Real Tennis and Banking

by Steve Brown

We spent some time watching US Open tennis on the tube recently. The athleticism is fantastic and the tournament is a real showcase for New York City. We also found out that the modern game is pretty wimpy compared to the beginnings of the sport. Tennis in medieval times, now that was challenging! The enclosed court had numerous obstacles - slanted roofs that one could bounce balls off, a flying buttress, a cowbell and a ball sent through a strategically placed window brought points to a sudden end. The game was more like pinball than modern tennis. The ball had about as much bounce as a dropped shoe and the racquet face was about the size of a cantaloupe. Henry VIII was quite an avid player until he filled out to the rotund size that we see in most portraits. The sport did not have a good reputation though and it was eventually banned in 17th Century England in an effort to curb a gambling epidemic.

All risky pursuits have repercussions and we learned of some interesting developments regarding bank directors of failed institutions, the assessment of civil money penalties and insurance policies designed to protect in such circumstances. It's been said every credit crisis has its cycles - the crash phase, the recovery and finally retribution. Congress passed legislation in the 1980s that significantly increased the penalties for both banks and individuals who violated laws and regulations (or for violation of conditions imposed by any of the Federal Banking agencies in a written agreement between the bank and the issuing agency).

Failed bank litigation has piled up as bankers and regulators alike worked through this credit cycle. Now, examiners are leveraging "lessons learned" from the crisis and are digging a little deeper in a number of areas as they look to recover future losses to the FDIC fund. As such, D&O insurance policies are of keen interest as a way to do just that. In particular, regulators are interested in policies with a "regulatory exclusion" that could limit what might be available to the FDIC. Typically one would expect a focus on bank liability insurance policies for such endorsements, but regulators are looking into bank D&O policies as they review "Civil Money Penalty" endorsements. If they find such an endorsement, the bank can be cited with a violation of regulation and be required to have the endorsement deleted from the policy.

There is a regulation which stipulates that a depository institution may not purchase an insurance policy that could be used to pay or reimburse the cost of any judgment or civil money penalty assessed against officers and directors in an administrative proceeding or civil action commenced by any federal banking agency. This regulation can be found in the Deposit Insurance Act (12 USC1828(k) Part 359.1(1) (2) Golden Parachute and Indemnification Payments.

To be sure, this is a relatively recent approach and it's even possible that the bank's insurance agent used such an endorsement in the policy as a "selling point". This new focus in reviewing bank insurance though, has brought to the forefront a rule that may have been overlooked before. Bankers should know this and check with their insurance carrier as well as the policies directly to be sure they don't carry prohibited Civil Money Penalty Endorsements.

As with our medieval tennis example above, this is but one more example of how negotiating your way through regulations often feels like the tennis ball itself, as you are knocked around all over the place during the game.

BANK NEWS

Branch Closure

Pioneer Community Bank (WVA) will close 2 branches in West Virginia due to their low profitability.

Regulation

The FDIC is reportedly preparing to issue guidance around payment processors. The FDIC is concerned banks doing business with entities such as online short-term lending, telemarketing, debt consolidation, online gaming, online tobacco, online firearms sales and online pharmaceutical sales companies are engaged in higher risk activities that are not permissible under state and federal law.

Refunds

US Bank will pay some 2.7mm people refunds totaling $55mm related to a settlement around overdraft fees charged in prior years.

Bigger Bailout

On Friday we ran the story that the FHA was expected to seek $1B from the Treasury. They ended up asking for $1.7B due to hits related to its reverse mortgage program, lower loan volumes and higher interest rates.

Employees

McKinsey research finds the interaction tasks that take up the average worker's week are doing role specific tasks (39%), reading and answering email (28%), searching and gathering information (19%) and communicating and collaborating internally (14%). A shift from one-to-one communications to one-to-many using social channels could improve productivity up to 25% according to McKinsey.

CRO Job

A Deloitte Global risk management survey finds 80% of institutions responding said the job of the chief risk officer is to escalate risk issues to the CEO and/or the board, identify risk concentrations and identify new and emerging risks. This same percentage said internal audit also audits the activities of the CRO and enterprise risk management. Another best practice for community banks.