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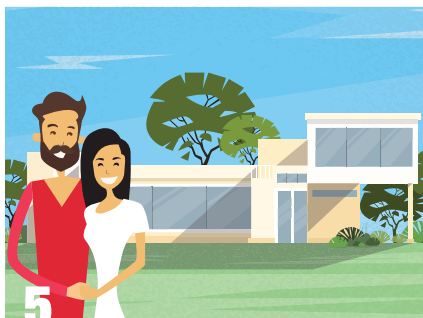
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MOST SHARED

Brokered Deposits Get a Bad Rap

It is time for regulators to rethink their notion of what constitutes a quality deposit portfolio, MainStreetBank's chairman and chief executive, Jeff W. Dick, wrote in a BankThink piece.



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How Citi 'Co-Creates' Innovative Apps

Yolande Piazza discusses Citi FinTech's unique process for getting customer feedback on new apps and the challenges of innovating inside a large company like Citigroup.



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Editor's Note

BY BONNIE McGEER

To lure talent, banks get more creative, generous

Though a slow economy proved burdensome for banks, an improving one presents its own challenges – particularly in recruiting and retaining staff.

“There’s a battle for talent,” says Timothy Reimink, a managing director in the financial services sector at Crowe Horwath.

Reimink has insight into personnel practices in the industry through Crowe Horwath’s annual survey of bank compensation and benefits. The firm has been doing the survey for 36 years, and released the latest results in September, with data compiled from 375 banks, most of them with less than \$5 billion in assets.

The survey shows salaries have been rising for several years across most types of bank jobs. Everyone from tellers to top retail banking officers has been getting raises.

Reimink expects pay to trend even higher, particularly since the majority of banks are looking to add employees in the year ahead. He says they might have to get more creative with how they go about attracting new hires, as the competition for people gets fiercer across many industries.

For the first time since the Great Recession, more than half of banks surveyed said they plan to increase overall staffing during the coming year – 42% through organic growth in their existing business and 13% through expansion. The number of banks that plan to maintain current staffing levels held relatively steady at 35%, which is near the lowest level in years.

Among the challenges is getting younger people to consider a job in banking – “which doesn’t seem particularly sexy and doesn’t necessarily seem like it’s helping solve world peace,” Reimink says.

One inventive way some banks are finding candidates is to recruit from other industries that have strong training programs.

The thought process about what makes someone right for a certain job is evolving – with a focus on the skills needed rather than on directly relevant experience. “They no longer think about it in terms of, ‘Well, I need to hire somebody who works at a bank,’ ” Reimink says.

He cites Enterprise Rent-A-Car as an example. The company likes hiring young people, training them in the Enterprise way, then promoting the best of them.

“There are certain people skills, certain sales skills, certain management skills that they develop,” Reimink said.

“And I know of some banks that have taken note – alumni of Enterprise Rent-A-Car have skills they would like to have in branch managers.”

Even as banks are looking to add staff, employee turnover rates have reached record levels, exacerbating the hiring needs. Turnover is at 7% for officers and 19% for nonofficers, the survey found. It’s the third consecutive year that banks reported an increase.

So banks are working harder on retention too, not only granting salary increases, but offering flexible work arrangements, improving paid-time-off programs and employee perks, and even changing how employees are evaluated.

About 20% of banks say that they’re pursuing an above-market compensation strat-

egy – a figure that has been trending up gradually from about 9% during the recession, according to Reimink.

Over the past 10 years, the number of banks with employee casual days has increased more than 18%. The number offering wellness programs is up about 8%, health club memberships more than 6%, and employee assistance programs – an employer-sponsored service designed to address personal or family problems – 6%.

“I wouldn’t call it a dramatic shift or a sudden shift,” Reimink says, “but you can see that banks have progressively loosened up their practices around dress, around hours, around flexibility.”

In what might be a shift to accommodate millennials – who tend to like frequent feedback on job performance – the annual review is becoming less common. “One of the things we see banks doing is focusing on their performance-review process and making it more meaningful to the employees, as well as to the bank achieving its objectives,” Reimink says. “Moving to less about the annual review and more frequent, continual review – and it’s really not so much review, it’s just conversations between the employee and their supervisor.”

But Reimink highlights at least one worrisome data point from the survey

The chief human resources officer is one of the few positions to see a decline in average pay in the past year – which he says is surprising and concerning given the heightened need to attract talent and reduce turnover.

It suggests some banks have yet to recognize the challenges posed by the tightening labor market. □

Briefings

LAW & REGULATION | MORTGAGES | SMALL BUSINESS



Homebuying Gets a Boost As Millennials Get a Break

More people with student debt qualify for mortgages, thanks to a policy change by Fannie Mae

By Laura Alix

A RECENT PUSH BY FANNIE MAE TO enable more millennials who are burdened by student debt to buy homes appears to be having its intended effect. Bankers said that they are finding it easier to qualify young homebuyers as a result of the policy changes.

Fannie announced the new rules back in April. Perhaps the most consequential change was a revision to the formula that banks use to calculate a borrower's debt-to-income ratio, which is a gauge of the

person's ability to make monthly payments.

Under the previous guidance, a lender would consider the higher of either a borrower's amortizing student loan payment, or 1% of their student loan. A borrower whose monthly payment was reduced from \$500 to \$100 on an income-based repayment plan might be rejected under those rules because the lender had to use a more conservative measure than the actual monthly payment.

Under the revised rules, the lender can use the borrower's actual monthly student loan payment for the purpose of calculating the debt-to-income ratio.

Fannie also expanded a cash-out refinance option, which may enable some existing homeowners to pay off their

student loans. Plus, the government-sponsored enterprise allowed mortgage lenders to take into account the fact that borrowers' parents sometimes cover certain nonmortgage debt payments.

Bankers say the changes have made a difference, although it's early yet to quantify just how much.

Michael Sheahan, the retail lending manager at the \$1 billion-asset Chelsea Groton Bank in Connecticut, recounted the story of a borrower the bank had expected to decline, before Fannie announced the changes. Under the old rules, the borrower's debt-to-income ratio was too high. But calculated under the new rules, the ratio dropped to an acceptable level.

The changes were Fannie Mae's answer to a problem that has vexed mortgage lenders in recent years: Young people aren't buying homes at the same pace that previous generations did, and student debt is a major obstacle. Fannie aimed to give lenders more flexibility in how they evaluate student debt.

"There's a large bucket of millennials that are burdened with student debt, and this relaxed guideline really makes sense," said Bob Cabrera, the national consumer lending sales manager at Regions Financial in Birmingham, Ala. "If in fact you're not paying 1% of your outstanding debt and it's not part of your monthly responsibility, why include it in the [debt-to-income ratio]?"

Steve Shoemaker, director of residential mortgage production at Synovus Mortgage, said that Fannie's changes have brought attention to the demand for mortgages among student debt-addled millennials. He said that Fannie Mae is "reacting much more quickly than I think we would have seen in the past in trying to meet the needs of our consumers, so that everyone has this opportunity."

Of course, challenges remain. For many young adults in major metropolitan areas, high home prices and a shortage of available inventory are particular concerns. More borrowers may now be

able to qualify for a mortgage, or qualify for a bigger mortgage than they would have previously, but finding a home to buy is another story.

That's one of the main challenges for borrowers who show up to the \$2.4 billion-asset Belmont Savings Bank in Massachusetts, said Chief Executive Bob Mahoney. Count him among those who harbor some suspicion about Fannie Mae's changes.

Specifically, Mahoney has concerns about Fannie Mae's tweak to the debt-to-income ratio. The change may result in more applicants qualifying for mortgage loans, but it does not reduce their overall debt burden.

"When parents are paying the debt, I buy that one. Fine, take that off the list," Mahoney said. "But sometimes we get into trouble by lending too much money to good people. There's the other side of the coin."

Digital with a Human Touch

Camden National rolls out online mortgage portal

STEPHEN SESSLER, THE DIRECTOR OF mortgage banking at Camden National Bank in Maine, has some advice for bankers who are hesitant to try digital mortgages.

"Don't be afraid to jump," Sessler, a senior vice president at the bank, said at the Digital Mortgage conference this fall in San Francisco. "You think it's a bigger step than it really is."

The \$4 billion-asset Camden is one of about 35 banks that have partnered with Blend, a San Francisco cloud-based software company, to originate digital mortgages. Others include Wells Fargo and U.S. Bancorp.

In April, Camden launched its online mortgage portal, which it calls MortgageTouch, to automate the application and

preapproval process. Camden closed its first loan through the portal in mid-May.

Because consumers are inputting street address and other basic data themselves, the time spent on problem applications has dropped, and now most applications are ready 12 to 14 days before closing, Sessler said.

Borrowers can access the portal through their cellphones and other devices to securely sync bank statements, tax returns, payroll information and other data needed to apply for a home loan.

After just six months, 48% of mortgage applications are coming through the portal, with 31% of them coming from mobile devices, Sessler said.

Camden rolled out the digital platform in stages because it wanted to prove to loan officers that the technology had many benefits, particularly in improving the integrity of borrower data.

"Anything that smacks of replacing [loan officers] with technology does not go over well," Sessler said, to some laughter from the audience.

Brian Kneafsey, head of client operations at Blend, said there is a view that banks moving into digital mortgages are trying to bypass loan officers.

"It's really supposed to be something that supports a bank's operations," Kneafsey said. "Sometimes there's a misnomer that this is consumer direct."

Camden also wanted to assure its customers the real humans still would be available to assist with the process, which is why it used the word "touch" in the title of its portal.

The foray into digital mortgages has reduced the inaccuracies in mortgage applications that can hold up the loan process, Sessler said.

Because consumers are inputting the data themselves, they are less likely to misspell their street address or get their Social Security number wrong. The time spent on problem applications has dropped, and now most applications are ready 12 to 14 days before closing.

"Our application accuracy has gone

up, which has cleared up issues in the back office,” Sessler said. “There are no missing pages of a bank statement, no wrong Social Security numbers, because the borrower is getting the information directly from a provider.”

There are other benefits. Borrowers can work on their mortgage application at any time, often at night, so loan officers have more time for other tasks during work hours.

Sessler also sees the digital mortgage platform as a recruiting tool. Since many experts believe the \$10 trillion mortgage market is moving to the cloud, the new technology gives potential employees the sense that the lender has some staying power.

Still, not everyone is ready for a major change. The bank got blowback from real estate agents and had to “re-manage” how they promoted the portal, he said.

“Initially there were some unnerving responses,” Sessler said. “It was one thing we hadn’t really thought through in the process of what the reaction might be from realtors.”

Going forward, the bank is looking to add home equity lines of credit and potentially auto loans and other consumer products. The bank, a unit of Camden National Corp., has a national mortgage license and envisions spending about \$100 million to expand in the Northeast.

Sessler said the bank is “strongly considering” offering mortgages directly to consumers because the digital mortgage platform has freed up its strategy.

— Kate Berry

SBA's Partner Riles Bankers

Are credit unions just ‘filling a niche’ in small business?

A PUSH TO GET CREDIT UNIONS TO make more Small Business Administration loans is underway.

The SBA recently renewed a February 2015 agreement with the National Association of Federally Insured Credit Unions that is designed to persuade members of the trade group to make more of the government-backed loans. The SBA also is planning events with the trade group to create more awareness of how credit unions can get involved in these loans.

The initiative shows that the SBA views credit unions as a prime source for small-dollar loans, said Dan Berger, NAF-CU’s president and chief executive.

Berger said 80% of credit unions’ loans are for \$1 million or less, and go to borrowers that banks have largely abandoned. “We’re filling a niche,” he said.

But banking advocates were quick to dismiss such claims.

“I don’t think you’re going to find a banker who isn’t going to make a credit-worthy loan to a creditworthy borrower regardless of size,” said James Ballentine, executive vice president for congressional relations and political affairs at the American Bankers Association.

Credit unions have made some inroads with SBA lending. Since 2006, the number of credit unions certified to make SBA loans has gone from fewer than 150 to 389 as of June 30, Berger said. Of those, 194 have made at least one SBA loan this year.

Despite industry consolidation, the number of SBA-certified credit unions has increased by 4.3% since early 2015, Berger said.

NAFCU and the SBA plan to collaborate on an initiative to educate the roughly 5,400 credit unions that don’t participate in this type of lending about the merits of getting involved. Outreach is expected to be through webinars, training sessions and appearances at conferences.

The goal is to have at least 250 credit unions hold a minimum of 10 SBA loans on each of their books by the time the agreement expires in 2020.

The SBA signed a similar pact with the National Credit Union Administration in

early 2015, agreeing to help familiarize credit union examiners with SBA loans and to provide marketing and educational materials for credit unions.

— John Reosti

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BankTechnology



What data is fair in credit models?

Additional data enhances the ability to provide credit to thin-file consumers. But could it create other issues?

By Penny Crosman

IT'S LONG BEEN A MANTRA IN THE fintech community: Traditional underwriting models that rely heavily on conventional credit scores leave out people who haven't built up a credit history. A percentage of these people are credit-worthy, but without a history to go on, the credit bureaus haven't created profiles of them yet.

To assess whether unscored people can repay loans, lenders are increasingly looking at "alternative data" — informa-

tion that comes from someplace besides a traditional credit bureau that can help predict how a potential borrower will behave. Examples include bill payments for mobile phones and rent.

Many online lenders use this type of data and some traditional lenders have been experimenting with it.

But a growing chorus of observers wonders whether the use of alternative data actually helps the disadvantaged or rather allows lenders to flout the principles of fair lending and disparate impact.

When the Consumer Financial Protection Bureau granted a "no action" letter to the online lender Upstart Network in September, it further stirred up the debate around the use of alternative data. (A no-action letter advises recipients that

the staff has no present intention to recommend initiation of an enforcement or supervisory action, meaning they can proceed as they are for now.)

“The bureau is exploring ways that alternative data may be used to improve how companies make lending decisions,” the agency said in its letter.

In exchange for this promise of no action, Upstart will share certain information with the CFPB regarding the loan applications it receives, how it decides which loans to approve, and how it will mitigate risk to consumers. It also will share information on how its model expands access to credit for traditionally underserved populations.

“Because a machine learning-based model can change every day, typically in small ways, we have built a monitoring system to supervise what the lending system is doing, and that system will report the data to the CFPB on a regular basis,” said Dave Girouard, the chief executive of Upstart.

The hope at the CFPB is to use this information to better understand how these types of practices impact access to credit generally and for traditionally underserved populations.

The agency has been studying this since February, when it launched an inquiry into the use of alternative data. Its concern is whether lenders can use alternative data and still comply with the Equal Credit Opportunity Act and Regulation B.

The two regulations prohibit creditors from discriminating against a potential borrower on the basis of race, religion, sex, age, color, national origin, marital status, or receipt of public assistance.

“Although the general principles reflected in ECOA and Regulation B are clear enough, the expected evolution of Upstart’s automated underwriting model and potential changes in the applicant pool over time result in substantial uncertainty concerning the facts to which those principles would be applied and what actions Upstart should take to

prevent, mitigate, or remedy potential discrimination that might arise,” Upstart wrote in its application.

In the same vein, the rules around disparate impact can be hard to assess in practice.

“It’s not as simple as women should be 50% of loan approvals, it’s more about how our model approves them on a relative basis, other things held equal,” Girouard said. “There are different research camps about what is the right way to assess disparate impact. It’s one of the academically debated topics.”

‘Safe’ alternative data

Banks already use some alternative data, including employment and payment histories, in their loan decisions.

The alternative data credit bureau eCredable scores consumers, at their request, by getting data from landlords, power companies, day care centers, phone companies and such. (About 80% of this data gathering is automated, and 20% is done through phone calls.)

“Our hypothesis was that of the 45 million or so so-called ‘credit invisibles’ in the U.S. who are not scorable, probably a third are creditworthy but they just don’t have a score to prove it,” said Steve Ely, eCredable’s chief executive. “We’re trying to go after that third near the top that have a history of paying bills on time. If we can get to that history and get it into our scoring model, we can score them and present them to a lender.”

The scores are intended to be a proxy for the traditional FICO credit score.

“We didn’t invent a new credit score,” Ely said. “We don’t go to a bank and say we have this really wild and crazy innovative new credit score we want you to use to lend with. Because that’s a very short conversation.”

BBVA Compass uses eCredable’s scores to underwrite an unsecured credit card. The average eCredable score in that credit card portfolio is 700.

“As a lender, if you can find someone who has no credit score but acts like a

700, you can charge them like a 640,” Ely said. “There’s a lot of margin in that portfolio.”

Professional data also appears to be fair game. Upstart, for one, considers college major and field of employment in its models.

“Even in times of recession or unemployment, nurses are the types of individuals that in all statistical likelihood will be steadily employed,” said Dave Girouard, the CEO of Upstart. “Teachers also tend to be steadily employed because there’s almost always a shortage of teachers.” Both professions are also represented in minority and low-income neighborhoods.

The online lender Enova looks at 68 different alternative data sources when it considers potential borrowers with no credit file. These include VantageScore, LexisNexis, telephone companies, and data aggregators (for bank account transaction information).

For small-business loans, accounting data, business checking account data, payment processing data, and social data for businesses that use Facebook are useful, said Kathryn Petralia, co-founder and head of operations at the online lender Kabbage.

“Engagement with their customers is a really strong predictor of performance, because if they’re engaged with their customers then you know they’re working to run their business,” she said.

Google Analytics can give a good view of website traffic and shipping data is helpful too, she said.

“If a nail salon is getting more packages, that probably means they’re doing better,” Petralia said.

So what about “alternative data” is in question?

College controversy

The most controversial data type is education.

Many people believe that if you feed a credit model information about the college a loan applicant went to, you’re

likely to run afoul of disparate impact rules. Especially if you use artificial intelligence technology that finds its own correlations between factors like school and creditworthiness.

“Contrast a kid who just graduated from Tupelo Junior College to a graduate of Boston College, the outcome will be dramatically different,” Ely said. “Not only will the loan approval rates be different, but I suspect the lender’s offer will be very different – the kid from Boston College might get an offer for a \$50,000 loan, the guy from Tupelo a \$500 loan. Then you get into those kinds of disparate impacts.”

Petralia said education is usually a proxy for affluence. “Not always – there are some kids from Harvard and Princeton who went there on scholarship and they come from economically disadvantaged backgrounds,” she said. “But the preponderance of them didn’t.”

SoFi and Upstart are among the online lenders that today include college data in their underwriting models.

According to Girouard, Upstart considers education as just one of many elements of creditworthiness.

But he maintained that Upstart’s approach is less discriminatory than traditional underwriting models.

“You may intuitively believe that using education would cause disparate impact, but in our system the additional variables we look at reduce the disparate impact that is inherent in lending,” he said. “Because FICO scores and income are correlated, they have bias embedded in them inherently. The additional data we use tends to level the playing field more than cause an uneven playing field.”

Upstart measures the outcomes of its underwriting models for disparate impact with respect to gender and race.

“The bottom line is, the data demonstrates that we don’t have disparate impact in our system,” Girouard said.

Sarah Davies, senior vice president for research, analytics and product development at VantageScore, said the

joint venture of TransUnion, Experian and Equifax doesn’t consider education in its credit scores because of regulatory concerns.

“You have to be sure there’s no disparate impact with these pieces of data,” she explained. “For that reason, we don’t use anything like address information. And in some part, student information is a proxy for address. It immediately creates a red flag for us.”

Davies also said it’s hard for any company to say the use of a type of data isn’t causing disparate impact, because the principle itself is complex.

“We’ve studied it for 10 years,” she said. “There’s lots of ways disparate impact can seep into these models, even when you’re not using soft data like student information. So it’s not as cut and dried that a model does or doesn’t have disparate impact, depending on how it’s used, the time it’s being used, the type of products – you’ve got all these other overlays that make it a complicated question.”

The other problem with education data, Davies said, is the need to provide a clear reason code for a low credit score or a decline on a loan.

“The reason codes are things like, you failed to make your payment on time or your utilization is too high, and all those things have to be related to risk,” Davies said. “It’s almost impossible to create a reason code statement that says one person got a great score because they went to Harvard and another got a poor score because they went to Iowa State.”

Social media data

The use of social media data is also debated. Here again, the reason codes required by the Fair Credit Reporting Act are an issue.

“If one of the reason codes is, you visited this website, can you imagine having to deal with that?” Ely said. “I know enough about how regulators think that this isn’t going to be in our underwriting models for a long time.”

Upstart does not use social media data currently.

“We’re not into fanciful things like what you put on your Facebook page or who your friends are,” Girouard said. “A lot of companies have done a disservice to alternative underwriting with fanciful ideas that are not grounded in anything.”

Some lenders use social media to avoid fraud – for instance, if an applicant has no presence on social media and the associated email account was created a week ago, that could be an indicator of a synthetic identity.

In small-business lending, social media data has more practical use. It can reflect engagement with customers, as Petralia noted. It could also be used to spot signs of trouble. For instance, lending platform provider Credibly takes in Yelp data to be alerted if a restaurant has had a management change or is closed. Those red flags get passed on to human underwriters.

Phone-use data

MyBucks, an online lender that does a lot of work in Africa, has built an AI system that can take in any data to do credit scoring.

Currently in Kenya, the company gathers data from Android smart phones, with the customer’s consent, including potential borrowers’ calling patterns, the duration of their calls, their cell phone bill payment history, geolocation and all payments made from the phone.

“It turns out that in small countries where mobile money is widely used, data from smartphones is a great source,” said Richard van der Wath, chief data officer at MyBucks.

Phone-use data might not ever be acceptable in the U.S.

“The inappropriate data types are the ones that are generally used as proxies for things like age, gender or race,” said Joao Menano, chief financial officer of the online lending platform provider James. “One that is particularly concerning is the use of your mobile data information,

like SMS, WhatsApp messages and Facebook posts. It becomes quite easy to combine different variables that in practice are a proxy to race, for instance. I'm not saying that one should not use that data if it has predictive value, what I'm saying is that in those cases one should have extra caution to ensure fair lending practices."

Girouard said Upstart would not consider phone use in lending decisions unless it saw data proving a link to credit-worthiness.

However, he noted that in Africa there are no credit bureaus and the phone is the only means of collecting data.

"In the case of somebody who's lending in Africa, I wouldn't pass judgment on that, other than to say having some data and making credit available is valuable," he said.

Davies has trouble envisioning such data being used in the United States.

"How would I say to a consumer, you made 10 phone calls to your mother, therefore you're arguably lower risk because you're a better child?" she said. "How is this data indicating direct risk to a loan that's being made?"

Public records

In July, credit bureaus were forced to drop information about public records, specifically civil judgments and tax liens, from credit scores. This information was often incorrect.

According to LexisNexis, a provider of public record data, part of the challenge was that it's hard to accurately align public record information with credit files. Lenders can still buy the public record

data directly from the company.

"Certainly public-record information is valuable," Davies said. "It's indicative of payment behaviors and propensity to pay."

However, VantageScore ran a study with a credit scoring model from which it removed all public record information and added in other attributes such as very high balances on credit cards.

"That information was as predictive if not more predictive than the public record information," Davies said. "These public records were incurred several years ago. Whereas if consumers run up high balances, there's a potential that they've gotten themselves into a more risky situation."

Such data is already included in some credit models, she said.

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A high-quality black leather office chair with a perforated backrest and red armrests. The chair is centered in the frame against a plain white background.

Take a seat, please

It's tough to be a bank director these days, as the public and elected officials hold the board responsible for misdeeds that occur on their watch. Turnover is up, and filling the seats is more of a challenge than ever.

BY JOHN ENGEN



Chairman Stephen Sanger had just wrapped up his milquetoast presentation on Wells Fargo's sales-practices woes at the company's annual meeting last April when Bruce Marks, a housing activist and shareholder, jumped up and called on all of the board members to defend themselves.

"Tell us what you knew and when you knew it. Were you complicit or incompetent?" Marks demanded before being hauled out by security personnel. "Each one should stand up and explain why they should be reappointed to the board."

The directors, sitting in the front row with their backs to the crowd of assembled shareholders, shifted uncomfortably in their seats but remained silent.

When the election results were tallied a few hours later, four of the 15 directors, including Sanger, had received fewer than 60% of the votes cast, while another eight garnered less than 80% — an almost unprecedented rebuke for the board of a large company.

"What we clearly heard from shareholders was, 'We're sending a message,'" Sanger said after the annual meeting. "We don't view it as being about any individual director. We view it as being dissatisfied with the whole board."

Wells officials did not respond to interview requests, but it's difficult to see how the high-powered business leaders who sit on the company's board could not take personally being chastised in a public forum and rebuked by shareholders.

"That's the reality for board members today," said Susan O'Donnell, a partner with Meridian Compensation Partners in Newton, Mass. "When you have a scandal today, the question always rolls up: Where was the board?"

"If you're a director, it stings," she added.



Most people who serve on bank boards will tell you that it's a rewarding experience — a way to give back to the community and learn about an important industry.

But anecdotal evidence also suggests that the

work demands and perceived risks are making it tougher to find directors with the skills and diversity needed to lead companies in a competitive world.

Those concerns have even captured the attention of federal regulators, who in response to director feedback are working to clarify board regulatory expectations.

There was a time not that long ago when serving on a bank board was a ticket to respect, if not riches. Directors were local business leaders who plied their connections to land business for the bank, rubber-stamped the CEO's plans and boasted enviable cocktail-party credentials.

The post has always come with greater expectations and demands than serving on the board of a nonbank company. Prospective bank directors have long been expected to undergo FBI background checks, share personal financial data and get fingerprinted, for example, which is intimidating to many.

But it also carried prestige, country-club memberships and other perks, such as access to credit and preferential loan rates. And it really wasn't all that arduous. A few directors were even known to catch some shuteye during meetings.

"Fifteen or 20 years ago, things were pretty predictable," said David Porteous, who has been on the board of the \$100 billion-asset Huntington Bancshares since 2003, and is the company's lead director. "If you had a challenge, you were able to build a bridge to solve it and then take a breath and assess. ..."

"The outside scrutiny wasn't horrible."

Those glory days have passed, eclipsed by the industry's own missteps and the cacophony of the mob.

Over the past decade, bank directors have been pilloried in the press and vilified by some in Congress — transformed into lightning rods for the popular angst and frustration following a financial crisis and recession for which banks shouldered much of the blame.

Their workloads have increased sharply. The tasks, challenging enough on their own, are all the more so when viewed collectively: setting institutional risk appetites; establishing a cultural tone at

the top; hiring, firing and paying senior management; and plotting strategies capable of turning a profit in an environment teeming with fintech disruptors and cybercrooks.

At the \$28 billion-asset Iberiabank in Lafayette, La., the monthly board packet is typically 1,200 to 1,500 pages long. “I worry about directors not reading the whole packet. That’s pretty much impossible,” said nonexecutive Chairman William Fenstermaker. “We’re trying to cull some of that down, but there are so many requirements and only so much time.”

Fear of falling prey to a cyber breach is endemic among directors. So is an attack by an activist investor, a bad rating from the proxy advisers or a Bank Secrecy Act-related violation.

It’s a part-time gig with full-time work, lots of pressure and few of the old perks. By one count, the average bank director logs more than 20 hours a month, and often it’s more than that.

Bank board members endure greater scrutiny and risk than independent directors in other industries, and get paid less. Some smaller banks don’t pay their board members at all, and others even demand investments from them.

According to the search firm Spencer Stuart, average compensation for directors of banks in the S&P 500 was lower than all industries except utilities and consumer goods. A survey commissioned by the American Association of Bank Directors found that average pay for a board member of a publicly traded bank with less than \$1 billion in assets is about \$25,000.

Even worse, there’s the threat of personal liability. About 35% of bank failures result in directors being sued by the Federal Deposit Insurance Corp., according to David Baris, president of the bank directors’ association.

While insurance often covers those

costs, Baris said he knows of directors who have paid “substantially” out of their own pockets in confidential settlements.

“When the bank isn’t doing well, you have directors wondering if they should get off the board to avoid liability. And when things are going well, you hear complaints about the enormous amount of information they have to digest,” said Thomas Vartanian, a partner at Dechert LLP, a Washington law firm. “It’s not an easy job.”

As a recent headline in the op-ed section of *The Wall Street Journal* asked, “Why Would Anyone Sane Be a Bank Director?”

It’s a fair question – one with potentially important implications for the industry, which needs sharp leadership to compete.



There are certainly personal, career and financial benefits to being a bank director. CEOs-in-training often are offered up for bank board positions to enhance their understanding of finance and build connections – a signal they’ve arrived.

While director pay itself often isn’t great, people who serve on bank boards are more likely to get promotions and raises in their day jobs, said Steven Boivie, an associate business professor at Texas A&M University who co-wrote a recent study on board service.

“It sends an important signal to the market that other really smart people think you have potential,” he said.

Many people who serve as bank directors cite the intellectual and emotional rewards of learning about an important industry in a time of change, the networking opportunities and sense of doing something good for the community.

In many communities, being director of the local bank remains a source of

pride. Elsewhere, it’s simply a passion-driven avocation.

“You have to love the bank,” Iberiabank’s Fenstermaker said. “Our directors love the bank.”

Terry Lehman, a retired accountant who worked with banks for 30 years, is on the boards of two community banks, and relishes the opportunity to attend industry conferences and touch base with old friends.

“People think I’m crazy,” said Lehman, whose boards include Citizens & Northern Corp., a \$1.3 billion-asset public company in Wellsboro, Pa., and the \$200 million-asset MidCoast Community Bank in Wilmington, Del. “But I have a huge affinity for the industry, and felt like I could be a real help for any board I joined.

“It keeps me in the game,” he added.

Porteous feels such a strong bond with Huntington that he regularly hosts employee forums in various markets to gather feedback. “Those visits provide an almost magical opportunity for people in the organization to ask questions of the board,” said Porteous, who had a September meeting with Huntington staff in Cincinnati.

“I enjoy them even more” than employees do, he added.

Such sentiments are common among people already on boards, but the rigors of the job, combined with the industry’s image problems, can make it difficult to recruit good new directors.

About one-quarter of board members in a recent survey by the bank directors’ association reported having someone either quit the board or turn down an offer.

“The job just isn’t as attractive as it used to be,” Baris said.

“It’s the fear of liability and the time commitment. If you don’t have enough time, you can’t do the job right,” he added. “That’s making it more difficult to recruit qualified people to be directors.”

Paul Simoff, a senior consultant with ProBank Austin, a Louisville, Ky., compliance firm, tells of a bank client that thought it had lined up a good director candidate.

When the chairman showed the prospect the monthly board packet, he said, “Thanks but no thanks. I have a company to run, and you’re asking me to run another company where I have no expertise. Why would I do that?” Simoff recalled.



The recruiting challenges come at a time when bank boards, for reasons both practical and political, are keen on making their ranks more tech-savvy and diverse.

Risk, cyber and technology specialists who can help plot strategy in a rapidly changing world are in high demand. So are former bankers. “Ideally, you want several people who have operational banking experience and understand the nuances of the business,” Porteous said.

Boards are placing a special emphasis on adding gender, racial and age diversity to their ranks. “You want your board to be reflective of the communities you serve,” said Patricia Husic, CEO of the \$500 million-asset Centric Bank in Harrisburg, Pa.

Attracting the right people takes diligence and creativity. Husic spent nearly two years looking for a qualified female director before recently landing Nicole Kaylor, a 38-year-old lawyer. “You have to be very specific and intentional in your search,” Husic said.

Boards and managements also are doing what they can to make the position more appealing. Company-supplied iPads and portals with names like BoardPacks and Director Access help keep all of the documentation in order. Executive summaries and CEO letters that direct attention to important matters help focus discussions. Many boards have added

committees simply to spread the workload around.

It also doesn’t hurt to sweeten the pay. Todd Leone, a Minneapolis-based partner at McLagan Aon Hewitt, a compensation consultant, said director pay has increased by 4% to 6% in each of the past two years. “It’s tied to the workloads,” he said.

In 2016, each of Iberiabank’s directors received \$131,000 in fees and stock awards. “We had to raise it,” said Fenstermaker, who is recruiting new candidates for his board and said pay is an issue. “We’re competing with other industries to get the right people, and compensation matters.”

The biggest recruitment boost might come from, of all places, the Federal Reserve System. In August, after a three-year review, the agency proposed scaling back some of the daily minutiae for the bank and holding company boards it supervises.

The agency would rescind most of the 170 supervisory expectations that have been directed at boards in recent years.

Among the notable changes: Removing boards from the mailing list on time-consuming Matters Requiring Attention (MRA) notices. Addressing the notices to management and the board, a recent addition, has left directors feeling they must intercede in what was traditionally a management responsibility.

“The lines between management and board responsibility have gotten blurred,” said Alejandro Johnston, a partner in the financial risk practice at the consulting firm PwC. Directors “feel like they’re doing things management should be doing.”

If the proposed guidance changes are adopted, boards would see their efforts refocused on their “effectiveness” in big-picture areas such as governance, strategy and management oversight, as opposed to more routine regulatory mat-

ters.

“We do not intend that these reforms will lower the bar for boards or lighten the loads of directors,” Fed Gov. Jerome Powell cautioned at an August director conference. “The intent is to enable directors to spend less board time on routine matters and more on core board responsibilities.

“A strong and effective board provides strategic leadership and oversight, which is much more challenging and important than checking off lists of assigned tasks,” Powell added.

The changes would be especially beneficial to systemically important banks with more than \$50 billion in assets, where the workloads (but also the pay and resources) are greatest. But all boards would likely feel the effects.

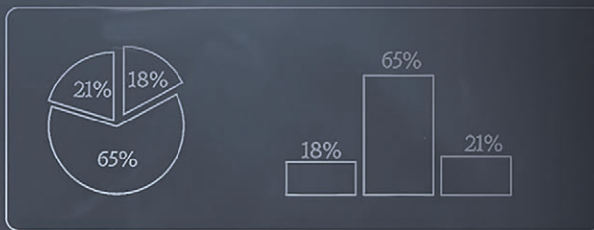
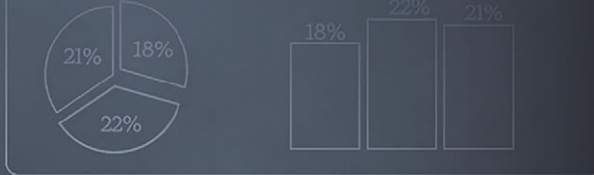
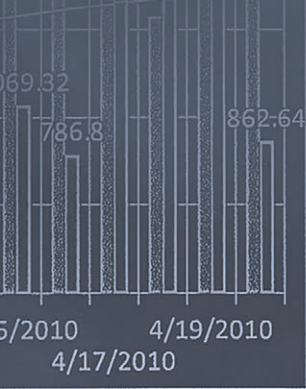
Robert Voth, head of the commercial and consumer financial services practice at Russell Reynolds, a search firm, said reducing the board’s compliance load will not only make board service more attractive, but also broaden the pool of potential candidates.

“When we look back to the high-water mark of regulation, it’s going to be the Federal Reserve itself recognizing the need to eliminate all these redundancies,” Voth said. “We’re entering a period where bank boards can do a whole-scale refreshment of how they’re constructed, ushered in by the Fed.”

At Wells, the board’s composition is already changing. In August, shortly after Sen. Elizabeth Warren, D-Mass., called on the Federal Reserve to replace the company’s board members (yes, it can do that), Sanger and two other directors announced they would resign from the board at the end of this year.

In Sanger’s place, former Fed Vice Chairman Elizabeth Duke, who joined the board in 2015, will become the first woman to serve as nonexecutive chairman of a major banking company. □





Add MUFG Union to the roster of traditional banks launching a digital division that aims to steal market share from the industry giants. Here's what the competitive landscape looks like and how their strategies are evolving.

DUELING DIGITALLY

BY BRIAN PATRICK EHA

The competition for online savings accounts is heating up.

MUFG Union Bank aims to fund its loan growth by pursuing deposit customers through a whole new division called PurePoint Financial.

PurePoint is offering an annual percentage yield of 1.30% on deposits — far more than traditional banks and better even than the interest rates offered by digital competitors such as Ally Financial, Synchrony Bank and Goldman Sachs.

But PurePoint is selective about its customers, accepting only those who can make a minimum deposit of \$10,000. And it doesn't yet provide

any products beyond savings accounts and certificates of deposit.

The product lineup is comparable to Goldman's GS Bank, which launched in April 2016. GS Bank offers a 1.20% interest rate on all deposits of \$1 or more, as well as one-year and five-year CDs.

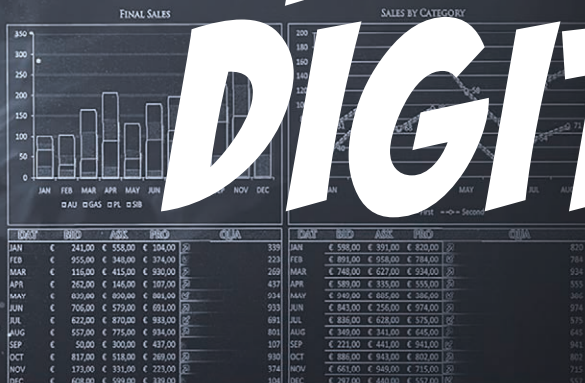
Though it is an MUFG Union unit, PurePoint operates independently, with its own logo, core banking system and financial centers. It attracts and serves customers primarily through digital channels.

While MUFG Union isn't the first traditional bank to launch a separately branded division as a way to get new customers, PurePoint is different from other entrants in some ways.

Goldman entered the direct banking market through its acquisition of GE's deposit platform, which has remained essentially unchanged since its rebranding as GS Bank. Though revising its approach lately, Capital One started out with a similar strategy, acquiring ING Direct in 2012 and rebranding it as Capital One 360.

In contrast, PurePoint is home-grown.

"This is not a new, new thing, but I think we have moved ahead of a lot of people with our willingness to disrupt ourselves," said Steve Cummings, the chief executive of MUFG Union and of the U.S. operations for its Japanese parent company, Mitsubishi UFJ Financial Group.



Being owned by the world's third-largest banking company means that PurePoint can rely on compliance and risk management expertise on the back end while still starting fresh with a modern technology platform.

"It's a unique position for me to be in," said PurePoint President Pierre Habis. "In many ways I feel very entrepreneurial. But I'm also part of one of the largest firms in the world."

At least some of the cost savings are passed on to customers: There are no monthly fees on PurePoint accounts.

"We're trying to be the no-fee, no-asterisk bank," Habis said.

Additional products are said to be in the offing. But even in its current form, observers said PurePoint, which launched in February, should be able to grab market share from incumbents, with its market-leading interest rate on deposits.

It ultimately should help boost MUFG Union's bottom line as well. The bank had a loan-to-deposit ratio of 87.80% at June 30, according to data from the Federal Deposit Insurance Corp. At this level the bank has more room to grow loans than it did with the ratio of 94.36% a year earlier.

A visit to PurePoint's recently opened flagship store on Park Avenue in Manhattan shows the extent to which MUFG Union's new division is rethinking the traditional bank branch. Tasteful minimalism prevails. There are no teller windows or rope lines. A reception desk and a few glass-walled offices staffed with bankers and outfitted with Microsoft Surface Pro 4 tablets suffice for customer service.

"A check is the only piece of paper you might see in here," Habis said. "When you take away all the costs that don't give you a return, this is what you get."

The changes are more than surface. To keep costs low, PurePoint did away with MUFG's legacy technology and obtained

"We're trying to be the no-fee, no-asterisk bank," PurePoint Financial President Pierre Habis says.



a modern core banking system from FIS. The key question, said Habis, was, "Why would you build the bank of the future on the bank of the past's platform?"

PurePoint opened its first financial centers in Chicago and Miami. The addition of the New York location in August brought the total to 18 branches, with some of the others located in Dallas, Houston and the Tampa Bay area.

More openings are slated this year, though PurePoint isn't looking to recreate the vast retail networks of the biggest banks. Its financial centers average just 2,000 square feet and 2.5 employees.

"You don't need to be on every corner," said Habis. "You just need to be accessible to folks."

As Habis gives an overview of PurePoint's growth, the business model becomes clear. PurePoint serves more than 20,000 customer households, and their average deposit balance is \$150,000 – exponentially greater than that of the typical American bank account. Those funds, about \$3 billion so far, can be used by MUFG Union to make loans.

While PurePoint may have its own branding – evidenced by the plush red chairs and sprays of artificial roses in the Park Avenue branch – its ties to MUFG Union offer a business advantage. Through PurePoint, MUFG Union is claiming an early lead in what it anticipates will be a future of higher interest

rates while also acquiring a pool of capital to drive its other businesses.

"MUFG has businesses that generate a significant amount of assets, and this is a lower-cost way of raising funding to support asset growth than trying to push more volume through the existing system or raising corporate deposits through the New York operation," said Todd Baker, the managing principal at Broadmoor Consulting and a senior fellow at Harvard University's John F. Kennedy School of Government.

Baker, who was involved early on in the process of brainstorming what became PurePoint but left MUFG Union before it moved forward with the idea, suggests that banks have gotten too comfortable with low interest rates over the past decade. Hardly anybody is competing on price for customer deposits. Even online-only banks such as Ally, which tout high-yield savings accounts, rarely offer much more than 1% interest.

"They teach you about the time-value of money in business school, but there is no time-value in our world" due to chronically low rates, Baker said.

That may be one of the reasons people aren't saving much these days. According to PurePoint's own research, the vast majority of New Yorkers have less than \$10,000 in savings – the minimum deposit to open a PurePoint account. Among city residents, only 27% of women and 20% of men could come up with the minimum.

But for the mass affluent and high-net-worth customers that PurePoint is targeting, "there's an enormous pent-up demand for low-risk or zero-risk, high-yielding deposits," said Baker. "If you go back to periods in history when significant interest was being paid on deposit accounts, it was typical to see very large balances as part of people's retirement and asset allocation strategies."

Baker said he thinks most of Pure-



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Point's market share will come from big banks, those groaning under the weight of legacy infrastructure and extensive branch networks. For years, banks on the order of Wells Fargo have offered interest rates of a tiny fraction of 1% on their basic savings accounts. (Even with a balance of \$99,999 – let alone \$10,000 – Wells Fargo's Platinum Savings account provides an APY of only 0.03%, with the potential for a "bonus" APY of 0.08% if certain requirements are met.)

Like Habis, Stephen Scherr, CEO of GS Bank, thinks banks will soon be forced to compete more fiercely for customer dollars. His ambition for GS Bank is to stay at or near the top of available interest rates.

"I think customers are voting with their deposits. They gravitate, as one might expect them to, to the institutions that offer both value and ease of use," Scherr said. "There's little question that if a bank wants to remain competitive, interest rates paid on deposits are going to be the principal basis on which a consumer makes a decision."

The nation's largest banks may be starting to act on that insight. In recent months, Capital One has twice raised the rate on its 360 money market account, first from 1.00% to 1.10% APY for balances of \$10,000 or more, then to 1.20% APY. The account has no minimum balance requirement, but balances of less than \$10,000 earn only 0.60%. The McLean, Va.-based company introduced the account only 18 months ago.

But while MUFG Union and Goldman are looking at their digital units "as a platform on which we can grow new businesses," in Scherr's words, Capital One is phasing out the separate brand.

Earlier this year, Capital One 360 was absorbed into Capital One, after it had gone several years as an independent division following the acquisition of the popular ING Direct online banking operation. Although some products still carry

the "360" branding, the division is no longer separate.

Goldman plans to combine GS Bank with Marcus, its online consumer lending platform, by the end of this year. When that is done, Marcus likely will develop a mobile app for its online offerings, Scherr said. Additional products may follow.

Goldman also plans to launch a U.K. online deposit platform in the second half of 2018.

Against direct banks like Goldman's, PurePoint's chief advantage is the peace of mind consumers get from physical branches, according to MUFG Union executives and others.

Having a physical location shows people "that your brand is real," Baker said. "Most people never need personal service, but they like to believe that they can have it."

Even so, PurePoint's growing network of financial centers runs counter to the industry trend.

Goldman is betting that the cost savings make being entirely digital the way to go. "We don't have – and we have no intention of building – branches," Scherr said.

Scott Blackley, Capital One's chief financial officer, said at an industry conference in June that Capital One had shrunk its branch network from 900 branches to fewer than 600 over the past five years. "Having more branches is not something that we're after," he said.

Mark Schwanhauser, director of digital banking at the research firm Javelin, said that PurePoint's singular focus on savings products – at least for the time being – gives it a lower cost basis than competitors that are trying to do more, such as Capital One.

"The digital features necessary to oversee idle cash are much different than those for consumers who are coping with a fuller range of on-the-go finan-

cial chores and activities such as paying at the checkout, monitoring cash flow, scheduling bills, trying to ensure the credit card balance doesn't outstrip the checking account balance, paying roommates for rent and utilities, monitoring the strength of one's borrowing power and paying debts smartly, saving for an emergency fund or longer-term goals, and so forth," Schwanhauser said.

While PurePoint offers only savings and CDs right now, Habis said it intends to roll out checking accounts, credit cards and digital mortgages eventually.

He's not worried about a Wells Fargo or JPMorgan Chase starting a nimble new division of its own and beating PurePoint.

"There's nothing to stop them," Habis said. But a big national bank would risk cannibalizing its existing business if it were to launch a new brand offering superior rates, he argued.

PurePoint has thus far avoided opening its financial centers on the West Coast, where MUFG Union has branches.

Some community banks also have separately branded digital banking units to pursue customers outside their market area, such as Customers Bancorp with its millennial-focused BankMobile.

But Habis said most smaller banks likely would struggle to raise the funds to build a whole new division – something that wasn't a problem for MUFG Union.

Baker said the interest rate may keep PurePoint in the lead for quite some time. "Right now, very few institutions are matching – or coming close to matching – the PurePoint offer," he said. "It's not surprising to me that the reception has been very strong."

Competition for deposits is about to get much more challenging, Baker added. "The last 10 years, any idiot could raise deposits," he said. "But now it's going to start to go back to being a delicate dance." □

BankThink

BY D. BRYAN JORDAN

What women's growing wealth means for banks

While I've witnessed myriad innovations in the financial services industry throughout my career, there is one area where banking has been slower to evolve: investing in women.

Up until the last few decades, the financial world imposed nearly impenetrable barriers that prevented women from reaching the highest levels. This was the case both in terms of hiring women and offering products.

But these days, equality has become a widely touted priority for businesses and positive gains have been occurring within the industry and the regulatory community. In 2014, Janet Yellen became the first woman to chair the Federal Reserve, for instance. While not banking specific, the number of women on the boards of Fortune 500 companies has grown to 20%, up from 15.7% in 2010.

While I'm optimistic we're moving in the right direction, we still have work ahead, both in the services we offer and whom we hire – not only because prioritizing equity is the right thing to do, but because the business stakes are equally compelling.

Nearly 60% of the women in this country participate in the labor force. Furthermore, more women than men are enrolled in graduate school, and women are earning more advanced degrees than men, trends highlighted in a study by the Council of Graduate Schools. Studies also show that women control more than half of the personal wealth in America, own nearly one-third of the nation's private businesses and are the sole or primary breadwinners in 40% of U.S. households.

When I consider saving and planning for the future, I think about my two daughters, who are both in their 20s. They have opportunities that weren't available to their grandmothers. As a proud father, I hope they will be high achievers throughout their careers. I hope they embrace opportunities to save and invest for the future. As a professional banker, I hope the financial services industry is where they and their friends turn for advice. But this outcome can only happen if the financial services industry invests more in women.

My daughters – like most of their contemporaries – deeply care about what companies do for communities. Indeed, a study by Omnicon Group's Cone Communications revealed that 70% of millennials say they want to spend their dollars with companies that support the causes they favor. As millennials increasingly invest and save as they age, they will seek banks that actively work against inequality. Financial institutions should have the same expectations as the age demographic – banks can't succeed unless the communities they serve succeed alongside them.

Although women continue to increase their share of private wealth, only a small percentage of financial institutions are reaching out to this growing market. Meanwhile,

D. Bryan Jordan is the chairman, president and chief executive of First Horizon National Corp., the parent company of First Tennessee Bank and FTN Financial.



fewer than one-third of financial advisers are women. We, as banks, must help change those statistics as they have led to a gap in the market.

Research shows women tend to be better investors than men, earning more annually on their investments. Women also tend to save more and take fewer financial risks than men, which can be an advantage in retirement planning. But according to the U.S. Department of Labor, women traditionally have not begun saving as early as men. Fewer than half the women in this country contribute to 401(k) plans, for instance.

Companies should engage more with women about their retirement options, especially since they typically live longer than men, and it is vital for them to be prepared.

While some banks are responding to women's wealth management needs to help fill this gap, we must dedicate more energy and resources to reaching this important market. We can and should do better. Furthermore, promoting equity outside the company should be mirrored by parity within. Besides marketing to women, we must create engaging workplaces that are supportive of female employees. In so doing, we will help attract and retain the most talented bankers.

By becoming a more equitable institution, customers benefit, employees are empowered and banks get better. By investing in women, we create a culture that rewards us all. □

OPINION

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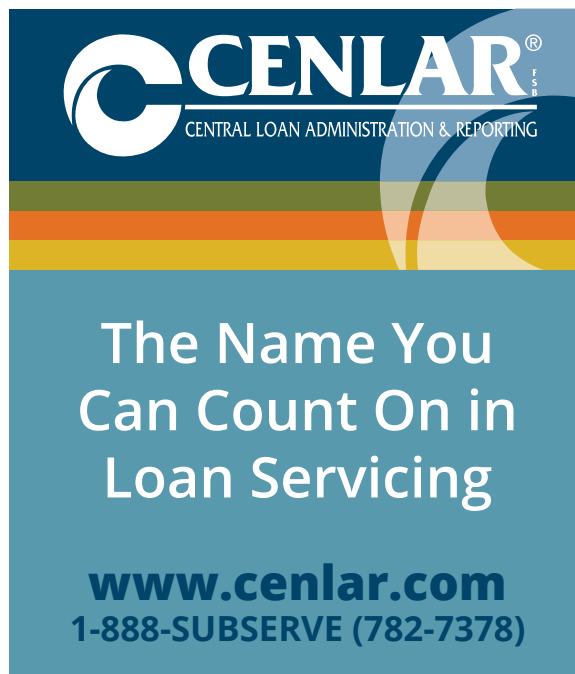
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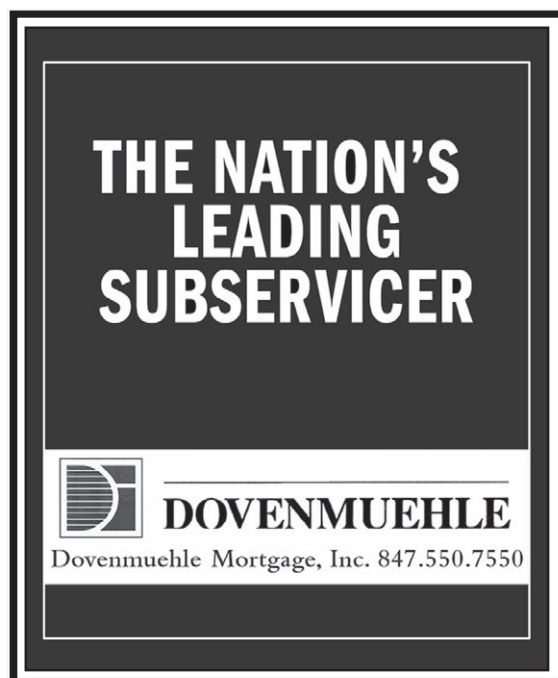
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GREG WALDEN

"I don't think we can pass a law that, excuse me for saying this, fixes stupid. I can't fix stupid."

U.S. Representative from Oregon at a House committee meeting on the Equifax breach

ARTHUR LEVITT

"For a company as aggressive as SoFi, I think the chances of that happening were slim. Now they become almost impossible."

Former SEC chairman, on SoFi's hope for a bank charter after a sexual harassment scandal forced out the online lender's CEO

BILL DEMCHAK

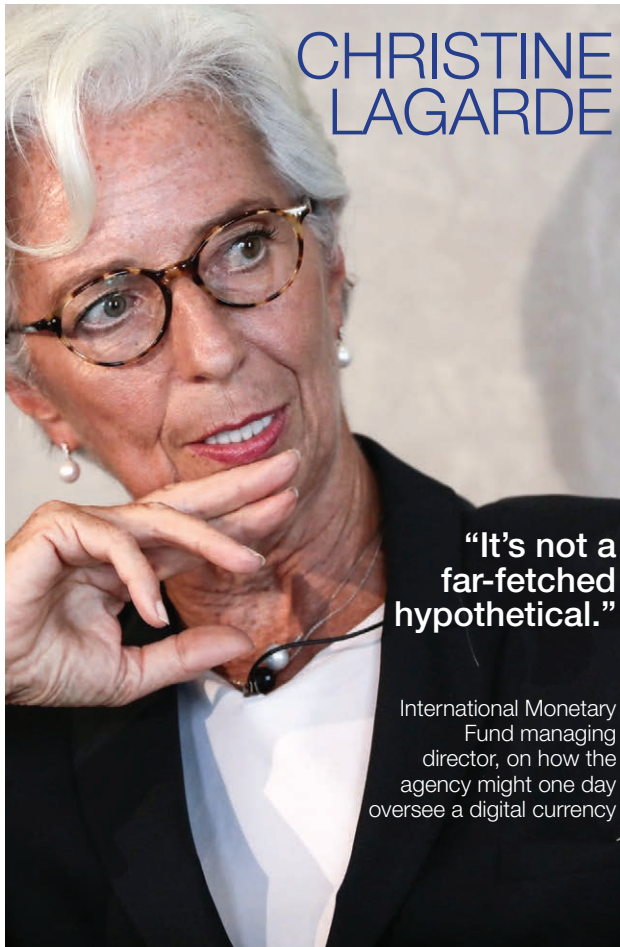
"It remains to be seen if regulatory relief, tax reform or a dramatically improved economy is going to materialize here."

PNC Financial Services' CEO, on the industry ending the year on a less hopeful note than it started

RISTO MURTO

"It seems as if there is no president in the U.S. If I look at what is the moral and practical power, there is no longer a traditional president."

CEO of Varma Mutual Pension Insurance Co. in Finland, attributing his \$53 billion fund's decision to cut back on U.S. stocks to a lack of faith in President Trump



"It's not a far-fetched hypothetical."

International Monetary Fund managing director, on how the agency might one day oversee a digital currency

JAMIE DIMON

"If we had a trader who traded bitcoin, I'd fire him in a second for two reasons. One, it's against our rules. Two, it's stupid. You can't have a business where people are going to invent a currency out of thin air."

JPMorgan Chase's CEO, who caused a stir with his comments dissing bitcoin

BALAJI SRINIVASAN

The blockchain — which is not just bitcoin — is the most important invention since the internet. I'm not sure if that's consensus among Silicon Valley now, but it's getting there."

CEO and cofounder of 21 and a board partner at Andreessen Horowitz

DEAN CLANCY

"It is an agency about protecting the little guy, and that is tough to oppose."

Policy analyst, saying public support for the Consumer Financial Protection Bureau helps the agency withstand Republican attacks

JESSE VAN TOL

"Banking while black in this country is still a hazard."

National Community Reinvestment Coalition executive, arguing that black and Hispanic borrowers face extra challenges in getting loans to buy homes



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