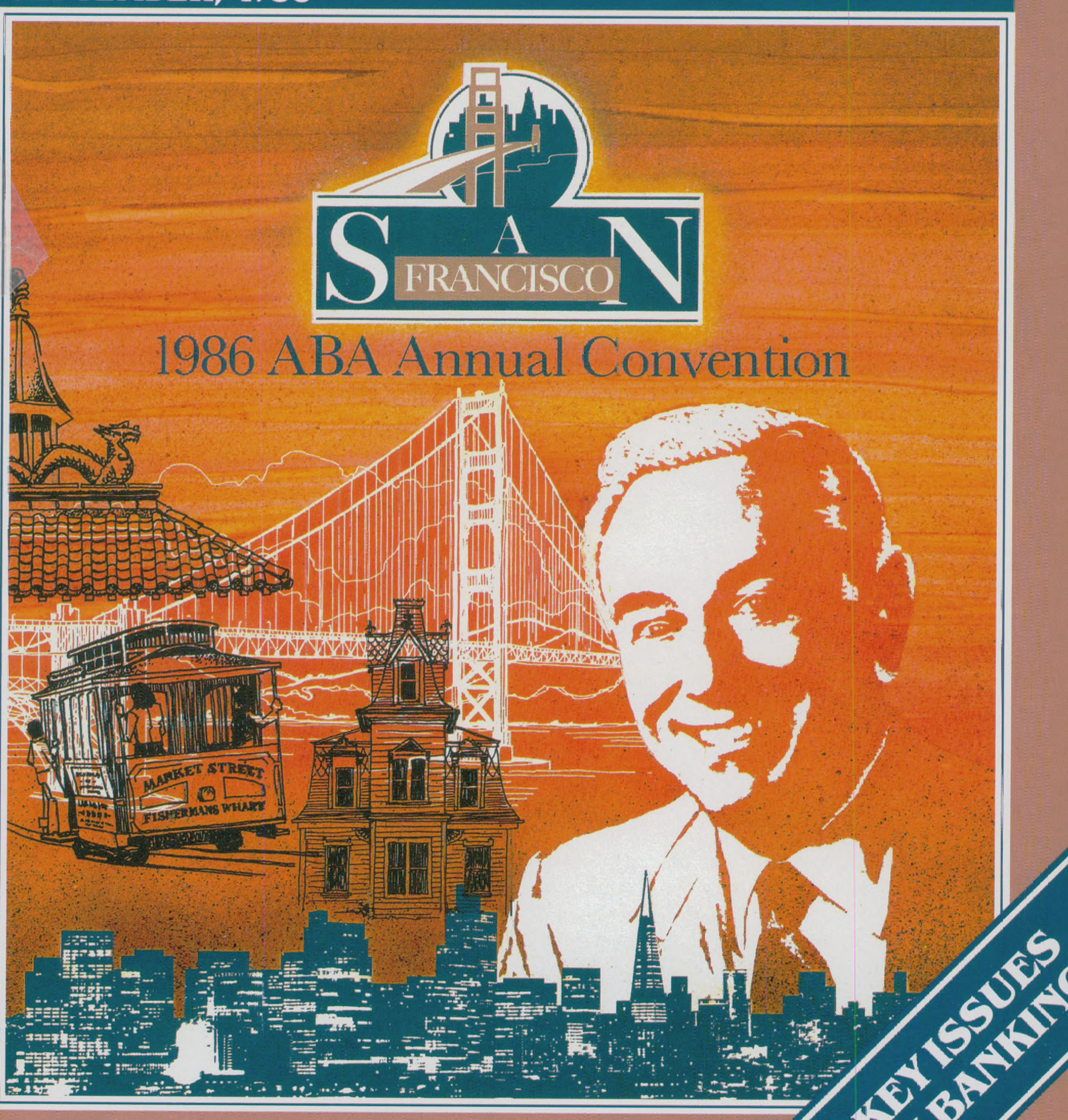
MID-CONTINENT BANKER

FEATURES

Interstate-Banking Roles
Meeting Nonbank Competition
Combatting Management Shortage
Tax-Bill's Significance

SEPTEMBER, 1986



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MID-AMERICA'S BANKING PUBLICATION

BANKING WIRE

MID-CONTINENT BANKER

September, 1986

Late-Breaking News From the World of Banking

INTEREST-RATE SLASHING BY AUTO MANUFACTURERS is being challenged by the ABA and the Consumer Bankers Association (CBA). The ABA has mounted a "buyer beware" program and the CBA has queried state attorney generals asking if financing practices that cut out financial institutions are legal in their states. "Consumers are more confused than ever" by auto manufacturers' efforts to reduce 1986 model-car inventories, says Patrick W. Harrison, chairman of the ABA's consumer credit division. "It's difficult for consumers to determine which choice is really the better deal" when manufacturers give customers a choice of low- or no-interest-rate loans or cash rebates. He recommends that buyers check with their bankers before making decisions. The CBA reports that some attorney generals have agreed to investigate the legality of automakers' sales schemes. Both the ABA and the CBA want bankers to be able to participate in sales plans offered by automakers. The ABA is distributing a consumer-information brochure entitled "Ten Tips to Financing Your Car or Truck" which gives advice on avoiding the additional costs often associated with reduced-rate financing.

TEXAS IS TRAVELING THE INTERSTATE ROUTE in an effort to prop up the fortunes of its many near-failing banks. Support among Texas bankers is broad and "there's no question that Gov. Mark White will sign the bill before October 1," says Sam Kimberlin Jr., executive vice president, Texas Bankers Association. The bill permits out-of-state financial institutions to acquire Texas banks, bank HCs or S&Ls and doesn't require the acquiring institution's home state to have enacted a reciprocal interstate banking law. Effective date for acquisitions is January 1. One unusual provision states that the board of any financial institution bought by an out-of-state institution must have a majority of Texas residents.

THIRD NATIONAL, Nashville, is joining the SunTrust Banks empire by means of a stock swap with an indicated value of more than $733 million. The acquisition, the first in Tennessee by a "super-regional," will place SunTrust in the No. 2 spot in size for southeastern financial institutions. The agreement calls for SunTrust to swap 1.67 of its common shares for each of Third National's 18.9 million shares outstanding. Third National is No. 1 in Nashville and Chattanooga and No. 3 in Knoxville in terms of market share. The acquisition is expected to raise SunTrust's total assets to $23.8 billion.

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INDUSTRY-WIDE GUIDELINES by which banks can gauge their Community Reinvestment Act records have been established by the Fed in its order approving a long-delayed merger by New Orleans-based Hibernia Corp., with Southwest Bancshares, Inc., Lafayette, La., according to Hibernia's general counsel. Settlement of the case means that banks "no longer have to rely simply on guesswork" when measuring their performance against their CRA obligations, says Robert G. Coury. The Fed rejected a complaint by a community-action group about the lending practices and service-delivery policies of Hibernia National, New Orleans, and stated that neither the Bank Holding Company Act nor the Community Reinvestment Act is intended to dictate a financial institution's product mix, require the allocation of credit to any person or group or establish credit underwriting standards that are not consistent with safe and sound banking operations in order to extend credit to a preferred group. Hibernia is believed to be the first financial institution to fight a CRA-based challenge.

"SAFEST BANK IN THE NATION" is the designation bestowed on Missouri's Commerce Bancshares, Inc., headquartered in Kansas City and St. Louis, by Olson Research Associates. Basis of the designation are 10K filings with the SEC and annual reports of the institution. Performance of the nation's top 300 banks was analyzed to determine a "risk component" of 60 points based on asset quality, liquidity, interest-rate sensitivity and capital and reserves. Commerce scored a near perfect 59. "Results of the survey reinforce my opinion that the highest performing banks are not the money-center banks, they are the regional banks," says David W. Kemper, president/CEO of Commerce.

LOWER CHARGE-CARD RATES have been announced by First American Corp., Nashville, and First Tennessee, Memphis. First American's new rates are 15% on balances above $2,500 and 17% on balances of $2,500 and below, down from 20% for balances to $1,500; 18% for balances between $1,501 and $2,500; and 16% for balances above $2,500. First Tennessee has reduced the rate on its Premier Visa card to two points over the New York prime. the rate varies monthly and is based on the New York prime as of the first of each month. Customers maintaining $10,000 in deposit accounts or who charge more than that amount on their Premier Visa cards during a calendar year have the $35 annual fee waived. Declines in the cost of money are credited with the changes.

A KANSAS BANK recently disbursed escrow funds of $1.254 BILLION, via 265 wire transfers, in slightly more than an hour's time. The amount almost equalled total assets of Bank IV, Wichita, which was authorized by the U. S. District Court to invest oil overcharge funds and manage them in escrow until litigation concerning them was settled. Principal for the disbursement was money collected from oil overcharges between 1973 and 1981, a period when prices for existing and newly discovered oil were set at different levels by the government. Recipients of the funds included all 50 states, six U. S. territories, the Department of Energy, refiners, resellers, retailers, ag cooperatives, airlines, surface transporters, rail and water transporters and utilities.

MID-CONTINENT BANKER

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MID-CONTINENT BANKER

September, 1986/Volume 82, No. 9

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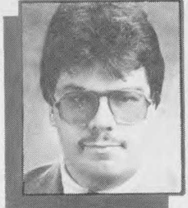

Banking's 10 Key Issues

IN MID-CONTINENT BANKER'S annual American Bankers Association's (ABA's) convention preview issue each fall, we traditionally review some of the key issues bankers probably would be discussing when they reached the convention.

This is a good time of year for reflection. The economic pattern for the current year already has been established and plans are being made for the new calendar year based on individual assessments of how the economy is shaping up. Of course, there's always the danger in any list of 10 "key" issues that some people will disagree with the choice of the issues on the list. The issues we've elected to focus attention on this year are based on a poll of our editors and represent a good cross section of the items likely to be on bankers' agendas when they reach San Francisco in late October.

You have to wonder why lists like this always seem to fit so neatly into 10 components. Why not six key issues or 15? Ten just seems to be a good number of items to have on any list. If you have more than 10, people grow bored and won't remember any item on the list past 10 anyway. If you stop at seven, eight or nine, you're likely to create the impression you were either too lazy or stupid to think of other items to round out the list. Even God felt compelled to push on and add a few more sins than necessary to His list of commandments just to make sure He wasn't accused of sloth, one of the seven "deadly" sins.

Seven can be a good number of items for a list. It's regarded as a lucky number and people feel comfortable with it. Unfortunately, it is almost impossible to create a list with seven items on it. Try it and you'll find you always end up with six or eight, and then you ultimately decide you might as well try for 10.

In any case, the 10 key issues we've asked our panel of banking-industry experts to tackle this year are broad enough to encompass just about any significant concern bankers are likely to have, not only in the year ahead but for the remainder of the decade. So far, 1986 has all of the makings of something of a watershed year for the banking industry. It will not be the year in which Congress gets around to passing an omnibus banking bill, but that's not because of a lack of effort.

Some of the patterns of what banking is evolving into have become more clearly discernible in recent months, however. We can now see, for example, at least the outline of what regional interstate banking will look like in the Midwest and in much of the South. That's something you probably couldn't have said last year at this time unless you are blessed with uncommon foresight.

We've seen banking attempt to come to grips with its image problem and the need to educate bankers more thoroughly in the skills they will need if they are to compete more effectively in the decade ahead. In late July, the ABA announced a long-term program to enhance the soundness and service of the commercial banking industry. Based on the recommendations of the ABA Commission on Safety and Soundness, the ABA identified eight key areas of self-improvement commercial banks should concentrate on: risk-related capital management; written codes of ethics; disclosure of information about the financial condition of the bank; employment of outside auditors; utilization of boards of directors; asset quality; operating risks; and disclosure of product information to consumers.

We won't delve into why the commission stopped short of recommending 10 areas for self-improvement. It's enough to know that banking is aware of its image problem and is taking steps through its "The Extra Mile: A Commitment to Soundness and Service in Banking" program to deal with the problem head on.

As ABA President Donald Senterfitt (pictured on our cover this month) said in announcing the "extra-mile" program, even though return on assets at banks has declined from .82% in 1980 to .70% at the end of 1985, the banking industry, as a whole, remains sound and prudently managed. However, public perceptions of banks can be just as important to banking's success as reality, according to Mr. Senterfitt. This is why the ABA is asking commercial banks to "go the extra mile and achieve excellence in all aspects of their operations."

Almost simultaneously, the ABA announced that it is beginning a new Professional Development Program that will standardize the educational requirements for bankers and ensure that they have the necessary knowledge, skills and commitment to excellence consumers increasingly will demand. We've maintained in this column for some time that there's no shortage of management talent in banking, only a shortage of the skills bankers need to compete in a deregulated environment.

The passage of the tax-reform package is another milestone event that will have long-range implications for all businesses, especially banks. The problem-loan situation may lessen the immediate impact on larger banks of the loss of the deductibility of the additions to loan-loss reserves, but the consensus seems to be that most banks will ultimately find their tax burden a little heavier thanks to the Congress' 1986 tax-reform efforts.

We could go on about the progress we've seen in recent months in bankers' efforts to more completely integrate their operation functions, the competition bankers are facing from outside forces which — if anything — has grown fiercer and more broadly based, and the debt problem at the international, federal, business and consumer levels. But it's time to preview the ABA convention, then turn the discussion over to the panel of industry experts we've assembled for this issue. After you've read what they have to say about the 10 key issues in banking, we think you'll rate this issue of MID-CONTINENT BANKER a "10."

— John L. Cleveland
Editor/Associate Publisher

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San Francisco to Host ABA

Future of Banking to Be Explored At ABA Convention Next Month

FOUR prominent banking-industry leaders will discuss the future of banking at the ABA's 1986 annual convention, set for October 25-29 at the Moscone Center in San Francisco.

Participants on the panel will be Randall A. Killebrew, president, First National, Petersburg, Ill.; Robert V. Lindsay, president, Morgan Guaranty Trust, New York City; John B. McCoy, president/CEO, Banc One Corp., Columbus, O.; and Joseph J. Pinola, chairman/CEO, First Interstate Bancorp., Los Angeles. Moderator will be Donald G. Ogilvie, ABA executive vice president.

Issues expected to be addressed by the panel include new powers for banks, regional and interstate acquisitions, bank failures and what a bank has to do to be among the survivors in this era of deregulation and nonbank competition.

Mr. Killebrew has long been active in the ABA. He is a past chairman of the community bankers council and continues as an ex-officio member. He currently serves on the ABA's advisory committee to the Treasury and is vice chairman of the government relations council.

Mr. McCoy is a delegate to the ABA's banking leadership conference and presides over one of the most aggressive HCs in Ohio; one that has already acquired banks in adjacent states and has made the maximum number of commitments in Indiana permitted by state statute governing deposit share.

Mr. Pinola is the champion of franchise banking and his HC recently was the successful bidder for failed First National, Oklahoma City, which has as its president ABA Chairman James G. Cairns.

Mr. Ogilvie, now in his second year as ABA executive vice president, proved his mettle recently by facing angry demonstrators of Acorn, a highly vocal and visible consumer-activist group that has been harassing the banking industry regarding its adherence to the provisions of the Community Reinvestment Act. He also has been actively espousing the ABA's views through visits to state association conventions.

Some of the nation's most sought-after speakers will complement the convention program, including

International-affairs consultant Henry A. Kissinger is scheduled to address convention delegates.

PROGRAM AT A GLANCE

Saturday	Sunday	Monday	Tuesday	Wednesday
• CONVENTION OPENS • Registration • Exhibits • Committee Meetings • Banking Industry Sessions • Personal Development Sessions	• Registration • Exhibits • Committee Meetings • Fellowship Gathering • Banking Industry Sessions • Personal Development Sessions • ABA Reception/ Entertainment	• Registration • Exhibits • General Session • Banking Industry Sessions • Personal Development Sessions	• Registration • Exhibits • General Session • Banking Industry Sessions • Personal Development Sessions • ABA Reception/ Entertainment	• General Session • Convention Adjourns — 11:00 a.m.

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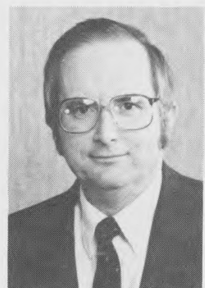
Future-of-Banking Panelists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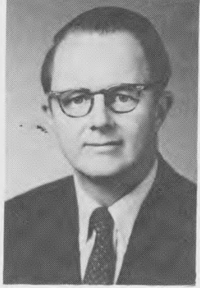
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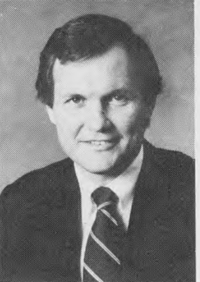
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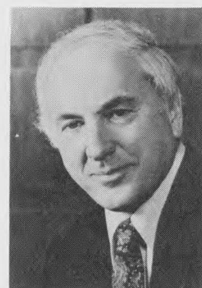

PINOLA

nationally-syndicated columnist George F. Will, well-known for his advisory role with President Ronald Reagan; international-affairs consultant Henry A. Kissinger, secretary of state during the Nixon-Ford administrations; and Coca Cola Co. Chairman Roberto Goizueta, mastermind of soft-drink acquisitions.

No ABA convention would be complete without representatives of the bank-regulatory fraternity. Fed Chairman Paul Volcker is *not* scheduled to appear this year, but new Comptroller of the Currency Robert L. Clarke and new FDIC Chairman L. William Seidman are expected to address the general sessions.

A panel on world affairs will feature former Central Intelligence Agency Director Stansfield Turner and former National Security Affairs Assistant Brent Scowcroft. Hugh Sidey, contributing editor, *Time* magazine, will moderate the panel.

Presiding at this year's convention will be Donald T. Senterfitt, ABA president and vice chairman, SunTrust Banks, Inc., Orlando, Fla. His president's address will be given at the first general business session on Monday, October 27. ABA President-Elect Mark W. Olson, president, Security State, Fergus Falls, Minn., is scheduled to address the general session on Tuesday, October 28.

A multitude of workshops will focus on a variety of banking issues, including tax reform, expanded powers, directors and officers liability insurance, agricultural lending, mergers and acquisitions, asset/liability management and bank culture.

More than 200 firms are expected to display products and services in the exhibit area, which also will be the site of the activity center. The latter will feature a fun fitness center for golf, tennis and running tips, a house and garden center for landscaping tips, flower-arranging and interior design and a gourmet center with cooking demonstrations and tasting of California food and drink.

The Rev. Robert Schuller of the well-known "glass" church in Southern California will be featured speaker at the annual Fellowship Gathering on Sunday morning, October 26.

Two receptions will be held. The "California Carousel" on Sunday evening will feature musical entertainment and food from around the golden state. "Romancing San Francisco" is the theme for the Tuesday-evening reception. ● ●

Last Time the ABA Met in San Francisco . . .

THE ABA convention was last held in San Francisco in 1981 and featured speakers included Rev. Robert Schuller, then-Treasury Secretary Donald Regan, Fed Ch. Paul Volcker, and former CIA Dir. William E. Colby.

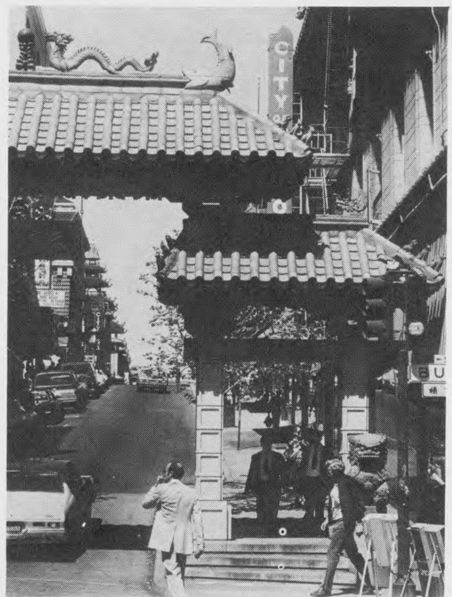
Rev. Schuller is appearing at this year's convention in the same capacity as in 1981 — speaker at the Fellowship Gathering.

The community bankers division of the association made its debut at the 1981 convention and a rousing speech titled "I'm Glad to Be a Community Banker" was given by the division's first chairman, Charles A. Bruning, president, Edgewood Bank, Countryside, Ill.

Another speaker was James D. Robinson III, chairman/CEO, American Express, whose talk on how his firm planned to compete with commercial banks was on the minds of many bankers throughout the convention. Mr. Robinson told bankers that a strong tide of new forces would propel the financial-services industry into a new era of deregulation and competiton.

"Successful financial institutions will be those that focus more on how to increase their competitive capabilities and their comparative marketing advantages, rather than waste time longing for the good old days," he said.

Presiding at the convention was Lee Gunderson, who then was president, Bank of Osceola, Wis., and who now is a partner with Arthur Young, New York City.



San Francisco's Chinatown

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Heading the ABA for the 1985-'86 term (from l.): Donald G. Ogilvie, e.v.p.; James G. Cairns Jr., ch.; Donald T. Senterfitt, pres.; Mark W. Olson, pres.-elect; and Thomas P. Rideout, treas.

Senterfitt, Olson, Rideout Top ABA Officers

PRESIDING at this year's ABA convention will be Donald T. Senterfitt, ABA president and vice chairman, Suntrust Banks, Inc., Orlando, Fla. President-elect of the association is Mark W. Olson, president, Security State, Fergus Falls, Minn., and treasurer is Thomas P. Rideout, president/CEO, Savannah (Ga.) Bank & Trust. James G. Cairns, president/CEO, First Interstate, Oklahoma City, is ABA chairman and Donald G. Ogilive is ABA executive vice president.

Mr. Senterfitt has held his post at SunTrust since 1980. He joined the organization in 1964 after service as an attorney. He is a former aide to Senator Charles O. Andrews of Florida and served as chief counsel for the Florida Bankers Association.

Mr. Olson began his banking career as a management trainee at First National, St. Paul, in 1966. He was promoted to consumer-banking officer three years later. He took time out from banking to work in the political arena prior to joining his present bank in 1976 as president. He is a former chairman of the ABA's government-relations council.

Mr. Rideout joined Wachovia Bank, Winston-Salem, N. C., in 1963. He was elected senior vice president in 1973 and manager of the financial-institutions department two years later. He joined his present bank in 1980 as president/chief operating officer and was named CEO in 1984. He is a former chairman of the ABA's banking-professions council and has chaired the association's correspondent-banking division.

Mr. Cairns joined First National, Oklahoma City, in January as CEO, coming from Peoples National of Washington, Seattle, which he joined in 1962. When First of Oklahoma City was closed by the Comptroller of the Currency in July, Mr. Cairns became CEO of the surviving institution, which was purchased by First Interstate Bancorp., Los Angeles, and named First Interstate of Oklahoma.

Mr. Ogilvie joined the ABA as executive vice president early last year as successor to Willis Alexander. He formerly was with Celanese Corp., where he served as vice president responsible for government relations, communications and health, safety and environmental affairs. He has held positions in the federal government.

Mid-Continent-area bankers serving on the ABA's board include the following: Joe S. Hiatt, chairman/CEO, American State, Charleston, Ark.; Charles A. Bruning, president/CEO, Edgewood Bank, Countryside, Ill.; Jon S. Armstrong, chairman, Midwest Commerce Banking Co., Elkhart, Ind.; Jordan L. Haines, chairman, Bank IV, Wichita; Charles W. McCoy, chairman, Louisiana National, Baton Rouge; and Charles Pistor, chairman/CEO, RepublicBank Dallas. ● ●

□ Sell
□ Swap
□ All of the above

The gnomes know that lenders have different needs at different times. So Freddie Mac offers two choice ways to participate in the secondary market.

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Sell or Swap? Your Freddie Mac representative can tell you why the answer is *all of the above*. And that's a piece of gnome knowledge that is just too good to file away.

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ABA President Reports

Banking-Service Emphasis Stressed Throughout Term

By Donald T. Senterfitt
ABA President and
Vice Chairman, SunTrust Corp.
Orlando, Fla.

WHEN I assumed the ABA presidency at the 1985 annual convention in New Orleans, I issued a challenge. I said it would be up to every banker to reaffirm to the people of the United States that service to their customers and their communities remains the absolute top priority of the banking industry.

I said then, as I believe now, that America's banks are far from being impersonal masonry monoliths, as some delight in portraying them. They are simply businesses — in most cases small businesses — run by hundreds of thousands of dedicated men and women who work every day to assure the safe handling of other people's money. And they do it with a solid continuity, a deep and abiding professionalism, that makes everything else about banking seem transparent and easily taken for granted.

But in today's environment, providing top-flight service means more than performing traditional tasks with exceptional competence. Today, bank customers want more service from us — the kind of full service that can only come from freeing banks to compete — permitting them to diversify to meet the developing demands of the marketplace.

A top priority of mine this year has been to secure products-and-services legislation for banking. Certainly that's not a new goal. The banking industry has been pursuing it in one form or fashion ever since money-market mutual funds made their presence felt over a decade ago. It remains a vital goal for the industry, and progress has been made.

Senate Banking Committee Chairman Jake Garn introduced a comprehensive banking bill this summer that promised many of the significant changes the industry has been seeking, including limited new powers and closing the nonbank loophole. Unfortunately, because of Congress' unwillingness to come to grips with the need for comprehensive banking legislation, Senator Garn decided to postpone his efforts until next year.

On the House side, the ABA worked with Georgia Congressman Doug Barnard Jr., to draft alternate legislation that would promise greater product and services opportunities for banks. The bill, the 1986 Financial Services Competitive Enhancement Act, goes beyond the Garn legislation. The Barnard bill would authorize bank holding companies to offer real estate brokerage, investment and development services and insurance brokerage, agency and underwriting services; permit bank holding company affiliates to underwrite any asset-backed security; and authorize national banks to offer full-service brokerage services.

The ABA is trying to persuade Congress that

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competitive freedom is not purely a banking issue. It's a consumer-and-general-business issue as well, because bank involvement can help to lower real estate commission rates, make insurance premiums more affordable and make it cheaper for consumers to buy and sell stocks. That can all be achieved simply by letting the free market forces of competition go to work.

The ABA conservatively estimates that total savings in these three areas could amount to as much as $5 billion a year. That represents the savings for bank customers — not banks.

However, the ABA's effort to obtain new products and services is not all directed at the Congress. We're taking advantage of every forum we have — legislative, regulatory, executive branch, the courts — to strengthen our chances. If we can persuade the Fed, the Comptroller, the FDIC, an appellate court, or any other agency or institution to authorize new services for banks, then we'll go after that prospect.

Another priority during my year as ABA president was to develop a voluntary program to strengthen the soundness and service of the banking industry. To achieve this goal, the ABA Commission on Safety and Soundness, consisting of 14 prominent bankers and ABA Executive Vice President Donald G. Ogilvie, was asked to determine how the industry could effectively exercise leadership in addressing the important issue of public confidence. Its focus was on what banks can do for themselves, as opposed to what Congress or the regulators can do. The result was a thorough and penetrating report approved in April by the ABA board of directors.

The Commission concluded that the best way banks could demonstrate their commitment to soundness and service was through excellence in management practices.

In addition to maintaining consumer confidence and trust, a secondary benefit of the campaign is to help the banking industry attain a high level of self-regulation to complement existing and essential government supervision.

The recommendations of the Commission covered eight areas:

1. **Risk-Related Capital Management:** The Commission concluded that bankers should assess the risk of their balance sheet and off-balance sheet components and then determine the level of capital required to absorb the potential losses that those risks could represent. Because the process requires intense self-evaluation, it will cause bank managers to address more thoroughly all aspects of risk in managing their banks.

2. **Code of Ethics:** The Commission also recommended that all banks adopt or revise a formal code of ethics. A bank's reputation, one of the most valuable assets, often is determined by the conduct of its officers, other employees and directors. While many banks already have formal or informal codes and all bank employees have an understanding of the conduct expected of them, a formal, written bank code of ethics can provide specific direction for action in a variety of situations as well as offer general guidelines for both business and personal behavior that could impact the integrity or image of a bank.

3. **Financial Disclosure:** Currently, all banks with federal deposit insurance are required to file periodic financial reports disclosing substantial amounts of information. Bank holding companies with 500 or more shareholders also must comply with Securities and Exchange Commission requirements. Although these reports are available to the public, the material often is overwhelming in its length and complexity.

For customers, such as uninsured depositors, who have both a desire and need to understand the financial condition of their banks, institutions should assemble packages of clear, concise information that are readily available.

4. **Outside Audits:** The Commission felt that outside audits would promote public confidence in the soundness of a bank. Outside auditors also benefit banks by providing an objective, third-party evaluation of management practices and by bringing to the bank the benefit of knowledge gained from the practices of other institutions. Directors also receive an independent assessment of the bank's management. Because the value of the certified audit will more than offset the costs, the Commission felt all banks should voluntarily adopt certified audits in the next few years.

5. **Directors:** Like outside auditors, bank directors, most of whom come from outside the bank, can provide objective guidance to management. Bank directors' responsibilities traditionally have included supervision of the business of the bank, monitoring of management performance, policy-making, ensuring compliance with the law and protection of owners' assets.

The rapidly changing financial-services market and the resultant challenges to bank management have made the supervisory role of directors increasingly important. Therefore, the Commission recommended that banks should place heightened emphasis on keeping their boards of directors informed, independent and active.

6. **Bank-Asset Quality:** The Commission concluded that there is no substitute for the traditional management practices of prudent lending and careful asset quality review. Vigilance also is required for all other asset activities, such as investments or off-balance-sheet financing. Therefore, management must give rigorous attention to asset quality, the Commission stated.

7. **Operating Risks:** These concerned the Commission because unexpected operating disruptions or internal fraud can impair the soundness of a bank. For example, operating procedure that worked well in a paper-based, slower-paced environment may be inadequate today and lead to a systems failure. Bankers must learn not only how to recognize operating-risk activities and implement standards, policies and programs to control them, but also how to detect emerging risk.

8. **Consumer Disclosure:** As deregulation of the financial-services industry proceeds, the number of companies and products continues to grow. This has vastly expanded the choices available to consumers. As an advocate of continued deregulation, the banking industry should voluntarily help consumers by clearly, concisely and consistently providing significant product information, such as interest rates and fees.

The ABA already has developed several new products that will facilitate banks' adopting the Commission's recommendations. On the subject of operating risk, the ABA has completed guidelines for bank practices when settling Fed funds transactions. Also completed is a guide to developing or revising a bank code of ethics.

The ABA has begun a long-term program that will continue during the next few years along with the ever-changing banking industry. The result will be continued soundness and service — overall — for the dynamic, growing banking industry. • •

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ABA Exhibitors Introduce New Products

FIRMS PLANNING to exhibit at the ABA convention in San Francisco were surveyed recently about their plans for the convention. Many of the exhibitors will be introducing new products and services at the convention. Others plan receptions and prize drawings. Firms that responded to the survey are listed alphabetically below, along with booth numbers.

AMERICAN CREDIT INDEMNITY, Baltimore

Product: ACI will be highlighting their export credit insurance for Western Europe. The company provides protection against excessive credit losses for U.S. and Canadian companies shipping to debtors in 18 Western European countries.

Personnel: R. A. Nelson, senior vice president/marketing; and R. W. Jolivet, vice president, bank/broker relations.

Booth: 813

* * *

ATIS, LTD., Norcross, Ga.

Product: ATIS will be demonstrating its TTC Digital Time and Temperature Announcement System, the MS500 Communications Recorder, for recording two to 12 channels and the CG100 Professional Voice Recorder.

Personnel: Cathy Knotts and Tony Vespoli.

Booth: 1609

* * *

BAGMASTERS, Buena Park, Cal.

Product: Bank bags with plastic security seals, plastic bank deposit bags, night deposit bags with locks, coin bags and customer deposit bags.

Personnel: Richard Whittier and Jon Hanson.

Booth: 844

* * *

BANK BUILDING CORP., Atlanta, Dallas, Denver, Hartford, St. Louis, San Francisco

Product: Bank Building Corp. will be featuring its No Risk Program, which guarantees peace of mind before the final commitment is made. Using the firm's proprietary DART-I System, the firm creates an initial design that will suit present and projected requirements in service delivery, functionality, image and budget.

Personnel: Tom Spalding, Tom Williamson, Pat Fussner, Rex Dunlap, Carl Weis, Russ Eichman, Dave Sullivan, Don Kunkel, Rich Breitenfeld, Bruce McMickle, Gary Strong, Dave McAfee and Walt Yesberg.

Booth: 1018

* * *

BROADWAY & SEYMOUR, INC., Charlotte, N.C.

Product: This computer systems and services company designs software for financial institutions, including Maxim and Liberty. Maxim is a branch automation system designed and implemented for the IBM 4700 family of hardware; Liberty is an IBM System/36-based banking software package installed in more than 200 financial institutions.

Booth: Island 1216

* * *

DANIELSON ASSOCIATES INC., Columbia, Md.

Product: Consultants to banks, Danielson & Associates specializes in strategic planning, merger assistance and delivery systems analyses.

Personnel: Arnold G. Danielson, president; and Lynn A. Hatheway, research associate.

Booth: 312

* * *

DELOITTE, HASKINS & SELLS, Atlanta, Ga.

Product: The firm will be featuring Bank ControlPlan, a micro software program that evaluates internal control systems and determines where adjustments may be needed.

Booths: 202 & 204

Special Event: Nightcap Party, October 25, 9 p.m.-1 a.m., Sheraton Palace, Garden Court.

* * *

ELECTRONIC DATA SYSTEMS (EDS), Richardson, Tx.

Product: EDS offers the financial services industry a wide variety of processing alternatives, from turnkey systems and remote processing options to project management, teleprocessing and total resource management arrangements. EDS specializes in meeting each bank's specific processing needs.

Personnel: Ed Ladd, Jim Lorence, Dave Perry, John Hoffmeister, Ed Murray, Larry Thon, Coley Clark, Jim Kildebeck, Mike Littell, Bob Besch, Joe Hamrick, Vince Vachio, Jeff Brown and Tom Fox.

Booth: 1024

Special Event: Drawing in ABA Resource Center for one year free lease on 1987 Cadillac Sedan DeVille courtesy EDS.

* * *

FEDERATED INVESTORS INC., Pittsburgh

Product: Federated Investors provides a variety of investment and cash management services for bank trust departments and commercial banks.

Personnel: Senior administrative management and marketing sales representatives.

Booths: 901, 903, 905

* * *

FINANCIAL PUBLISHING CO., Boston

Product: Financial promotional products geared toward the banking industry, including calendars, books, charts, software and hardware.

Personnel: Kathleen Ventola, Douglas Evert and Theresa Mahoney.

Booth: 412

* * *

FINANCIAL TECHNOLOGY, INC., Chicago

Product: Banc Planner: complete asset/liability management and financial planning; Banc Manager: general ledger/financial information system; Banc Investor: securities accounting and portfolio analysis system; accounts payable system and fixed assets system.

Personnel: Jerry Franckowiak

Booth: 411

* * *

JOHN M. FLOYD AND ASSOCIATES, INC., Houston

Profit: Profit improvement programs and decisions support systems. The firm specializes in training, operations analysis and productivity, cash management, asset/liability management, strategic resource management and marketing.

Personnel: John M. Floyd, chairman/CEO; Everett W. Ladd Jr., and Jerry L. Crutsinger.

Booths: 1031 and 1033

* * *

FORBES PRODUCTS CORP., Rochester, N.Y.

Product: Vinyl products including pocket diaries, desk diaries, desk portfolios, carrying portfolios, passbook covers, sheet protectors, proposal covers, business card holders, credit card holders.

Personnel: Patrick McCormick, Alice Valentine

Booth: 211

* * *

GRECO & ASSOCIATES INSURANCE SERVICES, INC.

Product: Secured Value — Lenders Universal Policy: Protects lenders against loss in excess of collateral wholesale value, skips, all risk physical damage and residual value on balloon note loans and leases. Collateral Protection Insurance: Automated tracking to keep all borrower collateral insured to protect lender's interests. Lenders Comprehensive Single Interest: A blanket, non-tracking program to protect lender's interest in automobiles, boats, recreational vehicles and chattels.

Personnel: Dominic "Dick" Greco, president/majority stockholder; Nathan "Nate" Sutton, chief financial officer; Randy Fetters, agent.

Booth: 732

Special Event: Twice daily drawings for door prizes.

* * *

HBE BANK FACILITIES, St. Louis

Product: Design/build services for banks, including planning, architectural and interior design, engineering, construction, furnishings.

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Personnel: Tom Lombardo, Arnold Goodman, Sally Eaton, Bob Whiles, Bill Russell, Ron Berg, Bob McDone, John Setear and Terry Altomari.

Booth: 1002

Special Event: Coupons will be distributed that can be redeemed at the booth for a quartz digital watch on a zippered sweatband. Also, a drawing for a dozen live lobsters, delivered to the winner's door.

* * *

ISC SYSTEMS CORP., Spokane, Wash.

Product: Will be demonstrating Pinnacle branch automation system.

Personnel: Robert Trepper, western regional sales manager; and Mark Walker, director, national sales.

Booth: 303

* * *

LEFEBURE, DIVISION OF L. B. FOSTER, Cedar Rapids, Ia.

Product: Touch screen ATMs, color CCTV, new overhead pneumatic systems, modular vaults, cash dispatch, modular counters, Insider (in-house pneumatic system).

Booth: Island 424

* * *

LEON SHAFFER GOLNICK ADVERTISING CO., Ft. Lauderdale, Fla.

Product: New television, radio and print campaigns, new marketing ideas.

Personnel: Greg Golnick, Marshall Golnick

Booths: 630-632

* * *

MPSI SYSTEMS, INC., Tulsa.

Product: Retail Planning System and Retail Location System, software which can develop models of retail markets which planners and marketers can use for "what-if" analysis related to facilities, ATMs, POS units and network location analysis. Geographic Information System integrates a variety of tabular and geographic data allowing users to analyze market dynamics through CRT displays, color maps and custom management reports.

Personnel: Gary L. Tandy, marketing manager/financial services; Kenneth J. Smith, senior director/financial services; Marci Belcher, marketing manager/GIS.

Booth: 1112

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MANUFACTURERS HANOVER TRUST CO., New York

Special Event: ABA Reception, Saturday, October 25, from 11:30 a.m. to 2:30 p.m., at the Grand Ballroom of the Fairmont Hotel.

* * *

MASTERCARD INTERNATIONAL, INC., New York

Products: MasterCard Credit Card (standard); Gold MasterCard (for preferred customers); BusinessCard (for businesses of all sizes); MasterCard Travelers Cheques; MasterCard Universal Travel Voucher; MasterTeller (ATM interchange network); MAPP (automated POS network) and MAPP 100 (a low-cost, high performance POS terminal). Also to be featured: "Master the Possibilities," MasterCard's new advertising campaign.

Personnel: Steven Johnson, vice president/regional sales and account management; Susan Kirk, account vice president; Susan Roller, reg. marketing director; and Alan Gehrig, reg. marketing director.

Booths: 1324 and 1326

* * *

MELLON BANK DATACENTER/DATA-LINK SYSTEMS, INC., Pittsburgh

Product: Mellon Bank Datacenter, Pittsburgh, recently acquired Carleton Financial Computations, Inc., South Bend, Ind. Carleton's principal subsidiary, Data-Link Systems, Inc., makes a valuable addition to Datacenter with its excellent Mortgage Banking System, according to Datacenter. This product complements Datacenter's line of totally-integrated online systems. Mellon Bank's Datacenter and Data-Link Systems, Inc., will be exhibiting side by side at the convention.

Personnel: Kerry Ryan, senior vice president/Datacenter Group; Tom Kelly, vice president/Datacenter Marketing Division; Joe Pitts, president, Data-Link Systems; and Rich Mayo, vice president/Data-Link.

Booths: 323, 325, 327, 329, 331

* * *

OAK RUBBER CO., Ravenna, O.

Product: IMPACT imprinting of domestically manufactured quality balloons and balls for promotional advertising. IMPACT printing gives the most bold, sharp images available, and gives a bank a prestige image, the firm reports.

Personel: Murray P. Collette, executive vice president; Perry Williams Jr., senior account executive; and Ron J. Kusmier, special markets manager.

Booth: 1107

* * *

PHOTO CORPORATION OF AMERICA (PCA), Matthews, N.C.

Product: Portrait promotion program designed to increase loans, deposits, IRAs, etc., and to celebrate anniversaries, new branch openings, etc.

Personnel: Bill Simms, national sales director, Gene Remo, Dick Shutze, Geoff Squire, Barry Fratkin, Larry Johnson and Mark Speer, regional account directors.

* * *

ROSS, DELANY & McGARVEY INC., Marietta, Ga.

Product: Specializes in non-interest expense reduction, merger operations, economies of scale, systems and workflow improvement.

Personnel: Jim McGarvey, Dick Ross, Tom Karson and Andrea McManus

Booth: 413

* * *

SHESHUNOFF & CO., INC., Austin, Tex.

Product: Bank Marketing Services, targeted programs designed to match a bank's best customer prospects with the services the bank offers. Includes analysis, planning and implementation of effective sales campaigns. Also Financial Information Services: publications and microcomputer software for improving performance and profitability.

Personnel: Alex Sheshunoff, Mike Morrow, Harold Brewer, Cass Bettinger and Jack Jacobs.

Booths: 729, 731, 733

* * *

SOUTHERN VITAL/DATAPLEX, Flora, Miss.

Product: Dx3600 and FCPSpc: A low-cost check processing system for smaller financial institutions. Also Ambankpc: An integrated applications software system for smaller financial institutions.

Personnel: Dallas L. Nash II, Robert "Bob" Young, John Scott and Sandra Hardeman.

Booth: Island 624

* * *

TSSI, TECHNICAL SUPPORT SERVICES INC., Ossining, N.Y.

Product: Provides a single source for maintenance of IBM 3600/4700/327X financial networks; installation of cable networks; turnkey network installation and network cable reconfiguration; equipment sales/leasing; and TELLERLINE, a line of problem-solving auxiliary products.

Personnel: Tom McLaughlin, president; Ann Zeller, marketing director; Bill Dix and Frank Sutherland, marketing representatives; and Linda DeBeech, show coordinator.

Booth: 218

* * *

UNIVERSAL PENSIONS, INC., Brainerd, Minn.

Product: UPI is a full-service organization specializing in IRA, SEP and Keogh programs. UPI offers professional education, toll-free consulting, publications, forms, IRA compliance review and marketing materials.

Personnel: Thomas Towne, Arnold Johnson, Dale Schmeck, Thomas Anderson.

Booths: 441-443

* * *

UCCEL CORP., Dallas

Product: New software and services includes Infopoint:TMS, designed to process transactions regardless of where they originate. A building block of this new product will be the Infopoint:ACH, for electronic transfers.

Personnel: Don Steele, Frank Marlow, Jack Meredith, David LaFleur, P.J. Hoke, Tony DeTaranto, Bob Wiseman, Tina Duy, John Capobianco and Avery LaFollette.

Booth: 1242

* * *

VISUAL CONTROL SYSTEMS, INC., New York

Product: VISCON, electronic and magnetic signage and point-of-purchase displays. Will be featuring LiteLine, new backlit rate sign, and GIFILA, new marketing system for welcoming customers and monitoring traffic on the banking floor.

Personnel: Barry Puritz, Howard Lynch, Dale Denmark and Rick Meikle.

Booth: Island 212

* * *

B.C. ZEIGLER & COMPANY, West Bend, Wis.

Product: Fixed rate debt and capital debt for banks and bank holding companies.

Personnel: E.H. Rudnicki

Booth: 504

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Facing the Future: Ten Key Issues

BANKERS TODAY must feel a little like Alice after she fell down the rabbit hole. In this deregulated world of financial services, it takes all the running you can do just to stay in the same place.

However, this month, MID-CONTINENT BANKER invites you to step off the treadmill for a few moments, and take a look around. As our industry meets in San Francisco for its annual convention and takes stock of its future, let's consider 10 key issues that will shape banking for the next decade and beyond.

For this look at the future of our industry, MID-CONTINENT BANKER polled academics, regulators, consultants, lawmakers and leading bankers at institutions ranging from small community banks to New York money-center institutions. Their remarks begin on page 20.

We hope their words inform you, possibly help you, but most important, get you thinking about these key issues:

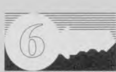
Interstate Banking
How will the structure of the banking industry be changed by regional and eventual national banking? What will be the roles of money-center banks, regional banks, community banks?

Nonbank Competition
How can banks meet the threat of new, nonbank competitors, such as brokerages, insurance companies, money-market funds, retailers, etc.?

Small Banks Squeezed
Small banks are seeing their earnings squeezed — why, and what can they do to bring earnings back up?

Debt Problems
Bad debt is in the news constantly — LDC, ag, energy, real estate, the consumer debt load, the trade imbalance, the federal budget deficit, leveraged buyouts — should bankers be worried about it? What should they do?

Shortage of Managers
Is there a shortage of managers who can handle the tumultuous changes in banking? If so, what can banks do about it?



Telecommunications
How successful will banks be in integrating telecommunications and other technological services over the next five to 10 years? Will they be left behind by competitors?

Liability Crisis
How can banks convince their managers to take more responsibility for their actions when the liability safety net to protect them from the results of failure is disappearing?

New Products and Services
How successful will banks be at competing in nontraditional markets, such as insurance, securities, real estate, etc., over the next five to 10 years?

Banking Bill
Will we ever see an omnibus banking bill? What will be its most significant provisions?

Tax Reform
What effect will the new tax bill have on banking?

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Interstate Banking

Conventional Wisdom Is Wrong

By Joseph G. Sponholz
Executive Vice President,
Chemical Bank, New York City

WE ALL KNOW that deregulation will increase competition, promote consolidation of the industry and separate institutions that can compete in a free market place from institutions that cannot. We have to move beyond these general points to more of the specifics.

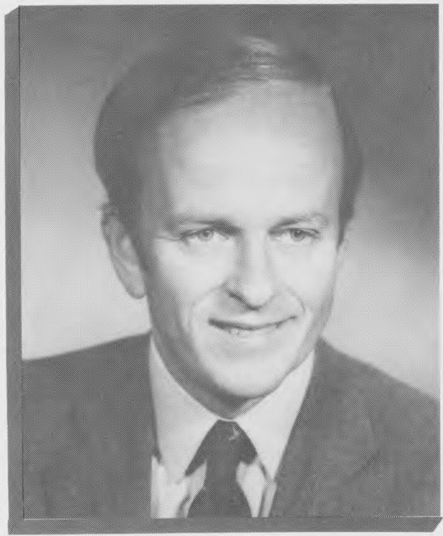
In several areas, the conventional predictions are wrong.

• Conventional wisdom holds that economies of scale in banking are unlimited; that bigger is better, and that if nationwide banking were permitted, a few aggressive competitors would expand into giant superbanks, each operating on a national scale and wielding great financial power.

The evidence simply does not support this view. In fact, the evidence suggests that economics of scale in banking may be limited to single metropolitan regions.

Major banks in California have tended to concentrate their operations in either Los Angeles or San Francisco. These profit-maximizing firms chose specific metropolitan regions instead of the entire area in which they were permitted to branch. If opportunities to achieve economies of scale through broader expansion had existed, these banks would have acted to take advantage of them.

Those of you whose home states allow statewide branching know this is true in your own states. I certainly know it's true of New York, where downstate New York City banks have not succeeded in expanding profitably into upstate regions on most any basis, much less economies of scale.



"*De*concentration is just as likely to occur in some markets as increased concentration is in others."
Joseph G. Sponholz

• My second observation is that many factors determine whether a market will become more or less concentrated, and *de*concentration is just as likely in some markets as increased concentration is in others.

For example, statewide concentration has actually been *de*creasing in California for many years — not only because it's too high given the existing demographics of the state, but also because California is a high-growth state. Economic growth increases the demand for funds and attracts new entrants into the market.

• My third observation is that deregulation will not necessarily lead firms to offer a broader line of products. In fact, there are economic forces encouraging specialization today and these forces will, if anything, be stronger in a deregulated environment.

• My final point is that attempts to integrate local and/or specialized business into nationwide so-called universal banks are as likely as not to fail. There are two reasons.

First, no value is created for shareholders by merely acquiring businesses and allowing them to operate independently.

The second reason universal "super banks" won't commonly succeed is the high cost of acquisition. An acquiring company not only must add value by contributing to the target, it also must justify often substantial merger premiums to its shareholders.

I predict much greater diversity in financial services than exists today, and certainly not the supermarket/superbank homogeneity commonly expected. While there will be fewer, larger banks, this strategy will not succeed across the board.

I especially expect technology to have a profound influence on our business.

Many acquisition-oriented banks are going to pay far too much for the privilege of operating across current geographic boundaries, and I'm forecasting, therefore, the dissipation of some shareholders' wealth.

You can expect the winners to be bankers who are both strong thinkers and effective managers, who look before they leap. • •

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Interstate Banking

Credit Allocation In Jeopardy

By Frank K. Spinner
President
Lemay Bank & Trust
St. Louis

I HAVE BEEN fortunate during my banking career to have the chance to work in the management of a large regional bank, a statewide bank and two independent community banks.

I have seen firsthand the role each plays in supporting small and medium-size businesses which are so vital to the American free-enterprise system. Employment statistics of the last 10 years clearly show that new jobs come primarily from small and medium-size businesses.

While there are only a few banks in most other nations following the capitalist system, there are approximately 15,000 individual banks in America.

This large number of banks improves the ability of small and medium-size businesses to borrow. These businesses usually cannot go to the stock or bond markets. Their books are not the most comprehensive. Many do not use CPA firms. They need banks and bankers who will listen and act, based on the borrower's honesty, integrity and willingness and ability to pay.

When banks become part of holding companies, and function in effect as branches, the loan policy changes. Figures become all-important. Holding company executives have no way to judge the aforementioned qualities of the borrower. Many worthy loan requests are rejected. New business ventures and business expansions are stifled.

In my opinion, as the number of independent banks declines, there is a corresponding decrease in the ability of small and medium-sized businesses to fulfill their financial needs.

Carried to the extreme, this could lead to the death of the goose that now lays the golden egg for our economy.

"Employment statistics clearly show that new jobs come primarily from small and medium-size businesses."
Frank K. Spinner

States Have Right to Experiment

By U.S. Senator Jake Garn
Chairman, Senate Banking Committee
Special to Mid-Continent Banker

IN THE RISE of regional interstate banking compacts, the individual states once again are acting as laboratories in the evolution of alternative banking structures. These experiments with geographic deregulation parallel the experiments the states have conducted with product deregulation under the dual banking system.

The federal government has deferred to the states in setting geographic boundaries on banks' deposit-taking operations since the charter of the Second Bank of the United States expired in 1836.

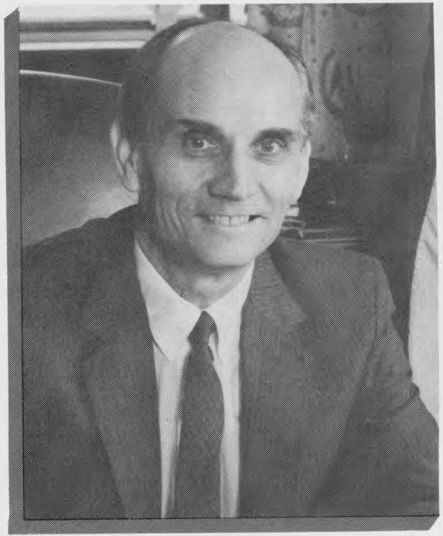
Several arguments against geographic deregulation have been advanced. One argument is that it will lead to excessive concentrations of financial power.

A second argument against geographic deregulation is that banks will become less attuned to the needs of their communities.

By experimenting with regional compacts, states will be able to determine whether there is a real threat of excessive concentration of resources, or loss of attention to community needs.

Numerous arguments also have been advanced in favor of geographic deregulation. One such argument states that it will improve customer service through more convenient banking offices (a bank office near the consumer's home and another near his or her office), and through larger lending limits.

I do not believe that all wisdom resides in Washington. If the states find there are net pluses to geographic deregulation, I have no doubt that the states will continue to expand their regional compacts to reap those benefits.



"If the states find net pluses to geographic deregulation, I have no doubt the states will continue to expand their regional compacts."
U.S. Sen. Jake Garn

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NonBank Competitors

Banks Should Exploit Advantages

By Joel Friedman
Director, Strategic Management
Arthur Andersen & Co.
San Francisco

NOUN. AN INSTITUTION for receiving, lending and safeguarding money.

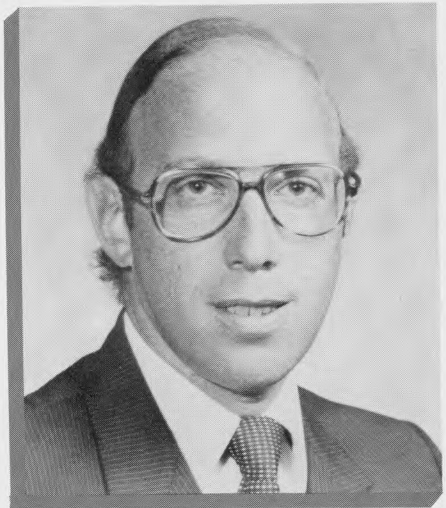
According to the Random House Dictionary, the definition above describes a bank. According to today's typical financial-services customer, it also could apply to Merrill Lynch, General Motors, Sears, Prudential and hundreds of other nonbank competitors.

In the past few years, we have seen the emergence of the "neo-bank" attacking traditional bank markets by reinventing the ground rules of competition. What is the outlook for banks in the years ahead? Can they sustain an advantage against these new invaders, or has the tide turned?

The answer will be shaped by three factors: the barriers to entry against nonbanks, the diversification strategy of these new providers and the ability of banks to exploit competitive advantages. Let's briefly examine each factor.

There are a variety of potential barriers to entry, including regulation, proprietary technology, large required capital investments, economies of scale and high buyer switching costs. In reality, however, barriers to entry into the banking business have all but vanished.

Even if Congress closes the nonbank loophole, many new entrants will be grandfathered. Bank charters are not required to make loans or offer deposit-like instruments. Capital access is hardly a restraint to new financial-service giants like Sears or GM, and the insurance companies and securities firms have highly competitive distribution channels.



"Banks can expect a continuing, relentless drive of new competitors onto banking turf."
Joel Friedman

Given the lack of entry barriers, many nonbanks have adopted ambitious diversification strategies at the same time banks are attempting to enter insurance and securities markets. These strategies are founded on several fundamental business needs:

- The need to improve the efficiency of the distribution system. Insurance firms, for example, want to turn agents into financial planners, as do securities firms with their brokers.
- The need to broaden the customer base. As all market segments become vulnerable to competition, institutions can reach more customers by offering more products and meeting a larger portion of their financial-services needs.
- The need to diversify earnings. In recent years, insurers have learned the perils of depending on whole-life premiums, while S&Ls have paid the price for their dependence on mortgage loans. A broader service base may lower this risk.

Consequently, banks can expect a continuing, relentless drive of new competitors onto banking turf.

How can banks sustain their traditional competitive advantage?

First, banks have the lead in this competitive race and have an inherent advantage. In consumer markets, for example, they still offer the best combination of convenience, price and product breadth. They will continue to be the primary consumer financial institution, although increasingly sophisticated consumers are willing to maintain multiple relationships.

In commercial markets, banks still provide the best package of services to meet the needs of corporate treasurers, although corporations frequently bypass banks and access financial markets directly.

It is dangerous for bankers to rest on their laurels. The new competitors are chipping away at markets, targeting selected niches.

To compete effectively, banks may need to maintain the mantle of "full-service banks," while focusing their efforts instead on products and customer groups that offer the greatest sustained profitability.

Finally, banks must not lose sight of their primary competitors, namely, other banks. Competitive battles will be waged, not against industries such as securities or insurance, but against individual institutions. Each bank must identify its true competitors carefully. By exploiting existing positions of strength and targeting selected markets, most banks should be able to withstand the new competition. • •

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William C. Nelson
InterFirst Bank
Dallas, Texas

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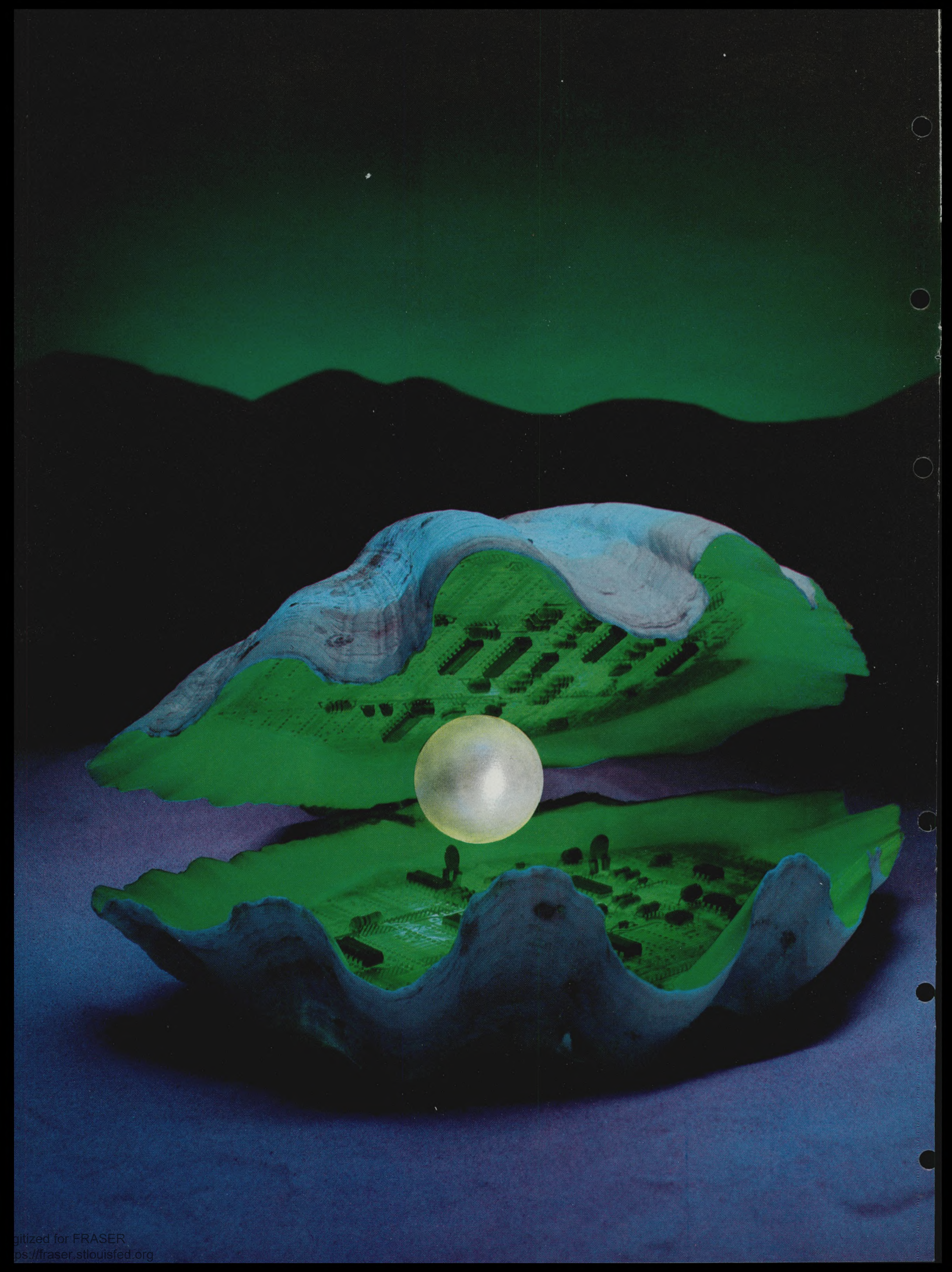

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NonBank Competitors

Old Techniques No Longer Safe

By Eileen M. Friars
Senior Vice President, and
Paul D. London
Associate
The MAC Group
Chicago

THE THREAT OF DEREGULATION and the inevitable invasion of armies of nonbank competitors have begun to hit home.

Not only money-center banks, which regularly absorb the first shock waves, but also regionals and small community banks are feeling the effects of nonbank competition.

Must banks take the full force of these assaults, or can they deflect the blows?

The solution will require banks to end their reliance on historically successful products and delivery methods, and there is no time to waste.

We can no longer afford to be all things to all people and compete in markets that once belonged solely to us. Banks must act quickly but intelligently to establish sustainable competitive advantages in specific target markets.

In the consumer arena, banks must think of market positioning and unhinge themselves from the branch mentality. Convenience should be transactional rather than locational.

Bankers should offer relationship pricing to "lock in" profitable customers, offering product packaging and bundled pricing. In this market, product development also will be a key competitive weapon.

In the commercial market, banks must begin to move away from lending and find ways to add value to the services they offer. Specializing in an industry or providing consulting services will give banks opportunities for profit in serving commercial accounts.

Corporate account officers must offer financial strategy analysis, problem identification and solutions, which may or may not mean lending. Non-credit service products also can add value, by allowing for more sophisticated financial/business analysis.

Commercial banks can meet the challenge of nonbank entrants, but only through innovation and value added.

"In the commercial market, banks must move away from lending and find ways to add value to the services they offer."
Eileen M. Friars

Senior managements must seize the opportunity and change their organizations now. Tomorrow may be too late. • •

Eileen M. Friars is a senior vice president and head of the Chicago office of the MAC Group, an international management consulting firm. She is also co-director of the firm's financial services industry committee.

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Fixed-Rate Mortgages Favored

MORE THAN nine out of 10 Americans getting home loans from mortgage companies choose fixed-rate instruments over other types of loans, says the Mortgage Bankers Association of America (MBA).

A recent survey showed that 93.5% of home loans originated by more than 20 of the nation's largest mortgage bankers in July were of the fixed-rate variety.

Popularity of fixed-rate loans has increased steadily since the summer of 1984, when adjustable-rate mortgages accounted for 36% of single-family home-loan originations made by mortgage firms.

Americans favor fixed-rate mortgages because they permit easier budgeting of monthly payments, says the MBA. They also favor the certainty of a fixed-rate loan.

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John L. Cleveland

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Small Banks Squeezed

Keep Operating Costs Down

By Thomas H. Olson
President-Elect
Independent Bankers Association
of America

COMMUNITY BANKERS are going through a period of pressure on earnings, which is challenging local bankers to keep earnings at respectable levels.

Two factors underlie much of the pressure on local bank's earnings. One is the legacy of interest rate deregulation, which since 1980 has increased the banks' average cost of funds and has tightened operating margins in the traditional lending business.

The other factor is that many banks are committed heavily to smaller business customers in industries such as agriculture and energy that are also experiencing depressed earnings.

However, success requires careful and constant attention to the banking business. Above all, the community banker must keep his operating costs down. Today there is no margin for error. Banks must be low-cost producers of products and services if they are to achieve adequate margins.

This certainly applies to the cost of funds. Bankers must consider whether the cost of additional funds is warranted considering their return from reinvestment.

Being a low-cost producer also applies to banks' transaction costs, insurance and other operating costs. The Federal Reserve payments system, bankers' bank services and other means available to community banks may be essential to maintaining independent banks' access to state-of-the-art technologies necessary for low operating costs.

Community banks can broaden their sources of earnings by constantly seeking new and different products, including niches that use the unique resources of the bank or that might be available temporarily to offset reductions in earnings from the regular product lines.

Organizations can help local bankers identify and develop products that can be retailed by community banks to their customers. For example, the travelers check and credit card programs sponsored by the Independent Bankers Association of America are enabling many local banks to offer those products.

To make earnings more stable, community banks need to devote more attention to diversifying assets and spreading risks. This may mean securitizing more of the loans they originate. Efforts are being made to create a strong secondary market for longer term farm real estate loans. If this is successful, community banks will be able to derive more of their earnings from loan origination and servicing fees and share the credit risks and rewards from those loans with investors who buy the mortgage-backed securities.

Even with astute management that takes advantage of earnings opportunities, many community banks that have been hard hit by the deflationary forces of the 1980s will need time to rebuild their earnings and replenish the capital base on which risk-based earnings are generated.

In summary, although there is no single formula for healthy earnings for community banks, there is no reason our community banks cannot remain effective competitors. I am confident that the vast majority of our local banks can and will be vibrant competitors in serving their communities in the years ahead. • •

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Debt Problems

Sky Not Necessarily Falling

By Murray L. Weidenbaum
Director,
Center for the Study of American Business
Washington University,
St. Louis

MANY IMPORTANT parts of the American economy have been suffering from the burden of rising debt — agriculture, oil country, banks lending to Latin America and so on. Total domestic debt (excluding that of financial institutions) rose from $2.3 trillion at the end of 1975 to $7.0 trillion in early 1986.

Those numbers are astronomical and the trend bears watching, but all this is not cause for alarm.

Here's some perspective: The federal government has increased its indebtedness more rapidly than the private sector — from $572 billion in 1977 to $1.6 trillion at the end of the first quarter of 1986. During the same period, nonfinancial business firms expanded their indebtedness at a slower rate, but by a larger absolute amount. Total business indebtedness rose from $1.0 trillion in 1977 to $2.4 trillion on March 31, 1986.

The indebtedness of all three major sectors — government, business and households — has been expanding faster than the GNP.

How heavy has the expanded debt load of American business become in comparison to the ability to carry it? One basic measure, the debt/equity ratio, shows a significant rise — from about .7 in the early 1970s to over 1.0 at present.

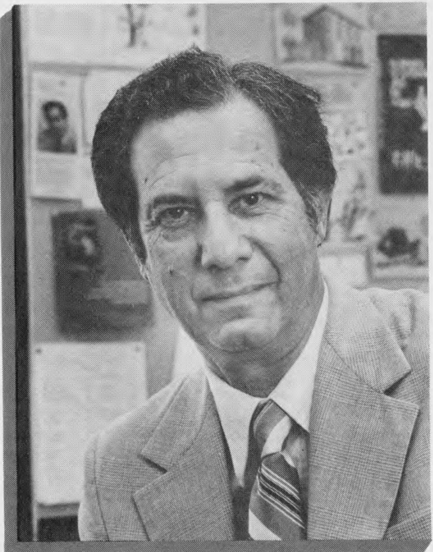
However, when the data are converted from book to current market values, the ratio of debt to equity remains well below the peak of 1.3 reached in the middle 1970s.

Perhaps the most relevant but rarely-used measure is the relationship between corporate indebtedness and productive assets which it finances — the increase in long-term investment plus working capital compared with the total rise in debt over the same period. In every single year over the last decade, the growth in corporate physical assets has been larger than the rise in their indebtedness.

In other words, there seems to be real value behind the heavier debt load of American business.

Before 1970, the big swings in business and government debt tended to offset each other. In the last several years, however, both public and private borrowings have been rising faster than the economy as a whole, driving the debt to GNP ratio to a new high. Clearly, the debt situation deserves our continuing attention — but this is hardly the time to push the panic button. • •

Dr. Weidenbaum is Mallinckrodt Distinguished University Professor at Washington University in St. Louis. He was President Reagan's first chairman of the Council of Economic Advisors.



"The indebtedness of all three major sectors — government, business and households — has been expanding faster than the GNP."
Murray L. Weidenbaum

Spread Risk, Be Vigilant

By Edward J. Williams
Treasurer,
Brown Brothers Harriman & Co.
New York

Mr. Williams is 1985-'86 president of Robert Morris Associates.

LDC DEBT, ag lending, energy lending, consumer debt, real estate debt, commercial and industrial loans, securities lending and so on, are all forms of debt we have heard much about in the media over the past few years.

Usually the publicity exposes excesses that have resulted in losses to lenders, and in some cases, failure of the lenders themselves.

The common factors in all debt are the debtor, the lender and the economic purpose the obligation was undertaken to achieve. The problem in common is the miscalculation of the ability of the economic purpose to generate sufficient funds within the stipulated time to repay the lenders, on either the term agreed, or at all.

Lenders must accept risk as part of their business. No banker realistically can expect every loan to be repaid as originally planned, or even that every loan will be repaid.

However, I feel we as lenders must give greater attention to evaluating concentrations of risk. The failure of any economic area should not result in losses so great that they seriously impair the capital of a financial institution, except perhaps in the most ex-

(Continued on page 47)

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Shortage of Managers

Hire and Develop New Skills

By Lloyd C. Lyons
Senior Vice President
Indiana National Corp.,
Indianapolis

Mr. Lyons is a member of the executive committee of the human resources division of the ABA.

WHAT MANAGERIAL skills will banks likely be lacking, and what can we do about it?

First, lets look at the skills that will be needed:

• Bank managers will need the skill to orchestrate tactical and strategic business thinking simultaneously.

• Bank managers will need the skill to manage people by objectives, to achieve expected business results, rather than to manage by methods, style or personality.

• Bank managers will need the skill to visualize needed organization change, to communicate that need for change in a contagious way and to adopt systematically and persistently the steps necessary to ensure the change occurs.

What can be done about a skill shortage?

• Attract successful managers (line and staff) from other industries that have undergone rapid change and place them in key positions.

• Use consultants to help bring about some organizational changes and include "up and coming" managers in the projects so they can experience first-hand management of the change process.

• The top manager should begin to demonstrate results-oriented management rather than methods-oriented management so this management philosophy can be embraced by the rest of the organization.

• Management teams can study other industries' responses to environmental changes.

• Top management can adopt an organization-wide macro change model to help younger managers visualize and implement the process of change.

Present day line managers may find their skills and themselves extinct in the near future. This phenomenon may create an oversupply in this group of bank managers, as their skills may not be considered usable to succeed in the changed banking environment. The result will be terminations, early retirements, outplacements, transfers, etc.

A void of "new banking" managers will develop. The void will develop not because of a shortage of people, but rather because of a shortage of people with the skills to achieve results in the "new banking" environment. • •

Challenged to Retain Talent

By Don W. Schooler Jr.
President
Don Schooler Jr. & Associates
Springfield, Mo.

THOSE WHO ENTERED the banking business in the 1940s and 1950s followed a structured journey up the ladder of banking into significant management positions. Some of these bankers had college-level educations, but more did not.

Those who followed this traditional pattern of rung-climbing normally had to rely on the intelligence of their predecessors for their management training, supplemented by trade journals, seminars and some banking and lending schools.

For many, this brought great success stories. This traditional method of producing bank management fathered many successful bankers.

During the 1980s we have watched with amazement as many of our peers have closed the doors on institutions that seemed to perform very well during the past several decades. In almost every case, traditional banking mistakes finally led to the terse explanation of "poor management."

With this background, what is the current outlook for talent in the banking business and what can be expected in the near future?

The banking business is seeking and attracting candidates with much more education. Beginning in 1960, according to the flow of bankers through our company, there has been a much higher ratio of candidates with BS degrees, post graduate degrees and technical banking school certificates.

Banks are putting much more emphasis on post-collegiate industry education, which seems to have been encouraged by national and state banking associations, the regulators and the keen perception that ongoing education may help banks avoid problems.

Banking historically has been able to attract quality individuals because the profession has had a positive image. Until recently, turnover in banks was remarkably low compared to other industries. Now, middle and upper management in banks have become increasingly mobile.

We believe bankers should seek top talent, provide ongoing education as an annual prerequisite and provide competitive compensation packages to retain those who lead the bank into top performance.

Even though our industry has seen notable changes, it is a mature industry with a deep pool of talent and a great database of successful management techniques available to all bank officers. The talent is available if bank ownership will apply the resources to achieve success. • •

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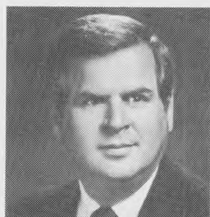

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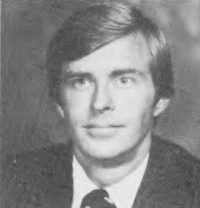

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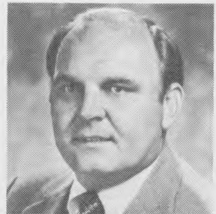

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Telecommunications Delivery

The Electronic-Banking Race

By J. David Huber
Executive Vice President
Mercantile Bank
St. Louis

THE PROSPECTS for electronic banking resemble a race between banks and their nonbank competitors. To the victor belongs the larger customer base.

Amid discussions of smart cards and a retailer's new multi-purpose financial services card, it may be surprising to bankers to realize that our industry's toe is against the starting mark, not three paces back.

Not only are we in the race but we also have an advantage. We have the customers for financial services. It is easier to keep customers than to capture their allegiance.

Our industry also benefits from its extensive experience with data processing and electronic communications. About one-third of our customers use automated teller machines for routine cash withdrawals and balance inquiries. With shared systems, those transactions can be carried out miles or even continents away from the customer's home bank. The equipment is incredibly reliable — up and running more than 99% of the time.

The banking industry also has developed extensive systems to support wire transfers and credit-card purchases anywhere in the world. We're adept at using computer and electronic capabilities to indirectly enhance our service to customers as well.

As an industry, therefore, we understand the convenience and cost-saving potential of electronic banking. Furthermore, since our lessons have been learned through the discipline of handling customers' money, we take for granted the need to be accurate and timely, and it's second nature for us to consider how our decisions affect service to our customers.

Those are some of the advantages banking brings to this race. But it is just as important to realize that our nonbank competitors also come well-conditioned for the contest.

The leaders among them operate with a retailer's mind-set. They perceive the plastic access device as a component of a delivery system rather than a vehicle to activate a process. Their sales strategy rests on identifying and serving market niches, influenced but not limited by local preferences. Perhaps the biggest advantage for nonbank competitors is that they approach the starting block without the weight of regulation to which banks are accountable.

We should remember that we've been training for this race longer than our competitors have. And several factors give us additional time to hone our skills.

In some cases the capability of available equipment outpaces our customers' readiness to use it. That gives us leeway to integrate the systems into meeting our customers' needs, not vice versa. In the process we will each decide what kind of bank we want to be and how best to serve our customers. We will become market-driven, step-by-step and through our own offensive decisions. The midwestern heritage of conservative consumer and legal attitudes provides additional time to weigh the considerations. It can be our ally in implementing electronic banking appropriately for our customers and for our institutions.

The economies of scale are tipping toward electronic banking. The demographics point in its direction. Competitive factors make its consideration imperative. That leaves one potential stumbling block for us as bankers — our own attitude toward electronic banking. It is time to admit its viability. Our nonbank competitors already recognize it as a market demand and have accepted the challenge. I am confident banking will not forfeit the race. • •

Banks Can Fill the Demand

By Thomas A. Spall
Senior Vice President
Indiana National Bank
Indianapolis

FINANCIAL institutions are active in expanding their geographic-market targets to the extent allowed by regulators. As market penetration broadens, banks will become more dependent on telecommunications and other technology services.

It's becoming more important to provide financial services to the customer when and where they are desired. The growing use of electronic-payment systems by customers makes it difficult to support these financial transactions without use of integrated technology. This creates added business demands for telecommunications and technology to be integrated into the products, services and, especially, delivery systems of such institutions.

Bank managements will utilize telecommunications and technology as they expand through acquisitions and mergers into larger geographical areas. This utilization will help lower costs through economies of scale. Telecommunications also will be required to provide timely and meaningful information.

Management will, as a result, continue to place more emphasis on strategic business plans to identify business targets that require such technological support. This will help

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influence proper commitments of resources to the tactical-planning process to assure the overall success of business plans.

The growth in cost will be a driving factor to unite national networks to help utilize economies of scale to reduce unit costs. This will occur in both bank and nonbank networks. Financial networks will continue to advance with use of integrated telecommunications and technology and provide banks with a cost-effective alternative to participate in the electronic-payment system for the forseeable future.

I believe standards for integrating telecommunications and technology will improve as the struggle within the communications industry identifies the ultimate survivors, making it easier to deal with integration issues. No matter how quickly this occurs, alternatives will be available to the banking industry to support its needs.

The banking industry will be successful integrating telecommunications and other technological services as it realizes the fundamental need of serving the customer and managing the enterprise. • •

Marketing Is the Real Question

By Robert J. Listfield
Principal
Golembe Associates, Inc.
Boston

FROM a purely technological standpoint, banks will no doubt be successful in integrating telecommunications and other technology-based services over the next decade or so. There is little doubt that banks can, and have, attracted highly competent technical staffs. Furthermore, as banks and bank HCs grow as a result of in-state and interstate mergers and acquisitions, banks will be able to better afford to upgrade their technical staffs and will have greater need for such talent in order to electronically interface with their far-flung affiliates.

But I do not see the real question as technological in nature. Rather, the real question, as I see it, is a marketing one. And that is, "Will banks be able to anticipate the technology-based service needs of their customers and provide the products and services that meet that demand in a manner that enhances or at least does not detract from the banks' profitability?" Unfortunately, based on past experience, I am not convinced that the answer to this question is as positive as that of the former.

Many bankers rue the day they started the service, as the net cost of their corporate deposits has risen, or balances have been directed elsewhere. It is too late to withdraw such services because of competitive pressures. Banks now have to offer cash-management products because a failure to do so will result in lost corporate business. Nonetheless, except for a few major cash-management practitioners, the service, taken in its entirety, has probably not resulted in better bank profitability.

An analogous situation can be found with ATMs. While also technologically sound and popular with users, I am not convinced that ATMs have been of net positive benefit to most banks. A few banks may have benefited from increased market share by having a superior ATM network, some banks (probably not most) may actually have saved money from a reduction in tellers and brick and mortar. But on balance, most banks *must* have ATMs to remain competitive even if it results in increased cost. Sure, many customers like ATMs because they provide for convenient access to funds, either after normal banking hours or in remote locations. Do most banks charge for this convenience? I doubt it.

The bottom line is that banks should not offer technology-based services simply because they have the skill to do so. Rather, they should use technology to provide services that will result in less cost or that meet a customer demand; and if customers do want a more expensive service they must be expected to pay for it, or it should not be offered.

I believe the message of past sins is clear. Before a bank offers a technology-based product, it should attempt to assess what the impact of the product will be on its bottom line and who will pay the extra cost, if any. If no one will pay the cost, it probably is a service that should not be offered. If someone will, it should be priced to offer a fair return on investment. • •

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Liability Crisis

Look Before You Leap

By Richard H. Klovstad
Vice President
Risk Management/Insurance
Norwest Corp.
Minneapolis

BANKING in the U. S. is undergoing a major structural change. New competitors, many of which are formidable opponents, are entering the arena that traditionally has been a sanctuary for commercial banks. Many of those competitors have superior marketing capabilities, wide variety of products and vast resources to mount aggressive competitive campaigns.

It's clear that only strong banks will survive over the long term. Weak or marginal performers will find it increasingly difficult to compete. If a bank is to survive this challenge, it must offer products and services to its customers that are superior to those offered by competitors. This will require management and staff to be resourceful, bold and innovative. Thoughtful risk taking must be encouraged if proper results are to be achieved.

At first blush, it may seem that such long-term survival strategy will enlarge the risk to which the bank and its officers and managers are exposed. While there are personal risks in most business endeavors, they can be effectively managed.

Bank management traditionally has relied on directors and officers (D&O) liability insurance as a means of protection against malpractice claims. With D&O largely unavailable today at less than extraordinary prices, investigation is being made into what safeguards exist to stave off personal liability.

First, it should be realized that bankers must elevate their level of care and diligence if they are to avoid personal liability.

Even though a bank officer may not be protected by D&O insurance, significant protection normally is afforded by bank bylaw indemnity agreements. In most cases, a bank officer can be indemnified for claims of malpractice if he/she acted in good faith and in the best interest of the organization he/she serves.

Personal liability usually can be avoided if the following principles are adopted:

- Avoid any activity that can lead to a real or perceived conflict of interest. Self-serving practices and conflicts of interest can lead an individual into serious trouble. Many successful claims against bank officers are the result of such conflicts.
- Operate with openness, fairness and complete candor. Activities conceived and executed in an air of secrecy and stealth raise questions in people's minds about their appropriateness.
- Don't make a bad situation worse. If a mistake has been made, accept responsibility for it. Make proper disclosure and seek corrective action.
- Ensure that actions and decisions are made in good faith and fair dealing and that an arms' length relationship exists between bankers and their customers.
- Never compromise personal convictions about what is right or wrong. Above all, operate with complete integrity.

While risks can never be totally eliminated, it is comforting to know that they can be properly managed with proper thought and action. • •

Danger of Pulling in Horns

By William H. T. Bush
Chairman
Bush & Kobusch Management Consultants, Inc.
St. Louis

IN A number of situations bank managements and directors have pulled in their horns and become more cautious in dealing with customers because of the liability crisis.

While such action may be advisable to protect oneself against legal liabilities, one has to question whether bank management is doing service to its customers and its bottom line in the long run.

Banks are unusual businesses. Part of their charters deal with serving the convenience and needs of the community. The Community Reinvestment Act requires banks to prove they are doing just that.

Documentation in the banking industry is extensive for any and all transactions, no matter how small or large, so if the loan officer or customer-relations person is doing the job properly, the bank should be protected and the customer served.

I always have believed that the cornerstone of being an excellent banker was knowledge of one's bank, of one's trade and of one's community. Senior management must have clear policies that can be followed, with exception procedures that are responsive and timely. Operations and lending personnel should know those policies and know when and where to go for exception processing. Information should flow up and down the chain of command relatively smoothly and people should feel free to go to whatever level of authority necessary to get an appropriate decision.

All of the above sounds basic and unsophisticated, but it is amazing how frequently problems result from violating these basic concepts.

A bank that performs consistently in its market will stand less risk of direct liability than one that has volatile and unfamiliar policies. If a bank has a traditionally strict lending policy, the marketplace is not surprised by a conservative decision made by the loan committee or lending personnel.

If, however, a bank is perceived to

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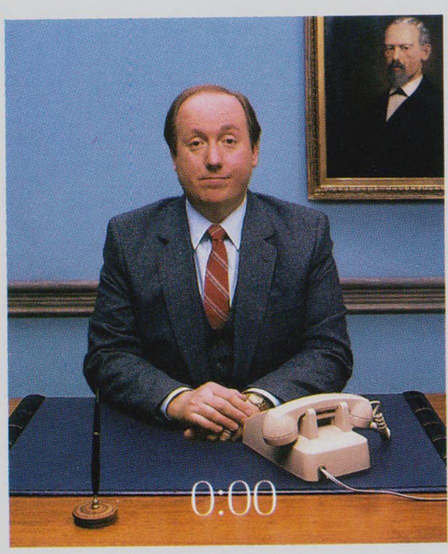

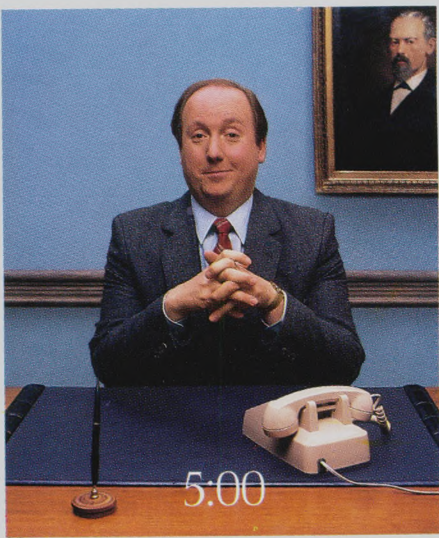

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be a liberal lender and suddenly changes its stripes, customers and the marketplace as a whole become concerned and the result could be serious misunderstandings and litigation.

There seems to be a softening in the markets for D&O insurance at the present time resulting from higher rates, tort reform and several citizens' propositions throughout the nation. This should mean a more stable environment and one that should be of less concern to bank directors and managements. • •

Combatting Banker Unawareness

By Keith J. Lazarz
Insurance Officer
Northern Trust Co.
Chicago

IT SHOULD be apparent to senior management that the cost of corporate insurance has increased substantially. What may not be apparent, however, is that the quality of the insurance being purchased today may not be as broad in protection as were previous policies.

More restrictive language contained in today's contracts, higher deductibles and aggregate limits of liability translate to more risk being assumed by banks.

The realization of this increased risk to the bank is critical to the successful implementation of loss controls that can act to replace nonexistent or unavailable insurance.

The insurance industry has been asked to foot the bill for shoddy banking practices. Multi-million-dollar loans made against nonexistent collateral have been submitted to bonding firms for recovery. Poor direction and management by directors and officers that could lead to financial demise have resulted in shareholder or regulatory actions for which D&O liability policies must respond. Unprofessional performance of fiduciary responsibilities has prompted legislation by cotrustees and beneficiaries that may not result in judgments but invariably entail legal expenses. Trust department errors and omissions policies have been asked to respond to these claims.

Restrictive coverages, high deductibles and caps on liability limits have not reduced or eliminated the exposure presented to banks. Risks that previously were thought to be transferrable to an insurance firm now must be identified and assumed by the respective bank.

The problem may be that managements that do not recognize the existence of the risk may not have translated what should be an increased awareness for loss control through the ranks.

A complete understanding by brokers or agents of both the exposures present in the bank as well as terms and conditions of today's policies sometimes is missing.

Solutions to problems arising from the "liability crisis" are not uniform or clear cut. The realization that individual personalities are present at each institution dictates that what may succeed for one bank may not for another. The least that should be understood is that the insurance responsibilities at any bank should not be dismissed as casually as in the past. • •

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Nontraditional-Service Delivery

Leaders Will Be Successful

By John Russell
Vice President/Marketing
Banc One Corp.
Columbus, O.

Mr. Russell is president, Bank Marketing Association.

BANKS that maintain leadership positions will be successful in marketing nontraditional services. They enjoy reputations as being safe and sound institutions and have traditionally been good service providers.

But banks will fail in the delivery of nontraditional services if they are not prepared to compete aggressively. Some banks will fail because of lack of competitive expertise due to poor leadership on the part of management.

All deregulated industries are in the same boat, which makes banks little different from airlines. Those that are poorly run are in danger of failing.

There are plenty of nonbank competitors eager to out-perform banks. Sears is trying to figure out its market and will take up to five years to do so. Brokerage houses and insurance firms are expected to expand their product lines. All this competition will make it difficult for consumers to choose service providers along traditional lines since all financial-service providers will resemble retailers.

Among the nontraditional services banks are expected to offer: full-service brokerage, insurance underwriting and direct money-market funds.

Cost is a major factor in delivering nontraditional services. Bank competitors have the benefit of lower overhead now, which means banks must lower their costs through provision for electronic delivery of services. Electronic delivery is the most cost effective way of delivering services, providing volume is sufficient to justify the cost.

To be on the winning side of the competitive battle, banks must develop better exclusive services and generate higher income streams. Just as customers are willing to pay more for an auto with automatic shift, they are willing to pay more for automated banking services.

Planning for future service delivery is the most challenging — and rewarding — aspect of strategic planning. • •

Strategic Preparation Is Vital

By John Fraser
Vice President
First Wisconsin National Bank
Milwaukee

THE SUCCESS banks have in competing in nontraditional markets over the next 10 years will be in direct proportion to the efforts they devote now to strategic planning for change.

Deposit-rate deregulation and increasing interest on the part of larger organizations — banking and nonbanking — in new markets across the U. S. have created sweeping winds of change in our formerly comfortable and rather predictable business. Since the competitive environment is so radically altered, the old *raison d'etre* for many banking organizations no longer obtains. Change or be changed is the choice banks will have pressed on them within the next few years.

A rational process of organizational change must begin by accurate environmental and self assessments. While most organizations can construct adequate — on occasion even prescient — assessments of environmental factors and their implications, many fail to achieve their potential because they are incapable of being objective about themselves.

An environmental assessment should include analysis of how businesses the organization is currently in — or might be entering — will be affected by changes in technological, economic, regulatory, competitive, social and demographic factors. Self-assessment should include ruthlessly objective appraisals of the organization's strengths and weaknesses, competitive advantages (current and realistically possible), resources needed to maintain competitive advantages and to overcome competitive weaknesses. Key factors for success in the businesses, niches and segments selected for emphasis also should be considered.

Only after such careful and objective assessments should key strategic questions be addressed.

Banks in isolated, small or unattractive markets may find that change isn't necessary, but others will start to develop corporate strategy for change that outlines what they are trying to become over a five- to 10-year period.

This strategy should articulate not only how banks will delete or change current businesses with respect to geographic areas, niches, segments and marketing approaches, but what kinds of new business units they should add because of the distinctive contribution each is expected to make to the overall portfolio of businesses.

Many banks fail to go through this methodical process of assessment and strategy construction because they feel their choices are limited — perhaps even obvious — or that events are passing them by. Experience shows that banks almost always have more options and more time to make the choices than is thought possible.

Banking history of the past six or seven years is littered with new business and product failures that resulted from a misplaced sense of urgency, the "we've got to do something syndrome." Examples include home banking, retail repos, sweep accounts, loophole certificates and early approaches to debit cards and discount brokerages. • •

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Key Factors to Ensure Success

By William D. Miller
President
Financial Industry Group
Marshall & Stevens, Inc., St. Louis

BANKS can be very successful in nontraditional markets, although they all won't be.

A number of key factors will determine their degree of success in entering and succeeding in new markets.

Change is the most critical factor. The next 10 years will see dramatic changes in the financial-services industry regarding competitors, technology, opportunities, services, etc. Bank management must be open to change, viewing it as an opportunity.

One way to overcome resistance to change is being taken by General Motors. It created a new firm to develop its new auto. This route was taken because it was felt that "mainstream" business might resist, delay or even kill such a venture.

Banks have used similar strategy when entering new markets, usually utilizing the HC route.

Quality of staff associated with nontraditional products is vital. Without good people to implement plans and sell products, success is unlikely.

Compensation practices, compensation levels and employee training should be considered when motivating staff. Rewards and knowledge go hand in hand to create successful sales staffs.

Effective use of technology is important in these two areas:

- How the bank interacts with customers.
- Maintaining efficient backroom operations to keep costs competitive.

System and technological constraints can greatly impact how successful a bank will be in a nontraditional market.

Other important factors include strategic focus, financial controls and exit strategies.

Knowing when to get out of a nontraditional market often is as important as knowing when to get in. Recognizing when a strategy has not succeeded, or met internal criteria, is essential to overall success. • •

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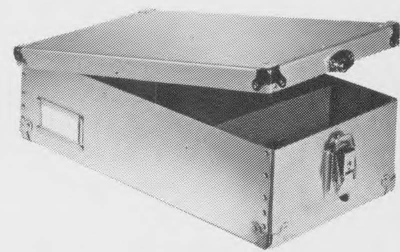

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Banking Legislation

A Welcome 'First Step'

By Andrew J. Paine Jr.
President
Indiana National Bank
Indianapolis

Mr. Paine is chairman, ABA government relations council.

FROM a banker's perspective, the Senate omnibus banking bill represents a welcome "first step." It is legislation that speaks to items that bankers wish to see resolved, such as the nonbank loophole and additional powers/services such as expanded securities activities.

However, rapid changes continue in the financial-services marketplace.

Unfortunately, the banking system is governed by out-of-date laws, some of which were enacted more than 50 years ago.

Bankers would prefer that the bill be broadened to give banks the opportunity to provide consumers with competition in real estate and insurance markets. Instead, this legislation proposes to further restrict the already limited insurance powers of banking institutions. Given the current publicized lack of availability and increasing costs with respect to insurance, it seems inappropriate for Congress to be considering limitations on banks as a source of insurance services.

The areas of this legislation that probably will receive the most congressional attention are (1) bank regulators' provisions which extend emergency bank/thrift acquisitions, and (2) FSLIC recapitalization. Due to the shortness of time remaining in this congressional session, these two issues generally are seen as ones that may be singled out for prompt resolution.

Congress needs to act on comprehensive changes in the laws governing banks and others offering financial services. Not only are these changes needed to ensure a strong and vital banking system, but consumers in the marketplace deserve the best service possible from all the competitors in the financial-services industry. • •

On the Plains of Hesitation

By Randall A. Killebrew
President
First National Bank
Petersburg, Ill.

LAST June, Sen. Jake Garn (R.-UT) finally unveiled S. 2592, the Deposit Insurance Reform and Competition Enhancement Act, which truly is comprehensive legislation containing more than 12 titles incorporating numerous proposals dealing with many different aspects of banking. The bill, while not perfect in every feature, deserves commendation for trying to address the need for banking-law reform in a comprehensive way.

However, Sen. Garn has concluded that the bill now is politically too controversial to be considered this close to congressional adjournment and the November elections, since 34 Senate seats are on the line. He is focusing his legislative efforts on passage of a bill to provide more funds for the FSLIC and to provide the FDIC with extraordinary emergency powers to assist troubled banks.

This situation reminds me of a stanza to an old poem: "Upon the plains of hesitation, bleached the bones of countless millions who, on the threshold of victory sat down to wait, and waiting they died."

Politicians, bankers and the American public all recognize that current circumstances require new rules and regulations so that traditional banking institutions can continue to serve their customers' needs.

I fear that Congress' indefinite postponement of fundamental banking-law revision dooms our industry to economic death as it waits on the plains of legislative hesitation. • •

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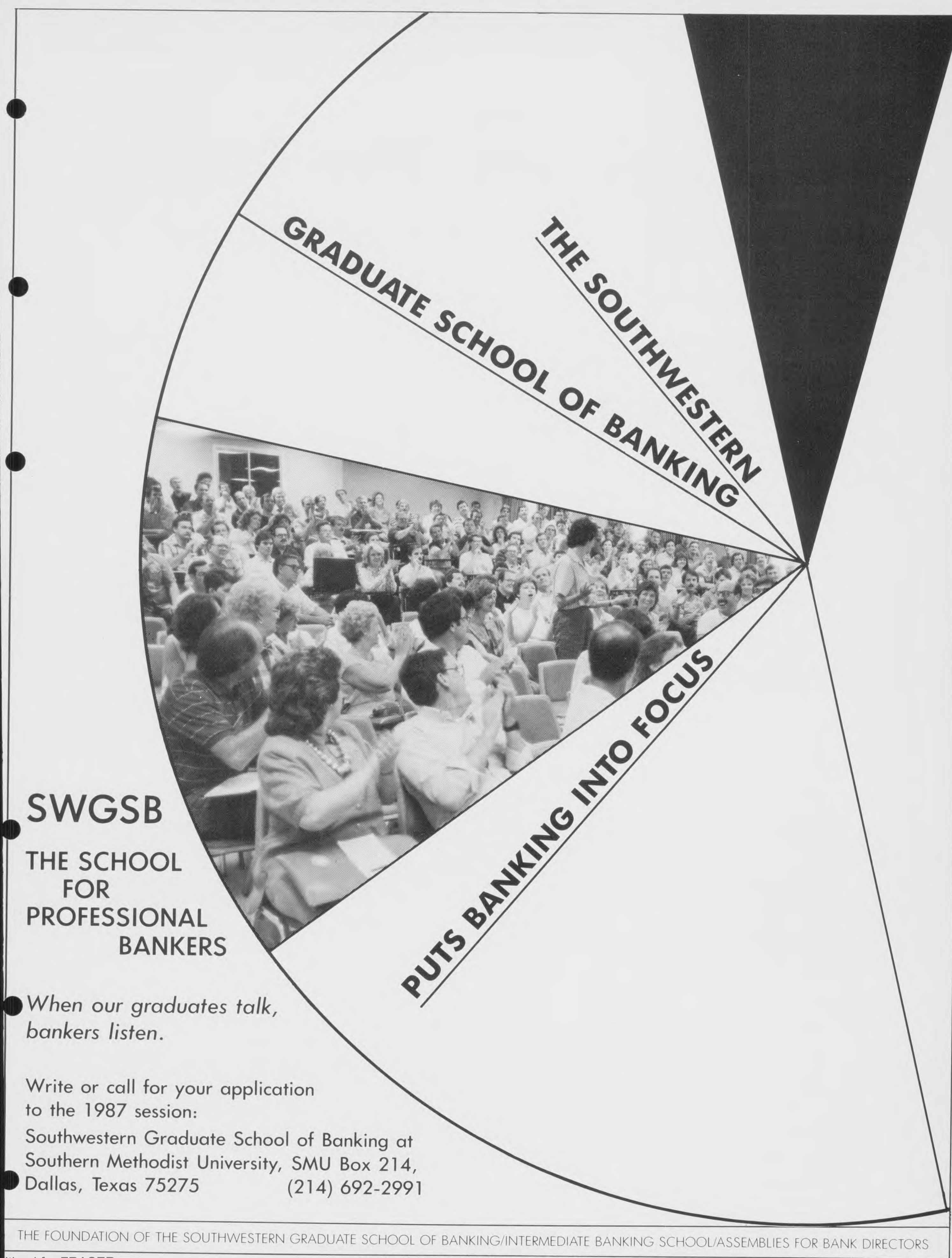

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The Tax Bill

Fairer, Simpler, More Neutral

By Richard C. Amacher
Senior Vice President
and Manager/Taxation
MCorp
Dallas

THE TAX BILL will achieve the objectives the Reagan administration outlined when the process began. Its enactment will give America a tax code that is fairer, simpler and more neutral with respect to its effect on business decisions. In general, it is a revenue-neutral bill, providing tax cuts to individuals of some $120 billion over five years and taxing business to provide the revenue.

The bill has the potential to negatively affect the economy at our present stage in the business cycle. Over the long term, taxing business rather than individuals may be desirable; over the short term, however, hitting business with such huge additional taxes at a time when business fortunes in general may be turning down will be very painful.

• **Effect on Banking.** Banking's share of the $120 billion approximates $9 billion from the loan-loss and cost-to-carry issues and significantly greater amounts from foreign tax-credit and alternative minimum-tax provisions. Banks are hit hard in terms of direct tax increases but they can anticipate being harder hit due to tax-law changes affecting their customers.

Provisions affecting the real-estate industry and its investors may throw many existing loans into default. Tax cash flow is needed to service the debt.

Denial of consumer interest deductions will discourage consumer spending and borrowing. This in turn will dampen production, employment and investment, which will cause a decrease in tax revenues.

Denial of carrying-charge deductions will discourage consumer spending and borrowing. This in turn will dampen production, employment and investment, which will cause a decrease in tax revenues.

Denial of carrying-charge deductions related to bank tax-exempt holdings will force states and political subdivisions to pay more to borrow. This in turn will increase state and local tax burdens of individuals, raising the after-tax cost of home ownership, disqualifying many prospective borrowers, which will further dampen the fortunes of the real-estate industry.

Changes affecting the energy industry, although not as detrimental as originally proposed, may add to its troubles and may preclude it from raising much-needed capital. This in turn would force more companies and people out of productive capacities, lowering overall tax revenues and placing the demands on the economy that usually accompany hard times.

IRA provisions will discourage retirement savings relative to current law. This will place more reliance on strained social security and welfare systems and may diminish core bank deposits that would otherwise have been available to support economic expansion.

Foreign-tax-credit provisions will discourage future overseas lending, which will have the effect of placing industries exporting American-made products at a competitive disadvantage with foreign exporters. Foreign banks will do the financing for foreign exporters.

Since the enactment of the first tax code in 1913, Congress has successfully tinkered with taxes to encourage taxpayers to behave in ways to achieve specific social and economic goals. Now, in one fell swoop, our tax code is to become neutral with respect to these goals. Can our fragile economy adjust, in a very short transitional time span, to a complete reversal of the policies encouraged for the past half century?

An astute banker once said, "Grow your community and your community will grow your bank." Our community is America and this tax bill will not, at this time, promote America's growth.

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Banks to Experience Tax Hike

By Eugene R. Mason
Vice President/Taxes
First Bank System, Inc.
Minneapolis

THE House and Senate tax-conference committee reported out a bill last month that will increase the tax burden of the banking industry.

Key provisions impacting banks and their customers include the following:

• **Repeal of Deduction for Loan-Loss Reserves.** Under current law, commercial banks take a deduction up to 0.6% of outstanding loans. This deduction is repealed for banks and HCs with assets in excess of $500 million. Recapture of existing reserve balances into taxable income would take place over four years on the following schedule: 10% in 1987, 20% in 1988, 30% in 1989 and 40% in 1990.

According to the conference committee, "troubled institutions" could suspend recapture of existing reserves but would be required to continue recapture when financially sound. Financially troubled institutions are tentatively defined as those whose assets exceed 75% of capital. Repeal provisions are effective for taxable years beginning after December 31, 1986.

Repeal of loan-loss reserves will have a significant impact on the banking industry. It comes at a time when banks are being urged by regulators to increase reserves because of troubled loans. From a tax-policy perspective, it fails to provide an appropriate matching of current losses with cur-

(Continued on next page)

Spread Risk, Be Vigilant *(Continued)*

treme situations.

"Don't put all your eggs in one basket" seems a simple task. However, concentration of risk is not an easy subject to master.

For example, while discussing energy loans recently, a representative of a large bank told me his bank had forecast early the problems in the oil industry. The bank took corrective action to reduce its exposure in this economic area.

However, it did not include in its analysis of concentration the fact that it also had written many personal loans and leases for trailer homes, cars, etc., to workers in those areas. So, it still found itself with workouts and losses.

We are responsible as lenders for reviewing the economic purposes for which debt is incurred and for setting limits on the concentration of risks we are willing to accept. To do this thoroughly we must analyze *all* the potential risks which are created.

We must be prepared to make some difficult, and sometimes unpopular decisions to limit concentrations, no matter how good the climate looks at the time.

If we believe the concentration policies we set in our risk-management policy are valid, we must not be quick to change them, even though changing might mean higher current earnings or less pressure to extend credit.

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rent revenues.

• **Interest on Debt to Purchase or Carry Tax-Exempt Obligations.** Commercial banks would be denied interest deductions that are allowable to tax-exempt obligations acquired after August 7, 1986. An exception is made to governments that reasonably expect to issue no more than $10 million of governmental or Sec. 501(C)(3) obligations during the calendar year.

The bill will discourage future purchases by banks that currently hold about 30% of all tax-exempt obligations. Combined with lower tax rates, these two provisions will place increased pressure on bond yields. The ultimate burden will be borne by taxpayers.

• **Net Operating Losses of Financial Institutions.** Current law permits commercial banks to carry net operating losses back to the preceding 10 years and forward to the succeeding five taxable years. Portions of net operating losses attributable to bad-debt losses continue to be carried back 10 years until 1994. For taxable years beginning after December 31, 1986, losses other than bad debts will be subject to general corporate rules (i.e., three years back and 15 years forward).

Reduction of the carryback provisions from 10 years to three years exacerbates a problem wherein banks are reporting lower income to regulators and shareholders than they report on their federal income-tax returns. This mismatching is reported for financial and regulatory accounting purposes as a prepaid tax. Accounting rules require a direct charge to or against earnings where current year's taxes plus taxes paid in carryback years are less than the reported prepaid amount.

• **Alternative Minimum Tax.** The bill imposes an alternative minimum tax of 20% to a base of regular taxable income plus preferences and payable to the extent it is in excess of the regular tax liability. For years 1987, 1988 and 1989, banking would be affected by a new preference item equal to half the amount by which book income exceeds alternative minimum taxable income. Book income would include tax-exempt income and the deductible part of portfolio dividends received. After 1989, book income would be replaced by earnings and profits.

Banks and HCs with a regular tax liability less than the alternative minimum tax will discover the alternative-tax increase will have the effect of decreasing yields on tax-exempt obligations and portfolio securities.

• **Cash Method of Accounting.** Banks with average gross receipts of $5 million or less may continue to use the cash method of accounting. All others must convert to the accrual method as of January 1, 1987. Any additional income resulting from change must be included in taxable income ratably over a four-year period.

• **IRAs.** The bill eliminates deductions for contributions to IRAs by taxpayers whose adjusted gross income before the IRA deduction exceeds $50,000 ($35,000 for singles) and who are covered by employers' pension plans.

Individuals are permitted to make nondeductible IRA contributions to a separate account to the extent they are ineligible to make deductible contributions.

• **Bank Products.** Deductions for consumer interest will not be permitted beginning January 1, 1987. This provision is phased in over five years: 35% in 1987, 60% in 1988, 80% in 1989, 90% in 1990 and 100% in 1991.

Mortgage-interest deductions are limited to the purchase price plus improvements. An exception is made for borrowings to pay educational and medical expenses.

If this tax bill falls short of its goals, we can look forward to the Tax Reform Act of 1987! • •

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Sept. 14-17: **National Association of Bank Women Annual Convention,** Ceasars Palace, Las Vegas.

Sept. 14-19: **Robert Morris Associates Loan Management Seminar,** Columbus, Oh.

Sept. 21-24: **ABA National Conference on Human Resources,** Fairmont Hotel, San Francisco.

Sept. 21-24: **BMA Annual Convention,** Washington Hilton, Washington, D.C.

Sept. 23-25: **ABA Chief Financial Officers Forum,** Westin Hotel, Washington, D.C.

Sept. 28-Oct. 1: **Robert Morris Associates Fall Conference,** Hyatt Regency Houston.

Oct. 5-8: **Microbanker Expo,** Hyatt Regency at Peachtree Plaza, Atlanta; for information call (717) 848-4782.

Oct. 5-11: **ABA National Compliance School,** University of Oklahoma, Norman.

Oct. 25-29: **ABA Convention,** San Francisco.

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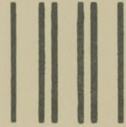

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Boatmen's Vice President Ted Smothers working with Bob Menz, Chairman and President of The First National Bank of Highland. Whatever your correspondent needs, Boatmen's has knowledgeable people to assist you. Call Ted Smothers. He can help.

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