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2022

Meet Your Chairman

Jim King,
Bank of Monroe

The 128th Annual WVBankers Convention Recap

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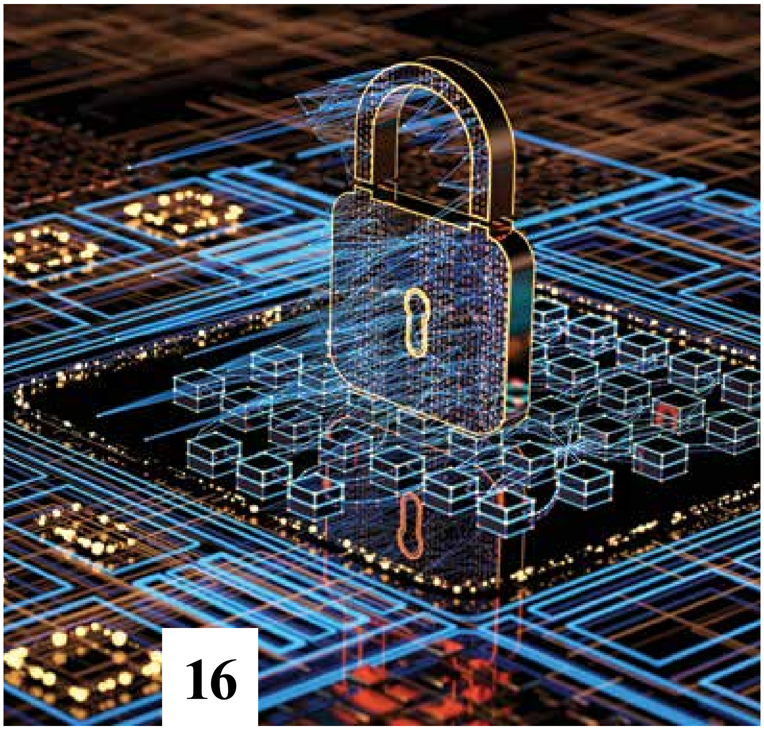

THE newsLINK group

President's Message

Association Focus

By Sally Cline, President and CEO, WVBA

At our recent 128th Annual Meeting and Convention, I was given an opportunity to speak, and I chose to highlight all we have accomplished together over the past six years. Because our organization is member-driven and member-inclusive, ALL should be aware of our successes. I have therefore decided to use this space to share an excerpt of my comments:

Your Association continues to perform well and is financially strong. We continue to be successful by focusing on improved operational efficiencies, reduced and controlled overhead expenses, and a renewed attention on the for-profit subsidiary. Successes in each of these areas resulted in board approval to decrease the 2021 dues assessment rate by 10%, as well as a $5,000 reduction in the dues cap, or the maximum amount of dues paid by any member bank. We continue to work toward further dues reductions as we move forward.

Operational efficiencies were realized in 2019 when we moved from an in-house IT system to an outsourced managed service solution allowing staff to focus attention on our core objectives of professional development, advocacy, and communication. The IT vendor selected through an RFP process has the experience and depth to deliver what we need to not only keep our operating systems protected and performing well but also allow us to operate more efficiently, both in terms of work processes and costs.

Similarly, we have identified a better solution to help with Association management and add value to our organization by creating efficiencies in workflows. This new tool will help us to better focus on increasing member engagement and identifying opportunities for non-dues revenue. We plan to migrate to that system later this year. Because the new solution will allow us to discontinue existing vendor contracts, we will be able to save almost $8,000 per year, representing 5% of total operating expenses.

Overhead expenses were reduced in 2017 when we relocated our offices, saving almost $30,000 per year, and

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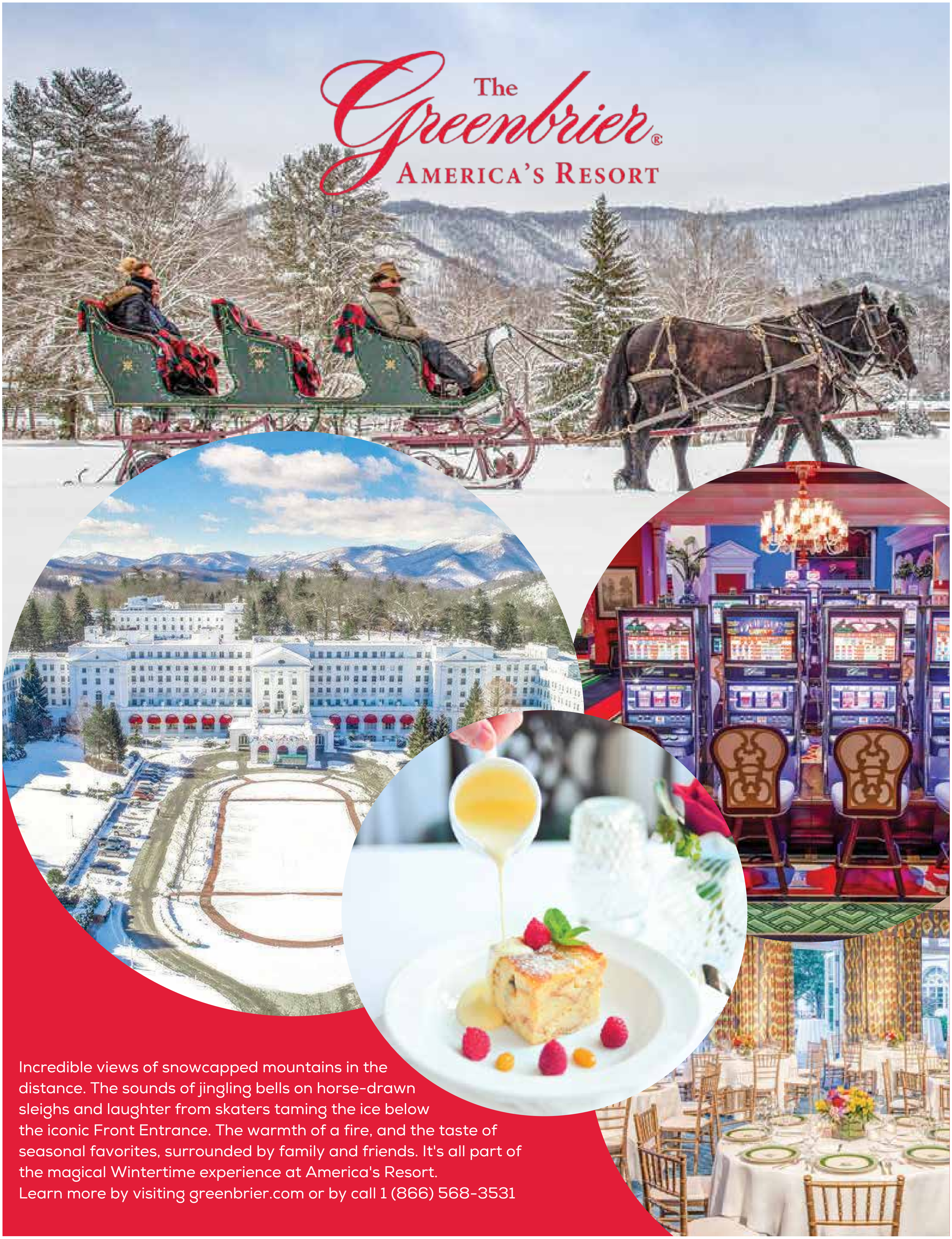
we have reduced salaries and benefits by downsizing from six full-time staff members to five as of Oct. 1, 2020.

A renewed emphasis has also been placed on our for-profit subsidiary. The company was formed in 1999 to develop, maintain and provide access to high quality products and services that benefit our member banks and support day-to-day bank operations. The corporation is governed by a Board of Directors who is responsible for screening and approving vendors that best meet the needs of Association members. All endorsed partners must demonstrate the benefits of aggregate buying power, direct member discounts, expense reduction and/or revenue enhancement to receive our seal of approval. Since I took over the CEO position in 2016, the for-profit board has approved the endorsement of four companies and the company's gross revenues have increased 108%.

Advocacy on behalf of the industry is, and always will be, a top priority of your Association. Since 2016, the Association has advocated for 24 bills signed into law that were favorable to the banking industry. Our success is due in large part to increased participation by West Virginia bankers in grassroots activities such as our annual Legislative Day Event and Calls to Action. Legislative successes are also attributed to increased participation in WVBankPAC, the Association's political action committee. Contributions to WVBankPAC continue to grow, 50% since 2016, and we could not be more thankful. WVBankPAC allows us to directly contribute campaign dollars to those legislative candidates who are pro-business, pro-growth, and understand the importance of a strong banking industry.

Looking back over my six-year tenure as your Association's CEO, I am proud of our accomplishments. The Board and I are aware that to stay on a path of success, the Association must be nimble and willing to change with membership change amid an industry that continues to consolidate and grow geographically. Our future success will depend on our ability to recognize and create a value proposition that changes with member needs. With the support and direction of both Boards of Directors, we are up to the challenge.

You will be pleased to know that during our annual meeting, the Board of Directors again voted to reduce bank member dues. Effective May 1, 2023, the dues assessment rate will decrease 17% and the dues cap will decrease $10,000. Again, this is a huge accomplishment made possible by focusing on improved operational efficiencies, reduced and controlled overhead expenses, and a renewed attention on our for-profit subsidiary. Thank you for your belief in our organization and all that you do to help us be successful. ■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Meet Your Chairman

Jim King, Bank of Monroe

The West Virginia Banker's Association is happy to introduce its members to our Chairman, Mr. Jim King of The Bank of Monroe. His charm and candor, along with his vast banking experience, make him an excellent selection as chairman, and we believe you will enjoy this interesting interview he graciously provided for us.

How did you start your banking career?

My dad was a vice president and director at Greenbrier Valley Bank, so I grew up surrounded by the profession and its people. My actual career began as a bank examiner with the State of West Virginia. After a three-year stint, I accepted a position with One Valley Bank in Greenbrier County. Shortly after One Valley was acquired, I was recruited by Tom Bulla to come to First National Bank, where I spent nine years before returning as a bank examiner in 2010. In January 2013, I accepted a position at The Bank of Monroe, then became President in October of that year.

Are there any individuals who had a major impact on your career?

As I mentioned, my dad was a career banker and a great person and role model, but as far as other people enhancing my career, I would say Tom Bulla was very instrumental in helping me during my time working with him and even through his retirement. I also have to mention Sally Cline. She and I met when I was a bank examiner the first time, and she provided great assistance and guidance years later by allowing me to return to my position as a bank examiner to reset my personal life and career path. She has been a great friend and ally over the years. Lastly, knowing and having a personal relationship with Jack Rossi since I was a child has also greatly benefited me.

What is the best professional advice you have received?

I don't know of any particular piece of advice that stands out, but I have learned much about the ins and outs of the profession through my affiliation with West Virginia Banker's Association and our Top Net group. It has allowed me to develop a network of peers and friends I can rely on for leadership and advice.

What has been the most rewarding part of your career?

Being allowed to lead a community bank in the town where I grew up has been a great honor. Also, helping people obtain a loan can be the most rewarding thing you can do. I have had people come to me years later thanking me for helping get them started in life with a first loan or first home loan.

What do you think will be some of the dominant trends in the banking industry over the next five to 10 years?

Bankers will need to adapt to all types of digital presence and find ways to serve customers more efficiently and effectively. The self-checkout method implemented by Walmart will spill into our industry at a more rapid pace. Partnerships with fintech companies will be essential, as will branch transformation. I believe there will be additional bank consolidation, but I am not convinced it will be for the betterment of service and the communities we serve.

Why is being a member of the WVBA important?

We are a voice for West Virginia bankers on both state and national levels. Bankers must have a voice at the Capitol; we provide that through our WVBankPAC and the Association. My involvement with the Association has also allowed me to be active with the American Bankers Association's Community Bankers Council and the Federal Reserve Bank's CDIAC group, where I have been able to meet with and learn from President Tom Barkin and other community bankers in the Fifth District.

How long have you been active in the West Virginia Bankers Association?

I became president of The Bank of Monroe in October 2013, and shortly thereafter, Joe Ellison stopped by to talk about the Association and offered me a spot on the Board. I was overwhelmed with the role I had been put in, but his invitation was truly an honor I gladly accepted.

We are a voice for West Virginia bankers on both state and national levels. Bankers must have a voice at the Capitol; we provide that through our BanPac and the Association.

What are you looking forward to most as the Chairman of the WVBA?
I look forward to working with the board, expanding our presence with our state leaders, and ensuring West Virginia banks continue to have a voice. I have also been tasked, along with other members of our Board, with finding a new leader for the organization, which will be extremely important for our future.

Do you have any advice you would give emerging leaders in the banking industry?
Be adaptive to change, never quit educating yourself, find a peer networking group, and enjoy what you do.

Tell us your favorite memory or experience of your career.
No one particular memory stands out, but as I mentioned before, helping someone purchase a home is at the top of the list. I also enjoyed my time as a bank examiner, which for better or worse, allowed me to see how other bankers operated, which greatly benefited my career. My most rewarding experience was working with FHLBank Pittsburgh to develop a grant program to help flood victims finance new homes after the devastating floods of 2016. I was given an award in 2017 by the Affordable Housing Advisory Council by FHLBank Pittsburgh for The Bank of Monroe's involvement in the aftermath of the floods.

What is something about you that might surprise fellow bankers?
I learned from my mother and grandmothers the art of cooking and canning, and with my Blackstone and Pitt Boss, I have expanded my craft to the expense of my waistline. I probably think I am a better cook than I am. I also own a John Deere track loader and enjoy cutting brush with it at our farm.

Tell us about your family. And do you have any special interests or hobbies or contribute to any specific charitable organizations?
Linda and I have been married for 29 years and have three children, Griffin, 25, Karly, 23 and Kyle, 20. For 20 years, our days and nights were spent on ball fields or dance competitions, but now we stay at home a lot more with my grand-dog Kate, our English Setter. We have a 240-acre farm in Greenbrier County that we own with my family Jim and Jean King and my sister Kim has a house on the property. The farm is used mostly for growing an abundance of deer and turkey and other wildlife for hunting purposes, as well as providing a place to shoot skeet and our other guns. I spend fall Saturdays with football, usually making the trip to Morgantown to attend a WVU game or watching college football on TV. At one time, I was an avid golfer, but banking got in the way of that. Hopefully, I can start back again soon.

What advice would you give someone considering entering the banking industry?
There are so many paths you can take, and I recommend you explore several areas to see where your skillsets lie. If you are in college, I would do what I could to obtain an internship. I also believe that being a bank examiner or auditor can give you a leg up as you see so many different banks and methods of doing things. The training provided by the banking agencies is second to none. I credit that advanced training to much of my success over the years. ■

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The 128th Annual WVBankers Convention Recap

Nearly 300 industry professionals gathered for the 2022 WVBankers Annual Convention held July 24–27 at The Greenbrier in White Sulphur Springs, WV. WVBankers is incredibly grateful for our attendees, sponsors, speakers, exhibitors and the remarkable staff at the Greenbrier for making this event possible. Attendees came together for three days to learn, make new connections, and continue moving the banking industry forward. We hope to see you next year, to learn more please visit www.wvbankers.org/convention.













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Cybersecurity Is Everyone's Responsibility

By Nicholas P. Mooney II and Alexander L. Turner, Spilman Thomas & Battle, PLLC

A recent survey by PricewaterhouseCoopers (PwC) revealed that U.S. executives now consider cyberattacks the number one risk their companies face. Concerns about cybersecurity have moved beyond the Chief Information Security Officer (CISO) to the entire C-suite and corporate boards. Recent developments show executives are right to worry about those attacks because they can result in monetary loss, personal liability, and reputational risk.

Litigation & Governmental Action

Cyberattacks that result in data breaches often lead to litigation, but courts have been quick to dismiss lawsuits when the plaintiff complains only of a fear of identity theft or some other type of future harm. In those instances, courts have held that those plaintiffs lack the required injury-in-fact that conveys standing to bring a lawsuit. Courts also have held that companies are not required to absolutely protect customers' and employees' personally identifiable information (PII) but that they only need to take "reasonable" steps to protect the data they maintain.

On the other hand, there is a real concern regarding possible governmental action if it is determined that officers and board members failed to take necessary steps to secure their companies' computer networks. The Consumer Financial Protection Bureau (CFPB) recently stated that financial institutions may be in violation of the Consumer Financial Protection Act (CFPA) if they fail to take adequate measures to safeguard consumers' data. The CFPB stated that financial institutions should implement multi-factor authentication, adequate password management, and timely software updates. Although the CFPB did not require financial institutions to implement these recommendations, it did state that failure to implement these simple suggestions could trigger liability under the CFPA.

Reducing Risks for the Company

The lack of a comprehensive federal cybersecurity law complicates the ability of CISOs to take steps to reduce the risk of a lawsuit or governmental action. Nonetheless, there are several steps they can take to reduce these risks:

- Implement protocols and procedures that protect the company's IT infrastructure from attack. These protocols and procedures include:
  - Mandatory employee training on preventing the disclosure of sensitive information
  - Third-party cyber assessments for all vendors
  - Segregation of sensitive information and requiring additional authentication to limit access to that information
  - Routine checks for new risks to the IT system
- Be aware of the details of the company's privacy policy and ensure the company is actually taking the steps to implement its promises to protect PII.
- Be current with industry-specific laws and regulations that address data breaches and the required notice provisions to ensure those procedures and deadlines are included in the data breach response plan.
- Communicate potential risks and breaches timely to upper management and the Board of Directors so they can take appropriate actions to address those risks and breaches.

Working as a team to secure customers' data will reduce the liability of directors in the event of a data breach.

- Ensure the company's data breach response plan is strictly adhered to in the event of a breach.
- Retain counsel experienced with handling data breaches and cybersecurity litigation to help guide the CISO through the breach response process.

Implementing these policies and procedures, along with the CFPB's recommendations, should help stave off enforcement actions by federal and state regulators in the event of a data breach or ransom attack, in addition to lessening the risk of civil litigation.

Reducing Personal Risks for the C-suite & Boards of Directors

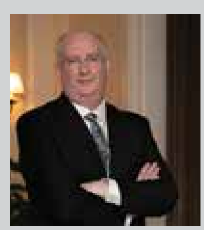
Another concern is that officers and directors risk being personally named in lawsuits brought by customers whose personal data was exposed as a result of the breach and by shareholders against the financial firm. CISOs have immediate responsibility for a company's cybersecurity, and they would likely be the first target for a plaintiff looking for officers to name personally in a lawsuit. But, in the past ten years, plaintiffs have tried to hold C-suite executives and company directors personally liable. These classes of plaintiffs likely will allege that the officers breached their fiduciary duty to protect the plaintiffs' personal information or that they unnecessarily exposed the company to liability. If the lapse in cybersecurity can be shown to result from the director's failure to properly prepare for cyberattacks, there is a narrow path for aggrieved parties to hold directors personally liable: a plaintiff must prove that (1) the board of directors made a decision that resulted in a loss because that decision was ill-advised or negligent, or (2) the board failed to act in circumstances in which due attention would, arguably, have prevented the loss. Attentiveness to known threats and taking reasonable actions to counter those threats will provide strong defenses against personal liability claims against officers and directors.

There are many steps officers and directors can take to reduce the likelihood that they are held personally liable after a cyberattack or data breach. They include:

- Ensuring the directors have sufficient cybersecurity training.
- Conducting regular discussions about cybersecurity as part of board meetings.
- Overseeing the implementation of cybersecurity protocols.
    - This can include the adoption of quantum computing and quantum-resistant encryption, zero trust security, and zero-knowledge proofs. Quantum computing and quantum encryption can generate truly random numbers for encryption keys, which prevents hackers from cracking the company's encryption. Some privacy laws incentivize encryption, like the California Consumer Privacy Act, by stating that a company's failure to encrypt personal information can result in a direct cause of action by customers in the event of a data breach. Zero trust security is used to mitigate the danger of an insider threat by requiring all users and devices attempting to access the network to verify their identity. Zero-knowledge proofs use a blockchain to protect data transmitted over the Internet.
- Regularly review the status of the company's cybersecurity protocols to ensure they are up to date.
- Ensure the company's IT department is vigilant and actively monitors the status of the company's computer network.
- Require regular reports from the company's IT department and conduct regular communications with that department regarding potential threats to the network and steps to be taken to protect the data the company maintains.

Working as a team to secure customers' data will reduce the liability of directors in the event of a data breach.

The PwC survey shows that cybersecurity issues are front-and-center in U.S. executives' minds. The above-referenced recommendations may not stop all data breaches, but by enacting them, your financial institution will significantly lower the likelihood of litigation after a data breach. Putting these recommendations into service also will help keep the regulators at bay. If litigation or governmental action cannot be avoided after a cyberattack, implementing these recommendations increases the likelihood of a favorable outcome.

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Will the Federal Reserve Sell MBS?

By Andrea F. Pringle, The Baker Group

This question is likely to garner different responses, depending on whom you ask, and a plethora of caveats. It is a tough call for the Fed because stifling housing-related inflation without punishing everyday homeowners is a tricky task. For investors, this question matters a lot because the Fed's cessation from active Mortgage-Backed Securities (MBS) purchases eliminated demand from the largest buyer in the market and had a punitive impact on MBS valuations. If the Fed starts actively selling into the market, that could exacerbate things even further.

Why Sell?

There is a solid case to be made for selling MBS because the Fed has repeatedly conveyed its desire to hold a portfolio of predominantly Treasury securities. It has already stopped active MBS purchases as part of Quantitative Easing (QE) and is allowing the amount of MBS that naturally runs off its portfolio through principal pay downs to increase over time. Unfortunately, this may not be enough to get to a Treasury-only portfolio.

With mortgage rates nearly double the historic lows set over the past couple of years, virtually all existing mortgages have lower rates than those available today. As a result, refinance – and even purchase activity – has slowed dramatically. As high mortgage rates disincentivize people from refinancing and moving, mortgage balances are being paid down more slowly, and the resulting runoff of the Fed's MBS balance sheet is happening more slowly as well. In fact, the maximum runoff caps set by the Fed to facilitate a gradual removal of its footprint likely will not even be reached through natural paydowns.

The Fed announced plans to gradually and predictably reduce its securities holdings by setting caps on the amount of MBS and Treasury paydowns reinvested in those securities. This process began in mid-June with an initial monthly cap of $17.5bn MBS for the first three months, which shifts to $35bn/month in September. However, with prepayments slowing in response to higher primary mortgage rates, the Fed's playdowns are already running below the planned maximum $35bn cap. In other words, organic MBS portfolio reduction will be much slower than the Fed wants.

To make matters worse, the Fed's Treasury holdings do not have this problem. The cap for Treasury securities was initially set at $30bn/month and shifted to $60bn/month in September. Because Treasury securities are not plagued by slowing prepayment activity like MBS, principal pay downs of Treasuries will be able to hit the full $60bn/month cap much more efficiently. This dynamic will cause the share of MBS in the Fed's portfolio to increase relative to Treasuries rather than decrease.

Additionally, a large part of the Fed's targeted Consumer Price Index (CPI) measure considers rental and housing costs.

The Fed announced plans to gradually and predictably reduce its securities holdings by setting caps on the amount of MBS and Treasury paydowns reinvested in those securities. This process began in mid-June with an initial monthly cap of $17.5bn MBS for the first three months, which shifts to $35bn/ month in September.

In order to rein in inflation, shelter prices as a component of CPI need to come down. Over the long term, shelter prices in CPI tend to follow trends in home prices, which have yet to slow materially despite higher mortgage rates. This suggests shelter prices could remain strong until at least mid-2023. Thus far, the Fed has only attempted to control this by raising interest rates, but pervasively high shelter costs could put pressure on the Fed to take further action to bring down CPI.

Why Not?

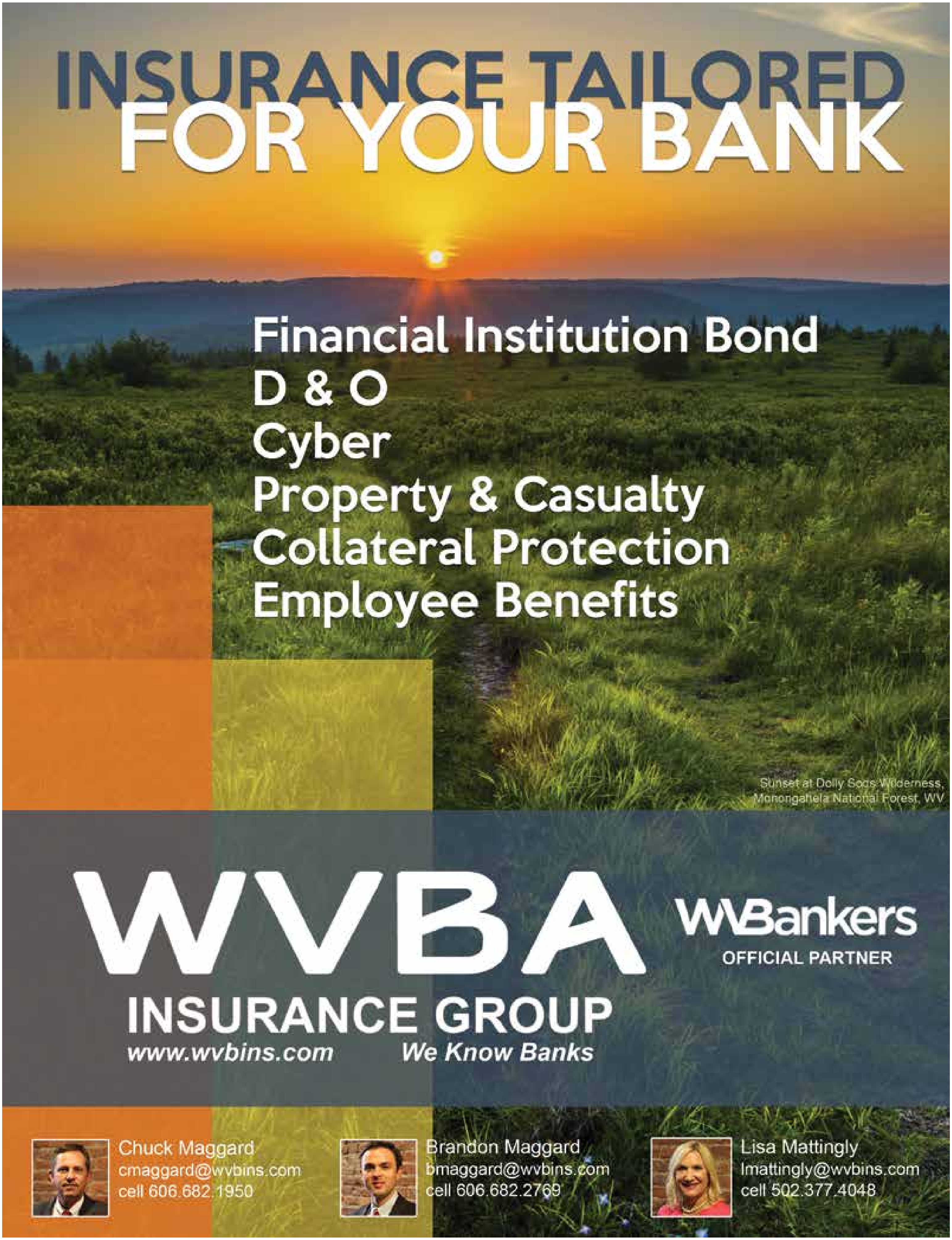
While the case for MBS sales may seem strong on the surface, the Fed has a delicate tightrope to walk to avoid overly burdening homebuyers/homeowners and significantly distressing the broader housing market. It takes time for rate hikes to actually cool inflation, so selling MBS may not do much to directly impact housing inflation in the near term. We are also starting to see the beginnings of a slowdown in housing activity, so taking further action now may be an unnecessary step.

Fed action has already worked to nearly double borrowers' mortgage rates at a time when home prices are also extraordinarily high. The combined effect of both dynamics has made it almost twice as expensive to buy the same house today as it was just two years ago. Consequently, some would-be homebuyers simply give up the search and are forced to rent instead. This serves to increase demand for rental housing and further raise the price of rentals. It follows that increasing mortgage rates when rental supply is already limited might actually have the effect of temporarily increasing housing inflation rather than decreasing it. Potentially worsening an already difficult housing affordability dynamic may give the Fed pause about pursuing MBS sales too soon.

Additionally, the MBS purchased by the Fed during the last round of QE was made up of mortgages with much lower rates than today. As a result, if the Fed were to start selling its holdings now, it would impact the supply of very low-coupon MBS. There would be relatively little effect on the price of higher-coupon MBS, which sets the secondary market for mortgages originated today. In other words, Fed sales of MBS would likely have a rather minor impact on thirty-year mortgage rates today.

Whatever course the Fed will take regarding MBS sales is anybody's guess. It seems prudent to err on the side of caution and refrain from outright sales in the near term to give its previous actions some time to work. If the slowdown in housing activity that appears to be underway now sticks, further action may be unnecessary. But if housing-related inflation becomes incessant, the Fed may have to resort to any means necessary to temper it.

Andrea F. Pringle is a Financial Strategist and MBS Analyst at The Baker Group. She began her career in Washington, DC, earning her MBA from George Washington University. Andrea worked on the Capital Markets Sales and Trading Desk at Fannie Mae for five years before returning to Oklahoma to work in corporate finance. Andrea joined The Baker Group in 2020, and her work focuses on mortgage products. Contact: 800-937-2257; apringle@GoBaker.com.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West Virginia Shortens Tax Sale Redemption Periods

By Amy J. Tawney & Sandra M. Murphy, Bowles Rice

In the 2022 regular legislative session, the West Virginia legislature significantly revised the process and timeline for redemption of real estate sold at a tax sale. The new law, effective June 10, 2022, overhauls the process for payment of property taxes, tax sales and redemptions with the goal of streamlining the process. It also amends the current statute to allow for payment plans and payment by credit card.

During the legislative session, the banking industry worked with the State Auditor's Office to ensure that the new legislation would incorporate specific requirements for the service of the notice of redemption included in the existing law to provide protection to real estate owners and lien holders. Although these specific notice requirements are included in the revised statute, the new law significantly shortens the timeline for redemption from a minimum of four months to 45 days.

Most financial institutions take proactive steps to address the risk presented by a potential tax sale. Many lenders roll property taxes into the borrowers' loan payments and then make the tax payments on behalf of the property owners. Some lenders require borrowers to establish escrow accounts for taxes or hazard insurance as permitted under the Real Estate Settlement Procedures Act. Other lenders include in their loan agreements that the failure to keep current on property taxes constitutes default of the loan and would allow the bank to demand immediate payment of the remaining balance. While these steps can reduce the risk that a tax sale will occur, they cannot prevent a tax sale from jeopardizing a bank's collateral position in all cases. In response to the new West Virginia law, banks should review their internal controls and procedures to consider the shortened time periods.

The new redemption procedure and timeline is set forth below:

Tax Purchaser Prepares List of Persons to be Served. Under WV Code § 11A-3-52, following the tax sale by the Auditor, a tax sale purchaser must prepare a list of interested parties to be served with a notice to redeem. This list must be prepared within 120 days following the

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tax sale, and the tax purchaser much deposit or offer to deposit with the auditor the costs of preparing and serving the notice. If the tax purchaser fails to meet these requirements, then it may receive an additional 60 days to comply if it requests a written extension within 30 days of the expiration of the time period and pays the greater of $100 or 10% of the amount paid on the date of sale plus a $25 extension fee.

Service of Notice to Redeem on Interested Persons. After the Auditor receives the list from the tax purchaser, it then prepares the notice to redeem and serves it on the persons named in the list. Both the real estate owner and the lien holder should be included in the list. WV Code § 11A-3-55 provides that the notice must be served by the Auditor within 30 days following the request for the notice from the tax sale purchaser. If the notice is served on persons residing or found in the State of West Virginia, then it must be served by the following means: (A) in the manner for service of process commencing a civil action, (B) by certified mail, return receipt requested or (C) by other types of delivery service courier that provide a receipt. The notice must be served in a similar manner on persons who do not reside in or cannot be found in the State of West Virginia.

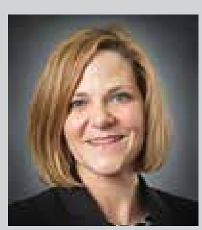
Publication of Notice to Redeem Where Address Unknown. If the address of a person is unknown to the tax sale purchaser and cannot be discovered by the tax sale purchaser, then the notice must be published as a Class III-0 legal advertisement and such publication must be commenced within 60 days following the request for the notice from the tax purchaser. If publication is necessary, then the notice must also be mailed to the last known address of the person to be served.

Service of Notice to Redeem on Occupants. If the real estate subject to the tax lien was classified as Class II property at the time of assessment, then the Auditor must also forward a copy of the notice to redeem addressed to the "occupant" of the property by mailing a copy of the notice by first class mail or in the manner provided for service of process commencing a civil action to the physical mailing address for the subject property.

Although the new requirements for service of the notice to redeem are similar to the prior law, the only time limitation relating to the issuance of the deed to the tax purchaser is set forth in WV Code § 11A-3-55, which provides that the notice must be mailed and, if necessary, published by the Auditor **at least 45 days prior to the first day that a deed may be issued to the tax purchaser.** Under the prior law, the tax deed could not be issued before April 1 of the second year following the sheriff's sale of the property. Because this time period was set by statute, it provided property owners with a minimum of four months to receive notice of the right to redeem and to gather the funds to redeem the property.

Most financial institutions take proactive steps to address the risk presented by a potential tax sale. Many lenders roll property taxes into the borrowers' loan payments and then make the tax payments on behalf of the property owners. Some lenders require borrowers to establish escrow accounts for taxes or hazard insurance as permitted under the Real Estate Settlement Procedures Act.

The notice to redeem issued by the Auditor should include the date after which the deed to the tax purchaser will be made if the owner of the real estate fails to redeem by that date, presumably 45 days from the date notice is sent since that is the earliest date the deed to the tax purchaser can be issued under the new law. However, the property owner and the bank may not receive the notice to redeem for a week or so, depending on the timeliness of the mail delivery, or may not see the notice published in the newspaper. This means that the real estate owner could have less than 45 days to redeem the property. Banks should review their internal procedures and consider this shorter redemption period when assessing the impact of the new law. ■



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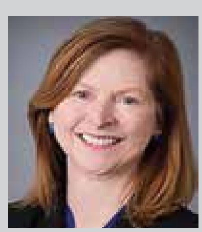

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The Battle for Deposits Is Heating Up: Are You Ready?

By Achim Griesel and Dr. Sean Payant, Haberfield

Core deposits, especially low-cost ones, have long been the key driver for franchise value in the financial services industry. That said, with the start of the pandemic and the ensuing influx of cash from stimulus checks and increased personal saving rates, financial institutions saw so much excess liquidity that bankers began to question the value of any deposits, including low-cost core deposits.

Total deposits in FDIC-insured banks grew by over five trillion from the end of 2019 to the end of 2021. In the two years prior, deposits had grown just over one trillion. These same trends on a smaller scale held true for credit unions.

Peak deposit growth happened in 2020. By September 2021, the personal saving rate was back at pre-pandemic levels. Deposits at financial institutions continued to grow, but at a much slower rate than in 2020. Finally, starting in March 2022, the data showed that personal checking account balances dropped for the first time since Q3 2021.

Source: U.S. Bureau of Economic Analysis (fred.stlouisfed.org)

Strategically growing low-cost funding today is the key to successfully positioning your organization for tomorrow. Even if you have excess liquidity now, there isn't a better time to grow low-cost funding by growing your customer base and increasing your checking and savings deposits.

In addition, consumer spending is now soaring. According to a recent article in Bloomberg, the top four banks in the nation have seen a 27% average increase in consumer credit card spending for Q1 of 2022 vs. Q1 of 2021.

Inflation is at record highs, and Federal Reserve Chairman Jerome Powell indicated early in 2022 that multiple 50bp rate hikes should be expected in the remainder of the year; this actually translated into the most recent 75bp rate increase.

Unlike in previous rising-rate environments, financial institutions haven't, until recently, felt the same pressure to raise rates in light of the excess liquidity in the system. That said, financial services analysts expect deposit betas in the 25-50% range over the next two to three years. For financial institutions, that means passing on 25-50% of these rate increases to our depositors. That is significant, and the response will not be the same for all institutions.

Given this variety of possible responses, we anticipate seeing rate offers from financial institutions – most likely led by online and digital banks, with community-based financial institutions following at a slower pace and on a smaller scale. Assuming the bulk of this effort won't happen until late 2022, and beyond, the question financial institutions must ask themselves is, "What should we do ***now***?"

Institutions with low-cost and less rate-sensitive funding are well positioned for any rate environment, especially the one we are experiencing. The chart below illustrates the deposit cost advantage when a financial institution has a lower cost of funding. The rate environment we are entering is similar to what we saw in 2016–2018. As rates were rising, the deposit cost advantage over peers dramatically changed. In a low-rate environment, it was small but grew to 63bp when rates were at the level we expect to see again in late 2022–2024.

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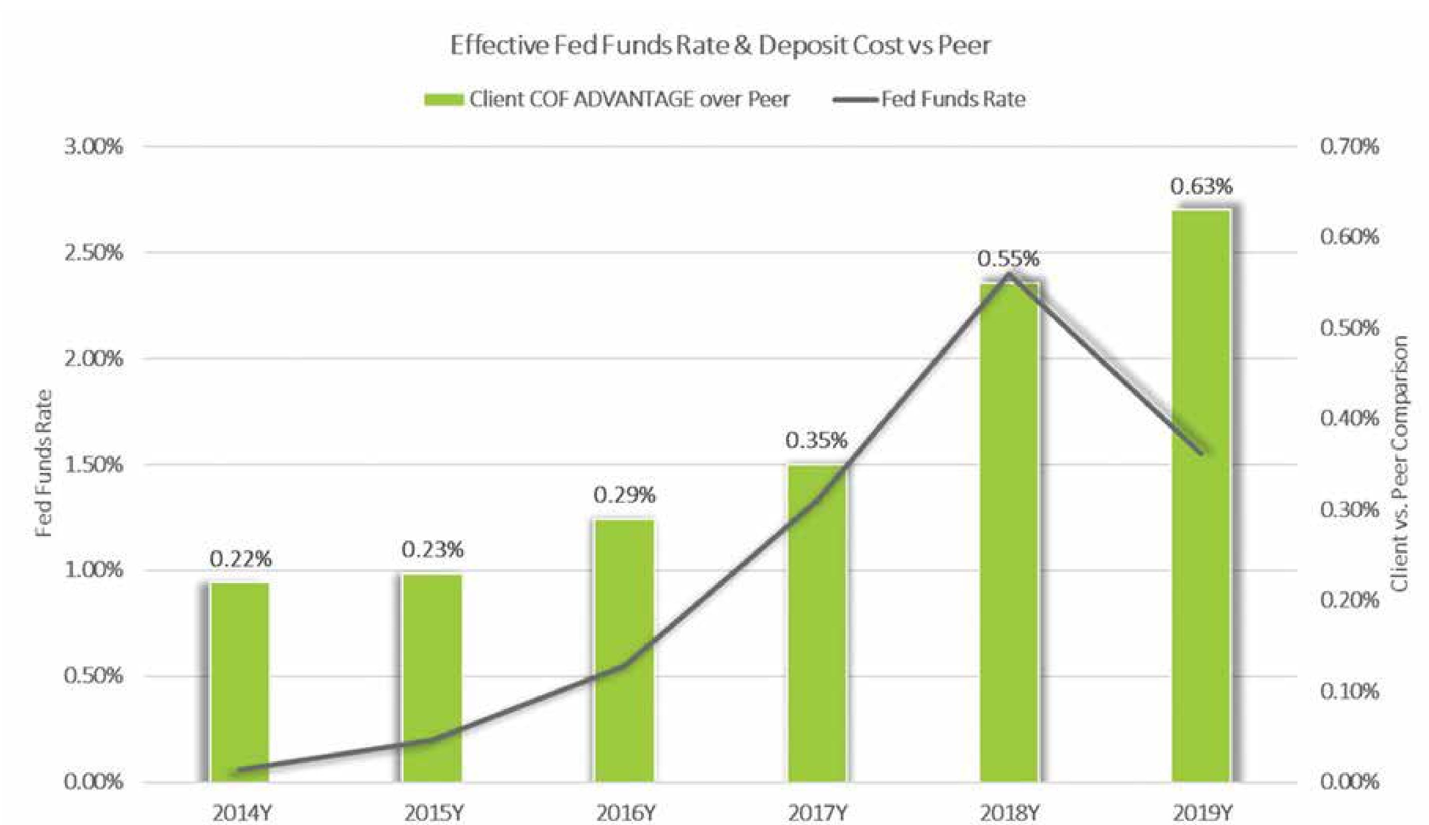

If your strategic goals include low-cost funding and a strong position in any rate environment, you must be intentional about growth. If you focus on growing core relationships, you will not have to follow other institutions up and down the rate cycles.

Continued from page 25

Strategically growing low-cost funding today is the key to successfully positioning your organization for tomorrow. Even if you have excess liquidity now, there isn't a better time to grow low-cost funding by growing your customer base and increasing your checking and savings deposits. The majority of these funds will be non-interest bearing, and those that are interest bearing will be at the lowest rates.

To position your financial institution for the coming battle for deposits, it is imperative that you: (1) offer compelling retail and business deposit products; (2) remove barriers to growth (e.g., evaluate your Customer Identification Program); (3) use data-driven targeted marketing to reach high-probability conversion prospects; and (4) equip your employees with the skills to capitalize on every opportunity every time.

If your strategic goals include low-cost funding and a strong position in any rate environment, you must be intentional about growth. If you focus on growing core relationships, you will not have to follow other institutions up and down the rate cycles.

Achim Griesel is president, and **Dr. Sean Payant** serves as the chief strategy officer at Haberfeld, a data-driven consulting firm specializing in core relationships and profitability growth for community-based financial institutions. Achim can be reached at 402.323.3793 or achim@haberfeld.com. Sean can be reached at 402.323.3614 or sean@haberfeld.com.

NSF Fees:

Prepare for a new regulatory focus

By Mark Mangano, Jackson Kelly, PLLC

Financial institutions have long assessed customers a nonsufficient funds (NSF) fee when a check or Automated Clearinghouse (ACH) transaction is presented for payment on a customer's account, and the customer has insufficient funds in the account to pay the check or ACH. There is little regulation related to NSF fees, and the regulatory review standards related to the NSF process have long been stable. However, the regulatory approach to NSF fees appears to be changing.

On Aug. 18, 2022, the Federal Deposit Insurance Corporation (FDIC) issued "Supervisory Guidance on Multiple Re-Presentment NSF Fees" (Guidance).[1] The Guidance articulates the FDIC's focus on re-presentment NSF fees. Re-presentment occurs when a merchant or other payee in a transaction learns that a check or ACH has been declined and resubmits the check or ACH for payment. The Guidance addresses potential risks related to multiple re-presentment fees, suggests risk mitigation practices, and articulates the FDIC's supervisory approach.

> *The FDIC will consider a bank's proactive efforts to self-identify and correct violations in determining whether to cite a bank for unfair or deceptive practices.*

Potential risks from multiple re-presentment NSF fees

The FDIC identifies three primary risks related to re-presentment practices: consumer compliance, third party, and litigation.

- **Consumer compliance**
  The primary consumer compliance risks identified in the Guidance are the potential violation of the subjective standards for "deceptive practices" and "unfair practices" defined in Section 5 of the Federal Trade Commission (FTC) Act. The Guidance also identifies the potential for "abusive" acts or practices defined in Section 1036(a)(1)(B) of the Dodd-Frank Wall Street Reform and Consumer Protection Act of 2010.

Evaluating compliance will begin with assessing the bank's disclosures related to re-presentment NSF fees. However, the Guidance suggests that unfairness violations may be found even if the disclosure is not found to be deceptive.

- **Third-party risk**
  The FDIC acknowledges that third parties, including core processors, may be deeply involved in identifying and tracking re-presented items and providing systems that determine NSF fee assessment. The FDIC stresses that responsibility for the third-party vendor remains with the bank. Banks are encouraged to review the third-party vendor NSF processing settings and the vendor capability to identify and track re-presented items.

- **Litigation risk**
  The Guidance notes that some FDIC-supervised institutions have faced lawsuits alleging breach of contract and other claims because of alleged failures by an institution to adequately disclose re-presentment NSF practices in account disclosures. The associated costs have been customer restitution and legal fees.

Risk Mitigation Practices

The Guidance recommends that banks review their practices and disclosures related to charging NSF fees for re-presented transactions. The Guidance also details a list of mitigation measures banks may consider in reducing the risks of consumer harm and potential violations of law related to multiple re-presentment NSF fee practices.

FDIC's Supervisory Approach

The Guidance states that the FDIC's supervisory response to re-presentment of NSF practices will focus on identifying related issues and ensuring both correction of deficiencies and remediation to harmed customers. The FDIC will consider a bank's proactive efforts to self-identify and correct violations

in determining whether to cite a bank for unfair or deceptive practices. The FDIC also indicates that its evaluation of whether a bank has met its remediation obligations will be based upon the bank's ability to retrieve, review, and analyze re-presentment data.

Conclusion

The Guidance suggests a supervisory emphasis by the FDIC in evaluating how NSF practices and procedures may present unfair or deceptive practices. While the Guidance does not have the force and effect of law and the recommendations contained therein are not mandatory, it does indicate how the FDIC proposes to enforce other laws. All banks, including those that have not changed their NSF practices since a prior satisfactory compliance examination, should expect that their NSF procedures will be scrutinized.

Banks should carefully consider the recommendations contained in the Guidance as they evaluate the risks associated with their NSF practices. Evaluating whether re-presentment NSF fee practices potentially violate regulatory standards may require examining many factors and exercising informed judgment regarding the subjective standards discussed in the Guidance.

[1] https://www.fdic.gov/news/financial-institution-letters/2022/fil22040a.pdf

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