The Regulatory Focus

The Division of Financial Institutions

October 2016

John R. Kasich, Governor | Jacqueline T. Williams, Director | Charles Dolezal, Superintendent | Kevin Allard, Deputy Superintendent

Strategic Planning: A Regulatory Perspective

Now is the time for boards of directors to focus on strategic planning. Banks have emerged from the financial crisis with improved levels of capital, earnings and liquidity. Problem asset portfolios have been resolved. It is now time to look toward the future. Community banks, savings banks and savings associations have many opportunities open to them. Proper strategic planning will allow boards of directors to set a course for growth and success.

Strategic planning sets priorities and focuses energy and resources. There are many models available for strategic planning, but no one right model. Each board should find something that works best for its bank. Most include very similar concepts – to define strategy, or direction, and make decisions to allocate resources to pursue that strategy. In other words to decide – Where are we now? Where are we going? How do we get there? Are we on track?

In this issue:

Though often tasked with developing the strategic plan, directors cannot develop a plan by themselves. It takes input from employees, customers and even your competitors. Employees are the people that, to a large degree, will carry out the strategic plan – their contribution and buy in is crucial. A key element of a strategic plan is feedback from your customer base. If you do not provide the services they want, and where and how they want them, a bank cannot survive. By evaluating your competition, you can determine what differentiates your bank. What makes your bank more appealing than the bank down the street?

The elements of a strategic plan

There are four basic components of a strategic plan – Places, People, Products, and Financial Elements. All four of these components are interrelated and each has to be considered relative to the other components. Projected changes in any of these components have an impact on the other three.

- Places: The plan should determine where and how you will conduct business. This includes the use of bricks and mortar – the necessary facilities for customer service and bank operations, and the branching system – the number and locations. Things to consider are where you want to operate, where are your customers, are local communities

Continued on page 2

shrinking or growing, are you going to acquire branches or will you be adding branches or acquiring a bank? It also includes the use of electronic and/or mobile banking, the effectiveness of the ATM network, and the IT department infrastructure, capacity, and security. The IT service provider should be evaluated to make sure that it will meet any changing needs.

Proper strategic planning will allow boards of directors to set a course for growth and success.

- People: The "people" aspect is very broad based and is multi-faceted. It involves not only the people that will carry out the plan—the staff, senior management, and the directors—but also existing customers and potential customers. Expectations and demands of customers, employees, directors and shareholders vary greatly and may often conflict.

The plan needs to address the effective and efficient use of the institution's human resources. For employees, managers and directors, it means training, segregation of duties and succession planning. Board vacancies should be filled quickly with a person with previously-identified desired qualities. Vendors or contract workers (e.g., auditors, accountants and attorneys) should be evaluated.

The strategic plan must also address the desired customer base. The board should identify who you want as customers and how to retain or attract them. Look at demographic data – what is happening in your market area? Marketing to different generations can be challenging. Each may want different products and delivery channels.

Shareholders want dividends, high levels of earnings per share, undiluted ownership, and increasing market value – all of these may be at cross purposes if aggressive asset growth is your strategy.

Products: It is important to look at the products the bank offers. Review them from a viewpoint of obsolescence and cost effectiveness. Look at products from the standpoint of their appeal to current and targeted customers. Remember that concentrations in product lines can increase your risk profile and they may require additional expertise to manage them.

- Financial Elements: Without a doubt, almost all strategic initiatives have short- and long-term financial impacts upon the bank – some positive and some negative. Income and expenses, capital levels, concentrations of credit and/or funding sources, growth rates, interest rate risk and balance sheet mix can all be affected. Capital levels must be commensurate with the risk profile of the bank. New products, services, markets, etc. can elevate risk and may necessitate higher capital levels. The need for additional capital creates new challenges. The marketability of your stock has to be determined - can you sell it, to whom, how much can you raise, and will any change of control thresholds be met are some of the questions that will need to be answered.

The impact of all of these four elements should be incorporated into financial projections for generally three to five years. Strategic planning involves making many assumptions. It is not an exact science. There are many external factors that impact your bank (e.g., economic swings, natural disasters, unemployment and terrorism) for which you cannot control or specifically plan. You can plan somewhat how you react to them.

Evaluating strategic plans

Examiners will review a bank's strategic plan as part of a routine examination. Although models may vary, they are looking for some standard concepts.

- Group Effort: This should not just be the vision of the management team or just the board throughout the entire process. For success, you have to have buy in from everyone. If a consultant is used, the plan should be customized to your bank, and it still takes considerable effort by everyone involved.
- Realism vs. Idealism: The plan has to be feasible and attainable. If goals cannot be

Continued on page 5

Cybersecurity Threats Are on the Rise: Are You Protected?

Cybersecurity is a growing concern. Financial institutions have long been dependent on technology systems to manage data and conduct daily affairs, but as the role of technology systems has evolved and expanded to new platforms, the risk of outside attacks on those systems continues to increase. Cyber criminals have become more

sophisticated and pose a multitude of risks to financial institutions. If a breach were to occur, the costs associated with forensic investigations, public relation campaigns and legal fees could be significant. It should come as no surprise, then, that mitigation efforts are receiving increased scrutiny by regulatory agencies. And regulatory agencies like the Division of Financial Institutions are here to help.

While we are all too familiar with the irony of the phrase "I'm from the government and I'm here to help," the Federal Financial Institutions Examinations Council (FFIEC) released a helpful tool that will impress even those most skeptical of regulatory intentions. On behalf of its members, the FFIEC developed a Cybersecurity Assessment Tool, or CAT. The CAT is a repeatable and measurable assessment process to help financial institutions identify their cyber risks and evaluate their readiness against potential cyberattacks.

> *If a breach were to occur, the costs associated with forensic investigations, public relation campaigns and legal fees could be significant.*

The CAT provides guidance on the respective roles and responsibilities that CEOs and directors should play in the assessment process, and guidance and useful questionnaires to assist in the assessment process. It also provides a framework that incorporates IT industry standards.

The process itself is divided into two parts. The first part assists management in measuring the institution's inherent risk profile with respect to cybersecurity. The inherent risk profile is measured considering the following five elements:

- Technologies and Connection Types
- Delivery Channels
- Online/Mobile Products and Technology Services
- Organizational Characteristics
- External Threats

The second part of the process, referred to as cybersecurity maturity, measures the institution's level of risk and mitigating controls across five key areas or domains:

- Cyber Risk Management and Oversight
- Threat Intelligence and Collaboration
- Cybersecurity Controls
- External Dependency Management
- Cyber Incident Management and Resilience

A review of the institution's inherent risk profile in relation to its cybersecurity maturity status will reveal if misalignment exists amidst any of the domains. If a misalignment does exist, strategic actions may be needed to change the inherent risk profile or risk management practices and controls may need enhancement to achieve the desired cybersecurity maturity.

All financial institutions should have an effective cybersecurity program that periodically measures inherent risk and cybersecurity maturity on an enterprise-wide basis. Additionally, changes in business strategy or development of new products and services should also be evaluated for their impact to cybersecurity preparedness. While not intended to replace an institution's risk management process and cybersecurity program, the CAT provides a clear, comprehensive and useful approach to complement the cybersecurity assessment process. And best of all, it's free!

Financial institution managers and directors should review the CAT and consider incorporating it into their cybersecurity governance processes. The [CAT, instructions, guidance, questionnaires, and a helpful video presentation] are available on the FFIEC website ([www.ffiec.gov/cyberassessmenttool.htm]). ■

From the Superintendent

Superintendent Charles Dolezal

Welcome to the Summer edition of *The Regulatory Focus*. With continuing improvement in market conditions and moderate to strong loan growth, I am pleased to report that Ohio-chartered banks and savings institutions are doing well, with the number of regulatory actions at an all-time low.

However, Bankers continue to experience challenges in several areas, including a changing customer base that desires more mobile transactions, new TRID regulations from Washington and competition from online lenders. With the baby boomer generation starting to retire, community bankers are finding it difficult to attract and retain talent. As a result, they must focus their energy on professional development and succession planning.

These and other issues including CECL and vendor management will be topics of discussion at our upcoming Fall Regional Roundtables, the dates of which are listed in this newsletter. I hope you will put these on your calendar and be sure to join us.

Last but certainly not least, I'd like to take this opportunity to share with you the 2016 Annual Report for the Ohio Department of Commerce. In addition to the Division of Financial Institutions, the Department works in many diverse areas to keep Ohioans safe, sound and secure. You can read the report on the Department's website: bit.ly/AnnualReport16.

As always, if you have any questions on these or any other topics, please feel free to contact me directly at Charles.Dolezal@com.ohio.gov or 614-644-7501. ■

Announcements

Annual Fall Roundtables Scheduled

Save the Date! The Division's Annual Fall Roundtable dates have been scheduled. The topics that will be covered in the Roundtables include an update on state and regional banking conditions, CECL: what bankers should be doing now to prepare, CRE concentration risk management, and shared services: risk management considerations.

Sessions include:

- October 24: North Canton
- October 27: Bowling Green
- November 2: Blue Ash
- November 8: Athens
- November 14: Columbus

Register online.

If you have any suggestions for topics to be discussed, please contact Deputy Superintendent Kevin Allard at Kevin.Allard@com.ohio.gov. ■

Division Supervisor Instructor for CSBS School

Robert Rusbacky, Regional Supervisor for the Division's Southwest Ohio region, recently served as an instructor for the Conference of State Bank Supervisors (CSBS) Credit Evaluation School, held in April 2016 in New York City. The Credit Evaluation School is designed to provide basic training on reviewing and analyzing credit. Bob provided instruction to examiners with the New York Banking Department. He taught the course again in August. ■

DFI Superintendent Elected to National Leadership Position

Superintendent Charles Dolezal was elected as Chairman Elect of the Conference of State Bank Supervisors (CSBS) Board of Directors at the May 24 CSBS annual membership meeting held in Denver, Colorado. Superintendent Dolezal is an active member of CSBS and has served in various capacities, including serving on the Board of Directors and Executive Committee since 2014. ■

How to Contact Us:

Ohio Department of Commerce - Division of Financial Institutions

77 South High Street
21st Floor
Columbus, Ohio 43215-6120

Tel: 614-728-8400
Fax: 614-644-1631
TTY/TDD: 800-750-0750

www.com.ohio.gov/fiin
E-mail: webdfi@dfi.com.ohio.gov

Charles Dolezal, Superintendent
Charles.Dolezal@com.ohio.gov
614-644-7501

Kevin Allard, Deputy Superintendent
Kevin.Allard@com.ohio.gov
614-728-2631

Sheila Schroer, Chief Examiner
Sheila.Schroer@com.ohio.gov
614-644-6228

The State of Ohio is an equal opportunity employer and provider of services.

Strategic Planning, cont'd

achieved, then they are useless. They should be challenging, but reasonable.

- Communication: General communication between the board and employees, and feedback from customers is vital during the entire process from development throughout implementation. Goals cannot be achieved if no one knows what they are. Information has to flow from the board, but also back up to the board as the plan is implemented.
- Monitoring: There should be a mechanism to monitor progress so that you can adapt for changing conditions or necessary course correction. This allows for accountability in achieving various provisions of the plan. Regular monitoring will disclose if a certain initiative gets off track, because the earlier it is found, the easier it can be addressed.

Strategic planning is time consuming, but the exercise will yield significant benefits. It will allow you to take advantage of opportunities and mitigate risks by leveraging your strengths and addressing known weaknesses. ■

Ohio Banking Commission

- Kevin Allard - Chairman, Division of Financial Institutions
- John Brown - President/CEO, Security National Bank, Springfield
- Harvey Glick - former President/CEO, Insight Bank, Columbus
- Mark Klein - President/CEO, The State Bank & Trust Co., Defiance
- Jordan Miller - President, Fifth Third Bank, Columbus
- Eddie Steiner - President/CEO, CSB Bancorp, Millersburg
- James Smail - Chairman, The Monitor Bank, Big Prairie

Savings and Loan Association & Savings Bank Board

- Kevin Allard - Chairman, Division of Financial Institutions
- Fred DeBiasi - President/CEO, American Savings Bank, Middletown
- Robert Lameier - President/CEO, Miami Savings Bank, Miamitown
- William Martin - President/CEO, Mercer Savings, Celina
- Deborah Schenk - Former President/CEO, Mechanics Bank, Mansfield
- Thomas Westfall - President, The Arlington Bank, Upper Arlington