DIRECTOR EDUCATION - BASICS

by Steve Brown

We hear from bankers that at times, they wish they were chameleons. This would allow them to change quickly to help blend their directorship into a formidable force to help the bank along. Some bank management teams really feel their board is actively engaged, while others aren't so sure. No matter what your environment, this week we will focus on providing training to help everyone better understand the ins and outs of directorship. Whether you are a bank director yourself, officer or employee, the information we will be providing should be helpful in raising awareness and creating additional understanding in this quickly changing environment.

It should be noted that the board of directors is ultimately responsible for the conduct of the bank. The board is accountable to regulators, depositors, shareholders and even the communities served by the bank. To ensure the bank remains strong, directors must be independent and attentive. The basic structure is that shareholders elect the board of directors to consider the bank's interests before their own and oversee bank management in the process. These factors are the underpinnings of a good board.

While many directors we know are great business people, some may not fully understand the complexities of the banking industry. Unlike a small business, most of the funding for banks comes directly from depositors. This adds a wrinkle unique to banking as the funds are then reinvested into loans or investments. The goal is to provide a reasonable return to shareholders, given an acceptable (and board determined) risk profile. That sounds simple enough, but as we have seen recently - when economic conditions deteriorate quickly, even the best laid plans can result in unintended consequences.

Every bank director is also going to eventually interact with the regulatory agencies. By structure, banks take insured deposits, so the quid-pro-quo is that the government wants to make sure the bank is using insured deposits wisely. The way this is accomplished is through a regular examination process, which includes a review of most bank activities.

This interaction and review process has become very obvious in the current environment and many bankers are reporting an extremely rigorous regulatory examination process. Given the extent of the credit crisis, additional loan writedowns and increased pressure to boost loan loss reserves, this is to be expected. Unfortunately, the high level of regulatory pressure has also resulted in unintended consequences. Most boards have experienced the most rigorous examinations of their directorship. The result has been a predictable one. Given a tough examination process, directors have aggressively throttled back the risk they feel their bank should be taking right now. While generally that may be good, right now it has also led many boards to demand their management teams tighten credit standards and focus on maintaining capital ratios by deleveraging. Perhaps even more problematic, the cycle of a tough exam and resulting lower lending activity by the bank will not be reversed until directors see first-hand (thorough their next examination) that the examination report does not include new downgrades or other problems to be addressed. The examination timing process is a slow one, given most are annual; but it is also the only one we know that will serve to reverse the current trend of continual reductions in lending activity. Until then, look for directors to apply pressure on their banks to reduce risk across the board and cut back on lending activities, until they hear the 'all-clear' sound from the regulators after an examination.

Banking is about properly managing risk and directors play one of the most critical roles in that endeavor. We'll continue our discussion on the role of directors tomorrow, as we evaluate the changing nature of the environment. As can be seen, to be a bank director these days, sometimes it helps to have the traits of a chameleon.

BANK NEWS

Bank Failures (20 YTD)

Marco Community Bank ($119mm, FL) was closed by the State with its assets and deposits (1.5% premium) assumed Mutual of Omaha Bank ($3.8B, NB). The La Coste National Bank ($54mm, TX) was closed by the OCC with its assets deposits (0.51% premium) assumed by Community National Bank ($112mm,TX). George Washington Savings Bank ($412mm, IL) was closed by the State with its assets and deposits (0.31% premium) assumed by FirstMerit Bank, N.A. ($10.7B, OH).La Jolla Bank, FSB ($3.6B, CA) was closed today by the OTS with its assets and deposits (no premium) assumed by OneWest Bank, FSB ($18.8B, CA). For details and graphics on the closed banks, go to https://biganalytics.bancinvestment.com/

Housing Help

President Obama announced that $1.5B of TARP funds will be directed to those states that have suffered a 20% drop in housing prices or more. These states are: CA, NV, FL, AZ and MI.

Credit Cards

The new credit card rules go into effect today that will mandate greater transparency and limitations on fee generating tactics. However, some banks have already established new "inactivity fees" or raised their annual fee to compensate. The Fed has established a slick Flash driven site to help explain the new changes to consumers: http://www.federalreserve.gov/creditcard/

Copyright 2018 PCBB. Information contained herein is based on sources we believe to be reliable, but its accuracy is not guaranteed. Customers should rely on their own outside counsel or accounting firm to address specific circumstances. This document cannot be reproduced or redistributed outside of your institution without the written consent of PCBB.