

# MEETING OF THE BOARD OF BANK ADVISORS

January 12, 2009

1:00 pm

Department of Financial Institutions  
324 South State Street, Suite 201  
Salt Lake City Utah

Minutes

## **BOARD MEMBERS PRESENT:**

Craig White, Cindy Johnson, Leonel Castillo, Doug Bringhurst, and Dave Brown.

## **DEPARTMENT OF FINANCIAL INSTITUTIONS STAFF PRESENT:**

Tom Bay, Commissioner Ed Leary, Paul Allred, and Sonja Long.

## **OTHERS PRESENT:**

John Sorensen, Home Savings Bank; Kendall Phillips, Liberty Bank; Bill Swadley, Bank of American Fork; Michelle Loghry, Centennial Bank; Doug Durbano, America West Bank; Don Norton, Far West Bank; Curtis Taylor, Heber Valley Bank; Paul Matthews, Holladay Bank.

### **1. Call Meeting to Order – Chairman Cindy Johnson**

### **2. Elect new chair and vice-chair**

Cindy Johnson explained that with it being January it was time to elect a new chair and vice-chair from the board members. Leonell Castillo nominated Dave Brown as chair, Doug Bringhurst seconded the motion. Doug Bringhurst nominated Craig White as vice-chair, Leonell Castillo seconded the motion. It was unanimous. Cindy turned the meeting over to Dave.

### **3. Minutes –**

Changes to the minutes, Leonel Castillo asked to check the spelling of his name; at the top of page two the word is loosing and should be loosening. At the top of page three the word employee should just be employ. Doug Bringhurst said that Louise's last name is Zeenati. Cindy Johnson made the motion that the minutes be approved with those changes; Craig White seconded the motion, unanimous approval.

### **4. Current Topics & Trends – Tom Bay**

He wants to talk about two or three things. First he would like to update numbers for 3<sup>rd</sup> quarter and then he would like to talk about some of the exam issues that are being found, and then some miscellaneous items.

As of 3<sup>rd</sup> quarter, for Utah State chartered institutions commercial banks only; year over year asset growth – the recent high was year end '06 it was 23%. As of 3<sup>rd</sup> quarter it has gone down to 6%. This is expected as we are cutting back lending, it is also following the trend that we saw last quarter. All of these numbers will continue to follow the trend from the second quarter. Non-performing assets have increased to about 43% of equity capital. That is up from 13% from year end '07. That trend has gone up fast. When we talk 43% past due to equity capital that is approaching what we would consider a “3” rating in asset quality. We will probably continue to see that go up for the 4<sup>th</sup> quarter. Past due and non-accrual loans have increased to about 7.8% of total loans. That is up from year end '07, minus about 3.2, more of a reasonable number. Utah has the highest percentage of non-current loans in the 12<sup>th</sup> District. We are higher than Nevada, Arizona, California, etc. The allowance accounts have gone up. The allowance to total loans has increased to 1.7%. The average for 12<sup>th</sup> District banks shows about 1.6%. That is asset quality.

Dave Brown asked, you hear of markets that are substantially worse than ours, Nevada, Arizona, California. How do they manage to have that kind of scenario with numbers that are seemingly better than ours? Tom isn't sure that he has a good answer. When he said that we have the highest percent of non-current loans, it is not too much higher than some of the other states, but it is slightly higher. Commissioner Leary said that the only reason he can find is we have always surpassed them in our acquisition, development, and construction loans percentage than any other state.

As far as earnings, ROA peaked in 1<sup>st</sup> quarter of '07 and it stayed pretty steady at about 2.1%, right now it has been consistently down, it is at .7%. The 12<sup>th</sup> District average for all commercial banks is .23%, so we are above that. The provision expense has jumped from .26% of average assets as of year end '07 to 1% of average assets. Tier 1 Capital would now average 12.5%, Total Risk Based is 16.75%. The trend is decreasing, 12<sup>th</sup> District ratios are 10.8%, Tier 1 and 13.9% Total Risk Based. We have pretty good numbers with capital.

Projections for 4<sup>th</sup> quarter, Tom is thinking that the numbers will continue to decrease, and we will see these negative trends continue. A discussion was held on the changes that everyone is seeing.

Commissioner Leary said that the economic report to the Governor was recently presented by Kelly Matthews; his sense was at least the existing inventory should be burned through by the end of '09. He is thinking that the number of households that we are still developing will still need housing and should start driving some turn around by 4<sup>th</sup> quarter of '09. Commissioner Leary said that he did not get that sense from the bankers who were here today.

Kendall Phillips asked Howard Headlee how he felt about a matching State tax credit for new home buyers. Commissioner Leary explained that Howard sits on the new Utah Housing Coalition that the Governor has put together. Howard said that there have been detailed discussions on how to structure that and how the federal one may be restructured because it still has to be repaid. It hasn't been very successful and they are not sure why. Most of the people in the industry feel like right now it is consumer confidence that is holding people back from signing up for a 30-year commitment in this market. There have been a lot of debates; to do something like that at the State level would cost a lot of capital and you would have to be really sure that it would work and there wasn't the consensus that it would work. Howard said that the Governor has \$5 million built into his budget proposal to do something that the group tells him is most important. The group may very well come back with something like that proposal. The group is meeting today to talk about the ideas. That is assuming that the \$5 million that the Governor put on the table is really there. There are a lot of other ideas that have been suggested and so the group is looking at everything to see what the best suggestion could be.

Tom asked if we could move on, he said that the exams are obviously taking longer in today's world. We are looking at bigger loan samples; we are seeing more issues that are arising because of asset quality. We are also doing more interim visitations and target exams. There are more downgrades. It is tough for us and most certainly harder for the institutions. Some of the most common issues are; the bank is experiencing higher classifications, higher past dues, and maybe there are some management issues with monitoring. Right there you are probably looking at a downgrade in asset quality and management. From there, if we are downgrading asset quality you have earnings that are affected and capital and liquidity that all have potential downgrades. This seems to be the current model. We are seeing issues with downgrading proactively, banks aren't being quite as proactive as the department would hope to see in downgrading the credits and looking at what the reality is out there in the market that you are in. We are seeing some hesitation and as a result, the allowance account sometimes has some issues, either it is not funded adequately or the methodology isn't up to par with what we would like to see. The FED is focusing a lot of energy on adequate allowance, adequate methodology, and appraisals. That is their focus lately.

We have talked about appraisals a lot, it has been a frustration, but it is becoming an issue with exams. Liquidity – we are seeing more banks being downgraded in liquidity which we almost never did during good times. Dave Brown asked about brokered deposits. Tom said that we are seeing issues there. If a bank funds with brokered deposits then, if the bank becomes stressed there are limits that kick in. If you become less than well capitalized for PCA or you are under a formal enforcement action, the FDIC can limit your brokered deposits. They do that by requiring you to apply for and be approved for a waiver to continue offering brokered deposits or rolling them over. And they don't always give that waiver.

Craig White asked for more on what the FED is looking at concerning appraisals. Tom said that the issue has come up when an outdated appraisal is being used. If it is a troubled asset, how good is your appraisal valuating.

Commissioner Leary had a call from the media today, are you as community bankers seeing an increase in deposits? Most said that yes, they were. There was a brief discussion on those deposits and where they were coming from and what other trends that everyone sees.

Tom said that the department has had a busy second part of '08. We have had some institutions that have converted over into commercial banks. Grand Valley National Bank has converted. Tom welcomed Curt Taylor here today. Curt explained a little about his bank, their roots are in Grand Junction Colorado. They opened a de novo in Heber, Heber Valley National Bank. They have since consolidated the two charters; they have three branches in Utah and four in Western Colorado. They have been a national bank since 1983. They have converted to a Utah charter; Heber Valley Bank with Colorado branches. Tom said that there have been some industrial banks that have converted to be commercial banks; GMAC Bank has been approved and CIT Bank has also been approved. GMAC is \$33 billion and CIT is about \$3 billion. There are a few others that are in the process. Commissioner Leary said that American Express has been granted bank holding company status.

## **5. Legislative Preview – Paul Allred**

Paul said that he was at a meeting last Thursday with a lot of the bankers when he mentioned what is happening with the department in the '09 legislative session.

The SAFE Act was passed by Congress in July and signed by the President requiring all loan originators that are working in non-depository settings to be licensed in the states where they operate. What Congress did was give the states the opportunity to put a licensing scheme in place; if the states don't do that then HUD will step in and take over. The State of Utah was licensing loan originators before this in the Division of Real Estate, so we will maintain that licensing scheme. The Division of Real Estate has a bill already filed, SB31. They will amend their title 61-2-c to be compliant with the SAFE Act. That means that the mortgage piece that falls under our department will have to also be amended. We have two titles that it falls under Title 70D and Title 70C that will have to be amended to comply with the SAFE Act. The Commissioner opened a bill file and we have a bill in draft form and a sponsor. You will hopefully see a bill early in the session. HUD approved CSBS' model state law and we are using that as our pattern for our amendments. That is the only piece of legislation that the department is working on.

We have heard that there are members of the legislature that are interested in running an interest cap bill. Paul had a discussion with a legislator about that bill. The frustration by the legislature is that we have an industry here in the state, the payday lending industry, that has extremely high interest rates and they feel it should be regulated. The session begins on January 26.

## **6. Commissioner comments – Commissioner Ed Leary**

Commissioner Leary wanted everyone to be aware that for the state legislative session, budgets will be cut. The department has been asked to present a 7.5% cut, and a 15% cut to our department budgets. Every agency head has been asked to do that. This morning the committee met talking about what each agency would do to arrive at that 7.5 and 15% cut. While that is the issue, savings can only be derived from general fund agencies; we are not a general fund agency and have been able to evade those severe cutbacks in the past. On the other hand, Commissioner Leary remains concerned that they not raid our restricted account; which is what each of you pays into the department through your annual fee. Absent a raid on the restricted funds, informally, the legislature has asked that while they may not be asking the cuts of our department, what would you do to demonstrate good faith with these kinds of things. We responded with we currently have four examiner positions out of 41 authorized that are vacant. We have indicated for the immediate future we would not fill those vacancies.

## **7. Other business**

Michelle Loghry asked when you are filing SARS with the Division of Real Estate for fraudulent realtors, developers, appraisers, and borrowers do we see anyone pursuing those cases? Paul Allred said that the State of Utah is working with the FBI on a mortgage fraud task force and there have been some prosecutions lately that were posted on the Division of Real Estates website and the FBI's website. They are aware of the problems. We have referred a couple of situations to them. If you have any problems, give Tom or Paul a call and they can give you the contact person from the FBI.

## **8. Next meeting – April 13, 2009.**