DIRECTOR EDUCATION - EXAM PREPARATION

by Steve Brown

Sometimes you can be wandering along day dreaming and a song enters your head. It may have come from deep within your subconscious or it may have wafted out of a nearby window. Music, like banking examinations, can come from anywhere and either be music to your ears or quite jarring indeed. Since banks are always trying to figure out where regulators are going to crack down, we take a moment to try and help clarify things. As a director, understanding what regulators are looking for can be as difficult as writing a song that reaches the Billboard charts.

When regulators wander into a bank for an examination, they are there to review risk management systems, policies, procedures, processes and personnel. When they find significant deficiencies in one or more of these components, they will probably surface it as a deficiency in overall risk management. Here is what they are looking for in each critical area:

Policies are designed as a way to capture the board's intent toward risk tolerances and in achieving results. They are designed to set standards. Strong policies tie into the banks values, principles and clarify risk tolerance. They should clearly articulate standards/responsibilities and directors need to ensure policies are adhered to by the management of the bank. Regulatory examiners will typically check bank results against policy parameters to make certain risks are controlled, exceptions are clearly and actively reported and modifications to policy have all approved by the board of directors.

Procedures are yet another way banks will pursue objectives. These can include programs and practices, but are designed to define how daily activities are to be carried out. Top performing banks have strong processes that are not only consistent with policies, but also highly efficient. Here, regulators are looking for directors implement a series of checks and balances. In other words, the board must show that the proper risks are being monitored, understood and that they are proactive in making corrections in a timely manner.

Management teams are another area where regulators are taking a closer look these days. Directors should know they have the responsibility to ensure personnel at the bank in top positions are qualified, competent and perform as expected. It is important that directors make sure executive management teams adhere to the bank's mission and that all policies have been followed. As stresses have increased, management teams have come under increased strain. Regulators will be looking for directors to have compensation programs that attract, develop and retain qualified personnel; but do not add unacceptable risk to the organization.

Finally, directors should be receiving all reports needed to make sure they clearly understand what is going on within the bank. Some reports should focus on credit, while others may measure performance, track interest rate risk or other exposures. Directors must have the tools and technology to support a rigorous assessment of the effectiveness of management teams and bank performance. In addition, reports must be timely, accurate and easy to understand. Regulators expect directors to be armed with the information they need to not only measure performance, but also assist in organizational decision-making.

Tomorrow we will tackle the committee structure of a board and introduce final key concepts, as we close off our discussion this week on the important subject of how to be an effective director. Until then, please hold as you enjoy the music.

BANK NEWS

FHLB 4Q

he banks reported a $552mm profit compared to a $715mm loss in the 4Q 08. The 12 banks also took a $436mm charge for bad mortgages.

Mobile Banking

We are closing off our mobile banking survey that we are conducting as part of our Executive Management Conference in May. If your bank has or is thinking about having a mobile banking platform, please take a minute for our survey. In exchange, we will not only give you the survey results, but will provide you with our vendor analysis comparing different offerings when complete in May. Go here to take the survey: http://www.zoomerang.com/Survey/?p=WEB22A9EHDJZ3Z

Mortgage or Credit Debt

A study by FICO found consumers with scores over 760 defaulting 2X more often on mortgages than credit cards in 2009. The inverse is true for consumers as a whole, with card accounts defaulting 1.6X more often, though the trend has dropped from 3X more in 2005.

Accounting Changes

The SEC agreed to support a single set of internationally accepted accounting standards. Before this can happen, several differences between IFRS and FASB need to be resolved.

Employment

To solve the unemployment problem, it is important to get small businesses hiring again. In fact, the BLS indicates businesses with less than 20 employees account for 38% of all job gains and those with less than 500 employees make up 77% of all hiring.

Credit Card Profit

House Financial Services Chairman Barney Frank (D, MA) also told attendees at the CUNA that Congress will not tackle interchange fee reform this year.