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FEATURES

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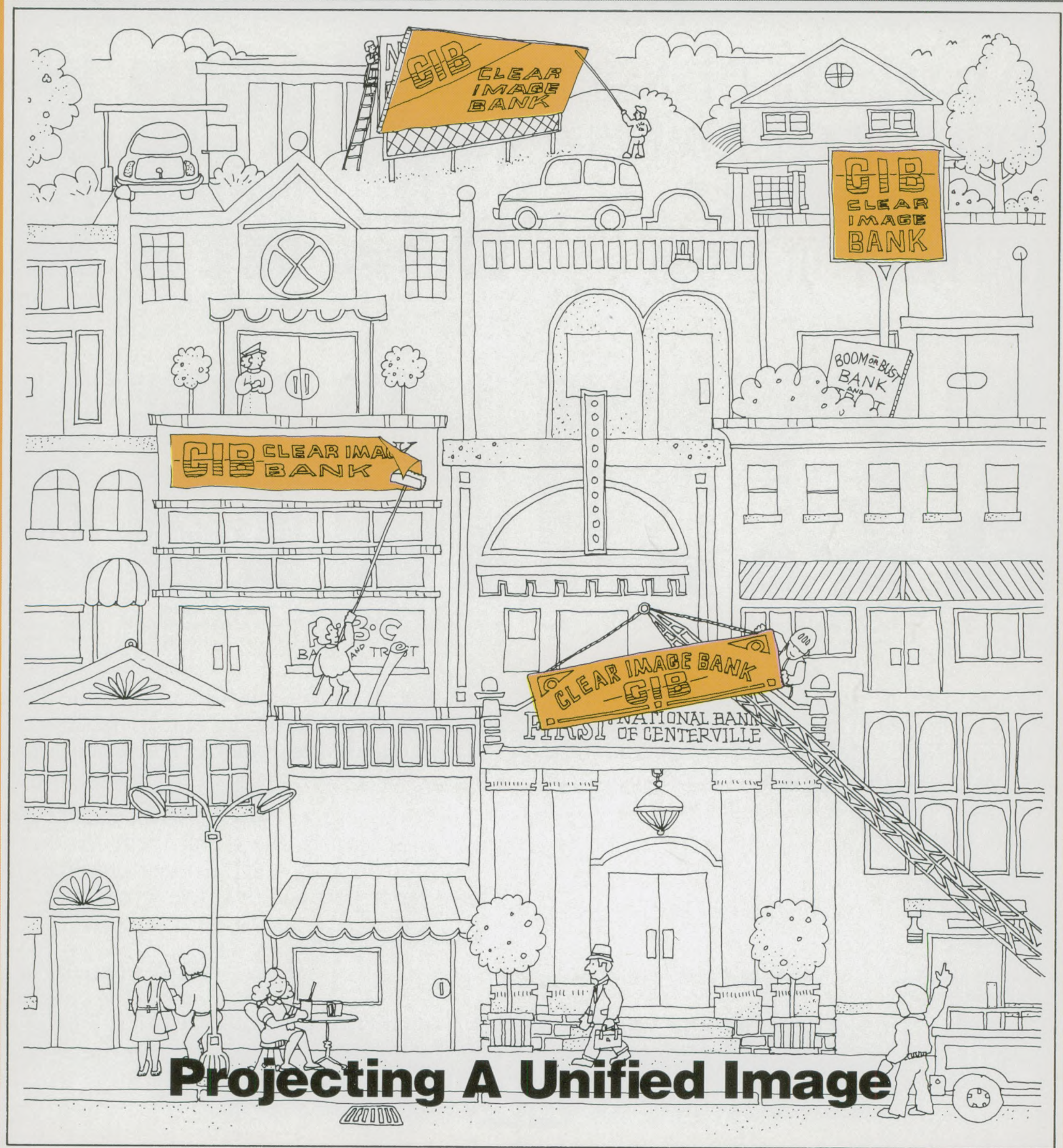
Reopening a Failed Bank

Avoiding Personal Liability

Ag Banking Faces Transition

OCTOBER, 1986



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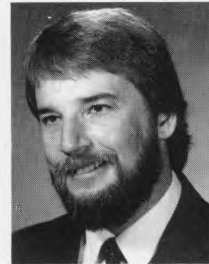

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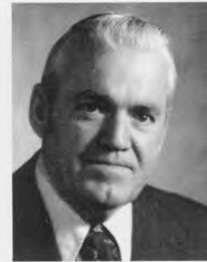

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BANKING WIRE

MID-CONTINENT BANKER

October, 1986

Late-Breaking News From the World of Banking

TAX-REFORM LEGISLATION WILL HAVE A POSITIVE EFFECT OVER THE LONG TERM, but will be mixed for the near-term, says Robert J. DeBenedet of Marquette Capital Management Corp., a subsidiary of Marquette Bank Minneapolis. Results will be a "mixed bag" for consumers, with increased consumption by lower-income individuals and less dependence on tax considerations for investments by higher-income individuals. Corporations that will benefit most are those that have historically paid high marginal tax rates, Mr. DeBenedet says. Losers will be those that have made substantial use of depreciation and investment-tax credits to reduce tax liabilities. Real estate will be especially hard hit. Stock-market volatility will increase and interest rates will lower over time. Investors will seek income rather than capital appreciation, according to Mr. DeBenedet.

NEW-POWERS LEGISLATION FOR BANKS IS OVERDUE, said the ABA's Donald Ogilvie late last month when speaking to directors of Mercantile Bancorp., St. Louis. The U. S. hasn't critically reviewed its banking laws in half a century, Mr. Ogilvie said, yet competition has continued to intensify. Banks are facing increased taxes and other costs of doing business but current law limits the kinds of products and services they can offer and the ways they can structure their businesses. Banks can help get laws changed over the long term by adopting codes of ethics, undergoing outside audits, sharing more information with directors, stepping up efforts to educate consumers and fully disclosing aspects of bank services, according to Mr. Ogilvie, who is ABA executive vice president.

REGULATORS CLEARED OF GRAMM-RUDMAN CUTS BY HOUSE. As this issue went to press, the House passed a bill exempting most federal regulators from spending cuts mandated by the Gramm-Rudman deficit-reduction law. The agencies were exempted because their fees come from financial institutions and thus don't affect the federal budget. The Senate hadn't considered the bill at press time.

CONGRESS CAN PREVENT "SLOW EROSION" OF BANKS' ROLE IN FINANCIAL SERVICES, ABA President Donald T. Senterfitt said in recent testimony on Capitol Hill. Should product/service restrictions on banks remain, he said, an increasing number of banking functions will be performed by nonbanks, which will "undermine the ability of banking laws and regulations to protect the stability of the financial system." The ABA favors HR 5220 as a "prescrip-

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tion for a sound legal framework by which banking organizations can catch up to the financial marketplace," Mr. Senterfitt said. The bill would authorize banks to offer securities, insurance and real-estate products/services currently prohibited. Products include mutual funds, insurance brokerage and real-estate brokerage.

NOT ONLY BANKS, BUT BANKERS, ARE CROSSING STATE LINES. Samuel B. Hayes III has left Bank of Oklahoma, Tulsa, where he was president/chief operating officer, to become president/CEO at Boatmen's National, St. Louis. James R. Bullard has left Hawkeye Bancorp., Des Moines, Ia., to join Hutchinson (Kan.) National as executive vice president/director. He was vice president/counsel to credit administration at Hawkeye.

FAILURE TO HEED CONSUMER COMPLAINTS COULD PROVDE COSTLY TO BANKS if they don't take voluntary action to defuse them, says Borod & Huggins, bank consulting firm. Among the most pressing complaints are failure to inform customers about new rules/procedures concerning new products, failure to reduce charge-card rates, lengthening delays in clearing checks against newly established accounts, increases in service charges and far-ranging spreads of average balances required for free checking. Banks' failure to address these situations is prompting consumers to question banks' commitments to consumers, according to Borod & Huggins.

CHIEF EXECUTIVES APPOINTED AT MID-CONTINENT BANKS. John C. Dean has succeeded James G. Cairns Jr. as chairman/president/CEO, First Interstate, Oklahoma City (formerly First National, Oklahoma City). Mr. Dean formerly was president/CEO, First Interstate Systems, Inc., Los Angeles. Mr. Cairns, current ABA chairman, has joined the Financial Institutions Group within the Hallwood Group as president...Steven G. Elliott has been appointed executive vice president/chief financial officer at First Commerce Corp., New Orleans. He formerly was with Crocker National, San Francisco...Robert E. McNeilly Jr. has been elected president/CEO, First American National, Nashville. He retains his chairman title and succeeds Andrew G. Higgins, new president/chief operating officer, First American Corp....Josh C. Cox Jr. has been elected president/CEO/director at First Guaranty Bank, Hammond, La. He formerly was with a bank in West Virginia...W. E. Ayres now is president/CEO of Simmons First National Bank and Simmons First National Corp., Pine Bluff, Ark....William A. Crumrine Jr. has added the title of CEO to that of president at Texas American Bank/Amarillo...Owen G. "Bob" Shell has been elected president/CEO, Commerce Union Bank, Nashville.

TEXAS INDEPENDENTS REVERSE STAND ON BRANCHING INITIATIVE. An ad hoc group of the Independent Bankers Association of Texas (IBAT) has convinced the IBAT's board to withdraw support for a countywide branching proposal that will appear on the ballot in Texas next month. The IBAT board voted to withhold any resources for the campaign when it learned that nearly 50% of the association's members oppose the initiative.

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MID-CONTINENT BANKER

October, 1986/Volume 82, No. 10

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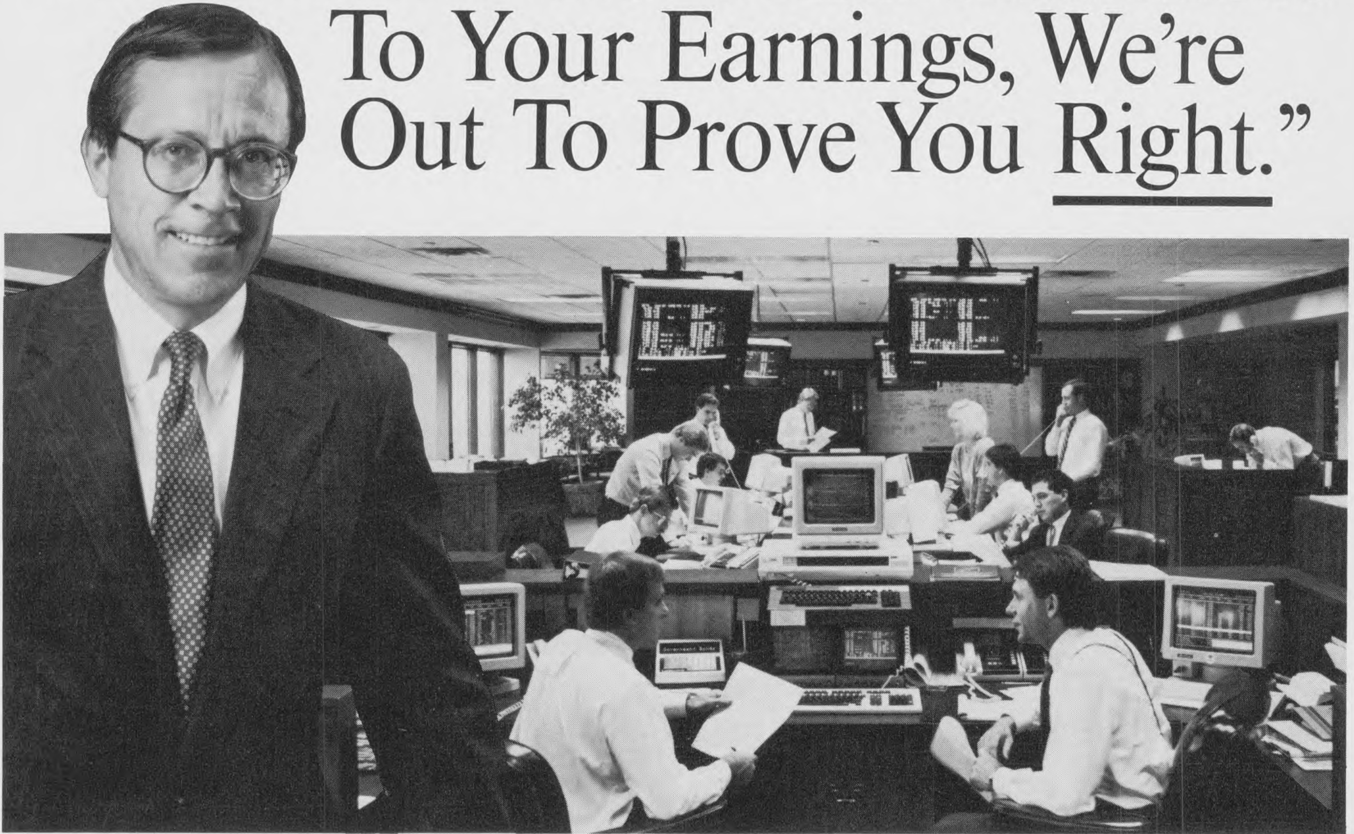

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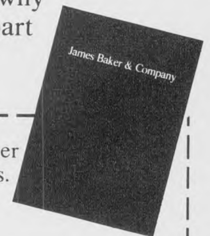

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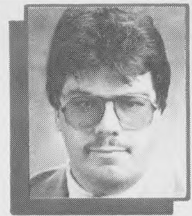

. . . And Then There Were None

LAST month, Central Bank, Tulsa, earned the dubious distinction of becoming the nation's 100th official bank failure in 1986. By year's end, another 60 banks could suffer similar fates.

Nearly 10% of the nation's banks now are on the problem list and almost every day another joins their beleaguered ranks. The percentage growth in nonperforming bank loans in the first quarter of 1986 kept pace with the growth in gross lending, but still rose by an estimated $2.6 billion and, in agriculture- and energy-dependent states, the nonperforming loan problem grew appreciably worse. In Oklahoma, for example, nearly 7% of gross loans are considered nonperforming (versus 6% at the end of 1985), so it should come as no surprise that Oklahoma alone accounts for nearly a third of all bank failures this year, including one of the largest on record, First National, Oklahoma City.

Is this the attrition that advocates of banking-industry deregulation predicted years ago? Poor lending practices coupled with severe economic downturns in certain regions of the country have helped to exacerbate the financial problems banks are experiencing, but deregulation has been a contributing factor. You'll recall that deregulation was supposed to make financial markets more efficient by driving some inefficient producers out of business or at least into mergers with institutions more capable of surviving in a fantastically more competitive market. Consumers would benefit in the form of lower prices and a wider array of financial services.

There's no question that consumers have a wider array of financial options today, but at a considerable price: increased confusion about which products to buy and greater risk. A case could be made that consumers are benefitting from lower prices. Loan interest rates have dropped dramatically; even credit-card rates are under intense downward pressure. But deregulation hardly can be fully credited with that development. Banks also are charging for services they once offered free and are paying lower rates to attract new deposits. As far as most consumers are concerned, financial-industry deregulation thus far has been a mixed bag.

Of course, proponents of deregulation argue that the full benefits of deregulation have yet to accrue to consumers. In other words, "we ain't seen nuthin' yet!"

If that's the case, we have to wonder what the bank failure rate will be once deregulation runs its course. Perhaps banks will adjust to their new environment and the failure rate will stabilize. Being optimists, we tend to think that will be the case, but we have to admit there are times when we despair that the cumulative effects of the government's two-handed policy toward banking and recent shocks to the economic system will combine to make the pessimistic predictions about the future of full-service banking come true.

For the truth is that banking has been only partially deregulated and the remnants of the past are helping to kill those institutions that deserve to be called banks. Regulators long ago decided there is something special about banks, and despite their instincts that the time has come to cut the apron strings, they continue to make banking a special case. If banks' new competitors were accorded the same loving attention, banks would be in no worse shape than their competitors.

But banks are hemmed in by archaic laws that limit the types of businesses they can enter and the prices they can charge. The banking industry had to mount a strong lobbying effort recently to defeat a proposed cap on credit-card interest rates and, under pressure from consumer lobbying groups, accepted a Federal Reserve policy encouraging banks to adopt voluntary efforts to meet the needs of low-income consumers.

A policy requesting voluntary compliance is a better bargain than new legislation, but why isn't someone in government worried about forcing Neiman-Marcus to serve the needs of low-income consumers? Of course, the answer is that banks have a position of public trust and responsibility akin to those of a utility. So maybe banks are special and there's something about them that ought to be preserved.

We have no doubt that if every full-service bank disappeared tomorrow, consumer financial needs still would be met by the growing army of limited-service providers. But would these limited-service institutions match the standards of integrity and occupy the same role in the economy and in their communities that banks have?

No one we know has provided a satisfactory answer to that question. Before the number of failed and failing banks climbs much higher, however, it might be wise to have that answer. Perhaps some attrition is desirable among full-service banks, but just how far do we want to let that process go?

As long as a bank charter continues to be a competitive liability rather than an asset, the process will continue to work toward its logical conclusion, which is something no one seems to want. Government has two choices: It must either allow banks the same competitive freedom afforded competitors or make banking's competitors meet the same regulatory standards banks do. No amount of delay will make that decision any simpler or easier.

— John L. Cleveland
Editor/Associate Publisher

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Making a Clear Statement

What your facility and signs say about your bank's market approach can obfuscate or illuminate the image you wish to cultivate

By John L. Cleveland
Editor/Associate Publisher

HOW DO your customers perceive your bank?

If your bank is typical, your loyal customers probably think of your bank as friendly, safe, prosperous, growing — and perhaps not indistinguishable from any other bank.

These days, it's no longer enough to be typical, however. Banks have to differentiate themselves from their competition, not only from the limited-service newcomers to the financial-services field but from the bank down the street.

The analogy has been made that banking is coming to resemble the retail market, where, not coincidentally, some of banking's more formidable new competition had its start. In the financial-services market of the future, the reasoning goes, only the largest players will be able to be all things to all people in all markets. Everyone else will be a niche player to some degree.

It follows, then, that if your bank is going to be constrained to serving a demographic or geographic market niche, you want to choose a location, an architectural style and an interior decor that says something about the role you've chosen for your bank. First appearances still are important in attracting and retaining customers and many customers form that first impression from the appearance of the facility in which the bank is housed.

In many ways, retailers have a far easier task in differentiating themselves from their competitors than banks do. Walk into almost any type of store and you'll quickly be able to tell what the retailer's primary market orientation is. It might be convenience, discount versus high-end merchandise, senior citizens, yuppies, business people, college students, residents from the local neighborhood or people whose occupations or inclinations keep them out and about late at night.

Whatever the retailer's primary market thrust may be, it is reflected in the location of the store, the interior decor and the selection of merchandise. Banking, on the other hand, is a far less transparent enterprise. Bank facilities are every bit as varied in style and location as retail outlets but form does not always follow market function and there's no visible merchandise to provide clues.

Blending in while standing out is a tricky balancing act that Citizens Banking Co. building in Sandusky, O., manages to make look easy. — *Photo courtesy of HBE Corp.*

If you're going to make a statement with your facility, nothing succeeds — or, in some cases, exceeds — like making it big and bold for all to see. Tony Harbour, managing principal of Gensler & Associates, Houston, an architectural firm with a great deal of experience in banking, says that an impressive or distinctive architectural style still can convey a bank's desire to dominate or become a major player in a given market.

"For example, I'm looking out my window now across the street at (Dallas-based) RepublicBank's Houston main bank which formerly was located on the second floor of a nondescript office building," he says. "You could have driven by and never known a bank was there. With their new facility, RepublicBank wanted to convey the strength of the bank and the fact that they were a major presence in the community and they chose a very distinct and prominent architectural style that did just that."

Not every bank can afford to dominate the local skyline and market, however, so a more subtle statement may be appropriate. In fact, at many desirable locations, integration with the surrounding environment may be the key to standing out from the competition.

"Sometimes the best locations aren't in shopping centers but in residential areas," says Thomas Spalding, marketing director, Bank Building Corp., St. Louis. "You may be able to find a location on a corner somewhere that you can place a facility that enhances and fits into the surrounding neighborhood. Rather than sticking out like a sore thumb, you become a friend to the neighborhood."

Maintaining a sense of being a part of the local community may be one of the most effective marketing tactics available to community banks these days. Despite the alleged fickleness of today's financial-services consumer, most people want to have their financial needs met close to home and deal with people they believe have a stake in the community. A banking facility that seems to say to local residents — assuming that's your target market — "We're a part of you," will generally draw more business than one apparently designed to fit anywhere or that

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A 12,500-square-foot simulation of a branch bank in Michigan demonstrates how banks can differentiate themselves from competitors while retaining the capability to adopt a different market strategy in the future. — *Photo courtesy of Herman Miller, Inc.*

clashes with its surroundings.

Tom Lombardo, director of marketing, HBE Corp., St. Louis, cites as an example the three-story Citizens Banking Co. building in Sandusky, O., where the challenge was to create a new facility that blends in with nearby buildings dating from the 1920s. Designing a building that manages to both blend in yet stand out isn't easy, but it is one way to make a subtle but important architectural statement, he says.

Architectural design also can say something about a financial institution's roots in the community, according to Mr. Lombardo. When a New Orleans thrift relocated from the French Market section of the city to an area of rapid growth, there was a desire to take along some of the ambiance from the past. The new facility was built in a French colonial style with Queen Anne and Georgian furniture throughout the interior.

Bank Building Corp. recently completed a bank facility in Indiana with an exterior hitching rail for the bank's primarily Amish customers who travel to the bank in horse-drawn buggies. When your market is clearly defined, it's easy to incorporate design and functional elements that help make your clientele feel more comfortable doing business with you.

Some banks have attempted to de-

In Business For Business

By Lisa Hoogerwerf
Financial Shares Corp., Chicago

THE MILLIONS of dollars spent annually by financial institutions on advertising and public relations demonstrates management's recognition that a good name and solid reputation are among their bank's or banking group's most vital assets.

Many contend that although promotional materials may create awareness of new products or services as well as reinforcing credibility, word-of-mouth advertising from satisfied customers is what really translates into strong, bottom-line results. This is particularly true of institutions that cater to a specific target market.

With small-to-medium size privately held businesses as its primary market, the $645-million-asset Affiliated Banc Group, Inc., Chicago, is a good example of a multi-bank holding company that has successfully carved out a niche for itself in the commercial market. Affiliated offers an array of products in the lending, money-management and trust-service area while continually maintaining contact with its customers through seminars and newsletters. All products and services reinforce Affiliated's underlying theme: "We're in business for business."

The Affiliated Group, which currently is comprised of five member banks in the Chicago area, began cooperative efforts to attract small business customers about 25 years ago while still maintaining legally separate HCs. In 1983, the group developed a marketing program that recognized all banks as members of the Affiliated Banc Group. When Illinois passed its multi-bank HC law in 1984, Affiliated took the next step of consolidating HCs.

The final step in the consolidation process currently is underway. All member banks are changing their names to reflect their involvement in the Affiliated Group. This step was taken only after a brief questionnaire mailed to individual bank customers indicated that customer acceptance would not be a problem.

The name changes include: Affiliated Banks in Franklin Park, Morton Grove, North Shore and Cicero. First Security Bank of Addison, acquired by the HC last November, already had been renamed Affiliated Bank/DuPage.

The group's advertising campaign highlights the addition of the HC's name to the individual bank names while emphasizing that the size of the combined banking group creates resources for customers that would not otherwise exist. The variety of resources has helped the group to cross-sell products and services while maintaining a local identity in each community served.

With its combined resources, Affiliated also has been able to sponsor informative seminars for customers on such topics as the benefits of micro-computers or the effects of the proposed tax-reform bill on small businesses. Two Affiliated-produced quarterly newsletters, *Financial Forum* and *Business Insights*, address topics of interest to small businesses and are sent to commercial customers along with letters from the president of the local Affiliated bank.

A new Business Development Group, headed by a sales director and staffed by 12 full-time persons, calls on new businesses much the way Affiliated's commercial loan officers do. It also participates in local trade shows and community activities. By emphasizing its commitment to the business customer in every phase of its operation, Affiliated Banc Group has made itself special in the eyes of the key customers it wishes to serve.

When people consider you to be something special, they talk about you and all of that word-of-mouth advertising eventually shows up where it counts — on the bottom line.

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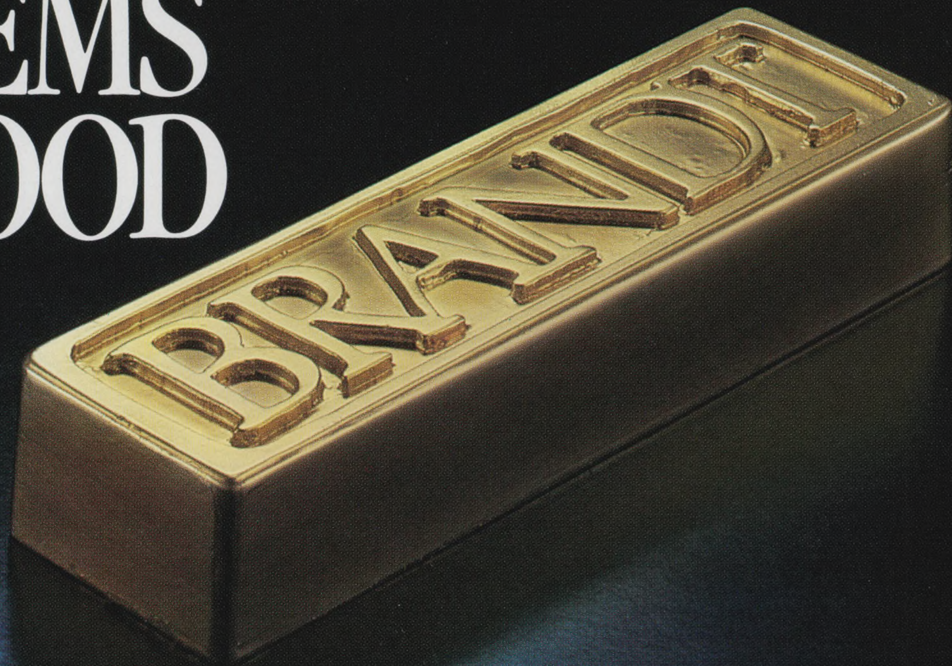

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William C. Nelson
InterFirst Bank
Dallas, Texas

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lineate less clearly defined segments of the general populace as their primary market, however, and it's not always so easy to create an environment that appeals to one market segment without turning off another. In recent years, for example, a number of banks vigorously have pursued upscale customers, in some cases offering special entranceways and sit-down counseling areas with more plush surroundings than the average customer sees. Perks for VIP customers have proved successful in other markets besides finance, but some banks have mistakenly designed their facilities for upscale clients as if all high-balance customers fit the same mold.

Rather than plush carpet and paneled walls, a truck driver, whose income combined with that of a working spouse can be substantial, may prefer to bank in a less pretentious setting, for example. Of course, the major problem with upscale customers is that there just aren't enough of them to go around. Most banks will find it necessary to serve a mixture of high-balance and less well-to-do customers. A facility that makes both groups feel comfortable should be management's paramount objective in such cases.

The elderly represent another demographic group that banks have singled out for special attention. Some banks have set aside areas where elderly customers can get coffee and visit with friends during their visits. Others make available meeting rooms to senior citizens' groups or sponsor seminars on topics of interest to senior citizens.

Whether senior citizens or left-handed Mongolian hairdressers are your primary target market, customers' needs should dictate facility design. If a facility is going to be used for evening meetings by senior citizens, for example, easy, after-hours access to a multi-purpose meeting room should be considered an important part of the design, says Mr. Lombardo.

Young people are less awed by technology and will adapt to ATMs and other gadgets more quickly than will older customers. Business customers generally don't like long waits. Guaranty Bank in Mt. Pleasant, Tex., provided a separate parking lot and drive-up facility for its commercial customers, a convenience many local business people found so helpful, they shifted all their banking relationships there, says Mr. Spalding.

Who can say what innovations in market segmentation the financial-services industry will uncover in the future? In fact, changes in the types of products banks legally can offer that are in consumer demand may dictate sudden changes in market strategy. In today's financial marketplace, it's wise to stay flexible and not make architectural statements you can't inexpensively retract or expand on as conditions warrant.

Last spring, Herman Miller, Inc., a Michigan office-fixture-and-furniture firm, opened a 12,500-square-foot exhibit it calls the Great Lakes Bank & Trust, which incorporates modular-design elements in customer and back-office areas that can be expanded or contracted as needs dictate. Through August, more than 150 banks had sent representatives to tour the exhibit, which is authentic even down to the rubber stamps placed at work stations.

"Bankers tell us the exhibit is so real they would feel comfortable rolling up their sleeves and going to work there," says Judy Leese, market manager, financial institutions.

Originally, Herman Miller had planned to close the exhibit this summer, but now plans to keep it open until the end of the year. Popularity of the exhibit is evidence that deregulation has created a need for greater flexibility in bank design, says Mrs. Leese.

"For the first time, it's starting to make sense to be able to reduce or expand the number of teller lines or add areas for new products as market conditions change," she says. "In a deregulated financial market, time is of the essence and you may not want the expense of having to knock out walls or putting in new permanent marble tile."

Modular fixtures permit a bank to be inexpensively reconfigured over a weekend, says Mrs. Leese. Extensive use of dark mahoghany, rich fabrics and marble ensures that banks won't sacrifice the plush environment their customers may expect.

As banks shift their product mix for maximum competitive advantage, management may have to create a separate section of the lobby for insurance sales, another for real estate and yet another for securities. Some new product innovations will be dismal failures; others will generate more income and require more space than originally planned.

A hitching rail was incorporated into the design for this Odon, Ind., bank. Many of the bank's customers are Amish farmers who drive horses and buggies to town to do their banking. — *Photo courtesy of Bank Building Corp.*

In this chaotic environment, banks may be able to differentiate themselves by the manner in which they keep customer confusion to a minimum. Signs that direct customers to the appropriate section of the bank are only a partial solution, says Mr. Spalding. A reception area in a prominent place in the lobby staffed by someone whose full-time function is to assist customers and help them get to where they need to be can be a tremendous asset, he says.

Many bankers consider a reception area a non-income-producing luxury they'd just as soon avoid. Often, there's no clear indication of who has been designated the bank's information source and it sometimes turns out to be a clerical worker for whom an inquisitive customer is an infringement in a busy day.

(Continued)

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"In some banks, you have to go all the way back into what feels like the inner sanctum before you find someone who can answer a simple question like, 'Where do I go to find the officer who handles such and such?' "

A pleasant receptionist who can direct the customer to the appropriate location and make him/her aware of other services the bank offers may be all it takes to bind that customer to the bank for life. All the best marketing theories and plans may go out the window if the customer doesn't feel comfortable and welcome the first time he/she walks in the bank.

For all of the changes in banking brought about by deregulation, the medium still is the message, even if your media are architecture and interior decor. ● ●

Adopting A Retail Strategy

By Jim Fabian
Senior Editor

DURING the heyday of bank premiums, when banking floors were dotted with displays of cookware, dinnerware and crystal, many bankers deplored the "retail-store" atmosphere of their institutions.

Little did these bankers realize they were seeing a preview of things to come!

Not that displays of kitchen utensils will be the norm in banks — those days seem to be gone forever. But the retail angle is refusing to die. It's the focal point of "new thinking" about bank survival in today's environment.

"Retailing is vital for survival of the banking industry," says Mark Gibson, vice president, Retail Planning Associates, Inc., Columbus, O. Mr. Gibson is a chronicler of innovation in banks and his firm is a consultant to Bank One Corp., widely regarded as one of the nation's most innovative financial institutions.

Formerly with Battelle-Columbus, a midwestern think tank, Mr. Gibson is convinced that financial institutions are not on the right track when it comes to effective selling of products/services.

"There's a vital link missing in their sales efforts," he claims, and its the fact that customers are not getting information about products/services before being asked to purchase them. There's a need, he continues, for customers to be "pre-sold" before they sign up for a service.

To remedy this situation, Mr. Gibson recommends that banks adopt a retail attitude when designing their facilities. For instance, they should provide visual presentations featuring services that customers are likely to be considering, such as IRAs during "IRA season," which is just before income-tax filing time.

Bank floor plans should be arranged to guide customers through the institution, with visuals at vital spots to introduce them to services. How many times have bankers walked past exhibitors' booths at banking conventions to get to the registration desk? The concept is similar to what Mr. Gibson has in mind.

The entrance to the bank and the teller area are the most effective positions for visuals hawking services, Mr. Gibson says. Visuals near the entrance should be general in nature, but those nearest the teller area should be specific. Visuals should be entertaining and attractive as well as providing information about a bank service, he continues.

He admits that its a challenge to make intangibles, such as bank services, tangible to customers. But it can be done through a subliminal approach that suggests how desirable a product/service can be. Customers find it easy to grasp visuals, Mr. Gibson says.

Bank One is in the forefront of this approach, says Gary Kaiser, an associate of Mr. Gibson, who is vice president/design director for Retail Planning Associates.

"This bank is creating an environment that will sell services," he says. It's using what could be termed a "boutique" arrangement, one that surrounds the banking floor with specialty shops offering related services that may not be legal for banks to offer on their own.

This concept isn't brand new — as witness Sears financial centers — but it's one that most banks haven't embraced. Bank One is on the leading edge, Mr. Kaiser says, and his firm is designing a "financial center" for Bank One that can best be described as something between a department store and Epcot Center. Messrs. Kaiser and Gibson won't comment further on this project, as specifics are proprietary information at this time.

"We're trying to change banking's conservative appearance," Mr. Kaiser says, "so the business operation can be expanded." He adds that contemporary decor is the trend of today, a fact that is underscored by the appearance of the newer malls.

Bank One's Upper Arlington Branch, which has been the showcase of the bank's innovative efforts, is about as "mod" as any commercial bank in the nation. Its doorway features an arched canopy that makes the bank look like a tony retail shop on Rodeo Drive in Beverly Hills. The facility features "boutiques" housing tax preparers, financial consultants and attorneys. A travel agency and brokerage service also are on the premises.

What about results? Deposits have risen more than 15% since the branch was opened last November, the travel agency averages 50 customers a week and "dozens" of customers have been retained because of brokerage-service availability, according to John F. Fisher, senior vice president.

Other banks climbing on the retail bandwagon include Huntington National, Columbus, which is incorporating a Sears-like marketing strategy that uses retail display and marketing techniques to direct products/services at customers needing them. This approach is an attempt to turn the 95% of customers using the bank for traditional services into customers taking on extra services — in other words, to make buyers out of them each time they enter the bank to make a deposit or cash a check.

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has announced its intention to affiliate with
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Case Study

Solving the image problems of buying and reopening a failed bank

By Thomas G. Ramey and M. Scott Lawyer

MONDAY, April 7, 1986

4:07 p.m., Alexandria, La. The call comes. Henry Kinberger, president, Security First National Bank of Alexandria and a former president of the Louisiana Bankers Association, receives a telephone call from the FDIC: "A $40-million bank in a northern Louisiana market will be closed this Thursday. We would like to give Security First National the opportunity to bid."

4:35 p.m. Mr. Kinberger calls M. Scott Lawyer, president, Lawyer & Associates, Inc., Jackson, Miss., a firm which specializes in the acquisition of problem banks.

Messers. Kinberger and Lawyer speculate that the institution is First National, Ruston. Both agree that this college town located between Monroe and Shreveport would be an ideal market for Security First National to enter. Mr. Kinberger decides that he will, indeed, be a bidder. He retains the Lawyer organization to represent his bank.

5:10 p.m. Mr. Lawyer, a former regional counsel of the FDIC, calls a meeting of his staff, which includes former bank presidents, bank auditors and attorneys. Among those gathered in the conference room is Thomas Ramey, president, Ramey & Associates, an organization specializing in bank marketing.

Mr. Lawyer outlines the scenario to his assembled team. Each member of the team knows what his individual mission will be for the coming week.

Tuesday, April 8, 1986

Mr. Kinberger presides over a meeting of his board of directors, where he announces the FDIC's invitation to bid on what he believes to be FNB Ruston; the enlistment of Lawyer & Associates; and the need for extreme secrecy.

Lawyer & Associates begins peer-group analyses of banks of this size operating in the region and begins preparing the array of documentation needed in the acquisition of a failed institution.

Wednesday, April 9, 1986

Teams from Lawyer & Associates and Security First National fly to New Orleans, the FDIC's designated office to receive bids.

Mr. Ramey is president, Ramey & Associates, and Mr. Lawyer is president, Lawyer & Associates, both in Jackson, Miss.

Bid packages are circulated to interested parties. About 20 institutions appear to be potential bidders.

6 p.m., New Orleans. The Security First National team assembles in a working suite at the hotel headquarters with all bidding materials and other data necessary for the decision.

The team considers such questions as whether the bank should be a newly chartered institution under the existing holding company, or be operated as a branch of Security First National in Ruston.

Financing of the new bank is discussed.

Meanwhile, Messers. Kinberger and Ramey huddle to discuss the initial marketing of the new institution. Mr. Ramey argues for heavy initial advertising to reassure the people of Ruston that their money is safe and that all banking services will be continued.

The FDIC plans to close the bank Thursday. If Security First National is the winning bidder, the bank will reopen as a branch of Security First National Friday morning.

"All precautions must be taken to avoid any type of run on the new bank early Friday morning. As the newspaper will not be out until Friday afternoon, our only option is immediate heavy radio advertising," Mr. Ramey says. Mr. Kinberger concurs.

8:30 p.m. Mr. Ramey phones his staff, on standby in Jackson, and relays the information necessary for them to begin producing the newspaper and radio advertisements. He outlines the budget agreed on by him and Mr. Kinberger.

Later, Mr. Kinberger, Mr. Lawyer and their staffs work into the night preparing the necessary applications for the OCC and develop dozens of scenarios to determine payback periods under various bids.

Thursday, April 10, 1986

8 a.m., New Orleans. While the bid team prepares the agenda for a 16-hour day, Mr. Ramey is meeting with his staff to approve the concepts prepared during the previous night by his creative staff.

The concepts are valid and the media is scheduled. Everything is ready.

2:30 p.m. The bid team presents its case in a pre-bid meeting with the state banking department, the OCC, the Fed and the FDIC.

In the course of the meeting, the Security First National team is asked if it is prepared to open the bank the next morning. On cue, Mr. Ramey presents finished copies of the newspaper ads and the script for the radio spots, which are being produced in Jackson at that moment.

He also distributes a prepared press release and outlines the plans for removing the former First National Bank of Ruston signage and replacing it with temporary canvas signs that are being painted.

5 p.m. At the close of business in Ruston, OCC and FDIC officials move in and seize First National Bank. The bank now is the property of the FDIC and can be put up for bids and awarded to the winning bidder. Regulatory of-

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ficials standing by in New Orleans are notified and the process begins. The bidders are notified that the bank has been closed.

5:15 p.m. The bids are presented. There are six contenders besides Security First National.

6 p.m. The assistant regional director of the FDIC steps from the room. "Security First National is awarded the bid."

After a telephone call from New Orleans, Lawyer & Associates' staff, waiting across the street from the failed bank in Ruston, is allowed into the bank. Staff members establish a working relationship with members of the FDIC liquidation team and officers and employees of the failed bank.

6:12 p.m. Time is now of the essence for Mr. Ramey and his organization. Because of the secrecy of a bank failure, the advertising agency could not tell the local radio stations the name of the advertiser for whom they were buying the radio time. The agency could not send the radio dubs to the stations, because the dubs were commercials assuring depositors of the former First National Bank of Ruston that their money was safe.

If the commercials had been distributed to the stations prior to the FDIC closing of the bank, a run could have started.

Mr. Ramey's organization immediately begins telephoning the radio stations with which they have reserved time. The stations are instructed to have a representative at their local airports at a designated time. The stations would have the commercials in hand within the hour.

7:35 p.m. Mr. Ramey's plane lands in Ruston. The local radio station representative meets the plane and takes Mr. Ramey and his staff to the bank. The plane continues on to Monroe and Shreveport to distribute the remaining radio dubs.

7:45 p.m. Mr. Ramey and company arrive at the bank and are greeted by members of the Lawyer & Associates group, already in place.

Armed guards are stationed at the locked doors. Inside, FDIC personnel are everywhere. Files are being moved and examined; cash is counted.

7:55 p.m. William Hankins, executive vice president of Lawyer & Associates, calls a meeting of bank employees. He describes Security First National's philosophies and notes that Mr. Kinberger, president, and Larry Acosta, senior vice president of Security First National, are en route from New Orleans.

Mr. Ramey is introduced to employees and he explains the need for employees to present a positive attitude in the morning to reinforce what is being told to the public on the local radio stations.

8:10 p.m. Mr. Ramey hires a local electrical contractor to begin removing the former First National Bank of Ruston signage at both locations.

Bank calendars are removed from the walls. Ashtrays, pens, pencils, anything with "FNB Ruston" on it, are removed from the bank. The former bank no longer exists and there is no reminder of the past. Local conversation will be more than enough to remind the town of the bank failure.

Meanwhile, Mr. Kinberger enters his new branch and reassures the fearful staff. "You have a job. We do not intend to come in and make widespread changes until we have had time to fully analyze the situation. Welcome to the Security First National family."

Friday, April 11, 1986

9 a.m., Ruston. Security First National opens for its first day of business in Rouston, and what a day it is! Greeting the customers are smiling employees, sporting boutonnieres or corsages, offering cake, cookies and coffee. Copies of the newspaper ads are mounted and displayed prominently in bank lobbies.

Mr. Ramey returns from Jackson and brings business cards for the bank officers and name tags for all bank employees.

As the day progresses, the Lawyer & Associates staff works in tandem with the FDIC to facilitate the smooth transition in operations.

6 p.m. Security First National Bank concludes its first full day of business in Ruston. Public anxiety has been overcome. Bank employees and FDIC personnel are amazed at the smoothness of the transition. Everyone is relieved that the bank does not normally open on Saturday. Former employees of the failed bank, members of Security First National's staff and the Lawyer & Associates team have worked side by side and implemented the plan conceived only 48 hours ago.

All in all, it has been a good, if hectic, work week. ● ●

Tax Bill's Effect on Tax-Exempts

By Rachel Balbach
Vice President/Economist
Centerre Bank
St. Louis

AMONG the most interesting issues of the Tax Bill is the effect it will have, both directly and indirectly, on the market for tax-exempts.

The most direct impact on banks comes from the loss of deductibility of the interest cost on funds borrowed to carry tax-exempts bought after the effective date of the provision. The immediate result is a loss of liquidity in banks' existing portfolios, as the market value of the securities will be smaller than the value of holding them with the advantage of the deduction.

As for new issues, the apparent retention of current deductibility rules for the securities of state and local entities that limit their debt issues to $10 million or less annually will very likely give rise to a two-tier market, with the debt of these smaller issuers commanding higher prices relative to that of larger. Nevertheless, they won't escape the narrowing of the interest-rate differential that must result from lower corporate tax rates.

Lower individual tax rates, as well as the stiffer alternative minimum tax, also will lower individuals' demand for tax-exempts. This reduction in demand will be partially offset in many states by their increased attractiveness as shelters from state income taxes for residents of states that exempt interest on their own obligations.

This surely will occur in states that base tax calculation on federal returns and whose residents therefore face significantly higher tax liabilities due to base broadening. Also working in this direction is the likelihood that states will shift to a greater dependence on income taxes, which retain their deductibility under the proposed tax bill, from sales taxes, which do not.

The loss to larger banks of the deductibility of additions to the loan-loss reserve generally is considered to be potentially the most costly of the new provisions, although most bankers seem to have concluded that its immediate financial impact is lessened by current levels of problem loans.

In time the cost will be greater, but it's not at all clear that credit policies will be materially changed, as has been suggested in some quarters. ● ●

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ATMs:

Some New Placements, But Mostly Replacements

By Joe Lawler
Assistant Editor

SALES OF ATMs continue flat as bankers continue to join networks and seek to better market their existing ATMs. However, some observers see a trend toward placing new ATMs in drive-up lanes and in some off-site locations, such as malls and plants.

At least for now, however, most ATM manufacturers continue to rely on the replacement market — bankers replacing aging ATMs — for the major share of their ATM sales.

These conclusions come from conversations with several major manufacturers of ATMs.

Original ATMs Aging

"Ten years ago, ATMs were installed in quantity," says Donald F. Bartoo, director of corporate communications at Diebold, Inc., North Canton, O.

"The write-off period was five to seven years. So now banks are looking at replacement," he says.

"It has become economically feasible to consider replacement because of the lower maintenance costs of new ATMs, the marketing capabilities and the lower cost of operations," Mr. Bartoo says.

"Most of our business is coming from replacement. This means full-configured, through-the-wall ATMs at the branch," says Robert Jansen, president of Omron Financial Systems, Inc., Las Colinas, Tex.

Total sales of ATMs are running about 8,000 to 10,000 a year, with a little more than half those going for replacement, according to manufacturers.

"The replacement market will be the major part of our business over the next five years," agrees Serge Prizant, marketing manager in the Financial Systems Group of LeFebure, Cedar Rapids, Ia.

"A good chunk of the existing machines are more than five years old," Mr. Prizant says. Maintenance costs are spurring bankers to replace them, he adds. He expects sales of ATMs for replacement to be 50% greater than sales of ATMs for new placements.

> Some bankers are replacing pneumatic systems with ATMs in drive-up islands, manufacturers say.

New Location: Drive-Ups

Several ATM manufacturers see a trend developing of placing ATMs in drive-up lanes.

"We see our drive-up ATM as being a very strong item," says Mr. Prizant of LeFebure.

The trend is strongest in the Midwest and Southeast, but weak in the West, where real estate often is too expensive to devote to drive-up lanes.

LeFebure recently introduced a new line of drive-up ATMs, Mr. Prizant adds. "We predict that this will be 50% of our total volume by mid-1987."

NCR also recently introduced a new line of drive-up ATMs. The company added the line when it saw the trend developing, says Dick J. Mazzarella, assistant vice president, ATM marketing division at NCR Corp., Dayton, O.

"In 1982, drive-up ATMs represented 8% of our through-the-wall business," he says. "In 1985, 35% of our through-the-wall business was for drive-up ATMs."

Two out of five new products introduced by Diebold last fall were drive-up ATMs.

"People already like drive-up banking," says Mr. Bartoo of Diebold. "The ATM adds another level of convenience." People also like the safety of staying in the car, he says.

The ATM industry sees great potential in this trend, "when you consider that there are 50,000 to 60,000 drive-up lanes in the country that use pneumatic air tubes," says Mr. Bartoo.

So far, the typical scenario is a bank adding a drive-up lane and deciding to use an ATM in the new lane, says Mr. Prizant.

Banks justify the drive-up ATM on the basis of its 24-hour service and the reduction in human teller costs, he says.

A leading consultant on marketing ATMs to consumers, Catherine L. Bond, encourages her clients to put ATMs in drive-up lanes. She is president of a company that bears her name in Hartfort, Conn.

"In my mind, the drive-up is the ultimate convenience," she says. Banks

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that put an ATM on the outermost lane often find they can get by with one less human teller, she says.

"This might lead to the question, 'Why haven't drive-up ATMs caught on sooner?' Some bankers have been put off by the logistical problems — the hassles of demonstrating the ATM; left-handed drivers might have trouble using it; the 'footprint' of the ATM has been too big for the pneumatic space," Ms. Bond says.

"But the hardware is getting better. And some bankers are widening the island to fit the ATM."

Robert Zellan has attempted to help solve this problem. A builder of traditional ATM shelters, Mr. Zellan, president of Doane & Williams, Chicopee, Mass., was asked to help fit ATMs onto islands. "The banks came to us and said, 'Hey, we have this problem.' " After designing drive-up cabinets for ATMs, "Now we go to the banks," he says.

"Drive-ups and kiosks are coming on strong. In '85 and '86 we've used a lot more drive-ups. This is the next least costly installation after the supermarket," he says.

Off-Premise ATMs

The top-volume locations for off-premise ATMs still are supermarkets and convenience stores, manufacturers say.

For example, retail placements, mostly in supermarkets and convenience stores, represent 70% of the neutral-site sales at NCR. Corporate placements in offices, plants, hospitals, etc., represent the other 30%, according to Mr. Mazzarella.

The latter trend is gaining steam, manufacturers say. More banks are placing an ATM in a company's office or plant, sometimes in conjunction with direct deposit of payroll, as the key to a relationship with the company.

With such an arrangement, the company's employees can avoid the necessity of going to the bank. "On payday, employees aren't likely to go out at lunchtime, get caught in the long lines and come back to work late," says Mr. Bartoo of Diebold.

Retail placements, mostly in supermarkets and convenience stores, represent 70% of the neutral-site sales at NCR. Corporate placements in offices, plants, hospitals, etc., represent the other 30%.

"We are a convenience-driven society," says Mr. Mazzarella of NCR. "We are starting to see more strategic, convenient placement of ATMs."

Bank Lobby Placements

"We think there is going to be an increasing trend to lobby automation," says Mr. Bartoo of Diebold. The reason is that the role of ATMs has shifted, he adds.

"The original strategy with ATMs was to increase market share by placing them off-premises. Placing them in the lobby was not top-priority because they would not help increase market share there. You weren't likely to find your competitor's customers walking through your lobby.

"But now the cost of providing transactions through automation is less than providing them through human tellers. So we believe there will be an increased interest in lobby automation," he says.

Marketing Still Needed

Even with some possible new trends such as these developing, many observers believe ATMs will not gain wide acceptance with the public until banks learn to market them better.

"Why do we have a 33% wall?" asks Mr. Prizant, referring to the common belief that only one-third of a bank's customers will use ATMs. "Because much of the population is not computer-comfortable."

While ATM manufacturers put the responsibility for marketing ATMs on bankers, they also feel they are doing their bit by building more "user-friendly" ATMs.

The new generation of ATMs has a variety of features and options — "friendly" color graphics, audio messages for instruction or marketing, touch screens and, in some cases, interim-statement capability.

"Color graphics have become extremely important to attract and assist customers in using the ATM," says Mike Morache, vice president of marketing and product management at Fujitsu Systems of America, Inc., San Diego. "It seems that for every ATM we sell now, the bank is ordering color graphics."

Future Is Hazy

ATM manufacturers hope they see signs of new markets in ideas such as drive-up ATMs, bank-at-work and other off-premise ATM placements. Yet some manufacturers admit they may have to rely on building ATMs mostly for the replacement market — perhaps until a new generation that grew up on video games and personal computers begins using ATMs. • •

• **Ryan, Beck & Co./Southwest** has opened an office in Dallas that will provide underwriting, market making and consulting services for southwestern regional banks and thrifts. J. David Stanford serves as president.

• **Dana H. Cook** has been selected to serve as special adviser to the Comptroller of the Currency. He is a partner in the Houston office of Peat, Marwick, Mitchell & Co.

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Downtown Kansas City Celebrates As Commerce, United Mo. Open Hqs.

TWO RIBBON-cutting ceremonies in downtown Kansas City within a four-month period testify to the progressive images of two of Missouri's leading banks.

In August, a ribbon-cutting ceremony was held to open the new headquarters of Commerce Bancshares and Commerce Bank of Kansas City.

In November, another ceremony will be held to officially open the new corporate headquarters of United Missouri Bancshares and United Missouri Bank of Kansas City.

The August event featured pealing chimes, ringing bells and the release of balloons. About 200 invited guests attended from government, business and media sectors of the Kansas City area.

The new building is the fourth downtown structure built by Commerce this century. The other three are the Commerce Trust Building, erected in 1906, the Commerce Tower, built in 1965 and the Executive Plaza Office Building, opened in 1974.

The new Commerce Bank Building rises 19 stories above the block between Walnut and Main on Tenth Street. The 477,000-square-foot building features an exterior of polished granite and clear glass at the base, with a granite skin and bronze reflective glass on upper floors.

The structure features business and retail tenants, an enclosed skywalk connecting it with the Commerce Tower and Commerce Trust buildings and a public art gallery featuring the Commerce art collection. A new connected 650-car garage is part of the development.

United Missouri's building is bordered by Grand Ave., Eleventh and Walnut streets. It consists of five stories above street level along Grand Ave. and three stories above street level along Walnut.

Future plans call for increasing the building's height to 25 stories.

The 255,800-square-foot structure will house most bank functions, with support and operational functions remaining in the bank's adjacent structure. It features imported, polished red granite and reflective solar glass, granite finish in interior lobbies and a landscaped courtyard. A two-level, below-grade garage accommodates more than 300 cars.

Some departments have moved into the new building and others will be moving throughout the balance of this year.

Official opening ceremonies are set for November 22. ● ●

Missouri Transitions

Carlos E. Uribe has been elected vice president at Centerre Bank, St. Louis. He joined the bank in 1981.

Stephen A. Mace has been appointed trust officer in the trust new business section at Boatmen's National, St. Louis. He is new to the bank.

Mercantile Bank, St. Louis, has named Jerry S. Goldstein head of the private banking division. He formerly was senior vice president, Mercantile Bancorp. John Q. Vye has been named senior vice president of the HC to head a restructured planning/marketing department.

Dedicating new Commerce Bank Building in August were (from l.): David Rismiller, bank ch.; Jonathan Kemper, bank pres; KC Mayor Richard Berkley; James Kemper Jr., ch., Commerce Bancshares; Rev. Earl Cavanaugh and Rabbi Michael Zedek.

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Avoiding Personal Liability Vital for Bank Survival

"Look before you leap" still is practical advice, but many bankers and directors aren't taking it

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. • •

Right People in the Right Jobs

By Robert Vecchiotti
President
Organizational Consulting Services, Inc.
St. Louis

HAS liability protection been an excuse to take the low road and do less than required to meet new challenges or has it been an excuse to shift blame for fouling up elsewhere?

Tradition and habit were comforting until bank closings began to rise at a dramatic pace. Bank closings for 1986 could total 145 — nearly three per week.

What did the managements at these failed banks do to jeopardize peoples' savings and trust? Executive accountability may have fallen short of what was required to meet the demands of a competitive financial-services industry and a sophisticated customer.

The measure of success in banking is market share with a good return on equity. The competitive edge will go to banks that are willing to downsize and restructure with the right people in the right positions.

Bank executives can encourage greater responsibility for actions with less liability protection by selecting or developing people who have clear vision, are good self-managers, are not adverse to taking risks, can think beyond the edge of the balance sheet, can tolerate and make clear ambiguous situations and can maintain the excitement of seeing new opportunities each day.

Selecting the right people for the right positions may mean going outside the banking industry to find talent in marketing, cash-flow management, strategic planning, human-resource development, financial planning and business consulting.

The use of task forces helps distribute accountability to more people. Task forces can bring diverse views together to focus on key issues such as loan criteria, loan/loss ratios, cost control and marketing. A sense of urgency and a sense that individuals can make a difference by immersing themselves in work and problem areas helps boost creativity. The attitude that it's OK to make mistakes as long as the lessons learned are clear and shared with the team can be encouraged.

It all boils down to the realization that bankers lead the informed, not the uninformed. Banks that trust their people, allow them the freedom to choose how to meet business objectives and provide feedback on results will do well. • •

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Iowa BA Centennial Convention Features Cake, Bubbly, Balloons

ABA presents preliminary suggestions of ag study during ag breakfast

By Jim Fabian
Senior Editor

BANKERS and their spouses attending last month's annual convention of the Iowa Bankers Association feasted their eyes on what may well be the largest cake they have ever seen during ceremonies honoring the IBA's centennial.

The two-layer creation was more than ample in size to feed those in attendance. But many were so occupied waving small U. S. flags and blowing horns typical of New Year's Eve parties that the cake and accompanying champagne almost became secondary in importance.

Would that Iowa banking were as pleasant as the IBA's centennial observation! During the convention, one speaker stated that he thought the ag crisis was bottoming out. The next morning, the front page of the Des Moines *Register* proclaimed that Iowa banks were facing better times. Bankers shook their heads in disbelief when they saw the headline, commenting that the reporter who wrote it was overly optimistic.

It was difficult to get any banker in attendance to predict when things will return to normal — which most consider to be the 1970s. However, one speaker frankly told his audience that the 1970 decade was an aberration, not normalcy. He implied that today's situation is likely to become the norm — at least, for the forseeable future.

As usual, the most valuable portions of the convention were the special-interest sessions. On the first day of these sessions, a regulator taking part in a panel titled "Meet Your Regulator" commented that banks facing regulatory action too often engage an attorney to go to bat for them and often the situation becomes one of confrontation rather than civilized discussion.

IBA officers blow out candles on huge centennial cake during convention break. From l: L. Fred Hagemann, treas.; Neil Milner (hidden), e.v.p.; J. Bruce Meriwether, outgoing pres.; R. Russell Howard, new IBA pres.

As if planned, an illustration of what he said took place during the next day's sessions, when an attorney presented a workshop titled "How to Control Your Regulator." The attorney told how she had assisted banks that were having regulator trouble and that she often had made regulators "blink" when she challenged some of their actions!

The Iowa convention was chosen by the ABA as the launching pad for presentation of initial information from "Transition in Agriculture: A Strategic Assessment of Agriculture and Banking," the study authorized by the ABA last year.

Only preliminary statements could be made at the convention and they were made by an impressive duo — the past and present chairmen of the ABA's agricultural banking division: Alan R. Tubbs, president, First Central State, DeWitt, Ia., and Mike Fitch, vice president, Wells Fargo Bank, San Francisco.

Key portions of the report indicate that the ag crisis will deepen without new policies and practices. In order to survive, farmers must better utilize technology and strengthen the business management of farming operations, according to the study.

Mr. Fitch said the ABA study "offers the tools needed for development of sound long-term planning, policies and procedures consistent with the new realities for the agricultural and ag-banking industries." He added that the project's planning guide will enable individual banks to adopt specific strategies consistent with their unique situations and needs.

He said the report points out that ag banking must form new coalitions to control its own destiny by becoming pro-active in the political process on behalf of farm customers as well as itself.

He said the study shows that the demise of the small independent bank is not a certainty and that securitization in the form of a secondary market for farm real-estate loans is necessary.

Mr. Tubbs said the study suggests that macro-economic policies — fiscal and Fed monetary policy — are more important in determining the long-range economic environment for agriculture than is agricultural policy.

He sees a situation in which farms become big businesses to be serviced by regional and even money-market banks. Small farms will continue, but will be part-time operations and will be serviced primarily by small banks.

He termed the study a "road map" that will be helpful in adopting legislative strategies and providing assistance to Congress. It also should help every bank understand the fundamental structural changes occurring today and help them assess their changing market and adopt competitive strategies for the future.

The IBA reinstated its traditional ag breakfast at this year's convention. Messrs. Tubbs and Fitch spoke at that event. Iowa was selected as the location to introduce the ABA study's preliminary results because of the importance of agriculture to the state's economy.

Special "moments in history" presentations were made during the convention, during which students from nearby educational institutions presented historical anecdotes about the history of the IBA. ● ●

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ABA Banking Advisors Tour Nation To Enlighten Consumers, Media

Interest in banking, personal finance is high; few instances of antagonism noted by four Mid-Continent-area banking ambassadors

By Jim Fabian
Senior Editor

ONE OF the first conclusions an ABA banking advisor comes to after meeting with media representatives and the consuming public is how eager these people are for knowledge about the banking industry.

A second conclusion is that precious little knowledge of banking and the changes it is experiencing because of deregulation is being disseminated to the general public.

"Bank customers are confused by recent changes in the financial-services industry and it's our job to inform people how those changes affect them and how they can benefit from them," says Lynn L. Anderson, president/CEO, First National, Lawrence, Kan. Mr. Anderson is one of 16 banking advisors circulating throughout the nation under sponsorship of the ABA and one of four interviewed for this article.

The importance of the advisor program is emphasized by J. Douglas Adamson, senior vice president, Bank One Lafayette, Ind.: "We are financial advisors and problem solvers, and it's important that our customers know they can come to us for solutions to their financial puzzles."

Mr. Adamson discussed banking issues with the public in four major population centers over the past year — Charlotte, N.C., Atlanta, Boston and Tulsa.

"If banks are to continue as a major force in the American financial system, they must remain competitive by offering a diversified array of financial services. Our customers have indicated they are interested in satisfying their financial needs at one source, and commercial banks want to be that source." This is one of the conclusions Emma Lou Brent, executive vice president/CEO, Phelps County Bank, Rolla, Mo., drew from talks with consumers in Indiana, Pennsylvania and Louisiana during the year.

James A. White, executive vice president, First National, Tulsa, told consumers in Detroit and Scranton, Pa., that "Bankers are responsible, concerned citizens and provide important services to their communities and customers. Given the freedom to offer additional services, banks would be able to offer customers the ability to obtain most of their financial needs at one place and at lower cost."

Banking advisors at briefing session at ABA headquarters. From l.: Lynn Anderson, pres./CEO, First Nat'l, Lawrence, Kan.; Jim White, e.v.p., First Nat'l, Tulsa; Phil Corwin, ABA government relations.

All four advisors are committed to the program for another year and are sold on the benefits such a program offers, both for the public and bankers.

"I like the program because it enables me to make a contribution to the banking industry and be benefitted personally," says Mr. White. Due to the extensive interaction he has had with representatives of the media over the past year, he feels he can do a better job working with local media contacts.

He lauds the banking-advisor program as good for the industry. "The banking industry needs a program in which it presents itself in a positive manner," he says, "one that features bankers willing to talk about industry problems in the context of consumer interests."

He found on some occasions that he was more eager to tell banking's story than some media representatives were to listen to it; but, generally, media people expressed a genuine interest in what he had to say.

At each stop, local media representatives are briefed about issues affecting the financial-services industry. When an advisor appears on a local TV show or is interviewed by a reporter, he is expected to respond to questions they pose.

Mr. White found the issue of bank safety and soundness to be of great interest to media representatives. He happened to be in Detroit on the very day the Michigan reciprocal banking bill landed on the governor's desk for signing. He was ready for media questions on the topic because he had met with local bankers to become familiar with the Michigan banking situation. He also had gone through an extensive training program at ABA headquarters prior to his travels. This training includes mock interviews and includes "baptisms by fire" by actors pretending to be antagonistic reporters.

While most advisors report they had few antagonistic interviews, Mr. Adamson participated in a call-in show in Boston where the host was critical of both the banking industry and Mr. Adamson as a banker. Mr. Adamson soon learned that Bostonians are concerned with consumer issues, such as life-line banking. The situation provided him with an excellent opportunity to tell the public about the banking industry's desire for additional powers so it

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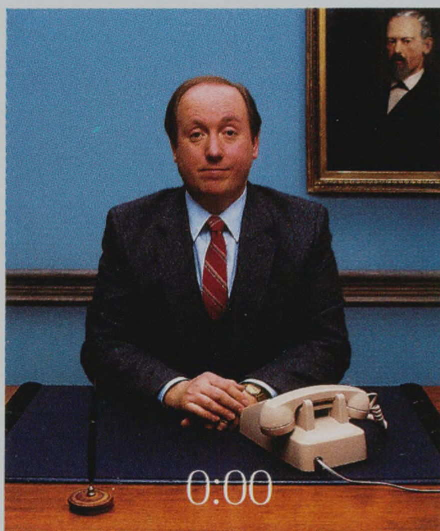

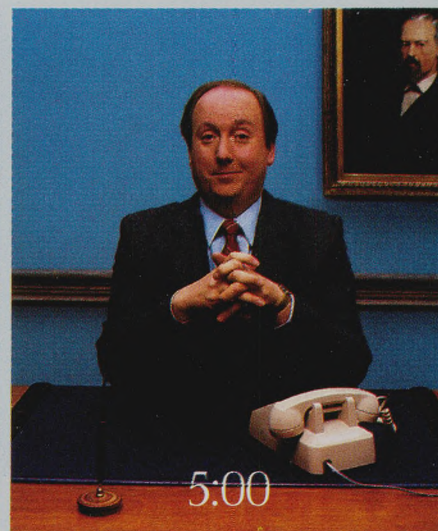

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can offer the new services the public wants. He has a tape of the show and has been told that he did a good job projecting the industry in a good light.

"But they didn't buy all of it," he admits.

Ms. Brent was faced with a somewhat similar situation in Louisiana, where she appeared on a program aired on a minority-owned radio station. She sensed a defensive attitude from both the interviewer and those who called in with questions.

Being banking advisors enables us to understand the media better and do a better job in getting our message out.
—J. Douglas Adamson

"I gave them information they could use when seeking help when presenting loan requests to banks," she says. "I told them where to go to get assistance, such as university extension centers or regional planning commissions." She knew she had made progress when one of the callers told her that she had "made his day."

The current group of banking advisors started out a year ago stressing the fact that banks are offering basic-banking services and making disclosures about rates and checkholding policies. However, about midway through the year, emphasis was switched to explaining banking's desire to secure expanded powers that would result in savings for consumers.

Ms. Brent says her experience as a banking advisor has had an effect at her bank. "It's made me realize the need to be more consumer oriented, to find out what the customer wants before creating a product the bank thinks the customer wants. I listen more now."

One of Mr. Anderson's themes was shopping for banking services as he travelled in Minnesota, New Jersey and California.

"The public doesn't know much about new services being offered by banks resulting from deregulation," he says. That's because there is a significant information gap between bankers and their customers.

There also is an information gap between bankers and the media, he says, which means banking's story isn't being adequately told. Although some reporters were knowledgeable about banking, many were not and these were very receptive to the information he presented.

He visited a college class in New Jersey where students were interested in bank profitability and how individuals could best handle their personal finances. Ms. Brent visited a college class that was studying the Federal Reserve System. Most questions were about the Fed and students were interested in how a check passes through the system. When visiting a college class, Ms. Brent typically gives a 15-minute presentation about banking before opening the session to questions.

She happened to arrive in one city on the same day a local bank was closed. It was the first closing in that area and she was kept busy responding to questions about bank safety and soundness. She took time to discuss the FDIC insurance system and how it works.

Banking advisors typically make three trips a year, and participate in from five to 10 interviews per day. They are accompanied by ABA-supplied representatives who set up interviews with newspaper reporters and radio/TV hosts. Some programs feature called-in questions. Advisors have precious little time to think of responses when they are on the air!

Among the challenges banker advisors face is being willing to listen rather than talk all the time and avoiding the use of banking-industry jargon that confuses the public. Surprises are abundant. One example is a comment made by a newspaper reporter in Tulsa to Mr. Adamson. The reporter said Mr. Adamson was more credible to an Oklahoman than a local banker would be because Mr. Adamson was from Indiana, where banks have a better safety/soundness record and the economy is not suffering as is Oklahoma's. Mr. Adamson drew a completely opposite reception from some media representatives in Boston, who, he feels, didn't want to give heed to a Hoosier banker because they could draw on the expertise of bankers in nearby New York City.

Questions asked varied according to the area of the country, advisors say. Safety and soundness was on consumers' minds in areas where banks are failing and the fate of banks that are acquired was of concern in areas where merger/acquisition activity is rampant.

Mr. Adamson was well-equipped to respond to the latter topic, since his bank was acquired recently. Relatively few questions were asked about lifeline services but questions about IRAs were asked almost everywhere.

Ms. Brent says she felt like a teacher enlightening the public, telling them about consumer topics, such as how to get information from a bank. "The public is somewhat intimidated by bankers," she says. She told consumers about new accounts and urged them to take advantage of these accounts. She stressed the fact that the small saver is the principal beneficiary of bank deregulation.

We're more like teachers than advisors, telling the public about consumer topics, such as how to get information from a bank.
—Emma Lou Brent

"The process of training bankers to speak out is extremely important to the industry," Mr. Anderson says. A program such as banking advisors wasn't as necessary in the days of regulation. "There is a great lack of understanding on the part of the public about how deregulation affects consumers and these changes have a great positive impact on the public. It's banking's responsibility to speak out."

All four bankers say they are looking forward to another year on the road.

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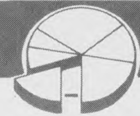

What Do Consumers Want?

Service of value, fast service and personalized service—not necessarily in that order.

By Joe Lawler
Assistant Editor

MOST CONSUMERS fall into one of three major stereotypes. Banks will have to become adept at reaching all three of these consumer types to be successful, according to Dr. Leonard Berry.

Dr. Berry is Foley's/Federated Professor of Retailing and Marketing Studies at Texas A&M University, director of the Center for Retailing Studies and currently is president of the American Marketing Association.

These three types are the "Get My Money's Worth" consumer, the "Time Buying" consumer and the "I Am An Individual" consumer.

Dr. Berry described these three types, and outlined strategies for reaching them, at the annual correspondent bankers conference of Mercantile Trust, St. Louis, held recently in St. Louis.

The "Get My Money's Worth" Consumer will buy generic facial tissue because he or she perceives no difference in quality with the high-priced brand. "At the same time, this consumer will go into a store and buy the highest-priced appliance because of its reputation for quality," Dr. Berry said.

This consumer's financial goals involve *making* money, not storing it.

To appeal to this consumer, Dr. Berry recommends the following:

— *Market a custom investment portfolio*. This portfolio should include accounts designed for specific goals: safety, tax avoidance, high potential return, liquidity, trust, etc.

Using this portfolio, the banker can sit down with this consumer and custom package an investment portfolio.

— *Provide financial planning services*. These consumers need help formulating financial plans. While many affluent consumers already have assistance available in some form, much of the middle market needs help in meeting future needs, avoiding taxes, meeting retirement goals, and so on.

These consumers don't want someone telling them what do to; they want an unbiased planner telling them the alternatives. "If they feel the planner is pushing a particular product, they will walk," Dr. Berry added.

Most banks do not yet have the staff expertise and systems in-house to offer a good financial-planning service. However, financial planning provides the potential for a new stream of fee income and provides a core for relationship banking.

Financial planning is a menu of services provided by a broadly-based generalist, backed up by specialists. So, instead of having to run hither and yon all over the bank to get what he wants, the customer can go to the financial planner, who acts as a clearinghouse for him. The financial planner then contacts the other departments of the bank to arrange services, making the bank much easier to deal with.

"Time buying" consumers have made microwave ovens the fastest selling appliances.

"Until we do this, we're whistling Dixie about relationship banking," Dr. Berry said.

— *Sponsor consumer education programs*. Provide financial information to the consumer through customer access terminals (also known as answer machines), newsletters and magazines, micro software for home banking and finance, and so forth.

The traditional cornerstones of banking — storing funds, transacting funds and loaning funds, are no longer enough for these consumers, Dr. Berry said. "Consumers are becoming investors, and your competitors more and more are investment houses."

The "Time Buying" Consumer has much to do and little time. These consumers have made microwave ovens the fastest selling appliance of recent years.

To appeal to these consumers, become a time-efficient bank, Dr. Berry said. Make high-quality, fast service available when and where the customer wants it.

Bring the bank to the customer through a hub-and-spoke system, with drive-ins, ATMs, shopping-center branches, apartment-complex branches, luxury branches in upscale shopping areas and home banking, Dr. Berry recommended.

Some of the features of the time-efficient bank are:

- Signage attracts and directs consumers.
- Contact employees are trained to sell, equipped for electronic banking and able to handle telephone banking and selling.
- CIFs (customer information files) are easily accessible to contact personnel to speed service.

Being time-efficient is becoming more crucial than ever to the success of banks. However, it is not enough by itself, Dr. Berry added. It is simply one requirement of success.

The "I Am An Individual" Consumer wants to be treated with personal service.

To appeal to these consumers, Dr. Berry recommended the following:

— Become a relationship bank. Treat customers as clients rather than customers. A customer is anonymous, someone who comes in and buys a service once and perhaps is never seen again. A client is a regular customer of the bank, who has a relationship with that bank.

— Send them handwritten notes occasionally.

— Call them instead of bouncing their checks.

— Call them by name when they come in.

— Satisfy all their financial needs.

— Assign a personal banker to the client.

To become a relationship bank, a

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Financial planning provides a core for the relationship with value-oriented consumers.

bank must take the following steps:
— Segment the market. To perform at a superior level, the bank must segment the market and focus its resources on particular segments. At the same time, the bank should not close its doors to any other customers.
— Offer a core service around which the relationship can be built, for each segment the bank is targeting.
— Make account representatives available. These should be bankers with the competence and authority to satisfy all the financial needs of the client, on the spot.
— Offer relationship pricing. This provides an incentive to the client to consolidate accounts. The incentive can be discounted fees, discounted loan rates, perks, etc.
— Finally, the bank should ensure that its staff is courteous and helpful by providing staff training and education.

Community banks are in an ideal position to treat customers like clients, Dr. Berry added, because they know all their customers.

For the same reasons, many small banks are being formed in California, Dr. Berry added. Many people like being treated like individuals in California, and so they like doing business with a small bank.

Many consumers have some traits of all three of the preceding consumer types, Dr. Berry concluded. A wise banker will find ways to appeal to all three types. ● ●

Tax Bill: Boon to Ag Real Estate?

THE new tax bill is expected to deter "tax-loss" investors from agriculture and encourage a new breed of investors looking for no-debt, safe, conservative investments with cash return each year, says a spokesman for a firm specializing in farm real estate and investments.

"Agriculture is in the position today to afford such investments," says Murray R. Wise, president, Westchester Group, Inc. "We're seeing some very astute money coming to this marketplace."

In addition to creating a new investment philosophy, this shift is better for the farm economy as a whole, he says. Productive farms are being sought, reversing a downward trend in the market. Many people are working with tenant farmers, which allows the farmer who accumulated a large debt when land prices were high a way of resolving that debt with a new source of income.

"The proposed tax bill also has the effect of opening up the market to a broader range of people, Mr. Wise says. Farmland syndications, or limited-liability partnerships, are growing in popularity, letting in the limited-capital investor. They also make it possible to own parts of farms in different geographic locations.

He believes any harmful effects of the tax bill will be seen in true commercial real estate and will bring back to farmland some of the capital diverted in the past.

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Banking-Legislation Politics

They are such that only in a crisis situation is passage of legislation likely

By Michael A. Greenspan

AS STRONG as the certainty of death and taxes is the uncertainty of the congressional process. Nevertheless, it appears that legislation on nonbanks will not pass this term. This was legislation not opposed by the vast number of affected interests and *strongly favored* by the Independent Bankers Association of America; the Federal Reserve Board; Congressman Fernand St Germain (D-RI), chairman of the House Banking, Housing and Urban Affairs Committee; and Senator Jake Garn (R-Utah), chairman of the Senate Banking, Housing and Urban Affairs Committee.

This article is about politics and the prospects this term for banking legislation which must reconcile the conflicting views of the House, Senate and administration on the proper role for banks and other financial institutions.

In the House, the banking committee and the House as a whole embrace a "traditional" role for banks, thrifts and other financial institutions: Banks and thrifts should be confined to their traditional activities, the Glass-Steagall Act barrier against mixing banking and securities activities should be retained and the barriers between banking and commerce should be kept in place. The essence of the position is that banks and thrifts each have a unique role to play in the national economy and each has been given certain legislative advantages to help them perform those roles (deposit insurance, discount-window access, favorable tax legislation, etc.). To permit these organizations to operate outside their traditional spheres is unfair to those who do not have these advantages, creates distractions to the organizations' performance of the jobs they were created to do and is potentially unsafe and threatening to the stability of the financial system.

The Senate banking committee has a differing view, which is shared by the Senate as a whole, and, to an even greater extent, by the administration. To be neutral, let us call it simply the "nontraditional" view of the role of financial organizations. It asserts that financial institutions must have the ability to adapt to changing times; that many, if not all, of the Glass-Steagall-Act prohibitions are no longer necessary; that a single institution blending the powers of banks and thrifts should offer to customers a complete array of financial services, very broadly defined; and that the asset side of the bank's balance sheet should be deregulated to an extent that parallels deregulation of the liability side to permit banks to better spread their risks.

Views of the proper roles of banks and thrifts differ greatly in Congress. Harmonizing them is extremely difficult in view of the practical aspects of passing legislation today.

It is obvious that the views as to the proper role of banks and thrifts differ greatly. Harmonizing them is *extremely* difficult. And it is even more difficult in view of the practical aspects of passing legislation today. Lobbying today is very sophisticated. It leads to the following practical "rules" of politics:

1. Legislation can be passed if there is a crisis or a true consensus in support of it.

2. Legislation can be relatively easily passed (or an amendment obtained) that favors some politically knowledgeable person or group and that hurts no politically knowledgeable person or group.

3. Legislation can be passed only with great difficulty, if at all, if there is some politically knowledgeable group with a significant economic issue at stake that opposes legislation and that is not willing or able to compromise on that legislation.

4. The closer that consideration of proposed legislation comes to an election the less likely it is that someone running for office will take a position contrary to the interests of any important group.

5. Even legislation that passes the above tests and is widely supported can be stalled by being held hostage to the passage of controversial legislation.

Let us examine how these principles work in the context of four pending pieces of banking legislation: the recapitalization of the FSLIC; additional powers to regulators to facilitiate the sale of failed or failing banks; the closing of the nonbank "loophole"; and the granting of additional powers to banks.

Understanding the FSLIC recapitalization legislation is easy: The federal insurance fund for thrifts is in a precarious financial position. While there are substantial questions as to whether the industry or the government should pay, there is overwhelming consensus that action must be taken by someone at some time to strengthen the fund. Achieving legislation on just the recapitalization is a matter of compromising on its cost to the government.

Understanding the legislation concerning the sale of troubled banks and thrifts is only slightly more difficult. The Bank Holding Company Act prohibits companies from acquiring banks in more than one state without the approval of the other states and prohibits banks from acquiring thrifts. In order

Mr. Greenspan is a partner in the Washington, D. C., law firm of Thompson & Mitchell, which represents banks and HCs before Congress. He is a former Fed official.

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to provide stability to a financial industry that was facing the prospect of many failures, Congress in 1982 adopted legislation that overrode those prohibitions in the case of failed banks and thrifts that are large and not attractive to potential in-state acquirors.

There are two possibilities for filling the void. One is a simple extension of the expired legislation. The second, advanced by bank regulators, would permit them also to arrange for the acquisition of smaller financial institutions that have failed, or are failing. The opponents of both approaches, but particularly the latter, are concerned with a departure from the policy of allowing the states to decide the extent to which entry should be permitted by out-of-state organizations.

The nonbank controversy also must be seen in the context of the underlying issues. The Bank Holding Company Act not only prevents a bank HC from acquiring a bank in another state, but prohibits companies that control banks from engaging in nonbanking activities. "Bank" is defined in the statute as an institution that accepts demand deposits and engages in the business of making commercial loans.

The Supreme Court has ruled that the definitions of those terms should be read narrowly: "demand deposits" do not include NOW accounts and "commercial loans" do not include CDs or similar investments that banks normally make. The result is that a nonbanking company can acquire one of these "nonbanks" and combine banking and commerce to that extent and a bank HC can acquire a "nonbank" in a state that does not permit acquisition of its banks by out-of-state organizations.

It is not clear whether the Congress that adopted the current definition of "bank" would have regarded the ability to operate through nonbanks as a loophole. Nevertheless, virtually everybody has endorsed, or at least not opposed, legislation closing the "loophole": the Fed strongly favors the bill, regarding it as one of the more important banking issues facing Congress; the Independent Bankers Association of America strongly supports passage of the legislation; the chairmen of the House and Senate banking committees have gone on record as strongly favoring the legislation; the House banking committee has approved the legislation; and in 1984, the Senate approved legislation containing this provision by a vote of 89 to 5.

Major opponents are certain large bank HCs (their opposition has lessened with the Supreme Court approval of regional compacts) and some large companies that would like to enter banking. These companies are not particularly vocal, because of the possibility that their entry into banking may result in Congressional authorization for banks to enter their fields.

As far as the topic of new powers for banks is concerned, legislation passed by the Senate in 1984 would have expanded the authority of banks to sell and distribute revenue bonds and mortgage-backed securities. The administration has gone further and has supported, not only these powers, but the sponsorship and sale of mutual funds; real-estate investment, development and brokerage; and insurance underwriting and brokerage.

The conflict is quite clear: The House and the affected industries are opposed to the legislation; the administration, the banking industry and the Senate presumably would take the same "liberal" positions they have been taking.

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1. Certain senators on the banking committee that voted in favor of banking powers in 1984 are running for reelection this year and do not want the committee to consider banking-powers legislation at this time; it is too close to an election. In accordance with Political Rule 4, the people you hurt remember the injury more often than the people you help remember the favor. See also Political Rule 3: Politically savvy and organized opposition to legislation generally can stop it in the absence of a bona fide crisis or a national consensus on the issue. It goes without saying that industries opposed to expanded banking powers are politically savvy.

2. The House Committee that oversees the securities industry has insisted that it, as well as the banking committee, should consider any legislation expanding the securities powers of banks. See Political Rule 3.

3. Knowing how important the nonbank legislation is to the House, Senator Garn and the administration have stated that they will not allow that legislation unless banking powers are expanded. See Political Rule 5 on legislation as a pawn.

4. Knowing how Senator Garn feels about achieving some legislation, Congressman St Germain has stated that the House will not consider any banking legislation at all unless it includes nonbanks. See Rule 5 on legislation as a pawn.

5. The apparent stalemate caused by points 3 and 4 caused Senator Garn on August 7 to announce that he was submitting new legislation that would deal only with the recapitalization of the FSLIC and the acquisition of troubled institutions (together with some other minor matters), but addressing neither nonbanks nor new-powers issues. On August 13, the Senate banking committee approved the bill.

Chances for passage of even this limited legislation are problematical because of the hostage principle of Political Rule 5. Senator William Proxmire (D Wis.) has announced that he will attempt to prevent Senate passage of the legislation, by filibuster if necessary, if it does not include nonbank legislation. Other senators may try for additional banking powers. Senator Garn and the administration have flatly stated they will not allow nonbank legislation unless new powers are adopted. And in the House, Congressman St Germain has threatened to stop all banking legislation that does not plug the nonbank "loophole," although other members of his committee believe passage of FSLIC and takeover legislation is necessary.

This raises the question of how these strong views are to be resolved. Political conflicts resemble the teen-age practice known as "chicken," in which two people drive cars toward one another until one, in a moment of sanity, "chickens out" and swerves to avoid the catastrophe.

In speculating about which partisan will "chicken out" in politics, as in any negotiation, one must try to assess how strongly each one wants his goals and how unpalatable to each are the other's goals. In addition, on the political level, there is the question whether the public interest requires (not suggests) a particular course of action.

The first question is what absolutely must be done now. Legislation to capitalize the FSLIC certainly is desirable but probably could be put off for a short time. Emergency takeover legislation is desirable, but the need for it could be obviated by state legislation. Powers legislation may or may not be desirable, depending on one's philosophical view of the role for banks, but even its supporters do not claim it is mandated by a crisis. And there seems to be no real push for nonbank legislation at this time because companies are not rushing to establish them, primarily because they fear Congress will retroactively prohibit them.

Where does that leave the legislation? It is at least relatively clear that powers and nonbank legislation, which are inextricably tied together, both are dead; and FSLIC recapitalization and emergency takeover legislation, having cleared the Senate banking committee, have a reasonable chance of passage. Both Senator Proxmire's threat of filibuster and Congressman St Germain's threat could derail even those matters. I think most observers regard the chances of even this limited banking legislation passing this term as being too close to call.

In the longer run, it is clear that the FSLIC recapitalization will have to be addressed. As far as powers are concerned, it is difficult to imagine the passage of major powers legislation until the affected industries are more willing to compromise the scope of the activities in which each may engage. (See Political Rule 3 on the relative ease of blocking legislation.) And nonbank legislation remains doubtful as long as the powers question remains in doubt.

All of which is subject to the political rule that supercedes all political rules: In politics, nothing is *ever* certain.

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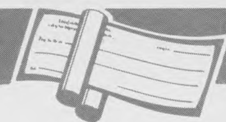

Telecommunications Marketing Formula

The shift in responsibility for long-term financial security from banks to individuals will accelerate the demand for more personalized, cost-effective products

By Richard Darwin
Battelle Memorial Institute
Columbus, O.
and Bruce Niswander
Objective Financial Systems
Columbus, O.

INFORMATION is the raw material that fuels the engine of today's financial-services industry. Historically, this statement has always been true, in spite of insistence by many bankers that their major concern was the ability to attract and manage money. The skillful application of information resources will become even more important as the combined effect of deregulation and the computer permanently alter the financial-services industry.

Any further consideration of this forecast requires an understanding of certain "givens" or assumptions. The first assumption is to recognize the existence of what we prefer to call the "right" formula used in the design of profitable information systems. That is, access to information must be delivered to the "right" person, at the "right" location, at the "right" time, at the "right" price! A simple concept, yet too often ignored by network designers and information-service providers.

The "Right" Formula

A significant number of firms pursuing the financial-services market have recognized the existence of the "right" formula and have invested heavily in the development of network-oriented computer systems. Their primary goal is the ability to provide consumers with limitless access to financial services in a cost-effective manner. Many companies such as Citicorp, Merrill Lynch and Sears, make no attempt to disguise their belief that telecommunications technology will play a major part in serving a constantly changing marketplace.

Witness the rapid evolution of the regional, national and, in many cases, international EFT networks. These signs indicate that future-oriented corporations believe the highway to further profitability lies in a properly constructed telecommunications network. Thus, one can conclude from these activities that the banking community is on top of things and the corporate strategic plan is on target.

Even with all this frantic activity, something still is missing and, if not recognized, could spell disaster for companies operating in the banking industry.

Consumer's Role Not Defined

Information as a corporate resource is not a recent discovery. Recall from your studies of modern economic theory that a number of scholars believe that information deserves to be included with land, labor and capital as a factor in the classic definition of the production function. In fact, a few economists believe that information technology already is the dominant factor in this formula which confirms the basic forecast of this article. Even if one agrees with this restated formula, the "information economist" has not gone far enough in describing the role the consumer will play in forcing information to become the driving force in the financial-services industry's production function.

Unfortunately, many economists and bankers alike are completely unaware of the powerful forces beginning to take shape in today's already unsettled economic environment. A combination of events will result in an unprecedented demand for financial products and services tailored to the unique needs and requirements of the individual. The customized nature of this demand requires the banking community to begin immediate development of the "right" formula for pursuing this new market.

Deregulation of the financial-services industry will convert a market currently dominated by product sellers to one controlled by the unique requirements of the individual consumer. A second factor in this transition will be the wholesale shift in responsibility for personal financial decisions and long-term economic security from the employer and government agencies to the individual. These changes will result in a dramatic increase in the demand for comprehensive product information capable of being delivered to every consumer.

This trend will culminate in a comprehensive set of products capable of satisfying each consumer's unique set of financial needs.

The most successful companies will be those capable of capturing detailed information about a client's current financial position and in turn, using that data to plan for future needs and objectives. It is important to note that the limitless combination of personal desires and financial factors makes each individual as unique as his or her fingerprint.

Creating Economic Roadmap

The goal will be to electronically capture each client's "financial fingerprint" and use that information in conjunction with cost-effective products to create a comprehensive economic roadmap. This strategy will guide the individual through a constantly changing economic environment. The distinguishing qualities of this advice will be its technical accuracy, ease of creation, flexibility and timeliness. The ability to formulate this strategy in an increasingly cost-conscious environment will require the creation of large-scale expert systems connected to the outside world via a comprehensive telecommunications network.

At the same time new data files of comprehensive product information will be created, resulting in a global clearinghouse of financial products. With the advent of the personal computer and low-cost electronic terminals, this information will be accessible by corporations as well as individuals. Using this network to satisfy a unique set of financial needs will

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require a sophisticated computer system capable of linking the consumer's financial fingerprint to the expanded electronic marketplace. Sophisticated expert systems will use the client's profile to project future needs, and in turn, conduct high-speed reviews of generic product information. The ability to access this network in an efficient fashion will be enhanced by a portable data carrier such as a smart card capable of capturing an exhaustive list of financial factors. Through the use of biometrics, financial security and privacy will be controlled by the individual rather than the system.

This comprehensive system will convert the traditional product-distribution network from one dominated by mass-marketing principles to one controlled by the unique demands of the individual consumer. In brief, personalized information will become the driving force in the financial-services industry. The fact that this network will control the distribution of capital means this revolution will directly affect the entire economy with particular emphasis on those in information processing, computer systems and telecommunications. The number of no-load and low-load products delivered through a totally electronic market will increase dramatically. Razor-thin profit margins will cause inefficient purveyors to disappear.

From a timing standpoint it is important to note that this revolution already is well underway. Many commodities already trade in global markets. Artificial-intelligence systems for accessing large data bases of information using such features as natural-language inquiry are near completion. Expert computer systems with open analytical logic are in place and connected to data bases of existing product information. Portable data carriers in the form of smart cards using integrated circuits and laser technology are available for capturing the owner's financial fingerprint. As large corporations become aware of these products they will begin to deliver a vertically integrated list of products capable of satisfying virtually every need of the individual consumer.

As this network begins to take shape, the information broker will replace the salesperson as the human element in the distribution process. Product design as well as pricing will be highly personalized with fees being negotiated at the time the transaction is completed.

In summary, the shift in responsibility for long-term financial security from the institution to the individual will cause the economic cushion in the average consumer's budget to disappear. This, in turn, will accelerate the demand for more personalized, cost-effective products. The results will be a new formula for corporate survival focusing on product designs that are infinitely flexible. This will replace today's mass-marketing strategy where a small list of static products is combined with a large promotional budget to attract/or retain an increasingly sophisticated consumer. ● ●

Banks Institute Programs To Reduce Loan Losses

A majority of banks have begun programs to reduce loan losses, according to the ABA's 1986 Retail Bank Credit Report.

The report indicates that installment loans made at commercial banks increased rapidly in 1985, along with delinquencies and losses.

For all types of installment loans by banks, gross dollar losses were equal to .53% of total outstanding, an increase from .44% in 1984 but lower than the 1983 loss level of .60%.

Net dollar losses after recoveries for 1985 were .39% of outstandings, higher than in 1984, when the figure was .28%, or 1983, when it stood at .36%.

Total outstanding installment debt was $535.1 billion at year-end 1985, compared to $453.6 at year-end 1984, according to the Fed. Commercial banks held a 45% market share at year-end 1985, compared to 46.1% at year-end 1984. Finance companies increased from 21.2% to 22.5%, and savings institutions increased from 8.9% to 10.4% during the period.

Credit unions, retailers and gasoline firms lost market share.

For 1985, banks reported average gross losses of $135,600 on personal loans, down from $157,000 in 1984.

Approximately three quarters of all banks reported using a formal program or policy to reduce loan losses in 1985, with large banks the most likely to have done so.

Steps taken to minimize consumer-credit losses include tighter loan-approval criteria (reported by three quarters of all community banks and more than half the midsized and large banks) as well as tighter procedures for internal-loan review (reported by between 70% and 80% of banks of all sizes).

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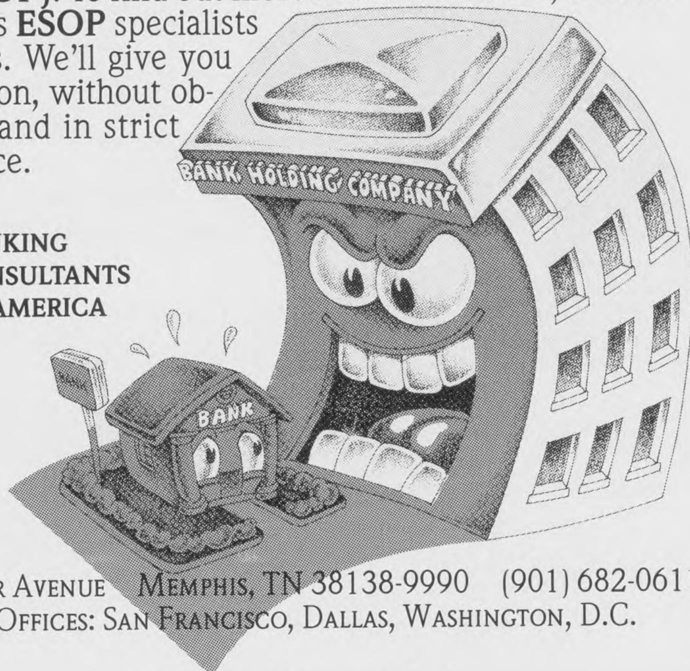

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Bank Earnings Optimism

The formula for tomorrow's success, for stable or higher earnings, is simply to practice the fundamentals

By M.E. Bond
President
Borod & Huggins Educational Services, Inc.,
Memphis, Tenn.

EXPERTS DIFFER in their opinions on the condition of earnings of community banks. By measures of ROA and ROE, community banks have performed well and often have experienced higher measured returns than regional or big-city counterparts.

Recently, however, community banks have watched a relative decline in their performance ratios. The reduction is partly due to the large percentage of community banks that operate in the depressed agriculture and energy areas. However, the impact of these segments of the economy is transitory.

The reduction in earnings also is partly due to more fundamental changes within the banking industry. These changes are secular and will make a more lasting impact than the transitory changes.

The trend of declining net interest margins is due to these fundamental changes. The low-cost, core deposit base of many community banks has changed as depositors transfer funds into higher-yielding deposit accounts.

Community banks also witnessed a decline in their loan production as consumer loans, the community banker's staple product, are being shared with new forms of competition, such as nonbanks, captive finance companies and regionally credit card operations of larger banks and thrifts.

Also, some community banks have lost deposits because of declining customer loyalty. Customer loyalty at community banks is no longer as intense and no longer as tied to community pride, as once was the case.

Even given these changes, however, there is reason to be optimistic about earnings prospects at many community banks. The formula for tomorrow's success, for stable or higher earnings, is simply to practice the fundamentals.

First, the banker must stay informed about the bank's market and clients. The banker must stay in front of changes within the bank's geographical service area. Many describe this as "niche playing." Others describe it as being responsive to needs, or filling the personal banking need.

Regardless of the terminology, it is the community banker's responsibility to understand his market and his clients, to stay abreast of changes and to practice good banking fundamentals.

Another reason for optimism can be found in bank operations. Community bankers must learn new ways to leverage existing overhead for higher rates of return to the bank. Looking back to the more regulated times, bankers had little incentive to worry about leveraging overhead. In fact, there was little incentive at all to worry about overhead.

The new environment has not changed the bank's overhead cost — fixed asset facilities are still used and still require servicing, and human capital and employee expenses are comparable to earlier times.

Recognizing this commitment to overhead, the community banker now must be attentive and receptive to new ways to leverage overhead for greater returns. He should search for ways to increase the productivity ratios of deposits, loan portfolios and total asset size to fixed overhead expenditures.

Bankers who have instituted programs to leverage overhead have discovered good results in the bank's earnings.

High-performance community banks have validated this two-part formula. Yet the records show that many bankers have room for more leverage.

In summary, know your markets, know your clients, practice good banking fundamentals that serve the market niche and develop strategies to leverage overhead. This combination promises new prosperity and higher returns to the community bankers of tomorrow. • •

Near-Term Recession Possible?

TAX-REFORM legislation could increase prospects for near-term recession, according to the senior economist at IDS Financial Services, Inc., Minneapolis.

This opinion is based on the fact that, under current legislation, the investment-tax credit would be repealed, real after-tax rates would be higher and corporate financial subsidies would be cut back. In tandem with budget cuts already legislated, the impact could be a $70-billion-plus reduction in the federal deficit in 1987.

This swing to a sharply more restrictive fiscal policy could easily shave 2% or more from real GNP growth, says William Melton, increasing chances of a recession in a major way.

He says ITC repeal will reduce investment spending and consumers will reduce purchases of durable goods because they will experience a slight tax increase and lose the consumer-interest deduction.

But Mr. Melton feels the Fed's response to tax legislation will be a more accommodative monetary policy, which should mean GNP growth in 1987 only slightly lower than that in 1986.

Long term, he believes the economic impact of tax reform will be positive.

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Ag Banking Faces Transition

ABA study reveals tactics bankers should take to survive crisis

By Jim Fabian
Senior Editor

Alan Tubbs (c.) and Mike Fitch discuss ABA's new ag study with member of Iowa Bankers Association at centennial IBA convention in Des Moines last month.

A NEW ABA study is telling a large group of people where agriculture and ag banking are going and what should be done to return both to a sound financial footing.

This large group of people includes members of Congress, the administration, regulators and ag-industry leaders — not to mention ag bankers.

The study, called "Transition in Agriculture: A Strategic Assessment of Agriculture and Banking," was authorized last year by the ABA's agricultural banking division. It was made by John Hopkin of Texas A & M University.

Preliminary information from the report was presented at the Iowa Bankers Association annual convention in Des Moines on September 16 and at the Agricultural Credit Conference sponsored by the Illinois Bankers Association in Decatur the following day.

Mike Fitch, chairman of the ABA's agricultural bankers division, said the study "offers the tools needed for development of sound long-term planning, policies and procedures consistent with the new realities for the agricultural and ag-banking industries." He predicted that the project's planning guide "will enable individual banks to adopt specific strategies consistent with their unique situations/needs."

Mr. Fitch is vice president, Wells Fargo Bank, San Francisco. He appeared at the ag-banking breakfast at the Iowa convention and later that day at a press conference held in conjunction with the convention in Des Moines.

"The release of this very important research project illustrates a recognition by commercial agricultural bankers that agriculture and its related businesses are clearly not just experiencing the usual cyclical liquidity problems with which we have become accustomed; they are undergoing fundamental structural changes in need of basic re-directions. The study responds to the reality that ag bankers, as well as their borrowers, are searching for direction on which reasonable plans, policies and projections can be based."

He said the report points out that ag banking must form new coalitions to control its own destiny by becoming pro-active in the political process on behalf of its farm customers, as well as itself.

The study had not been published when Mr. Fitch spoke; he touched on only a few of its recommendations.

"One revelation I consider especially important is that, contrary to the general feeling that the demise of the small independent bank is certain, the research suggests that banking deregulation and structural changes in agriculture are, in fact, consistent with the existence of a large number of different types and sizes of banks."

He said that because it's critical that everyone understand the fundamental principle that the need for capital in agriculture is greatest when the cost/price squeeze is at its worst, he considers the project's treatment of the needs for securitization, particularly a secondary market for farm real-estate loans, to be especially important.

He quoted from the report: "Banks will need to materially increase their capacity and willingness to make farm real-estate loans"; and "the securitization of agricultural credit provides one means of access to the nation's capital markets."

"These quotes illustrate the responsiveness of the researchers to the industry's pragmatic needs," Mr. Fitch said.

Researchers were asked to take the risk of suggesting what bankers should do to help themselves rather than merely passively and reactively accepting legislative and regulatory control of banking's destiny, he said.

To make sure the planning guide for individual banks is a usable and practical instrument, two independent bankers (one in Kansas and one in Wisconsin) actually tested it by using it for their own banks. They told Mr. Fitch they were so pleased that they question how others can survive, let alone prosper, without it.

Mr. Fitch urged all bankers to subscribe to the report. They were given

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brochures that gave brief descriptions of it and how to order it.

He said he considers this research project to be merely the beginning of a process, not a document to be read and shelved. "The ABA already has formed an industry task force to recommend to legislators and regulators mechanisms for development of a viable secondary market for farm real-estate loans," he said.

Alan R. Tubbs, president, First Central State, DeWitt, Ia., appeared with Mr. Fitch at the Iowa convention. He is immediate past chairman of the ABA ag-bankers division.

He said the study suggests substantial changes in the structure of farming will continue to occur because of reduced profitability, economies of size and debt distribution. The study concludes that the transition in farm structure will continue to occur with an exodus of farms in moderate size categories and with an increase in large and part-time farms.

This structural transition in farming units will leave an impact on rural communities, he added. It will change retail trade patterns to the extent that more retail trade will be carried on in towns that the research group refers to as "regional trade centers." Smaller communities will suffer retail sale reductions and will need to assess what kind of community they will become. Other communities may determine that they can become regional trade centers, although such centers will be limited in number, which means farmers will travel further to purchase supplies, consumer goods and credit.

This transition will force banks in rural communities that rely on agriculture as their base to reassess their markets. The research group identifies three types of banks serving the new agricultural structure and suggests what they may have to do to remain competitive.

Mr. Tubbs declared that competition for sound ag credit will remain intense and the Farm Credit System will survive and eventually thrive and be a part of that future. He added that serious consideration must be given by the banking community to future availability of long-term loans and services now in the planning stages by the Farm Credit System. "Banking must develop a game plan as to how to compete with this new Farm Credit System and what role the Farmers Home Administration should play in the future," he said.

"This study goes a long way in assisting individual banks and the industry plan for the future. It will be a road map that will be helpful in adopting legislative strategies and provide assistance to the Congress," he said.

In a micro-sense, he added, it should help every bank understand the fundamental structural changes that are occurring today and help them assess their changing market and adopt competitive strategies that will ensure success in the future. • •

U. S. Ag Efficiency Questioned

THE U. S. is not necessarily more efficient than other countries when it comes to agricultural production. It produces a glut of ag products but doesn't necessarily do it in the cheapest or most efficient way.

These are the views of Alan R. Tubbs, president, First Central State, DeWitt, Ia., and Otto Doering, professor at the department of agriculture and economics, Purdue University. They spoke recently on the topic at the Midwest Banking Institute at the University of Minnesota, Morris. The Institute is sponsored by five state banking associations, including Minnesota and Wisconsin.

Dr. Tubbs pointed out that 63% of all ag debt is held by 19% of the nation's farmers. This means many farms are servicing too much debt and therefore can't be efficient. The proportion of debt has risen in recent years as prices on crops decreased because of the glut on world ag markets.

Professor Doering said technology has had a great influence on agriculture. Although technology has made bigger crop yields possible and shortened some labor tasks, it hasn't proved economically efficient in many cases.

Farmers who have taken on large debts because of high-priced machinery and technology while getting low prices for their crops are prevented from reaching their highest possible economic efficiency because they are servicing too much debt, he said.

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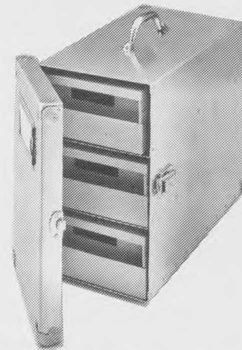

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Reducing Farm-Borrower Debt Is Critical Issue, Says IBAA's Olson

IBAA president-elect calls for concerted effort to avoid large-volume debt forgiveness

By Jim Fabian
Senior Editor

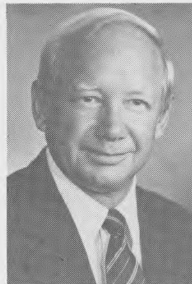
RETIREMENT of farm-borrower debt is a critical issue, according to Thomas H. Olson, president-elect, Independent Bankers Association of America.

Mr. Olson, who also is president, Lisco (Neb.) State, is concerned that the U. S. Department of Agriculture has not agreed to assign payment-in-kind payments to lenders on the same basis that cash payments are assignable.

Farm-program payments should be devoted to the maximum extent possible to the retirement of debt owned by those borrowers, he says. "If a major part of these federal payments is not used to retire the backlog of accumulated debt, when and how is that debt going to be repaid?" Payments for 1986 are expected to be approximately $24 billion, about equal to total net farm income for the year.

One answer he gives is that much of this debt may never be retired by borrowers, forcing them to declare bankruptcy.

Mr. Olson is concerned that bankruptcy legislation in Congress could turn the Bankruptcy Code into a procedure for forcing collateralized lenders to forgive debt in large volume under the guise of debt reorganization, with virtually no attention given to the capacity of commercial lenders to absorb such loan losses.



Ag-debt forgiveness would put a chill on ag credit — Thomas Olson.

"I believe this legislation is very shortsighted," he said, "because it will not serve the real ongoing interests of either farmers or lenders."

He added that farmers can't really expect to continue their operations unless they have future sources of operating credit. Lenders can't be expected to extend that credit if they are frozen into major loss positions on collateralized loans with no opportunity to recapture some losses even when conditions improve and farm assets begin to recover in value.

Mr. Olson agrees with Iowa Bankruptcy Judge Richard Stagemen who said he can "think of nothing that would more quickly put a chill on farm credit . . . than to impose all debt forgiveness on an isolated class of creditors."

Mr. Olson is looking for a way to make this basic point before the pending bankruptcy bills move further toward final enactment. "Somehow, we need to focus more attention on how the backlog of unmanageable farm debt is going to be disposed of. As much as possible we need to work with farmers in finding a mutually acceptable way to resolve this issue," he said.

It's imperative that consideration of the pending bankruptcy legislation be brought into this broader context, he added, one in which farmers and lenders can work together toward a better solution.

He lamented that no one seems to have specific answers to this dilemma. But pressures are building for something to be done differently in agricultural policy, he said, with farm-program costs ballooning and no progress being made to expand markets and reduce surpluses of most commodities.

One idea getting attention: Provide a virtually open-ended export subsidy to the major grains, such as corn and wheat, by applying the so-called "marketing loan" to these commodities.

"Under the circumstances, I suspect this would greatly escalate federal costs, but not improve export marketings measurably, since other exporters would make every effort to offset resulting price reductions," he said.

Given the huge expenditures of federal funds, Mr. Olson said, "Wouldn't it make sense to try to channel some of those federal payments to retiring the backlog of unmanageable debt owed by farmers?"

He thinks there must be a way to assign at least any additional payments being made by the federal government toward repayment of existing farm debt, with the farmer able to maintain his farming operations as a result.

He stressed the point that, as pressures mount to again reconsider agricultural policy, it's necessary to get the debate focused on the backlog of debt and what can be done about it. That debate needs to be broad enough to consider how the whole range of federal dollars is being spent on farm income and credit programs.

"And we need a concerted effort, hopefully involving lenders and farmers, to get more of this overall effort devoted toward resolving the farm-debt backlog," he said.

"Only then," he added, "can we look toward a truly brighter and less tension-ridden future for credit-financed agricultural production in this country." ● ●

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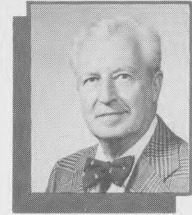

Getting Rid of Bad Apples

The banking industry must rid itself of officers, directors and insiders guilty of criminal misconduct

By Dr. Lewis E. Davids
Professor Emeritus Finance
Southern Illinois University, Carbondale

AN ATTITUDE of ambivalence surfaces when the topic of criminal misconduct in banking comes up. No one likes to hear about it, but the press is reporting on it almost daily in connection with failing banks.

Throughout the years, vigorous efforts have been made to hush up any instance of impropriety in banking, with bank managements taking great pains to avoid damaging publicity, often at the expense of the bank and its shareholders.

Present-day examination procedures make cover-ups more difficult and regulators are ferreting out those guilty of criminal acts; but the bad apples discovered so far may represent just the tip of the iceberg.

Insurance and bonding firms have benefitted from cover-ups in the past because they do not have to pay off claims if they're not filed. Yet banks doing the cover-ups are technically voiding their financial-institution-bond policies.

But someone or something must be the loser from a cover-up. Banks generally can get some restitution for an embezzlement, either from the criminal or, not infrequently, from the criminal's relatives. Such a result saves the bank the embarrassment that would occur if the crime were made public.

But it should be remembered that the whole structure of banking rests on public confidence in the banking system. Each criminal act against a bank sets the stage for erosion of this confidence, should the act become public knowledge. Rather than take the chance that such acts will be made public, it behooves bank management to remove any criminal element from its ranks.

Years ago when I was a New York City banker, it was policy to turn down profitable business that appeared to have originated from suspect sources. We didn't want our bank's reputation to be blemished by someone being able to say a reputed gangster or drug dealer had his accounts with our bank. Today many banks accept deposits with no questions asked and eventually subject their managers to embarrassment if the deposits in some manner place the bank in a bad light.

A former Comptroller of the Currency believes bank-related crime deserves more enforcement attention in order to ensure the safety and soundness of individual institutions and the stability of the banking system.

The Justice Department should be applauded when it updates its systems so it can cross check names to determine if banking-industry criminals are involved in more than one bank and to permit the department to do a better job circulating knowledge of bank criminals among other enforcement agencies.

Regulations tend to make banks cautious about blowing the whistle on criminals in their midst. Such was not the case in the past, when it was bank policy to cooperate with law-enforcement agencies and other bankers by providing information about individuals in situations pertinent to banking. Fear of litigation has prompted bank attorneys to caution against sharing of information about suspected criminals. This can lead to the compounding of criminal acts against banks.

A middle-level officer at a bank began to stipulate loans after spending too much time in Las Vegas. He stipulated that the borrower make payments directly to the officer. When bank management discovered the situation, it fired the officer, but covered up the crime.

Recent actions by regulators and others indicate that the punishment for criminal conduct on the part of bankers is beginning to fit the crime.

That same officer subsequently became the founding executive of a national bank and the Comptroller of the Currency was ignorant of the officer's past record, so it chartered the institution.

When the first bank received inquiries about the officer from the Comptroller, the bank's legal counsel advised that the bank provide only the barest information. It told the agency that the officer had worked at the bank from date X to date Y, but it didn't tell the agency that the officer had been fired for stipulating loans. This policy was followed "to protect the privacy of the individual," which was how legal counsel interpreted regulations.

The strongest deterrent to criminal misconduct by bankers is the swift and sure prosecution of potential violations of criminal law, say regulators. And they are beginning to follow this policy after years of benign neglect.

It's thought that about half of the current bank failures are results of insider abuse. Recent actions by regulators and others indicate that the punishment for such conduct is beginning to fit the crime.

But the fact remains that much grief could be avoided if bank managers took action to rid their institutions of criminals before things reached the stage where regulators are obliged to prosecute after the bank has failed. • •

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Loan Evaluation:

Preparing for the Exam

Good preparation for an examination often is the key to a successful one

By William L. Perotti
and Joseph B. Nester

THE OVERALL tone and result of a regulatory examination may be determined by how examiners perceive the quality of your bank's lending function. The key to a successful examination often is your bank's preparation.

With the ratio of problem banks to experienced examiners increasing almost daily, regulators now rely more and more on internal bank loan-review systems to detect and deal with potential problem loans. These systems, which must be effectively developed before an examination occurs, will lead to a smoother examination for the bank.

Examiners have been prompted by the Comptroller of the Currency and state banking commissioners to work with banks so banks can work with their customers. To support this environment, you'll want to incorporate several steps into the examination preparation process.

First, it is important to anticipate what the examiners' needs and questions may be. Don't wait until these needs and questions are expressed by the examining team. Waiting until the loan discussion comes up to provide information to an examiner may reduce credit given for new data. From the examiners' viewpoint, information that should be in the files should not have to be requested. If you anticipate that examiners may question a certain item, information to respond to the question should be contained in the file. The key is to create as few questions as possible in examiners' minds as they make their review.

Credit and collateral files must be documented completely before an examination. All updated and necessary documents, including current financial statements (balance sheets and income statements), call reports, status reports, approved loan memorandums, etc., should be placed in the file. A commitment to keep these files current and complete on a continuous basis dispels the appearance of confusion and disorganization that can result when a credit file is completed during the course of the loan discussion. Such a situation only adds to examiner uncertainties as to the overall capabilities of management.

Documents should not only be current, but realistic. A balance sheet based on equities without corresponding debt (direct and/or contingent) is of little value when evaluating the quality of an obligor's indebtedness. The borrower's cash flow must be well defined and understood by bank staff. Presently, the perceived attitude of examiners is that cash flow repays a loan while collateral reduces the bank's potential loss exposure.

Further support for a loan is provided by collateral valuations that are current and realistic, given existing market conditions. While a collateral-dependent loan still may be classified substandard, portions of it may avoid being moved to "doubtful" or a worse rating if the valuation is current. It is essential that current collateral valuations be obtained for all loans, especially those for real estate and energy. If possible, values for income-producing collateral should be related to existing cash flow, and assumptions should conform to the market. To supplement valuations, documentation supporting cash flow from collateral should be available; i.e., rent rolls and production-run data.

Another step in the preparatory process is to develop a problem-loan list to be shared with examiners. At a minimum, this list should include non-accruing loans, renegotiated loans, loans delinquent 90 days or more and all other internally identified problem loans. Along with this list, additional information about these loans should be provided to examiners — why a loan is a problem, what is being done to resolve or, at least, improve a given situation and a probable timetable when action is expected to occur. Examiners are more understanding if you can both identify the problem and demonstrate that you have a handle on it.

The lending-function evaluation is a subjective review, and if a bank can document its preparation efforts for the examination, it can help regulators formulate their conclusions.

Today, more than ever, examiners expect bankers to perform other essential evaluations, such as identifying concentrations of credit, and to react accordingly. Credit concentrations, by their very nature, are dependent on a common component, and a deterioration in that component could have a negative effect on every loan in that concentration.

Concentrations are defined by examiners as obligations, direct or indirect, of the same or affiliated interests that represent 25% or more of a bank's capital structure. However, each bank needs to define its own con-

Mr. Perotti is vice president/asset review, Cullen/Frost Bankers, Inc., and Mr. Nester is assistant vice president/asset review, Frost National, San Antonio.

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centration levels, depending on its marketplace. For example, in today's environment, loans secured by office-building construction in a depressed area such as Houston that exceed 5% of capital might be considered as concentrations.

Bankers should establish and identify concentrations and recognize the inherent risk that exists in them. Providing this information to examiners demonstrates that the bank knows and understands the composition of its loan portfolio.

Another area that is being closely scrutinized by examiners is borrowings by insiders (directors, executive officers and principal shareholders). These borrowings will be examined carefully, thus, credit and collateral files should be complete. To avoid potential problems ranging from classifications to civil money penalties, financial data, collateral valuations and all necessary loan approvals must be included and clearly documented.

To further demonstrate the bank's willingness to identify and solve potential loan problems, management should develop its own list of credit and collateral exceptions. This list, updated monthly, can be created when adequacy of the bank's loan files is reviewed. These exceptions should be segregated by the handling officer so someone can respond to each exception.

After developing and implementing the above procedures, management should carry the loan-evaluation process one step further. Internal procedures that ensure that the allowance for possible loan losses is maintained at a sufficient level to absorb the loss inherent in the loan portfolio must be developed. Regulators have stated that directors and bank management are responsible for establishing written policies and procedures to evaluate loan-portfolio risk, to ensure timely charge-off of loans and to properly reflect estimated future loss in the allowance. Regulators feel that the absence of satisfactory controls to ensure that the allowance is maintained at an adequate level may constitute an unsafe and unsound banking practice.

Before starting the evaluation process, banks must disregard two guidelines used in the past: the historical benchmarks that the allowance for loan losses should equal 1% of total loans and that arbitrary reserve allocations of 10% for substandard credits and 50% for doubtful credits are sufficient.

Presently, the method preferred by regulators to evaluate the loan-loss reserve has three primary components. The first is based on estimating the amount of potential loss applicable to specific, adversely classified loans. For classified loans where no loss estimate can be made, the second component — an estimated loss ratio for each type of loan based on the preceding five years, or a shorter period if considered acceptable — is used.

The final element relates to nonclassified loans. With this method, the potential loss reserve is estimated by using the average ratio of nonclassified net charge-off loans to nonclassified loans for the past five years.

Any examination can be successful if the bank staff demonstrates it has identified its loan problems and has attempted to solve them, while acknowledging that some potential loss exposure exists. The lending-function evaluation is a subjective review, and if a bank can document its preparation efforts for the examination, it can help regulators formulate their conclusions. • •

• **Susan Goold** has been promoted to director of information services by the National Automated Clearing House Association. Barbara Hill has been named manager of meeting services.

• **Joan P. Cronin** has been named general counsel/secretary for the St. Louis Fed. She succeeds F. Garland Russell Jr., senior vice president/general counsel/secretary, who retired.

• **Kevin M. Blakely** has been appointed director for special supervision at the Office of the Comptroller of the Currency. He heads the office that monitors troubled national banks.

• **Charles F. Hoffman** has been named director of the ABA Stonier Graduate School of Banking, succeeding William H. Baughn, who served as director for 20 years.

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LOAN OFFICER — Michigan banker handles commercial and ag loans. Ref. says, "He turned things around in this bank." BS Bus. $33-$35,000.
FORMER BANK EXAMINER — Strong at credit analysis. Manages rural bank. "Learns easily . . . gets along with others," says ref. BS Finance. $30-$35,000.
SENIOR LOAN OFFICER — 14 yrs. ag credit with same employer. "Thorough, detailed, persistent," reports ref. $32-$34,000.
AG/COMMERCIAL LENDER — Five yrs. bank exp. Good collector. "Very good credit analyst," says ref. BS Ag $25-$28,000.
agri CAREERS, INC.
AG BANKING PERSONNEL SPECIALISTS
Jean 712/779-3567, Massena, Iowa 50853
Sandi 515/394-5827, New Hampton, Ia. 50659

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NEW PRODUCTS/SERVICES

Use the Reader Inquiry Service on facing page to obtain further information about the products reviewed on this page.

• **Marsh Chalkboard Co.** is offering its contemporary conference cabinet designed to complement the modern office environment. It features bull-nose edges and measures (closed) 48″x48″x4¼″. Cabinet doors open to give a 48″x96″ visual communication work center.

For information, circle 116

* * *

• **Murata Business Systems** offers its ImageMate™ facsimile machine. It transmits a page to another Murata machine in less than 18 seconds and can perform up to 10 delayed dialing commands, according to the firm. The compact machine measures 16″x5″.

For information, circle 117

* * *

• **Panel Concepts** has introduced its Series One Operational Chair that's tailored to support users of video-display terminals and other keyboard tasks. It has a medium-low back and gives concentrated postural support along with comfort during extended periods.

For information, circle 118

* * *

• **Financial Technology, Inc.**, offers Banc Planner, which is available in three levels. Level I provides for interest calculations, rate-sensitivity analysis, "what if" simulations and management reporting. Level II provides for A/L management and gap analysis, funds pools and a funds-matching matrix, plus Level I features. Level III provides more sophisticated A/L management features, including amortization and repayment assumptions, ARMS, re-invested interest and others.

For information, circle 119

* * *

• **Triton Systems, Inc.** offers ATM jr.™, a series of desk-top demonstrators that duplicate the operation of a number of ATMs on the market. They are designed to bring live ATM demonstration capability to the desks of customer sales reps.

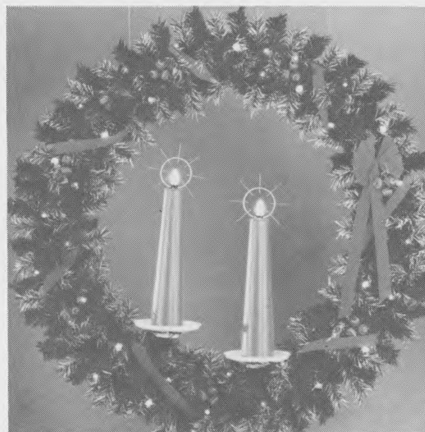
For information, circle 120

• **Krueger, Inc.**, offers add-on arms for its 2005 task chair that convert the chair to an armchair model for use by managers/supervisors. The arms permit chairs to be positioned close to desks or workstations.

For information, circle 121

* * *

• **General Plastics Corp.** is offering single-face Pine-Glo wreaths for building-front displays for the holiday season. They are available in eight, five and three-foot circumferences and come in various colors and feature red ornaments, ribbons, bow and centerpiece candles and bells. Wreaths for pole mounting also are available.



For information, circle 122

• **Diebold, Inc.**, has introduced a new design for vault doors that provides better security than conventional doors, according to the manufacturer. The Rotary Wedge-Lock Vault Door is made of a specially formulated material that is reinforced with steel. It's 16″ thick and has high p.s.i. compression strength. A wedge device prevents the door from being forced open.

For information, circle 123

* * *

• **Durham Manufacturing Co.**, is offering two policy/security boxes with three-digit combination locks that can be set without tools. Custom name plates or silk-screened personalization are available.

For information, circle 124

* * *

• **Hamilton Safe** offers modular vault panels said to be light enough to be installed on the upper floors of many buildings. The panels feature 15-, 30- and 60-minute U. L. ratings against forced entry. The vaults are relocatable, according to the manufacturer.

For information, circle 125

* * *

• **MMF Industries** is offering a new Key Control Catalog. The catalog is designed to aid the buyer of key-control products by illustrating how the various systems operate. The line includes single- and two-tag systems in cabinet, rack, keyboard and drawer styles.

For information, circle 126

* * *

• **Republic Money Orders Inc.** offers its electronic Republic Money Order Dispenser. The device is designed for use in supermarkets, bank lobbies, chain stores and malls. Features include increased speed/accuracy; elimination of in-store and back-office paperwork; and prevention of loss through a built-in security system that disables the unit if unauthorized use is attempted.

For information, circle 127

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Reader Response Page

October, 1986

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110 111 112 113 114 115 116 117 118
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Coming Events

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

Oct. 26-30: **ABA National School on Human Resources,** University of Colorado, Boulder.

Nov. 16-19: **BAI ATM9, Electronic Delivery Systems Conference,** Bonaventure Hotel, Los Angeles.

Nov. 16-19: **BMA Trust and Personal Financial Services Marketing Conference,** Sheraton New Orleans Hotel.

Nov. 16-19: **ABA National Ag Bankers Conference,** Opryland Hotel, Nashville.

Dec. 3: **NACHA Corporate Cash Management Seminar,** Airport Sheraton Grand Hotel, Dallas.

Jan. 27-30 **ABA National Security and Risk Management Conference,** Sheraton Harbor Hotel, San Diego.

Feb. 15-18: **BMA Community Bank CEO Seminar,** Marriott's Mountain Shadow Resort, Scottsdale, AZ.

Feb. 22-25: **BMA Electronic Banking Product Strategies Conference,** Phoenix Hilton.

March 8-11: **ABA National Conference for Community Bankers,** Hyatt Regency and Hilton, Phoenix.

March 15-18: **NACHA Annual Conference,** Intercontinental Hotel, San Diego.

April 1-5: **Independent Bankers Association of America Convention,** Marriott's Orlando World Center.

April 9-12: **Louisiana Bankers Association Convention,** New Orleans Hilton.

May 7-9: **Oklahoma Bankers Association Convention,** Shangri-La Resort, Afton.

May 11-14: **Alabama Bankers Association Convention,** Colonial Williamsburg, Williamsburg, VA.

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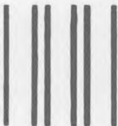

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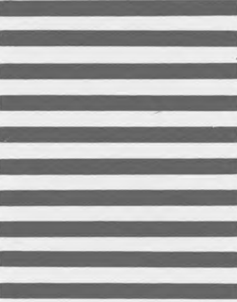

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