BULLYING CAN HARM ONE'S REPUTATION

by Steve Brown

The odds are 1 in 3.1 that a student will get bullied at school during the school year. Bullying happens when kids take teasing too far and shift into a mode of intentional tormenting another child through physical, verbal or psychological actions. Nearly every school has a bully and nearly every child can tell you who it is. Unlike bullies who don't care about their reputations

very much, community bankers do. Much has been made about reputation risk in the banking

industry for obvious reasons. In fact, the FFIEC defines reputation risk as the risk that negative publicity regarding an institution's practices will lead to a loss of revenue or litigation. That is important, so protecting the bank's reputation is one of the most important jobs any management team must face.

In an interesting study, BusinessWeek sought to calculate the amount of shareholder value attributable to reputation. The results are interesting, because while 97% of senior executives surveyed rated reputation risk as a high-level concern, most said they did not specifically measure, monitor or manage reputation risk. That is particularly scary when you consider for most banks somewhere between 40% and 70% of market capitalization according to the study are driven directly by reputation.

We have been in countless risk management meetings and what invariably comes up at one point or another is that reputation risk is simply too squishy to quantify or track. While that may be true at some level, brand communication, investor relations and other factors clearly need to be coordinated; given the potential impact reputation risk could have on the bank.

Whether a bank is trying to protect and monitor corporate, regulatory or stakeholder communication; our global technology environment makes things even more difficult. Banks should have established processes to handle crises as they arise and also incorporate business relationship management. Banks need to be sure they are thinking about their own reputation when they evaluate business partners, customers and other potential connection points. A strong due diligence process is mandatory, as it will ensure partners are good ones at the beginning and remain so over the longer term.

Another study of international financial firms on reputation risk reported recently by The Economist found such risk can be caused by many things and come from many sources. Risk managers surveyed ranked the failure to comply with regulatory or legal obligations as the single biggest threat to reputation. That was followed by a failure to deliver minimum standards of service and product quality to customers; unethical practices; security breaches; failures of crisis management and risk by association with third parties that fail to perform. Now that these areas of reputation risk have been highlighted, the question remains as to what a community bank can do to protect itself.

Start by monitoring external perceptions of your bank. These can include blogs, internet posted comments, newspapers, etc. Assigning someone internally to periodically check for negative news about the bank is important. Next, train employees to know what to look for. They can be a great line of defense and quickly thwart those who would intend to harm your bank. Finally, banks should have a program to systematically track, report, and respond to these risks. This should include a robust contingency plan that focuses on acknowledging a potential issue, committing to fix it and moving quickly to control and isolate the problem.

By communicating quickly and effectively to employees, customers, stakeholders and others; banks stand a much better chance of helping everyone understand the issue while demonstrating the bank is aggressively taking action to address any problem.

BANK NEWS

Closed Banks (26 YTD)

Sun American Bank ($536mm, FL) was closed with most assets (loss share) and all deposits (no premium) assumed by First-Citizens Bank & Trust ($15.8B, NC). Bank of Illinois ($212mm, IL) was taken over with Heartland Bank and Trust Company ($1.5B, IL) assuming the assets (under loss share) and deposits (3.6% premium). The assets and deposits of Waterfield Bank ($156mm, MD) were placed in an OTS bridge bank with deposits being returned. Centennial Bank ($215mm, UT) was shut with depositor funds returned.

Ugly Potential

An FDIC auction of more than $1B in loans next month could impact community banks nationwide. About 63% of the loans are participations and banks are worried they may have to take writedowns on their own stakes as a result of the sale. The FDIC reports sales of performing loans from failed banks in 2009 delivered an average 43% of book value, while nonperforming loans were sold at 26% of book.

Small Business

The National Small Business Association reports 59% of those surveyed used credit cards to finance their businesses and 33% had seen their credit lines decreased over the past 12 months. In related news, the SBA is expected to re-instate the higher, 90%, guarantee amount and lower fee structure that was originally set by the 2009 American Recovery and Reinvestment Act but since expired.