

## **Director's Corner: Seeking Useful Information in the Data-dump World**

**By Shawn O'Brien, President, QwickRate and Greg Dingens, Executive VP, Head of Investment Banking, Monroe Financial Partners, Inc.**

**“Good decisions begin with good information. A bank's board of directors needs concise, accurate and timely reports to help perform its fiduciary responsibilities.”**

*OCC Detecting Red Flags in Board Reports: A Guide For Directors*

In today's market of low interest rates and low growth, the ability for a bank to earn an acceptable return on equity is increasingly difficult. Earning a good return, however, should be a critical objective for bank directors, both to ensure the bank's long-term survival and its ability to raise capital to take advantage of opportunities. The best way for management and directors to measure progress toward that goal is to actively track the absolute and relative performance of the bank, both near term and long term.

Moreover, regulators have made it explicitly clear that bank directors have a responsibility to be informed of, and truly understand, the performance of the institution they oversee. For many years, the FDIC, the OCC and the Federal Reserve have all been on record with requirements for banks to create reports that are “carefully framed to present information in a form meaningful to the board”<sup>1</sup> and to compare their bank to the performance of peers. More importantly, directors are on the hook for knowing their bank, because “if they neglect to carry out their fiduciary duties and responsibilities, they may be financially liable if the bank fails or experiences loss...”<sup>2</sup>

This is serious stuff, with serious consequences, and many boards struggle with getting good information to make informed decisions. The responsibility of delivering this falls to the management team, many who typically struggle with sifting through scads of data and reports to present relevant information in a constructive way.

### **The challenge: Navigating the Data Dump**

Lack of data is not the problem for banks. The scope of important data is large and growing. There are call reports and Uniform Bank Performance Reports (UBPRs), ALCO reports, internal budgets, investment portfolio reports, liquidity reports - the

list could go on and on. Many community bank board reports consist of 50+ pages, often in multiple, different formats, fonts and orientations.

The real issue is finding a way to see through the overwhelming flood of paper, and that responsibility lies squarely on the shoulders of the bank's management team. It is their job to efficiently deliver critical data and analysis in a useful format, so that directors are not buried under reams of minutiae and can spend their time focused on what is important to the success of the organization. At the same time, the board cannot manage what it cannot measure, so the right information has to be considered as well.

### **Simple Rules to Create Highly Effective Board Reporting**

Here are three simple rules to follow for usefully organized, relevant content for the Board:

**1) Access, analyze and condense all the performance data of the bank over a meaningful time period (NOT just this month compared to budget)**

Performance metrics should include both current and historical data. Directors need to see where the bank stands today, and how that compares to past performance. This permits them to understand how performance is trending over time, measured both over recent quarters (especially last 4 quarters) and over many years.

In addition to offering a comprehensive picture of the bank's performance, management must make sure to emphasize the few critical factors that are key to thriving. Metrics such as ROAA, ROATE, Core Operating Earnings and Total Credit Costs are more important than pledged securities to total securities, for instance.

## 2) Do the same for a group of peers that can be used to place the bank's performance into context

Peer comparisons may include standard UBPR groups, but should ideally be composed of custom peer groups whose characteristics (size, type, operating philosophy) are very similar to your bank's. Develop a system to rank and/or grade peer performances to make it easier to compare how your bank stacks up to other institutions and where it excels or underperforms. Provide side-by-side performance averages, rankings and grades for your bank and all peers. In other words, both absolute and relative performance are critical for management and the Board to understand.

## 3) Present the information in a format that can be easily digested by all directors, including those who are not experienced or formally educated in interpreting financial information

Keep things visual. Transform details into easy-to-grasp charts and diagrams. For example, show trends as graphs; they're much easier to interpret. Pay attention to the arrangement of data. Top and bottom performers can be spotted at a glance when they're presented in order. Also, choose a report format and stick with it. A consistent presentation style makes it simpler for everyone to learn to interpret trends and issues.

### What About The UBPR?

Many banks use UBPRs for some portion of Board reporting. It is beneficial to review UBPR analysis, since the regulators employ this tool to evaluate the bank. However, the UBPR has its challenges. It is an outdated, dense report that's hard to decipher, and with 40 pages of data, it can easily overwhelm bankers with its minutiae. The UBPR peer groups also tend to be too large and are therefore non-informative. Difficult to download, and even more difficult to glean any trends from, this is not a report that can be just handed over to directors.

## New Regulatory Requirement: The Credit Stress Test

Management and directors must now also focus on another new regulatory imperative — the credit stress test. This report dictates the need to gather a daunting amount of peer information, and to measure the impact of a variety of scenarios by manipulating that data. The regulatory agencies have explicitly required community banks to create this new analysis, and have given some guidance around the requirements for this test. It involves gathering peer loss rates by all loan categories over many years, and measuring the impact of several scenarios of potential credit cycle losses. The math sounds simple, but the proper execution is very time consuming. Custom peer groups are important here also. Regulatory agencies have made it very clear that directors are responsible for owning this analysis

### Bottom Line: Solutions Are Available

The question is, how do you supply this kind of valuable information without having to invest huge amounts of time, effort and expense?

Fortunately, there are a couple of automated options in the marketplace that make board reporting easier for community banks and relieve the manual burden associated with keeping directors educated and informed. (We'll be showing examples that banks are currently using in our presentation at the FMS Finance and Accounting Forum.)

*Disclaimer: The views and opinions expressed in this article are those of the author(s) and do not necessarily reflect the official policy or position of the Financial Managers Society.*



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1 FDIC, *Pocket Guide For Directors*

2 Federal Reserve, *Duties and Responsibilities for Directors*, Effective date April 2013



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