Insights Into 2012

Credit Unions Balance Growth, Efficiency and Compliance

Abound Resources shares results from its annual survey of credit unions and provides its insights into winning strategies for 2012

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Executive Summary

Each year Abound Resources surveys senior executives at credit unions across the U.S. about their priorities, plans and concerns for the upcoming year. Several of our findings were expected: For example, CEOs remain concerned about the weak economy and continue to view regulatory compliance as a significant challenge. Also consistent with prior surveys, operational and technology efficiency remain high priorities.

Other survey results were surprising, and even worrisome. There's a technology disconnect in 2012 that we've never seen before in our annual credit union survey. CEOs told us that their top technology priority was to better use the technology the credit union already owns yet the remainder of the C-suite is focused on implementing technology that improves member convenience such as mobile banking. Apparently the CEO and the rest of the executive team have different agendas for 2012, likely due to a lack of communication as well as confusion about the impact technology can actually have on efficiencies.

Another disturbing finding is that even though fee income fell for the first time in 2011, CEOs are not pushing initiatives that will replace this income. We've found an almost head-in-the-sand response to declining NSF/OD fees at the same time other costs related to compliance, personnel and technology are increasing. There are ways for credit unions to recover this lost income and we outline some of the most promising strategies later in the paper, including tapping into the small business market and driving payments volumes.

However, we are pleased to learn that CEOs are placing significantly more importance on improving sales and marketing than in previous surveys. They also indicated increasing online presence—a potential sales and marketing play--as a major priority. We only hope that credit unions will finally do the hard work needed to reverse the anti-sales culture common in many credit unions and quickly evolve from order takers to consultative advisors.

There's a real juggling act occurring in credit unions as executives struggle to balance their desire for growth with the needs for efficiency to combat increased compliance costs. However, like quite a few CEOs in our survey, Abound Resources is optimistic that credit unions can meet these seemingly divergent requirements. The CEOs and C-suite executives we've had the pleasure to work and speak with display a real roll-up-your-sleeves attitude now that most of the regulatory uncertainty surrounding the Dodd-Frank Act and Durbin Amendment has lifted.

Yes, it's time to get back to work, and in a nod to that enthusiasm and sense that the worst is behind us, we've added the *Top 5 Credit Union Strategies for 2012* to our survey results to help you translate our findings into action.

Key Survey Highlights

- ✓ Forty-three percent (43%) of CEOs are optimistic about the coming year, an almost identical finding to 2011.
- ✓ CEO's top concerns are the weak economy and loan demand (70%) followed by regulatory burdens (53%).
- ✓ The top three priorities for CEOs in 2012 are to address regulatory compliance requirements (61%), use technology for better efficiencies (58%) and improve sales and marketing (57%).
- ✓ About half (46%) of CEOs intend to expand their online presence even though the return on investment in online account opening and mobile banking is unclear.
- ✓ Just 28% of CEOs plan on buying new technology, while 97% of CFOs, COOs and CIOs have purchasing plans and 62% expect increases in technology spending over 2011.
- ✓ The top three purchasing priorities are mobile banking (48%), ATM hardware (42%), and mobile payments (39%) and consumer remote deposit capture (39%) which were tied.

About the Survey

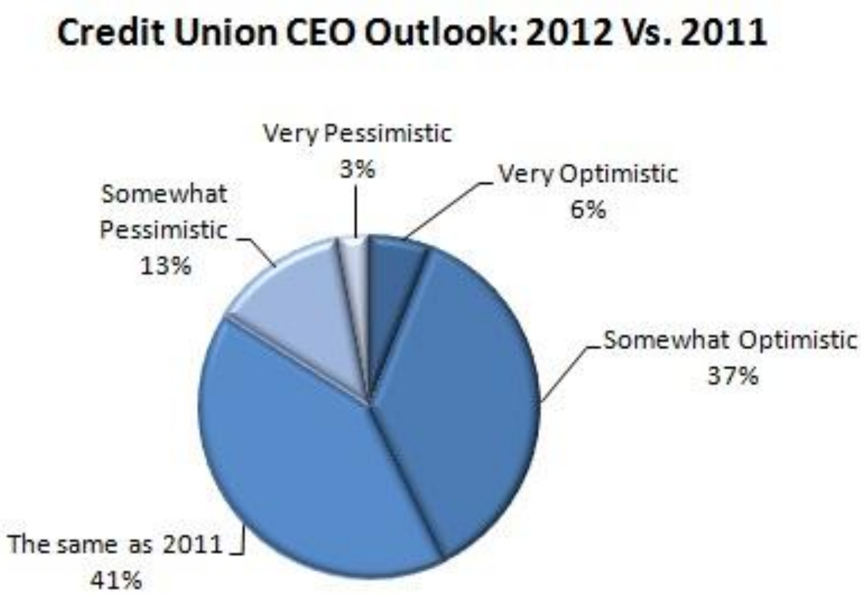
Abound Resources conducts an annual web-based survey of senior executives in credit unions throughout the U.S. This year's survey, administered in December 2011, received 339 responses from Presidents/CEOs and 127 responses from COOs, CIOs and CFOs. Responses were distributed as follows:

Asset Size	Responses
Less than $100MM	55%
$100MM - $250MM	19%
$250MM-$1BB	19%
More than $1BB	7%

The CEO Perspective:

The Worst is Behind Us

There's little doubt that it's still a difficult and challenging economic and business environment for credit unions but, as in 2010 and 2011, credit union CEOs remain a pretty optimistic bunch. Only 16% report that they are somewhat or very pessimistic about the next year. Six percent (6%) are very optimistic and although that is still a small percentage of total respondents, it's more than twice as many as last year.

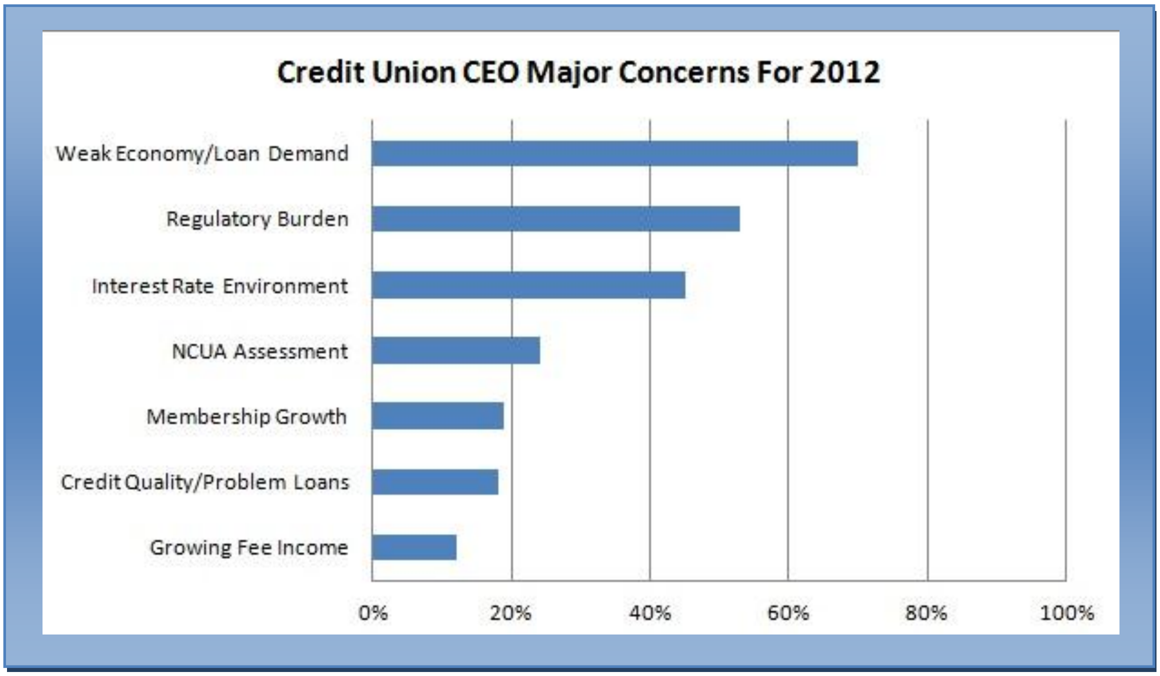


In our conversations with credit union CEOs, these executives convey an overall sense that the worst is over. They feel that the economy will continue to stumble along but it won't slip back into recession. The Dodd-Frank Act and the Durbin Amendment are now law and although CEOs don't like the current regulatory environment they, as they have so many times before, have largely accepted it and are moving forward on dealing with the new regulatory reality. The environment may not be good—and in fact many CEOs express anger about it— but at least some of the anxiety and uncertainty about what will happen in D.C. has subsided. Of course, the fear remains that the new Director of the Consumer Financial Protection Bureau (CFPB) will change all of that.

***The environment may not be good—and in fact many CEOs express anger about it— but at least some of the anxiety and uncertainty about what will happen in D.C. has subsided*.**

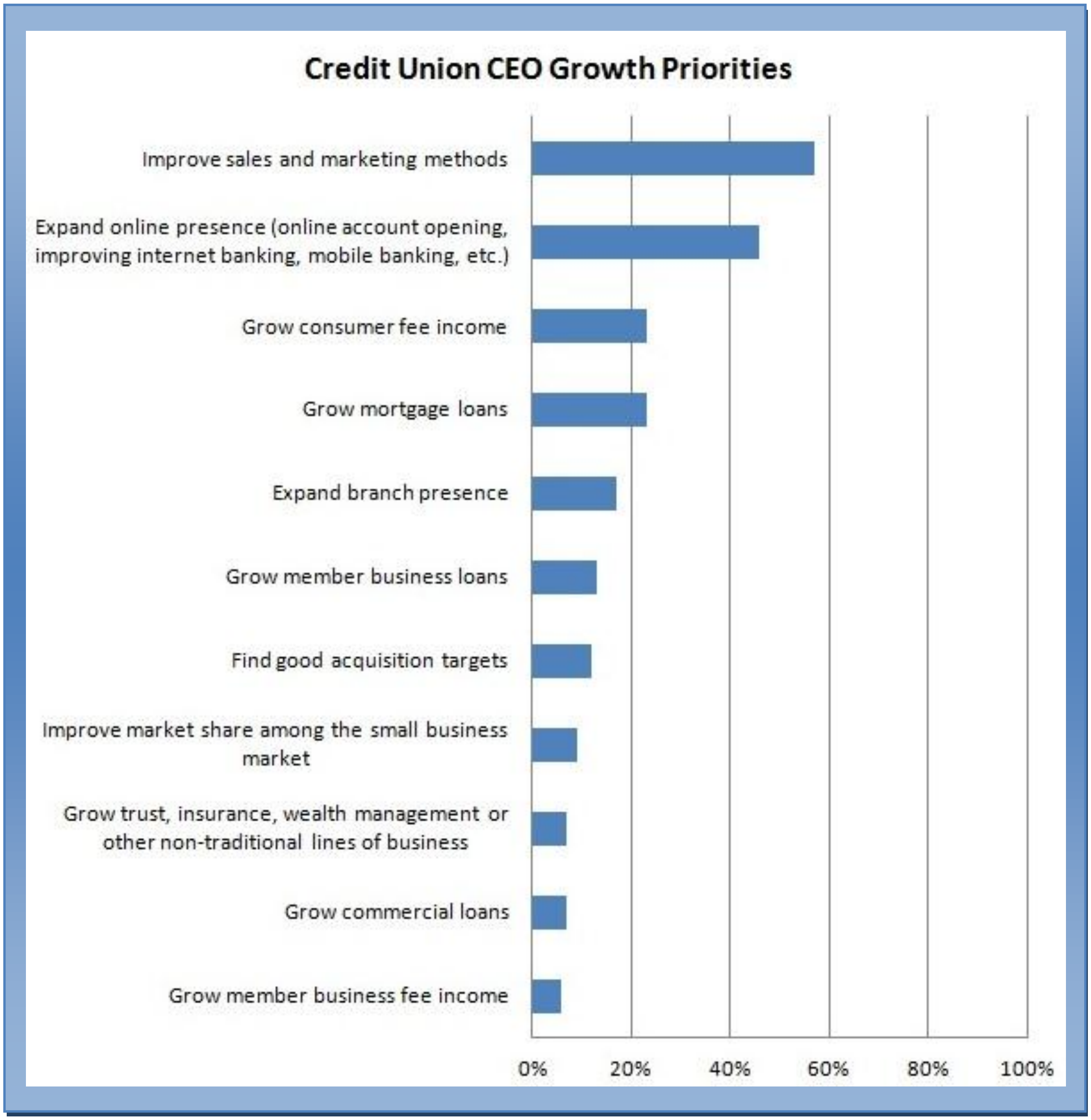
Macro Issues Cause Concern

We asked a new question in our 2012 survey: "What is your biggest concern?" We found that CEOs expressed the most trepidation about macro factors that are largely outside of their control, including a weak economy and loan demand (70%), regulatory burdens (53%) and the continued low interest rate environment (45%). Member growth (19%), credit quality/problem loans (18%) and growing fee income (12%) -– factors that the CEO can act upon and influence-- were less of a concern.



Growth Priorities Evolve but Fee Income Falls

The number one growth priority for credit union CEOs in 2012 is improving sales and marketing methods (57%), a somewhat significant increase from 2011 (44%). We believe that sales and marketing have much room for improvement, especially in the burgeoning area of online marketing and social networking, and we are encouraged that CEOs share our enthusiasm in improving this aspect of their business.



There's a question though as to whether CEOs will commit investments and drive the cultural changes required to truly improve sales and marketing. Credit unions have given plenty of lip service to "improving sales" over the last decade, yet many continue to view it as a once-every-few-years training exercise.

There's a question though as to whether CEOs will commit investments and drive the cultural changes required to truly improve sales and marketing.

Expanding online presence (46%) was the second most cited growth strategy even though the track record for actually growing membership via online delivery channels remains cloudy at best. Credit unions justify adding or improving mobile and Internet banking with, "We need to have an online presence to attract younger members." However, since the majority of credit unions do not establish actual targets or implement product and marketing strategies to target those prospects, the number of new accounts actually opened online has been disappointing.

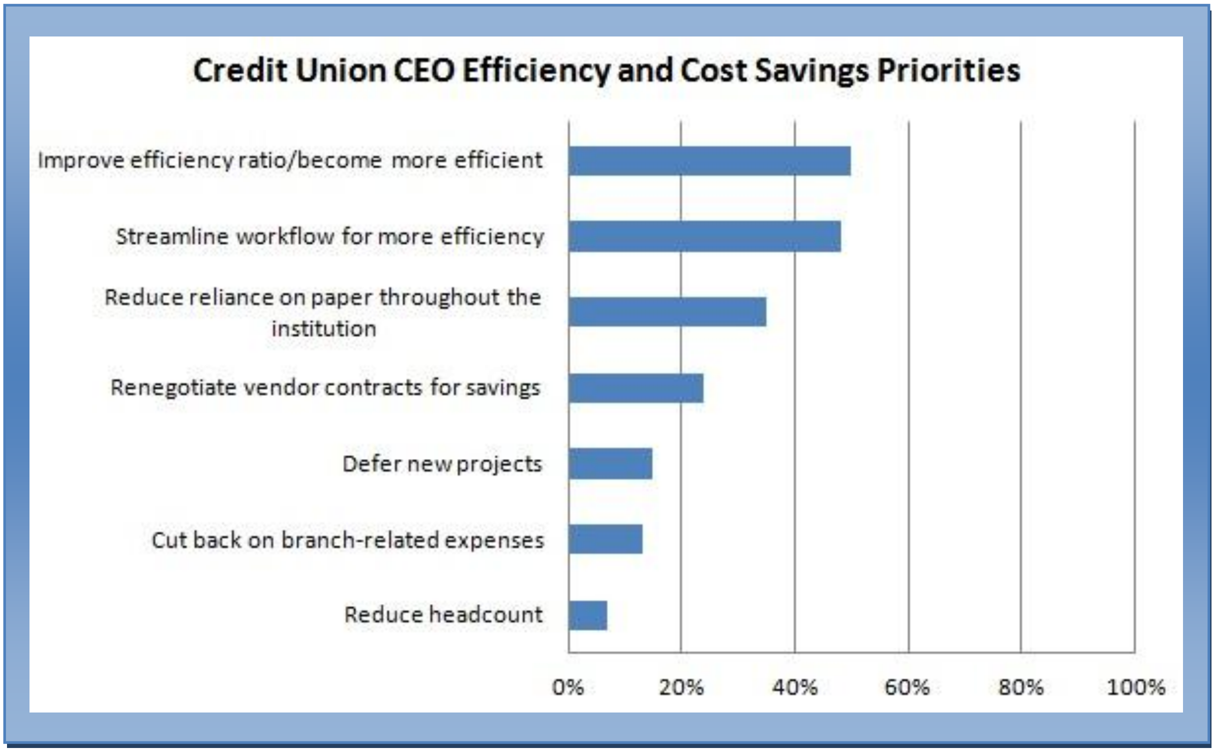
The most startling survey results surround fee income: only 23% of CEOs indicated growing consumer fee income as a priority and growing business fee income (6%) is dead last on the priority list. Fee income was a huge issue for credit unions going into 2011 due to the potential interchange fee caps proposed by the Durbin Amendment. Although that legislation will only impact institutions with more than $10 billion in assets, credit unions remain incredibly dependent on fee income. We are very concerned that fee income is such a low priority. NSF/OD income continues to decline while compliance, personnel and technology costs continue to climb. And now that the Fed has indicated it will keep rates flat for the next year or two, we know that spreads are not going to change much. Where is the revenue going to come from?

We are very concerned that fee income is such a low priority. NSF/OD income continues to decline while compliance, personnel and technology costs continue to climb.

Tapping into the small business market can help offset that lost revenue and should be part of the revenue replacement strategy for many credit unions. Unlike the consumer market, where less than one third of accounts are profitable, nearly all small business accounts are profitable. A member with a business account will typically generate more than $1,000 in annual profit. In addition, small businesses have become comfortable with credit unions and are more receptive to credit union marketing than they have been in the past.

Chasing Efficiency Ratios

This year once again the top two efficiency and cost savings priorities are improving efficiency ratios/becoming more efficient (50%) and streamlining workflows (48%), but the order of priorities has flipped. In 2011, streamlining workflow was the number one CEO response.



Our experience is that even credit unions that have asked for contract reductions from their vendors continue to overpay for technology.

Renegotiating vendor contracts has become less important for CEOs since last year's survey. In 2011, 41% of CEOs named contract renegotiation as a priority compared to 24% in 2012. This decrease could be because credit unions believe they have already exhausted renegotiation as a cost savings strategy. However, our experience is that even credit unions that have asked for contract reductions from their vendors continue to overpay for technology. There's a lot of money still left on the table and renegotiation remains among the easiest cost savings since it doesn't impact members or employees.

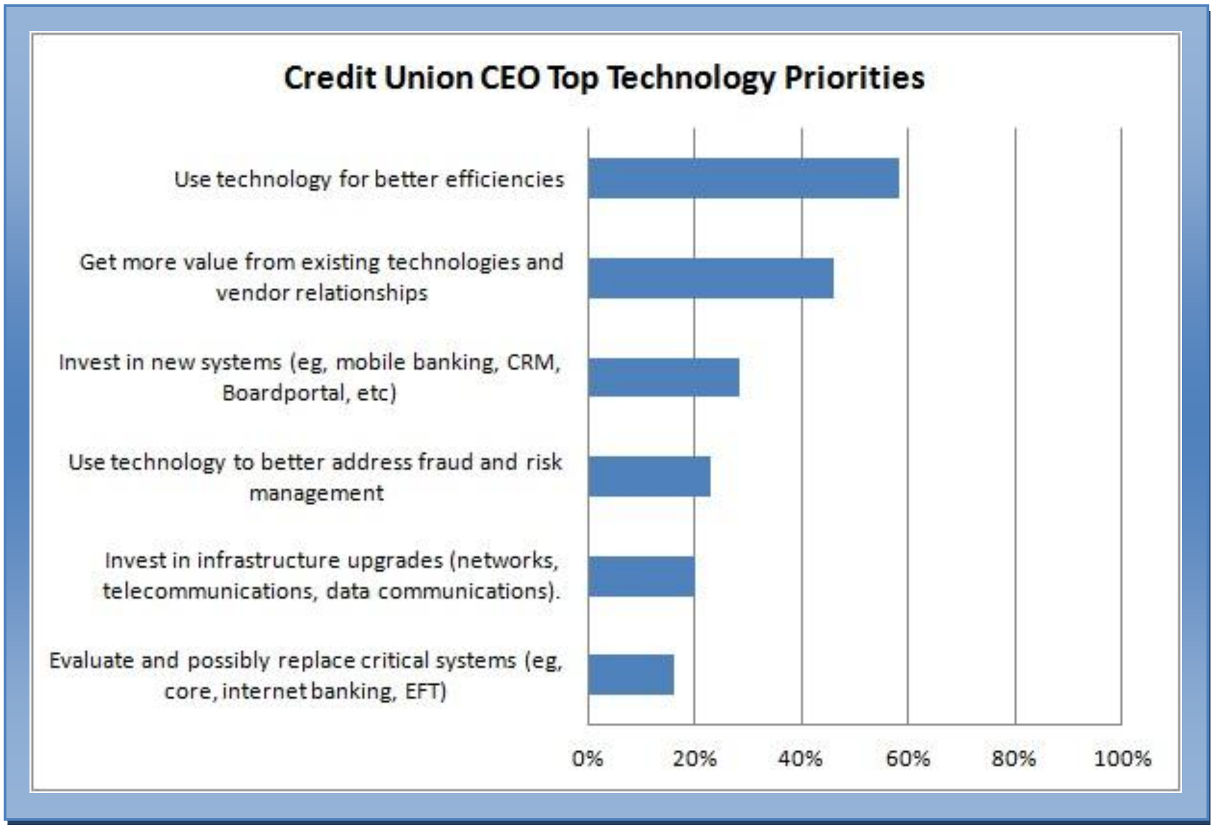
Compliance Trumps All

In today's regulatory environment, it's not surprising that addressing regulatory compliance requirements (61%) remains overwhelmingly the most pressing financial and risk management CEO priority for 2012, dwarfing improving lending policies and processes (31%).

Again, a prominent change from last year's survey is the lack of focus on replacing NSF/OD income with other fee sources. In 2011, replacing fee income was the number two concern for CEOs—this year it is only number seven on the list. Last year, the Durbin Amendment was a big worry for credit union CEOs but even with the Durbin Amendment laid to rest, as we stated earlier, Abound Resources believes that replacing fee income should be a higher priority.

Getting Better Technology Mileage

The technology priority story has remained consistent from 2011 into 2012 with using technology for better efficiencies (58%) once again topping the list of CEO technology priorities.



We predict that 2012 will be another difficult year for vendors as credit union CEOs report more interest in using the technologies that they already have rather than investing in new systems or upgrades (although CFO/COO/CIOs have a different view).

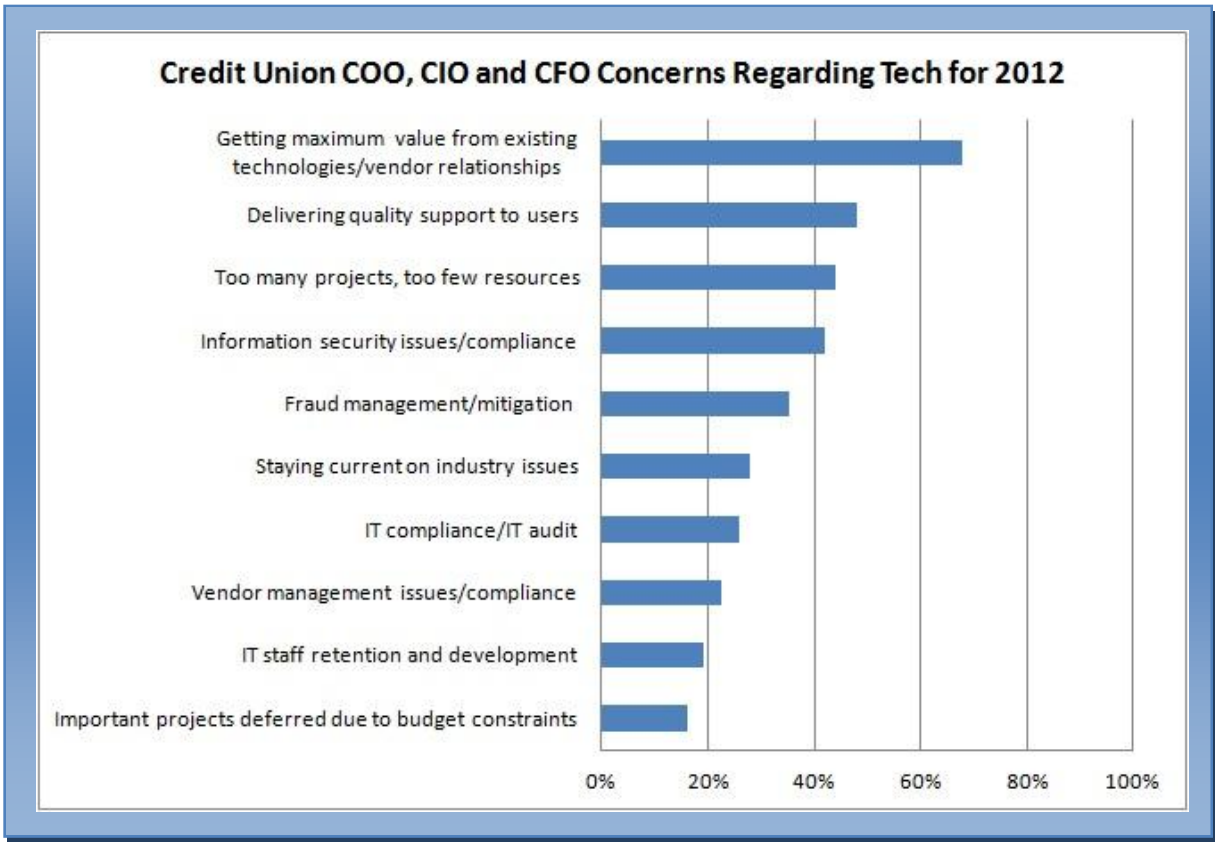
Based on our experience negotiating several hundred vendor contracts in 2011, it remains a buyers' market. Vendors experienced an uptick in activity in the fourth quarter of 2011 after two very difficult years, but they should be prepared for some tough negotiating and to offer big discounts throughout the first half of 2012. More importantly—and as we've been preaching for 15 years-vendors should be pro-active in helping credit unions improve the use of their existing products to drive better efficiencies. Unfortunately, the majority of vendors remain more focused on new customers, new products and new revenues than on improving existing customer utilization and satisfaction.

More importantly—and as we've been preaching for 15 years-vendors should be pro-active in helping their credit unions improve the use of their existing products to drive better efficiencies.

The COO, CIO and CFO Perspective

Maximizing Value

For the third year in a row, the top technology concern for credit union finance, operations and IT executives is getting maximum value from existing technologies and vendor relationships (68%). In fact, the top five technology concerns remain constant between the 2011 and 2012 survey; however, the order of those concerns has changed. In 2011, the second most pressing concern was information security/compliance; in 2012 it's moved down to number four.



The good news is that it's very easy to significantly improve technology utilization. The real challenge is getting both the business lines and the IT function working together. In our experience, poor utilization is as much a reflection of management styles and credit union culture as it is vendor failure.

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Delivering quality support to users jumped three places from our 2011 survey to take the number two spot in 2012. Quality support has not historically been a high priority but we think that the importance of improving use of existing technologies may be driving the increase.

Spending Starts a Slow Rise

Nearly two-thirds (72%) of COO, CIO and CFO respondents report that their technology spending will increase in 2012. Certainly it's very difficult to cut technology spending since the bulk of spending increases are those "built-in" non-discretionary spending increases such as increased volumes or users, inflation adjustments in contracts and increased benefits costs. We did see a number of 2011 projects (namely mobile banking) deferred until 2012 so increases in discretionary spending will likely be driven by some of these deferred projects.

For those CFOs, COOs and CIOs with technology budgeting responsibility, we recommend that you reconcile technology spending priorities with your CEO. Less than 28% of CEOs expect major technology purchases in 2012 and these executives may have unrealistic expectations about technology spending in 2013 as well.

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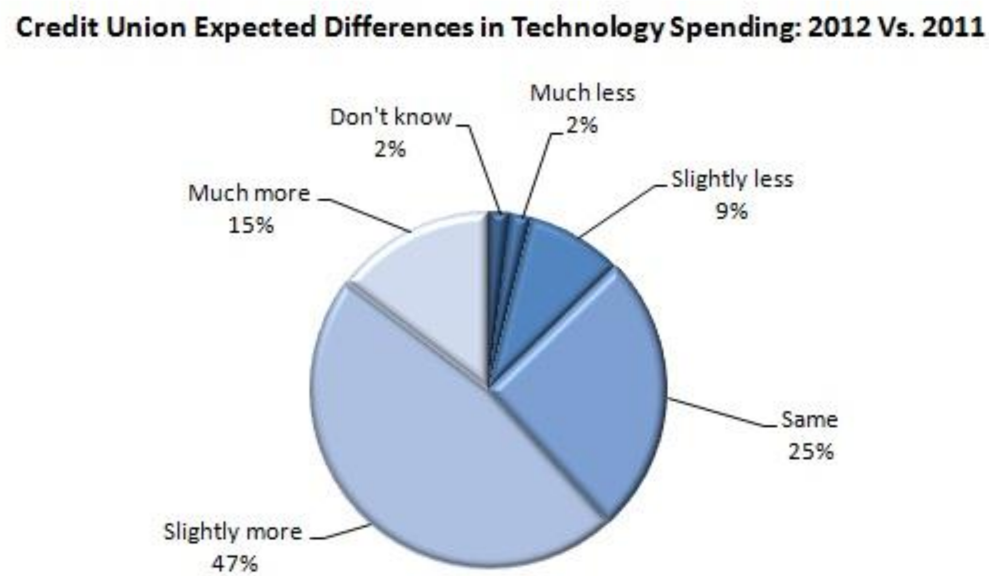

CEO-C-Suite Spending Disconnect

Credit union purchasing priorities remain largely the same from 2011 to 2012 with only a few exceptions. ATM hardware pushed into the top ten projects due to the ADA Standards for Accessible Design guidelines that take effect in March 2012 and mandate upgrades in voice, video and tactile input. ATM upgrades have been a huge "surprise" cost to credit unions and the money spent will unfortunately yield little return for institutions other than allowing them to comply with ADA legislation.

Top 10 Project Priorities For Credit Union: New or Replacement Purchases	
Mobile banking	48%
ATMs, hardware	42%
Mobile payments	39%
Remote deposit capture - consumer	39%
Online account opening	34%
Consumer internet banking	26%
Remote deposit capture/merchant capture - commercial	25%
Personal financial management (PFM) tools	25%
Loan origination and underwriting systems	24%
Tablets, iPads	23%

Mobile banking is the number one purchasing priority for the second year in a row. Many mobile banking projects in 2011 were deferred into 2012 and now first time mobile buyers are asking if they even need a text or SMS version. With nearly 60% of US adults owning a smart phone (Javelin Research), the question has become do you roll out your iPhone or Android app first.

Mobile payments moved up the list even though many credit unions don't know exactly what that means. Is it online bill pay through mobile? Is it person to person payments through Paypal? Is it mobile credit card akin to Google Wallet? Is it something like the Starbucks' payment app? Mobile payments is the Wild Wild West of credit union technology right now. Venture capital money is again being thrown at 24 year old programmers in Austin and the Silicon Valley. This time the money is going to the next cool mobile payments idea. But be warned – most of these emerging companies aren't focused on privacy, security, compliance or interfaces. So be sure you know what it is you are trying to accomplish, what your members want, how you're going to secure it and how you're going to make money on it.

> ***Mobile payments is the Wild Wild West of credit union technology right now.***

Consumer remote deposit capture is largely a convenience play. Few credit unions, if any, are driving any fees or efficiencies from it, but many are responding to the very visible advertising campaigns from large banks such as Chase's QuickDeposit™. The drive for online member conveniences raises this question - if your members aren't coming into the branch anymore and the majority of your sales processes are branch-based, how are you going to sell in the future?

Online account opening promises to address this very issue, so it's no surprise that online account opening continues to be a high priority project. Unfortunately, online account opening has been a disappointment in its most common form. It's CRM déjà vu all over again. Many credit union CEOs have been convinced that simply adding online account opening systems will drive a flood of new account openings (just as CRM vendors convinced them that simply adding CRM systems would increase cross-sells). A technology-only strategy never works. If you do not improve your sales and marketing practices, online account opening will be a disappointment.

Online account opening continues to be a high priority project despite a disappointing return on investment.

In comparing the top technology project plans of C-suite executives with the list of CEO priorities, it's clear that there is a disconnect and lack of alignment. While COOs, CIOs and CFOs are focused on member convenience projects such as mobile banking and consumer remote deposit capture, credit union CEOs list improving sales and marketing, gaining efficiencies and dealing with regulatory compliance as their top priorities.

The top technology projects for 2012 listed above won't move the needle on what CEOs are most concerned about and it appears that the COO, CIO and CFO is traveling down a different strategic path from the CEO.

Although we've seen this disconnect in our community bank surveys, this is the first year we've seen this disconnect in credit unions. The top technology projects for 2012 listed above won't move the needle much on what CEOs are most concerned about, and it appears that the COO, CIO and CFO might be traveling down a different strategic path from the CEO. In a year of tight budgets, technology/strategy alignment is critical.

In another disconnect, only 28% of CEOs noted that they planned new technology purchases in 2012 yet 97% of COOs, CIOs and CFOs are planning new purchases.

Holding Vendors Accountable

Last year, the number one utilization priority for the CIO, COO and CFO was core processing systems. This year, it moves down to number five. Since the core system is the most expensive item on the technology system budget, credit unions should continue to focus on improving the core. Even if they have already embarked on core optimization, it makes sense to revisit and tweak that optimization strategy each year.

Top 10 Project Priorities for Credit Unions: Improve Use of Systems	
Consumer internet banking	38%
Document imaging/document management/workflow (ECM)	38%
Bill Payment	35%
Asset liability management (ALM) systems	35%
Core processing system	35%
eStatements	34%
Debit/Credit/ATM/EFT systems and services	33%
Network Equipment/Storage/Server Virtualization	32%
Vendor management systems/services	31%
Call center systems	31%

The high priorities of improving Internet banking and bill pay are likely about improving member penetration. With all the focus on improving online capabilities, credit union's primary online channel is still grossly under used. Often, we'll see credit unions with less than 50% of their member checking accounts using Internet banking and only 20% of those using bill pay.

For those considering mobile, keep in mind that Internet banking use is the best indicator of mobile adoption. Typically you can guesstimate about 20% of your Internet banking users will become mobile users in the first 18 months. So if you have low Internet banking penetration, you might consider addressing your overall online strategy before rolling out mobile.

Bill pay use remains the stickiest service you have so if your penetration is low, consider marketing campaigns, 90 second how-to videos, incentives, etc. to drive penetration.

Most credit unions have document imaging, but many have never used the workflow component of those programs. In our experience, workflow is the number one technology to support your efficiency improvements. Just be sure and redesign your workflows first before you automate them. Otherwise, you still end up with bad processes.

> ***Workflow is the number one technology to support your efficiency improvements.***

In a play to improve member penetration, eStatements is the number six technology project priority. While eStatement adoption continues to grow, few credit unions have had great success lowering vendor costs as most members receive both an electronic and paper statement.

Vendor management systems/services remains in the top ten list of priorities. Our experience is that most credit unions still manage their vendor management program in Excel or use a vendor management system (VMS) only as a repository and checklist. Today, there are many VMS options with workflow and risk assessment wizards (disclaimer: Abound Resources is endorsed by CUNA for vendor management) that can help credit unions better automate the growing complexity of their vendor management program.

However, effective vendor management is not just about VMS. It includes the policies and processes you use to maximize the benefits, minimize the costs and mitigate the vendor costs. Effective vendor management should also improve your system utilization.

Top 5 Project Priorities for Credit Unions: Renegotiate Existing Contracts	
Bill payment	9%
ATMs, hardware	8%
Debit/Credit/ATM/EFT systems and services	7%
Telecommunications/datacom	6%
Asset liability management (ALM) systems	6%

Bill pay and EFT costs have come down significantly in the last 18 months so you should expect to see good savings when renegotiating those contracts. Be diligent when negotiating new ATM contracts. Often vendors are bundling in upgrades, maintenance and servicing which makes it difficult to negotiate. You must look at the individual unit prices to see where the savings opportunities are.

And historically credit unions have not paid enough attention to renegotiating telecom/datacom contracts. With a significant drop in market pricing, it's likely that credit unions could achieve big cost savings (and often improved performance) by renegotiating. As an example, Abound Resources just helped a $200 million client save $280,000 on their telecom/datacom bill. Once again, this is an indication that credit unions are leaving money on the table with their technology vendors.

From Survey to Action: Top 5 Credit Union Strategies for 2012

While survey results are helpful in benchmarking your credit union against your peers, the real value is in translating those findings into actions at your institution. With that in mind, and based on our 2012 survey results as well as our consulting work with credit unions throughout the U.S., the Abound Resources team recommends these five strategies for 2012.

1. Grow Revenues Through Advice-Based Sales and Fee Income

In our survey, CEOs said that improving sales and marketing methods was their number one priority. Experience shows, however, that it is much easier to talk about it than to actually do the hard work necessary to improve sales.

Sales has always been a bit of a dirty word in credit unions. Credit union employees balk at the idea of being turned into a used car salesperson so they have instead evolved into order takers. If a member knows what he or she wants and is willing to visit a branch, employees are pretty good at guiding the member to the best product and opening the account (i.e.: taking their order). But what about those members who don't know what they need? Or those who don't know you have a similar product to the large national bank they just called for a quote? Or those who don't come into your branch? Or those who aren't yet members?

> ***Experience shows, however, that it is much easier to talk about it than to actually do the hard work necessary to actually improve sales.***

You need to continually drive awareness of solutions to members and prospects so that when they need the solution (whether they know it or not), you can help them explore options. That's called marketing.

When you do get that opportunity to sell, understand what's driving their need so you can determine whether your solution will solve their problem. That's called sales.

If you want to survive, you must be willing to market and sell your products. While no one would suggest taking the hard-sales approach of the much-dreaded used car salesman, a consultative advisor who serves members by recommending the right products and solutions likely fits with your brand and can be a point of differentiation from the big bank "hard sell" approach.

> ***If you want to survive, you must be willing to market and sell your products.***

The issue is whether or not CEOs are willing to make the investments and drive the cultural changes required to improve sales and marketing. Here, in no particular order, are the most common mistakes we see in credit union sales and marketing:

- Lack of data to identify good prospects for products and campaigns. We remain an industry awash in data and devoid of actionable information.

- Wasted marketing dollars. Today, marketing requires more than placing an advertisement in the Sunday newspaper, posting interest rates on your website or sponsoring the local little league team. Credit unions need to embrace electronic lead generation with tools that may include e-newsletters, webinars, Google AdWords and social media such as Facebook, LinkedIn and Twitter. These do not replace traditional or offline tactics; they compliment them. The most effective marketing campaigns typically incorporate many different media.

- No competitive differentiation. If your marketing messaging highlights your great rates, great service and great locations, you have not yet identified your competitive differentiation. Every other credit union, community bank and even some big banks in your area say the exact same thing. What will make you stand out in a very crowded marketplace?

- Fear of setting sales goals. You get what you measure so don't ignore holding marketing employees accountable for lead generation and sales employees accountable for closing. Some business line managers are using the mortgage-focused incentive compensation regulations as an excuse to cloud the accountability issue but you can incent behaviors and remain in compliance.

- Jumping into sales training without building the proper infrastructure to monitor and measure results or doing one time training instead of on-going coaching and reinforcement of sales techniques.

- Not rewarding your best members with loyalty programs.

In addition to improving sales and marketing, credit unions must drive more fee income. That doesn't mean just raising fees and copying big bank strategies. Rather, it means driving cards and payments volumes, creating new small business programs and smart fee collection.

There is no slam-dunk new product that will solve the challenge of replacing fee revenue.

There is no slam-dunk new product that will solve the challenge of replacing fee revenue. As an industry, we became intoxicated on NSF/OD income and there's a pervasive feeling that a product will come along to replace it. We don't see any on the horizon, and even if there is a great product or service that promises new or additional sources of fee revenue, it seems likely in this environment that the Consumer Financial Protection Bureau or the court of popular opinion will pounce on it. Just ask Bank of America or Verizon how new consumer fees worked out for them.

We feel that the real fee income growth opportunity is in the small business market and payment services (ACH, cards, RDC) that drive fee income. You likely already have most of the products you need for a successful business program. Now you need to tie it together with effective sales and marketing.

The solution to the revenue problem isn't new and it isn't sexy. The solution is better execution of fundamental sales and marketing techniques: competitive differentiation, target marketing, lead generation campaigns, sales targets, training and coaching and accountability and incentive rewards.

2. Redesign Workflow to Improve Efficiency

The number one CEO cost savings priority for 2012 is improving efficiency ratios/becoming more efficient. Although CEOs often use the terms "efficiency" and "efficiency ratio" interchangeably, they are different concepts. Efficiency refers to the idea of "working smarter" or "doing more with less" while efficiency ratio is a calculation of how much revenue the credit union is able to drive from its overhead expenses. Efficiency ratio is more of a measurement of sales effectiveness than expense management.

When exploring expense reduction, executives and/or consultants must factor in whether those expense reductions impact revenue generation.

Since the efficiency ratio is most heavily influenced by revenue, any project designed to improve the efficiency ratio must address margins, fees <u>and</u> expenses. When exploring expense reduction, executives and/or consultants must factor in whether those expense reductions impact revenue generation. For example, is it better to close an under-performing branch and lose the corresponding revenue or invest in branch sales and marketing to possibly generate more revenue?

Making significant financial improvements in expense reduction requires addressing credit union's three biggest non-interest expenses: people, technology and facilities. In our experience, credit unions loathe the idea of closing branches or laying off employees so the easiest ways to improve efficiency are improving the use of technology, streamlining workflow and improving branch performance.

If credit unions buy technology, say vendors, efficiencies will come. The reality is that technology is only one piece of the efficiency puzzle.

Survey results clearly showed that CEOs expect technology to drive efficiencies, a mindset perpetuated by vendor marketing-spin. If credit unions buy technology, say vendors, efficiencies will come. The reality is that technology is only one piece of the efficiency puzzle. You must also revisit your policies to see if they are driving more work than is needed, streamline your workflows to take advantage of the new technology, evolve your culture to one that tracks production metrics (e.g.: loan turnaround times, new account opening error rates), push the vendor to make continued improvements and empower your employees to make decisions.

How many credit unions have invested in automated lending systems only to continue to print documents for review or to ship folders of documents for approval? You can buy Lance Armstrong's bike but if you're not going to change your training program and your nutrition plans, you won't cycle much faster. You simply must improve the workflows to achieve better utilization and increase efficiency.

Proper vendor management can also drive efficiencies and was cited as a top 10 priority by C-suite executives. Although the term "vendor management" has become synonymous with the annual compliance process of gathering financials and Service Organization Control Reports (i.e., SSAE 16, formerly SAS70 reports), effective vendor management maximizes benefits (through utilization improvement) while minimizing costs (through contract negotiations) and manages risks (through better contracts, insurance, business resumption plans and the like).

We recommend including vendor management in your technology planning discussion so it becomes a strategic initiative rather than an afterthought you consider only when the examiners are due to visit.

We recommend including vendor management in your technology planning discussion (more on this below) so it becomes a strategic initiative rather than an afterthought you consider only when the examiners are due to visit.

3. Create a Technology Plan to Support Your Strategic Plan

CEOs tell us that they want to use technology to drive efficiencies (think document management and workflow or process automation) but our survey results show that the number priority for COOs, CIOs and CFOs is mobile banking – a member convenience play. This disconnect can be very expensive to the credit union and costly to the COO, CIO and CFO's career.

The best way to avoid a disconnect between the CEO and the rest of the C-suite and reap the most benefit from your technology spending is to create a technology plan that identifies the technology projects or purchases that align with the organization's strategic objectives.

The best way to avoid a disconnect between the CEO and the rest of the C-suite and reap the most benefit from your technology spending is to create a technology plan that identifies the technology projects or purchases that align with the organization's strategic objectives. The plan ensures that credit union strategy drives execution rather than the other way around.

Technology planning begins with the credit union's strategic plan (whether written or in the CEO's head) and is then built based on input from the business lines and IT about how to use technology to support that plan. The end result is the top five technology initiatives for the next three years with dates, dollars and accountability assigned. The plan should be reviewed, discussed and ultimately approved by the CEO (and perhaps the Board). Whenever the CEO or a business line manager approaches the CFO/COO/CIO with a new technology request, the executive can refer back to the plan. The question becomes: “Is this request more important than these top five, and if so, which of the five gets taken off the list?”

4. Explore New Regulatory Compliance Models

More than half (53%) of CEOs responding to the survey named dealing with regulatory burdens as a top concern heading into 2012. Regulatory compliance is eating up more time and resources than ever before and the trend shows no sign of abating.

We’ve identified two key tactics to cost-effectively improve regulatory compliance. The first is to “bake” compliance and risk management into workflow or efficiency process improvements. For example, when redesigning your loan origination process, build in controls so you can capture and resolve exceptions before they become a reporting issue. Pay for an interface to minimize styling differences on legal names. Automatically notify the credit officer if a document is missing before you get to closing. Good systems should improve both efficiency and risk management.

Second, consider the emerging model of co-sourcing for regulatory compliance. Vendor management is quickly moving to a co-source model where credit unions use consultants to either help with large evaluation and negotiation projects or to run their entire program. Regulators expect you to add more people to stay current with compliance, but you will never be able to afford the number of experts required. Additionally, legal and consulting firms are expanding their staffs, creating a talent shortage and driving up salaries. Co-sourcing becomes a cost-effective alternative to building expertise in house and adding to staff and we recommend considering at least two distinctly different models:

Regulators expect you to add more people to stay current with compliance, but you will never be able to afford the number of experts required.

	In House Model	Co-Source Model #1	Co-Source Model #2
Compliance Functions			
· Advise	In House	Outsource	In House
· Monitor	In House	In House	Outsource
· Train	In House	Outsource	In House
· Manage projects	In House	In House	Outsource
· Audit	Outsource	Outsource	Outsource
Type of In House Personnel Needed	1-2 experts and several generalists	Several generalists with project management skills	1 compliance expert, typically an attorney in larger institutions
Pros	More control	Easier to staff, more expertise, less expense	Less expense
Cons	More expense, less expertise	Less control	Less control

One co-sourcing model outsources technical expertise and training while relying on internal staff to handle day-to-day projects and monitoring. Another outsources monitoring, reviews and project management while in house staff stays current on technical expertise and handles internal training. In either model, the credit union still owns the process (it's co-sourcing, not outsourcing), but benefits from outside expertise. As an added bonus, examiners look more favorably on independent, external reviews.

5. Begin the Move to Enterprise Risk Management

Regulatory compliance is clearly a top concern of CEOs, but it is only one part of the broader risk spectrum facing credit unions. As the NCUA noted in a October 2011 report, "Credit unions should work to gain a broader understanding of their overall risk profile." As many CEOs and Boards discovered over the past few years, strong net worth and earnings doesn't guarantee careful risk management. Earnings and capital can quickly evaporate during a severe economic downturn as many credit unions that ventured into member business lending and buying loan participations learned in 2008 to 2009.

> ***"Managing risk is at the very core of a credit union's existence. If risks are managed well, a credit union can add increased value to their membership. If risks are managed poorly, a credit union diminishes this value and can even jeopardize its very existence."***
>
> **NCUA Report October 2011**

Abound Resources recommends five key steps to manage enterprise-wide risk:

Step 1: Evaluate risk. Determine how much risk your credit union can take, must take, and afford to take to reach its strategic business objectives. Prepare a comprehensive "risk appetite" statement. For example, calculate best, expected and worst case loss scenarios based on planned loan types and amounts. If you don't have sufficient net worth to absorb the possible worst case scenario losses, rethink your strategy.

Step 2: Translate "risk appetite" into measurable risk guidelines. What amount of loss exposure is management and the Board comfortable with in different types of lending (i.e., direct vs. indirect, real estate, member business lending, credit card)? Translate the risk appetite into specific industry and geographic risk concentration guidelines. Consider the risks of various types of commercial real estate loans since they differ significantly (office versus retail building use, owner-occupied versus non-owner occupied).

Step 3: Monitor and evaluate risk on an on-going basis and measure performance against risk guidelines. Identify key leading and lagging risk indicators and track them regularly. If the strategic business objective is to increase penetration of the "millennial" market, track the number of accounts sold to that group. If portfolio risk is driven by factors such as employment, home sales or new home starts, track those indicators. If the risk guidelines set a limit for member business loans as a percentage of new worth, track that. Consider tracking the dollar-weighted risk grades of loans in particular segments to look for signs of deteriorating quality. Use forward looking, leading risk indicators, such as loans made as exceptions to credit scores or policy guidelines rather than lagging indicators like past dues.

Step 4: Implement an effective risk management structure. Consider outsourcing or co-sourcing as a cost-effective means to ensure sufficient, skilled resources are available for compliance, audit, loan review and IT security. Make sure that controls are effective and appropriate within your risk environment.

Remember that credit unions that proactively identify, measure, monitor and control risk will provide the greatest value to their members even in the most difficult economic environments.

Step 5: Finally, investigate enterprise risk management (ERM) systems that automate risk assessments, create audit reports and track audit findings. These systems are still evolving and even if you are not ready to consider a purchase, you can learn a lot about the concepts of managing credit union risk by viewing vendor demonstrations.
Remember that credit unions that proactively identify, measure, monitor and control risk will provide the greatest value to their members even the most difficult economic environments.

Conclusion

It's been a difficult few years for the entire financial services industry, including credit unions. Many of those headwinds—including economic uncertainty and increased regulations—will likely remain throughout 2012. While credit union executives are resigned to leading in this "new normal," they won't be able to rely on business as usual type practices. Instead, we encourage credit unions to look at new ways to drive fee income, finally improve sales and marketing, align technology purchases with strategic objectives and explore new models of cost-effective compliance. The CEO, the executive team and the Board need to work together to ensure that each step they take, whether it be rolling out mobile banking or getting more functionality out of existing systems, is done with the goal of supporting the strategic plan.

It won't be an easy transition but in a time of compressed margins and tight budgets, it's a necessity.

About Abound Resources

Abound Resources is a full service management consulting firm with a sole purpose to help credit unions achieve their goals - whether those are growth goals, efficiency goals, technology goals or risk management goals. In fact, we are so sure of our ability to help you achieve your goals, we guarantee it.

Abound Resources offers an array of services designed to improve performance and profitability and help credit unions cope with an increasingly stringent regulatory environment.

Our seven practice areas are each headed by an experienced practice leader:

- **Technology** – technology plans, vendor evaluations, contract negotiations, vendor management

- **Operations and Payments** – workflow improvement, efficiency studies, payments strategies

- **Lending** – loan process improvement, loan origination vendor evaluations and implementations

- **Small Business** – member business deposit and fee income growth programs, business lending programs

- **Strategic Planning** – strategic plans, risk tolerance planning, one page strategic plans, competitive differentiation

- **Sales and Marketing** – branch performance improvement, sales coaching and training, e-marketing strategies and campaign management

- **Risk Management and Compliance** – ERM, IT audits, information security assessments, compliance, BSA review

Abound Resources is proud to be an alliance provider of CUNA Strategic Services http://www.cunastrategicservices.com/Abound_Resources_96.html

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Abound's Free Resource Library

Technology

- ☐ Negotiating Better Contracts For Your Credit Union
- ☐ Vendor Management Disconnect: Why Credit Unions are Unhappy with their Vendor Management Program
- ☐ Six Ways to Save Time and Improve Compliance with Vendor Management
- ☐ Core Decision in Next 30 Months? How to Save Money and Improve Performance
- ☐ Technology Utilization: If You're Only Using 50%, Why Are You Paying for 100%

Risk Management and Compliance

- ☐ Understanding The Consumer Financial Protection Bureau & How It Impacts Your CU
- ☐ Developing the Enterprise Risk Management Infrastructure for Credit Unions
- ☐ 3 Specific Solutions for your CU to Respond to Regulatory Change & Slow Economic Recovery
- ☐ Regulation Q Update White Paper

Strategic Planning

- ☐ Top Ten Reasons Your Credit Union Might Need A New Strategic Plan

Small Business and Commercial

- ☐ Small Business Market - an Untapped Source of Increased Fee Income for Credit Unions

Operations and Payments

- ☐ Top 10 Best Practices for Consolidating Your Back Office
- ☐ 5 Keys to Improving Your Efficiency Ratio This Year
- ☐ The Right Way to Efficiency Improvements: Improving the Bottom-Line AND the Customer Experience

Lending

- ☐ 5 Secrets to Successful Online Account Opening and Online Lending

Sales and Marketing

- ☐ Opt-In Secrets, Margin Management and Sales Success: The Other Side of Efficiency Ratio

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