**COMMISSIONER’S COMMENTS**

G. Edward Leary, Commissioner

**FINANCIAL LITERACY – A CHALLENGE FOR ALL**

“Today’s increasingly complex financial services market offers consumers a vast array of products, services, and providers to choose from to meet their financial needs. While this degree of choice provides consumers with a great number of options, it also requires that they be equipped with the information, knowledge, and skills to evaluate their options and identify those that best suit their needs and circumstances. This is especially the case for populations that have traditionally been underserved by our financial system.

Financial education also is essential to help consumers understand how to prevent becoming involved in

**CHIEFLY SPEAKING**

Michael Jones, Chief Examiner

The U.S. Postal Service (USPS) recently sent some information which we wanted to pass on to the institutions we regulate. It concerns USPS-issued money orders. Over the past year, the USPS has seen a growing number of fraudulent money orders presented to financial institutions. In response to this problem, the USPS has established a positive pay system which will enable institutions to verify the authenticity of USPS-issued money orders.

The positive pay system is being implemented in two phases. The first phase, which is available now, is an Interactive Voice Response (IVR) phone system. To access the IVR phone system, institutions can call 1-866-459-7822. The caller will need to provide the 11-digit serial number, 1- to 6-digit dollar amount, and 6-digit post office ID number from the money order. The issue date of the money order needs to be at least 48 hours and not more than 90 days prior to the verification call. With this information, the USPS will either verify that the money order was issued in the dollar amount entered or indicate that it does not match their database of issued money orders.

Only one money order at a time can be verified through the IVR system. However, any number of verifications can be made during a single call. The system will prompt you when to enter the next set of serial number, dollar amount, and post office ID number if an additional verification is needed.

The USPS recommends that the following steps be taken if the money order does not match their database:

1. Double check the numbers and try again. The money order may be outside of the two to 90 day timeframe, it could be the wrong combination of serial number and dollar amount, or it could be fraudulent.

**Inside This Issue**

3 Application Activity Report
5 2006 Legislative Update
7 Toward Better BSA Compliance
8 Commercial Real Estate Lending
10 Revisions to the Report of Condition and Income (Call Report) for Commercial and Industrial Banks
11 E-Banking Update
12 Board of Bank Advisors

continued on page 2 . . .

continued on page 7 . . .
transactions that are financially destructive, how to avoid becoming victims of fraud, and how to exercise their consumer protection rights. Financial literacy can empower consumers to be better shoppers, allowing them to obtain goods and services at lower cost. This optimizes their household budgets, providing more opportunity to consume and save or invest. In addition, comprehensive education can help provide individuals with the financial knowledge necessary to create household budgets, initiate savings plans, manage debt, and make strategic investment decisions for their retirement or their children’s education. Having these basic financial planning skills can help families to meet their near-term obligations and to maximize their longer-term financial well being.”

Forward, The National Strategy for Financial Literacy, issued April 4, 2006, by the Financial Literacy and Education Commission

All of us involved in the financial services industry have a challenge to do all we can to educate our customers, members, or citizens about financial services. An educated consumer is a better consumer. In that light, I wanted to review some actions of the department, the Legislature and Utah’s financial institutions to help people become smarter consumers of financial services. I know that many other actions are occurring that should be acknowledged but there is not enough space here to do so, perhaps, more can be highlighted in a future article. We commend all efforts you are taking.

DEPARTMENT ACTIONS

Section 70C-8-102 of the Utah Code compels the Department to report biennially to the Legislature regarding the need for education programs to promote prudent and beneficial use of credit by consumers and department efforts to promote the education of consumers with respect to credit practices and problems. The Department is also charged with coordinating with representatives of education, government, and the financial services industry and assisting in the preparation of a financial services education curriculum.

The Department commenced consumer education presentations in 1997, since then there have been 584 presentations to 17,300 people. The presentation is entitled “Tips to Avoid Frauds, Scams and High Cost Loans”, and is conducted by financial institution examiners trained in consumer compliance and mortgage issues. One of the examiners that conducts this training is one of two people that normally answers queries and questions in the office.

The vast majority of presentations have been to high school students. The presentations are conducted in a PowerPoint slide program. Copies of the program are left with teachers for future use. The PowerPoint slide program is also available on the Department’s web site. High school groups of particular interest where programs have been conducted include alternative high school programs, young parents, low-income parents and English as a second language. A number of senior citizen groups have also received the presentation.

The Department opened a home page on the Internet in September 1998. One of the subjects presented within the home page is “Consumer Tips” where useful tips, alerts and pitfalls to avoid are identified and explained. The subjects addressed include: auto loans, mortgage loans, fraud alerts, accelerated payment programs, checking accounts - pitfalls to avoid, establishing credit, credit reports, co-maker, co-signer, or guarantor, credit cards, interest rates, debt-to-income ratios.

LEGISLATIVE ACTION

An omnibus education bill known as Senate Bill 154, sponsored by Sen. Hatch was passed during the 2003 legislative session. Included in that bill are provisions that originated with Rep. Hogue in another bill that requires instruction that stresses general financial literacy from basic budgeting to financial investments, including bankruptcy education in the core curriculum beginning no later than the graduating class of 2007.

continued on page 6 . . .
# Application Activity Report
Utah Department of Financial Institutions

*For quarter ending March 31, 2006*

<table>
<thead>
<tr>
<th>Branch Approval</th>
<th>Address</th>
<th>Received</th>
<th>Status</th>
</tr>
</thead>
<tbody>
<tr>
<td>Premier Services Credit Union</td>
<td>outlet shared services of Mountain America Credit Union</td>
<td>1/14/05</td>
<td>Time suspended 1/31/05</td>
</tr>
<tr>
<td>State Bank of Southern Utah</td>
<td>145 S River Rd, St George</td>
<td>2/18/05</td>
<td>Approved 3/10/05</td>
</tr>
<tr>
<td>Bank of American Fork</td>
<td>2691 W 12600 S., Riverton</td>
<td>8/5/05</td>
<td>Approved 8/29/05</td>
</tr>
<tr>
<td>The Village Bank</td>
<td>650 W Telegraph St, St George</td>
<td>9/19/05</td>
<td>Approved 10/17/05</td>
</tr>
<tr>
<td>Centennial Bank</td>
<td>Center Street and Orem Blvd, Orem</td>
<td>9/29/05</td>
<td>Approved 10/17/05</td>
</tr>
<tr>
<td>Centennial Bank</td>
<td>1066 W South Jordan Pkwy, S Jordan</td>
<td>12/12/05</td>
<td>Approved 1/6/06</td>
</tr>
<tr>
<td>SunFirst Bank</td>
<td>1150 W State Hwy 9, Hurricane</td>
<td>10/28/05</td>
<td>Approved 11/29/05</td>
</tr>
<tr>
<td>Weber Credit Union</td>
<td>5300 S Adams, Ogden UT</td>
<td>11/10/05</td>
<td>Approved 11/21/05</td>
</tr>
<tr>
<td>Home Savings Bank</td>
<td>911 E Pioneer Rd, Draper UT</td>
<td>1/11/06</td>
<td>Approved 2/9/06</td>
</tr>
<tr>
<td>SunFirst Bank</td>
<td>800 W 200 N, Cedar City UT</td>
<td>2/10/06</td>
<td>Approved 3/17/06</td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>Relocations</th>
<th>Address</th>
<th>Received</th>
<th>Status</th>
</tr>
</thead>
<tbody>
<tr>
<td>Grand County Credit Union</td>
<td>from 186 W Center St, Moab to 725 N Main, Moab</td>
<td>4/26/05</td>
<td>Opened 1/17/06</td>
</tr>
<tr>
<td>Newspaper Employees CU</td>
<td>from Main Street to 4770 S 5600 W, Kearns</td>
<td>9/30/05</td>
<td>Opened 1/3/06</td>
</tr>
<tr>
<td>SEA Credit Union</td>
<td>from 55 N 300 E, Richfield to 38 W 100 S, Central Valley</td>
<td>2/3/06</td>
<td>Opened 2/24/06</td>
</tr>
<tr>
<td>National J.A.C.L. Credit Union</td>
<td>from 242 S 400 E, SLC to 3776 S Highland Dr, SLC</td>
<td>1/23/06</td>
<td>Opened 3/24/06</td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>Credit Union Mergers</th>
<th>Credit Union merging into Received</th>
<th>Status</th>
</tr>
</thead>
<tbody>
<tr>
<td>WASCO Credit Union</td>
<td>Utah Community Federal CU 11/10/05</td>
<td>Approved 2/13/06</td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>Branch Discontinuance</th>
<th>Credit Union branch location Received</th>
<th>Status</th>
</tr>
</thead>
<tbody>
<tr>
<td>Intermountain Credit Union</td>
<td>7134 S Redwood Rd, SLC 3/16/06</td>
<td>Approved 3/22/06</td>
</tr>
</tbody>
</table>

continued on page 4 . . .
## De Novo Charter

<table>
<thead>
<tr>
<th>De Novo Charter</th>
<th>Address</th>
<th>Accepted</th>
<th>Status</th>
</tr>
</thead>
<tbody>
<tr>
<td>ComData</td>
<td>500 N Market Place Dr. #250</td>
<td>9/25/03</td>
<td>Approved 12/19/03</td>
</tr>
<tr>
<td></td>
<td>Centerville UT</td>
<td>11/19/04</td>
<td>Approved 12/23/04</td>
</tr>
<tr>
<td></td>
<td>Extension</td>
<td>5/27/05</td>
<td>Approved 6/15/05</td>
</tr>
<tr>
<td></td>
<td>Extension</td>
<td>12/6/05</td>
<td>Approved 12/14/05</td>
</tr>
<tr>
<td>Allegiance Direct Bank</td>
<td>136 W Center St</td>
<td>12/1/04</td>
<td>Opened 8/1/05</td>
</tr>
<tr>
<td></td>
<td>Cedar City UT</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Union Financial Services Corp.</td>
<td>181 E 5600 S Ste 240</td>
<td>2/28/05</td>
<td>Approved 5/25/05</td>
</tr>
<tr>
<td></td>
<td>Salt Lake City UT</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Daimler Chrysler</td>
<td>268 S State St, Ste 200</td>
<td>7/6/05</td>
<td></td>
</tr>
<tr>
<td></td>
<td>Salt Lake City UT</td>
<td></td>
<td></td>
</tr>
<tr>
<td>LCA Bank Corporation</td>
<td>5532 Lillehammer Ln, Ste 401</td>
<td>7/22/05</td>
<td>Opened 1/26/06</td>
</tr>
<tr>
<td>(Lease Corporation of America)</td>
<td>Park City UT</td>
<td></td>
<td></td>
</tr>
<tr>
<td>CapitalSource Bank</td>
<td>2817 Canyon View Dr</td>
<td>8/16/05</td>
<td>Approved 12/18/05</td>
</tr>
<tr>
<td></td>
<td>Salt Lake City UT</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Marlin Business Bank</td>
<td>2795 E Cottonwood Pkwy Ste 120</td>
<td>1/10/06</td>
<td></td>
</tr>
<tr>
<td></td>
<td>Salt Lake City UT</td>
<td></td>
<td></td>
</tr>
<tr>
<td>American Pioneer Bank</td>
<td>39 Jamestowne Ct</td>
<td>2/13/06</td>
<td></td>
</tr>
<tr>
<td></td>
<td>Baton Rouge LA</td>
<td></td>
<td></td>
</tr>
</tbody>
</table>

## Loan Production Office

<table>
<thead>
<tr>
<th>Loan Production Office</th>
<th>Received</th>
<th>Status</th>
</tr>
</thead>
<tbody>
<tr>
<td>First Utah Bank</td>
<td>11/15/05</td>
<td>Opened 2/1/06</td>
</tr>
<tr>
<td>First Utah Bank</td>
<td>11/15/05</td>
<td>Opened 1/2/06</td>
</tr>
<tr>
<td>Community South Bank</td>
<td>11/4/05</td>
<td>Opened 1/17/06</td>
</tr>
<tr>
<td>America West Bank</td>
<td>11/23/05</td>
<td>Opened 1/2/06</td>
</tr>
<tr>
<td>America West Bank</td>
<td>12/21/05</td>
<td>Opened 1/2/06</td>
</tr>
<tr>
<td>Franklin Bank SSB</td>
<td>12/19/05</td>
<td>Opened 2/1/06</td>
</tr>
<tr>
<td>First Utah Bank</td>
<td>3/6/06</td>
<td>Opened 3/20/06</td>
</tr>
<tr>
<td>America West Bank LC</td>
<td>3/17/06</td>
<td>Approved 3/22/06</td>
</tr>
</tbody>
</table>
2006 LEGISLATIVE UPDATE
Paul Allred, Deputy Commissioner

The 2006 Utah Legislature passed 395 bills during the General Session. In this article, the Department’s annual legislative review, eight bills will be highlighted. Each of these bills will impact financial institutions and other entities under the jurisdiction of the Department of Financial Institutions.

S. B. 116 - Financial Institutions Fee Increase
The Department operates entirely from fees set in statute at Section 7-1-401. Financial institutions subject to the Department’s jurisdiction pay fees into a Restricted Fund. Fees have not been increased since 1992. In fact in 1997 and again in 2001, the Department reduced its fees. The reserve in the Restricted Fund has been reduced to the point it was necessary to request a fee increase. Senate Bill 116 amends the fee schedule set forth in Section 7-1-401. The bill had the support of the financial institutions under the Department’s jurisdiction.

S.B. 123 - Utah Consumer Credit Code Amendments
Senate Bill 123 amends two provisions in the Utah Consumer Credit Code (UCCC). The first amendment exempts nonfederal guaranteed student loans from the UCCC. The second amendment modifies the notice requirements for change of terms to open-end contracts from 30 days to 15 days. These amendments are consistent with federal law.

S.B. 162 - Department of Financial Institutions Enforcement of Applicable Law
Senate Bill 162 clarifies that persons under the Department’s jurisdiction that violate applicable federal law are in violation of the Titles 7, 70C and 70D.

H.B. 127 - Limited Liability Company Amendments
Senate Bill 127 establishes series Limited Liability Company within the Limited Liability Company Act.

H.B. 430 - Department of Financial Institutions Pay Plan
The financial institutions industry asked Rep. Alexander to sponsor this bill. Senate Bill 430 directs the State Department of Human Resource Management to use market comparability surveys for examiner positions with federal agencies to establish commensurate pay scales for our state examiners.

S.B. 252 - Consumer Credit Code Amendments
Senate Bill 252 imposes requirements on the waiver of class action rights related to closed-end and open-end consumer credit contracts. It also modifies provisions related to changing an open-end consumer credit contract.

S.B. 69 - Protection of Information in Consumer Credit Databases
This bill takes effect on January 1, 2007. The bill requires any person who maintains personal information to maintain procedures to prevent unlawful disclosure or misuse and destroy records that are not necessary to be retained. In addition, if the person becomes aware of a breach, they must investigate the likelihood of it being misused. If it can be misused, notice must be provided to Utah residents. Financial Institutions are exempt from the destruction of records section. Finally, the Utah Attorney General may enforce the law and a person who violates the new law is subject to a civil fine of $2,500.

S.B. 71 - Consumer Credit Protection
This bill allows a consumer to place a security freeze on their credit report by making a written request and paying a fee. The freeze must go into effect within five business days. The consumer reporting agency must provide a pin or password for temporary removal of the security freeze. If the request for temporary removal is made in writing and mailed, it must be removed in three days. If the request is made through electronic contact, it must be removed in 15 minutes. The consumer reporting agency may charge a reasonable fee for the temporary removal unless the consumer is the victim of identity theft and the consumer has provided a copy of the police report or case number. The Utah Attorney General may enforce the law and a person who violates the new law is subject to a civil fine of $2,500. Finally, the bill takes effect on September 1, 2008.
Pursuant to the legislation, the Utah State Board of Education developed a curriculum designed to help Utah’s youth prepare for the choices and challenges of today’s financial markets. A better understanding of personal finance will help students move into adulthood making more informed monetary decisions, realizing a greater potential for personal wealth, and fostering a stronger state and national economy.

The core course for Utah high schools is the “General Financial Literacy Course” designed for Grades 11-12. The course includes sections on: Income, Money Management, Spending and Credit, Saving and Investing, Consumer Protection and Risk Management. It has four standards which cover decision making and goals, income and careers, principles of money management, and savings, investing, and retirement planning. It will be implemented with the graduating class of 2008.

More information about the General Financial Literacy Course can be found at: www.uen.org/financial_lit/

FINANCIAL INSTITUTIONS ACTIONS

Jump$tart Coalition for Personal Financial Literacy is a statewide, all volunteer, 501(c)(3) non-profit organization dedicated to improving the financial literacy of Utah’s youth. Consisting of individuals and organizations, the coalition brings together leaders from business, government, and education. Its mission is to improve the financial literacy of Utah youth by promoting the teaching of personal finance in kindergarten through college. The Coalition believes that all youth must have the financial literacy necessary to make informed financial decisions. There are representatives on the Jump$Start Board from both the Utah Bankers Association and the Utah League of Credit Unions. The Department also has a representative on the Board, currently serving as Treasurer. The national group was formed in 1995 and the Utah Coalition was formed in 2000.

More information about Utah Jump$Start can be found at: www.utjumpstart.org

Junior Achievement (JA) is a national organization with the goal of teaching kids about personal finance. JA offers teaching materials for children of all ages, from elementary to high school. They seek to expose school children to topics such as supply and demand, credit cards and checking accounts, and various types of loans. Many financial services people are involved in using this program to teach kids in school. Nationally, JA uses volunteers, educators, parents, and contributors who reach out to more than four million students, each year, in grades K-12.

National Endowment for Financial Education (NEFE) is a nonprofit corporation offering a free basic financial planning curriculum, and Utah’s education office encourages schools to use it where applicable. Many bankers and credit union employees participate in NEFE on a year-round basis.

The Utah League of Credit Unions has commenced an outreach program aimed at helping credit unions across the state better serve Latinos. The program, titled “Poder Economico” translates to “Economic Power Project.” In an effort to build trust and reach this growing segment of Utah’s population, Utah credit unions have recently started hosting workshops to reach this community and overcome Latinos’ distrust of financial institutions. The Utah League of Credit Unions is partnering with community leaders, the Mexican Consulate, Univision - a Spanish language TV station, and the Governor’s Office on Hispanic Affairs to offer financial education to the Latino community.

For years, the Utah Bankers Association has sent representatives of the banking community into classrooms to teach the course “Your Bank and You.” While that effort has continued, the Consumer Education Committee has reviewed the course to update it, including the addition of chapters about Internet Banking, Credit, Savings, Investing and Budgeting. The objectives of the program are to introduce high school students to banks and the services they offer, provide students with a foundation for making sound financial decisions and to encourage financial responsibility. Components of the program include videos, worksheets, transparencies and checkbook kits, supplied free of charge to schools. The program is a one-week banking course endorsed by the Utah State Office of Education. The program uses “hands on” banking experience through writing and recording checks, reconciling a bank statement, figuring the cost of credit and setting financial goals. Each year the program is presented to more than 5,000 students in approximately 50% of the schools, utilizing more than 100 bankers as instructors.
2. Check the Security Features of the money order. Publication Notice 299, which highlights the security features of USPS’ money orders, may be downloaded from the Internet, at: http://www.usps.com/missingmoneyorders/security.htm.

3. Follow the system prompts to speak with a help desk representative for additional verification.

4. Refuse to cash the money order for the customer.

5. If possible, confiscate the money order from the customer and provide them with a copy or receipt of the money order. If the customer does not wish to relinquish the money order, suggest that they take it to the local Postmaster and let them know that the money order could be fraudulent.

6. Call the USPS Inspection Service fraud hotline at 1-800-372-8347 (Monday-Friday) or contact your local Inspection Service office. You can locate your nearest Postal Inspector from the Internet, at: http://www.usps.com/ncsc/locators/find-is.html. You will need to provide the money order details and the customer’s contact information to the Inspection Service.

The second phase of USPS’ positive pay system will allow batch computer lookups for verification of more than twenty money orders at one time. The USPS will provide more information on this phase as it becomes available. Updates will be posted on the Internet at: http://www.usps.com/missingmoneyorders/security.htm.

If you have questions about accepting Postal Money Orders, call your nearest U.S. Postal Inspection Service Office or Post Office. Call the fraud hotline at 1-800-372-8347 (Monday-Friday) or visit www.usps.com/postalinspectors for additional information.

---

**Toward Better BSA Compliance**

Orla Beth Peck, Supervisor of Credit Unions

Recently the Department hosted three sessions of training on the Bank Secrecy Act (BSA), the USA Patriot Act, and OFAC. Two sessions were designed for credit union BSA officers and the other for examiners and other auditors who review BSA compliance.

Although these regulations have been in existence for many years, the USA Patriot Act for 5 years, BSA for 20, and OFAC since 1812; they are complicated and highly technical. Opportunities for training have been hard to come by, especially for small credit unions.

The training was taught by Ann Gregson, the Department’s BSA compliance specialist. She covered the basics on these three Acts including the history and purpose of the laws. She also illustrated the four pillars that are required to be in compliance with the law. These are:

1) Designate an individual who is responsible for compliance with BSA, USA Patriot Act, and OFAC.
2) Establish a system of internal controls sufficient to ensure compliance.
3) Hold and document annual training of all appropriate staff
4) Independent transaction testing. This test should be extensive enough to determine not only that the CTRs and SARs that were filed were appropriate; but that CTRs and SARs were filed in all cases where necessary.

This was a train-the-trainer class, and a manual containing information, training materials, and sources of additional information was provided for the attendees to take back to their credit unions.

It is the Department’s desire that whenever possible we provide help to the institutions under our jurisdiction to comply with laws and regulations, rather than just criticism when they don’t.
COMMERCIAL REAL ESTATE LENDING

Proposed Interagency Guidance

Early this year federal bank and thrift regulatory agencies sought comment on proposed interagency guidance relating to sound risk-management practices for concentrations in commercial real estate (CRE) lending. Following is response by the Conference of State Bank Supervisors (CSBS) to the proposed guidance, submitted March 24, 2006. The Utah Department of Financial Institutions is a member of CSBS, and Commissioner Leary, Deputy Commissioner Allred, and Supervisors Rude and Bay contributed input and support to this comment.

State regulators are strong advocates for a safe and sound banking system that serves and protects the residents of our states and meets the economic development needs of local communities. We recognize the risks that concentrations in commercial real estate can pose and the importance of banks exercising strong risk management practices utilizing appropriate analytic and monitoring tools. We have, however, several concerns regarding the proposal. These are:

• The proposed guidance does not recognize that risk varies among CRE sub-markets.
• The proposed guidance would place an especially heavy burden on community banks.
• The proposed guidance could impair banking industry competitiveness in commercial real estate lending.
• Supervisory tools already exist, and are being used to deal with unsafe banking practices, such as unsound concentrations, in any line of bank business.

The commercial real estate market is not homogeneous. There are a multitude of sub-markets within the CRE category that are characterized by varying levels of risk. We note that the proposed guidance does not differentiate among the assorted-risk sub-markets in the CRE sector. It is important to recognize that many bank lenders exercise risk mitigation procedures by limiting their involvement in higher risk aspects of the CRE market, and by placing limitations such as lending limits on construction and development lenders, imposing individual builder limits, placing aggregate limits on certain types of lending, and imposing cash flow and other financial requirements on borrowers.

We are concerned with the unnecessary burden several of the requirements in the guidance will place on all institutions, but especially community banks. The guidance will require institutions to:

1. Perform an analysis of the potential effect of a downturn in real estate markets on both earnings and capital;
2. Develop internal rating systems that consider an assessment of a borrower’s creditworthiness and of an exposure’s estimated loss severity to ensure that both the risk of the obligor and the transaction are clearly evaluated; and
3. “Measure and control CRE credit risk on a portfolio basis by ... performing market analysis and stress testing.”

These requirements will demand significant resources to produce and will be of little value to community banks. We note, again, that many institutions mitigate risk by lending in the less risky segments of the CRE market. In addition, the guidance fails to recognize perhaps the greatest risk mitigation tool available to community banks—the proximity of the lender to the borrower. These institutions, by their very nature, are closer to the economic realities of their markets and the credit worthiness of their borrowers. We must recognize that risk monitoring tools deemed valuable and reasonable for the larger institutions may not be feasible, valuable, or necessary for the smaller organizations.

The guidance also calls for banks to “compare the institution’s underwriting standards for individual property types with those that exist in the secondary market.” Institutions with standards which are “substantially more lenient” will be required to provide justification and document long-term plans for their credits. The secondary market plays a vital role for banks to mitigate risk and provide liquidity. However, we believe this homogeneous approach to commercial real estate credit limits lender judgment, diminishes the real value of a community banker, and will negatively impact the economic opportunities of small businesses and their communities.

continued on page 9 . . .
We believe the proposed guidance will lead banks to determine they have little choice but to rethink the manner in which they serve their communities. Regulatory guidance should not chase banks from a business line where they understand the market and risks, to a business line in which they lack expertise. Diversion of bank resources into other lines could have significant negative effects on competition in even the lowest-risk segments of the CRE market and on the availability of CRE credit in local markets.

The current interagency guidelines for real estate lending (FDIC, Part 365) set an aggregate limit on CRE lending that exceeds supervisory loan-to-value ratios to no more than 30% of total capital. Institutions approaching this limit will receive “increased supervisory scrutiny.” The guidelines outline the general supervisory review to include:

- The nature and scope of the institution’s real estate lending activities.
- The size and financial condition of the institution.
- The quality of the institution’s management and internal controls.
- The expertise and size of the lending and loan administration staff.
- Market conditions.

The current approach allows management flexibility and supervisory judgment based on actual conditions.

Supervisory tools are already available and actively used by regulators to deal effectively with unsafe practices and unsound concentrations in commercial real estate lending. State regulators report participating recently with federal regulators on joint examinations at institutions showing high CRE concentrations. In virtually all cases, either risk management practices were deemed sufficient or corrective action was implemented in a timely manner.

We note, as well, that pilot projects conducted by federal regulatory agencies to review observed CRE concentrations in several metro areas around the country disclosed that, by-and-large, institutions are utilizing appropriate risk mitigation techniques in CRE portfolios. These findings have been well publicized in FDIC publications.

It is appropriate to raise the awareness of risk in commercial real estate and to point out increasing levels of concentration. In doing so, however, we should not be overly or broadly prescriptive in how this risk is managed. We must also consider the shuttering effect such a regulatory pronouncement will have on bankers, small businesses and local economic development. We must have confidence in our supervisory processes and the enforcement powers already available and utilized by state and federal regulators.

POSTSCRIPT:

In remarks at the America’s Community Bankers Risk Management and Finance Forum in Naples, Florida on April 10, 2006, Fed Governor Susan Schmidt Bies made the following comment.

“...we have received hundreds of comment letters on the proposed guidance so far... I would...like to mention up front that the proposed guidance is not intended to cap or restrict banks’ participation in the CRE sector, but rather to remind institutions that proper risk management and appropriate capital are essential elements of a sound CRE lending strategy. In fact, many institutions already have both of these elements in place.”~
Revisions to the Reports of Condition and Income (Call Report) for Commercial and Industrial Banks

The Federal Financial Institutions Examination Council (FFIEC) has approved revisions to the reporting requirements for the Reports of Condition and Income (Call Report). As outlined below, the revision of existing items and the addition of new items will be spread over the period from March 31, 2006, through March 31, 2008.

1) Changes that took effect March 31, 2006, included eliminating for some or all banks existing items for estimated uninsured deposits, asset-backed securities held as investments, income from nontrading derivatives, and bankers acceptances; adding items for life insurance assets, types of credit derivatives, remaining maturities of credit derivatives, and certain foreclosed properties; and revising the reporting of income from international operations.

2) Revised signature and attestation requirements will take effect September 30, 2006. The chief financial officer (or the individual performing an equivalent function) must sign the Call Report. This officer's attestation statement would not assert that the chief financial officer is responsible for establishing and maintaining adequate internal control over financial reporting. However, consistent with longstanding agency policies, a general statement that the bank's board of directors and senior management are responsible for establishing and maintaining an effective system of internal control, including controls over the Call Report, will precede the attestations.

3) In addition, as of September 30, 2006, items pertaining to Federal Home Loan Bank advances and other borrowings, nonaccrual assets, certain secured borrowings, residential mortgage banking activities, and certain amounts payable and receivable on credit derivatives will be added or revised.

4) Effective March 31, 2007, revisions will be made to the reporting of lease financing receivables; income from annuity sales, investment banking, brokerage, and underwriting; and trading revenues by type of exposure. On that report date, new items will also be added for residential mortgage banking revenues and net gains (losses) on certain credit derivatives.

5) Finally, beginning March 31, 2007, banks with $300 million or more in assets and certain banks with less than $300 million in assets will report two-way breakdowns of their real estate construction loans and their nonfarm nonresidential real estate loans in a number of Call Report schedules. All other banks with less than $300 million in assets will begin to provide these loan breakdowns as of March 31, 2008.


For the March 31, 2006, report date, banks were allowed to provide reasonable estimates for any new or revised item for which the requested information was not readily available. This same policy on the use of reasonable estimates will apply to the reporting of new or revised items when they are first implemented at subsequent report dates in 2006, 2007, and 2008.

For further information or assistance, state member banks should contact their Federal Reserve District Bank. National banks and FDIC-supervised banks should telephone the FDIC's Data Collection and Analysis Section in Washington, D.C., by telephone at (800) 688 FDIC (3342), Monday through Friday between 8:00 a.m. and 5:00 p.m., Eastern Time, or by e-mail at insurance-research@fdic.gov.
E-Banking Update  
Shaun Berrett, Senior Examiner

In October 2005, the Federal Financial Institutions Examination Council (FFIEC) released new guidance affecting financial institutions that offer certain banking services over the Internet. This guidance was communicated to banks in FDIC FIL-103-2005 and to credit unions in NCUA letter 05-CU-18 (issued in November). Because this guidance imposes approaching deadlines for implementing new requirements for Internet banking, the Department thought it worthwhile to remind the institutions under our jurisdiction of these new requirements.

The guidance is entitled Authentication in an Internet Banking Environment. “Authentication” is the means by which customers identify themselves to your institution’s Internet-based systems. Typically, this has been done through a sign on-ID (e.g., user name, account number) and password.

New Requirements:

1) The guidance states that use of single-factor authentication alone is unacceptable for high risk transactions conducted over Internet banking systems. A “factor” is (1) something a user knows (e.g., password, PIN, shared secrets), (2) something a user has (e.g., ATM card, smart card, USB token), or (3) something a user is (e.g., biometric characteristics, like a fingerprint). Most commercially available Internet banking platforms have relied on single-factor authentication by only requiring users to provide something they know, traditionally, a user name and password.

2) Institutions are required to perform a risk assessment of their Internet platforms to identify all “high risk transactions.” The guidance defines high risk transactions as anything that grants access to sensitive customer information, or allows the movement of funds to another party.

3) Institutions should then deploy an authentication technology based on the results of their risk assessment. High risk transactions should be mitigated through the use of multifactor authentication, layered security, or other controls.

Further guidance may be issued in the future. For now, indications are that the agencies will consider bill payment as a “movement of funds to third parties,” thus qualifying bill payment as a high risk transaction. The agencies have also suggested that customers cannot “opt out” of a stronger authentication requirement.

Compliance:

The guidance requires compliance by year-end 2006. Most Utah institutions have their Internet banking platforms supplied by a third party vendor. Vendors have been made aware of the guidance and recent press releases suggest that the largest, national providers are working on solutions. Some already have compliance solutions available. While vendors may implement specific solutions for their own product lines, local management is still responsible for ensuring their institution complies with the guidance in a timely manner. A solution may be available from your provider, but unless you request it, your institution may not be putting forth a good faith effort to comply.

The Department encourages management teams to plan ahead for compliance. Management teams should become familiar with the guidance, conduct the risk assessment as soon as possible, and, where applicable, contact their vendors to discuss the status of an appropriate authentication solution that meets the needs identified in the risk assessment.
Board of Bank Advisors
Tom Bay – Supervisor of Banks

The Board of Bank Advisors was formed and started meeting in 2001. It is made up of five members of the banking industry appointed by the Governor according to Utah Code 7-3-40. The meeting is a forum to bring together bankers, the Commissioner, and others in the Department to discuss topics and issues of interest, and to voice industry concerns.

The Board meets quarterly. The meetings are open to the public, and we invite all bank representatives to attend.

Topics and discussion items from past meetings include:

- Bankruptcy Law – how the recently enacted changes will affect Utah banks.
- Public Funds – changes to the Money Management Act rules for calculating the maximum public funds allotment.
- Loan Loss Reserve – a review of FAS 114 and FAS 5, and what regulators expect to see with regard to impairment analyses and reserve methodology.
- Commercial Real Estate – how banks can mitigate CRE concentration exposure.
- BSA and Anti-Money Laundering – a regulatory perspective and update, and what examiners will be looking for in an AML program.
- Mortgage Fraud – what banks are seeing, and how they are protecting themselves.
- Appraisals – regulations and related guidance, and what examiners are seeing as common concerns.
- Information Technology – authentication in an internet banking environment, and common IT recommendations and findings from recent examinations.
- Mortgage Lending – oversight and issues.
- Loan Review Process – the need for independence from the lending function.
- Legislative updates – new legislation that will affect banks.

The next meeting is tentatively scheduled for July 18th at 1PM. The location will be the Department of Financial Institutions, 324 South State, Suite 201, Salt Lake City. The meetings last about 1 ½ - 2 hours. If you are interested in attending, please call the Department at 801-538-8830 to verify the date and time.

On the Web . . .

An electronic version of the Networth News including past issues is available on the Department’s website.

The website is located at:

www.dfi.utah.gov

Networth News is a publication of The Utah Department of Financial Institutions

Please contact the Department at 801-538-8830 with questions, comments or suggestions.