The Meeting of the Advisory Committee on Community Banking

of the

Federal Deposit Insurance Corporation

Federal Deposit Insurance Corporation Building

Washington, D.C.

Open to Public Observation via Webcast

October 28, 2020 – 1:00 P.M.

The meeting of the FDIC Advisory Committee on Community Banking (Committee) was called to order by Jelena McWilliams, Chairman, Federal Deposit Insurance Corporation (FDIC) Board of Directors.

Committee members present at the meeting: Shaza Andersen, Chief Executive Officer (CEO), Trustar Bank, Great Falls, Virginia; Dick Beshear, Chairman, President and CEO, First Security Bank and Trust Company, Oklahoma City, Oklahoma; Fred DeBiasi, President and Chief Operating Officer (COO), Valley Central Bank, Liberty Township, Ohio; Keith Epstein, Executive Vice President and CEO, Roxboro Savings Bank, SSB, Roxboro, North Carolina; Sarah Getzlaff, CEO, Security First Bank of North Dakota, New Salem, North Dakota; Stephen Hayes, Chairman and President, Dakota Prairie Bank, Ft. Pierre, South Dakota; James J. Edwards, Jr., CEO, United Bank, Zebulon, Georgia; Kenneth Kelly, Chairman and CEO, First Independence Bank, Detroit, Michigan; Bruce Kimball, President and CEO, First Community Bank of the Heartland, Clinton, Kentucky; Thomas Leavitt, President and CEO, Northfield Savings Bank, Northfield, Vermont; Lori Maley, President and CEO, Bank of Bird-in-Hand, Bird-in-Hand, Pennsylvania; Patty Mongold, Chairperson, President and CEO, Mt. McKinley Bank, Fairbanks, Alaska; Gilbert Narvaez, Jr., President and CEO, Falcon International Bank, Laredo, Texas; Mark Pitkin, President and CEO, Sugar River Bank, Newport, New Hampshire; Alan Shettlesworth, President and COO, Main Bank, Albuquerque, New Mexico; and Louise Walker, President and CEO, First Northern Bank, Dixon, California. All Members attended via videoconference.

Committee members absent from the meeting: Teri Messerschmitt, President and CEO, South Ottumwa Savings Bank, Ottumwa, Iowa; and Cathy Stuchlik, Chairwoman and President, Clackamas County Bank, Sandy, Oregon.

Director Martin J. Gruenberg attended the meeting. Corporation staff in attendance: James L. Anderson, Zachary Anderson, Shannon M. Beattie, Mary Calkins, John Conneely, Kymberly K. Copa, Brian Cox, Chad R. Davis, Doreen R. Eberley, Diane Ellis, Pamela Farwig, Jasa J. Gitomer, Shannon Greco, Patricia S. Gurneau, Isaac Hernandez, Travis Hill, Angela Hinton, Daniel Hoople, M. Anthony Lowe, Christopher Lucas, Samuel Lutz, Brandon Milhorn, Jonathan Miller, Rae-Ann Miller, Kathy Moe, Shayna Olesiuk, Mark E. Pearce, Harrel M. Pettway, Nicholas J. Podsiadly, Jon Pogach, John Rieger, Lisa K. Roy, Betty Rudolph, Mark Savi, Michael Shaheen, James P. Sheesley, Mona Thomas, John F. Vogel, and James Watts.

Jocelyn Sutton attended from the Consumer Financial Protection Bureau.

William Briggs, Dianna Seaborn, and Susan Streich attended from the U.S. Small Business Administration.

Chairman Jelena McWilliams opened and presided at the meeting. Chad R. Davis, Deputy to the Chairman for External Affairs and the Committee's Designated Federal Officer, moderated the proceedings.

Introductory Remarks

Chairman McWilliams welcomed members to the Committee's second virtual meeting, noting that much had happened in the months since the Committee last met, and that the FDIC is working hard to ensure community banks can continue the business of banking amidst dire pandemic circumstances and unprecedented business closures. She welcomed new Committee member Stephen Hayes, Chairman and President of Dakota Prairie Bank, Fort Pierre, South Dakota, then introduced Mr. Davis as moderator.

Mr. Davis invited opening comment from Director Gruenberg, who thanked members for their participation, and said he looked forward to hearing their current experiences and their outlook on the upcoming months.

Community Banking Conditions

Mr. Davis then introduced a roundtable discussion of community banking conditions. The Committee members discussed a range of trends and issues related to local banking environments and conditions, including the following:

COVID-19 Pandemic. The pandemic and its economic and banking consequences permeated the members' discussion. Those from areas with significant COVID-19 case numbers early in the pandemic generally reported improvement in conditions over the summer, while some members from rural areas less affected by the late winter and spring outbreaks described increasing spikes. All members indicated concern about the prospects of rising cases with winter's arrival, and with it the potential for economically consequential responses. Within that uniformity, members described a variety of local conditions and operational responses.

Although all members indicated that some modifications to operations were in place to protect their employees and the public, the actual practices ranged from continuing branch or lobby closures to business-as-usual (with masks) in the front office and expanded telework behind the scenes. Many stated their institutions increasingly relied on "non-contact channels" such as online and telephone banking. Those members reporting COVID-19 infections among staff expressed a belief that their operational response had precluded spread within their offices, with several stressing the importance of protecting customer and staff alike. Two members recounted positive experience with remote examinations necessitated by the pandemic: Member DeBiasi stated his hopes that this experience leads to a "paradigm shift" in the manner of conducting examinations of smaller institutions, while Member Maley noted the continuing importance of face-to-face contact during this process.

Committee members also noted that the pandemic highlighted the importance of community banking. Member Shettlesworth echoed Chairman McWilliams's prior public statement that community banks hit "above their weight" in delivering stimulus to their communities during the crisis, noting that the institution in his state with the most deposits did not make a single Paycheck Protection Program (PPP) loan in-state. Member Epstein expressed a belief that the community bankers' customer knowledge enabled prudent exercise of flexibility in managing the credit needs of borrowers impacted by the crisis. Member Maley noted a sense that, unlike prior financial crises, "banks were friends, not foes" providing aid to communities through extensions of PPP loans and Coronavirus Aid, Relief, and Economic Security (CARES) Act funds, as well as by sharing rate reductions with customers.

Most members who reported involvement in PPP described their experience with the forgiveness program, noting some difficulties and surprise at the requirement to deduct Economic Injury Disaster Loan (EIDL) advances from the forgiveness amount – resulting in an unexpected need to carry a balance on the loan after forgiveness. Member Mongold commented favorably on the recent Interim Final Rule providing temporary relief from Part 363 Audit and Reporting requirements for banks that have experienced temporary growth due to participation in the PPP and other stimulus programs.

Member Leavitt and Member Kelly said that their institutions had resumed action on long-term strategic initiatives paused earlier in the pandemic. Still, no member indicated that the end of the pandemic is in sight. Subsequent sections of these minutes address the variety of continuing effects of and responses to the pandemic, which the members expect to continue until an effective vaccine or therapeutic treatment is widely available.

Economic Conditions. Members reported significant economic improvement since the July 2020 meeting. Most said that the robust employment recovery continued in their communities, though Member Leavitt noted that many job seekers had “opted out” of the labor market, and Member Epstein expressed concern that anticipated pandemic closings would lead to increases in unemployment. Nearly all members described robust single-family housing market conditions, with high demand for construction, expansion, purchase, and refinance loans. This demand, members said, was attributed to low rates and strong price appreciation due to limited inventory – itself a result of increased purchase interest and high construction labor and materials costs. Members Edwards and Walker spoke of home buying in exurban and rural areas being driven by workers exploring telework as a result of the pandemic, while Member Kimbell posited that the draw of “country living” explained increased demand in his region. Member Andersen said that her institution purchased a mortgage company to expand its reach in this market, while Member Epstein said his bank invested in an improved online platform to compete with nonbank mortgage lenders. According to the members, agriculture is also performing above expectations in 2020, thanks to direct support programs and improved growing conditions over 2019. Member Kimbell said that farming “is on top of its game” and that this buoys all sectors in some rural areas. Member Walker noted the strength of the education and healthcare sectors.

Members identified difficulties in other sectors, notably hospitality and commercial real estate. Most members reported that the hospitality industry in their markets continued to suffer from pandemic-driven reductions in demand. Some members observed that summertime recovery was now at risk due to the return of indoor weather and the threat of shutdowns aimed at controlling COVID-19 infections. Member Narvaez said that border crossing restrictions in his location had heavily affected hospitality businesses. The transition to telework raises long-term questions about demand for office space, according to Members Getzlaff and Andersen. Other impacted industries include the nonprofit sector, with Member Pitkin noting that the survival of many nonprofits may hinge on additional stimulus.

Many members attributed the overall positive economic conditions to federal and state stimulus programs. Members indicated that doubts as to further stimulus programs, just like doubts about the course of the pandemic itself, give rise to overall uncertainty about 2021, a year that Member DeBiasi described as a "wildcard."

Banking Conditions. Across the board, members reported strong banking conditions prevailing in their institutions and local markets. Member Shettlesworth expressed a shared sentiment of surprise, noting that his bank will end the year with record earnings and loan and customer growth, which "doesn't make sense" given the challenges posed by the pandemic and recession.

Nearly all members reported strong asset quality, with few borrowers continuing to use the deferrals, extensions, and other forbearance extended earlier in the year. Member Edwards said that past-due loans were at "unbelievably" low levels even without considering the pandemic. Members Leavitt and Epstein praised the conscientiousness and fortitude of borrowers in keeping loans current despite 2020's challenges. Members also reported asset growth, with a fraction attributed to stimulus programs but with organic growth noted as well. Member Kelly observed that asset quality is strong, but qualified this as a "short run" observation, and that his institution was increasing its allowances for loan losses – something reported by roughly half of the members.

Members continued to report significant deposit growth, attributing much of it to the stimulus programs as well as to traditional asset-growth strategies, such as branch openings. Members told of a variety of strategies to address the capital implications of asset and deposit growth. Member Maley described a successful capital raise, and Member Shettlesworth said his institution was considering one.

Several members noted record years for earnings, with some pointing to mortgage origination and sales as a "bright spot" for community banks. Members identified net interest margin compression, reduced interchange fees due to recession-related decreases in spending, and the earnings effects of increasing reserves as challenges to earnings. Some members expressed caution about earnings prospects for 2021.

Diversity and Inclusion. Several members complimented the FDIC's efforts, and Chairman McWilliams's leadership, on diversity and inclusion in 2020. Member Kelly noted that in "a capitalist society, economics are the measuring stick" and that 2020 provides an opportunity to be equitable. To this end, he called attention to the National Bankers Association's priorities of equity investments, revenue-generating business opportunities, and deposits. Member Leavitt mentioned the FDIC's recent publication, "Investing in the Future of Mission Driven Banks" and his institution's support for a Vermont community development financial institution, as well as its own "Equity Framework."

Other Topics. Members mentioned competition with nonbank lenders, with Member Hayes noting that recent revisions to agricultural appraisal requirements helped level the playing field with nonbank agricultural lenders. Member Maley urged a reconsideration of FDIC treatment of "Amish Aid" flood insurance, saying that discrepancies in regulatory approach advantage national banks over FDIC-supervised institutions. Member Epstein recounted recent experience with cyber-attacks in his area, noting the success of his institution's response plans and his initiation of further training and testing to prevent social engineering attacks. Member Pitkin discussed the importance of vigilance against fraud, especially in the area of unemployment insurance claims. Member Hayes told of a successful emerging leaders program at his institution, designed to train newer workers and involve them in succession planning. Finally, Member Getzlaff recounted her involvement in a recent small business panel convened by the Consumer Protection Financial Bureau as part of its rulemaking to implement Section 1071 of the Dodd-Frank Act. Member Getzlaff explained some of the issues explored by the panel relating to data collections regarding applications for credit by women-owned and minority-owned businesses. She advocated for a $10 billion institution size threshold for loan-level data collection requirements to avoid unintended impacts on borrowers and undue burdens on smaller institutions.

After the committee member roundtable, Mr. Davis introduced FDIC staff members to discuss their national and regional observations. Shayna Olesiuk, Associate Director, National and Regional Risk Analysis, Division of Insurance and Research (DIR), presented on the national economy and banking trends. John Conneely, Regional Director, Chicago region, and Kathy Moe, Regional Director, San Francisco region, presented observations from local FDIC staff.

Following this discussion, Mr. Davis announced the meeting would briefly recess. Accordingly, the meeting stood in recess at 3:13 p.m.

Update from the Minority Depository Institutions Subcommittee

The Committee reconvened at 3:22 pm. Mr. Davis introduced Member Narvaez and Ms. Rudolph, National Director, Minority and Community Development Banking, RMS, to present an update on the Minority Depository Institutions (MDI) Subcommittee, which had met the day before.

Following the presentation, Member Kelly provided feedback about the request for proposal (RFP) for financial advisors to support the new Mission Driven Bank Fund. He expressed concern about the RFP creating exclusion based on experience. By way of example, he said that if an RFP has a magnitude of $2 billion, but no minority firm reaches that threshold, the RFP should include some provision for inclusion. In addition, he suggested that minority organizations have a representative in the process of standing up the fund. He expressed his willingness to work with the MDI Subcommittee to ensure the process is inclusive.

Ms. Rudolph thanked him for those suggestions, and she shared that the MDI Subcommittee had discussed the importance of ensuring the fund investment committee understands the MDI and CDFI bank sector, which is different from mainstream banking. She added that the FDIC solicited minority and women-owned law firms to assist in drafting fund documents and helping with the RFP. She noted that the FDIC is focused on ensuring diversity of participation.

Proposed Changes to the Supervisory Appeals Process

Mr. Davis next introduced Samuel Lutz and James Watts, both Counsel in the Legal Division's Assessment Unit, who presented on proposed changes to the supervisory appeals process.

Following their presentations, Members Hayes and Edwards asked whether the FDIC had considered adding a banker to the proposed Office of Supervisory Appeals to enhance its independence. Mr. Watts responded that the FDIC had received similar comments in writing as well as in listening sessions and webinars and will consider these comments as the proposal is finalized. Member Edwards added that new office should be diverse and include others besides bankers.

Supervision Update

Mr. Davis then introduced a panel of RMS representatives to provide updates on supervisory matters. Doreen Eberley, Director, RMS, outlined the topics to be discussed.

Next, John Rieger, Chief Accountant, RMS, discussed Financial Institution Letter (FIL) 74-2020 issued on August 3, 2020, which provides direction on prudent risk management and consumer protection principles for financial institutions to work with borrowers as loans near the end of their initial accommodation period.

Then Shannon Beattie, Deputy Chief Accountant, highlighted differences between Section 4013 of the CARES Act and discussions in the Interagency Statements of April 7 and August 3, 2020 regarding loan modifications related to COVID-19.

Mr. Rieger then discussed an interim final rule the Board approved on October 20 that provides certain relief under Part 363 regarding audits, financial reporting, internal controls, and the makeup of Boards.

Ms. Beattie then concluded the panel's presentation by discussing the Call Reports for March 31, 2020 and June 30, 2020. She noted that those Call Reports contained revisions associated with several capital-related and other interim final rules and a final rule issued in response to COVID-19's impact on financial markets and strain on the U.S. economy. Ms. Beattie added that institutions should refer to the separate stand-alone September 2020 COVID-19 Related Supplemental Instructions, which address these revisions.

Following these presentations, Member Walker asked whether the FDIC had considered adjusting the CRA thresholds due to the unusual growth in assets. Ms. Eberley responded that the FDIC is looking at other thresholds and factors that might have been affected, as noted in the background section of the *Federal Register* notice relating to the recent Part 363 interim final rule (as announced in FIL-99-2020).

Member Hayes then requested clarification on the evaluation process regarding Threshold Adjustments Due to Unusual Asset Growth mentioned in the presentation. Ms. Eberley responded that it related to the foregoing discussion of how the FDIC is evaluating regulatory thresholds in light of balance sheet increases, and made one adjustment while continuing to review others.

Next, Member Epstein suggested, as a topic for future consideration, the challenges banks will encounter in evaluating extensions of commercial credit as a result of the pandemic impact on cash flow or debt service coverage for 2020. He suggested considering these measures over a multi-year period, or substituting a pro forma statement for 2020 figures. Ms. Eberley responded by referencing the examiner guidance and instructions issued in June, which advises examiners to be cognizant of difficulties with financial statements and the potential use of pro forma financial statements due to continuing uncertainty or disruption. Ms. Miller added that examiners are instructed to look at the risk assessment process, and she expressed a willingness to discuss the topic at the next meeting.

Rapid Prototyping Competition and Request for Information on Proposed Voluntary Certification Program to Promote New Technologies

Mr. Davis then introduced Brandon Milhorn, Deputy to the Chairman and Chief of Staff, who presented an update from FDiTech on the Rapid Prototyping Competition and Request for Information on Proposed Voluntary Certification Program to Promote New Technologies. Member Epstein expressed support for the initiative.

Update from the U.S. Small Business Administration

Mr. Davis then introduced staff from the U.S. Office of Small Business Administration (SBA) – William Briggs, Deputy Associate Administrator, Office of Capital Access; Dianna Seaborn, Director, Office of Financial Assistance; and Susan Streich, Director, Office of Credit Risk Management – to discuss issues relating to forgiveness of PPP loans.

Ms. Seaborn noted the National Association of Government Guaranteed Lenders national conference was occurring that week, and the SBA had been hearing more about issues regarding PPP loan forgiveness. She added that the SBA recently issued information on change of ownership rules for business owners who received PPP funds.

Mr. Briggs reported that the SBA released its FY-20 data that day. Combining PPP, EIDL, and the SBA's regular loan program, the SBA had issued nearly nine million loans and over $750 billion worth of financial assistance for small businesses this year – a record in the agency's history.

Member Shettlesworth asked about the SBA's timeline for responding to forgiveness applications, and whether the SBA can send forgiveness notices to lenders who communicate directly with the borrowers.

Mr. Briggs began by reminding the Committee that the borrowers apply to the lenders for forgiveness, and the lenders then send the forgiveness decisions to the SBA. He noted that the SBA has not yet received the vast majority of forgiveness decisions from lenders. Mr. Briggs added that the SBA has begun remitting payments to lenders who submitted forgiveness applications, and he expects that pace to pick up. He stated that since the remittance payment is the point at which taxpayer funds are exposed, the SBA has been working with its Inspector General as well as the U.S. Government Accountability Office (GAO) and congressional committees on implementation of the PPP. He expressed willingness to look into how forgiveness notices are distributed. Ms. Seaborn noted that they will evaluate whether they can provide access to the portal to more staff members at each lender. She added that direct receipt of forgiveness notices is facilitated by lenders' signing up in the portal, and ensuring they enter correct ACH information.

Member Shettlesworth next asked about potential tax consequences of PPP loan forgiveness. Mr. Briggs and Ms. Seaborn provided general responses regarding federal and state tax consequences, with Ms. Seaborn advising that the SBA is in discussion with the IRS about CARES Act tax exemptions.

Next, Member Walker asked the SBA's timeline for responding to borrowers after banks submit requested items for forgiveness applications. Mr. Briggs responded that the SBA does not have a specific timeframe, but tries to handle applications expeditiously.

Member Mongold then asked about unexpected reductions of forgiveness by EIDL advances. Mr. Briggs emphasized that Section 1110 of the CARES Act requires EIDL advance deduction from the forgiveness amount. He said the SBA is aware of this issue, but it would require a statutory remedy. He noted that EIDL advances are shown in the portal.

Next, Member Leavitt asked how to ensure the SBA does not subtract the EIDL advance amount again during the forgiveness process, in the event a borrower already subtracted it. Mr. Briggs responded that the SBA is looking into that with the Department of Treasury. He advised that, since the SBA will deduct the EIDL amount, if a borrower already deducted the EIDL advance amount, the lender should wait to apply for the forgiveness decision as the SBA and Treasury work to resolve the problem.

Member Shettlesworth then asked what documentation the SBA wants lenders to send with forgiveness applications under Form 3508S for smaller loans. Mr. Briggs said that supporting documentation is required regardless which form is used. Ms. Seaborn added that the SBA does not expect a level of confirmation involving external review, but does expect that a lender would not move a forgiveness application forward if they believe, in good conscience, that there is an issue.

Division of Insurance and Research Update

Mr. Davis then introduced a panel from DIR: Angela Hinton, Senior Financial Analyst; Daniel Hoople, Financial Economist; and Jonathan Pogach, Chief, Financial Modeling & Research Section. They discussed deposit trends, the Deposit Insurance Fund, and the FDIC's Academic Challenge.

Ms. Hinton highlighted the unprecedented deposit growth reported in the first half of 2020. She presented statistics for the industry as a whole, and for all FDIC-insured institutions, and detailed the impact of that deposit growth on the FDIC's reserve ratio.

Next, Mr. Hoople discussed the restoration plan adopted by the FDIC Board in September, including the necessity for the plan, its components, and underlying analysis.

Following the presentations, Member Shettlesworth asked about the possibility of the FDIC increasing deposit insurance assessments to raise the DIF ratio. He questioned whether, in those circumstances, the increased assessments would apply across the industry, or focus on larger institutions. Mr. Hoople responded by noting that the FDIC’s desire to avoid overburdening the banking system at this time is evidenced by its recent decision to maintain assessment rates, but described scenarios in which increased assessments could become necessary and related considerations.

Finally, Mr. Pogach presented on the 2020-2021 Academic Challenge, a nationwide undergraduate competition.

Closing Remarks

Mr. Davis invited closing comments from Director Gruenberg, who thanked the Committee Members for their participation in the lengthy virtual meeting and useful discussion. He reiterated that the Committee has been a valuable asset to the FDIC over the years, providing a line of sight into what community banks experience at the local level, and that their presentations reflect the value and commitment community banks offer to their communities.

Chairman McWilliams closed the meeting by thanking the Committee members and presenters for the feedback and interesting data points to consider on regulatory and supervisory fronts. She expressed her gratitude for the members whose Committee terms end this year: Members DeBiasi, Edwards, Epstein, Kimbell, Leavitt, Maley, Shettlesworth, and Walker.

Having no further business to discuss, the meeting adjourned at 5:38 p.m.

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Debra A. Decker
Federal Deposit Insurance Corporation
Deputy Executive Secretary
and Committee Management Officer
FDIC Advisory Committee on Community Banking

October 28, 2020

Minutes

of the

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of the

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Held in the Board Room

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I hereby certify that, to the best of my knowledge, the attached minutes are accurate and complete.

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Jelena McWilliams
Chairman
Board of Directors
Federal Deposit Insurance Corporation