theBHCA.org — Summer 2019

Bank Owner

Bank Holding Company Association Magazine

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Bank Owner

Summer 2019

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The Bank Holding Company Association, founded in 1981, welcomes Members from around the country. Holding companies of all sizes from throughout the Midwest make up a majority of the current membership. Companies that serve bank owners, their holding companies and banks, are welcomed as Associate Members.

The *Bank Owner* magazine is the quarterly publication of the BHCA. The magazine is your best source for BHCA information, including upcoming events. Members receive the magazine in the mail and have access to an online version in the members-only section of our website, theBHCA.org. Managing Director Tom Bengtson serves as editor. Contact him at (952) 835-2248 or 1-800-813-4754 or email us at info@thebhca.org.

Strategic planning will help association navigate changes

By Rick M. Wall
Highland Bancshares, Inc.
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The Bank Holding Company Association is the only one of its kind in the nation. We are unique. We are strong, with significant resources. Our members find value in belonging to the association, and in attending our events.

Given these strengths, the board has decided to conduct a formal strategic planning process to set a path for the association for the coming years. We have engaged Skip Rock Consulting to assist us with the strategic planning process set to begin this summer. Jaime Nolan, the principal at Skip Rock, has been hired to take the board of directors through a planning process. Until just recently, Jaime was the CEO and owner of IntrinXec Management Inc., a leading association management company. During that time, she worked with associations and small businesses on strategic planning, board governance, team development and organizational culture.

The BHCA has many strengths, including its executive director, Tom Bengtson, whose knowledge of our industry and passion for communication and event planning has benefited us all. Other members of his team, including Kelly Bauer and McKaela Laxen, make our events run smoothly, professionally and have made it easy for us to network, and grow in our industry knowledge. Another strength is that Tom is looking for ways to improve the Association, witnessed by the recent addition of a new directory and the recent geographic expansion.

This year the BHCA, at the suggestion of Tom, initiated a new product, a bound directory of all the holding companies in the country. You should have received your copy in the mail about a month ago. The association partnered with the Federal Reserve Bank of Minneapolis to obtain the data and present it in a format that is easy to use and understand. We are pleased that many of our associate members chose to support the directory. Please let us know what you think of this new offering.

Also, Tom recently further expanded the reach of NFR Communications, his publishing business, by purchasing the Kansas City-based BankNews Media. The deal brings together two media companies that each have more than a century of history. With this combined outreach, Tom and the BHCA will have more contacts and connections with bank holding companies in the Upper Midwest.

One of the questions that faces the BHCA is how much, if any, to expand the scope and offerings of the association. Unlike several years ago, when the BHCA only hosted events in Minneapolis, the BHCA has recently hosted events in Kansas City, Iowa and Wisconsin, and has considered other states as well. Should the association continue to geographically diversify? Another question the board needs to address is how else to serve its membership. Are there other kinds of programing, events or information that the BHCA could provide that would help us all be better in our businesses?

Should you have any insight on how you think the BHCA should evolve, please feel free to share it with a board member, Tom or me. We would like to have your insights to help us with our strategic planning process.

As banks consolidate, the number of holding companies and individuals involved in bank ownership will be decreasing. Combine that with the increasing pace of change in the financial services industry and those of us who are owners and executive operators will even more need an association to help us keep up with the pace of change within our industry and will continue to need a forum for connecting with other executives and owners in our field.

Thank you for your support and membership. I hope you have a wonderful summer, and I look forward to seeing you at our Fall Seminar, set for Oct. 7–8 in Bloomington, Minn. ■

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Big year underway; What we can learn from history

By Tom Bengtson
BHCA Managing Director

It's been a big year so far for the Bank Holding Company Association, with two successful seminars already completed and plans well underway for a Fall Seminar. In addition, we launched a brand new product and we are just beginning a sweeping strategic planning process. (See "President's Observations" column.)

If you attended our *Bank Owners' Bootcamp* Seminar in Kansas City or our *Innovation and Performance* Spring Seminar in Bloomington, Minn., I extend to you my thanks. I understand how busy everyone's schedule is; we at the BHCA understand it is not easy to carve out a day or two from your schedule, even for the best events. My sense is that the momentum on the Kansas City event is building. This was our second year in the City of Fountains and we look forward to continuing to cultivate that event with meaningful education for bankers in Kansas, Missouri, Oklahoma, Iowa and Nebraska. Judging from the evaluations turned in by attendees, our Spring Seminar was a real hit. The speakers delivered practical and thought-provoking messages. Whether it was our panel from the Innovation Center, the futurist, the succession planning expert, or any of the other consultants who spoke, I consistently heard useful presentations that informed, inspired and even entertained.

In addition, I hope you have had a chance to see the National Directory of Bank Holding Companies we launched this spring. It makes eminent sense that the Bank Holding Company Association should create this kind of product. We have a great relationship with the Federal Reserve Bank of Minneapolis, which provided the data. We sincerely appreciate their partnership on this product. We have tried to present the holding company lists, with their subsidiaries, in an easy-to-read format. I know there are other ways to get this information, but I am not aware of any other comprehensive list. The advertising support from our associate members was so strong that I expect we will be offering updated versions of this directory every year. Save your current copy and use it as a handy reference. We are most pleased to be able to offer this service.

As the Independence Day holiday approaches, I am reminded of one of my favorite books: "1776" by the popular historian David McCullough. While I learned a lot about the Revolutionary War by reading this book, I also picked up at least four lessons that I think any small business owner would find applicable. They are:

Goals change. The book demonstrated that it is okay to raise your expectations once you get into something. In 1775, the rebel Americans were merely interested in representation in the British Parliament. It wasn't until spring of 1776, after Americans won a major victory at Boston, that the rebels elevated their cause to full blown independence. In business, we make plans but we shouldn't be reluctant to alter those plans if the situation changes.

It takes a long time. The Revolutionary War ended with the signing of the treaty at Paris in 1783. The war lasted eight years! Nobody who went into the war expected it to last that long. My experience in business is that nearly every venture takes longer than expected to pay off. If you want a realistic shot at success, you have to be willing to stay in it for the long haul.

People are fickle. We think of General George Washington as a hero, but back then few people were truly loyal to the man who became this country's first president. When times were good, they praised him but when times were bad, they blamed Washington. His No. 2 officer even wrote letters behind his back, second-guessing his decisions. Leaders at all levels have to expect this. When earnings are good, everyone loves you, but hit a rough spot and people will grumble behind your back. Washington kept an upbeat public persona, privately considering the criticism of foes and making adjustments where he thought appropriate. That's a good model for any leader, whether you are heading an army or a business.

You can succeed, even against great odds. The Americans won independence with a rag-tag army made up mostly of untrained farmers. They went up against the most powerful military in the world. The Americans won because they wanted victory more than the British. The revolutionaries were fighting for their lives while the Brits were fighting only to hold onto one more piece of the empire. Anyone who runs a small shop should remember this. Fight for your life and you can win, even against the world's largest and most sophisticated competitors.

We live in a great country at a great time in history. Enjoy your summer, and I look forward to seeing you this fall at our Oct. 7–8 Fall Seminar. ■

Don't look to core processing giants for innovation

Smaller banks are more than capable of keeping pace with their bigger competitors in the fintech arena — just don't look to traditional partners to do so. That was the message Aaron Silva, founder and CEO of the core and IT negotiating firm Paladin fs, gave to attendees at the 2019 BHCA Spring Seminar held May 6–7 in Minneapolis.

"We know as a market community banks are not performing nearly as well as the large banks," Silva said. The industry "bigs" have poured millions


Aaron Silva

of dollars into upping their fintech games, and conventional wisdom has it community banks can't compete due to budget limitations and missing out on economies of scale. Not so, Silva assured his audience.

"You'd be surprised at how inexpensive it is to do a few things that really could make a big difference and give your bank that kind of cutting edge image and feeling," he said.

Like the big banks, large tech companies and core providers lack the nimbleness required to be truly innovative, Silva said, and they frequently buy smaller companies that offer useful products — only to eliminate competition and take the item off the market. Because there are so few core processing companies and their customers' are frequently locked into spendy, long-term contracts with hefty termination fees, they have a captive market. "They're doing just the minimum they need to do to keep the industry surviving, but they're not doing anything to help the industry thrive," he said. "We have these vendors that are holding us by the hair that are not innovating."

Fintechs fall into three buckets, Silva said: those that want to poach banks' customers for their own, fintechs that are willing to collaborate with banks, and the vendors that lag behind in bringing useful opportunities to their customers. It's the "Goldilocks" middle category that community banks should seek out. He said there are databases available that list many of the fintechs that want to partner with community banks.

An opportunity to collaborate with a fintech partner exists for a task like typing in large chunks of data, such as from loan applications; people can be replaced with robotic process automation. "You can train an RPA for less than $50,000 that will pay for itself in just a very short amount of time to do those repetitive tasks," Silva said.

Bankers can also be caught flat-footed due to their lack of familiarity with how software and coding works, not just on a technical level, but on broader strategy issues as well.

A key consideration for any bank, but especially those that want to up their fintech game, is whether it is an omnichannel bank or a mobile-first bank. The former offers many different ways of interacting but unifies the customer's experience while the latter prioritizes the mobile compatibility of all its functions. Mobile-first is the most difficult to get right, but also offers the greatest cost savings across a franchise, Silva said, because everything is oriented around one channel.

Once you decide whether to pursue omnichannel or mobile-first "everything else falls in that context," he said. "So when you select a new fintech supplier, [you have to ask] do they have a mobile solution that works with that choice?"

For banks ready to cut the cord on their core processor, a virtual or direct bank is a hot topic. In this scenario, the bank builds its own data warehouse and digital-only bank without geographic restrictions with an integrated appearance. "It's a way for banks to lessen their reliance on or de-handcuff themselves from the core provider because at the end of the day, that's really what we have to do," Silva said.

There is not yet a cloud-based core provider to pit against traditional providers — that solution is at least three to five years away — but this increased competition will only bring good things, Silva said. By then, "you will have systematically, over time, chipped off all of their inferior ancillary products, their online banking, their mobile, their bill pay, and you've gone to other,

Aaron Silva, *Continued on page 15*

Consultant encourages community bankers to do the digital shift

The "digital shift" is not a dance, but bankers need to prepare for it even if they feel like they have two left feet.

Speaking at the Spring Seminar of the Bank Holding Company Association on May 7, Steve Williams, president and partner at Cornerstone Advisors, urged bankers to make the most of digital opportunities to enhance the customer experience. Community bankers need to be life-longer learners, he stressed, and ultimately perfect their organizational development skills so they cultivate teams that can compete against the largest financial services industry players.

Williams put the current competitive environment into perspective. About 10 years ago, small banks were awash in liquidity and the largest banks were struggling to get deposits. Today, largely because the largest banks have so successfully developed their digital channels, they have ample liquidity to fund their loans. Most of the deposit growth in the last decade, Williams pointed out, has occurred at the top end of the banking industry with the nation's four largest banks growing their collective deposits by $2 trillion.

While the year 2008 is largely remembered among bankers as the year of a financial crash, it also was the year the iPhone was introduced. It was the first of the "smart phones" and marks the real beginning of the mobile banking movement. Historically, when large banks made acquisitions, neighboring community banks celebrated because the customer run-off post-acquisition usually meant lots of new customers for the community bank. Since so many large bank customers now rely on mobile channels, they tend not to notice when their bank makes an acquisition; the customer run-off is not taking place the way it once did.

The largest banks also are discovering they can close branches with little impact on the number of customers they serve since so many of them are using mobile channels and rarely come into an office. Williams stressed these are not solely retail customers. "Fifty-six percent of small business owners," he said, "like to use mobile for their business banking."

Williams said the big banks have "nailed the digital shift." Digital readiness, Williams said, is "more organization and process, than it is actual technology." Only about 30 percent of the effort is technology, he estimated. Furthermore, a digital bank does not need to convert 75 percent or more of its processes and products to digital. "More realistically, it is about 50-50," he said.

Steve Williams

Priorities for community banks should include building capability to market through digital channels, Williams said. By implementing digital systems, banks should be "reducing the friction out of these relationships because the big banks have already done that," he said. Digital systems should help a bank engage customers on an on-going basis.

But the challenge is that community bankers need to do this on their own. "You can't call Fiserv and ask for a 'future-ready' bank," he warned. "This is not just about the core system. You need web content management; you need origination systems. You need all kinds of back-end systems. You are going to have to have IT expertise to manage all this."

At many banks, most profit is generated from commercial lending; some banks fear implementing digital processes in the commercial area because they think it will disrupt a proven successful portion of the bank. But Williams said bankers have to be willing to implement digital solutions in the commercial lending area. Good digital systems can monitor commercial loan portfolios and actually help lenders underwrite more effectively. For example, Williams

Steve Williams, *Continued on page 15*




Scenes from the May 6–7 2019 BHCA Spring Seminar: INNOVATION *and* PERFORMANCE

Hyatt Regency Bloomington-Minneapolis













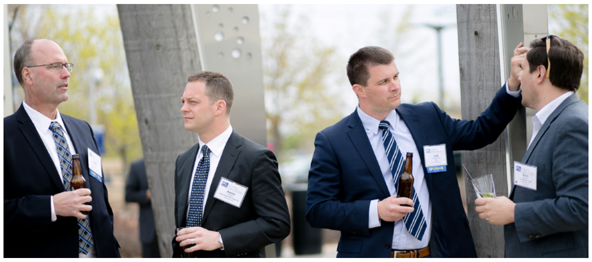







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The future ain't what it used to be — it's faster than ever

Technology is changing the world at an unprecedented rate; bank owners need to be aware of the change so they can "get ahead of the curve," futurist Jack Uldrich explained during the after-dinner presentation at the BHCA Spring Seminar on May 6.

Change is not occurring at a linear rate; Uldrich encouraged bankers to instead think of change as occurring at an exponential rate. To illustrate his point, he shared a story about a child who had to choose between $5 on the one hand, or one penny that doubles in value every day for 20 days. The child chose the five dollars, only to be told that a penny doubling every day would be worth $5,242.88 on the 20th day. The rate of technological change today is similar, he said, with surprisingly soaring results after some slower ramp-up time.

Uldrich showed a picture of a busy New York street in 1903, filled with horses and buggies. A picture of the same street 10 years later featured no horses, but a traffic jam of automobiles. "If you were in the horse industry, your world changed," Uldrich said. "We are all in the horse industry today."

Uldrich described several changes that are in the process of changing our lives. He described self-driving cars, which affect far more than the auto industry. He cited a store which is using self-driving cars to deliver groceries. Uldrich said as many as 50 percent of people who live in densely-populated urban centers say they have cars primarily to go grocery shopping. If the groceries are delivered to them, they won't need their cars. The money they save by avoiding the purchase of a vehicle may free them to pay off their student debt sooner, or purchase a home quicker than they otherwise would.

He also described a company that is manufacturing artificial meat, and a plumbing fixtures company that is making smart toilets which can be used to monitor users' health. He also noted that Uber, a tech-dependent company that did not exist a decade ago, now has a market capitalization in excess of all the major automakers combined.

"We need to buckle up, because the rate of technological change is not going to slow down," Uldrich said.

Uldrich listed 10 things that are growing at an exponential rate:

1. Bandwidth. "We are nowhere done," he said, referring to our ability to move electronic data. Most places have 4-G speeds, but he said 5-G is coming and it "will change the expectations of your customers; their expectations will go through the roof," he said, explaining that 5-G is 100 times faster than 4-G.

2. Augmented reality. "Digital information will come to us," he said. Companies will use augmented reality to more effectively show customers how to use their products. Banks, for example, might provide dramatic visuals showing the impact of saving money.

3. 3-D printing. A shoe company already is using 3-D printing to reduce shipping and warehousing expense. He said some auto companies already are printing parts with 3-D printers. He said a house can be printed using 3-D technology for as little as $10,000.

4. Robotics. A truck recently drove itself from California to Florida. There are 1.7 million truckers in the United States. "What will happen to them? How will we retrain these folks?" Uldrich asked.


Jack Uldrich

5. Internet of things. What happens when billions of things are connected by the internet? In some places, this technology is being used to provide highly targeted advertising messages.

6. Genome sequencing. Ten years ago it cost $100 million to sequence an entire person. The technology is rapidly improving, thus driving down the cost. Today, a person can obtain this service for $59. Uldrich said people will live much longer as a result. "What does this mean for retirement savings?" Uldrich asked as he encouraged bankers to provide education where needed.

7. Artificial intelligence. Virtual assistants such as Alexa and Echo are only the beginning.

8. Big data. The amount of data collected now is just the tip of the iceberg, he said. Companies will collect and store even more information about everyone.

9. Cybersecurity and privacy issues are also raised by the advent of technology, he concluded.

Uldrich urged people to try to keep up with the changes. He said human nature generally accepts change slowly. To illustrate his point, he asked people to identify the colors used on a "yield" sign. Many in the room of more than 150 people said yellow and black. Uldrich pointed out red and white signs replaced the yellow and black signs in 1971.

The BHCA is grateful to the following for their sponsorship of this year's Spring Seminar:

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Succession planning the 'last challenge of leadership'

With the median age of bankers creeping higher, succession planning has become an important part of a bank's strategic planning process. Tom Hubler, a succession planning consultant who specializes in working with family-owned companies, shared his insights into the sometimes fraught process of ownership transition on May 7 at the Bank Holding Company Association's Spring Seminar.

There are four focus areas to Hubler's "inside-out" succession plan: an ownership plan, a management and leadership plan, a business plan, and a family plan. The most fraught of those is often the family plan. "To avoid conflict over succession, especially in a family-owned institution, create win-win solutions where each person who has a stake in succession is committed to the other's success," Hubler said.

"The problem is, people get stuck in what I call win-lose situations. Whenever that occurs, it's always a lose-lose proposition.

"Nobody wants to be in their 60s and 70s and have their family disrupted by normal business and financial differences," Hubler said.

For longtime entrepreneurs, whether they founded the bank or have come in through successive generations, after 40 or 50 years, the idea of not doing it anymore is "like dying as far as they are concerned," Hubler said. "My belief is that owner/entrepreneurs don't have to leave the business but they need to change their job description and become the architect and the designer of a new ownership system, which includes the board of directors."


Thomas Hubler

No one is irreplaceable. Owners or directors or leaders have to find someone to take over. Sometimes the solution is creating a system that involves creating an active board of directors, Hubler said. "Make sure they're active."

Furthermore, the departing generation has become architect and designer of the new management and leadership system, which means training and preparing their next generation (which sometimes means adult children) for the responsibilities and stewardship of the bank. "That could be a 10-year process in terms of preparing the next generation for the responsibility, depending upon who they are and what their skills are," Hubler said.

Ultimately, the decision about who gets to succeed a current leader is the person who demonstrates the competency and the commitment. "The goal here is to help them rise to their highest level inside the organization or inside the bank," Hubler said.

In addition, there is also the issue of tax planning and wealth preservation planning. Sometimes people seeking to exit bank ownership want to retain a leadership role in bank management. This goal is attainable, but requires some forethought.

As for bank directors who are ready to retire? "You need to work with your organization to come up with a financial exit strategy to get your money out of the bank."

By Jackie Hilgert

By Brook Schaub

How forensic accounting uncovers secrets behind fraud

On the surface, forensic accounting and an audit may seem like they are similar services, but the fact is forensic accounting is significantly different. While an audit ensures the left side of the ledger matches the right side, forensic accountants are concerned with more than just figures. Using sophisticated software to identify possible fraud in documents, combined with skilled interview techniques and computer forensics, they can determine if a fraud has been committed, what pressures led to the crime, and what assets can be recovered.

Forensic accountants uncover the truth behind many frauds and schemes. Here are some examples.

Out of trust

The bank president was concerned about an auto dealership. The bank had a significant amount of depositor's money invested as a line of credit to the local car dealer. Periodic visits to the dealer to validate cars associated with the loans could not be personally inventoried. The dealer would profess that the vehicles in question were always "at the car wash" or "out for a test drive" or some similar excuse. Monthly reports to the bank were also creating suspicion that the dealership was paying too much money for vehicles in the inventory.

The dealership was a family-owned staple in the community. More recently, the operational reins had been handed down from retiring parents.

It became apparent to the bank president that perhaps there was out of trust selling and other issues that needed looking into. The investigation revealed that the bank had been defrauded of more than $1.5 million by various means. False monthly records to the bank were documented. Several employees were identified as being part of the scheme. They were duped into helping the fraud by the owner.

Computer forensics investigations helped to identify the pressure points that resulted in the fraud: Large personal expenses on company credit cards. Luxury vacations to Europe that included employees who helped commit the fraud, expensive clothing purchases, medical issues. All these things created pressure on the dealership owner. As an example, a single email was traced to a jewelry store in the Caribbean showing an almost $9,000 account credit. Having this information in hand, the forensic accountant could trace six-figure purchases of jewelry by the owner. Purchases on eBay, Amazon, and other online retailers could easily be documented from computer data through forensic tools, as could emails between those involved in the fraud. The dealer eventually was charged and convicted in federal court of bank fraud.

Another case centered on a successful construction business. However, total receipts were down and the owner could not figure out why there was a large amount of red ink on his ledger. A review by forensic accountants quickly identified the company accountant as the reason. Using one of several company checking accounts, he was embezzling more than $160,000 a year. To complete the case, computer forensics identified pressure for the theft and to try and determine if assets were recoverable.

The search began on the internet for digital information. Using the personal email of the accountant, public social media posts were found indicating that the accountant's leisure time involved significant visits to "gentleman's" clubs and visits to hotel rooms with the dancers. In one post, he acknowledged that he supplied one performer with $3,000 in one month for her various personal needs. Bank records showed the company checks being deposited and money withdrawn from the ATM machines at the club he preferred to visit.

The digital forensics investigation revealed that the accountant had numerous 401(k) loans outstanding. This information provided to the forensic accountant discovered that he was using company checks to repay the loans. Local hotel reservations for his trysts with the dancers were documented, as were other details on the company losses. In short, there were no recoverable assets to be pursued.

Computer forensics

Computer forensic examiners have seen an increase in business litigation related to breaches of loyalty and fiduciary duties by an employee. The changes in expectations of loyalty to one company can usually be defined by the age of the employee. Baby Boomers typically spent a lifetime being loyal to one company or organization. That is not the case anymore. Employees

Forensic Actg., *Continued on next page*

Aaron Silva, *Continued from page 6*

superior fintech suppliers," he said.

All too often, community banks are stuck with the vendors' offerings due to poor contract negotiation, he said. This gap led Silva along with others to found the Golden Contract Coalition in 2016.

"The point of the coalition is to bring together large numbers of community banks so that we can manufacture the leverage we need to force a negotiation with these core [processors] to get a fair contract," Silva said.

By the end of the year, it will have a little more than a billion dollars in total contract revenue as a negotiating chip, and Silva urged his listeners to consider the powers of collective bargaining carefully.

By Mara Gawarecki

Steve Williams, *Continued from page 7*

described a tendency some banks have to require too many covenants on some commercial loans, which can make those loans less profitable. With better data provided through digital systems, covenants can be designed to maximize the loan package.

Williams also encouraged bankers to take serious steps to understand their role in the payments system. Every bank should understand the payments business well enough that they have a strategy for making the most of it in their bank. "Who owns the P&L on the payments business in your bank? This could easily be a vice president level person," he said.

The biggest factor in achieving digital success is cultivating the right people, Williams said. Sometimes a bank can partner with a fintech to gain capability, but Williams warned that many fintechs don't have the same goals as banks. "They are interested in scaling and selling," Williams said. "They are not interested in doing the hard work of banking. Be careful who you partner with, and make sure you control the customer experience."

The best banks have engaged staff, and leadership makes a serious effort to hire and enable their people. Williams offered these observations about people who seem to work most effectively in banks that are serious about successfully undertaking the digital shift:

- They run their department according to Key Performance Indicators;
- They take ownership of their processes, and things that touch the customer experience;
- They have a vast exterior network of peers. They know what other folks are doing;
- They are analytical and use data to find answers;
- They are not victims of their vendors; they know the systems they use even better than the vendor's own help desks.
- They are not "super doers;" they develop teams, train people and build processes; and
- They always have a plan; they know where they are headed.

"Your job," Williams said, "is to find these people."

By Tom Bengtson

Forensic Actg., *Continued from previous page*

jumping to greener pastures or deciding to start their own competing business is becoming more common. Unfortunately, when the employee leaves, they frequently are leaving with a part of the company. Customer lists, marketing plans, product designs, bid sheets and invoices can go out the door with them. In some cases, they never leave the company. They just use the company knowledge and assets gained to start an internet company to compete with their present employer.

Computer forensics can provide value in any type of litigation, business or personal. Companies frequently use in-house IT resources for the review of digital evidence of wrongdoing. This policy can come with some litigation dangers, conflicts of interest being the most obvious. However, a business needs to realize when using in-house IT is appropriate, and when outside resources may be needed. The IT job is to keep the network host and client computers running smoothly and to correct any technical issues immediately. That is their specialty and their training. Computer forensic examinations are an investigation. Specialized examiners trained to follow the leads in a digital world to discover the truth of an issue. When combined with skilled forensic accountants, the matter can be quickly identified and resolved.

Brook Schaub is Computer Forensics Manager at Eide Bailly. He can be reached at bschaub@eidebailly.com.

Fed Notes is provided through a partnership the Bank Holding Company Association shares with the Federal Reserve Bank of Minneapolis.

How PASS Aids Regulators and Banks

By Ryan Bahr

The Payment Analysis and Screening System, or PASS, is a tool developed by the Federal Reserve Bank of Minneapolis to analyze payment data in order to risk-focus supervisory activities. The tool tracks payment activity of depository institutions (DI) using data from multiple platforms. These platforms include (1) FedCash, which helps DIs meet their cash demands; (2) checks, which are cash letters deposited or withdrawn by DI customers; (3) FedACH, a network that coordinates electronic payments and automated money transfers; and (4) FedWire Funds Service Data, a real-time gross settlement funds transfer system. PASS provides a systematic, controlled, and consistent process for providing Federal Reserve payment data to Federal Regulatory supervisory staff. PASS calculates the daily aggregate value of each DI payment activity. It also provides ongoing, institution-specific analysis and reports and facilitates peer group comparisons. In this article, we will explain how the Federal Reserve uses this data in supervision, how banks benefit when bank regulators use PASS, and how regulators actually use the PASS data.

How does the Federal Reserve use this data in supervision?

Federal Reserve supervisory staff use payment data to aid in examination scoping, particularly in the areas of operations risk and compliance with the Bank Secrecy Act and Anti-Money Laundering (BSA/AML).

The primary function of PASS is in risk-focusing from a supervision perspective. PASS reports and peer comparisons help identify potentially problematic transactions and the institutions processing them. This enables supervisory staff to focus on problematic areas, reducing supervisory activities in areas that are not high risk. The PASS tool is flexible and allows supervisory staff to create peer groups that share a similar structure or geographic location, such as the same city, district, or asset size. Such customized peer group analysis helps identify problematic or high-risk transactions.

How do banks benefit when bank regulators use PASS?

The use of PASS data and analysis by bank regulators has benefited banks in two ways:

1. Risk-focused supervision has reduced supervisory burden on banks.
2. Identification of potentially fraudulent activity has helped supervisory staff alert the bank.

Federal Reserve supervisory staff conduct reviews between exams to identify potential risks early on. These reviews allow regulators to work with institutions to ensure appropriate controls are in place and the activity is being monitored on an ongoing basis. For example, PASS-generated reports assist with target reviews of DIs, which result in a more focused on-site review, thus saving time asking bankers questions that could be answered off-site. Additionally, since banks generally know what their own activity is, especially in peak times, banks could potentially identify fraudulent activity by monitoring their own data.

How do regulators actually use this data?

Supervisory staff analyze and monitor the data to identify spikes in activity levels for various payment types. For example, an increase in ACH transaction volume between exams may suggest a new customer relationship or a new product being offered. The supervisory focus would then be on appropriate risk management practices. A majority of the spikes in activity levels can be explained by comparing current data to past data. A spike in currency and coin orders in the summer months, for instance, may be an indication of a county fair.

Fed Notes, *Continued on next page*

New to BHCA

The Bank Holding Company Association welcomes these new Holding Company and Associate Members:

NEW ASSOCIATE MEMBERS:

Armstrong Teasdale LLP
Paul Cambridge, partner
St. Louis, Mo.
For over a century, Armstrong Teasdale has forged long-term relationships with financial services and banking clients – large and small. We have grown to be one of the 200 largest law firms in the U.S., with offices across the country. Our attorneys work together to guide clients through virtually every challenge.

The Micah Group
Mike Nowezki, sr. director of sales
Justin Bjerkaas, CEO/founder
Scott Anderson, sr. director of national accounts
Excelsior, Minn.
The Micah Group is a financial technology company founded by a banker who had a conviction that there should be a faster and more efficient way to a loan decision for a borrower. Their solution is focused on getting banks quicker access to data from various sources so they can make a faster credit decision, and they don't believe technology should make auto decisions. Banking is a relationship business and banks should decide the WHY — Micah helps with the how and what. Micah (banking solution) is designed specifically for more complex/commercial lending processes and digitizes numerous document types in seconds. They create actionable access to the right data quickly to make decisions specifically tailored for each bank — separating, parsing, spreading and mapping (not imaging) to a banks decisioning criteria and COA/GL. The results of their technology and engagements accelerate the speed of trust between banks and businesses to get to a faster yes or no decision.

Skip Rock Consulting
Jaime Nolan, CAE, CGT, owner/principal
Minneapolis
Organizational development consulting. Services include strategic planning facilitation, board training, team development, and ongoing consulting. Also a certified Everything DiSC provider and accredited provider of "5 Behaviors of a Cohesive Team."

NEW HOLDING COMPANY MEMBERS:

Chippewa Valley Agency, LTD.
Rick Gerber
Hayward, Wis.
Chippewa Valley Bank

Choice Financial Holdings, Inc.
Brian L. Johnson
Fargo, ND
Choice Bank

Green City Bancshares, Inc.
Brad Doran
Green City, Mo.
Farmers Bank of Green City

Park Financial Group, Inc.
David Saber
Duluth, Minn.
Park State Bank

Reliance Bancorporation, Inc.
Todd Markman
Faribault, Minn.
Reliance Bank

University Financial Corp,
GBC DBA Sunrise Banks
David Reiling
St. Paul, Minn.
Sunrise Banks, N.A.

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However, some spikes in activity levels cannot be explained without additional information from bankers. As an example, one examiner compared transaction data on a month-to-month basis, identified spikes on certain days of the month, and confirmed that payroll was being processed on certain days. These actions allowed supervisory staff to relay the findings to operations exam staff for an upcoming exam, thus saving the exam staff and bankers time by answering questions beforehand.

In conclusion, the PASS tool and the associated banking data contained within the tool provide benefits to both bankers and supervisory staff. Staff members are better informed and prepared for upcoming examinations using PASS data, and bankers benefit from risk-focusing by supervisors and reduced regulatory burden. ■

Ryan Bahr is a project director at the Federal Reserve Bank of Minneapolis.

Holding Company Transaction Report

Here are selected recent bank holding company filings with the Federal Reserve Banks of Chicago, Minneapolis, Kansas City and St. Louis.

▷ Midland States Bank, Effingham, Ill., authorized to merge with HomeStar Bank and Financial Services, Manteno, Ill., and retain the acquired facilities as branches.

▷ Notice filed by William H. Davis, Fairview Park, Ohio, and others to acquire shares of Anchor Bancorporation, Inc., and control Anchor State Bank, both of Anchor, Ill.

▷ Change in control notice filed by Charles W. Bolen of Montezuma, Iowa, and others to retain and acquire shares in Arendts Inc., and control Peoples Savings Bank, both of Montezuma, Iowa.

▷ ChoiceOne Financial Services, Inc., Sparta, Mich., filed to merge with County Bank Corp and acquire Lakestone Bank & Trust, both of Lapeer, Mich.

▷ Margaret Kirschner GST Separate Trust for Pamela Kirschner Bolduc and others filed to retain and acquire 25 percent of Town and Country Financial Corporation and retain control of Town and Country Bank, both of Springfield, Ill.

▷ Waterman Acquisition Group, LLC, Wilmette, Ill., filed to become a bank holding company by acquiring Waterman State Bank, Waterman, Ill.

▷ Financial Services of Lowry, Inc., Lowry, Minn., filed to acquire The First National Bank of Osakis, Minn.

▷ Change in control notice filed by The Dawn M. Van Vugt Revocable Living Trust and others to acquire shares of First Rushmore Bancorp, Inc., Worthington, Minn, and join the Kooiman Family shareholder group, which controls 25 percent or more of First Rushmore. First Rushmore controls First State Bank Southwest, Pipestone, Minn.

▷ Merchants Financial Group, Inc., Winona, Minn., filed to acquire The First National Bank of Northfield, Minn.

▷ Meta Financial Group, Inc., Sioux Falls, S.D., filed to become a bank holding company as a result of the proposed conversion of its federal savings bank subsidiary, MetaBank, Sioux Falls, into a national bank to be named MetaBank, National Association.

▷ MNB Financial Services, Inc., McCook, Neb., filed to become a bank holding company through the acquisition of Graff Family, Inc., and MNB Financial Group, Inc., and acquire MNB Bank, all of McCook. In addition, MNB Financial Services, Inc., elected to become a financial holding company.

▷ Stark Bancshares, Inc., Canton, Ohio authorized to become a bank holding company by acquiring Farmers Financial Corporation, Bolivar, Mo., and acquiring Farmers State Bank.

▷ Katz Acquisition Corp., LLC, Tampa, Fla., is seeking prior approval to become a Bank Holding Company through the acquisition of Camp Grove Bancorp, Inc., Camp Grove, Ill.

▷ Walsh Financial, Inc., Minneapolis, filed to become a bank holding company by acquiring The First National Bank of Buhl, Mountain Iron, Minn.

▷ Jones Bank, Seward, Neb., filed to merge with Oak Creek Valley Bank, Valparaiso, Neb., and establish a branch.

▷ First Holding Company of Cavalier, Inc., Cavalier, N.D. authorized to acquire Northern Sky Bank, Crookston, Minn.

▷ Summit Bancshares, Inc., Chesterfield, Mo., authorized to become a bank holding company by acquiring The Bank of Houston, Mo.

▷ Discover Financial Services, Riverwoods, Ill., filed to acquire through the formation of a wholly-owned interim bank, DFS Bank, New Castle, Delaware.

▷ Change in control notice filed by James L. Moss, and others to acquire 10 percent of more of FNB BanShares, Inc., and thereby control Bank 1st, both of West Union, Iowa.

▷ Heather M. Plumski, Avon, Minn., as a trustee of the Stearns Financial Services, Inc., Employee Stock Ownership Plan and Trust, Saint Cloud, Minn., (ESOP), filed to acquire control of the ESOP, and thereby indirectly gain control of Stearns Financial Services, Inc., Saint Cloud, Minn., (Stearns). Stearns controls Stearns Bank National Association, Saint Cloud, Stearns Bank of Upsala National Association, Upsala, Minn., and Stearns Bank of Holdingford National Association, Holdingford, Minn.

▷ Citizens Community Bancorp, Inc., Eau Claire, Wis., authorized to acquire F&M Bancorp of Tomah, Inc., Tomah, Wis., and to acquire Farmers & Merchants Bank.

▷ Bethany Bankshares, Inc., Bethany, Mo., authorized to acquire by merger Fairport Bancshares, Inc., Maysville, Mo., and to acquire The Bank of Fairport, Mo.

▷ Old O'Brien Banc Shares, Inc., Sutherland, Iowa authorized to merge with R & J Financial Corporation, Inc., Elma, Iowa, and acquire Peoples Savings Bank. It also has elected to become a financial holding company.

▷ Pella Financial Group, Inc., Pella, Iowa, authorized to acquire Iowa State Savings Bank, Knoxville.

▷ Wintrust Financial Corporation, Rosemont, Ill., authorized to acquire Rush Oak Corporation, Chicago, and to acquire Oak Bank; and for Wintrust Bank, Chicago, to merge with Oak Bank and thereby establish a branch.

▷ Ameriprise Financial, Inc., Minneapolis, authorized to become a savings and loan holding company upon the conversion of its subsidiary, Ameriprise National Trust Bank, Minneapolis, into a federal savings bank to be named Ameriprise Bank, FSB. Also, it has elected to become a financial holding company.

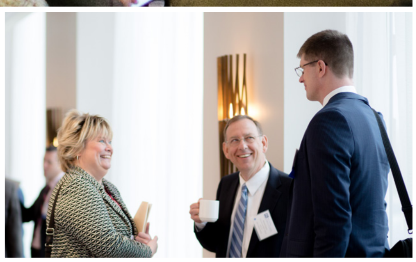
▷ Citizens Bank Group, Inc., St. James, Minn., authorized to acquire The Nicollet County Bank of Saint Peter, St. Peter, Minn.

▷ Sword Financial Corporation, Horicon, Wis., filed to merge with Markesan Bancshares, Inc., Markesan, Wis., and to acquire Markesan State Bank.

▷ Bethany Bankshares, Inc., Bethany, Mo., filed to acquire Fairport Bancshares, Inc., and to acquire The Bank of Fairport, both of Maysville, Mo.

▷ Forward Financial, Inc., Marshfield, Wis., and Forward Financial, MHC, authorized to become bank holding companies by acquiring The First National Bank of Park Falls, Wis.

▷ Richmond Mutual Bancorporation, Inc., a newly formed Maryland company headquartered in Richmond, Ind., filed to become a bank holding company by acquiring First Bank Richmond, Ind., in connection with the merger of First Mutual of Richmond, Inc., into Richmond Mutual Bancorporation, Inc., a Delaware corporation, both headquartered in Richmond, Ind.



BANK OWNER

Bank Holding Company Association
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