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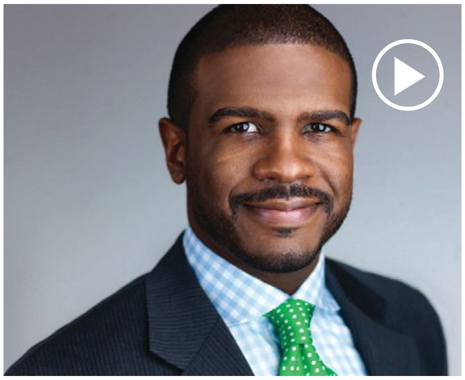

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John Pembroke • *john@cues.org*

SVP/CHIEF LEARNING OFFICER
Christopher Stevenson, CIE • *christopher@cues.org*

MANAGING EDITOR/PUBLISHER
Theresa Witham • *theresa@cues.org*

SENIOR EDITOR
Lisa Hochgraf • *lisa@cues.org*

EDITOR
Danielle Dyer • *danielle@cues.org*

DIRECTOR OF CREATIVE SERVICES
Nicole Morrison • *nicole@cues.org*

DIGITAL & BRAND EXPERIENCE MANAGER
Kristen Christianson • *kristenc@cues.org*

GRAPHIC/INTERACTIVE DESIGNER
Christina Harris • *christinah@cues.org*

VP/STRATEGIC PARTNERSHIPS & SOLUTIONS
Karin Sand, CIE • *karin@cues.org*

SUPPLIER RELATIONS MANAGER
Kari Sweeney • *kari@cues.org*

MARKETING COPY WRITER AND COORDINATOR
Molly Parsells • *mollyp@cues.org*

ADVERTISING/SALES REP
Catherine Ann Woods •
cathy.woods@mediawestintl.com
Phone: 602.863.2212
Fax: 602.863.6551

DESIGN & PRODUCTION
Sara Shrode • *sara@campfirestudio.net*

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TWITTER: @tawitham
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YOUR THOUGHTS

WHAT ARE YOUR CREDIT UNION'S GROWTH GOALS FOR 2019?

>> Email your answer to **theresa@cues.org**.

The Curiosity/ *Innovation Connection*

Have you ever asked, "Why do we [fill in the blank] like this?" and then not accepted the standard "because we've always done it that way" answer, diving into improving the process instead? If so, you've demonstrated the curiosity/innovation connection.

"Innovation benefits from divergent thinking and the generation of creative ideas through the exploration of many possible solutions," says CUES member Pete Reicks, CIE, SVP/analytics and innovation for $2 billion Elevations Credit Union (*elevationscu.com*) in Boulder, Colorado, in "A Culture of Curiosity."

Innovation can seem abstract and difficult. It may even seem unattainable or that you need to be the smartest brain in the room to do it. But we can all innovate. In our article, Arvind Sharma, chief digital and payments officer at $19.5 billion Central 1 Credit Union (*central1.com*), Vancouver, British Columbia, suggests how to start.

"People may be thinking, 'We've got to do what Apple does. We've got to invent the next big thing,'" he says. "Apple and others have set the bar really high, but my advice for credit unions would be to start small. Start with ideas for continuous improvement. Ask yourself: 'What are some little ideas we can take to market?'"

What doesn't work very well is innovation on demand. Imagine a meeting in which you are told to come up with the next big thing for your credit union. That would be unsuccessful for the credit union and incredibly stressful for you and your colleagues. However, innovation methods and models can help your team create innovative solutions to your biggest challenges.

"When people don't innovate, it's not because they're incapable of innovation. It's because they don't have a process in place," says Linda Bodie, chief + innovator at $33 million Element Federal Credit Union (*elementfcu.org*) of Charleston, West Virginia. Read more about how credit unions are approaching innovation on p. 10.

One area in the realm of financial services that could benefit from innovative thinking is marijuana banking. Many credit unions are hesitant to serve this large—and underserved—industry. But $670 million Salal Credit Union (*salalcu.org*), Seattle, has worked closely with its state regulator and is now making loans to pot businesses.

Salal CU is "absolutely" staking out an opportunistic claim for what could be a fast-growing and highly profitable product line, but it's not all about the money, says VP/Business Services Carmela Murphy Houston. "Most importantly, we see it as meeting our members' needs."

If you're curious about the innovations of Salal CU and a Colorado CU in serving this niche industry, read "Seeds of Success" on p. 16. You may also want to check out our larger article, "2019 Business Lending Outlook," starting on p. 14.

Theresa Witham

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Robust Performance *Feedback*

BY PETER MYERS

An aspect of leadership that sets the old adage "'Tis better to give than receive" on its head is the act of actively seeking feedback. Leaders are often quick to give assessments but may have a harder time accepting them.

In our leadership development work, executives often seek advice about how to let a colleague know that his or her interactions and collaboration could be ... better. Everyone has encountered this situation, armed with a juicy piece of feedback that will set someone straight. The executives are then asked, "When is the last time you really asked that individual feedback about you?" No one ever raises a hand.

By inviting and readily accepting feedback about their performance, leaders acknowledge that they are accountable to the values they proclaim. Their willingness to request and give assessments also demonstrates a commitment to learning, deepening relationships and being exposed and vulnerable. The acquisition of critical—that is, astute and relevant—feedback from colleagues and direct reports helps leaders broaden their perspective and increases their attentiveness to future possibilities. Receiving outside assessments also helps keep managers and executives grounded as a light is shined into the corners of their leadership blind spots, avoiding the possibility that they will become "legends in their own minds."

CUES member Joe Krull, member contact center manager with $1.5 billion Rogue Credit Union (*roguecu.org*), Medford, Oregon, says he has learned the benefits of asking his team for assessments.

In addition, "I now ask someone's permission before I offer an assessment, and that has been very helpful in building relationships and improving my coaching," Krull says. He realizes that the fact that he is a person's manager does not inherently stimulate an appetite for feedback. Feedback given after permission has been truly granted will be more readily considered and embraced.

That's not to say that sharing and receiving candid assessments is easy. "Giving honest feedback has always been hard for me. There's been a gap in what I'm thinking and what I say. I didn't want to hurt people's feelings or push into an uncomfortable place," says Jim Newstrom, regional branch manager of $859 million Seattle Credit Union (*smcu.com*) in Washington. "But if you want to help people, you have to be honest with them. You have to do that in the right way and be authentic. It's a work in progress, because I'm rewiring many years of behavior."

"Do I really want to know what others think of me?" That sometimes feels like a dangerous question. However, for managers who seek to grow in ways that support leadership development, it is invaluable to gain those face-to-face insights by:

Embracing opportunities to become a better leader. Without feedback on their performance, leaders can end up "floating in the sea of 'I'm doing OK,'" cautions Shelley Pierce, VP/branch operations with $1 billion Fibre Federal Credit Union (*fibrecu.com*), Longview, Washington. "But really, we want to do better than that ... so it helps to continually ask for feedback as part of professional development."

Defining your commitment to leadership. Consider these questions: What does it mean to be a leader? How do you want to be seen as a leader? What impression do you want to make? How willing to learn are you? Your answers to these questions can help you formulate a simple and succinct statement to guide your leadership development and stay committed as you face new situations, test and hone your skills, and stay focused over the long term.

Seeking diverse viewpoints. Michelle Wilcher, director of retail/north region for $1.2 billion DuPont Community Credit Union (*mydccu.com*), Waynesboro, Virginia, says she has learned to move outside her "safe place of communication" to seek out the opinions and perspectives of people who hold different—or even directly opposing—views, rather than seeking to primarily "bounce ideas off of peers who I felt shared the same views."

Fostering an environment of trust. Actively and continually soliciting assessments can help build trust with others, both directly and indirectly, as those who observe the solicitation see the openness and may extend more trust in their own interactions. An increased level of trust means a greater chance that others will be open and receptive to one's intentions, future actions and feedback.

Building trust allows leaders to freely admit that they don't have all the answers and to ask for feedback on their performance. Vulnerability in leadership "humanizes everyone," suggests Amanda Cashatt, DuPont Community CU's card services manager.

"It makes people more honest, more open and more willing to receive feedback—and, ultimately, it makes all of us, regardless of our commitment, a little bolder, to ask questions or to push either up or down, to make a request of our boss to say, 'I'm not getting what I need from you' or 'I need more help from you in this area,'" Cashatt says. "It gives us permission to push each other in a healthy way and develop each other, regardless of where each person falls in that hierarchy."

Peter Myers *is senior vice president of CUESolutions provider DDJ Myers Ltd., Phoenix* (ddjmyers.com)*. To read about more examples of how credit unions' mid-level leaders are creating an assessment-rich culture to increase performance, download the "The Missing Link in Strategic Execution: Developing Mid-Level Leaders" white paper* (cumanagement.com/0718ddjwhitepaper)*.*

Rich Brock

Title: National Practice Leader for Executive Benefits

Phone: 704.904.4159

Email: Rich_Brock@ajg.com

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How can credit unions be more successful?
Our best recommendation is to develop a program to protect human capital. It's one of a CU's larger expenses, yet often overlooked or undermanaged. Executive turnover can have a significant impact on a credit union, including creating delays in achieving strategic goals, making a poor impression on membership and potential candidates, and dampening employee morale. Plus, the tangible cost of recruiting and relocating executives can be more than three times an executive's salary.

The value of retaining key personnel for career service includes getting long-term ROI, keeping institutional knowledge in-house, and advancing your strategic vision.

What are the top issues you see for credit unions today?
Regulatory compliance, retaining and rewarding key executives, and due diligence. NCUA's recently issued examiner guidance for Section 701.19 and the new excise tax from the Tax Cuts and Jobs Act has many CUs re-evaluating their programs. Plus, many CEOs are getting ready to retire in a few years. We work closely with our clients to manage these changes and maintain examiner-friendly executive benefits programs.

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A Culture *of Curiosity*

CREATIVITY IN 2019 MEANS EXPLORING MANY OPTIONS—NOT JUMPING TO QUICK CONCLUSIONS.

BY DIANE FRANKLIN

Many credit unions have come to regard innovation as a specific function within their organizations—on equal footing with such mainstays as operations, technology, marketing and human resources. This trend is exemplified by the growing number of high-level executives—chief innovation officers, SVPs of innovation—who are tasked with formalizing an innovation process and implementing it organization-wide.

A requisite step for producing innovation is to build a culture where curiosity is encouraged. Francesca Gino, a behavioral scientist and professor at Harvard Business School, addresses this topic in "The Business Case for Curiosity," a recent *Harvard Business Review* article (*hbr.org/2018/09/curiosity*). In the piece, Gino describes curiosity as a vital component in helping organizations adapt to uncertain market conditions and external pressures.

"When our curiosity is triggered, we think more deeply and rationally about decisions and come up with more creative solutions," she writes.

Curiosity helps ensure a mix of ideas coming from all levels of the organization—leaders and employees alike. And this is a good thing.

LESS CONVERGENT THINKING

"Innovation benefits from divergent thinking and the generation of creative ideas through the exploration of many possible solutions. However, quickly identifying the 'correct' answer to standard questions is where we spend the bulk of our day—that is, convergent thinking," says CUES member Pete Reicks, CIE, SVP/analytics and innovation for $2 billion Elevations Credit Union *(elevationscu.com)* in Boulder, Colorado.

With its culture of innovation, Elevations CU focuses on implementing creative ideas that will make a positive difference for its members.

"We are currently designing and will soon deploy an internal innovation program focused on our strategic goals for a high-performance culture, member loyalty and financial sustainability," Reicks says.

"In addition, we have joined Members Development Company (*membersdevelopment.com*, Madison, Wisconsin), a network of 60-plus credit union and CUSO owners who have pooled resources to drive exploration and development in areas such as chatbots, robotic process automation, auto sharing (how financial institutions must adjust lending practices to take into account that car ownership is rapidly changing from owner-single-operator models to owner-multiple-operator models) and pilot opportunities with fintechs."

Reicks honed many of the skills necessary for successful innovation by attending Strategic Innovation Institute™ *(cues.org/sii)*, where he earned his Certified Innovation Executive designation. This institute, he reports, "really helps one understand the need for organizational ambidexterity, which includes the ability to efficiently manage today's business needs while simultaneously adapting to change."

STRIVING FOR INNOVATION

Implementing a formal innovation program with a dedicated budget is the best way to rapidly address new market trends and evolving business goals, writes Alex Goryachev from Cisco's Corporate Strategic Innovation Group in an article for *Chief Executive (tinyurl.com/ciscoinno).*

Formal innovation programs are a means to help CUs stay nimble in an environment in which innovation dominates.

"Everywhere you go, everyone is talking about innovation," says Arvind Sharma, chief digital and payments officer for $19.5 billion Central 1 Credit Union *(central1.com)*, a Vancouver, British Columbia-based organization that leverages its scale on behalf of more than 300 credit unions and other financial institutions in Canada. "Part of the reason is because of the growing importance of fintechs and the pace at which everybody is introducing new ideas. I believe organizations in general believe that they need to get faster at it."

Sharma observes that many organizations undermine their efforts by equating innovation with invention. But incremental improvement is also innovative.

"The problem is that invention is very hard to do," Sharma says. "People may be thinking, 'We've got to do what Apple does. We've got to invent the next big thing.' Apple and others have set the bar really high, but my advice for credit unions would be to start small.

"Start with ideas for continuous improvement. Ask yourself: 'What are some little ideas we can take to market? What are some ways we can: (a) improve an existing experience for our members, or (b) eliminate a step in a process to make an experience go faster?' That in and of itself is innovation because each incremental improvement ultimately adds up to bigger change."

At the same time, Reicks cautions against focusing too much on continuous improvement at the expense of other types of innovation. "When presented with creative ideas that have the potential to truly differentiate us, credit unions often find resources already swamped by a work queue full of traditional continuous improvement efforts," Reicks says. "Optimizing existing operations through continuous improvement is critical yet not sufficient. In order to remain relevant, we must leverage our talented workforce and the cooperative nature of the credit union industry to rapidly and systematically generate ideas, prototype solutions, test and learn."

Nonetheless, Sharma sees the pursuit for continuous improvement as a worthwhile endeavor, since it sets the stage for more impactful change. "You're exercising your innovative muscles, which will encourage people to come to the table with their ideas. And once you've done those things, there are methodologies that will encourage even greater innovation."

METHODOLOGIES AND TRENDS

Sharma cites several methodologies that CUs can use to encourage innovation, including Business Model Canvas *(tinyurl.com/canvasbizmodel)*, which encourages organizations to make a case for a business idea by considering nine essential elements: customer segments, value propositions, channels, customer relationships, revenue streams, resources, activities, partnerships and costs.

Another is a problem-solving model called "design thinking" *(tinyurl.com/designthinkingmodel)*, which begins with bringing stakeholders and customers together to gain an immersive understanding of a problem. "The problem might be: 'How do I originate a customer?' Or 'How do I do a better job of servicing a service data?'" Sharma explains. "An effective way to answer those questions is to bring in your customers (i.e., members) and work with them to develop the best ideas."

> **"When people don't innovate, it's not because they're incapable ... . It's because they don't have a process in place."**
>
> – Linda Bodie

Sharma also sees promise in customer journey mapping, which encourages organizations to think about the entire journey that a member is embarking on. "Take the example of someone who is buying a house," he suggests. "What does the buying-a-house journey look like? Where does the credit union play in that journey? Where *could* the credit union play in that journey? Start thinking broadly about what the member needs, not just in terms of a mortgage. The need is to find a home—to find someplace where their family is secure—so consider how you as a credit union can help satisfy that need besides lending them the money to buy the property."

Customer mapping is consistent with a trend toward greater personalization, which is impacting various areas of the credit union.

"One of the major innovation trends we anticipate in 2019 is the adoption of highly personalized marketing techniques," says Scott Hansen, chief marketing & strategy officer of CUES Supplier member Harland Clarke (*harlandclarke.com*), San Antonio, a leading provider of member engagement solutions. "From the moment a person joins a credit union, the institution gains a wealth of information about that member. That information can be used to do a better job of serving the member right from the start of the relationship and, if done right, is the source of an excellent member experience throughout the member life cycle."

Hansen defines "doing it right" as developing highly relevant and actionable pieces of multi-media content to support a wide variety of member relationship management activities—from new member onboarding to check ordering to targeted cross-selling to event invitations.

"By delivering this information through a personalized webpage, or a personalized URL (or 'PURL'), the credit union provides members with a distinctly relevant 'homepage' they can visit anytime, from any device, that is customized for

Innovation Enhances *Talent Development*

No area in credit unions remains untouched by innovation, and that includes talent development. Among the innovative trends in this discipline is an increasing practice to marry talent development with the overall strategic direction of the organization. At $3.1 billion Coastal Credit Union *(coastal24.com)* in Raleigh, North Carolina, these two functions fall under SVP/Chief Strategy & Talent Officer Willard G. Ross.

"Part of my role is to prepare the next generation of leadership at Coastal—not just as a succession plan but by developing several layers of talent," explains Ross, a CUES member. "We have three-year development plans for vice presidents and senior vice presidents, working with them to identify gaps—in experience, knowledge, etc.—and determining how to fill those gaps through training, projects and community involvement."

Among the innovative strategies used at Coastal CU is role rotation to ensure that leaders become more well-rounded. "For instance, prior to my current role, I was chief retail officer for eight years," Ross reports. "Our current CRO was senior VP in charge of CUSOs and, before that, in charge of IT. What we try to do is switch people around into areas where they don't have previous experience to see how they can apply their leadership abilities to those roles."

Coastal CU's strategy aligns with a model called "requisite organization" *(requisite.org)*, which Ross describes as "a total system for effective managerial organization, talent management and managerial leadership." Developed by renowned Canadian psychoanalyst Elliott Jaques, this concept optimizes the structures and systems of an organization to support productive work, while ensuring that employees are positioned within the organizational hierarchy in a manner that will allow them to do their best work.

To further the CU's work in organizational design, Ross uses the resources at PeopleFit (*peoplefit.com*) to create a high-performance organization that unleashes the best performance from each person in the workforce.

"We do a talent pool evaluation using that methodology every few years," Ross says. "To avoid falling victim to the 'Peter principle' *(tinyurl.com/peterprinc)*, we match our employees with roles that fit their problem-solving capability. This process also enables us to determine how many layers we need for optimal organizational performance and to match our employees with a manager who is capable of setting context and giving them guidance and direction.

Coastal CU also uses the Leadership JumpStart® and the Leadership Decathlon® programs from Grinnell Leadership *(grinnellleadership.com)* to better align leadership skills with organizational intent.

"Twelve of our vice president-level leaders have gone through Leadership Decathlon, which is an eight-month program," Ross says. "Through that program, we have learned how to collaborate more, work better as a team and optimize as a unit."

them—based on their unique needs and status with the credit union," he observes.

Reicks likewise sees personalization as a major innovation trend, noting that it is driven by analytics and digital delivery, along with the need to address all things having to do with payments. "These items definitely resonate as established trends we must effectively address as an industry," he says.

THE CUSO CONNECTION

Much of the industry's innovation is taking place among credit union service organizations. To highlight that fact, the National Association of Credit Union Service Organizations *(nacuso.org)* sponsors the Next Big Idea Competition. Now in its seventh year, the competition takes place at the annual NACUSO Network Conference with presenters showcasing ideas that have the potential for revolutionizing the CU industry.

"We basically ripped off 'Shark Tank,'" confesses Denise Wymore, NACUSO's member & advocacy development officer. "The first couple of years, we actually hired 'Shark Tank' judges Robert Herjavec and Daymond John."

Among the CUSOs that have presented their ideas at the NACUSO competition are CULedger LLC *(culedger.com)* of Denver, Colorado, which is working to bring distributed ledger blockchain technology to credit unions worldwide; OnApproach *(onapproach.com)* in Plymouth, Minnesota, which launched OA Caspian as part of its CU Analytics Ecosystem to provide a breadth and depth of data that is unprecedented in the CU industry; and CUProdigy *(cuprodigy.com)* of Layton, Utah, which extends its creative thinking from its modern, cloud-based core processing platform to a simple, straightforward approach to pricing.

CUSOs typically tread an innovative path by finding a niche that hasn't been filled before. Wymore cites the example of Constellation Digital Partners LLC *(constellation.coop)*, Raleigh, North Carolina, the 2017 winner of the Next Big Idea Competition. Constellation snagged the honor with its new platform that allows credit unions to easily shop for new digital services. Since winning the award, Constellation has gone on an innovation tear, recently unveiling its third major platform release, Boötes, to provide access to core systems and as a follow-up to its Aquarius and Aquarius 1.1 releases—all within calendar year 2018.

"They have a huge first-to-market advantage, because what they're doing is so unique," Wymore says. "But I think that's the nature of CUSOs. CUSOs succeed because they have a cooperative heart with a shrewd business mind. That's a beautiful combination."

Oftentimes innovation among CUSOs comes from a credit union identifying a need and thinking creatively about how to fulfill it. As an example, Wymore cites the origin story of Credit Union Direct Lending (now CU Direct, *cudirect.com*, a CUES Supplier member based in Ontario, California).

The idea for CUDL originated in the mid-1990s, when San Francisco-based, $12 billion Golden 1 Credit Union *(golden1.com)* approached local car dealerships about installing dumb terminals on-site to facilitate indirect lending. The big banks already had such a system, which gave them a huge leg up in getting the loan business of car buyers who were shopping during evening and weekend hours. When Golden 1 CU was rebuffed for having

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>
> – Pete Reicks, CIE

insufficient volume, then-SVP Diana Dykstra took matters into her own hands.

"Diana formed a CUSO and got enough credit unions on the platform that the car dealerships could no longer turn them away, and that's how CUDL was born," Wymore explains. "That's a classic collaboration story—credit unions getting together because when we get together, everybody wins."

LEVERAGING RESOURCES

Wymore points out that to be innovative, credit unions don't have to grow their own products and services internally. Rather, they can leverage the innovative solutions that CUSOs have created. As an example of a credit union that has mastered this idea, Wymore cites $33 million Element Federal Credit Union *(elementfcu.org)* of Charleston, West Virginia.

"Linda Bodie of Element FCU is what we call a CUSO power user," Wymore says. "She's our poster child for small credit unions using CUSOs to perform like a much bigger credit union for the benefit of their members."

Bodie, who holds the unique title of chief + innovator, acknowledges that leveraging the advantages of CUSOs has worked out well.

"Being a smaller credit union, you have to be nimble and creative in order to offer the level of products, services and methodologies that bigger credit unions offer," Bodie says. "CUSOs have enabled us to expand immensely what we're able to do. Anything we want to offer, we can offer through a CUSO if we can't do it ourselves."

Among those CUSOs are CU*Answers *(cuanswers.com)*, Grand Rapids, Michigan, which provides Element FCU with its core processor and offers solutions for various back-office functions, such as ACH payment processing, share drafts, call reports, accounting, P2P payments, remote deposit auditing and compliance. Other CUSOs that the credit union uses include Xtend *(xtendcu.com)* also in Grand Rapids, Michigan, for solutions in the call center, and eDOC Innovations *(edoclogic.com)* in Middlebury, Vermont, for secure image processing software.

Element FCU has investments in all of three of the CUSOs mentioned, and also uses the services of other CUSOs.

SUPPORTING INNOVATION INSIDE

While relying heavily on its relationships with CUSOs, Element FCU cultivates an innovative mindset internally that has led to some noteworthy revolutionary breakthroughs of its own. Citing the most high-profile advancement, Bodie reports, "We were the first financial institution to offer remote check deposit capture on the iPhone."

This industry-first innovation came about when Bodie was able to connect the dots between the digital check capture allowed by the Check Clearing for the 21st Century Act (Check 21, *tinyurl.com/chk21act*) and the greatest innovation of 2007, the Apple iPhone. She went to the credit union's IT head with her idea, and he was able to build an iPhone app quickly enough to deploy it before any other financial institution out there.

"We got noticed by national credit union media at the time because we were the small credit union that beat out giant USAA," Bodie reports.

Bodie stresses the need for credit unions to facilitate innovation by putting the mechanisms in place to make it possible.

"When people don't innovate, it's not because they're incapable of innovation," she says. "It's because they don't have a process in place."

Innovation happens most effectively when it is based on how people live their lives, she adds.

"We build a bridge between where they are and what they're doing and how we as a credit union can fit into that."

Diane Franklin *is a freelance writer based in Missouri.*

MORE ON INNOVATION

Embracing Limitation (*cumanagement.com/121318embracing*)

Special Report: Find Your Next Bright Idea in Fintech (*cumanagement.com/1018specialreport*)

Strategic Innovation Institute Stanford University (*cues.org/sii*)

2019 Business *Lending Outlook*

THREE KEYS TO AVOIDING LENDER REMORSE

BY RICHARD H. GAMBLE

Two dark clouds loom on the horizon for credit unions making member business loans in 2019: the mature business cycle and the presence of disruptors.

Today's economic cycle should be sending alerts to CU business lenders, says James R. Devine, CEO of Hipereon Inc. (*hipereon.com*), Kirkland, Washington, and faculty of the CUES School of Business Lending (*cues.org/sobl*).

"It's been hard to make mistakes the last few years," he notes, but in his experience, "credit unions tend to lend to businesses that sell nice-to-have products and services, not must-have ones, so those businesses rely on consumers with discretionary income. If that shrinks, they will struggle."

Credit unions have experienced solid growth for all loan types over the past five years of economic recovery, reports Larry Middleman, CEO of CU Business Group LLC (*cubg.org*), Portland, Oregon, a CUSO owned by six corporate CUs. CU Business Group helps 575 CUs make member business loans for their own portfolios. "These credit unions have built their programs, hired good talent and progressed a lot," he says.

However, with commercial real estate, which dominates CU business collateral, you have to be careful of exuberance based on recent success, warns Joel Pruis, senior director and practice leader for commercial lending at Cornerstone Advisers (*crnrstone.com*), Scottsdale, Arizona. "Booms build confidence that can lead to regret," he notes. "Opportunity can morph into overbuilding pretty quickly when the economy turns." Small businesses, he adds, are often the first to feel the pain of an economic downturn and the last to get the benefits of an upturn.

Lenders should also be aware of a ripple effect as businesses look for ways to leverage available space, he points out. A big-box store may close, which may not hurt a credit union directly. But the big-box space might be repurposed as office space, which could impact the overall commercial real estate market and negatively impact the cash flows of other CU-financed properties.

And CUs should be alert to unrecognized concentrations of risk—the Circuit City lesson, Pruis cautions. Prudent lenders limited their direct exposure to Circuit City after the company declared bankruptcy. However, lenders that had spread their loans among an assortment of mall owners and other retail properties didn't notice that Circuit City was a tenant in many of them until it was too late, he recalls. When Circuit City dragged its landlords down, lenders also felt the pain: Some landlords became delinquent and had to renegotiate their loans. Some went into bankruptcy.

Rising interest rates are another cyclical risk factor, even for CUs that stick to strong ratios and pay close attention to collateral, Middleman reports. CUs typically make fixed-rate loans to businesses with five-year maturities or with repricing points as long as seven to 10 years. If rates rise at these pricing points, businesses have to pay more money for the same loans, which can hamper cash flow and potentially put the loan in jeopardy, he notes.

The rising rate environment is causing most lenders to revisit stress testing at the individual loan and portfolio level, reports Susan Rice, director of business services at $4.6 billion Bellco Credit Union (*bellco.org*), with offices in the Denver suburbs. "Additional reviews of liquidity are in place for most to ensure that changes in rates and payments can be absorbed by the cash flow of the property and/or the guarantor," she notes.

DISRUPTIONS

While the economy is generally strong and friendly to business lenders, it has been prone to sector disruptions and dislocations, posing risks that come from outside the member businesses and challenge traditional underwriting, Middleman reports. Uber and Lyft catch on, and a handful of CUs that specialized in taxi medallion financing, once a lucrative market with solid prospects, go into conservatorship.

The shift to online shopping has sent some big-box retailers into a tailspin and cast a cloud over smaller retailers that might apply for CU business loans. "The risk around a loan to a storefront or mall kiosk business has changed," Middleman observes.

Then there are political disruptions. Unpredictable trade skirmishes are increasing risk for business lenders across the board, Devine says, and the risk is acute in his state of Washington. "We're very vulnerable," he notes. "We're a big grain and fruit producer and a big exporter. When there is not enough domestic demand for those perishable crops, and when tariffs have effectively closed the export market, it's scary."

The appetite for lending to the hospitality industry is also shrinking, partly due to disruption from online rental services like Airbnb (*airbnb.com*). "Not as many financial institutions are willing to make hospitality loans, which is forcing borrowers to shop around," Rice notes.

In today's eventful market, there's also a risk that a concentration in a particular business sector might go sour. But there's potentially a greater risk that credit unions might not be agile enough to respond effectively to online lenders, for example, says Middleman. Online lenders specialize in faster and easier approvals that CUs usually can't match, he notes.

Business members are less tempted by automated online nonbank lenders than consumers, Devine suggests. "Business owners think their issues require personal attention, and they like a brick and mortar presence and people they know by name and can reach. They don't like to be commoditized," he explains.

However, CUs sometimes lose opportunities—particularly small business loans—to online lenders when they cling to traditional in-depth underwriting practices, warns Middleman. Online lenders have found ways to streamline underwriting. He suggests CUs consider adopting some of that streamlining for smaller, unsecured loans. Federal Reserve studies show that small business borrowers have a high level of satisfaction with the online application and approval process, he reports. But they are not delighted to live with the loan, the study shows—most likely because such loans come at a high cost due to terms and rates that are well above market, he explains.

> **"Every portfolio is exposed to economic cycles, and we're in the 12th inning of a nine-inning game. It will get more challenging at some point."**
>
> – Scott Strand

Other potential market disruptions could be positive. Recent changes by Congress to Small Business Administration programs could allow some CUs to make more guaranteed business loans. A 2018 bill expands access to popular SBA programs.

"It doesn't reduce lenders' risk, but the changes do let them increase capacity," explains Rohit Arora, CEO of Biz2Credit (*biz2credit.com*), New York. "Important constraints on the program have been relaxed in some cases." But that offers little opportunity for many credit unions, he notes, because they still have their more restrictive caps on business lending.

"This could even hurt credit unions—they could lose market share—because the bigger banks can take advantage of increased SBA capacity and they (credit unions) often can't," Arora says.

HOW CUs ARE PREPARING

At $5.5 billion Ent Credit Union (*ent.com*), Colorado Springs, member business lending is good business. It has a higher net interest margin than the overall loan portfolio, says CUES member Mike Steppenbacker, director of corporate banking. And it has much lower delinquencies and charge-offs. In 19 years of commercial lending, he notes, Ent has charged off only one negligible loan.

But even with all that glitter, Ent is growing its business lending deliberately and cautiously. "We have about $263 million in MBLs," Steppenbacker notes, "and our cap is $1.245 billion. We're starting to narrow that gap but doing it slowly. We want prudent growth. We're not shooting to reach our cap."

Ent is a conservative lender, putting a high priority on managing risk. Its portfolio is over 80 percent collateralized by commercial real estate, half owner-occupied and half investor-owned. Its term loans reprice every three to five years, Steppenbacker reports.

"Except for some medical sector loans and a few commercial and industrial lines of credit, all our loans are secured." Multifamily housing units are looking a little "overheated" now in Colorado, he says, so Ent is asking for bigger down payments.

Seeds of Success: *Marijuana Banking*

One of most conspicuous opportunities and risks for credit union business lending is the fast-growing, largely unexplored marijuana industry. $670 million Salal Credit Union (*salalcu.org*), Seattle, is one of the rare regulated financial institutions that makes loans to marijuana businesses. The CU lends directly to both retail shops and producers and distributors. That puts Salal CU at the very front of the bleeding edge in lending to an industry most banks and CUs shun or avoid, but it's hardly a reckless move. "We've worked closely with the Washington State Department of Financial Institutions (*dfi.wa.gov*), our primary regulator," notes VP/Business Services Carmela Murphy Houston. "They know what we're doing. We also spent time educating other state and federal regulators about our program."

Salal CU is "absolutely" staking out an opportunistic claim for what could be a fast-growing and highly profitable line of business, but it's not all about the money, Houston says. "Most importantly, we see it as meeting our members' needs. ... We provide residential mortgages, consumer loans and consumer deposit products to cannabis business owners and their employees who are often shut out of banking services elsewhere."

The loans themselves come with features that protect the CU. Most are conservatively collateralized with real estate. And they come with personal guarantees—the business owner pledges to repay the loan from his or her personal assets if the business is unable to repay. "We require a personal guarantee from at least one principal and anyone with more than a 25 percent ownership interest," Houston explains. The marijuana businesses also have to use Salal CU as their primary financial institution. "We are relationship lenders, so we expect them to have their entire [banking] relationship with Salal if they want a loan from us," she says.

As a supplier of a scarce product, Salal CU can afford to be very selective. "We have to identify our primary source of repayment (business revenue) from historical financials," she explains. This eliminates many applicants that don't have a two-year history of positive net cash flow after taxes.

These hard-to-get loans are profitable. "We realize a rate premium," Houston says, "but the business still pays less than it would on a loan from a private money lender."

Marijuana businesses usually don't need banks and CUs to provide initial core capital, explains Choua Ly, VP/lending at $400 million Partner Colorado Credit Union (*partnercoloradocu.org*), Arvada, which takes marijuana business deposits and is exploring loans through its Safe Harbor division (*safeharborprivatebanking.com*). Business owners increasingly have access to private investment capital—including lawyers, doctors, successful businessmen and Canadian investors who want to be silent or vocal partners in the lucrative and fast-growing industry. The businesses' ample deposit balances would more than cover the funding for operating lines of credit—they would essentially be borrowing their own money for convenience, she explains.

Partner Colorado CU is stepping carefully toward lending. "We had conversations with our banking commissioner, our Senator, our auditors, our legal counsel, NCUA (our deposit insurer) and our bond insurer to make sure we were all on the same page and that they were on board," says Ly. So far, the CU has made personal loans to marijuana business owners— loans they couldn't get from other financial institutions. Direct loans to the businesses are underway for 2019, she reports.

Legal marijuana has reached the big money stage, now that 33 states either permit its sale for medical use or have it on an upcoming ballot, and 10 of those states plus the District of Columbia have legalized it for recreational use, says James R. Devine, CEO of Hipereon Inc. (*hipereon.com*), Kirkland, Washington.

Interest is high. "We've met with venture capitalists in New York and Washington, D.C., who want to buy a bank or credit union and focus on marijuana as a vertically integrated business line, but regulators have discouraged them," he reports, "because they don't like the risk of such a concentration." Even with regulatory consent at some state levels, there's still a stigma around pot sales, Ly reports, and retailers, growers, warehouse operators and even landlords and payroll service providers have been pushed out by their traditional financial institutions. However, the National Credit Union Administration (*ncua.gov*) insists that marijuana lending is not taboo from a federal regulation standpoint.

"It's a business decision for a credit union to make," explains John Fairbanks, public affairs specialist at NCUA. "A credit union needs to perform the appropriate due diligence in offering this product as it would with any other, and to mitigate for the risk."

Complying with the Bank Secrecy Act and anti-money-laundering regulations are essential, of course, and a CU providing marijuana banking needs to be familiar with the Financial Crimes Enforcement Network's guidance in this area (*tinyurl.com/y97nj3u4*), he adds.

"Ninety percent or more of our business borrowers have relationships with the credit union and use more than one service. We don't like one-offs. We work to get their deposits and transactional business."

– Mike Steppenbacker

A key part of Ent's risk management for MBL is that the CU rarely lends on stand-alone transactions. "Probably 90 percent or more of our business borrowers have relationships with the credit union and use more than one service," Steppenbacker reports. "We don't like one-offs. We work to get their deposits and transactional business. We don't mandate it, but we strongly encourage it and reward it with relationship pricing."

Those relationships can help resolve problems before they get serious—if the CU has the checking account, it can see if a business has overdrafts or started delaying payments to suppliers and could offer counseling to head off a credit problem, he notes.

Risk management is also top of mind for business lending at $19 billion BECU (*becu.org*), Tukwila, Washington. "Our risk profile is improving," reports Scott Strand, CCE, SVP/member lending/business and wealth management. "We've improved our mix—more multifamily, less retail—and our charge-offs were less than $200,000 on a $1.3 billion portfolio for 2017. We expect the same for 2018." But he also sees reason for caution. "Every portfolio is exposed to economic cycles, and we're in the 12th inning of a nine-inning game. It will get more challenging at some point." Rising interest rates are dampening demand for BECU's business loans. "That's to be expected," he observes.

PROTECTIVE RELATIONSHIPS

New commercial borrowers pose both a red flag and an opportunity for CUs. Roughly half of credit unions' business borrowers, Middleman estimates, are one-product members that join just to get the loan. These are typically real estate investors. The other half are traditional members who extend their personal ties to the CU to include their businesses.

These loan-only businesses pose a real danger as credit standards tighten, Devine warns. "The business owner who comes to you for a loan, particularly if he or she doesn't have an existing relationship with the credit union, has probably been pushed out the door by a bank and is a poor prospect," he notes. You want to find the good prospects proactively, and chances are that many of them are already members for their personal needs, he says. "You need to leverage those relationships—do the data mining to identify them and build on the trust you've already earned to talk about their business needs."

Using financial advice to build relationships is a powerful antidote to write-offs, Devine adds. One of the scariest statistics for lenders, he points out, is that more than 60 percent of the companies that file for Chapter 11 bankruptcy are profitable. "You can't pay bills with profit," he notes. "You have to have cash for that, and too many businesses mismanage themselves into death from illiquidity. They try to minimize their taxable income by acquiring assets, but you can't pay people with assets. This is an area where an astute business lender can be particularly valuable."

WISE PRECAUTIONS

Credit unions can further minimize risk by offering proactive advice and keeping eyes and ears open. Commercial real estate lenders should pay close attention to the square footage of tenants whose leases come up for renewal in the next six months to a year, Pruis suggests, and look at the tenants' potential alternatives—whether they could find comparable space at a lower rate and would have an incentive to move.

One more important step is sometimes overlooked: To anticipate trouble, you need to monitor alertly. There is a tendency, Pruis says, for CUs to book loans to small businesses and assume they're fine until a payment is late, at which point the opportunity for effective intervention may have passed.

"Once a small business has debts that are 60 days past due, it's rarely able to recover," he notes. "The death spiral has passed the point of no return, and there's little the credit union can do if the bank or credit union is not effectively monitoring its small business portfolio. Since the bank or credit union lender is usually the last creditor to go unpaid, they are often the last to hear the alarm if they only monitor delinquencies."

Richard H. Gamble *is a freelance writer based in Colorado.*

MORE ON BUSINESS LENDING

The Strong and Weak Sides of Credit Union Business Lending (*cumanagement.com/0718mbl*)

Sorting Member Business Loans (*cumanagement.com/061818skybox*)

Three Ways to Mitigate Risk in MBL (*cumanagement.com/0317mblrisk*)

Cannabis And Credit Unions (*cumanagement.com/0616cannabis*)

CUES School of Business Lending™ I, May 6-10, Orlando (*cues.org/sobl*)

Lending a *Helping Hand*

LYNETTE CUPPS' VISION FOR HELPING NONPROFITS EARNS HER THE 2018 NTCUE HONOR.

BY DIANE FRANKLIN

Credit unions subscribe to the idea of "people helping people," and they are not alone. Thousands of nonprofit organizations also work to fulfill an educational, spiritual or philanthropic purpose to better the lives of others. CUES member Lynette Cupps, CIE, VP/organizational development at $1.3 billion MAX Credit Union (*mymax.com*) in Montgomery, Alabama, used the natural synergy between CUs and other nonprofits as inspiration for a project that won her the title of 2018 CUES Next Top Credit Union Executive.

"The goal of my project was to look at how credit unions can empower nonprofit organizations by using the skills and resources that we have as business professionals to help both organizations grow," explains Cupps, the winner of the ninth annual NTCUE competition, which celebrates the next generation of credit union leadership by considering applicants who are 35 years of age or younger.

As one of five NTCUE Finalists, Cupps developed her project over several months before making a presentation before a panel of judges at CEO/Executive Team Network™ (*cues.org/cnet*) last November in Nashville, Tennessee. In her presentation, Cupps described what she saw as the potential for CUs to offer value-added services that go beyond financial wellness—for instance, by helping nonprofits in such areas as strategic planning, social media, marketing, hiring, leadership and compliance.

"[We could] do some of the heavy lifting by providing them with the business acumen that they may not have," she recounts, observing that CUs get something valuable from the experience as well. "It's great for brand awareness, it's a great give-back to the community, it can create revenue and build assets—so it works out well for both organizations."

A DIVERSE CAREER

Cupps owes much of her success in the NTCUE competition to the diversity of experience she has gained while working for MAX CU, where she started as a teller 15 years ago. While at the CU, she earned her marketing degree from Troy University and moved into roles of increasing responsibility.

"I worked in our branches for quite a few years, then came into our training department, and through that, I gained experience across our organization," she says. "It turns out that when you train people, you end up learning a whole lot of things yourself."

After serving as a professional development specialist in MAX CU's training department, Cupps held two consecutive AVP roles—first in member services and then in corporate communications. In that latter role, she launched the CU's formal volunteerism program.

"I took the vision of our CEO and our chief talent officer ... and engaged our employees," she reports. "That's also how I first opened up to the world of nonprofits and what they are doing."

Since becoming VP/organizational development, Cupps has been participating in strategic planning. "That's what allowed me to see ... how much we could help those in our community, far beyond what we were offering in financial education."

Because of her background in employee training and volunteerism, Cupps was able to think strategically about how these concepts could be married together to benefit nonprofits. "All of a sudden, it just clicked that we have all of these people who work at the credit union who have completed their certifications and education," she explains. "They have the expertise to help the nonprofits that have a desire and passion to help our communities."

While Cupps' project is still conceptual, she already has taken steps toward determining how the program could be rolled out. She has begun by giving her own time, serving on or assisting boards in a consulting capacity. In one case, she helped a nonprofit solidify its strategic plan as part of a process to solicit grant money. She helped train another organization to develop a social media campaign to boost brand awareness. She and others at MAX CU have also been helping local nonprofits improve the financial literacy of their staff members.

MORE ON INDUSTRY LEADERS

Building a Culture of Collaboration (*cumanagement.com/0118collab*)

A Transformational Leader (*cumanagement.com/1018transform*)

Bridging The Gap To Adoption (*cumanagement.com/1217adoption*)

CEO Institute (*cues.org/institutes*)

"At the credit union, we really focus on the impact we can have on our community," Cupps says. "Our goal with this program is to maximize the investment we're making in our employees' education by helping others who are also engaged in lifting up people in our community."

A REWARDING EXPERIENCE

The NTCUE competition has been a rewarding experience for Cupps in more ways than one. Not least is the tangible value of the $20,000 educational prize package that covers the expenses of two CEO Institutes (*cues.org/institutes*) as well as two remote coaching sessions from CUESolutions provider for leadership development DDJ Myers Ltd. (*ddjmyers.com*), Phoenix. This is in addition to the coaching she already received as one of the five Finalists.

"I will say the coaching was probably one of the most valuable things I have ever experienced throughout my career," Cupps says. "It challenged me in a way that I had never been challenged before."

Cupps also valued the experience of interacting with the other Finalists during the competition, all of whom impressed her with their high-caliber projects.

"I was humbled by the fact that my idea surfaced to the top, because the other competitors submitted such thought-provoking and holistic ideas that have the potential of impacting their credit unions and the industry we serve."

Throughout the process, Cupps was grateful for the support from her colleagues at MAX CU. "There have been some real cheerleaders from our executive team who helped me think through different ideas and encouraged me to pursue these opportunities," she says.

Among those cheerleaders is Sandra Stenger, PHR, MAX CU's chief talent officer, who has seen firsthand how Cupps' passion for helping others inspires those around her.

"Lynette has a true desire to make a difference in the lives of others," Stenger says. "Her strategic mindset is always finding a way to connect our organization with the needs of our community. She has the full support of the organization, and we couldn't prouder. MAX is truly blessed to have her as a part of our organization."

WHAT'S NEXT?

Cupps is working toward her black belt in Six Sigma (*6sigma.us*), a methodology for business process improvement. Notably, the VP isn't deliberately aiming for higher rungs of the corporate ladder.

"I don't think so much about titles as I do about the excitement of leading organizations that are member-focused and community-focused," she says. "I think the financial results and the success of the credit union will come if we can focus on relationships with a goal of impacting the lives in the communities we serve."

Diane Franklin *is a freelance writer based in Missouri.*

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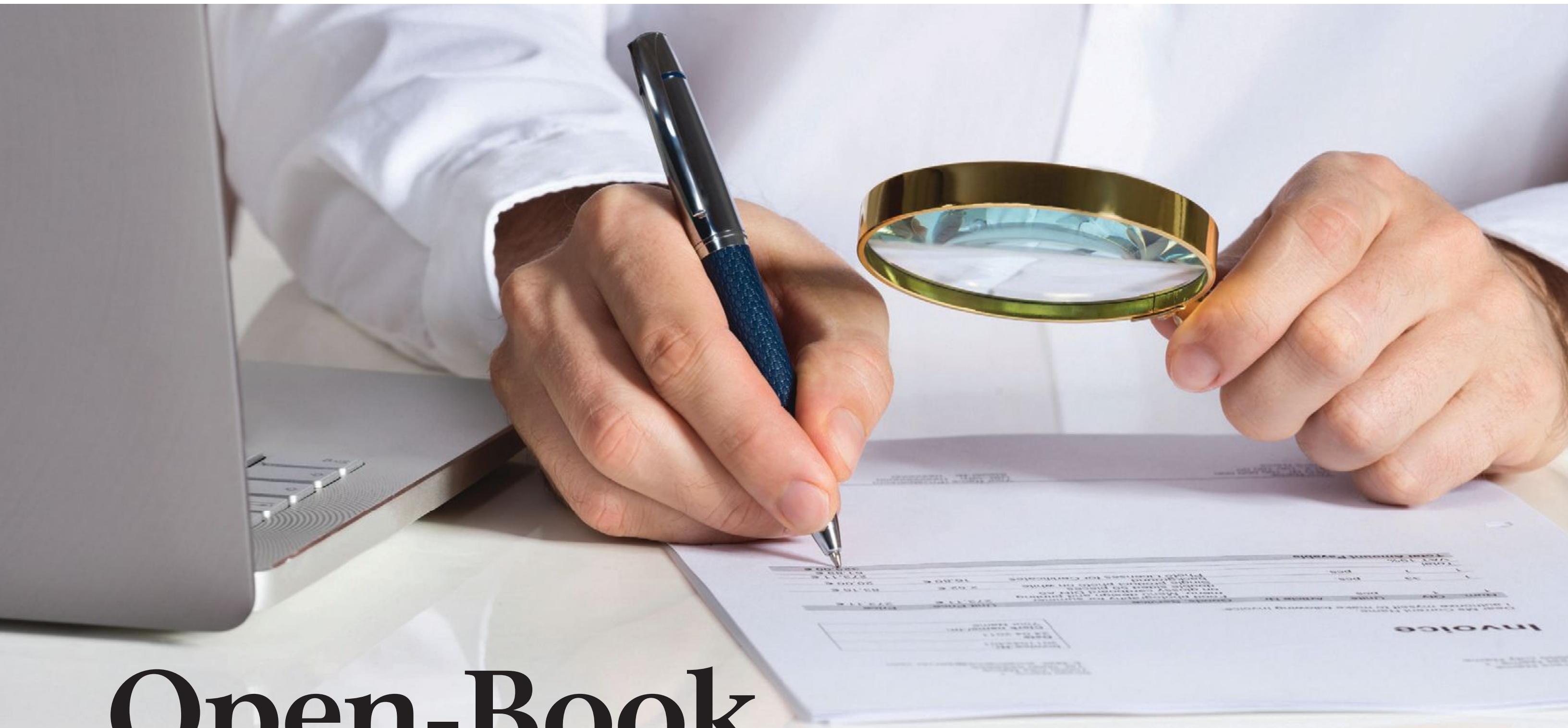

Open-Book *Executive Benefits Exam*

FOUR WAYS TO USE NCUA'S GUIDE TO STRENGTHEN YOUR CU'S APPROACH

BY JOHN PESH

If you've been through a number of National Credit Union Administration examinations, it's quite possible you've been on the wrong end of one that stopped cold when the examiner asked about investments tied to funding employee and executive benefit expenses.

Sometimes, credit unions struggle to find supporting documentation for their plans. Or perhaps board members and executives can't answer basic questions about the investment strategies and products they're using to prefund employee health plan and 401(k) expenses, fund a CEO's 457(f) plan, or myriad other benefits.

Whether you have a program or are looking to add one, you can avoid difficult, time-consuming examination glitches by using the online NCUA Examiner's Guide (*tinyurl.com/NCUAExaminersGuide*).

It's an excellent resource, especially in explaining the unique rules that pertain to investments for employee benefits.

Check out the section titled "Employee Benefits and Investments for Employee Benefits" (*tinyurl.com/NCUAEmployeeBenefits*). On this section's home page, NCUA establishes that, to fund certain employee or executive benefits, it "... allows federal credit unions to fund employee benefit obligations with investments that are not subject to the investment limitations of the Federal Credit Union Act and Part 703 (*tinyurl.com/Part703*) or, as applicable, Part 704 (*tinyurl.com/yafjpdfw*) of NCUA rules and regulations." (Many state-chartered, federally insured CUs have the same or very similar rules, some of which are detailed in this guide.)

With this wider scope of investments, of course, comes a wider array of risks. The online guide provides a thorough road map for navigating these risks. To help you use the guide, here are four key topics that deserve your attention.

1. HOW EXAMINERS ASSESS INVESTMENTS

The guide lists six steps its "field staff" should take in assessing a CU's otherwise impermissible investments. Among the steps are some quantifiable guidelines on the percentage of a CU's net worth these investments should represent, including:

- When a federally insured credit union's exposure to otherwise impermissible investments exceeds 25 percent of its net worth and the risk is not borne by one or more beneficiaries, field staff must expand the examination scope of review.

- Review the CU's exposure to single non-governmental obligors. Individual exposures in excess of 15 percent of net worth are considered unsafe and unsound. They may result in required corrective action and/or a downgrade in the CU's CAMEL or risk ratings unless there are sufficient mitigating factors.
- Review the credit union's concentration of any non-investment grade investments. A concentration greater than 25 percent of net worth is generally considered unsafe and unsound and may result in required corrective action and/or a downgrade in the credit union's CAMEL or risk ratings unless there are sufficient mitigating factors.

Such restrictions as the 15 percent of net worth for a single obligor most often come into play with insurance products such as life insurance and annuities. Even though the investments that underlie a life insurance policy may be diversified, the credit union's risk still lies with the viability of a single entity: the life insurance company.

Overall, the "Investments that Fund Employee Benefits" section of the guide is an excellent overview of the entire guide. It's almost like an open-book test for an exam.

Quick Click to This Section:
Federal credit unions: *tinyurl.com/NCUAFCUBenefits*
State-chartered CUs: *tinyurl.com/NCUAFISCUBenefits*

2. INSURANCE PRODUCT OVERVIEW

Insurance products are among the otherwise impermissible investments that can be used to fund benefits.

CUs don't appear to be using annuities as investment vehicles often, but they can be useful. For example, some include competitive fixed crediting rates, and certain varieties can protect against downside risk because the provider guarantees a floor for returns.

The life insurance material in the guidelines includes a good summary of the difference between "institutional insurance" and "retail insurance." This is a helpful distinction for CU executives and boards considering these products to fund supplemental executive compensation plans.

The key difference is that if you pay, say, a $5,000 premium for a retail life insurance policy, its surrender value at first may be something like $1,500. The cash values typically build slowly. But if you pay the same premium for an institutional policy, the initial cash value will usually be about $5,000. It looks more like a true investment. (*These numbers are for illustrative purposes only. They do not represent any specific investment and may not actually be achievable.*)

Quick Click to This Section:
tinyurl.com/NCUAInsuranceProducts

3. DEMONSTRATE DIRECT RELATIONSHIPS

NCUA hasn't given credit unions permission to earn unlimited returns from investments that are outside the limitations of Parts 703 and 704. You must show that these investments are "directly related to a defined benefit plan or employee benefit plan, when a credit union has an actual or potential obligation under the plan."

The "Direct Relationship Requirement" section summarizes how credit unions can demonstrate this direct relationship. In general, NCUA is looking for investments that have return profiles consistent with—but not more than—the projected expense.

Employee health benefits, for example, have a somewhat consistent cost year over year, so NCUA will be looking for an investment with a relatively predictable return.

This expense might be a good fit for institutional life insurance (often called BOLI; read more at *cumanagement.com/0217boli*). With the right type of policy, you get a consistent rate of interest as stated by the insurance carrier, and it typically has very low volatility. You can demonstrate to examiners how the investment ties to the expense, both through financial modeling and by examining the terms of the contract.

The guide states that equity and commodity investments generally aren't suitable for funding employee benefits because their expected returns aren't predictable. However, it doesn't state that such investments are prohibited, and details some circumstances in which equity investments would be permitted:

For example, a credit union may want to offer equity options for a senior executive's 457(b) plan. In such circumstances, it would be prudent for a credit union to manage the exposure of having an equity-based liability by holding an identical offsetting equity asset on its balance sheet. The matched asset and liability would mitigate undue basis risk (the credit union would avoid a net long or short exposure) and meet the direct relationship requirement.

An important point the guide makes about demonstrating a direct relationship between an investment and a benefit: You must have the benefit plan you intend to fund in place before making the investment. "This means the benefit plan has been formally adopted and the CU has calculated the projected expense using reasonable and supportable methods and assumptions," the guide says.

Quick Click to This Section:
tinyurl.com/NCUADirectRelationship

4. THE PRE-PURCHASE ANALYSIS

The "Pre-Purchase Analysis of Investments for Employee Benefits" section is a step-by-step due diligence guide. Again, almost like an open-book exam—except that these steps must be taken long before an actual NCUA examination.

The guide specifies that boards should have a written policy covering the investment pre-purchase research and decision-making process. It presents 10 steps as one example of an approach to a comprehensive pre-purchase process:

Step 1: Identify the need for the investment. The guide states: "A CU should determine if it actually warrants making an investment by first identifying the actual or potential benefit it seeks to fund (for example, deferred compensation agreement, post-retirement benefit, or others)." The guide also clarifies that these investments are to offset future expenses, not past expenses.

Step 2: Ensure what the amount and direct relationship of investments are. The language in this section includes, "When using investment strategies to recover employee benefit costs, the projected future returns from investments should not exceed the estimated benefit costs." If returns exceed benefit costs, NCUA may require CUs to reduce their otherwise impermissible investments.

Step 3: Determine the economic benefits and appropriate investment types. This advocates for using multiple scenarios when determining potential returns. For example: "Before purchas-

MORE ON EXEC BENEFITS

What Is 'Split-Dollar' Life Insurance? (*cumanagement.com/0518splitdollar*)

Split-Dollar Plans: Tools for Retention (*cumanagement.com/0717splitdollar)*

The CUES Podcast 61: Pre-Purchase Analysis of Investments for Funding Benefits Plans (*cumanagement.com/podcast61*)

ing insurance products for employee benefits, a credit union should analyze expected returns using multiple scenarios. A CU should consider using a range of interest-crediting rates and mortality-cost assumptions for insurance products."

Step 4: Assess the qualifications of insurance vendor(s), if applicable. Examiners are instructed to make sure credit unions know what they're buying and who they are buying it from. "Management should demonstrate a familiarity with the technical details of the credit union's insurance investment assets and be able to explain the reasons for, and the risks associated with, the product design features they have selected." In addition, the guide states: "A credit union that uses a vendor should conduct due diligence to assess the vendor's ability to honor its long-term commitments, particularly when the vendor will service the credit union's insurance program over an extended period of time."

Step 5: Review the characteristics of available insurance products. Basic insurance products can be combined and modified into more complex products, the guide warns. It also offers an example of how corporate-owned life insurance (COLI—also called business-owned life insurance or BOLI) can be configured for CU accounting advantages.

Step 6: Review the characteristics of available non-insurance investment products. Same basic advice as Step 5 about the complex nature of different and potentially complex investment instruments.

Step 7: Select a counterparty. The guide stresses that using brokers or consultants can help CUs choose which carrier to buy from (the counterparty); however, it keeps the final selection solely the CU's responsibility. "Before purchasing an investment, a CU should perform a credit analysis on the selected counterparty in a manner consistent with safe and sound investment practices."

Step 8: Analyze the associated risks and the ability to monitor and respond to risks. This includes a warning about using the right accounting methods for benefits-related investments. "There may be instances where CUs are unaware of the accounting for employee benefit investments and subsequent restatements will be necessary. Insurance products, in particular split-dollar insurance, have the potential for the most material restatements." See the "Accounting" section (*tinyurl.com/NCUAAccounting*)."

Step 9: Evaluate alternatives. Be able to show documentation that illustrates how you compared your options, and why you chose as you did.

Step 10: Make and document the investment decision. The nine previous steps constitute a comprehensive and supportable pre-purchase analysis. Include this in your documentation and update regularly as part of the ongoing oversight of the investments selected.

Quick Click to This Section:
tinyurl.com/NCUAPrePurchase

Documentation to Have *Ready for Examiners*

During an examination, NCUA field staff may request a list of any otherwise impermissible investments to fund employee/executive benefits. The online NCUA Examiner's Guide (*tinyurl.com/NCUAExaminersGuide*) lists other documentation the examiners may request to assess those investments, including:

- ☐ board minutes
- ☐ audit reports
- ☐ 5300 call reports
- ☐ investment schedules and reports, such as management contracts, executive compensation plan agreements, insurance policy contracts, etc.
- ☐ employee benefits policies, such as your policy for investments that fund employee benefits, which should include controls and limitations regarding investments that are permissible only for offsetting employee/executive benefits costs
- ☐ employee manuals
- ☐ financial statements for liabilities and other obligations, such as post-retirement benefits

SEE THROUGH EXAMINERS' EYES

If you already use otherwise impermissible investments to fund certain employee and/or executive benefits, studying the information that NCUA examiners use should help you prepare for examinations and audits.

If you *don't* currently use these types of investments, this guide can be a resource to help you start a solid investment program that can be used to offset some of the growing costs for employee benefits and supplemental executive benefit plans.

That fact that the guide was written primarily for NCUA examiners is an advantage. It helps you prepare by looking at your benefits funding program through the eyes of someone whose job it is to make sure you're doing the right thing.

John Pesh *is director of executive benefits at CUESolutions Platinum Provider CUNA Mutual Group* (cunamutual.com)*, Madison, Wisconsin. For more information about benefits prefunding and executive deferred compensation plans, contact him at* 800.356.2644*, ext.* 665.8223*.*

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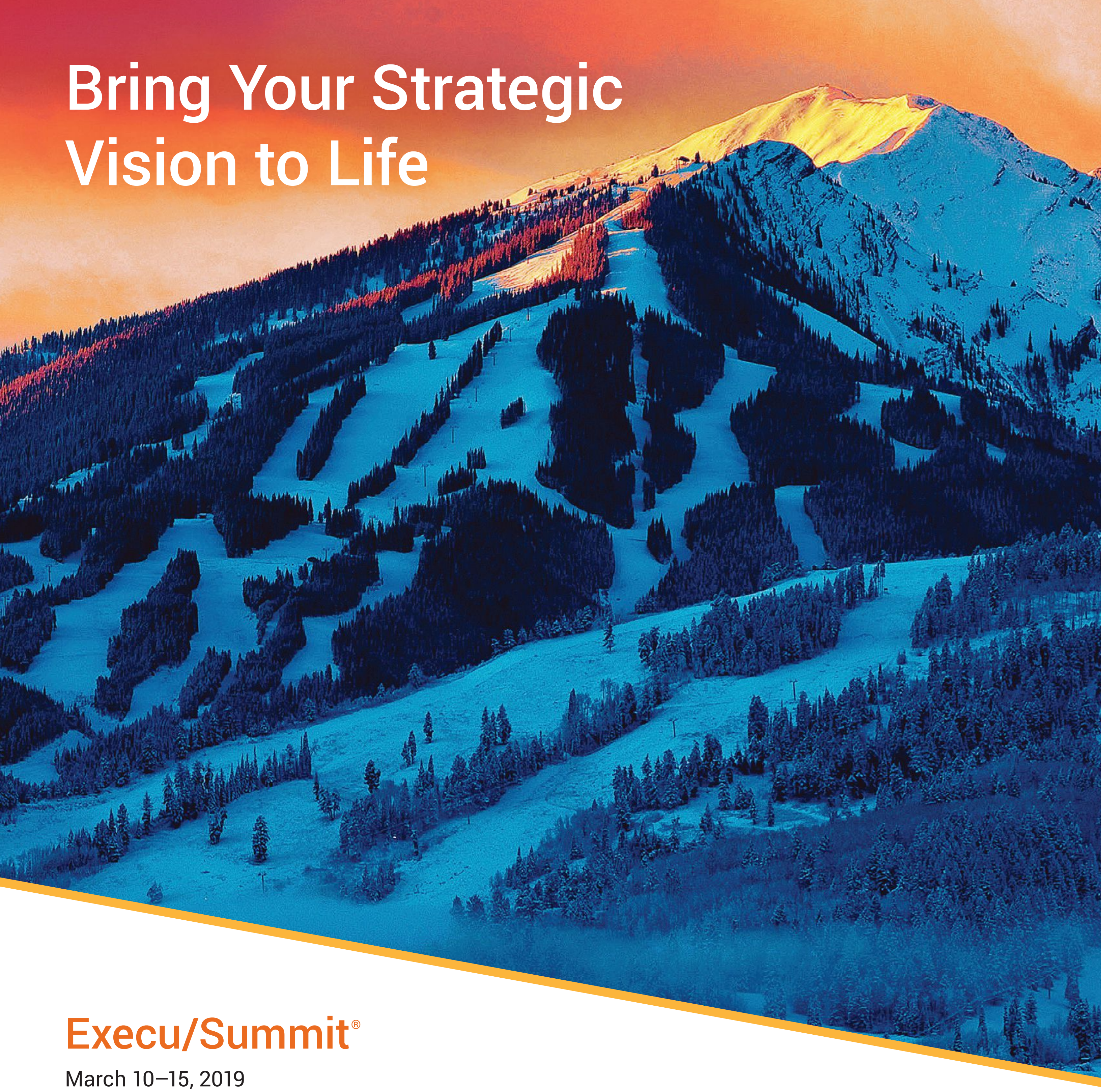

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Special Report: Growth

Credit Union Management

FEBRUARY 2019

THE BALANCE SHEET/ GROWTH CONNECTION

In early 2017, Oregon Community CU bolstered its net worth and ROA with a balance sheet restructuring. Find out why and how the CU did it.

PLUS

Manage Your Balance Sheet *for Growth*

IN 2017, OCCU RESTRUCTURED NOT ONLY ITS LOAN PORTFOLIO, BUT ITS ENTIRE BALANCE SHEET. THAT EFFORT BOLSTERED THE CU'S NET WORTH RATIO AND ROA.

BY BRYAN OCHALLA

Oregon Community Credit Union (*myoccu.org*) began 2017 with a loan portfolio of $1.6 billion.

As you might imagine, that figure pleased the Eugene-based CU's management and board.

A related figure that pleased both groups a bit less, or at least put them in a contemplative mood: A whopping $1.1 billion of that portfolio—70 percent of it—was in auto loans.

What did it prompt OCCU's leadership to put under the microscope in the months that followed?

For starters, it caused the CU's leaders to look at diversifying the $1.7 billion organization's loan mix. It also drove them to tackle a few other tasks they believed would also benefit its membership.

According to President/CEO Ron Neumann, CIE, a CUES member, the aim was "to lessen our concentration in vehicles while improving yield."

That improved yield would then strengthen the credit union's earnings as well as its net worth ratio, all while keeping liquidity and credit risk in check.

"We thought maybe we should have the balance sheet that we desire rather than the one we've been given" as a result of the CU's strong vehicle-loan growth, he explains.

How did Neumann and his team achieve that feat? Keep reading to find out.

THE BALANCE-SHEET PROJECT

For a bit of background, here are the board-sanctioned objectives the CU set out to accomplish in the early days of 2017:

- Realign the organization's loan mix to address the aforementioned concentration in vehicle loans.
- At the same time, reduce credit loss exposure and lower provision costs.
- Improve the CU's loan yield by "swapping" the auto loan portfolio into other higher yielding loan categories, too.
- Further enhance net interest margin by managing deposit growth and cost of funds.
- Ultimately drive higher loan revenues, concurrent with balance sheet growth management, into improvements to net worth and return on average assets for subsequent investment and growth.

Neumann and colleagues like CUES member Greg Schumacher, OCCU's chief financial and administrative officer, didn't just dive into these objectives, of course. They spent the early part of the year preparing. Those two or three months of modeling were key, Neumann says, "because you need to understand where you're at and where you're going before you can come up with how to get there and by when—and at what cost, too."

OCCU has a "robust business intelligence group that ... looked at the profitability of our various tranches and how we might participate out some of our balances in order to free up liquidity," Schumacher explains, "so we could then move those existing loan balances into other loan products."

All of that modeling, he adds, was "designed to prompt our thinking around how much we should have in auto loans and participations, and how much we should expect coming out of the auto book into mortgage and business book."

Within 90 days, Neumann says, "we had completed our modeling, and we had concluded that we were going to move in the right direction, that those moves supported the vision of the board, and that the board members themselves were supportive of the moves we were planning to make."

By the end of the second quarter of 2017, Schumacher shares, the CU was engaged in several "very deliberate activities to begin the process."

INDIRECT LENDING STRATEGIES

The activities Schumacher refers to here went beyond rate-sheet pricing changes designed to curb auto loan originations.

One example: Neumann says a critical area for the credit union was "to build our muscle around price elasticity as it relates to indirect lending."

What you're trying to do when you test price elasticity, Schumacher explains, "is drive indirect volume down to the extent that you can then replace those dollars with mortgages or other business but still remain a premier indirect lender within the market and also continue to serve your members."

"We did a lot of testing," Neumann adds. "We tried different pricing strategies. In some cases, we even raised the price—only to see demand increase. Which naturally made us think: *That's interesting*. It definitely wasn't what we expected."

Another "muscle" Neumann, Schumacher and their colleagues worked out in the months that followed their decision to restructure OCCU's balance sheet: loan participations.

"We're a strong originator," Neumann says. "Which means we sometimes originate more auto or RV loans than we'd like. But that's our job, right? To serve our members. So we asked ourselves: What can we do with that? How can we manage or control that side of the business, rather than exit it completely or grossly change all of the relationships we've developed over the years?"

The CU's response was to retain the servicing on those loans, but sell some of the excess origination. "That way," Neumann offers, "we could keep the member relationship and also diversify our balance sheet."

Succeeding at that was easier said than done, according to Schumacher. "We need to make these pools attractive enough for the investors to buy into, while at the same time we need to retain pools on our balance sheet that are attractive to us. The modeling we did allowed us to be really nuanced in terms of what we would sell versus what we would keep," he adds.

All of that hard work paid off in the end, too. "We sold millions of dollars' worth of participations at either par or better," Schumacher says. "At the same time, we retained—in a rising rate environment—those new rate-sheet loans that our elasticity testing told us were profitable in our portfolio."

4 Growth *Questions*

Mike Dionne, SVP/community markets, Americas at Finastra (*finastra.com*), a global company offering financial services software and cloud solutions, discusses obstacles and opportunities for credit union growth.

What are the main barriers for credit union growth? The primary barriers to growth are not having the proper insight and tools: insight in the form of understanding the needs of the credit union's membership and tools that help the CU reach that membership in the fashion the members prefer.

Credit unions have nearly unlimited growth opportunity with current members. Deepening those relationships represents a significant growth opportunity. Is this member part of a broader household? Where is this household in its financial life cycle? Understanding fundamental elements like these will inform the products and services your CU should be putting in front of members.

How the CU puts these products and services in front of the member is the second component in driving growth. The CU must have the tools to reach its members where and when members require. The most obvious example is in the digital arena. The migration of engagement from the physical to the digital world has been rapid. Has your CU kept up? For example, do you have the means of reaching your member with an informed cross-sell message on the member's mobile device?

How should credit unions think differently about growth? Historically many CUs have thought about growth in terms of entering new geographies, perhaps with a new branch. While physical locations will remain an essential component of CUs' service offering, they are not always essential to enter new markets. CUs need to think long and hard about the cost and effort associated with building new locations. In the digital era, significant growth can be achieved without a physical presence.

What mistakes do CUs make when they want to grow? Driving demand for your products and services is a big part of growth. However, responding to that demand in an expedited manner is essential for achieving growth. We've seen a number of credit unions develop new lending campaigns with strong response from their membership. But the campaigns fell short of expectations as the CU did not have the infrastructure in place to respond with timely decisions and fund the loans.

What are some positive CU growth stories you have seen? Consumer's Credit Union (*consumerscu.org*) in Michigan fueled substantial growth through a creative program called Consumers@Work (*consumerscu.org/businessservices/atwork*). Partner companies of Consumers CU invited the credit union in to educate employees with the intent of improving their financial well-being. Not only did this lead to a better educated consumer, it helped Consumer CU grow deposits and loans.

There is no one path to growth. The best day-to-day practice is simply a matter of educating yourself on the various paths your industry peers have taken.

MORTGAGE AND BUSINESS LOAN GROWTH, TOO

The strategy Neumann, Schumacher and others at OCCU employed to restructure and grow the organization's balance sheet went beyond improving their indirect lending efforts.

They also moved some of the credit union's auto loan dollars into other "higher yield, lower credit cost buckets," as they call them. Specifically, they moved them into mortgage and member business loans. (And most of those member business loans were in commercial real estate.)

"On the mortgage side, we purchased some mortgages," Schumacher explains. "And we purchased some that were in our market, so they were member-servicing as well."

The CUs' leaders also were able to "put more of the mortgages we originate into our own portfolio," he adds, "thereby increasing its (mortgages) percentage of the pie on our balance sheet."

For Schumacher, one of the keys to the CU's growth in this area was "opening up the gates for the folks in the mortgage area to serve members more aggressively than they had in the past."

Granted, the reason they could open those gates as wide as they did was because of the "newfound liquidity to do so coming off our new auto strategy."

Also helping matters: "Our marketing, member experience and channel folks created some very important digital opportunities around first-time homebuyer, mortgage education and referrals," Schumacher adds. "If you look at our mortgages today, for example, I would say a substantial number of our referrals come from those digital channels. And that's a testament to what those folks have done ... to drive that business."

As for the member business side of the equation, Neumann says that "while we've done it for many, many years, we didn't do so in a material way" until early 2017. Since then, OCCU has "very carefully built a portfolio out of commercial real estate."

Schumacher suggests a lot of the growth here has come as a result of "some important vendor and partner relationships, not unlike what we do on the indirect and participation side.

"As we sought to drive our balance sheet restructure and net worth growth, we employed both auto participations and volume reduction activities," Schumacher adds. "We leveraged two key partners, Raymond James (St. Petersburg, Florida, *raymondjames.com*) and Catalyst Corporate Credit Union (Plano, Texas, *catalystcorp.org*), plus our participating CUs, and especially valued our repeat buyers. In addition, our indirect auto dealer partners embraced and accepted our rate sheet changes and volume management efforts, while still providing volume at levels we desired. Our outcome could have been different absent this type of response."

DIGGING INTO THE DETAILS

How exactly have the moves detailed above as well as others helped restructure and even bolster OCCU's balance sheet?

For starters, Neumann and his team moved $119 million out of vehicle loans and into mortgages. That represents a 53 percent increase in the mortgage portfolio since the end of 2017.

And they moved $27 million from the credit union's auto loan "bucket" to its member-business loan one—a 140 percent increase in MBL balances, according to Neumann.

All of that "swapping out" allowed OCCU to reduce its concentration in auto and RV loans from 70 percent to 59 percent in just 11 months.

That last accomplishment, in particular, has thrilled both the CU's executives and board members. "To make a change like that is significant," Neumann asserts. "We've participated $350 or $360 million in 2018 alone," he adds. "Those are some very serious figures."

OCCU's growth in net worth ratio also could be labeled as serious. "We began 2018 at 8.38 percent net worth, and that's increased nearly 100 basis points since," offers Neumann. As of late November, that figure was at 9.33—and he expected it to inch up even a bit more by the end of the year.

LOOKING AHEAD

Neumann and Schumacher have a similarly rosy outlook for 2019.

"We are very happy with what we've achieved thus far, but we also see 2019 being similar to 2018 and 2017—in that we'll continue to work on refining our balance sheet," Schumacher says.

In other words, they'll continue to de-emphasize the auto portfolio. That said, after all they've done, "there's not as much room to do that now," he adds. "And with the market potentially slowing down, there may be less room to be aggressive on the mortgage side in 2019, too."

Where will OCCU look instead for growth? Home equity lines of credit are one possibility. "The refi business has kind of gone away, with rate environments staying in the upward trajectory, but there's still opportunity to build a HELOC book. We're looking at that," Schumacher points out.

They're also looking at building the organization's (relatively small, at the moment) credit card portfolio.

In general, though, Neumann expects to do "more of the same—while making some nuanced changes to our strategy that will help us move past the fundamental success we've seen so far and move toward further optimizing our balance sheet."

Bryan Ochalla *is a freelance writer and former* CU Management *editor based in Austin, Texas.*

MORE ON GROWTH

Mortgage Market: What Credit Unions Should Expect in 2019 (*cumanagement.com/1218mortgage*)

Getting Smarter with Student Loans (*cumanagement.com/1118studentloans*)

CUmanagement.com "Growth" archive (*cumanagement.com/growth*)

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Driving Stellar Service with Workflow Automation

Dupaco Community Credit Union automates processes to ensure compliance and focus on members.

The Challenge

Dupaco has grown into one of Iowa's leading credit unions. Along the way, their mission has always remained the same—to improve its members' financial position and build valued relationships with the community it serves.

In the last few years, they've been focused on growing into new areas and expanding their range of services while continually engaging existing and new members. As Dupaco grew, it needed to maintain the high level of service that its members had come to expect.

Keith Chaston, IT Operations Supervisor at Dupaco, says, "Whether it's opening a new account or issuing a mortgage loan, the services we provide often involve many different steps. As we took on more business, we wanted to avoid weighing staff down with more administrative work. Our teams should spend most of their time face-to-face with members, not hidden behind a computer. To free-up more time for one-on-one member interaction, we looked for a way to automate as many routine tasks as we could."

The Solution

Since 2010, Dupaco has counted on Fusion Phoenix from Finastra for its core technology. The organization decided to build on this foundation with Fusion Phoenix's workflow manager to automate key processes. "We were one of the first credit unions to go live on Fusion Phoenix's workflow manager, and were closely involved in the development process with Finastra," Chaston said.

Dupaco has harnessed the workflow manager to streamline several workflows, including payroll processing and transfers. Additionally, the organization automated Pay Pause requests—a popular promotion allowing members to pay $25 to pause a loan payment without incurring penalties. Dupaco typically runs the promotion in December, processing between 10,000 and 15,000 requests.

Many members deduct loan payments from their salary, and if they wanted to pause a payment, the payroll team had to manually remove the loan from distribution so that the funds would not be deducted, then fill in a new service request to return the loan to distribution. This process is now completely automated using workflow in Fusion Phoenix.

"In the past, we had a team of 10 to 15 people managing Pay Pause requests, whereas today we need just 3 people to handle the same work," comments Erik Chaston, Workflow Developer at Dupaco. "Fusion Phoenix's workflow manager has made our Pay Pause service much more efficient and profitable."

Newfound Insight and Control

Improved workflow management has also enabled Dupaco to track process changes in a more straightforward and consistent way. Previously, as employees worked through a certain process, they used paper checklists to track actions.

Now, Fusion Phoenix's workflow manager guides teams through pre-defined steps and provides a complete record of all actions taken, helping management to ensure that all tasks are completed properly and offering a full audit trail to strengthen compliance, giving them much better visibility and control of end-to-end processes.

Greater Efficiencies, Better Service

By automating key workflows, Dupaco empowers its team to work more productively and minimizes the risk of process errors and inconsistencies.

"When you have people manually handling a process and entering data into systems, it opens up room for errors to creep in," remarked Keith Chaston. "With Fusion Phoenix's workflow manager, we're reducing reliance on dual data entry and manual work and we feel confident that processes are running flawlessly." With employees free from tedious and time-consuming tasks, they have more time to devote to one-on-one interactions with members.

Growing Strong

As Dupaco adheres to its mission, the new efficiencies delivered by Finastra's technology will help the organization keep tight control over costs. "The workflow manager in Fusion Phoenix helps us maintain lean operations as we expand into new markets and welcome new members," says Erik Chaston. "We've been able to redistribute resources, as improved efficiencies have enabled us to move existing employees into different roles, which has been a great help in keeping costs down. Fusion Phoenix's workflow manager is a positive investment for member engagement, efficiency and accuracy."

Dupaco Community Credit Union automates processes to ensure compliance and focus on members.

GROWTH IS IN THE NUMBERS

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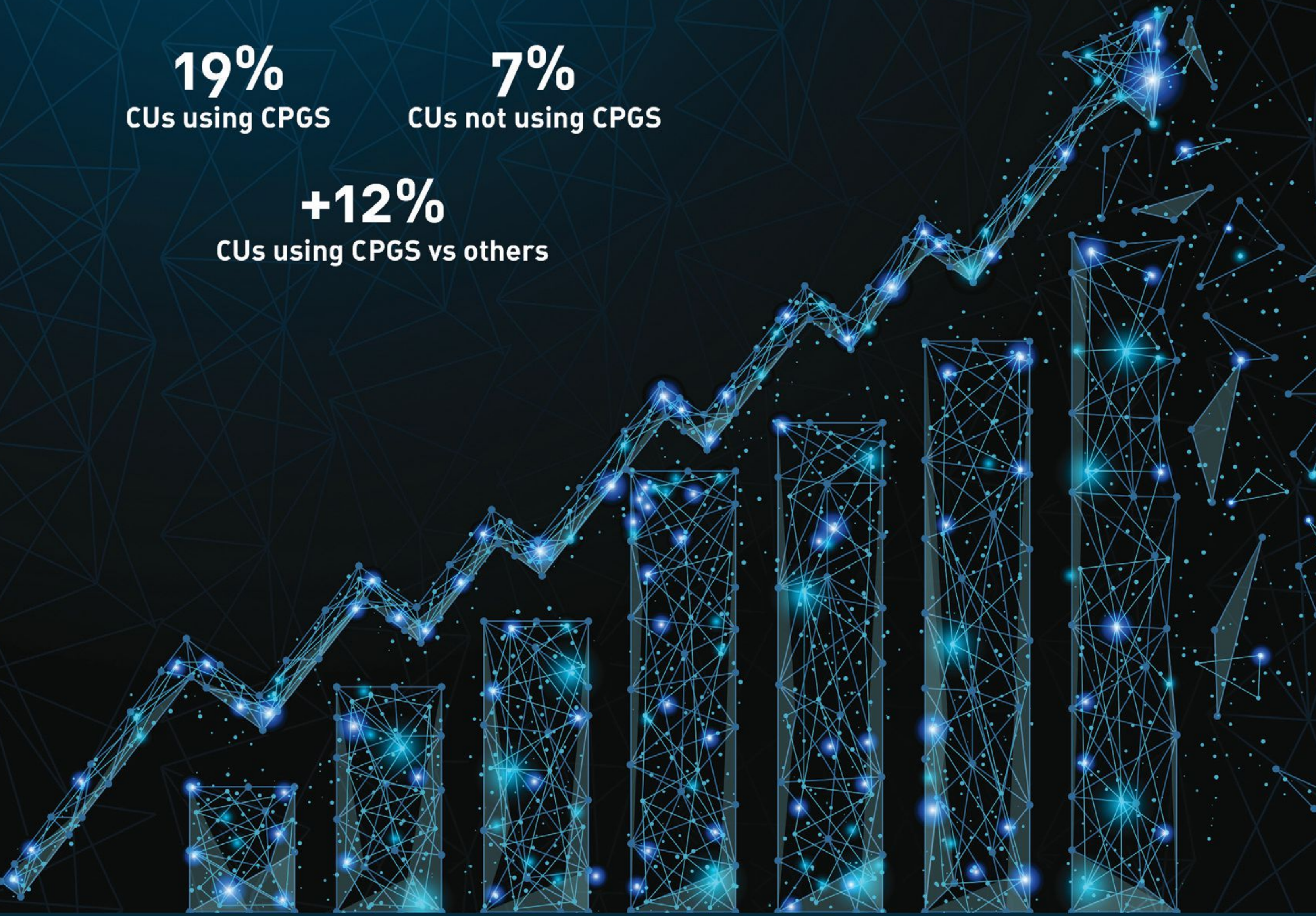

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CASE STUDY

TBA CREDIT UNION REAPS THE BENEFITS OF TRELLANCE'S CLIP

STAYING "TOP OF WALLET"

As the financial industry becomes more competitive and consumers continue to get multiple credit card offers, credit unions must maintain relevance by offering attractive card products and doing what is required to stay "top of wallet." One of the strategies that has worked for many credit unions and is encouraged by payments executives is conducting an annual credit line increase program (CLIP). "By using the data from card portfolios, credit unions can reward members with the limits they have earned based on their utilization and payment history," said Ann Farrell, Director of Portfolio Growth at Trellance. "This will give members more spending power, reduce voluntary attrition and enhance cardholder loyalty," she added.

GROWTH IS IN THE NUMBERS

Trellance has been assisting many credit unions to realize growth with their CLIP, which is packaged within their Card Portfolio Growth Solutions (CPGS) and a-la-carte. Also, the fact that it is brand and processor neutral make it accessible to all credit unions.

"We have seen some great results from credit unions that have participated in our CLIP in 2017 and 2018. The balances on the cards that received increases went up by $27.9 million, while the balances on those that did not receive increases went down by $3.2 million," stated Farrell. "We are estimating that we made $2.5 million in additional interest income for the credit unions that participated," she noted. To date, over 100 credit unions have participated in the program.

A VALUABLE VENDOR PARTNERSHIP EQUALS GROWTH

One of the credit unions that has benefitted from Trellance's CLIP is TBA Credit Union, which is located in Traverse City and boasts an asset size of $218 million and 17,000 members. Chase McLennan, Member Service Specialist at TBA, said that before the CLIP they did not have many initiatives to grow their card program and they were looking for opportunities to use their program as a tool to improve member relationships. "After seeing the incredible results other credit unions had with the CLIP offering from Trellance, we decide to use it. It seemed like a no-brainer to look into it," said McLennan. "Trellance was vital throughout the process. If I needed an answer, I was able to get it that day. It really helped to keep the ball rolling and meeting our deadlines," he added.

They increased the limits on over 1000 cards, and with an opt-out rate of only 2% approximately, they increased the overall balances for the qualifying group by +30%.

When asked how other credit unions can benefit, McLennan noted that "The program allows you to optimize and make your card portfolio much more efficient." He added that "Identifying and rewarding your loyal members will put your card "top of wallet" by providing members with additional spending power."

Moving forward, McLennan said his credit union would certainly consider implementing the CLIP again, along with other initiatives that will provide benefits for the credit union and its members. On her part, Ann Farrell notes that, "It is imperative that the credit union couples the CLIP with Trellance's Balance Transfer and Usage Promotions to get the full lift in outstanding balances, interchange, and finance charge revenue, making their card "top of wallet" and increasing the total profitability of their portfolio."

Negotiating *the What-Ifs*

CREDIT UNIONS CAN'T RELY SOLELY ON STANDARD BOILERPLATE IN VENDOR CONTRACTS.

BY NICK LANE

In novels and movies, business partners meet, shake hands and go on to make beautiful profits together. Credit union leaders and technology vendors desire the same ends, but the means—thorough and thoughtful negotiations over contract details—are the stuff that fiction writers leave out of their stories.

It is the nature of financial services that unexpected challenges arise, and that may be especially true in new and ever-evolving digital channels and systems. Since credit unions can't rely on superheroes and plot twists to solve those problems, they need to be able to turn to the terms set in their vendor agreements. That's why the potential impact of every clause on credit union operations must be considered carefully, not just dismissed as standard boilerplate.

Let's delve into two examples that may get short shrift in contract negotiations: addressing recourse for performance shortfalls in service-level agreements and getting a handle on deconversion costs in the event of contract termination. Beyond that, credit unions need to consider how issues of liability are handled by the contract—and what legal and consulting expertise they might need to help them make the best deal for the long term.

SLAs WITH TEETH

Many credit unions do a good job of asking for service-level agreements that spell out expectations for the quality and availability of the technology systems for which they are contracting. Where some fall short is in specifying the recourse options if the vendor does not deliver on SLA standards. What happens if the core processing system is offline beyond the benchmarks set in the contract? Does the agreement spell out credits or discounts the credit union would receive for excessive outages? If system issues persist, what termination rights does the credit union have?

Guidance from the Federal Financial Institutions Examination Council (*ffiec.gov*) clearly states that credit unions should insist on objective measurements for performance on significant service elements and "link SLAs to provisions in the contract regarding incentives, penalties, and contract cancellation in order to protect themselves against service provider performance failures." There is no set-in-stone contract language for these recourse provisions. They are vendor- and product-specific, and the type of recourse tech companies are willing to write into contracts varies widely.

ANTICIPATING A PARTING OF WAYS

A second example involves spelling out in the contract the costs associated with data transfers when a credit union switches to a new provider. In signing on for service with a new technology company, a credit union will need to negotiate the conversion costs involved in bringing account files or other records over to the new system—and the "deconversion" service costs charged by the existing company to assist in data transfer, cleanup and testing.

These charges are distinct from any penalties for early termination of a contract, but deconversion services are often covered in the same section of the agreement, typically in a stipulation stating that the vendor will assist the credit union with this process based on its "then-current rate." Regardless of the circumstances under which the credit union moves to a new system, it will need the existing vendor's programming assistance in transferring data, and the price tag of those services can be significant.

Negotiating more specific language regarding deconversion costs may not be easy. As with SLAs, the range of options and the willingness of vendors to negotiate well-defined contract clauses on this issue fluctuate extensively. Vendors may have a hard time projecting how they would price those services and how much special programming might be needed.

When our clients are negotiating vendor contracts, we recommend that they advocate for some type of deconversion cap. Most credit union executives don't think to raise this issue as they're discussing contract terms, and they end up dealing with sticker shock when they ask for a cost estimate from their current vendor while planning to switch to a new system.

By addressing this issue during contract negotiations, a credit union will be better prepared when the situation arises. If the topic of deconversion costs is not a standard part of contract due diligence, it should be. Technology contracts should spell out what services the vendor will perform and what the costs are throughout the relationship, including the exit stage.

BIGGER RISKS, GREATER SCRUTINY

Liability is a paramount concern in vendor negotiations. The credit union should focus on contract sections that address the potential for negative outcomes and aim to negotiate reciprocal terms. What are the vendor's and credit union's responsibilities for any liability that may arise as a result of this business partnership?

The contract should spell out the answers to this crucial what-if. A go-it-alone approach to negotiating these terms is not advisable, especially for mid-size and smaller credit unions that may not have the in-house expertise to guide these discussions and build in the necessary protections.

Bringing in legal and consulting assistance may seem like adding to the price of already expensive technology partnerships, but complementing the CU team's knowledge with insider know-how can pay dividends over the long term.

As with other aspects of vendor management, technology contracts are not created equal. The digital solutions that credit unions rely on today to power their operations and member service carry a wide range of costs and risk exposure. The risk ranking a credit union employs to guide vendor management also comes into play during contract negotiations. Systems and solutions with a higher price tag and greater risk potential—those in the top vendor management tiers—merit greater scrutiny during the due diligence process and greater expertise in contract negotiations. Will the technology have a significant impact on the credit union's ability to do business? Will the vendor have access to members' and/or employees' personal data?

The higher profile the technology—and the more the organization relies on that solution and the vendor behind it—the more essential it is to dig into the contract details and negotiate common-sense protections for the credit union. Thrillers may sell in the world of fiction, but drama-free reliability and safety should seal the deal on vendor agreements.

Nick Lane *is a senior consultant with CUES Supplier member and strategic partner Cornerstone Advisors* (crnrstone.com)*, Scottsdale, Arizona.*

MORE ON VENDORS

Tech Time: Getting the Upper Hand in Contract Negotiations (*cumanagement.com/1118techtime*)

Powering ROI (*cumanagement.com/0218powering*)

Veni, Vidi, Vici (*cumanagement.com/0717veni*)

Cornerstone Advisors (*cues.org/cornerstone*)

Payments University Sept. 11-12, San Diego (*cues.org/payments*)

Managing All *the Moving Parts*

The Federal Financial Institutions Examination Council guidance is a good place to start in identifying the contract terms credit unions should take special care to review in crafting an agreement with a technology provider. That guidance is not necessarily specific; for example, the council advises financial institutions to ensure that vendor contracts address limitations on liability without suggesting what those limits should be. Instead, the recommendations emphasize that credit union leaders take the time they need to review and understand how the contract will affect the organization and look for any missing elements.

In many cases, the credit union team can expect to work from the provider's terms and conditions in its standard master service agreement, which should reflect current regulatory requirements and market norms. Especially in the case of contracts for high-cost, high-risk technology systems, the credit union will benefit from bolstering the expertise on its negotiating team in the form of legal counsel and consultants who are well versed in the financial services vendor landscape.

Vendors draft and present contracts designed to protect their interests. That makes sense. It also makes sense for the credit union to have its own attorney and, in some cases, a consulting business partner who is familiar with technology providers and the current best practices in negotiating agreements that protect the credit union.

CUNA Mutual AdvantEdge Analytics
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CUES is pleased to announce its partnership with CUNA Mutual AdvantEdge Analytics (*advantedgeanalytics.com*), Madison, Wisconsin, as a Platinum CUESolutions provider, for its data analytics and digital transformation solutions.

CUESolutions is designed to easily connect credit unions with suppliers who have the products and services they need to evolve and elevate their success. CUESolutions providers have been identified as industry experts and partner with CUES to showcase their thought leadership.

"We are excited to partner with CUES and provide leadership and guidance that will help credit unions build their data analytics strategies. CUES member credit unions are very committed to innovation and supporting data analytics acceleration that will benefit the industry as whole," says Shazia Manus, chief strategy and business development officer for CUNA Mutual AdvantEdge Analytics.

"And with the continued insurgence of fintech and insurtech startups entering the credit union industry with disruptive and, at times, fragmented solutions, data requires more than a modern technology approach," Manus adds. "We continue to make great strides with accelerated adoption in credit unions, collaboration amongst industry partners like CUES, and strong leadership commitment to transform for the future."

"Building advanced data analytics capabilities and acumen in the credit union space strengthens not only our industry for the future, but it provides a level playing field competitively to grow and thrive long term. We're excited to begin this new phase of our relationship with CUNA Mutual AdvantEdge Analytics," says John Pembroke, president/CEO of CUES. To learn more about CUESolutions, contact Karin Sand, CIE, VP/supplier relations, at 800.252.2664 or 608.271.2664, ext. 341, or email *karin@cues.org*.

Develop High Potential Employees
With CUES Consulting

CUES is pleased to announce the addition of CUES Consulting (*cues.org/CUESConsulting)* to its list of offerings provided to the credit union industry.

Research shows that companies are not providing the next generation of leaders with the guidance they need to mature into a leadership role. Organizations often rely on a self-directed approach to learning and are failing to engage leaders in meaningful development. CUES Consulting supports the creation of focused individual development planning to impact the desire today's learners have for personalized learning and guidance.

"With the War for Talent as strong as ever, it is imperative for credit unions to identify, develop and retain their high-potential employees," says CUES President/CEO John Pembroke. "CUES Consulting offers credit unions a guided and focused leadership development program that they can utilize to advance and strengthen their leadership pipeline that is in line with their strategy and goals."

Most high-potential programs succeed when they are focused on building a talent pipeline within the organization, versus focusing on filling specific roles, which can halt the potential development of an individual. CUES Consulting guides credit unions in developing their leadership pipeline through:

- creation of customized leadership competency model(s) or behaviors aligned to current competencies;
- behavioral evaluation of high-potential employees;
- focused individual development planning; and
- organizational climate assessment.

CUES Consulting delivers on-site leadership training for emerging, developing and strategic leaders. "We offer direct support for credit unions to build their bench strength," says CUES Consulting liaison and Director/Professional Development Jennifer Stangl. "Our guidance and tools help focus development for leaders to build an action plan designed to promote innovation, creativity and change."

Webinars & Elite Access

CUES members can attend all webinars (*cues.org/webinars*) for free and access a library of webinar playbacks. CUES Elite Access Virtual Classroom (*cues.org/eliteaccess*) offers an innovative take on online education.

FEBRUARY 12
1 p.m. Central
Smart Makes the Difference: Using AI to Modernize Payments Business and Strategy (Webinar)

FEBRUARY 19
1 p.m. Central
More Benefits, More Value: Maximizing the Return on Your Investment—A Look at the New CUES Membership (Webinar)

FEBRUARY 19
1 p.m. Central
Your MBL Plan—Are You Asking the Right Questions? (Webinar)

FEBRUARY 20 AND MARCH 6
12 p.m. Central
Strategic Leadership Development for CFOs (Elite Access)

MARCH 19 AND MARCH 26
12 p.m. Central
Becoming an Extraordinary Credit Union Leader (Elite Access)

AD INDEX

To advertise, email ***cathy.woods@mediawestintl.com*** or visit ***cues.org/advertise***. CUES partners and CUES Supplier members are noted in **bold**.

Blending Strategy With *Leadership and Action*

Attend Execu/Blend™ (*cues.org/eb*), April 28-May 1, in beautiful Santa Rosa, California.

Spring can't come soon enough! Join your industry colleagues in welcoming warmer weather while strengthening your credit union at Execu/Blend™ (*cues.org/eb*) in California wine country this April. Like the popular CUES Execu/Net™ (*cues.org/en*) and Execu/Summit® (*cues.org/es*) seminars, this event features intensive learning sessions paired with time to explore Santa Rosa, the vibrant center of Sonoma County—including a field trip to experience how one small Sonoma winery differentiates itself in a highly complicated and complex wine market.

In the mornings, Execu/Blend attendees will learn from strategy and leadership expert Jim Austin, president of JH Austin Associates Inc. (*jh-austin.com*), lecturer at the Aresty Institute of Executive Education, Wharton Business School, and faculty of CUES CEO Institute I: *Strategic Planning* (*cues.org/inst*). Austin will provide a cross-industry perspective on board governance, including accountability and strategic assessments; strategic agility and customer-centricity, including discussions about adaptability and learning faster than the competition; and understanding the relationship between strategy and execution.

The event's final session, "Building a Bridge Between Strategy and Execution," will allow participants to explore a simple, four-part model to optimize execution as well as strategies to make core operations more efficient while keeping an eye to innovative opportunities. They'll also discuss practical "hooks" to guide daily decision-making, a key leadership skill needed to make organizations' strategic aspirations a reality.

"Everyone should feel empowered to bring ideas to the table," says Austin. But, "It's the leader's job to surface different ideas and points of view so that he or she can make the best decision." And that's not always easy, even in the age of data analytics. "I think it's very common that intuition conflicts with data," Austin notes. "In my experience, most decisions start at an emotional, intuitive level, and then we tend to look for data to rationalize it." (Read more from Austin about the art of decision-making at *cumanagement.com/0215eenie*.)

Execu/Blend is a unique event offering insight to credit union leadership from CEOs and senior executives to board chairs, directors and supervisory committee members. Time is running out, so register today at *cues.org/eb*!

2019

EXECU/SUMMIT®
March 10-15
Westin Snowmass Resort
Snowmass Village, CO

CEO INSTITUTE I: *STRATEGIC PLANNING*
April 7-12
The Wharton School
University of Pennsylvania
Philadelphia

EXECU/BLEND™
April 28-May 1
Hyatt Regency Sonoma Wine Country
Santa Rosa, CA

CEO INSTITUTE II: *ORGANIZATIONAL EFFECTIVENESS*
April 28-May 3
Samuel Curtis Johnson School of Management, Cornell University
Ithaca, NY

CEO INSTITUTE III: *STRATEGIC LEADERSHIP DEVELOPMENT*
May 5-10
UVA Darden Executive Education
Charlottesville, VA

CUES SCHOOL OF APPLIED STRATEGIC MANAGEMENT™
May 6-9
Embassy Suites by Hilton Orlando
International Drive Convention Center
Orlando, FL

CUES SCHOOL OF BUSINESS LENDING™ I: *BUSINESS LENDING FUNDAMENTALS*
May 6-10
Embassy Suites by Hilton Orlando
International Drive Convention Center
Orlando, FL

CUES GOVERNANCE LEADERSHIP INSTITUTE™
June 2-5
Rotman School of Management
University of Toronto

CUES SCHOOL OF STRATEGIC MARKETING™
July 15-18
DoubleTree by Hilton Hotel
Cleveland Downtown–Lakeside

CUES SCHOOL OF BUSINESS LENDING™ II: *FINANCIAL ANALYSIS AND DIAGNOSTIC ASSESSMENT*
July 15-19
DoubleTree by Hilton Hotel
Cleveland Downtown–Lakeside

STRATEGIC GROWTH INSTITUTE™
July 22-25
University of Chicago
Booth School of Business

SUPERVISORY COMMITTEE DEVELOPMENT SEMINAR
July 29-30
Portola Hotel & Spa at Monterey Bay
Monterey, CA

DIRECTOR DEVELOPMENT SEMINAR
July 31-Aug. 2
Portola Hotel & Spa at Monterey Bay
Monterey, CA

EXECU/NET™
Aug. 11-14
Summit at Big Sky Resort
Big Sky, MT

CEO INSTITUTE II: *ORGANIZATIONAL EFFECTIVENESS*
Aug. 11-16
Samuel Curtis Johnson School of Management, Cornell University
Ithaca, NY

CUES SCHOOL OF MEMBER EXPERIENCE™
Sept. 9-10
DoubleTree by Hilton Hotel
San Diego–Mission Valley

CUES SCHOOL OF BUSINESS LENDING™ III: *STRATEGIC BUSINESS LENDING*
Sept. 9-13
DoubleTree by Hilton Hotel
San Diego–Mission Valley

CUES SCHOOL OF LENDING™
Sept. 10-12
DoubleTree by Hilton Hotel
San Diego–Mission Valley

Note: CU directors are encouraged to attend events listed in blue. For all future CUES events, visit *cues.org/calendar*.

The Answer to the 'Most Important Question' *Should be Steering Your Strategy*

BY JEFF RENDEL, CSP

Albert Einstein is credited with stating, "If I had an hour to solve a problem ... I would spend the first 55 minutes determining the proper question to ask." What's the most important question your credit union's leadership team is asking about the future? What answers are steering your strategic plan?

More than 50 credit union CEOs from numerous asset sizes and locations have shared their "most important question." A dozen general themes emerged. Here is a sampling of what other leaders are asking to help set strategy:

- For continued success in membership growth and revenue, what products, services, or markets are necessary to refine, expand or introduce?
- We can't be all things to all people. Where should we focus our energies? What is our core market?
- What is our capacity for growth? Can we grow organically or should we seek partners? Are we better for our members as a merged credit union?
- The member experience is vital to success. What next levels of friction-free marketing, service, delivery and technology will be necessary for member engagement?
- Our members own the credit union. How do we best engage them as owners, continuing to deliver, increase and confirm value? What makes us the obvious choice?
- What measures of success are most important to gauge our strategic progress? What are optimal levels for revenue generation, service, efficient operations, profits and capital?
- How do we—as executives and board members—remain relevant for the members we serve and represent? Do our staffing and board compositions reflect our membership?
- Does our culture match our brand, and are we equipped to deliver the kinds of products, services and experiences that our members value most?
- Who is disrupting our business? What value are they providing to members? Can we compete? Can we partner?

Conventionally, credit unions hold strategic planning sessions each fall. In reality, it's always planning season. As you develop, expand and refine your strategic plans, consider some of the questions above. While several will be immediately beneficial, others will spur conversation and your own sets of "most important questions." Often, asking is the most challenging part of handling a question. The answers can set out your credit union's next strategic steps in serving the long-term needs of its members.

Jeff Rendel, CSP, *is president of Rising Above Enterprises* (jeffrendel.com), *Corona, California.*

Read more questions, leave a comment and subscribe to Skybox via email at cumanagement.com/121718skybox.

Our Favorite *Recent Posts*

"Knowing how your collector monitors its own performance will help you rest easy at night. A few questions you could ask your vendor regarding its quality assurance process include: 'What percentage of collections calls are reviewed by supervisors or managers?' 'How often are these reviews done?' and … 'What's the process for documenting collections calls, and how do we receive feedback from our members?'"

Brad Young, EVP/AutoPilot services for CUES Supplier member SWBC (*swbc.com*), San Antonio, in "Four Strategies for Tuning Up Your Outsourced Collections Machine" on CUES Skybox: *cumanagement.com/120618skybox*

"Every brand strategy should have consumer awareness at its center. Branding event ATMs is affordable, can create a positive experience for fair and festival goers, and can expose the brand to a large number of consumers at one time in one place. … Members will appreciate being able to perform surcharge-free transactions, and this type of branding can lead to loyal and dedicated accountholders that will turn to the sponsoring credit union for their banking needs."

Yonas Marcos, president/CEO of Star Financial Services (*gowithstar.com*), Elkridge, Maryland, in "Boost Your Brand With Event ATMs" on CUES Skybox: *cumanagement.com/121118skybox*

"Offer excellent mortgage education. Doing so will make or break the member experience. Home financing has changed since most people bought their last one. It's now a more complicated process that often requires more back and forth with the member to get to the closing table. Setting proper expectations will help the member get in the right frame of mind and, believe it or not, that [education] starts long before a member ever comes looking for a mortgage."

Alison Barksdale, AVP/marketing for CU Members Mortgage (*cumembers.com*), Addison, Texas, in "Mortgage Refis Are Dying as the Purchase Market Is Reviving" on CUES Skybox: *cumanagement.com/121218skybox*

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IMPACT OF TAX REFORM

Did you just get hit with the new excise tax?

The Tax Cuts and Jobs Act includes the new Section 4960, which imposes a 21% excise tax (current corporate tax rate) on tax-exempt employers for providing compensation in excess of $1 million, as well as for paying "parachute payments."

How to Minimize or Eliminate the Excise Tax

An existing 457(f) plan can be restructured or changed to a Split Dollar plan to minimize or eliminate the excise tax. The Split Dollar option is particularly attractive because the payments do not count as compensation in the excise tax calculation. Further, Split Dollar plans offer the organization cost and risk mitigation, as well as receive special treatment on the organization's 990 form.

Contact us to schedule an educational session

We'll help determine if your current executive benefit plans are subject to the excise tax and offer recommendations to help lessen potential taxes and other risks.

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