

In Touch

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8

THE COMING BANKRUPTCY
WAVE: A BANKRUPTCY
OVERVIEW FOR CREDITORS

12

SAFE ACT A DECADE ON

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4

FLOURISH

By Rebeca Romero, ICBA

6

**MUNIS FOR THE MANY
TAXABLE MUNICIPAL BONDS HAVE APPEAL
FOR NEARLY ALL COMMUNITY BANKS**

By Jim Reber, ICBA Securities, an Endorsed CBA Provider

8

**THE COMING BANKRUPTCY WAVE:
A BANKRUPTCY OVERVIEW FOR CREDITORS**

By Camber Jones, Spencer Fane

10

**HOW WILL DIGITAL LENDING BENEFIT
YOUR BANK?**

By Simon M. Fisher, CSI Banking Solutions

12

SAFE ACT A DECADE ON

By William J. Showalter, CRCM, CRP Senior Consultant;
Young & Associates, Inc.; Kent, Ohio

14

**COVERDELL ESAS COME WITH
DIFFERENT ROLES**

By Alayna Droke, CIP, CHSP

16

**HOW COMMUNITY BANKS CAN PREPARE
FOR CECL CHANGES**

By Risk Management Solutions Group

20

**LENDERS' OBSTACLES: MANY MANUAL
PROCESSES DESPITE DIGITAL PUSHES**

By Mary Ellen Biery, Abrigo

IN EVERY ISSUE:

15

ANNIVERSARIES

15

NEW ASSOCIATE MEMBERS

19

UPCOMING WEBINARS

22

PRODUCTS AND SERVICES REFERENCE LIST

FLOURISH

BY REBECA ROMERO, ICBA

OPTIMISM

"We must work to remain optimistic in the face of adversity and keep in mind that no matter how difficult that feat may be, it's worth the effort."

When I transitioned from a community bank CEO to ICBA president and CEO, my team gave me a beautiful handmade card with notes and best wishes. On the front is a favorite quote of mine from French writer Anatole France: "To accomplish great things, we must not only act, but also dream; not only plan, but also believe." To this day, the card sits on my desk.

I keep it there for sentimental reasons, and because that quote has been a daily inspiration to me throughout my career. It's a constant reminder that it's our choice to see the glass half empty or half full. We must work to remain optimistic in the face of adversity and keep in mind that no matter how difficult that feat may be, it's worth the effort.

Over the past year, community banks have had a crash course in this philosophy. We faced shifting requirements around the Paycheck Protection Program, not knowing if lobbies would be open from one day to the next, the health and safety of employees, friends and families, and so many other situations. Despite it all, community bankers remained committed to the path ahead. By knowing if we just stood the course and held fast to a singular focus on getting through the trials by increasing support for our communities, we would get through it even stronger. That unwavering optimism endured even in the most difficult times.

But it wasn't all smooth sailing. Challenge after challenge emerged. Yet, because community banks focus on the long haul,

we saw these difficulties as opportunities to experiment with new processes, products and approaches — like identifying more streamlined solutions for needs such as document signature and retention, and enabling enhanced remote work and banking capabilities. Thankfully, tenacity, agility and ingenuity helped us steer the ship around the storm and stay on course at our banks, enabling us to better rise to meet the needs of our communities.

So, it's no surprise that as we look at this month's 40 Under 40 winners, it becomes readily apparent that each of these emerging leaders demonstrates resiliency. But they also display a universal sense of optimism, a willingness to do what it takes to meet the needs of their communities. And that can-do outlook sits at the core of community banking. No matter the challenge, we see the light through the storm and persevere because of it. *



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Munis For the Many

Taxable Municipal Bonds Have Appeal For Nearly All Community Banks

BY JIM REBER, ICBA SECURITIES, AN ENDORSED CBA PROVIDER

I have some good news for community bank portfolio managers who have grown weary of some or all the following conditions that have persisted since 2020:

- declining portfolio returns
- erratic cash flows
- call option exposure
- paltry yield spreads

Chances are your bank's portfolio was affected by some of these conditions over the past year. The wild ride in interest rates kept producing surprises for the bond portfolio, and, in truth, the only thing positive to be said is that prices rose — then declined — over that period. So, banks' positions lost value in 2021, but current investment yields improved, which illustrates the mixed blessing.

Over time, one of the enduring determinants of investment performance is sector weighting. More specifically, the more a

bond portfolio consists of municipal bonds, the more likely it will have above-peer yields. According to Vining Sparks, as of Dec. 31, 2020, municipal bonds made up 53% of top-quartile community bank portfolios. At the other end of the spectrum, the bottom quartile was only 9% invested in munis.

Historically, the number of bank-owned munis primarily determines a bank's need to avoid tax liability. Some depository balance sheets have not had room for bonds, muni, or otherwise. Others have not been profitable enough to worry about that option. Still others, such as S Corps that pass earnings to shareholders, do not benefit from tax-free earnings.

Supply shift

Fast forward to the Tax Cuts and Jobs Act of 2017, which reduced corporate tax rates by around 40%. That was good news for bottom lines, but it lowered the effective yields on all tax-effected assets, such as traditional munis and bank-owned

life insurance. Since that time, banks have shed about one-fifth of their tax-frees.

Another subtle but significant feature in that legislation was to no longer allow muni issuers to "pre-refinance" their outstanding debt into other, new tax-free issues. Refinancing older bonds into taxable matters would significantly impact the types of munis issued in the current environment.

In the 2020 calendar year, fully 30% of municipal bond issues were of the taxable variety, a decade-plus high-water mark. Less than ten years ago, taxable munis were but a blip on the new issue screen. They would constitute somewhere between 3% and 7% of total new issuances. The only year taxable munis exceeded 2020's volume was 2010. And that was purely a function of the narrow window for issuing Build America Bonds (BABs), a type of taxable munis only available for issue in 2009–2010.

Crowd pleasers

Now to the afore-promised good news. If your community bank is not much invested in munis, taxables could bring some welcome relief to the issues mentioned in the first paragraph. As supply has grown and the interest rate curve has steepened throughout 2021, taxable munis can serve several purposes, not the least of which is a respectable return. An investor can also now realistically hope for an issue that is reasonably proximate to its footprint.

A high-grade general obligation taxable muni will out-yield a bank-qualified (BQ) issue at any point on the yield curve. As of this writing, a 10-year AA-rated BQ bond will have a tax-equivalent yield of about 1.85%, whereas a similar-duration taxable will be

about 2.10%. There are many reasons, including the relative lack of supply of BQ paper. Also, it bears mentioning that if S Corp banks have tax-free income, they may recognize higher tax-equivalent yields than their C Corp brethren.

What is the downside? As with any other taxable security, municipal bonds will have a higher degree of price volatility than tax-frees. However, the additional price risk is less than it used to be back in the era of 36% marginal rates for C Corps. It is unknown what the impact of higher marginal tax rates will be on the tax-free muni market, but higher rates should be supportive of tax-effected assets.

In the meantime, the growing supply of taxable munis should continue to produce attractive yields. The amount, both in absolute dollars and for a given issue (which is not limited to \$10 million per issuer per year that BQs are), should produce more than adequate liquidity. The benefits and availability of taxable munis should appeal to the many community banks looking for the right combination of risk and reward. *



Jim Reber, CPA, CFA is the president and CEO of ICBA Securities, ICBA's institutional, fixed-income broker-dealer for community banks. Connect with Jim jreber@icbasecurities.com.

FMSI is a small business founded and located in Kansas, specializing in assisting community banks to succeed, a mission consistent with core CBA values. We have partnered with community banks for nearly 25-years providing core advisory services including asset/liability, investment, and liquidity management.

FMSI advisors actively assess market conditions and bank balance sheets of different size, mix, and capital levels. Market conditions are constantly changing presenting opportunities and challenges for CBA member banks. Interest rates are increasing for the first time in nearly a decade and now is a perfect time to partner with a trusted, industry leader.

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The Coming Bankruptcy Wave: A Bankruptcy Overview for Creditors

BY CAMBER JONES, SPENCER FANE



Experts predict a continuing rise in bankruptcy filings as COVID-related debt relief expires. This article intends to provide creditors with a brief bankruptcy overview, including the most common types of bankruptcy cases, to enable them to participate more confidently in the bankruptcy process. Of course, bankruptcy is complex and each case is uniquely nuanced. Creditors should contact a bankruptcy attorney for assistance in responding to specific bankruptcy filings.

1. The Petition

Every bankruptcy case is initiated by filing a bankruptcy petition. A debtor who files under any Bankruptcy Code chapter is required to file certain statements and schedules outlining its financial condition, including secured and unsecured debts. Creditors should review a debtor's petition, statements, and schedules to gain insight into, among other things, the debtor's intentions regarding their obligations and related collateral.

2. The Automatic Stay

The filing of a bankruptcy petition triggers an injunction called the "automatic stay," which temporarily halts most collection actions against a debtor or a debtor's property. It is imperative that creditors not violate the automatic stay. When a creditor receives notice of a bankruptcy filing, it should immediately cease all actions against the debtor, including wage garnishments, collections, foreclosures, and repossessions.

3. Common Bankruptcy Types¹

Chapter 7

Chapter 7 is a "liquidation" bankruptcy. During a Chapter 7 case, a bankruptcy trustee gathers and sells a debtor's non-exempt assets and distributes proceeds to creditors. Where there are no non-exempt assets available for sale, unsecured creditors do not receive distributions. Secured creditors generally retain their valid liens and the ability to enforce them after a bankruptcy case concludes.

Chapter 11

Chapter 11 is a "reorganization" bankruptcy. In these cases, the debtor, acting in a fiduciary capacity as a "debtor-in-possession," typically maintains possession and control of its assets and operates its business during the reorganization process. Often, a creditors' committee is appointed to represent the interests of unsecured creditors.

In a Chapter 11 bankruptcy, creditors have the opportunity to vote on and object to confirmation of a debtor's proposed plan of reorganization. Because a debtor is highly motivated to confirm and effect such a plan, creditors often have substantial power to negotiate their claims.

Specific debtors may elect to proceed under subchapter V of Chapter 11, which simplifies and condenses the bankruptcy process to make reorganization less expensive for smaller debtors. After a Chapter 11 plan is confirmed (approved by the court), payments will be made to creditors according to plan terms.

Chapter 12

Defined as a hybrid of Chapters 11 and 13, Chapter 12 provides a more streamlined bankruptcy process for "family farmers" or "family fishermen" who have regular annual income. Qualifying debtors can propose and implement a plan to pay all or part of their debts over three to five years. Creditors do not vote on a Chapter 12 plan but may object to its confirmation. After a plan is confirmed, the Chapter 12 trustee will distribute funds per the plan's terms.

Chapter 13

Chapter 13 provides a way for individuals with regular income to propose and implement a plan to pay all or part of their debts over three to five years. Creditors do not vote on a Chapter 13 plan but may object to its confirmation. After a plan is confirmed, the Chapter 13 trustee will distribute funds per the plan's terms.

Proofs of Claim

In most bankruptcy cases, a creditor must file a proof of claim, including supporting documentation. The treatment of a creditor's claim depends on whether it is secured or unsecured. Creditors should determine whether their debt is secured, confirm the status and location of any related collateral, and file a timely and complete proof of claim.

Discharge

The result of a successful bankruptcy is an entry of an order discharging the debtor from liability for certain debts.

While the discharge timing varies based on the type of case filed, in all cases, the discharge permanently bars creditors from taking any action to enforce or collect discharged debts.

Regardless of the type of case filed, creditors should protect their interests by participating meaningfully in the bankruptcy process. This participation should include communicating early and often with the debtor and other parties in interest, promptly filing a proof of claim, carefully reviewing a debtor's proposed treatment of claims, and exercising the right to vote or object to a debtor's proposed bankruptcy plan when appropriate.

* On March 27, 2021, President Biden signed the COVID-19 Bankruptcy Relief

Extension Act. A bankruptcy professional can help creditors navigate the Act's effect on their rights and obligations in a bankruptcy case. *

¹ This article does not address bankruptcies commenced under Chapters 9 (municipality bankruptcy) and 15 (ancillary and cross-border bankruptcy) of the Bankruptcy Code.



Camber Jones is an associate at Spencer Fane's Springfield, Missouri office. She is a member of the firm's Banking and Financial Services Group.



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How Will Digital Lending Benefit Your Bank?

BY SIMON M. FISHER, CSI BANKING SOLUTIONS



Digital banking trends have accelerated due to the pandemic, and many institutions have pivoted toward digital transformation. But in the digital lending space, slow-moving institutions still face a disadvantage.

The economic slowdown and obstacles to in-person channels have changed lending demands. These trends, along with intensified competition and high borrower expectations, make loan origination an essential component of your digital banking strategy.

Before the COVID-19 pandemic, CSI conducted a digital lending trends survey of 107 banks. Of the respondents, around 58% prioritized digital lending to increase market share. Further, CSI's 2021 Banking Priorities Executive Report revealed 43% of bankers surveyed planned to prioritize digital lending when asked which technologies they would use to expand their geographic footprint and customer relationships. Though many banks have expedited their digital strategy over the past year, the adoption of digital lending has yet to meet the increased rate of demand.

The pandemic has driven customers to rely on digital channels instead of visiting branches, leveling the playing field between banks and non-bank lenders. As customers weigh their lending options, a seamless experience is a determining factor in their decision. Many banks have traditionally cultivated customer relationships in a branch, but with the prevalence of digital, your bank must now ensure a superior digital lending experience to acquire and retain customers.

Recent events aside, it is wise to broaden lending capabilities. Outdated technology and inefficient processes hamstring your institution against a shifting economy. And a lackluster or incomplete digital experience may drive customers elsewhere.

Exploring the Benefits of Digital Lending

Lending digitalization does more than aid loan processing. According to a recent AITE Matrix Report, digital loan

management software supports your bank's growth by providing the following benefits:

- **Improved User Experience:** A variety of companies — including non-bank lenders — vie for your customers, and brick and mortar banking isn't for everyone. A configurable lending platform integrated into your existing digital solution empowers customers to apply for needed funds without visiting a branch or turning to another provider.

In addition, omnichannel delivery synchronizes online and offline channels, allowing customers to receive lending services from whichever device they choose. Digital lending also enhances the back-end experience, improving lender responsibility. Creating and distributing a loan or transferring information to the core system no longer requires navigating disparate programs.

- **Efficiency Gains:** Digital lending streamlines the lending process and lending compliance while also providing quick resolutions to requests. And like many aspects of digital banking, automating the process saves time and money.

- **Business Intelligence and Analytics:** While big banks have leveraged data to gain market share, many community banks have fallen behind. As customer acquisition costs continue to rise, your institution must drive traffic via digital channels. A robust solution with exceptional intelligence and analytics opens opportunities to increase market share and cross-sell to current customers.

Besides marketing and strategic planning, you can use dynamic intelligence dashboards to reverse engineer the digital lending process. In doing so, you can quickly determine whether you can refinance a loan to save a customer money.

- **Credit Risk Management:** With digital lending, you can immediately feed data from a credit report into the loan

origination system and assess the five Cs of credit for your customers. This feature facilitates quicker turnaround and more confident decision-making.

While matrix-based lending scores may cause concern about overlooking loans or denying important customers, most digital lending solutions allow institutions to set the decision parameters. Immediately, obvious approvals or denials are processed, while others route to you for review.

- **Regulatory Compliance:** Digital lending makes data accessible, rendering manual searches for documentation unnecessary and decreasing the risk of human error. Digital lending platforms provide a complete audit trail for regulatory review, and automation creates a more consistent, strengthened compliance environment.

Automation Does Not Have to Mean Automated Decision Making

Your bank sets itself apart through its personal connection with customers. And because you value those relationships, digital lending may seem like you're sacrificing that human connection. But your bank can find a balance by embracing the right level of automation for your institution and using these tools to inform decisioning. Digital lending automates tasks that were once manual but should not be mistaken for automating the decisioning process.

However, in some circumstances, automating decisions can yield favorable results. For instance, if your institution has a

conservative lending policy, a properly configured digital lending system maintains tight controls and ensures nothing slips through the cracks. Similarly, if your institution is an early adopter of or is highly specialized in a particular type of credit, automation will drastically streamline the process.

Reinventing the Loan Origination Process

Institutions that wish to stay relevant must embrace digital technologies. Digital lending adoption does present some challenges, including upfront costs and vendor management. But you can offset these concerns by embracing automated loan origination tools along with the right digital lending strategy for your bank, allowing you to provide your customers with the service they need while improving your processes. *

Learn more about simplifying digital lending for your bank by watching CSI's on-demand webinar at csiweb.com/what-to-know.



Simon Fisher is product manager, CSI Banking Solutions. Prior to joining CSI, Simon worked as a consultant helping banks around the U.S. conduct core evaluations. Simon has worked many different lending roles for a community bank during his 10-year term, including retail, commercial and mortgage loans. Simon understands the complexity of different loan types and is working to deliver the best digital experience for loan officers as well as borrowers.

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SAFE Act a Decade On

BY WILLIAM J. SHOWALTER, CRCM, CRP

SENIOR CONSULTANT; YOUNG & ASSOCIATES, INC.; KENT, OHIO



We have been dealing with the Secure and Fair Enforcement for Mortgage Licensing Act (SAFE Act) since 2010. Still, questions surface or confusion exists over SAFE Act requirements.

- "A loan clerk quotes loan rates from a non-public rate schedule, along with payment amounts for inquiring consumers. Should she be registered?" (Maybe, she is performing a function of a mortgage loan originator, MLO.)
- "Our head of lending is our SAFE Act Officer. He also handles some mortgage loans, with his name on loan documents. However, his background is in commercial lending, and he has never registered with the NMLS. Do we have a problem?" (Yes, if he is involved in more than five mortgage loans per year, he must be registered.)
- "How often do we have to get criminal background checks for our MLOs? How about when their fingerprints expire?" (Criminal background checks are required only on initial registration. The fingerprint expiration date is only relevant for existing MLOs coming into the bank as new employees. No updating of fingerprints for ongoing MLOs is required.)

These queries reveal that confusion still exists over the requirements and how they impact banks and thrifts.

A little background

Congress enacted the SAFE Act in July 2008 to require states to establish minimum standards for the licensing and

registration of state-licensed mortgage loan originators and provide for the establishment of a nationwide mortgage licensing system and registry for the residential mortgage industry.

The SAFE Act required all states provide a licensing and registration regime for mortgage loan originators not employed by federal agency-regulated institutions within one year of enactment (or two years for states whose legislatures meet biennially).

In addition, the SAFE Act required the federal banking agencies, through the Federal Financial Institutions Examination Council (FFIEC) and the Farm Credit Administration (FCA) develop and maintain a system for registering mortgage loan originators employed by agency-regulated institutions.

The Dodd-Frank Act moved responsibility for the SAFE Act rules to the Consumer Financial Protection Bureau (CFPB), which rolled these rules into Regulation G (12 CFR 1007).

Licensing vs. registration

Most of the confusion at the outset seemed to center on licensing versus registration of mortgage loan originators (MLOs). The issue is deceptively simple.

- MLOs that work for federally supervised banks, thrifts and credit unions (and FCA lenders) must register with the national registry (NMLS).
- MLOs employed by other mortgage lenders (mortgage companies, etc.) must navigate the state licensing and registry system, a much more time-consuming, expensive, and burdensome process that also carries a continuing education requirement.

Coverage

A "mortgage loan originator" is an individual who both takes residential mortgage loan applications and offers or negotiates the terms of a residential mortgage loan for compensation or gain.

The term "mortgage loan originator" does not include individuals who perform purely "administrative or clerical tasks" (the receipt, collection, and distribution of information standard for the processing or underwriting of a loan in the mortgage industry). Nor does a "mortgage loan originator" obtain the information necessary to process or underwrite a residential mortgage loan. Also excluded are individuals who perform only real estate brokerage activities. These are duly licensed individuals or entities solely involved in extensions of credit related to timeshare plans, employees engaged in loan modifications or assumptions, and employees involved in mortgage loan servicing.

"Compensation or gain" includes salaries, commissions or other incentives, or any combination of these types of payments.

MLO registration

An MLO must be federally registered if the individual is: 1) an employee of a depository institution; 2) an employee of any subsidiary owned and controlled by a depository institution and regulated by a federal banking agency; or 3) an institution regulated by the FCA.

The final rule, as required by the SAFE Act, prohibits an individual who is an employee of an agency-regulated institution from engaging in the business of a loan originator without registering as a loan originator with the national registry, maintaining that registration annually, and

MLOs may submit their registration information individually, or their employer institution may do it for them (by a non-MLO employee).

obtaining a unique identifier through the registry. Employer financial institutions must require adherence to this rule by their employee MLOs.

MLOs may submit their registration information individually, or their employer institution may do it for them (by a non-MLO employee). Management should decide which approach will ensure consistency within the institution, especially since prescribed institution information must be submitted to the registry.

This MLO information must include financial services-related employment history for the 10 years before the date of registration or renewal, including the date the employee became an employee of the bank – not just the time they have worked for their current employer.

Employers of MLOs must remember to renew registrations annually for as long as an individual operates as an MLO. The renewal period opens November 1 and ends December 31 each year. If an MLO or bank registration lapses, it may be reinstated during a reinstatement period that begins January 2 and closes February 28 each year.

Other requirements

Bank and thrift managers also should remember that there are specific requirements in this rule for the institution to have policies and procedures to implement SAFE Act requirements and the use of a unique identifier (NMLS number) by MLOs.

At a minimum, the bank's SAFE Act policies and procedures must:

- Establish a process for identifying which employees have to be registered MLOs
- Inform all MLOs of SAFE Act registration requirements and instruct how to comply with those requirements and procedures

- Establish procedures to comply with the unique identifier requirements
- Establish reasonable procedures for confirming the adequacy and accuracy of employee registrations, including updates and renewals, by comparisons with its records
- Establish reasonable procedures and tracking systems for monitoring compliance with registration and renewal requirements and procedures
- Provide independent testing for compliance with this part conducted at least annually by covered financial institution personnel or by an outside party
- Provide for appropriate action in the case of any employee who fails to comply with SAFE Act registration requirements or the bank's related policies and procedures, including prohibiting such employees from acting as MLOs or other appropriate disciplinary action
- Establish a process for reviewing SAFE Act employee criminal history background reports, taking appropriate action consistent with applicable federal law, and maintaining records of these reports and actions taken concerning relevant employees, and
- Establish procedures designed to ensure that any third party with which the bank has arrangements related to mortgage loan origination has policies and procedures to comply with the SAFE Act, including appropriate licensing and registration of individuals acting as MLOs

The bank or thrift also must make the unique identifiers (NMLS numbers) of its registered MLOs available to consumers "in a manner and method practicable to the institution." The bank has the latitude to implement this requirement. It may choose

to make the identifiers available in one or more of the following ways:

- Directing consumers to a listing of registered MLOs and their unique identifiers on its website
- Posting this information prominently in a publicly accessible place, such as a branch office lobby or lending office reception area, and
- Establishing a process to ensure that bank personnel provide the unique identifier of a registered MLO to consumers who request it from employees other than the MLO

In addition, a registered MLO must provide his or her unique identifier to a consumer:

- Upon request
- Before acting as a mortgage loan originator, and
- Through the MLO's initial written communication with a consumer, if any, whether on paper or electronically (often by incorporating it into the signature information for standard letter and email formats)

Banks, thrifts, and their registered MLOs often also make their NMLS numbers available in other ways — such as including them in advertising or on business cards.

As with any compliance rule, banks and thrifts need to ensure they have systems in place to maintain compliance with SAFE Act requirements, including appropriate training for employees involved in the mortgage origination process. *



William J. Showalter, CRCM, CRP is a Senior Consultant with Young & Associates, Inc. (younginc.com), with over 35 years' experience in compliance consulting, advising, and assisting financial institutions on consumer compliance and compliance management issues. He has authored or co-authored numerous compliance publications and articles and developed and conducted compliance training programs for individual banks and their trade associations. Bill can be reached at (330) 678-0524 or wshowalter@younginc.com.

Coverdell ESAs Come with Different Roles

BY ALAYNA DROPE, CIP, CHSP



What are the different roles commonly seen on a Coverdell ESA application?

While they may vary somewhat from one forms vendor to another, the following terms and definitions describe the different roles with Coverdell education savings accounts (ESAs).

Grantor/Depositor: The grantor or depositor is the person who establishes the ESA with the approved financial organization for the benefit of the designated beneficiary and is usually the first contributor. (Be aware that persons other than the one who establishes the ESA may also contribute for the same designated beneficiary.)

Designated Beneficiary: The designated beneficiary is the individual on whose behalf the ESA is initiated. The grantor/ depositor identifies the designated beneficiary on the plan agreement or application upon establishing the account. An ESA may be set up with contributions for a designated beneficiary who has not turned age 18. A new ESA may be established through a transfer or rollover for a designated beneficiary under age 30.

Responsible Individual: When the ESA is opened, the grantor/depositor names the responsible individual on the plan agreement. The accountable individual generally is the designated beneficiary's parent or guardian. Document permitting, the responsible individual may be someone other than a parent or guardian. Only one responsible individual may be named on the plan agreement at a time; on some vendors' documents, a successor responsible individual may be identified.

Death Beneficiary: In the event of the designated beneficiary's death, one or more primary or contingent death beneficiaries may be named to receive the ESA assets. While the IRS model ESA forms do not facilitate the naming of death beneficiaries, most financial organizations use ESA applications or beneficiary designation forms to name death beneficiaries.

When can the designated beneficiary of an ESA be changed?

You must check the plan agreement. The grantor/depositor could elect to allow the responsible individual to change the designated beneficiary to a qualified family member of the designated beneficiary under age 30 at any point in time. Eligible family members include the designated beneficiary's spouse, child, grandchild, sibling, parent, niece or nephew, son-in-law, daughter-in-law, father-in-law, mother-in-law, brother-in-law, sister-in-law, and the spouse of any such individual. A designated

beneficiary's first cousin (but not a cousin of his or her spouse) is also a qualified family member.

When can the responsible individual of an ESA be changed?

There are two triggering events that allow the responsible individual to be changed from the named individual on the plan agreement: the responsible individual's death and if the plan agreement names or defaults to the designated beneficiary as the responsible individual upon the designated beneficiary reaching the age of majority.

If the original, responsible individual dies or becomes incapacitated while the designated beneficiary is still a minor, the successor responsible individual becomes the responsible individual. The successor responsible individual is a person named by either the grantor/depositor when the ESA is established or by the responsible individual at a later time. The successor responsible individual generally is the other parent or guardian unless the document permits the responsible individual to be someone other than a parent or guardian. If a successor is not named, the other parent or a successor guardian will be called the responsible individual.

The grantor/depositor can indicate on the plan agreement that the parent or guardian (or other named person) will continue as the responsible individual, even after the designated beneficiary reaches the age of majority under state law. This person will continue as the responsible individual until all assets are distributed from the ESA or — upon the designated beneficiary reaching age 30 — the account ceases to be an ESA. If not elected otherwise by checking an option in the plan agreement, the designated beneficiary of the ESA becomes the responsible individual when she attains the age of majority (as determined under state law). But if the responsible individual dies or is incapacitated after the designated beneficiary reaches the age of majority, the designated beneficiary will become the responsible individual. *



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How Community Banks Can Prepare for CECL Changes

The FASB's new credit loss model is one of the most significant accounting changes in recent history. The time to act is now — here is how you can prepare and comply.

In June 2016, the Financial Accounting Standards Board (FASB) issued a new expected credit loss accounting standard, which introduced an updated method for estimating allowances for credit losses. The Current Expected Credit Losses methodology (CECL) applies to all banks, savings associations, credit unions and holding companies.

If your institution has not yet adopted CECL, now is the time to refresh yourself on the fundamental changes and — most importantly — to start planning.

What is CECL?

The impairment model introduced by the CECL standard is based on expected losses rather than incurred losses. With that, an entity recognizes its estimate of lifetime expected credit losses as an allowance. CECL also strives to reduce complexity by decreasing the amount of credit loss models available to account for debt instruments.

This change was under discussion for many years before its issuance, with the impacts of the global economic crisis highlighting the shortcomings of the Allowance for Loan and Lease Losses (ALLL) framework. FASB concluded that the ALLL approach delayed recognizing credit losses on loans and resulted in insufficient loan loss allowances.

"There are a lot of decisions that need to be made. By starting as early as you can, you avoid any roadblocks in getting CECL implemented by the deadline." — Brian Lewis, RMSG Senior Risk Advisor

Differences between the previous and the new standards

Previous	New
Loans/leases (could be other valuation reserves)	All debt instruments carried at amortized cost (not those at fair value like AFS securities)
Does not apply to HTM investments	Applies to HTM investments
Threshold = probable loss	Threshold = expected loss
Reporting period focused ("incurred")	Reporting period + forecast ("life of the asset")
Individual assets (specific reserves) + pools at historical loss	Pools of assets with similar risk characteristics + historical loss adjusted for reasonable/supportable forecast period
Quantitative (data-driven) and qualitative (Q-factors)	Shifts focus to qualitative (adjustments based on reasonable forecasts) + quantitative

How will CECL impact my institution?

Adopting the new standard will influence internal controls and information likely not previously integrated into financial reporting efforts. In other words, the scope of CECL is far-reaching — spanning corporate governance, modeling, credit analysis,

technology and others. Additionally, CECL affects all entities holding loans, debt securities, trade receivables and off-balance-sheet credit exposures. In short, it will have significant implications for operations at most financial institutions.

How to proceed toward CECL transition

The time to get started — if you have not already — is now. This is a significant change with extensive effects and potential risks. Careful — and early — planning is critical. Here are nine key steps institutions can take to achieve CECL compliance:

1. Identify functional areas (such as lending, credit review, audit, management, and board) that need to participate in the transition project/implementation and ensure those working in these areas are familiar with the new standard
2. Determine your effective date and whether to adopt early
3. Make a project plan and timeline
4. Discuss the plan and progress with all stakeholders as well as your regulator
5. Determine the ACL estimation method/methods that may be used
6. Identify available data and any other data that may be needed
7. Identify potential system changes
8. Evaluate and plan for the potential impact on regulatory capital
9. Have a straightforward, well-understood process

Finally, it's necessary to take a holistic view to ensure a smooth transition, including:

- Built-in testing for data integrity and method estimation validation
- Update other bank policies and reports so they are consistent with processes
- Consider running parallel with the ALLL to evaluate risks
- Back-test as part of supporting modifications and improvements

What are the implementation timelines?

This standard was effective for many institutions by Dec. 2019, and all others will need to comply by March 2023. These dates are based on the Public Business Entity (PBE) status for institutions. Early adoption was allowed for any institution after Dec. 2018. *

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Lenders' Obstacles: Many Manual Processes Despite Digital Pushes



BY MARY ELLEN BIERY, ABRIGO

If there was a gold medal for financial services, lenders earned it in 2020 and 2021.

The rollout of the Paycheck Protection Program's (PPP), its associated changes, the next tranche of PPP, and the next, and now forgiveness (not to mention bankers' work with some existing business borrowers to modify loans under government programs), has kept staff at banks swamped for more than a year. These factors, most likely, have also kept most lenders deep inside their loan origination systems more intensely than at any other time in their history.

Widely reported, many financial institutions took the opportunity during the COVID-19 pandemic to digitalize some or many of their financial institution's processes and services, including lending.

Abrigo's 2021 Business Lending Process Survey found that a slight majority of respondents (53%) accelerated digital transformation plans as stay-at-home orders and other social distancing measures forced workers and customers alike out of branches or lending centers.

Largest lenders led the digital push

Digital transformation varied somewhat by the size of the financial institution in Abrigo's survey. 77% of institutions topping \$10 billion in assets accelerated digital transformation plans due to the pandemic. That compares with:

- 46% of respondents from institutions with \$3 billion — \$10 billion in assets
- 50% from institutions with \$500 million — \$3 billion in assets
- 52% from institutions with less than \$500 million in assets

COVID-19 and related events also led many banks to refocus on efficiency. Nearly half of respondents in Abrigo's survey said their institution renewed an emphasis on finding efficiencies due to the pandemic.

And just as the larger institutions more frequently reported accelerated digital plans than did smaller institutions, a larger share emphasized renewed efficiency among smaller banks and credit unions.

However, despite digital pushes and efficiency focuses, lenders across the board in Abrigo's survey reported their financial institutions use manual lending processes that add costs, create delays, and make their staff work harder than they must. Some of the same methods are also known for hurting lenders' ability

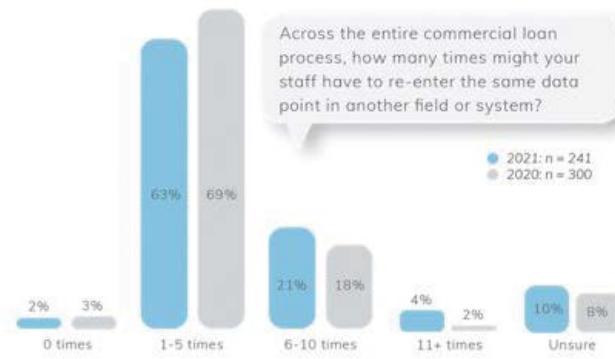
to drive loan growth, manage credit risk, and satisfy customers or members.

Repetitive data entry is a top lending obstacle

One example of processes that add costs, create delays and make staff work too hard is repetitive data entry. Most frequently named as the most significant obstacle to respondents or their institution in the commercial lending process was entering the same data multiple times or in multiple places. 35% of those surveyed identified repeated data entry as their largest lending hindrance.

What is the magnitude of repetitive data entry in business lending? Nearly two-thirds of respondents said their financial institution reenters the same data point for a loan in another field or system up to five times. A quarter of respondents reported entering the data at least six times. In a similar survey by Abrigo in 2020, 20% of respondents said they entered data at least six times.

In addition, only one of every three respondents in Abrigo's survey this year said their institution currently offers the ability to apply online for a commercial loan. Lenders with online applications can often port the borrower data across the origination platform, resulting in fewer repeat data entries. The good news is that a higher share of survey participants said they now offer more online business loan applications than they did last year when only 20% offered them. However, this year 13% of respondents said their institution does not provide or plan to offer online loan applications in the future.



Manual credit memo = more time

Another process typically tied to repeated data entry is the credit memo — unless it is automated.

Only 7% of financial institutions in Abrigo's survey reported using an automated solution to generate the credit memo. Instead, nearly half said their institutions enter this critical information manually. Another 42% reported using a combination of manual and automated methods.

Manual credit memos were most prevalent among the largest institutions in Abrigo's survey this year. Two-thirds of respondents from institutions with assets over \$10 billion reported entering credit memo information manually, and the other third reported using a combination of automated and manual systems.

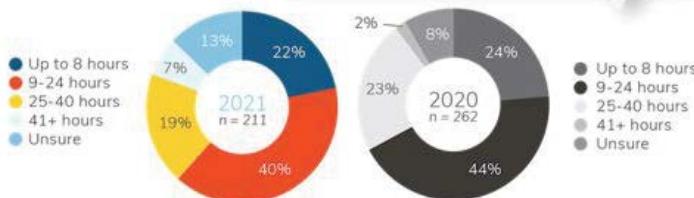
To create a credit memo the loan committee can review, a credit analyst is often inputting data from disjointed systems repeatedly. They must manually input consolidated borrower information, financial ratios, any global cash flow analysis, the assigned risk rating, proposed loan pricing, and terms of the proposed loan. Even using institution-created templates might not eliminate the need to cut-and-paste data, review for errors, and rewrite certain sections, depending on the template and loan. This time spent on administrative tasks throughout the life of the loan ultimately reduces the time an analyst can spend analyzing a business loan. Another potential consequence could be a longer processing time for business loans.

'Speed and consistency make or break a deal'

"Process automation is incredibly important in today's lending environment," said Brandon Quinones, Abrigo's Director of Client Education. "Speed and consistency will make or break a deal, so putting a system in place to drive that automation — enabling financial institutions to spend less time on redundant data entry or requests and more time on value-add activities — is something industry leaders recognize as no longer just an option for their business."

Forty percent of bankers said it takes their institution between nine and 24 hours to underwrite a loan. While 22% said their institutions could complete underwriting in less than a business day, another 19% reported a 25- to 40-hour window, and 7% said underwriting can take more than 40 hours.

How many labor hours does it take your institution to underwrite a loan?



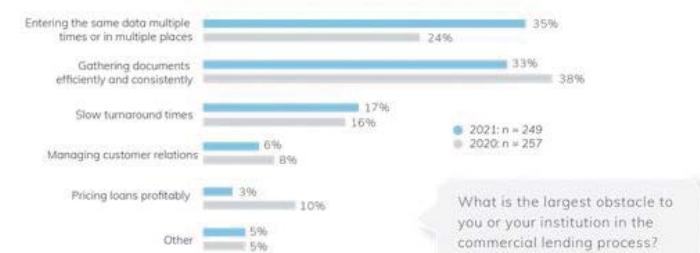
Including all processes, 46% of respondents said their financial institutions take at least five weeks to close a commercial loan. That figure includes many institutions (16% of respondents) requiring eight weeks or more.

Of course, banks focused on commercial real estate loans, which often require appraisals and entail more intense scrutiny than a small line of credit, tend to have longer turnarounds. However, the long wait time for a credit decision is historically the chief complaint among borrowers using small banks for financing. And with the economic outlook improving, lenders looking to grow the business loan portfolio in the quarters ahead with credit-worthy borrowers will face tight competition for them.

Document collection also a pain point

Another ongoing obstacle to the lending process, according to survey respondents, is being able to collect required documents. A third said gathering business loan documents efficiently and consistently is the most significant obstacle in their institution's commercial lending process. This was also the most frequently identified top lending obstacle from respondents in Abrigo's 2020 survey.

Asked about their biggest headache related to loan ticklers, the documents required for every loan file, 65% of respondents said it is tracking and following up on missing items. Only 17% of respondents said their institution uses automation for ticklers.



In addition to gauging the current state of digitization and automation within financial institutions' business lending processes, the Abrigo survey also assessed how banks are approaching other areas of business lending, including pricing loans, assigning credit risk, and growing their portfolio. The 2021 Business Lending Process Survey results highlight the importance of institutions finding ways to overcome inefficiencies and inconsistencies to scale loan growth and manage risk.

Some processes vary by institution size. For example, the highest share of respondents from institutions with more than \$500 million in assets said they set prices on loans based on internal profit measures, such as return on assets or return on equity. But among lenders with less than \$500 million in assets, the top loan pricing method was setting prices based on lender discretion and negotiation with the client.

Abrigo surveyed nearly 250 lenders, credit analysts, chief credit officers, chief risk officers, and other professionals involved in lending and credit risk at banks and credit unions in an online survey between Feb. 18 and March 23, 2021. *



Mary Ellen Biery, senior writer and content specialist at Abrigo. Abrigo is a leading technology provider of compliance, credit risk, lending, and asset/liability management solutions that community financial institutions use to manage risk and drive growth. Visit abrigocom to learn more.

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