I. Defining a Peer

II. Peer Benchmarking Metrics

III. Means of Conducting Peer Analysis

IV. Future of Peer Analysis

V. Peer Analysis Best Practices
What is a Peer?
What is a peer?

- Anglo-French, peir, Old French, per, and Latin, pār, meaning equal.
- Merriam-Webster defines a peer as one that is of equal standing with another; one belonging to the same societal group especially based on age, grade or status.
- In the banking industry, what once was a simple term has gone through an evolution of meaning and adaptation.
- A peer that once was a bank down the street is now an institution determined by size, location, business mix, and a combination of a multitude of other measurements.
Defining a Peer Group

- **Defining a peer group?**
  - Banks across similar markets of operation
  - Banks of similar size – include some that are the same size as your bank, some slightly smaller as well as the size your institution aspires to be
  - Depending upon the type of analysis, it is also important to look at a variety of performance metrics to see how your bank stacks up relative to the competition
  - Peer groups should be limited to 10-20 peers at most for a meaningful analysis
  - Rather than defining peers based on asset size and geography – a more innovative and realistic approach is to define peers based on operating strategy, lending practices, funding strategy, earnings strength, etc.
With $2.9B in total assets, StellarOne Bank is one of Virginia’s largest independent, commercial banks. StellarOne is the subsidiary of StellarOne Corporation which is headquartered in Charlottesville, VA. StellarOne Bank is headquartered in Christiansburg and has a strong presence from the New River Valley and Shenandoah Valley to Central and North Central Virginia. They also manage trust and wealth service assets of nearly $1B.

<table>
<thead>
<tr>
<th>Institution Name</th>
<th>HQ Location</th>
<th>Total Assets</th>
</tr>
</thead>
<tbody>
<tr>
<td>Bank of Hampton Roads</td>
<td>Virginia Beach, VA</td>
<td>$1.7B</td>
</tr>
<tr>
<td>Monarch Bank</td>
<td>Chesapeake, VA</td>
<td>$1.1B</td>
</tr>
<tr>
<td>Burke &amp; Herbert</td>
<td>Alexandria, VA</td>
<td>$2.5B</td>
</tr>
<tr>
<td>First Bank &amp; Trust Company</td>
<td>Lebanon, VA</td>
<td>$1.2B</td>
</tr>
<tr>
<td>Cardinal Bank</td>
<td>McLean, VA</td>
<td>$3.0B</td>
</tr>
<tr>
<td>TowneBank</td>
<td>Portsmouth, VA</td>
<td>$4.3B</td>
</tr>
<tr>
<td>United Bank</td>
<td>Vienna, VA</td>
<td>$3.5B</td>
</tr>
<tr>
<td>Union First Market</td>
<td>Richmond, VA</td>
<td>$4.0B</td>
</tr>
<tr>
<td>First Community Bank</td>
<td>Bluefield, VA</td>
<td>$2.7B</td>
</tr>
<tr>
<td>Carter Bank &amp; Trust</td>
<td>Martinsville, VA</td>
<td>$4.3B</td>
</tr>
</tbody>
</table>
## Redefining a Peer Group: StellarOne Bank

<table>
<thead>
<tr>
<th>Institution Name</th>
<th>HQ Location</th>
<th>Total Assets</th>
<th>Deposit Mix/Loan Mix</th>
</tr>
</thead>
<tbody>
<tr>
<td>StellarOne Bank</td>
<td>Christiansburg, VA</td>
<td>$2.9B</td>
<td>63% MMDA/30% Time Deps/0.25% Brokered</td>
</tr>
<tr>
<td></td>
<td></td>
<td></td>
<td>24% Cl-end 1-4/12% Rev 1-4/9% Const &amp;</td>
</tr>
<tr>
<td></td>
<td></td>
<td></td>
<td>Land/1.3% Consumer/7.89% C&amp;I/39% CRE</td>
</tr>
<tr>
<td>Bank of Hampton Roads</td>
<td>Virginia Beach, VA</td>
<td>$1.7B</td>
<td>26.7% MMDA &amp; Savings/18.2% C&amp;I</td>
</tr>
<tr>
<td>Monarch Bank</td>
<td>Chesapeake, VA</td>
<td>$1.1B</td>
<td>37.8% MMDA &amp; Sav/20% Brokered</td>
</tr>
<tr>
<td></td>
<td></td>
<td></td>
<td>Deposits/46.5% Cl-end 1-4</td>
</tr>
<tr>
<td>Burke &amp; Herbert</td>
<td>Alexandria, VA</td>
<td>$2.5B</td>
<td>69.9% MMDA &amp; Sav/6.4% Rev 1-4/25.3% Cl-end 1-4</td>
</tr>
<tr>
<td>First Bank &amp; Trust</td>
<td>Lebanon, VA</td>
<td>$1.2B</td>
<td>55.8% MMDA &amp; Savings/1.6% Rev 1-4</td>
</tr>
<tr>
<td>Company</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Cardinal Bank</td>
<td>McLean, VA</td>
<td>$3.0B</td>
<td>49% MMDA &amp; Sav/4.8% Rev 1-4 Fam/42.9% Cl-end 1-4</td>
</tr>
<tr>
<td>TowneBank</td>
<td>Portsmouth, VA</td>
<td>$4.3B</td>
<td>71.4% MMDA &amp; Sav/18.6% Const &amp; Land Dev</td>
</tr>
<tr>
<td>United Bank</td>
<td>Vienna, VA</td>
<td>$3.5B</td>
<td>45.6% Transaction Accts/21.6% MMDA &amp; Sav</td>
</tr>
<tr>
<td>Union First Market</td>
<td>Richmond, VA</td>
<td>$4.0B</td>
<td>57.4% MMDA &amp; Sav/8.1% Consumer</td>
</tr>
<tr>
<td>First Community Bank</td>
<td>Bluefield, VA</td>
<td>$2.7B</td>
<td>44.1% MMDA &amp; Sav/6.1% Const &amp; Land/4.6% Consumer</td>
</tr>
<tr>
<td>Carter Bank &amp; Trust</td>
<td>Martinsville, VA</td>
<td>$4.3B</td>
<td>19.59% MMDA &amp; Sav/0% Rev 1-4 Fam</td>
</tr>
</tbody>
</table>
If we were to re-evaluate our chosen peers for StellarOne Bank to focus on those most like StellarOne from a loan composition and deposit composition standpoint, you will notice our peer group has changed and we have introduced new players into our peer group analysis.

<table>
<thead>
<tr>
<th>Institution Name</th>
<th>HQ Location</th>
<th>Total Assets</th>
</tr>
</thead>
<tbody>
<tr>
<td>American National Bank &amp; Trust</td>
<td>Danville, VA</td>
<td>$1.3B</td>
</tr>
<tr>
<td>Virginia National Bank</td>
<td>Charlottesville, VA</td>
<td>$474M</td>
</tr>
<tr>
<td>TowneBank</td>
<td>Portsmouth, VA</td>
<td>$4.3B</td>
</tr>
<tr>
<td>Union First Market Bank</td>
<td>Richmond, VA</td>
<td>$4.0B</td>
</tr>
<tr>
<td>Central Virginia Bank</td>
<td>Powhatan, VA</td>
<td>$385M</td>
</tr>
<tr>
<td>Chesapeake Bank</td>
<td>Kilmarnock, VA</td>
<td>$629M</td>
</tr>
<tr>
<td>EVB</td>
<td>Tappahannock, VA</td>
<td>$1.0B</td>
</tr>
<tr>
<td>Valley Bank</td>
<td>Roanoke, VA</td>
<td>$784M</td>
</tr>
<tr>
<td>Burke &amp; Herbert Bank &amp; Trust</td>
<td>Alexandria, VA</td>
<td>$2.5B</td>
</tr>
<tr>
<td>National Bank of Blacksburg</td>
<td>Blacksburg, VA</td>
<td>$1.0B</td>
</tr>
</tbody>
</table>
Peer Benchmarking Metrics
Peer Benchmarking Categories

- Capital Adequacy
- Asset Quality
- Profitability
- Liquidity
- Loan Mix and Deposit Mix – Interest Rates
- Sensitivity to Interest Rate Risk and Market Risk
**Capital Adequacy**

- The cushion of equity and liquidity reserves needed to survive stress situations your institution may be facing that lead to losses or reductions of assets.

- Aspects to consider:
  - Composition and quality of capital
  - Quantity and quality of earnings to increase capital
  - Access to government programs and access to capital markets

- Key Capital Ratios and Metrics
  - Tier 1 Risk Based Capital Ratio (Tier 1 Risk Based Capital / Risk Weighted Assets)
    - Tier 1 capital is seen as a metric of a bank’s ability to sustain losses and track how much risk you are taking on (dollars held to dollars loaned out)
  - Leverage Ratio (Tier 1 Risk Based Capital / Average Assets)
    - Measure of balance sheet or economic leverage
  - Internal Growth Rate of Capital (Previous Period Net Income – Cash Dividends / Previous Period End Total Equity)
    - Measure capital strength, resilience, and bank’s ability to earn it’s way out of trouble through its profits from operations
Peer Benchmarking Metrics: Capital Adequacy

**Capital Adequacy**

- **Tier 1 Common Risk Based Capital Ratio**
  - Ratio introduced during the Supervisory Capital Assessment Programs (SCAP) in the government’s stress tests in May 2009
  - Tier 1 common capital is the highest form of loss absorbing capital.

- **Future of Capital Adequacy Assessments**
  - **Common Equity Tier 1 Capital Ratio**
    - Under the new Basel III rules Common Equity Tier 1 Capital, aka CET1, was created
    - CET1 includes common equity as defined under GAAP and does not include any other type of non-common equity under GAAP. New adjustments introduced.
    - **Revised Risk Weighted Assets** is denominator – increase in risk-weighted assets for 1-4 family loans based upon LTV, High Volatility Commercial Real Estate, and Past Due Loan Exposures
Asset Quality

Credit Quality of your bank’s earning assets, the bulk of which comprises your loan portfolio, but will also include your investment portfolio (i.e. fixed income securities) and off-balance sheet items.

Aspects to consider:

- Degree to which your loans are performing relative to other banks in your market and the likelihood that your loans will continue to perform.
- Loan Loss Reserves that you have set aside relative to other banks in your market with similar asset quality ratios.
- In assessing your risk profile relative to your peers, it is important to take into account the management strategy (i.e. aggressive expansion vs. conservative) and the market environment (booming economy vs. recession).
- CRE concentrations – overconcentration at Florida banks led to the demise of many banks during the recession. Assess how many banks in your market have Commercial Real Estate Loans / Total Risk Based Capital less than 300% as outlined in the FDIC’s Guidance on CRE concentrations.
Asset Quality

Key Asset Quality Ratios and Metrics

- Nonperforming Loans / Loans
- Nonperforming Assets / Total Assets
- Nonperforming Assets + Loans 90 days or more past due / Loan Loss Reserves + Tangible Equity
  - We also recommend looking at the adjusted ratios which net out delinquent government guaranteed loans and OREO covered by loss-sharing agreements with the FDIC.
- Loan Loss Reserves / Nonperforming Loans
  - See how your reserve coverage compares to peers in your market
  - Concerns if this dips below 100%
- Net Chargeoffs / Average Loans
- OREO / Loans and Restructured Loans / Loans
  - Lagging indicators behind Nonperforming Loans
  - When these ratios peak – recovery is likely under way
**Profitability**

- Earnings refer to both profits and profitability, with an emphasis on profitability
- Important to identify banks with strong earnings capacity and high profitability
  - Generate Revenue
  - Earn way out of trouble by building up capital
  - Understand how others are continuing to invest in and grow their franchise
- **Key Profitability Ratios and Metrics**
  - **ROAA**
  - **ROAE**
  - **ROACE**
    - Net Income available to Common (Net Income – Preferred Stock Dividends)/ Average Common Equity
- Important to adjust for S-Corps if your institution is, for U.S. federal tax income purposes, either an S corporation or a “qualifying subchapter S subsidiary” as defined by the IRS
Peer Benchmarking Metrics: Profitability

**Profitability**

- **Key Profitability Ratios and Metrics**
  - **Net Interest Margin**
    - Yield and Cost
      - Rates on deposit, mortgage and consumer loan products
    - Understanding fluctuations in earning assets & interest bearing liabilities to help maximize Net Interest Income
    - Margins under pressure for several quarters
    - Who is capitalizing on the low-rate environment to juice mortgage production?
  
- **Efficiency Ratio**
  - Non-interest expenses / Net Interest Income (FTE) and Non-Interest Income
  - What’s driving a peer’s ratio? Are you utilizing your resources for maximum production?
  
- **Aspects to Consider**
  - Volume of problem assets
  - Compliance costs
  - Branch Consolidation – trimming expenses
  - Median Efficiency Ratio for the industry as of 2012Q3 was 70.6%
  - Lowest Efficiency Ratio in 1997 at 61%
Peer Benchmarking Metrics: Profitability

**Profitability**

- Noninterest Income/Operating Revenue
  - Diversified revenue streams of banks in comparison to your institution
  - Reliance on service charges on deposits declining
  - Service charges for deposits fell from 27% to 17% among banks greater than $10B in assets
  - Service charges for deposits fell from 34% to 24% for banks with less than $10B in assets
Liquidity

Ability of your bank to access liquid funds (i.e. cash or cash equivalents – US Treasury Bills or money market securities) to meet current needs for such funds.

For example, acute need can arise if depositors panic and seek to withdraw their funds.

Aspects to consider:

- Do the banks in your market increase their dependence on non-core/volatile sources of funding such as large time deposits and brokered deposits to fund significant loan growth?
- FHLB Advances funding growth?
- Composition of funding sources, on/off-balance sheet, securitizations
- Funding Stability – deposits, cash and short term assets, commercial paper
Peer Benchmarking Metrics: Liquidity

**Liquidity**

**Key Liquidity Ratios and Metrics**

**Liquidity Ratio**
- Ability to pay off short-term debt obligations
- Higher liquidity ratios – higher margin of safety to meet current liabilities

**Liquid Assets/ Total Assets**
- Cash and Balances Due from Depository Institutions, Securities, Fed Fund & Repos, Trading Account Assets
- Net out pledged securities

**On Hand Liquidity/ Total Liabilities**
- Interest-bearing balances + Total Securities + Fed Funds Sold & Reverse Repos – Fed Funds Purchased & Repos – Pledged Securities / Total Liabilities
- The lower your ratio relative to peers, the greater the likelihood your bank will need to sell less liquid assets or use market funding sources to meet incremental liquidity needs

**Reliance on Wholesale Funding**
- Total Borrowings + Brokered Deposits / Total Borrowings + Total Deposits
- Total funds drawn from wholesale sources – absence of local deposit funding
- Who of your peers with extensive branch networks is avoiding expenses?
Loan/Deposit Mix

Important to define your peers based on lending practices and funding practices similar to your bank

Competitive pricing

- Once you determine those that offer similar products in your market the next step is understanding how your pricing across those products differs or aligns with your competition
- Understanding fluctuations and earnings assets & interest bearing liabilities as well as accurate view of competitive pricing = maximize Net Interest Income and margins
- Flexibility of pricing strategy relative to competition
- Promotional Rates and Specials

Loan / Deposit Ratio

- Assessment of a bank’s liquidity and lending capacity
- Reached lowest level – Aggregate as of 2012Q3 was 72.14%
- Shifts in lending practices
- Pricing – In line or out of line with market
Loan/Deposit Ratio

Growth of loans and deposits at US banks and thrifts

- Loans ($T)
- Deposits ($T)
- Loans/deposits (%)

As of Dec. 17, 2012
Financial data is based on regulatory filings by U.S. commercial banks, savings banks and savings institutions.
Source: SNL Financial
Peer Benchmarking Metrics: Loan/Deposit Mix

- **Loan/Deposit Ratio**

- **States with highest median 2012Q3 loan/deposit ratio** were VT (89.49%), NH (87.11%), RI (89.98%), MA (83.57%), and ME (100.78%)

- **States with the lowest median 2012Q3 loan/deposit ratios** were NM (59.76%), TX (62.26%), KS (63.87%)
**Sensitivity to Market Risk (Interest Rate Risk)**

- In assessing your bank’s market risk relative to peers, it is important to determine how changes in interest rates, foreign exchange rates, commodity prices, or equity prices could potentially reduce a bank’s earnings or capital.
- **Primary source of market risk is Interest Rate Risk**
  - Sensitivity to changing interest rates
  - Mismatches in the repricing term characteristics across assets and liabilities
  - **Gap analysis**
    - Measure of volume of assets and liabilities subject to repricing within a given period (month, quarterly, etc.)
    - Assets and Liabilities classified according to their maturity and repricing characteristics (short term to long term)
    - Gap between rate sensitive assets and rate sensitive liabilities – identifies mismatches
  - **Net Interest Income simulations** – determine impact of 1%, 2%, or 3% change in short term interest rates on earnings
**Sensitivity to Market Risk (Interest Rate Risk)**

- **Key Sensitivity to Market Risk Ratios and Indicators**
  - **Asset Depreciation of Tier 1 Capital**
    - Proportion of capital offset by estimated depreciation in the AFS and HTM investment security portfolios
    - Depreciation in asset classes indicates yields below current market rates
  - **Long Term Assets/ Total Assets**
    - Securities and Loans that mature/reprice in over 5 years + Collateralized Mortgage Obligations with remaining maturity over 3 years
  - **Repricing Risk**
    - Higher ratio = Sizable assets that can’t be repriced for a long period of time
    - Interest Rates rise → Assets lose value/depreciate → Paying lower yields relative to prevailing market rates
Peer Benchmarking Metrics: Sensitivity to Market Risk

**Sensitivity to Market Risk (Interest Rate Risk)**

- **Key Sensitivity to Market Risk Ratios and Indicators**
  - **Non-maturity Deposits / Long Term Assets**
    - Degree that non-maturity funding sources cover LT assets
    - Demand Deposit Accounts, MMDA, Savings, NOW accounts
    - Non-maturity deposits protect against rising interest rates
      - Yields generally low and don’t reprice as quickly as other funding sources
    - Low ratio → reliance on rate sensitive non-core funding
      - Likely to be sensitive to increases in interest rates
  - **Residential Real Estate / Total Assets**
    - Total 1-4 Family Loans + Residential Mortgage-backed securities at Cost Value + Structured Notes at Cost Value
    - Proxy for negative convexity in balance sheet due to embedded short options in mortgages, Residential MBS and structured notes
    - Short Options amplify interest rate risk
      - Compress margins in both rising and falling rate environments
Means of Conducting Peer Analysis
**Means of Conducting Peer Analysis**

- Federal Deposit Insurance Corporation (FDIC Website)
- FDIC Uniform Bank Performance Report (UBPR)
- State/National/Asset-Based Aggregate Analysis
- FDIC Summary of Deposit Data
- Office of the Comptroller of the Currency Canary Report
- Investment Banks
- 3rd Party Data and Analytics Provider
Means of Conducting Peer Analysis: FDIC Website

**FDIC Website and FFIEC CDR**

- Manual process of downloading individual bank 031 and 041 call reports from the FFIEC Central Data Repository’s Public Data Distribution Website
- Inputting data into Microsoft Excel Workbooks by hand
- Time Consuming – Should be reallocated to revenue related activities
- Potential for human error
- Accuracy – not capturing restatements
  - Banks can go back in time and restate or amend their call report filings
  - Essential that you are using the most accurate data relevant to your peer analysis
- Capturing data at holding company level for consolidated filers is conducted through the National Information Center (NIC) website
FDIC Uniform Bank Performance Report

FDIC UBPR is an analytical tool created for bank supervisory, examination, and management purposes.

Concise format

Shows impact of management decisions and economic conditions on a bank’s performance and balance sheet composition – safety and soundness

Preset group of peer banks – comparable in asset size, geography and/or tax status

Regulators also looking at the UBPR

Produced quarterly

Published 30-35 days after the date of a call report or on the call report due date

For example, March 31, Call Report is filed by banks on April 30, and UBPR will not be available until early June.
FDIC Summary of Deposit Data

FDIC Summary of Deposits (SOD) is the annual survey of branch office deposits for all FDIC-insured institutions including U.S. branches of foreign banks

Data as of June 30 of each year and released in October

Access data by:

- Single institution
- Institutions within geographic area
- Aggregated within geographic area

Market Share analysis to determine biggest players and competitors in a defined market down to Zip Code level

Aspects to Consider:

- Reliance of a Bank on a particular market relative to their total deposits
- Proximity Analysis
- Rate Intelligence – understanding pricing in markets down to a branch level
Office of the Comptroller of the Currency Canary Report

- Set of risk measurement tools developed by the OCC to identify institutions are risk for future financial distress
- Coal mine interpretation
- 15 financial ratios calculated and compared to OCC benchmarks
  - If a bank has a ratio that exceeds the benchmark – 1 is assigned
  - If a banks has a ratio that is below the benchmark – 0 is assigned
  - Zeros and Ones summed – if > 8 → Institution is considered by OCC to be at a higher risk for future financial distress
- 3 categories: Credit Risk, Interest Rate Risk, and Liquidity Risk
  - Credit Risk – 6 calculated ratios provide insight into whether or not a bank is adequately protecting itself in case of adverse developments in credit quality
    - i.e. composition and growth of the loan portfolio
  - Interest Rate Risk – 4 calculated ratios provide insight in exposure/impact of changing interest rates
    - i.e. Long-Term Assets/Assets and Residential RE assets capture level of repricing risk
  - Liquidity Risk – 5 ratios provide insight into funding structure and ability to meet debt requirements in near term as well as reliance on higher cost borrowings that are credit and price sensitive
    - i.e. Noncore funding dependence and reliance on wholesale funding
Means of Conducting Peer Analysis: Investment Banks

- **Investment Banks**
  - Reliance on investment banks for peer reports
  - No cost directly associated with peer reports
  - Lack element of hands-on customization
  - Not dynamic
  - Lots of back and forth to define a peer group
  - Time consuming
  - May not fully understand your growth, funding and lending strategies
    - This could be exposed through different angles of your peer analysis
Means of Conducting Peer Analysis: 3rd Party Data and Analytics Provider

3rd Party Data and Analytics Provider

- Evaluate the offerings of different providers
- Fixed Peer Groups vs. Element of Customization
- Level of Access Variations – Pay by user vs. Enterprise-wide access
- Niche focus vs. Broad Coverage
- Complete package – Peer Analysis, Market Analysis, M&A, News, etc.
- Compatibility with in-house data
- Level of support and training
Future of Peer Analysis
Future of Peer Analysis

- SNL Peer Analytics
- SNL Performance Analytics
- SNL UBPR Template with Directional Shading
- Regulatory Developments
  - Dodd-Frank
  - Basel III
  - Financial Accounting Standards Board
SNL Peer Analytics

- Interactive platform – easy to use, save time, and better leverage internal resources
- Fine-tune your balance and improve performance with peer benchmarking
- Comparisons against bank and credit union peers
- Pre-defined Regional, State, UBPR-like and asset based peer groups and custom peer groups
- “Comparability Score”
- Default peer logic that has been fully vetted by industry experts – logic is fully customizable
- Build custom reports with over 10,000 financial and market data points, including UBPR metrics
- Easily build customized peer charts and export presentation-ready graphics to PDF or Microsoft Excel.
SNL Performance Analytics

- Provides in-depth understanding of the factors driving ROAE for US banks and thrifts
  - Via tree-like structure, ROAE is broken down into detailed components such as yield on loans, cost of deposits, service charges on deposits, salary expenses, provision for loan losses and several other revenue and expense drivers
  - Easily see how your bank is performing relative to a custom peer group as well as industry aggregates and indexes
  - Model “what-if” scenarios to see hypothetical ROAE resulting from changes to performance drivers
SNL UBPR Template with Directional Shading

- Allows you to view a 5-period portrait of the financial trends and operating results for a bank, alongside a custom peer group
- Peers can also be UBPR Peer groups (State/National/Asset-Size)
- Provides context and clarity to executives and board meetings
- Easily identify key trends
- Analyze performance over time
- Set appropriate goals for future performance

Directional indicators help you visualize your bank’s areas of strength and weakness against peers.

Fully customizable percentage threshold to see where you are out- or under-performing peers.
Future of Peer Analysis: Regulatory Developments

**Regulatory Developments**

- Need access to data on the fly surrounding new regulation
- Build reports quickly to keep board members well informed
- Recent Regulatory Developments to Consider:
  - Basel III
  - Dodd-Frank Act and Elimination of the Office of Thrift Supervision
  - FASB Proposal around Loan Loss Reserves
  - Office of the Comptroller of the Currency Guidance on TDRs
Future of Peer Analysis: Regulatory Developments

**Regulatory Developments**

**Basel III Regulation**

- Basel III is a global regulatory standard on bank capital adequacy that strengthens bank capital requirements and introduces new regulatory requirements on liquidity and leverage.

- New capital measure called “Common Equity Tier 1 Capital” was introduced

- New Adjusted Risk Weighted Assets – increase in risk-weighted assets for 1-4 Family Loans based on LTV of the loans, Acquisition, Development and Construction loans (HVCRE), and Past Due Loan Exposures.

- Important to understand your new capital stance relative to the competition if all proposals were to be adopted

**Dodd-Frank and Elimination of the OTS**

- 2010 adoption of Dodd-Frank Act mandate

- Savings Institutions began filing Call Reports

- Heavier Reporting Burdens → 2500 line items vs. 1500 line items

- Importance of Common Regulatory Financials – metrics similar amongst call report and historical thrift financial report (TFR)

- Essential for Trend Analysis
**Regulatory Developments**

**FASB Proposal on Reserves**

- Financial Accounting Standards Board proposed improvements to Accounting for Credit Losses on Financial Assets on December 20

- Aims at more timely recognition of credit losses and more information for investors about the reasons behind your bank’s projections

- “Incurred loss” vs. “expected loss” model
  - Incurred Loss – requires banks to set aside money for troubled loans when losses appear probable or have begun to pile up
    - Issue – Difficult reads since reserve levels have swung wildly
  - Expected Loss – Proactive approach - requires banks to immediately project all losses on loans (for the life of each loan) and debt securities and then set aside money to offset such losses.
    - Goal – Smooth out reserve levels, provide consistency, and more up-front information

- Action plan in place, evaluate accounting tools and due diligence on reserve analysis

- Potential for banks to have to increase their loan loss reserves by as much as 50%
Regulatory Developments

OCC Updated Guidance on TDRs

In its June 2012 Bank Accounting Advisory Series, the OCC issued updated guidance on Troubled Debt Restructurings.

Loans discharged in a Chapter 7 bankruptcy must be written down to its underlying collateral’s fair value and classified as a nonaccrual TDR.

Reasoning: Borrower has been removed from responsibility of making payments.

Amount carried on books in excess of fair value of collateral must be charged off as uncollectible.

TDRs jumped by $14.49B in 2012Q3, with nonaccrual TDRs increasing to $58.57B from $45.77B in 2012Q2.
Peer Analysis Best Practices
Questions?