier.

In addition, financial institutions in the third quarter have boosted provisions to create increased allowances for credit losses, whereas a year ago, the release of previous provisions was benefitting net income.

In a recent Abrigo survey, more than three-quarters of C-level, credit management, and credit administration staff identified credit stress on current loans as a concern given the current rising interest rate and credit risk environment. Almost half of the nearly 200 bankers surveyed said they are concerned about an increase in modifications, workouts, and charge-offs, and 62% identified needing to enhance current credit risk management analyses and processes as a concern given the environment.

Meanwhile, regulators are focusing fresh attention on prudent credit risk management of loans, especially CRE, and loan modifications in general.

Regulators foster prudent loan modifications

Loan modifications include, but aren't limited to, a forbearance agreement, a new repayment plan, or interest rate modification. More extensive loan workouts can include a renewal or extension of loan terms, an extension of additional credit, or a restructuring with or without concessions.

Loan modifications have played an important role in the ability of borrowers to endure the impact of the pandemic, and regulators continue to urge banks and credit unions to work prudently with borrowers facing stress.

In 2020, federal and state banking regulators eased pressure on coronavirus loan workouts, urging financial institutions to work with their borrowers and members affected by COVID-19. Agencies agreed that these FIs would not be required to categorize as troubled debt restructurings (TDRs) those loan modifications made in good faith in response to COVID-19.

Under normal circumstances, a modification would generally be considered a TDR when the new terms represent a concession – terms that are not market-available. The TDR designation prompted a requirement for separate accounting using discounted cash flow models.

More recently, regulators' proposed Interagency Policy Statement on Prudent Commercial Real Estate Loan Accommodations and Workouts reiterated that in some cases, financial institutions may want to work with creditworthy CRE borrowers who remain willing to repay debts even if they face "diminished operating cash flows, depreciated collateral values, prolonged sales and rental absorption periods, or other issues that may hinder repayment." Comments on the proposal were due Oct. 3.

Interagency guidance during COVID said examiners would not criticize a financial institution's attempt to help borrowers impacted by the pandemic if the assistance was a part of a risk mitigation strategy intended to improve an existing loan that is beginning to display credit weakness. This principle was reaffirmed in the recently proposed policy on CRE loan accommodations and workouts.

The proposed updated policy statement also incorporates the Financial Accounting Standards Board's (FASB) recent move to eliminate separate TDR accounting for institutions that have adopted CECL, the current expected credit loss model for reporting credit losses. Under CECL, certain modifications tied to a borrower experiencing financial difficulty will instead be labeled as modifications and have enhanced disclosure requirements.

Keen regulatory eye on CRE, stress testing

Despite encouraging banks and credit unions to work with borrowers facing stress, regulators have repeatedly signaled a continued focus on credit risk management practices.

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this up with numerous letters, op-eds, grassroots calls to action and co-branded ads with the Texas and Kansas bankers associations that ran in their respective districts. The efforts were amplified by an op-ed from the Florida Bankers Association and a creative "Don't Let Congress Steal Your Credit Card Rewards!" social media campaign from the Missouri Bankers Association. In early December, we then expanded that effort into an all-out media blitz to stave off any last-minute efforts to attach the bill to a must-pass piece of year-end legislation.

Every step of the way, our efforts at the national level were complemented by robust advocacy efforts by our partners at the state bankers associations, who stepped up to make calls, attend Washington fly-ins, pen letters and columns, and even appear on national TV to address our concerns about the bill. Together, we blanketed Capitol Hill with a succinct, united message: the Credit Card Competition Act is terrible public policy that should not be enacted.

Our combined efforts proved the hollowness of this bill—it failed to attract a single cosponsor beyond the initial two in both the House and Senate or gain enough support to advance as a standalone measure and was successfully blocked from any other bills moving through Congress as the lame-duck session came to a close.

This win underscores the tremendous value of our state association alliance and demonstrates the power that our industry can have when we unite behind one message. It's also an important reminder about vigilance.

We can't say for certain whether and how these bad ideas will rear their heads again in Congresses to come. But what we can say is that if they do, our industry will be ready to respond.

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ous giveaways and sweepstakes to motivate people to transact using their bank accounts.

Here are some examples of how FIs introduced incentives and used social media to amplify their reach.

- **Money Talks:** Use monetary incentives to refer customers from loyal members. Cardmembers can be sent a $20 statement credit after spending $100 for each new family member or friend they refer. Make sure to start your email with a message of gratitude.
- **Go the Extra Mile (literally and figuratively)**: Reward cardholders with extra points or miles after each successful referral they recruited and get them going, and redeeming, sooner.
- **Sweepstakes Create Excitement**: You can also count individual purchases as entries to various sweepstakes to keep cards top of the wallet and incentivize spending. A card swipe for a chance to earn big will be well received. Plus, it will drive increased card usage.

Educate Customers With Your Connections

For FIs to gain traction, there are no alternatives to this option. Banks and credit unions will have to take up educational campaigns to help people understand the financial concepts and, in turn, gain their trust and confidence.

Topics related to improving individual financial health, budgeting, keeping credit-card debt in check, investments and personal finance are garnering a lot of attention. FIs can benefit by offering investment advice, tips for building better credit for gaining consumer attention and trust.

Does your FI have an investment arm or partnership? Provide your customers investment advice through your partnerships to help them through current inconsistent and changing market conditions.

Other FIs offer customers helpful information, interactive videos, and simulators through a partnership to help improve customers' credit health.

Banks Can Make the Most of The Tax Refund Season By Simply Helping Customers

We are all in this odd economic climate together. Therefore, for FIs to benefit from this tax refund season, they will have to help their customers achieve their financial goals. This will help FIs grab a share of the consumer wallet and retain customers.

To get deeper insights into the minds of your customers with our 2023 Consumer Outlook report.

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"Market and external conditions are changing the credit risk environment rapidly," the 2023 OCC Bank Supervision Operating Plan said. "Examiners should evaluate banks' actions to manage credit risk given volatile changes in market conditions, interest rates, and geopolitical events, as well as supply chain disruptions and areas of continued weakness from the pandemic such as urban commercial real estate performance (office, hotels, and retail). Supervisory efforts should focus on risk management functions to determine whether there is appropriate credible challenge. Examiners should evaluate banks' stress testing of adverse economic scenarios and the implications, such as amplified impacts to retail and commercial borrowers experiencing increased operating and borrowing costs at loan origination, at renewal, or over the term of the credit."

Managing commercial real estate (CRE) credit risk, especially managing CRE loan modifications and workouts, has received particular emphasis from regulators. Noting that 98% of banks engage in CRE lending, the FDIC has said CRE loans are the largest loan portfolio type for nearly half of all banks, and CRE loan volume (in dollars) is at a historic high.

According to a recent edition of the FDIC's Supervisory Insights publication, examiners in the upcoming cycle will prioritize resources "toward areas presenting the highest risk at an individual bank, which often includes significant CRE lending concentrations." Among other things, examiners will "assess management's ability to implement prudent credit modifications and underwriting, maintain appropriate loan risk ratings, designate appropriate accrual status on affected loans, and provide for an appropriate reserve for credit losses."

Given the environment and regulatory emphasis, financial institutions across the country should establish effective plans for managing loan workouts and modifications.

Create a plan to manage problem loans

So what can a financial institution do to prepare for an increased volume of loan modifications or loan workouts?

Abrigo advisors note that successful, high-performing financial institutions will:

1. Review and update as necessary their policies, processes, and procedures for loan modifications or loan workouts. "If you haven't updated your policies and procedures or dusted them off in 5 or 7 years, the time is now," said Abrigo Advisory Services Senior Advisor Paula King, who has assisted institutions with policy reviews and updates.

2. Add training on loan modifications and workouts. Many staff members may have joined since 2015 and therefore, lack experience working on modifications.

3. Review any system to manage requests or identified loans at elevated risk. This assessment will help ensure the bank or credit union can prioritize loan accommodation needs and manage the associated risk while maintaining profitability. Automated loan modification can save time and improve efficiency, King said. Importantly, loan modification software can ease the burden of the numerous, highly manual steps typically involved in modifications and workouts. King and an Abrigo client discussed loan modification management advice in detail during a recent webinar on credit risk management.

Among prudent risk management practices for short-term loan modifications that were outlined in the proposed policy on CRE lending:

- Updating and assessing financial and collateral information
- Maintaining appropriate risk grading and ensuring proper tracking and accounting for loan accommodations
- Obtaining proper management approvals
- Having timely and accurate reporting and communication.

Automated models also enable institutions to better understand how much revenue a bank or credit union could lose based on different scenarios. This can be achieved using a discounted cash flow model that reflects missed, deferred, or interest-only payments, for example.

More planning advice for managing loan modifications, workouts

Abrigo Senior Advisor Rob Newberry has noted that lenders with successful strategies for managing credit risk related to loan modifications also incorporate the following:

- Specific legal expertise in crafting agreements. As these agreements override the original loan documentation, the lender can gain more flexibility to call the loan or require additional collateral based on the new terms and covenants of the workout agreement.
- Methods to include and track additional review and due diligence on the borrower's existing loan documents
- Straightforward, measurable new terms and covenants for the borrower
- Expectations outlined to ensure the borrower has the ability – and desire – to follow through
- Borrower's potential recovery of their equity position tied to the par recovery of the original loan profitability basis, at minimum. Present-value recovery for the financial institution can inform an argument that the new terms do not represent a concession.
- Negotiation between impacted customers and personnel who have a direct interest in the health of the financial institution
- Timely, authoritative, accurate information on the state of the borrower, with all participants on the lender side communicating the same message
- "What-if" scenario stress testing to examine the impact on the portfolio and capital levels if charge-offs increase as expected.

Getting prepared for additional volume in loan modifications and workouts is especially vital for smaller, less complex lenders that lack the resources of large financial institutions. Taking steps now will help these banks and credit unions provide personal, prudent service while scaling institutional resources to handle added volume.

Mary Ellen Biery is Senior Strategist & Content Manager at Abrigo, where she works with advisors and other experts to develop whitepapers, original research, and other resources that help financial institutions drive growth and manage risk. Kylee Wooten manages and writes articles, creates digital content, and assists in media relations efforts at Abrigo.

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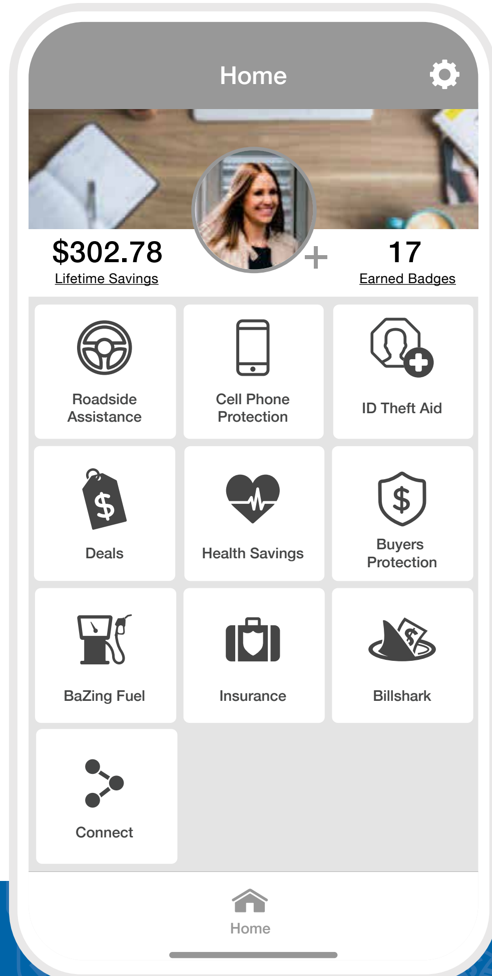

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