CUNA CFO COUNCIL

NEWS

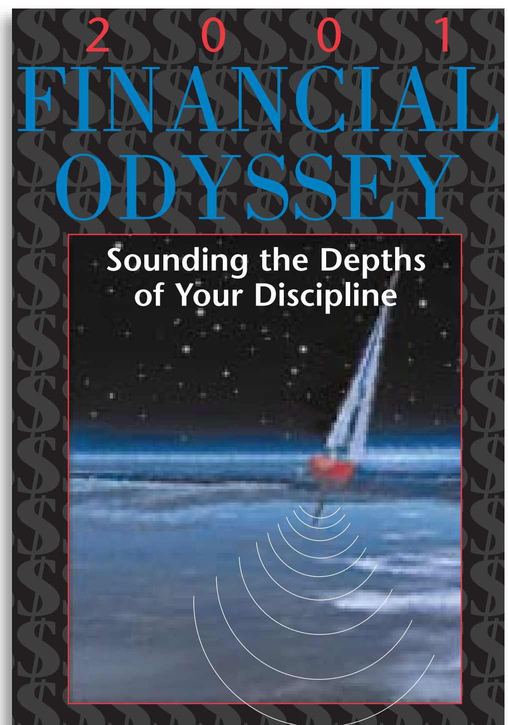
AUGUST 2001

AN ELECTRONIC REPORT FROM THE CUNA CHIEF FINANCIAL OFFICER COUNCIL

Conference Summary

by Judith Hillock, CFO
Research Federal Credit Union

Our seventh annual conference "2001 Financial Odyssey" included 200 financial professionals from various states that came to Seattle to partake in educational sessions and networking opportunities that were second to none. Our conference began with sunshine and inspiring speakers. Rick Neuheisel, Head Football Coach of the Washington Huskies, was our opening speaker. His humor and words of wisdom inspired us all. His strategy for creating a winning football team is the same strategy we can use for creating a top-performing credit union team. Rick stressed that importance of creating a vision, assessing team strengths and motivating them to reach the vision.



Two sessions at the recent CFO Council had a strong impact on me. The first dealt with employee problems such as how to deal with employees who don't want to take responsibility. Through effective COACHING skills, Carol Schillios of Schillios Consulting Group, Edmonds, WA, demonstrated how to address this and other difficult employee situations. Carol shared skills and strategies she has found in her experience working with managers and supervisors to be key in coaching employee performance. Here are key points that had an impact on me:

1. Facilitate discussions that create a two-way dialogue.

When employees feel they are a part of a discussion, they are more likely not to respond defensively. Two-way discussions also keep managers from coming across as lecturing.

2. Uncover employees' needs and concerns through probing.

Employees often come with apprehensions disguised as complaints. When managers help employees discover their own needs, it helps employees find their own solutions.

3. Keep discussion focused on issues, not personal attacks.

Employees often bring up issues in the form of personal attacks. By helping employees learn to address issues, not personalities, relations among employees improve.

4. Identify measurable behaviors to effect performance change.

Have you ever told your employees to "improve their attitudes"? Most employees will not change behaviors if they do not understand *what* to change or *how* to change it. If you cannot measure the behavior it is mostly likely unclear and performance will not change.

5. Help employees develop problem-solving skills by "out-loud" thinking processes.

Managers make decisions based on silent analysis models they automatically process silently. By speaking, their thinking processes out loud, employees learn the skill of problem-solving and are more likely to come with solutions.

6. Verify agreements and let employees come up with what the consequences of not changing will be to their own success.

When employees understand the personal impact of not changing and make a commitment to action, they are mostly likely to change behaviors.

After 26 years of consulting, Carol found that the key to long-term change is managers who have the **courage** to call people on behaviors that do not support the values of the organization. Carol works with credit union's to first identify their management philosophy and values, which form the base from which coaching follows. She commented that credit unions with values written down and shared with all employees have a guidepost against which to measure the success of the management team. Carol's firm can be reached at (425) 775-7391 or by e-mail at cyschillios@msn.com.

The second session that sparked my interest was a two-hour workshop presented by Jerry Hubbard, President, and Jim Douglas, SVP, of First Tennessee Capital Assets, Memphis, TN. This workshop, "Managing the Dynamics of the Mortgage Portfolio," was based on the philosophy that the loan portfolio is an investment asset, no different than the bond portfolio and that the processing of the lending is an investment activity, no different than buying or selling bonds.

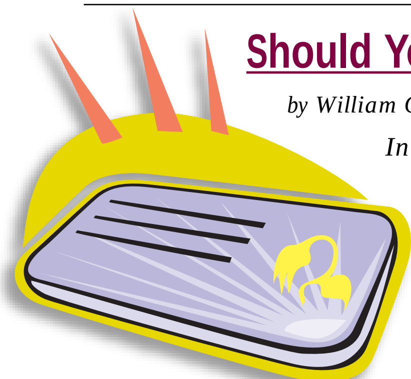
By relating to the loan portfolio from this point of view, credit union CFOs will see the difference between a good credit loan and a good loan investment. The result will be better returns and less balance sheet risk. This is a critical aspect of balance sheet management because loans are now one of the largest earning assets on thebooks of credit unions today. Due to the size of this investment, the economic performance of the loan portfolio will have a major influence over risk and profitability.

All CFOs in attendance had the opportunity to review a Portfolio Performance Analysis, which was prepared by First Tennessee Capital Assets Corporation. After the review of the sample credit union, we were able to see how the following three components fit together. 1) What do I own? 2) What is it worth? 3) What is its likely future performance? First Tennessee Capital Assets Corporation can be reached at 1-800-456-5460 or by e-mail at jim.douglas@ftcm.com.

Mark your calendar for next year's conference. It is scheduled for June 2-5, 2002 in Williamsburg, Virginia. ◆

Should You Sell Your Credit Card Portfolio?

by William C. Koo, Chief Executive Officer, AssetExchange.com, Portland, OR



In the last issue of CFO News, Mr. Koo covered several reasons for selling a credit card portfolio to managing a credit union's balance sheet. In this second part, you'll learn about critical factors in the sale process and what kinds of offers you can expect.

Critical Factors in the Sale Process

If you've examined your portfolio and found reasons to sell, what's next? Unless you are familiar with selling a credit card portfolio, the process can be confusing and create an unnecessary amount of work: data preparation, finding buyers, countless phone calls, responding to potential buyers' requests, and so on. It helps to work with someone who can guide you through the process and help you explore your options to get the best offer.

Getting Strong Offers from Multiple Buyers

It is important to get multiple offers so you can find the party that most values your portfolio. Buyers will make more aggressive offers if they know that others are bidding for the same portfolio. That's why you should maximize the exposure of your portfolio to as many qualified buyers as possible. You may want to employ a resource such as a secondary market exchange to help you. Such organizations can notify hundreds of potential buyers efficiently and easily share information with potential buyers using the Internet. At the same time, they can provide confidentiality and anonymity using the latest technology.

After obtaining broad exposure and multiple bids, you, your board, and regulators can feel confident that you have obtained a competitive and attractive offer.

Efficient Presentation of Portfolio Data

Dealing with multiple buyers on your own can create tremendous work for your team. Each buyer will have his or her preferred data requirements and format. Responding to multiple buyers' requests just to get a preliminary bid can create weeks of headaches. Organizations like AssetExchange can help alleviate this problem by providing a standard template that has been accepted by buyers as being comprehensive and complete. That way, data on your portfolio can be provided just once.

Anonymity and Confidentiality

It is usually best to retain anonymity for your credit union as you move through the initial stages of the sale process. Your position is stronger if you reveal your identity only to the final buyers. You'll remain in control of the process if you have the ability to determine what information is shared, and who sees sensitive detailed data.

Experience and Guidance

Perhaps this is the most obvious consideration, but make sure you work with someone who knows the secondary market for credit card portfolios, and can guide you through the process. Check the credentials of those organizations and individuals assisting you, and know their track record. Knowledge in one area of loan portfolio sales may or may not extend to credit card portfolios. And, of course, ask about their fees, exclusivity period, and other terms.

What Offers Can You Expect?

Selling is No Longer Just for the "Big Players"

In the past, "smaller" portfolios of less than $50 million received little attention from buyers. When working with traditional brokers, the fees on smaller portfolios made the transactions prohibitive. Now, even card programs in the $5 million range are attracting multiple buyers. That, coupled with the ability of secondary market exchange companies to provide wide exposure and assistance in the sales process, makes even small transactions practical and cost-effective.

110%–120% Offers, Plus On-Going Revenue Sharing

It is not unusual for credit unions to receive offers of 110–120% for their credit card balances. In addition to the high premiums, buyers are offering on-going revenue sharing. Such revenue sharing can be a combination of payments for new accounts, a percentage of net sales, a percentage of interchange, and/or a percentage of finance charges. Sellers are finding the quarterly payments, plus the premium on the sale, to be quite compelling.

Strengthen Your Portfolio's Credit Union Brand

Most buyers are aware of the close relationship between credit unions and their members, and for that reason, they will continue to promote the credit union name and brand in the card programs they purchase. While the buyer will be responsible for the costs of obtaining new cardholders and growing their balances, credit union input in these activities is encouraged. In fact, if executed well, many credit union members will not even be aware of the new card issuer. It is also assumed that the buyers will not cross-sell non-card products.

When Selling Makes Sense

The financial and strategic rewards of selling your credit card portfolio, added to a renewed ability to focus on other core services, can outweigh the benefits of keeping the card program. Should you choose to sell, there is a receptive market waiting for you.

About AssetExchange

AssetExchange (www.AssetExchange.com) is a network of 700 executives at credit unions and other financial institutions that buy and sell participations and loan portfolios. AssetExchange allows sellers to post summary information describing loan portfolios for sale, and allows buyers to be notified when particular assets are available. With the seller's approval, members may download spreadsheets with portfolio details. AssetExchange helps buyers and sellers efficiently find each other and manage the sale process. William C. Koo can be reached via e-mail at wkoo@assetexchange.com or by phone at 503-220-0007, ext. 100. ◆

Intranets and Credit Unions

As credit unions "morph" periodically in response to the endless demands of today's evolving workplace, a company intranet becomes a savvy business decision, crucial in maintaining a competitive edge. Now credit union professionals can arm themselves with contemporary strategies for achieving goals as detailed in the timely new handbook, *Intranets & Credit Unions*, in which author Sarah White makes a compelling case for the cyber-tool no credit union should be without. This book was co-branded by the CUNA Human Resources Council, which also assisted with expert content reviews.

An intranet can be an ideal virtual human resources office, and White describes what that entails while anticipating readers' needs in reaching the objective. She responds throughout the book with such useful devices as: a sample letter soliciting CEO support and articulating the credit union's need for an intranet; a cost/benefits analysis with a return-on-investment formula; even a step-by-step guide with IT instructions for the building and upkeep online. Produced by CUNA & Affiliates Center for Professional Development, *Intranets & Credit Unions* is a most practical resource.

For the 56% of credit unions already having an intranet, this book can be a measure of maximum benefit. A model intranet should help recruit and retain employees, offer pre-employment testing, provide online training for workers as needed or desired, and become a "one-stop shop" for communication with staff.

The virtual HR Office may host policies and procedures, a calendar of events, the credit union newsletter, monthly or quarterly reports, tax forms, the time-reporting procedures (for hourly staff), or a union contract. Restricted areas can be controlled with log-in protocols or passwords. The intranet can even be a scrapbook or album featuring photographs of events to build team spirit, and a sense of the credit union culture.

The employee handbook can be posted online, saving your credit union publishing and distribution costs on an item that could change in a few months, as new pension laws or other policies make it obsolete. On an intranet, new information can be posted anytime with an email message sent to staff to inform them of the change. Digitally encrypted signatures assure you that all have seen the changes, in a quick, efficient turn-around.

This top-notch resource also alerts legal departments to ramifications associated with two potential problem areas in posting the employee handbook online: discipline and pensions. If the manual spells out disciplinary steps, you are legally required to follow them to the letter. And, pension laws can change frequently rendering your intranet out-of-date. Revisions must be timely to reflect the latest rulings.

If you are in the planning stages of intranet development or considering it down-the-road, *Intranets & Credit Unions* is the kind of check list that can help you along the way. Focused primarily for Human Resources professionals, this handbook will be found on senior management, IT, and legal department bookshelves as well.

You can order this book by calling CUNA Customer Service at 1-800-356-8010 extension 4157. The cost is $39.95. CUNA Council members receive a 10% discount on this and other CUNA handbooks. ◆

Don't Get Burned by Hot Money

by Sally Myers, Chief Executive Officer and John Myers, President, C. Myers Corporation, Phoenix, AZ

The sputtering economy and the sagging stock market have uncovered a combination of dangerous risks for many credit union executives and board members. A flood of liquidity in the first quarter, stagnant loan demand, and a fear of increasing bankruptcy filings are risks that have become front burner issues.

The flood of liquidity that has pooled in many credit unions can be the trickiest of these risks. Excess liquidity can create temptations that seem innocent enough on the surface. Below the surface lurk dangers that are not often noticed until it is too late.

Before we explore those dangerous waters, let's rewind to about this time last year. The dynamics were very different. The issue of liquidity was 'too little' as opposed to 'too much.' Loan demand was high, but attracting low cost shares was very difficult. For credit union executives, stagnant or shrinking low cost share balances as a percentage of assets were a major concern. Consumers, on the other hand, continued to become more savvy. They wanted to see their excess cash working for them.

In recent years, low-cost money sitting in share accounts started a noticeable migration to higher interest accounts or more risky instruments such as equities. For example, in 1998, higher interest money market shares and share certificates represented about 53% of aggregate share growth in credit unions. For 1999, the figure was roughly 60%. For 2000, the figure was nearly 83%.

Almost overnight, consumer behavior has shifted away from more risky instruments such as equities. This change has caught most everyone by surprise. Driven by fear caused by an uncertain economy and an unmerciful stock market, billions of dollars have flocked into insured credit unions and banks. Some credit unions experienced annualized deposit growth rates of 25% and more in the first quarter of this year. It was a flight to safety and, when it flies in that fast, it is called 'hot money' even when it goes into regular shares. It could be dangerous for credit union CEOs and CFOs to lose sight of the reality that 'hot money' can fly away just as fast.

Hot money has no loyalty and it has no pride. Hot money is quite selfish. If it wants the highest rates, it will go to the financial services organization that can meet that need. If it wants temporary shelter from uncertainty, it will duck into an insured credit union or bank and stay just long enough until the weather clears.

Could the weather be clearing?

In April the Dow Jones Industrial Average skyrocketed, adding 856 points. If this is the beginning of a trend, is it reasonable to think that the funds representing recent liquidity growth will just as quickly fly away? If a primary reason for being in business is to maintain safety and soundness in order to serve member needs, then your answer needs to be yes.

But wait! In March the Dow Jones Industrial Average experienced a breathtaking (not to mention wealth-taking) 617 point loss. Is April's skyrocketing gain a trend-setting event after all? Maybe. Maybe not. In May it was up 177 points over April.

We can be certain of three things. First, we are in volatile times. Second, nobody can predict the future. Third, the more you understand about the possible long-term financial consequences of decisions you are considering, the better your decisions will be.

Many decisions being made today will help if rates continue to go down — but can hurt if rates turnaround and go up. So, what do you do? To be safe and sound, and adaptable, it is necessary for you to understand, in advance, the potentials for long-term risks to earnings and net worth in the event the position you take on rates proves wrong.

The Temptations

Now, what about the innocent appearing temptations of excess liquidity? When there is excess liquidity, as in today's environment, there is the temptation to reach for yield in the investment portfolio. You don't reach for yield by investing in Fed Funds or short-term Treasuries. To reach for yield, you have to invest longer-term and/or purchase investments with embedded options.

Many credit unions reached for yield in exactly this manner three short years ago when 3-month Treasuries hit a low of about 4% and 10-year Treasuries dropped below 5%. This reach often was in an effort to achieve predetermined earnings objectives. (Attempting to achieve a predetermined earnings objective, regardless of what happens with market rates, can be dangerous.)

Unfortunately, some of those credit unions were burned when rates increased slightly in 1999. When this happened, they were faced with undesirable options. A couple are described below.

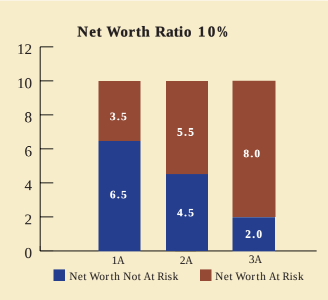
Fearing that rates would continue to increase, many opted to sell investments or mortgages at a loss. Others opted to wait it out, paying even higher dividends on their short-term certificates or money market accounts in order to retain funds to continue to support existing commitments to long-term fixed rate assets.

Before Deciding

So, before making investment strategy decisions, ask yourself the following question.

What is the primary objective for my investment portfolio? For example, is it liquidity? Is it earnings? Is it to help offset potential risks in other areas of my financial structure?

Liquidity, earnings and balancing of potential risks are very different objectives and each can call for a completely different investment strategy. However, investment strategy cannot be decided in isolation. For effective risk management, it is prudent to make integrated deci-



Net Worth Ratio At Risk[2] (red) and Net Worth Ratio Not At Risk (blue)

Risk Profile Net Worth Ratio 10%	Current Situation - 1A Short-Term Investments Generally < 1 year	Strategy - 2A Intermediate-Term Investments Generally < 3 years	Strategy - 3A Longer-Term Investments Generally < 5 years
Increase In Earnings From Current Situation	N/A	+ 6 basis points	+ 11 basis points
Short-Term Rates That Could Trigger Negative Earnings	8%	7%	7%
Well-Capitalized[1] Up Through Short-Term Rates at...	12%	10%	9%

sions. In other words, consider your entire financial structure. This would include your loan and deposit strategies, your operating expense structure, your fee and other income strategy and, of course, your net worth ratio.

While considering your entire financial structure, ask yourself these additional questions and get reliable answers. They will help you to avoid unwanted surprises.

In considering various investment strategies, what are potential financial consequences for my entire financial structure?

Are the potentials for long-term risks to earnings and net worth acceptable for my entire financial structure?

For example, your current investment portfolio may not be yielding much, but it could be helping to offset risks in other areas, making your entire financial structure positioned for safety and soundness, regardless of how rates change. If you reach for yield in your investment portfolio without considering your entire financial structure, you may be faced with undesirable options as well as excessive risks to net worth.

Why not know?

Following are examples of long-term risks to earnings and net worth. In each example the loan and deposit structures are the same, as are net operating expense structures. The net worth ratio is 10%. The only difference is the investment strategy. Investments represent 25% of assets in each case.

You intuitively know that longer-term fixed rate investments can increase risk in a rising rate environment. However, often it is not intuitive to know how material the increase in risk can be. You may be in the position to take on additional risk, but that risk needs to be quantified.

The Decision Steps

You will sleep better at night, especially in uncertain times, if you follow three basic steps in your decision making process. First, the only risk you have right now comes from commitments you have already made. Don't make any decisions about new business, including hot money, until you quantify and understand potentials for earnings, losses and long-term net worth at risk from your current commitments.

Second, decide risk limits, especially how much net worth you are willing to put at risk. You are in the business to take and manage risk for the benefit of your members. Additionally, each person has a different tolerance level for risk. It is prudent to have your board and management on the same page with respect to risk limits. That way, if risk is realized, it is not a surprise to anyone.

Third, almost every decision can change your long-term risks to earnings and net worth. Before you implement decisions, quantify and understand potential changes in long-term risks to earnings and net worth. Many CEOs and CFOs have found it is much easier to see ahead of time the potentials for long-term risks to earnings than it is to experience the risks and be surprised by it.

Think of it this way: what is the benefit of choosing not to know, when knowing is an option? ◆

[1] *Capitalization classification defined by the Credit Union Membership Access Act.*

[2] *Net Worth Ratio At Risk from losses that could occur due to interest rate risk exposures.*

Committee Chair Updates

The CFO Council has five committees made up of volunteers that work to enhance the value of Council membership. Here is an update on current committee activities and plans for the future:

Conference Committee—

Alan S. Wade, *Chair*

Members of the Conference Committee held a teleconference call to continue the planning process for the **2002 CUNA CFO Council Conference,** which will be held on **June 2-5, 2002 in Williamsburg, Virginia.** Committee members Alan Wade, Judith Hillock, and Frank Vassallo discussed a wide range of issues, including potential conference themes, topics, speakers and social events. The committee has already received significant assistance from other members of the Council, including Brady Cole, CFO of Navy FCU, and Ron Hoopes, SVP of Administrative Services at Navy FCU. Ron has extensive experience in organizing strategic planning meetings. Jay Scungio, CFO for WMASS Telephone Workers CU, has offered to procure a dynamic speaker that he highly recommends.

We are also pleased to announce that the first Partners in Finance patron has been secured. Travelers Express has committed to a contribution of $5,000 toward the success of the conference. Thank you, Travelers Express!

We plan to provide an outstanding agenda filled with a variety of good speakers, relevant topics, and entertaining activities for the 2002 CUNA CFO Council Conference. If you have any suggestions to help us achieve this goal, please forward them to Alan Wade via email at awade@memberonefcu.com.

Regulatory Comment Committee—

Frank Vassallo, *Chair*

The Regulatory Comment Committee coordinates responses to proposed legislation and NCUA initiatives. The goal of the committee is to provide feedback to the appropriate party or parties that will reflect the opinions of the CFO community. The committee is currently working on developing a format for responding to individual issues. The committee will periodically solicit feedback from the council membership to compile an appropriate response for each issue.

Recently the committee compiled an in-depth response to the NCUA regarding the Prompt Corrective Action (PCA) proposal. We are currently developing a methodology for responding to the upcoming NCUA Strategic Plan. Please feel free to offer any input you might have by emailing Frank Vassalo at fvassallo@ftbfcu.org.

Membership Committee—

Christina C. Brown, *Chair*

Greetings from the Membership Committee. New committee volunteers this year include Greg Krause, Orange County CU; Jennifer Lehn, Numerica CU; and Pam Finch, Mid Minnesota FCU. A carryover volunteer from last year is Colleen Murphy, CFO Council Executive Committee Member and SVP of Finance and Administration for the Oklahoma Credit Union League. This is a great team to work with. These volunteers are ready to roll up their sleeves and help!

One of our goals is the retention of existing CFO Council Members. We plan to do this by communicating to CFO Council Members the value the CFO Council brings to their professional lives through ongoing online networking via the listserv, educational opportunities at the annual conference, white papers, and more.

Our other main goal is to bring more CFOs into the Council so they may benefit from the exceptional networking and knowledge sharing. Of course, the Membership Committee can only do so much alone. What carries more weight is when you, and other Council members, spread the word about this worthwhile organization. We've got a great new referral program with an incentive for you - check it out at www.cunacouncils.org!

Benefits/Education Committee—

Colleen Murphy, *Chair*

Our mission is to bring to the CFO Council Members "benefits and education" that provide present and long-term value. Our previous accomplishments included developing and delivering the "CFO Salary Survey" based upon member responses, developing and delivering the council membership survey, and holding a CFO Regional Meeting in Pennsylvania.

Our action plan for this year includes:

- Gathering suggestions of key objectives from Executive Committee members

- Reviewing Benefits/Education Committee position description
- Reviewing current benefits received by membership and budget targets
- Reviewing May Conference membership comments relating to Benefits/Education
- Organizing Benefits/Education Committee
- Holding first committee planning meeting
- Organizing and holding two CFO Regional Meetings by April 2002

Our potential Benefits/Education subcommittee includes:

- Michael Calandrillo, VP Finance, Paragon FCU, mcalandrillo@paragonfcu.org
- Norm West, SVP Finance & CFO, Alaska USC FCU, n.west@alaskausa.org

Communications Committee—

Mike Lord, *Chair*

The goals of the Communications Committee are to improve the timeliness and quality of information distributed to Council Members. We wish to provide topical and relevant information that helps you succeed in your job.

We will communicate with you through periodic newsletters, white papers, the web site, and other means. The listserv is an excellent tool for CFOs to exchange information, trade solutions, investigate vendors, commiserate, and otherwise communicate. We invite you to take advantage of this benefit of your membership in the CFO Council.

If you have completed a research paper for your Board or Staff, or would be willing to submit an article on a specific topic, please consider sharing this information with your colleagues. It will benefit all of us.

You have recently been provided a list of the members of the Committee, which includes Jennifer Lehn, Vince Market, Judith Hillock, and Scott Waite. Please feel free to contact any one of us with your suggestions, criticisms, or communications that you would like to share. We welcome your ideas and input. I can be reached at mjlord@att.net. Thanks. We'll be in touch! ◆

CUNA CFO COUNCIL

NEWS

CFO News is a web-based newsletter published bimonthly by the CUNA Council. Send news and CFO Council information to Scott Waite, SVP/CFO, Patelco CU, San Francisco, CA, phone (415) 442-7158; fax (415) 442-7193 or Mike Lord, SVP/Comptroller, State Employees CU, Raleigh, NC, phone (919) 839-5084; fax (919) 839-5100.
For council membership and administration information, call Pam Frey, manager of CUNA council administration, at 1-800-356-9655, extension 4141 or e-mail her at pfrey@cuna.com.