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OVER A CENTURY: BUILDING BETTER BANKS — HELPING COLORADANS REALIZE DREAMS

There Are Some Good Aspects to This "New Normal"

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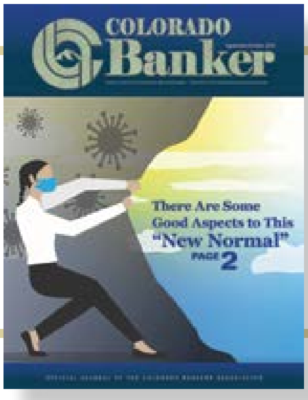

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A WORD FROM CBA

There Are Some Good Aspects to This "New Normal"

BY DON CHILDEARS, CEO, COLORADO BANKERS ASSOCIATION

As Colorado bankers and their customers have worked to navigate the "new normal" brought by the COVID-19 pandemic and its related precautions, CBA is working relentlessly to ensure Coloradans are informed, supported and cushioned from potential negative economic impacts.

CBA has produced 26 webinars since March, bringing information to more than 800 attendees, the bulk of which tackled COVID-19 and adjacent issues. Bankers have received dozens upon dozens of mass emails on topics surrounding COVID-19 and others, garnering attention from even non-member bankers who relied on CBA for the most up-to-date and accurate information.

One banker wrote to me saying, "You have been one of my two 'go-to' sources for information and confirmation of what 'I think I know' during the PPP roll out. God knows, SBA was not a source of information. Colorado Bankers made one heck of a difference for our bank."

A number you might find most exciting, though, is that despite a challenging economy, CBA's membership ranks grew; we added two new banks and three associate members. That tells us not only that our work is hitting the mark of assisting our members, but that others are watching, seeing our value and validating your continued investment in this organization.

CBA has also been focused on a slew of important issues impacting your bank and your customers. While the Colorado state legislature was in session, CBA worked successfully to block the introduction of a bill seeking to ban or restrict foreclosures and amended another bill seeking to limit debt collection amid the COVID-19 pandemic and beyond.

An informational white paper CBA created regarding the negative potential of a state or municipal-owned bank assisted in blocking a bill seeking to create such an institution, though we expect the concept will return next session. On every issue in which CBA engaged, we were successful in blocking or greatly mitigating negative impacts, and the winning streak continued on issues specific to banking. Only once did we not completely hit our mark; the exception was a proactive bill regarding Colorado's Unclaimed Property Act and related escheat laws, as this bill was written and promoted by CBA passed the Senate unanimously but died in the House as a result of Legislative limitations due to COVID-19. We will carry the bill again next year and have high hopes it will have a smooth path to becoming law.

Speaking of COVID-19, CBA efforts ensured banks could continue to serve their customers amid a statewide business closure by deeming bankers as essential workers. The safety of bank employees and customers was made concrete when CBA worked with the Governor's office to permit financial institutions to require customers to briefly remove their face masks amid statewide mask requirements, to establish identification.

With dozens of major issues boiling and frequent shifts in what is the "problem of the day," CBA is staying on top of the federal issues, advocating your interests assertively, coordinating with bankers associations nationwide for maximum impact and reporting relevant info back to you. As you'll read in our Chairman's column, also in this issue, efforts by CBA and others were successful

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in securing a delay in implementation of a strongly maligned 50 bp increase in GSE loan refinance fees. That gives us more time to fight the increase, which is opposed by several members of Congress and by President Donald Trump, in addition to bank industry advocates, consumer groups and others.

We at CBA are proud of the work we are doing to assist our members in fueling Colorado's economy, but we are most proud of our members and the work they do in their communities every day. We relish the opportunity to support and promote them.

Colorado bankers have never shied away from a challenge — quite the contrary; they run toward it and face it head-n. Together, CBA and its members have created two new task forces to tackle both new and ongoing challenges in the banking and business communities at large. One group is focused on banking-specific issues, including economic stimulus, the overall economy and COVID-19's effect on bank operations. Already, 10 separate webinars are planned for later this year on topics including tourism, oil and gas, agriculture, commercial real estate, residential real estate, retail, business failure and lost jobs.

The second group has tasked itself with improving diversity and inclusion in Colorado's banking industry. Its work will focus not only on establishing resources for CBA member banks to use in creating more diversity and inclusion in individual banks but also on creating an environment that attracts diversity in applicants for bank jobs, specifically high school and college graduates.

And the work will not end there. Efforts are already underway to ensure bankers on CBA leadership groups — including board and GAC — will more accurately represent growing diversity in the industry.

Our industry already has a strong foundation. The changes we are making will have long-lasting positive implications. And I know the challenges and changes we are facing today are solidifying infinite possibilities for tomorrow.

As H. Jackson Brown Jr. said, "The best preparation for tomorrow is doing your best today."

CBA's members can rest assured they are getting our best every day, just like Colorado bank customers get the best from their bank every day. ■

CHAIRMAN'S MESSAGE

Advocacy Amid COVID-19 Is an Endurance Game

BY NATHAN EWERT, REGIONAL VICE PRESIDENT OF
FNBO (FIRST NATIONAL BANK OF OMAHA) FOR
COLORADO & WESTERN NEBRASKA
2020-2021 CBA CHAIRMAN

In what some dubbed a "tone-deaf blunder," Fannie Mae and Freddie Mac in August announced a 50 bp price increase, aimed to be effective Sept. 1, 2020.

The move flew in the face of the Trump Administration's executive actions urging federal agencies to take all measures within their authority to support struggling homeowners amid the COVID-19 pandemic and associated economic pressure.

Within hours of the announcement, banks, their advocates, homebuilders, realtors, affordable housing and civil rights advocates railed against the move, drawing additional opposition from members of Congress and President Donald Trump.

Opponents of the proposal noted the price increase could have a significant impact on low- to moderate-income individuals by causing some loans to become high-priced loans, potentially pushing some of those borrowers out of the market. And, thousands of borrowers who did not lock in refinance rates could face unanticipated cost increases just days from closing.

Following weeks of pressure, the FHFA announced that implementing the refinance fee would be delayed until Dec. 1, 2020, giving borrowers a brief respite and opponents of the move more time to combat the idea.

That means our work is far from over. Banks must continue to urge our members of Congress to push the FHFA to exert its authority over Fannie and Freddie and block the increase. And to ensure our representatives in Washington do that, we must first ensure we have the right people in our corner.

Also, in August, CBA's Government Affairs Committee (GAC) voted unanimously to support incumbent U.S. Senator Cory Gardner. He has been a steadfast ally to the banking industry not only throughout his tenure in the Senate but previously in his service as a U.S. representative.

It is important to note that his challenger, former Colorado Governor John Hickenlooper, has been a friend to the industry, something of which CBA and bankers have not lost sight of.

Senator Gardner has, on numerous occasions, credited Friends of Traditional Banking (FOTB) for his victory.

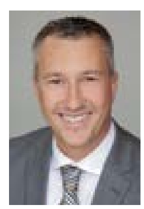
For those who may be unfamiliar, FOTB was founded in 2012 by CBA and others and is a nonpartisan grassroots effort organized by bankers. Two Congressional races are selected to support each cycle, and bankers and others are urged to donate directly to those campaigns. Instead of spreading a little bit of money to many campaigns, FOTB seeks to focus a lot on a couple of critical campaigns.

As of press time, Senator Gardner was on FOTB's shortlist of potential funding recipients. FOTB is open to anyone, specifically bankers, bank directors, bank shareholders and local business and community leaders.

Which brings me to my final point. While the world has slowed down around us, bankers have been running full speed to support their customers and communities, and we're going to have to keep up our endurance as Election Day comes and goes and far into 2021 as Colorado's legislature and members of Congress return to their desks.

CBA has worked to restructure its now 8-year-old Center for Bank Advocacy Training Practicum to ensure that bankers' ranks can continue to become educated on industry and policy advocacy, even if COVID-19 prevents in-person education and advocacy.

If you haven't yet, I encourage you to learn more about the program. Many of CBA's board of directors and GAC members are alumni of the program; I'm among them. In my time with CBA, I have learned firsthand the invaluable impact banker advocacy can have on policy. Our voices as bankers are the most effective tool our advocates have to ensure a healthy and thriving environment for our banks and our customers today and in the future. ■

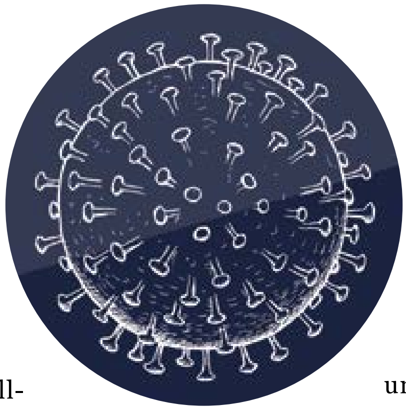


Nathan serves as Regional Vice President, responsible for leading teams that work with businesses in eastern Colorado and western Nebraska. His primary role is to fulfill client needs quickly and efficiently. He focuses on building relationships that last. In his experience, this is the best way to understand customer needs and to proactively help them meet their financial and life goals.

WASHINGTON UPDATE

Personal Finance for the Pandemic Era:
Why Bankers Should Deliver Fin Ed Lessons Today

BY ROB NICHOLS, PRESIDENT AND CEO,
AMERICAN BANKERS ASSOCIATION



The pandemic has forced many lessons on us, not the least of which is the importance of being prepared. I don't mean being-well-stocked-on-toilet-paper prepared. I mean having the ability and resources to survive an uncertain and even perilous period. For businesses, that requires having a well-crafted and tested business continuity plan. For households, the most important preparedness tool may be a well-funded savings account.

Those who may not have fully appreciated this before COVID-19 certainly understand it now. In fact, a Bank Rate survey this summer found that Americans' top financial regret is not having enough emergency savings to withstand the crisis, followed closely by not having enough retirement savings.

This presents an important opportunity for banks, which can — and should — help support both established and fledgling savers as they pursue their savings goals. Nothing is more fundamental to financial wellness than savings.

Given the massive economic dislocation caused by the pandemic, this may seem an odd time to exhort others to save. Many are suffering from a loss of income and find it challenging to pay their expenses; how can they possibly set aside money for a rainy day when it's already pouring? But there's reason to view this as the ultimate teachable moment, and an ideal time to convert lessons into action.

In a July survey of hourly workers (by DailyPay and Funding Our Future), 51% said that coming out of the pandemic, they are more likely to save for the future, as opposed to 15% who said they were less likely to do so. Meanwhile, 65% said they don't have any type of savings account, and 62% said they would save more if there was an easier way to set aside a portion of their paycheck.

This data points to a clear demand for information and tools to facilitate savings, and banks are a reliable source for both.

To help banks meet that demand — and prevent financial regrets in the first place by teaching financial fundamentals to today's youth and young adults — the ABA Foundation has adapted its financial capability programming for today's virtual world. Teach Children to Save lessons went virtual in April, and Get Smart About Credit, our fall program, has also been adjusted to include new resources and notes for delivering effective virtual presentations, as well as new modules around saving for the unexpected.

We all know that strong personal finance skills are essential to success in life. A majority of respondents in the latest Charles Schwab Financial Literacy Survey said that money management was the most important skill for children to learn, outranking the dangers of drugs and alcohol, healthy eating and exercise habits and safe driving practices. And nine in 10 agreed that a lack of financial education contributes to some of the biggest social issues our country faces, including poverty, unemployment and wealth inequity.

This brings us to another lesson learned from the pandemic: Significant disparities in health, education and job opportunities persist. Those disparities have exposed some populations to greater risk — of catching COVID-19 or losing a job — and they've left some children more vulnerable than others to the adverse effects of school closures.

Education, including financial education, can help reduce these disparities and give all Americans an equal opportunity to prosper. Few are more qualified to deliver lessons in personal finance than bankers, so I strongly encourage you to register as a volunteer for a financial education program today. The ABA Foundation makes it easy — and free. Visit aba.com/FinEd to learn more and sign up. This is one of the most important ways bankers can make a long-term difference in the lives of others.

The more individuals we reach with this valuable information, the better off our communities will be. And there's no doubt it is better to learn personal finance lessons in a class Zoom meeting than in a crisis. ■

FEATURE ARTICLE

CFPB Announces Its Spring Agenda

BY CHRIS W. BELL , ASSOCIATE GENERAL COUNSEL

The challenges we have faced in 2020 have come at us out of nowhere and at a lightning pace. The world continues to face a global pandemic, while regulators and businesses are mainly reinventing significant industries. We have dealt with the Paycheck Protection Program, stimulus checks, mountains of loan modification requests, significant pushes to online services, and many other things that were not on our 2020 roadmap. With so many unexpected developments, it's nice when we have the opportunity to anticipate some of the changes that will require us to take action.

The Consumer Finance Protection Bureau (CFPB) has been busy during the last several months, and the next 12 months promise even more change. The CFPB recently published its Spring 2020 Agenda as part of the Trump administration's Spring 2020 Unified Agenda of Federal Regulatory and Deregulatory Actions. The agency recapped some of its actions from recent months and gave us a preview of the regulatory roadmap through Spring 2021. Many of the changes follow up on proposals the agency had already announced.

Changes are underway to the escrow requirements of higher-priced mortgage loans (HPMLs). Under Section 108 of the Economic Growth, Regulatory Relief, and Consumer Protection Act of 2018 (EGRRCPA), Congress instructed the CFPB to conduct a rulemaking to exempt loans from the escrow requirements applicable to HPMLs if the lender has $10 billion or less in assets and meets other criteria. The CFPB published a notice of proposed rulemaking July 2 to implement Section 108 of the EGRRCPA. Comments are due by Sept. 21, 2020.

As we enter into the fall, the CFPB plans to take a significant step toward implementing section 1071 of the Dodd-Frank Act. Section 1071 requires lenders to identify women-owned, minority-owned and small businesses and collect data related to the race, sex, and ethnicity of the business owners, the purpose of the loan, the action taken with regards to the loan, the business's gross annual revenue, and "any additional data that the [CFPB] determines would aid in fulfilling the purposes of this section." In October, the CFPB will convene a panel under the Small Business Regulatory Enforcement Fairness Act to discuss this matter. Ahead of the event, the CFPB will be releasing materials that the group will discuss with representatives of small entities likely to be directly affected by the Bureau's rule to implement section 1071.

The fall will also likely see two proposals to modify the Home Mortgage Disclosure Act (HMDA). The first proposal follows the May 2019 advance notice of proposed rulemaking concerning data points that banks must report under the 2015 HMDA rule and coverage of business or commercial purpose loans. The second proposal addresses the public disclosure of HMDA data in light of consumer privacy interests.

In October, the CFPB expects to issue a final rule after the May 2019 proposed rule that would prescribe rules under Regulation F to govern the activities of debt collectors. The proposed rule would address communications connected with debt collection; and interpret and apply prohibitions on harassment or abuse, false or misleading representations, and unfair practices in debt collection. The CFPB did not announce when it plans to take final action on its supplemental proposal issued in March 2020, which addressed time-barred debt disclosures.

Finally, the CFPB is considering a proposed rule that would offer a new "seasoning" definition of Qualified Mortgages (QM). This definition would create an alternative pathway to QM safe-harbor status for mortgages when the borrower has consistently made timely payments for a period. This action would come on the heels of proposals to address the impending expiration of the Government-Sponsored Enterprises (GSE) Patch and amend the General QM definition in Regulation Z to replace the Debt-to-Income limit with a price-based approach. The comment periods for the existing proposals close on August 10 and September 8, respectively.

The CFPB also discussed its participation in the interagency rulemaking processes to update the guidelines issued by the Financial Institutions Reform, Recovery, and Enforcement Act of 1989 (FIRREA). This partnership with the Board of Governors of the Federal Reserve System, the Office of the Comptroller of the Currency (OCC), the Federal Deposit Insurance Corporation, the National Credit Union Administration, and the Federal Housing Finance Agency is developing regulations to implement the amendments made by the Dodd-Frank Act to the FIRREA guidelines concerning appraisals. The changes require implementing regulations for quality control standards for automated valuation models (AVMs).

One of the items listed in the preamble to the CFPB's Spring Agenda that has not generated much attention is the agency's study of the impact of artificial intelligence (AI) in the context of federal consumer financial laws and regulations. Banks raised issues related to AI in response to the CFPB's 2017 Request for Information Regarding Use of Alternative Data and Modeling Techniques in the Credit Process, the Bureau's 2018 Calls for Evidence, and in other outreach since then. The bureau continues to monitor developments concerning AI and is evaluating whether rulemaking, a policy statement or other action may be appropriate. With the OCC's recent proposal regarding technological innovation, it would not be surprising to see the CFPB announce something on this topic soon.

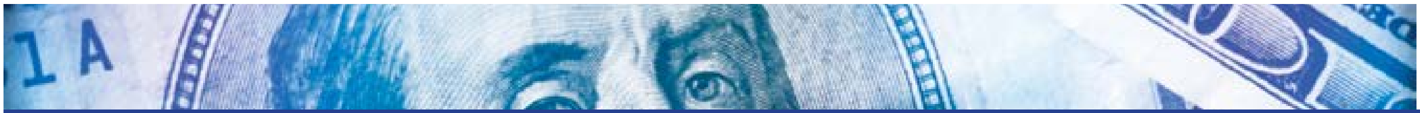
To fulfill its obligation under Section 1022(d) of the Dodd-Frank Act, the CFPB is also conducting its five-year review of its Integrated Mortgage Disclosures Under the Real Estate Settlement Procedures Act (Regulation X) and the Truth in Lending Act (Regulation Z) Rule and certain amendments. The CFPB announced it plans to issue its TRID Rule assessment report by October.

The CFPB also expects to conduct an additional review under section 610 of the Regulatory Flexibility Act, which requires the bureau to consider the effect on small entities of the rules it promulgates. The agency plans to review the Regulation Z rules that implement the Credit Card Accountability Responsibility and Disclosure Act of 2009.

Stay tuned to Compliance Alliance for announcements on these developments and more. ■

Chris W. Bell serves as associate general counsel for Compliance Alliance. He holds a bachelor's degree in Political Science from the University of Memphis, a master's degree in Political Management from the George Washington University, and a law degree from the St. Mary's University School of Law.

Chris began his career working for a regional bank in Tennessee, where he developed a passion for serving customers through the banking system. In law school, Chris focused his studies on the different financial aspects of the law, including the Internal Revenue Code and Uniform Commercial Code. Chris has worked in the legal department of a federal savings bank and for the Texas Department of Banking. As one of our hotline advisors, Chris helps C/A members with a wide range of regulatory and compliance questions.



COVID-19 Loan Modifications:
It Is More Than Just a TDR Issue

BY SCOTT POLAKOFF, CAMS, EXECUTIVE VICE PRESIDENT WITH FINPRO

Many banks across the country are at risk of CAMELS downgrades, increased deposit insurance assessment premiums and regulatory enforcement actions due to inadequate risk management practices for their COVID-19 Loan Modification Program.

Loan modifications have been part of most banks' lending operations for many years. Before the coronavirus, such modifications were often prompted by a borrower's "financial distress." Banks would attempt to work with the financially distressed borrower by granting a "concession" that the bank otherwise would not consider other borrowers with a similar risk profile. An example of such a loan modification might be an interest rate reduction from 5% to 3% for 12 months to help a financially distressed borrower. Generally speaking, this type of loan modification would be categorized as a Troubled Debt Restructure ("TDR") under accounting literature (ASC 310-40) and captured as such in Call Reports. TDRs are considered impaired loans.

Many banks have COVID-19 Loan Modifications approximating 25% of their commercial portfolio.

When the country became engulfed with the coronavirus, both Congress (Section 4013 of the CARES Act) and the Regulators (April 2020 Interagency Guidance) issued material to guide banks on TDR designation for COVID-19 related loan modifications. Bankers must understand that while Section 4013 and the April 2020 Interagency Guidance both discuss the applicability of TDRs, they have materially different requirements (modification duration, date of record for current/delinquency status, etc.) for determining when the TDR designation is necessary. FinPro urges all banks to specifically designate whether the COVID-19 Loan Modification was approved under Section 4013 of the CARES ACT or under the April 2020 Interagency Guidance. This document should be in each loan modification file and address the items shown in the graphic.

Was the borrower impacted by COVID-19?

❑ YES ❑ NO

Was the modification pursuant to Section 4013?

❑ YES ❑ NO

If yes, was the loan current as of Dec. 31, 2019?

❑ YES ❑ NO

If yes, was the loan modification before Dec. 31, 2020?

❑ YES ❑ NO

Was the modification pursuant to the Interagency Guidance?

❑ YES ❑ NO

If yes, was the loan current at the time of modification?

❑ YES ❑ NO

If yes, was the loan modification short term (i.e., six months)?

❑ YES ❑ NO

Remember that banks must maintain records on the number and dollar amount of loan modifications approved under Section 4013 of the Interagency Guidance and report this data to the board of directors on a regular basis.

The TDR determination is only the first step in the COVID-19 Loan Modification process.

Unfortunately, too many banks neglect to implement the second step in the COVID-19 Loan Modification process, which is vital to accurately identify, measure, monitor and control the bank's risk profile.

Banks must properly "Risk Rate" COVID-19 Loan Modifications and incorporate such risk ratings into their ALLL/ACL calculations. Loans modified under Section 4013 or the Interagency Guidance pertain ONLY to borrowers who have been impacted by the coronavirus. By definition, these borrowers have financial performance less robust than before COVID-19. In some cases, these borrowers may have serious cash flow problems driven by the coronavirus that impact their ability to service their debt. It is incumbent on banks to accurately "Risk Rate" these borrowers at the time of loan modification and on a regular basis going forward. FinPro has observed that many banks have internally "risk-rated" their COVID-19 loan modifications to a "watch" category.

Moreover, these new risk ratings must be incorporated into the ALLL/ACL calculation. One "best practice" observed for community banks across the country is to establish a "homogenous pool sub-tier" within the ALLL/ACL methodology to break out all such loan modifications within each homogenous pool. It is noteworthy that this approach is often used in conjunction with a new "COVID-19 Q-Factor" that many banks now incorporate their ALLL/ACL methodology. Some banks have actually appended a one- or two-digit code to COVID-19 loan modifications to ensure easy identification over time.

Lastly, effective corporate governance is critical to avoid CAMELS downgrades and enforcement actions. Corporate governance starts with a comprehensive documentation process. As noted earlier, banks must maintain records of all COVID-19 loan modifications, specifically noting whether such modifications were executed under Section 4013 of the CARES Act or the Interagency Guidance. Remember, modifications cannot fall under both categories since they have different (and competing) requirements. This information should be reported to the board of directors on a regular basis. Similarly, the management must inform the board of risk rating trends for COVID-19 loan modifications and how such ratings have impacted the bank's ALLL/ACL. These actions, together with updated policies and procedures to incorporate coronavirus actions, robust MIS and Risk Management practices, and comprehensive Internal Controls will properly prepare banks to address any regulatory concerns. ■

Scott Polakoff, CAMS, is executive vice president with FinPro, a full-service management consulting firm specializing in providing advisory services to the financial institutions industry. He can be reached at spolakoff@finpro.us/ www.finpro.us

This Could Be the Answer to Your Risk Management Goals

BY PAUL BRIGGS, VICE PRESIDENT/HEAD, WHOLE LOAN TRADING

In a low-interest-rate environment where earnings and risk management are front and center, the Whole Loan Trading market can be an effective mechanism to achieve your financial and risk management goals. All types of loans trade regularly, as well as all types of credit, and the market includes institutions of all sizes. Duncan-Williams, Inc. Whole Loan Trading Desk has the ability and expertise to help you achieve the best execution in the secondary loan market. For loan sellers, we strive to achieve maximum fair market value for your liquidity needs and A/L plans. For loan buyers, we also stress fair market value and always try to deliver your desired yield and duration preferences while also providing top-notch customer service, so the trade tracks from LOI to funding. We handle all trades the same way — with a hands-on approach throughout due diligence that enables us to expedite timelines, regardless of how cumbersome.

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- New Conforming 1-4 Resi Origination for CRA and Secondary Investors for New Product
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- Consumer Products for Released and Participation Inquiries

Whether you are a seasoned veteran of the Whole Loan market or a rookie learning the playbook, we stand ready to help you solve your problem with your risk management. Established over 50 years ago, our firm is well-capitalized and has a national presence focused on regional banks. Reach out to your DWI representative, or directly to our trading desk, with any whole loan questions. We look forward to working with you and appreciate any opportunities to do so. ■

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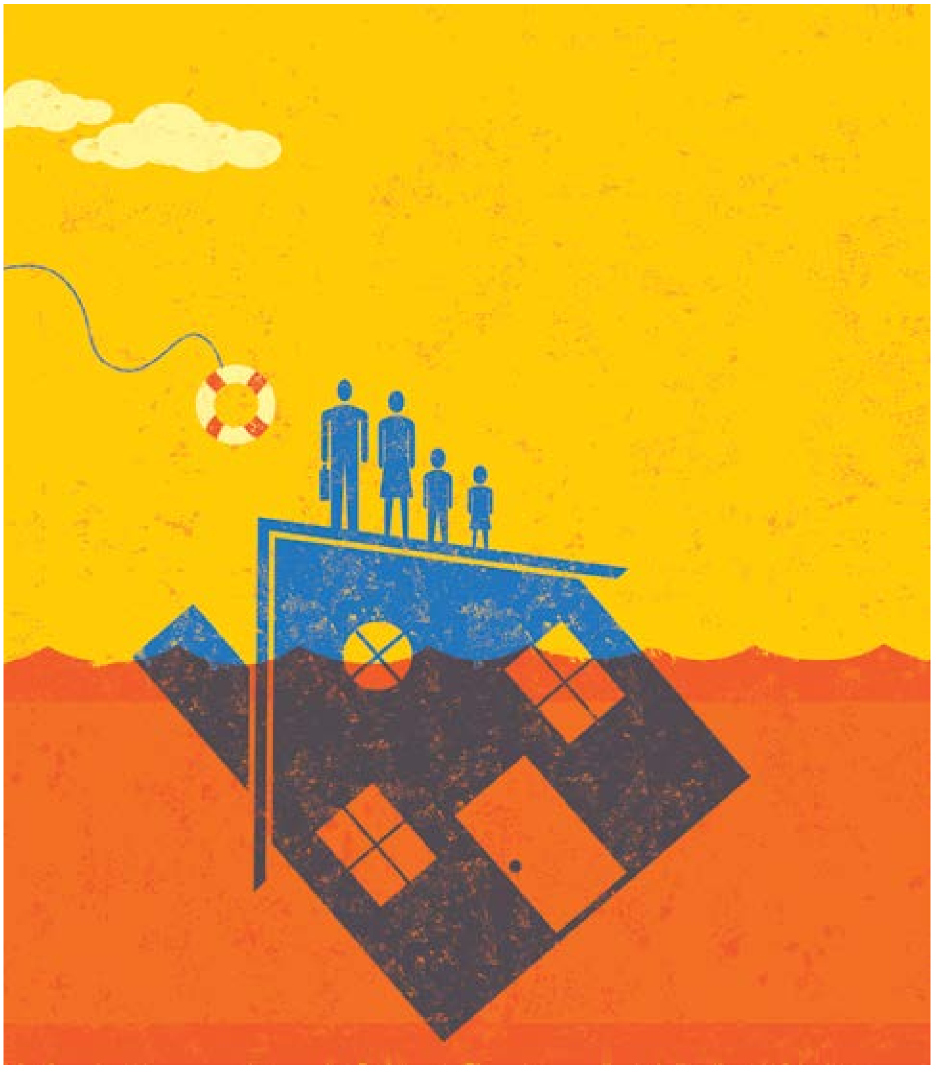
FEATURE ARTICLE

Foreclosure Protection: Where Are We Now?



The COVID-19 pandemic has changed American life as we know it. As the country continues to deal with the health crisis, the effects of containment measures ripple through the American economy. Unemployment remains high as state economies expand and contract in inverse proportion to the virus's spread. Regulators are in an arms race with rapidly changing markets, forcing banks to adapt to an ever-changing regulatory landscape. Even as we struggle to deal with the immediate concerns, we know the effects of this pandemic will be with us for some time. Economic shocks will continue to reverberate and play out in the housing markets around the country. As we shift into the next phase of operating in the pandemic and consider what options exist to help struggling mortgage borrowers, we should take note of the status of the expansive mortgagor protections passed by Congress, federal agencies and other government authorities.

Protection for Federally Backed Mortgage Loans

In the early days of the pandemic, Congress passed the Coronavirus Aid, Relief and Economic Security ("CARES") Act. One of the primary sections of this law established a 60-day moratorium on foreclosure proceedings against homeowners with federally backed mortgage loans. The CARES Act's mortgage foreclosure moratorium applied to single-family residential mortgage loans secured, guaranteed or made by FHA, USDA, VA, or Fannie Mae or Freddie Mac. Originally scheduled to expire at the end of June, the various agencies extended the moratorium on foreclosures and evictions until Aug. 31, 2020.

The CARES Act also granted federally backed mortgage loan consumers that are experiencing financial hardship related to the COVID-19 pandemic the right to request six months of forbearance (with an option of six additional months), regardless of delinquency status. Congress prohibited servicers from charging any fees related to this forbearance. Mortgage delinquency status is frozen in place during forbearance, even if the bank suspends payments during the forbearance. As it stands today, customers can request forbearance under the CARES Act until the earlier of the end of 2020, or the end-date of the national emergency concerning the novel coronavirus disease outbreak declared by the president on March 13, 2020, under the National Emergencies Act.

State and Local-level Protection

Many state and local authorities enacted policies to protect mortgage borrowers and renters. The details of these state and local foreclosure bans vary. Banks should refer to the official websites for their state and local governments to assess the scope and requirements of

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applicable prohibitions. While effective dates vary widely, many of these protections remain in effect until respective governors lift statewide emergency declarations.

Private loans

The CARES Act provided no relief for loans that are not federally backed. Banks should refer to the appropriate investor guidelines for mortgages sold to private investors. Banks should refer to guidance from its regulators concerning their expectations regarding non-federally-back mortgage loans held in the portfolio.

Troubled Debt Restructuring ("TDR")

If neither a federal nor state moratorium applies to a residential mortgage you hold in the portfolio, you may still be able to exercise your authority to assist pandemic-effected borrowers who are struggling financially. Regulators have urged banks to work with customers and prudently modify loans safely and soundly. Section 4310 of the CARES Act provided banks relief from TDR. In April, regulatory agencies issued revised interagency guidance to help banks sort modification requests into three groups: (1) loan modifications covered by Section 4310 of the CARES Act; (2) those outside Section 4310 deemed not to be TDRs; and (3) those outside Section 4310 that may be TDRs. In June, regulators released new interagency safety and soundness examiner guidelines. These guidelines instruct examiners to not criticize institutions for doing so as part of a risk mitigation strategy intended to improve existing loans, even if a restructured loan ultimately results in adverse credit classifications.

To be covered by Section 4310 of the CARES Act, a loan modification must: (1) relate to COVID-19, (2) be executed between March 1st and Dec. 31st (assuming the current national emergency does not end earlier than the end of the year), and (3) the underlying obligation must be not more than 30 days past due. If a loan modification meets these three criteria, financial institutions do not have to report it as a TDR; however, the financial institution should maintain records of the volume of such loan modifications.

If a loan modification fails to meet any of the three criteria for Section 4310 coverage, it does not automatically result in a TDR. Regulators will deem a modification as not constituting a TDR if it relates to COVID-19, extends no more than six months, and the underlying obligation is not more than 30 days past due. The only subjective criterion is the relationship of the modification to COVID-19. As a best practice, banks should have the borrower certify that the requested change is due to COVID-19. To not raise HIPAA concerns, the certification should be general and not address specific health details. While such a certification is not required to be in the loan file, it would show future examiners that the lender followed the guidance in good faith. If a bank receives a modification request that is outside the scope of Section 4310 and does not meet the described criteria, the bank should assess whether the modification would be a concession to the borrower that the bank would not otherwise consider and act accordingly.

As with everything related to the COVID-19 pandemic, expect mortgage foreclosure protections to change as the county continues to deal with the long-term effects of our national crisis. The federal agencies may extend the protections relating to the loans they back. Congress will undoubtedly reassess the CARES Act's protections as the end of its covered period draws near. Despite how things change, you can count on the Colorado Bankers Association to bring you the most up-to-date information available as we walk hand-in-hand through this crisis. ■

Being Proactive in Tricky Times

BY SCOTT C. SANDBERG, PARTNER,
SPENCER FANE LLP

The COVID-19 pandemic's first six months have proven predictably unpredictable for banks. PPP and other government assistance programs might have temporarily staved off widespread loan defaults, but they foisted unique challenges on the banks charged with disseminating relief funds.

And new PPP-related legal challenges for banks have begun rearing their heads. Bankruptcies have spiked, but foreclosures have remained stable relative to previous crisis periods. Financial markets have enjoyed record growth, while unemployment has skyrocketed.

With no way to predict the pandemic's length or impact on borrowers, lenders would do well to act cautiously pessimistic: hope for the best but prepare for the worst. What follows are proactive checklists to prepare for problem loans, defaults, lender liability litigation, and other events we hope won't happen — at least not on a massive scale.

With no way to predict the pandemic's length or impact on borrowers, lenders would do well to act cautiously pessimistic: hope for the best but prepare for the worst. What follows are proactive checklists to prepare for problem loans, defaults, lender liability litigation, and other events we hope won't happen — at least not on a massive scale.

Identifying Problem Loans

Consider whether action needs to be taken on loans with one or more of the following issues:

- Uncured monetary or nonmonetary defaults
- Uncooperative or hostile borrowers
- Borrowers involved in lawsuits or with other legal problems
- Borrowers in volatile business sectors
- Diminished collateral value
- Competing claims to collateral

Prepare a problem loan "plan" that includes:

- Measures the bank will take to resolve the problems
- The bank representatives who will communicate with the borrower, and the means of communication

Workout Arrangements

- Document all workout arrangements with signed written agreements
- Determine the preferred workout agreement structure (e.g., forbearance agreement, deed in lieu, modified loan agreements, restructured collateral)
- Obtain a release from the borrower of claims against the bank in exchange for the workout arrangement

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- Obtain the borrower's re-affirmance of the debt and amounts owing
- Resolve existing loan documentation issues (e.g., collateral description or perfection issues, missing signatures)

Loan Enforcement/Litigation

- Involve legal counsel
- Implement a "litigation hold" to prevent the alteration or destruction of relevant documents, paying close attention to electronically stored documents
- Organize and review the loan file and all records relating to the loan
- Compile and review emails and text messages to and from the borrower and internal emails concerning the loan
- Identify and interview all bank representatives with knowledge of the loan or dealings with the borrower
- Instruct all employees not to discuss the loan outside the presence of counsel
- If the bank has charged off the loan, then payoffs should be separately tracked in the same manner as before the charge off
- Determine where litigation will be filed based on dispute resolution provisions in loan agreements and legal requirements
- In the event of claims asserted against the bank, determine whether the bank has insurance covering defense or indemnity for the claim
- Identify any COVID-19 restrictions on loan enforcement (e.g., foreclosure timing or notice requirements or moratoriums) ■

Scott Sandberg is a partner at Spencer Fane LLP in the firm's Denver office. He is a commercial litigator who represents clients in trials, arbitrations, appeals and emergency injunction proceedings. For financial services clients, Scott represents lenders and servicers in a broad array of matters, including ag finance, loan recovery, lien priority and lender liability.

Thank the Fed for the Blueprint

BY ROBERT BIGGS, SENIOR MARKET ANALYST, FIXED-INCOME STRATEGIES GROUP
ADAM SASLAWSKY, VICE PRESIDENT, FIXED-INCOME SALES

In January 2012, Ben Bernanke introduced the world to the FOMC's first dot plot to clarify the Federal Reserve's rate outlook. The median projections were for 25 bps to conclude 2012 and 2013 with a 75 bps median projection by the end of 2014. The market priced short-term rates more hawkish with three-month U.S. Treasuries implied to be at 130 bps by the end of 2014. Ultimately, they were both too aggressive, as the FOMC maintained the 25 bps upper bound range until December 2015. Investors who accepted the Fed's low rate forward guidance outperformed as they extended loan and bond durations while lowering their cost of funds.

At the time, the dot plot was new and portfolio managers were skeptical. The effective fed funds rate had rarely been below 1% in the previous 50 years. A 0-25 bps range for an extended period was unparalleled. Today, the market is accustomed to a zero-rate environment, and the Fed is once again projecting a multiyear path of low rates. June's dot plot had 100% of Fed governors with a 0-25 bps range in 2020 and 2021. Only two Fed governors dissented from the 0-25 bps range in 2022. The market is in line with the dot plot: Fed Fund Futures imply a 0.24% effective fed funds rate in three years. However, depositories face a unique challenge compared to the Great Recession — low cost of funds.

In December 2008, when the effective fed funds range first reached 0-25, the average COFs for banks under $10BN was 2.53%. Over the next three years, they lowered their COFs by over 150 bps to 0.97% to support NIM. As of the 2020 Q2 call reports, banks under $10BN have a COFs of only 62 bps. Reducing COFs to protect margin will be more challenging in this round of low rates, so depositories will need to make the most of their investments. Fortunately, with the Fed's guidance, portfolio managers have a blueprint for investing lower for longer environment.

Invest in Longer Duration Securities With Call Protection

Banks and credit unions have a historic amount of excess liquidity. Many institutions deploy extra funds into longer investments with call protection such as CMBS and municipals. The expectation of low COFs grants them the ability to extend with muted fear of margin compression due to rising rates. Additionally, the curve has steepened with the Fed's most recent comments regarding higher inflation levels. The spread between five and ten-year U.S. Treasurys is near three years wide. The curve encourages investors to extend to improve earnings and generate gains from rolling down the curve.

Leverage Strategies

Depository studies and forecasts lack a "pandemic shock." Therefore, the outflow of excess liquidity is uncertain. Deposits have been stickier than anticipated, but with the conclusion of many government programs and the gridlock in Congress, the lack of future government intervention may cause deposit balances to fall. Institutions that are hesitant to deploy the excess liquidity because of deposit uncertainty can employ leverage strategies to take advantage of low borrowing costs on the front end of the curve and the spread over the last five years. ROA and NIM may compress, but the net income and ROE will improve, and capital ratios will support it.

Portfolio Repositionings

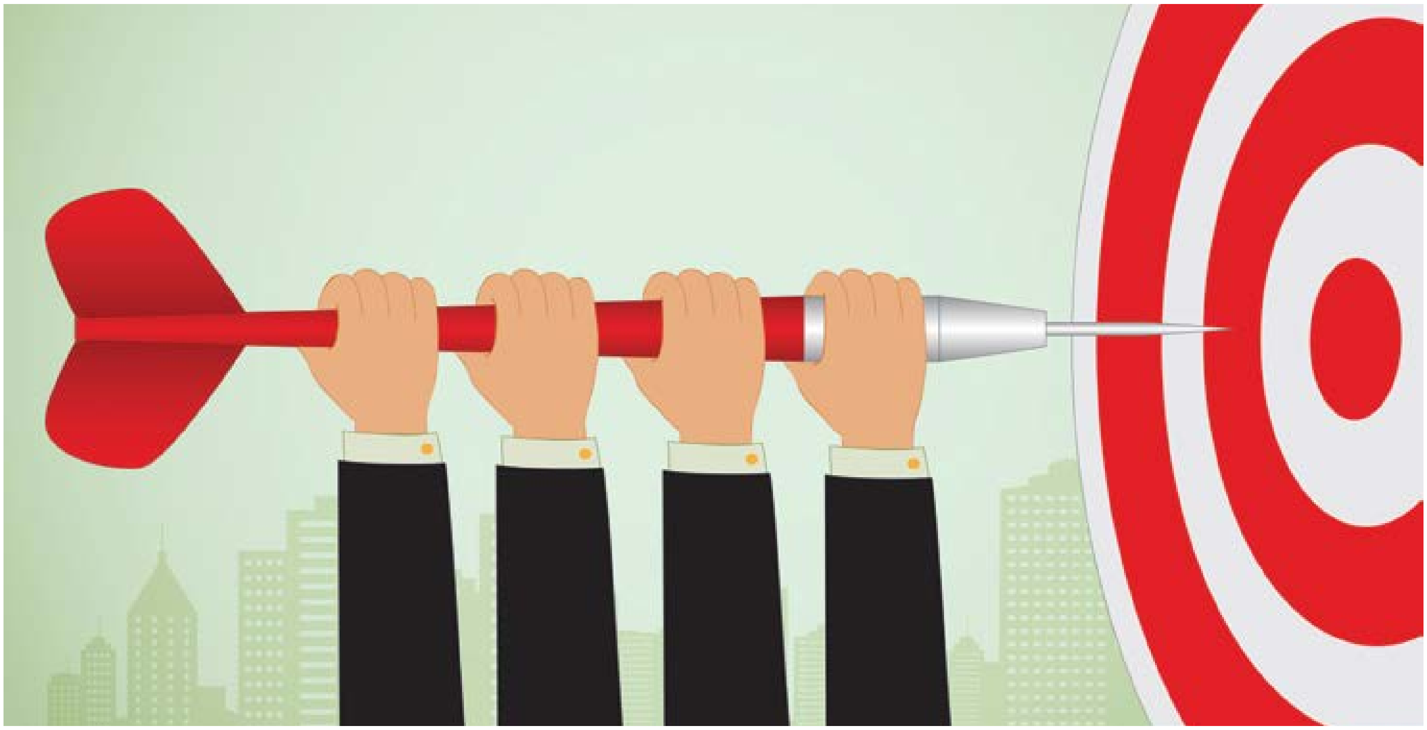
The lack of lending opportunities has renewed the focus on the investment portfolio. Even institutions without a surplus of liquidity and those who do not wish to borrow can utilize the existing portfolio to improve earnings and take advantage of the curve. The Fed intervention in the fixed-income market tightened spreads across most sectors, especially on the front end of the curve. By selling short bonds into the Fed's bid, investors can realize gains and position the portfolio into a more attractive part of the curve that will protect NIM.

More Aggressive Loan Terms

Banks historically gravitate toward short term or floating rate loans to lower interest rate risk. They would rather portfolio a 3/1 ARM than a 30-year fixed-rate mortgage. With the Fed's low forward rate guidance, deposit rates are not expected to increase. Therefore, institutions can hold more fixed-rate loans than has been historically possible. Longer fixed-rate loans will generate more coupon revenue, and the longer fixed-rate lock will protect NIM against low rates. Depositories will also become more competitive in their local markets by offering more fixed-rate loans. Additionally, banks can sell or participate in existing floating-rate loans knowing that the coupon is unlikely to improve in the near term.

Due largely to PPP, community banks have had attractive earnings in 2020. With interest rates expected to remain low and lending opportunities waning, 2021 is poised to be a more challenging year for revenue. Thank the Fed for the investment blueprint to prepare for this lower-for-longer environment. ■

ALERT:
Fraudulent Filings With the Colorado Secretary of State Targeting Banks



BY KAREN WITT, LEWIS ROCA ROTHGERBER CHRISTIE

Beginning as early as March 2020, there have been several fraudulent filings made with the Colorado Secretary of State ("SOS") involving former and current bank entities. Fraudulent filings have been made to change a bank's:

- Name,
- Form of entity,
- Registered agent,
- Registered address, and
- Jurisdiction of formation.

Although approval by the Colorado Division of Banking ("CDOB") is required for any filing of corporate documents with the SOS which include the words "bank," "trust," "trust company" or any derivation thereof, such filings may be made with the SOS without obtaining prior approval of the CDOB. A person making an online filing with the SOS does affirm that he or she is acting in good faith to make the filing and provides a name and address of the filer. However, it is a simple matter to provide a false name for the filer and complete the filing, which is automatically accepted by the SOS.

Depending upon the type of filing made against a bank's SOS record, correction of the fraud can take time and money to correct or undo.

Actions to Take Now

All banks and bank holding companies should insure that their entity records at the SOS have been locked for secure business filings. This does not occur automatically but must be elected for each entity. When you have accessed your bank listing on the SOS website, you will select "set up secure business filing." The SOS will mail a PIN to the bank's principal place of business. The PIN can then be used to lock your bank's file to require a password for all SOS filings. A bank can grant access to secure business filings to more than one person.

In addition, each bank should select an officer to subscribe to email notifications for all SOS filings made on your bank's record. On the SOS website for your bank listing, you will select "subscribe to email notification." Regular monitoring of your bank's corporate records with the SOS can help to quickly detect and correct any fraudulent activity. ■

Karen Witt is a partner and member of the Lewis Roca Rothgerber Christie Business Transactions group and co-chairs the firm's Banking Industry group. Her areas of practice focus on securities, mergers and acquisitions, regulatory compliance, corporate governance, corporate finance transactions and legal opinions. For more information, please contact Karen Witt at kwitt@lrrc.com.

Triaging for Your Institution's Credit and Liquidity Health

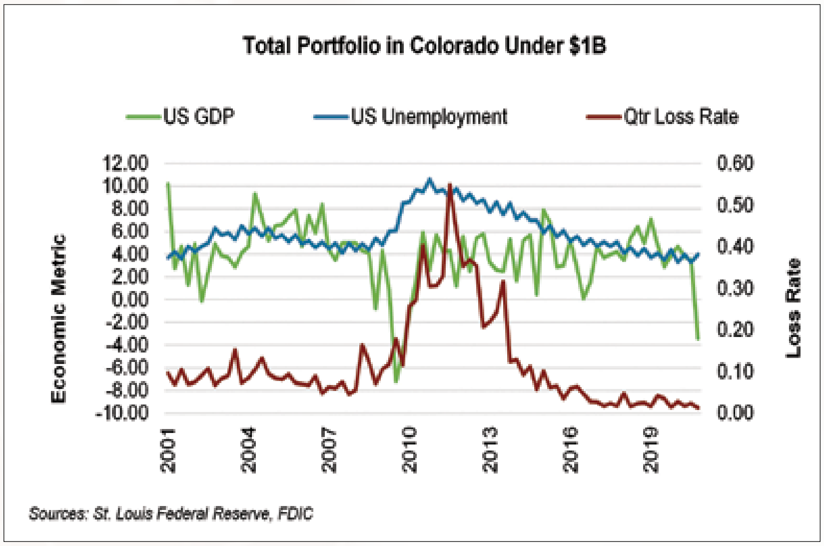
BY MATT HELSING | MHELSING@PCBB.COM | WWW.PCBB.COM

Being a member of the C-suite can be demanding, as you are responsible for the health and resiliency of your institution. The challenge in leading any organization is ensuring that the right questions are asked, the right priorities are set, and the right amount of resources are allocated. Choosing the right priorities is not unlike triaging patients in a busy emergency department on a Saturday night. Make the right choices, in the right order, and people thrive. Miss an important symptom, and the consequences may be dire. In this credit cycle, how do you triage quickly? This will depend on your institution's current situation.

Handling regulatory orders. First and foremost, you will want to address any regulatory orders or any open examination issues. Are examiners asking you detailed questions about debt coverage ratios or changes in your customers' FICO scores since the start of the pandemic? Are you being asked repeated questions about certain segment concentrations? If that's the case, this is urgent and needs to be handled ASAP.

So, how do you best handle it? With a loan portfolio bottom-up, perform a detailed stress test — one that will provide you and your institution with specific, supportable results by showing the different stressed scenarios and their impact on your capital. You should also dig deep into cash flows, the borrowers' statements and their supply chains. If you have the resources and the time, then this is your top internal priority. If you don't have time to complete that detailed analysis or you're missing information, then you need a third party to help.

Demonstrating resiliency. Triaging to the next level, urgent but not critical, you will need to be prepared to satisfy examiner expectations for institution resiliency. Examiners are going to ask specifically about the effects of the pandemic on your institution. While this can be answered with a bottom-up loan portfolio stress test, a faster alternative is a complete, quick top-down test. This approach uses the historical relationship between unemployment, GDP, and industry data loss rates. Using multivariate regression combined with future forecasts, you can quickly generate estimated loss rates. If the relationship between GSP (gross state product), state unemployment, and loss rates remains highly correlated, state data can be used instead of national data. Loans can also be segmented by industry classifications.



Sources: St. Louis Federal Reserve, FDIC

Recovery scenarios. The next step is to decide which recovery scenarios are the most likely to show adequate stress on your portfolio. With the large banks, the regulatory agencies asked that they simulate stress under V-, U- and W-shaped recoveries. You should also consider an L-shaped recovery scenario, which generates the longest period of losses. Under this scenario, unemployment is assumed to remain above 10% through Q1 2022, and during the same period, there is no economic recovery.

When you're asked about your resiliency — how future events affect your portfolio — you will know the answer with this swift top-down approach. Using the same regression model, the economic metrics forecast is adjusted to simulate the different types of recoveries resulting in different loss rates.

Consider Colorado as an example. Using Colorado's historical loss rates with the highly correlated national data for GDP and unemployment, we find that Colorado's aggregate capital levels under the V-, U- and W-shaped recoveries remain well above regulatory minimums. We also discover that total risk-based capital, barring a long-term recession such as expected in an L-shaped recovery, remains adequate.

Your actual results depend on several factors, such as your actual losses compared to state averages, your actual forecasts, tax rates and eligibility for loss carrybacks, in addition to the timing of the recovery or future infections in your local economy. However, by triaging effectively, you can focus your institution on the most needed activities. Once you have a top-down view, you can decide if it makes sense to spend time on more detailed actions. ■

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