The Balancing Act of Risk Mitigation — With an Eye on Today's Economy

State National prides itself on being a risk mitigation partner for hundreds of financial institutions across the country. We conducted these interviews on risk mitigation strategies as part of our ongoing commitment to support our partners with meaningful insights that will help them better manage their business.

For credit unions, maintaining superior customer and borrower relationships is a vital priority. Just as critical for the ultimate success of any financial institution is prudent management of internal and external risk. Risk mitigation management positions are perhaps some of the least visible among the roles of executive management at a financial institution, but like the Wizard behind the curtain, they are perhaps one of the most important in terms of striking balance between what is right for the financial institution and what provides a great experience for the customer.

Balancing these two priorities is a constant challenge. When you throw economic uncertainty and political volatility into the mix, that tightrope can seem even narrower.

Pre-Recession Indicators:

America's last recession ended in June 2009, and that in itself is an indicator that a recessionary period is likely on the horizon at some point, whether sooner or later. A few of the factors risk mitigation specialists are keeping an eye on are:

- **Yield curve margins**
- **Housing prices**
- **Economic growth spurred by trade relations vs. possible slowdowns caused by adversarial trade relationships**
- **Unemployment rates**
- **Increasing auto prices and lengthening loan terms, with more negative equity**

Comparing and Contrasting 2007-2009 and 2019

The Great Recession that began in 2007 was in full swing ten years ago and took some lenders by surprise, generating catastrophic losses for some institutions. We sat down with several risk specialists from credit unions across the country to ask what they see as some of the similarities between then and now, as well as any differences they notice.

Dave Brydun
VP of Consumer Lending, BCU, Vernon Hills, IL:

“Our loan-to-share is pretty similar now to where it was 12 years ago, before the last recession began in 2007, and unemployment is low, similar to that period. We’re seeing a pretty good economy in terms of the forecasts. Obviously, in lending having a low unemployment rate and strong consumer spending are two good things, and those are still flashing green right now. **I guess the question is, ‘Well, that’s the current state, but will what’s going on behind the scenes with the manufacturing slowdown and tariffs and other various factors eventually start impacting consumer spending and employment?’**”

Henry Robaszewski
Director of Risk Management, Finance
BCU, Vernon Hills, IL:

“We usually see all the indicators peak just before a recession starts. Like Dave said, everything’s looking good right now, but it did right before the last recession, too. So, everyone’s looking for that early indicator of ‘When is it going to turn?’ **We’ve been looking at the yield curve, because the inversion has been an indicator of recessions in the past.** There has been some inversion this time, but it hasn’t necessarily persisted, so we’re waiting to see if that does manifest itself ... the Fed is starting to ease in trying to prevent that from happening. Whether they’ll ease quickly enough to prevent a recession or not remains to be seen.”

Dave Brydun:

“We’ve been talking about recession readiness now for probably two or three years and we’re still here in 2019 and it’s yet to hit. **So, for us it’s just coming up with a readiness framework so that when the indicators start flashing in a direction other than they are today, we have a plan in place that we can activate.**”

Eric Fuglister
VP Consumer Lending
Wings CU, Apple Valley, MN:

“Twelve years ago, we knew the craziness that was mainly going on in the mortgage market couldn’t last forever ... home prices were going up unbelievable amounts every year — 10% or more each year. You had borrowers who really didn’t qualify for loans — whether their credit scores were low or they were the no-documentation, stated-income loans — all that stuff was pretty prevalent toward the end of the decade, from 2006 on. It had the signs that this stuff just can’t last forever. **I don’t think any of us thought it was going to unwind the way it did in terms of the severity and how it affected not only the U.S. economy, but even the world economy.** Back then, I remember thinking for a couple of years that real estate and mortgages can’t keep doing what they’re doing. And they did and they did ... and then finally, it all eventually broke and we obviously know what happened after that.”

Henry Robaszewski:

“To me, now it looks more like a growth slowdown as opposed to a collapse of the housing industry like we saw 12 years ago, so hopefully any recession that happens won’t be as severe once it does and the impact won’t be as great. **I think we’ve seen some potential pre-recession indicators, but I don’t know that we’ve seen the run-up in real estate prices that we did back in 2007.** There has been some run-up in some regional areas, but I don’t think it’s been as widespread and I don’t think there’s the same lending practices in terms of no-documentation loans and things like that that were more risky. So it’s probably unlikely that the same scenario would play out again.”

Dave Brydun:

“The last recession, the worst since the Great Depression, was primarily a real estate recession. **And that was really brought on, in the years leading up to it, by much looser underwriting standards within the industry that have since been corrected.** So hopefully, in terms of lenders and the lending environment, the recession isn’t as severe, because real estate loans are very high-dollar loans and the impact on a financial institution’s financials can be pretty severe if there is a greater deal of degree of losses that are concentrating in real estate versus other products.

“I think I tend to call it more ‘credit renormalization.’ Delinquencies and charge-offs probably bottomed out in terms of being really low, probably in 2015, 2016, and they have come up a little bit industry-wide, but I think we are and can probably continue to be in a very benign credit risk environment. For us, we just see credit renormalization and not so much anything that we’re largely concerned with. We keep our eyes on things, but I think this may be more normalization than any sort of indication that things will start heading south in any large way.”

Deborah McRae
VP Risk Management, Five Star CU, Dothan, AL:

“We opened three new branches during the first part of this year, which is a record for us — we’ve opened two in one year, but never three. **So from our point of view, clearly we thought things were going really well and I think we still feel that way.**”

The current consensus among the risk professionals we interviewed seems to be that while they are preparing carefully for a possible future recession, conditions as of right now have not yet warranted any drastic changes in their lending practices.

Perhaps even more importantly, they all agree that lending practices related to housing are drastically different now than they were in the late 2000s, which is a significant factor in their opinions when it comes to conditions surrounding the Great Recession and conditions today.

In our next article in this series, we’ll talk about what these professionals do to keep a pulse on economic conditions and which indicators they monitor to be sure they have adequate resources in place to protect their institutions from risk.

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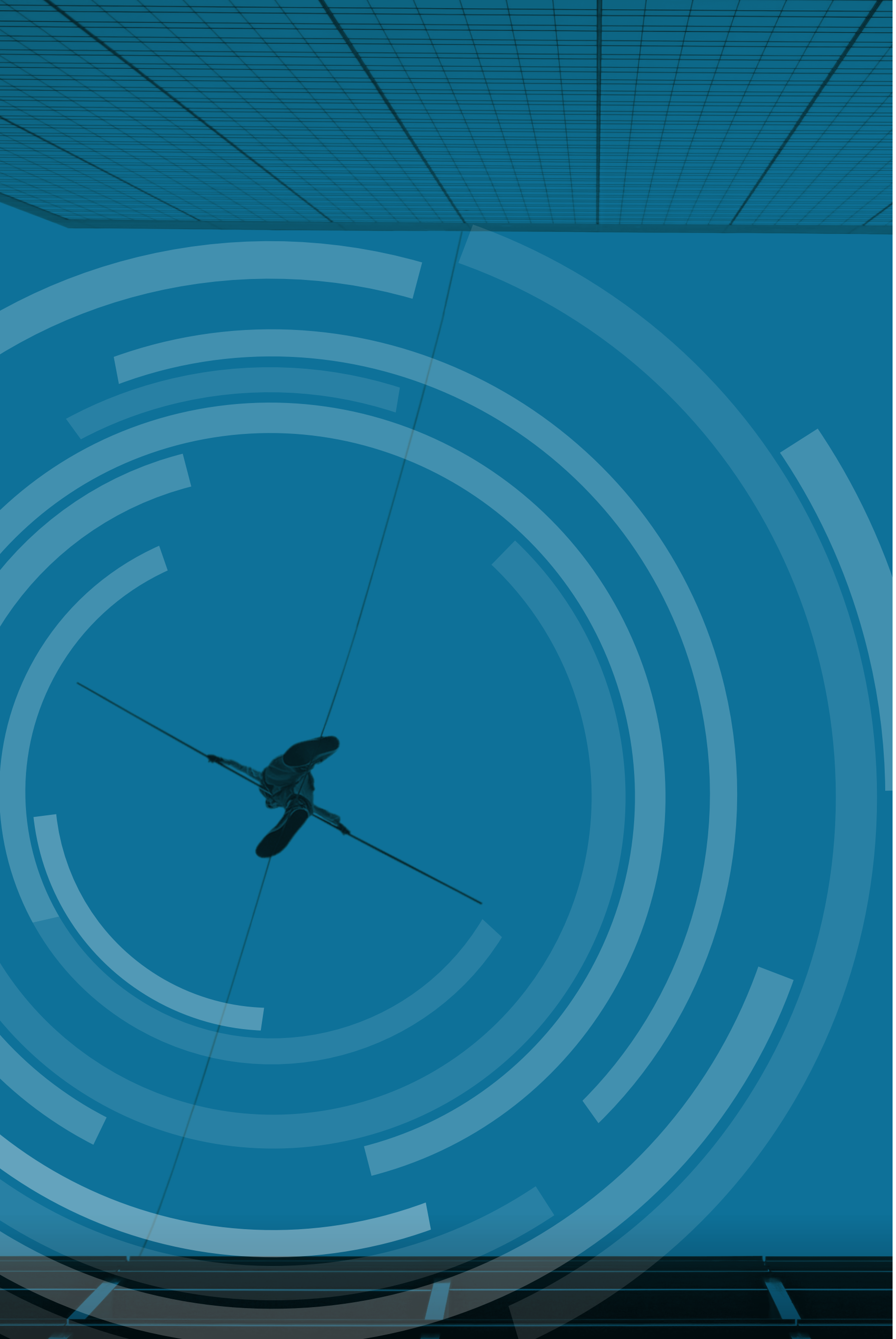

Credit unions have a two-fold mission — providing for the needs of their customers in terms of customer experience and access to financial products and services, and also protecting the institution so that it can remain profitable, grow, and be there in the long-term for future members.

The Many Faces of Risk

The sources of risk in financial institutions are plentiful, but certain areas spring to mind readily when thinking about the risks any financial institution faces:

Economic Risks:

- **Consumer Confidence**
- **Unemployment Rate**
- **Yield-Curve Performance**
- **Housing Market Performance**

Political Conditions:

- **U.S. Trade Relations**
- **Tariffs**
- **Public Opinion**
- **Media Influences**

Financial Assessments:

- **Loan-to-Value Ratios**
- **Collateral Protection/Loan Security**
- **Deposit Balances/Share Growth**
- **Delinquencies and Charge-Offs**
- **Fluctuating Interest Rates on Both Deposit Accounts and Loans**

In addition, there are some risks that may not be as obvious, but can be just as impactful in their effects. State National discussed a few of these myriad areas of risk that a credit union faces with a group of risk mitigation professionals.

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DATA INTEGRITY AND SECURITY

Dave Brydun

VP Consumer Lending, BCU, Vernon Hills, IL

"Over the past few years, we've increased the percentage of loans (auto loans, credit cards, unsecured loans) that are automatically decisioned, vs. manually decisioned by an underwriter, to roughly 60%. The next frontier for us in terms of growing this percentage entails the use of "on-us" data and incorporating it into our system decisioning. Having strong data quality within our organization enables this opportunity but also presents risk if the data isn't managed properly."

Henry Robaszewski

Director of Risk Management/Finance, BCU, Vernon Hills, IL

"This area of data quality also relates to CECL, the new loss allocation model for loan losses that FASBI has required to be implemented in a few years. Adoption hasn't taken place yet, but eventually all financial institutions will have to comply with that, so it is causing us to take a look again at the data, all the past history, and what it could mean for the future."

Eric Fuglister,

VP Consumer Lending, Wings CU, Apple Valley, WI

"Data security is obviously a huge risk. Especially with the Equifax data breach a couple of years ago — I think that should have shocked every financial institution down to its core. Every financial institution has a lot of sensitive information and you sure wouldn't want to have something like that happen. So your investment in data security and keeping on top of that is a huge deal."

COMPLIANCE OMISSIONS

Deborah McRae,

VP Risk Management, Five Star CU, Dothan, AL

"Failure to give disclosures on new accounts can definitely be a source of risk, and in lending, if you fail to disclose certain things in advance of a real estate loan, you've got issues. Whether in account opening or consumer loans there are so many disclosures we deal with, and the failure to do any one of those could get you into trouble because we're in such a litigious environment, where everybody wants to get together and have class action suits for everything."

TECHNOLOGICAL COMPETITION

Eric Fuglister

"One good reason to automate as many of your loan decisions as possible is the risk of competition. Each member, while they might be a member of your credit union, might also use a number of other institutions or have other financial relationships. So when a potential borrower is auto shopping, for example, when they apply you need to be able to get them their decisions as quickly as possible. Because if you don't, you're at a competitive disadvantage — gone are the days of, 'hey, submit an application, we'll get back to you in two business days.' Now you need to get them a decision right away because otherwise they're just going to walk across the street to someone else."

EVERYDAY OPERATIONAL/PHYSICAL RISK

Deborah McRae

"From janitorial or other staff as well as your members, every time you open the doors you've got the possibility of somebody slipping and falling and suing over a frayed carpet or a wrinkled up rug at the door. You might not think of that when you're talking about risk mitigation, but it is one of the many areas of which we should be aware."

HIRING, STAFFING, AND TURNOVER

Eric Fuglister

"Trying to hire, especially for entry-level positons, has become extremely tough and competitive, both on pay and what you have to offer in benefits. Getting people in the door has been tough. You schedule interviews and people don't show up, or you make offers and they accept and then they don't show up for the first day of work — this is not just at Wings, I think everyone has seen a lot more of that. And then when you're not fully staffed, your other employees are having to pick up the workload and you have staff burnout."

Deborah McRae

"Sometimes training can be a challenge, making sure staff is trained to watch for red flags of potential fraud. And if you're having a lot of turnover, it can feel like you never really get anybody trained before they're gone again, before they get past the basics of how to make a deposit or withdrawal and move up to the level of developing relationships with members so they can provide the proper products and services based on each memer's needs. That not only lessens the member experience, it means passing up income opportunities, which is a profitability risk."

WEATHER AND NATURAL DISASTERS

Deborah McRae

"Last year Hurricane Michael came onshore near Panama City Beach at Mexico Beach, moved into Georgia, and then made an easterly turn and went straight across the state. We had six branches damaged by that one hurricane. We had members who are also farmers who suffered financially due to damaged farmland. We just charged off approximately $200,000 because one farmer lost his crops the last two years due to weather. We did dozens of modifications on mortgages and extensions on loans after the hurricane. That's a situation where we, as a credit union, need to take on that risk, because that's our job — being there to help when our members need us."

VEHICLE VALUES AND EXTENDED LOAN TERMS

Dave Brydun

"Financial institutions are certainly taking on additional risk by originating auto loans with extended terms. Over the past few years, the percentage of auto loans with terms beyond 72 months has grown quite a bit. While we don't originate much volume above 75 months, for the small portion that we do, we make sure additional rate premiums are in place to ensure that we are being compensated for the additional risk. So, yes, even though it's a risk, in the end it's how the financial institution or credit union prices for the risk that's most important."

Eric Fuglister

"Yes, I think the average price of new vehicles now is well into the mid-30s, and it's not uncommon to have new vehicles well over $50,000. People are leasing or extending the terms to keep the payment down. Some financial institutions have even started going to 96 months to keep the payment manageable for the member or the customer. God forbid something happens and they total that vehicle or have something happen — all of a sudden they could be staring at a lot of negative equity. GAP claims have continued to rise because if someone does total their vehicle that deficiency balance on their insurance is getting to be larger and larger. It's not uncommon to have negative deficiency of $5,000, $10,000, even $15,000. And if someone doesn't have GAP it's a large enough number that they might have to structure a personal loan and maybe they can't really afford it. It has definitely created some issues in the auto lending world."

A comment from one of our interviewees summed up just how many areas of exposure a financial institution faces each and every day. When asked which parts of her business face risk, Deborah McRae said, "I can't think of one that doesn't! I don't know that there's any area that doesn't have risk."

Special thanks to Dave Brydun and Henry Robaszewski from BCU in Vernon Hills, IL; Eric Fuglister from Wings CU in Apple Valley, MN: and Deborah McRae from Five Star CU in Dothan, AL for generously sharing their time and expertise.

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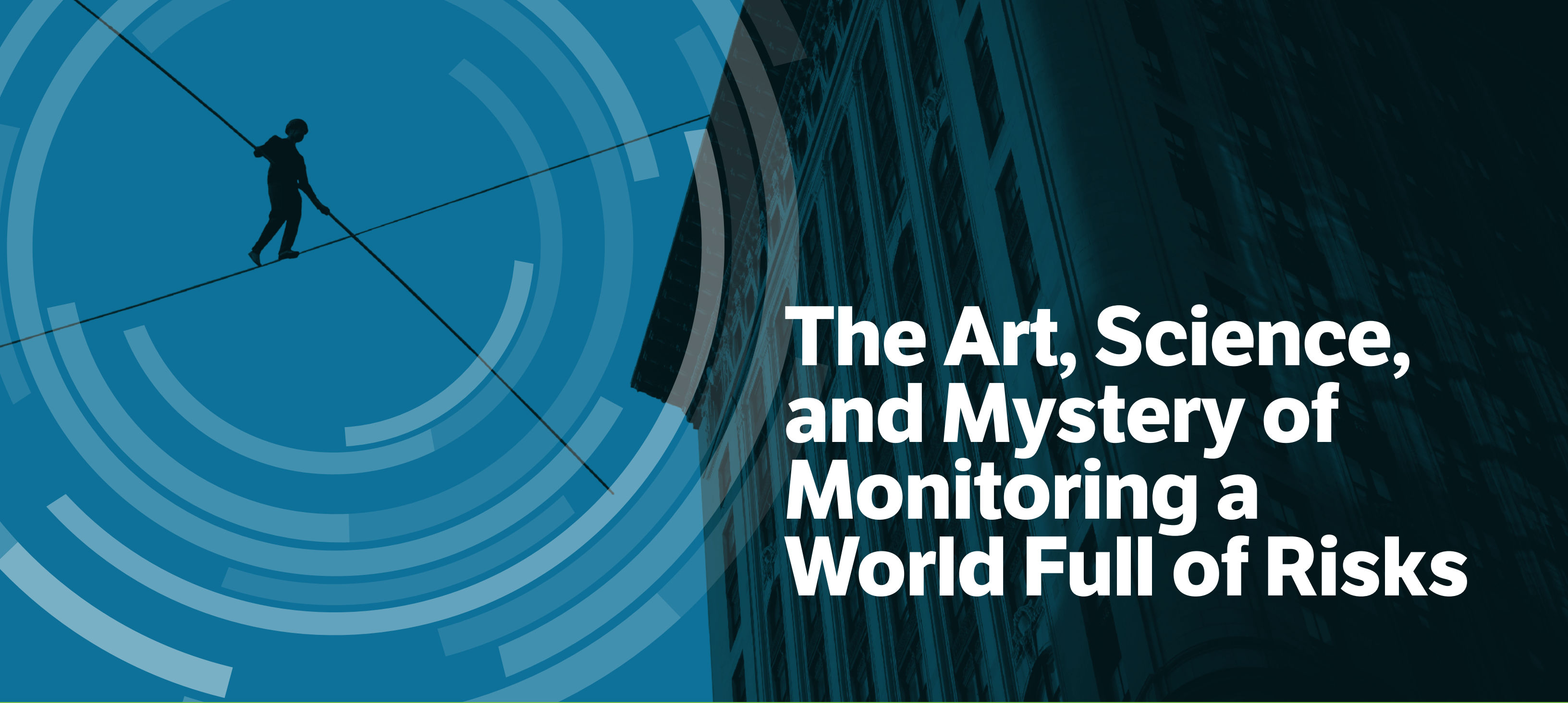
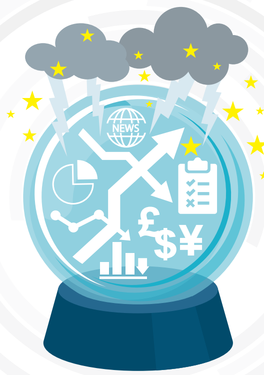
This article is the second in a special four-part series focused on various aspects of risk mitigation. Keep your eye out for the next article, which will discuss specific steps these experts take to mitigate risk in their institutions. If you missed the first article and would like to receive it, contact info@StateNational.com.



The Art, Science, and Mystery of Monitoring a World Full of Risks

State National prides itself on being a risk mitigation partner for hundreds of financial institutions across the country. We conducted these interviews on risk mitigation strategies as part of our ongoing commitment to support our partners with meaningful insights that will help them better manage their business.

In a world without financial risk, individuals would have access to complete information with thorough and accurate insight into the future, and buyers, sellers, savers, and borrowers would simply find each other organically. However, as evidenced by constantly changing and evolving economic conditions, advances in technology, and the increasingly rapid pace of information sharing, it is clear that the world is wrought with risk — which is why we must turn to financial institutions that are able to manage that risk in order to provide diverse consumer groups with access to the financial services they need to enhance their lives.



Risk mitigation happens largely behind the scenes and isn't generally visible to the member or customer, but in terms of long-term, organizational sustainability it is a critical function. Often, financial institutions will have to implement multi-pronged strategies to create a risk mitigation plan that provides their organization with necessary protections while still creating an open, engaging environment that meets the needs of savers and borrowers.

State National engaged several risk mitigation professionals in the financial services industry to discuss the internal and external factors they consider to help maintain the appropriate balance between growth and organizational protection as well as the steps they take when the inputs they monitor show signs indicating increased risk.

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Eric Fuglister

VP Consumer Lending, Wings CU, Apple Valley, MN:

"We monitor trends that are happening — car sales, car prices, things like that. And inside the credit union we look at 30- and 60-day delinquencies, even our loan late fees after 15 days. Our late fees are up this year, probably by almost 50%, which is an early indicator that while some people aren't late enough for it to impact their credit reports, they may be paying consistently 20 days late.

"We run credit scores on our entire loan portfolio quarterly, by product, to see if credit scores are rising, lowering, or staying the same. If more are declining that could be an indication that even if they're paying on time, if they've gone down from the A+ tier down to the B tier we may need to be proactive and reach out to the member.

"Our risk management department looks at risks across the credit union holistically, from credit exposure on the deposit side, to all kinds of different risks on our investment side. That's data I have access to and get information from on a monthly basis.

"Advances in technology have been a huge part of how we monitor and assess risk. I've got information at my fingertips, with a whole data analytics team — I've got dashboards for just about everything I want to look at, and most of it updates daily. I can compare trends, whether it's year over year, month over month, last week versus this week, yesterday versus today — so we can make adjustments much more quickly than we used to."

Deborah McRae

VP Risk Management, Five Star CU, Dothan, AL:

"We are trying to develop an enterprise risk management approach to how we deal with risk. Internal to the credit union, we have to monitor our operations for any signs of internal fraud, and we also have to make sure we're training our staff to watch for red flags that indicate any attempted member fraud.

"We also watch external signals, and we've got some policies that can be tweaked and tightened as necessary based on what we're seeing in the economy. We can call a meeting anytime we see something that looks like it's going upward or downward. Say, if trade relations with another country took a big downturn, that's something we'd quickly home in on. On the other hand, if a trade deal was signed that was very advantageous to the U.S., that's an indication we might be able to go back up on deposit rates or down on loan rates because it's a signal that the economy is likely to remain good for a while."

Henry Robaszewski

Director of Risk Management/Finance, BCU, Vernon Hills, IL:

"We've taken more steps, through both technology and data, in terms of analytical techniques. We've started an economic value-added process as well as risk-adjusted return on capital. **We're trying to incorporate more of the potential risks that are out there all together in a holistic approach, and then build that into the pricing so we can adjust our pricing to accurately account for the risks."**

Dave Brydun

VP Consumer Lending, BCU, Vernon Hills, IL:

"We have a playbook that's been put together that has a lot of detail for actions to take that are triggered off what we're observing as far as the macro factors Henry mentioned — yield curve, labor markets, things like that — industry factors. We keep close tabs on the industry through various reports that come out from Moody's, TU, Experian, and so on. We also look within our own portfolio in terms of any sort of vintage deterioration with our lending originations, and profitability concerns in various risk cells due to increased charge-offs where we're not being covered on the interest rate to cover those losses.

"If and when we start seeing signs of a downturn, we first focus on things we can quickly implement that have low member impact — things like tightening manual underwriting standards, reducing line exposure on new accounts. Then if things continue to deteriorate, we can move to actions like reducing existing credit lines, closing higher-risk accounts on the credit card side, or significantly changing up our automatic loan decisioning.

"We're utilizing as much of our existing internal technology as possible. The changes we've made to our monitoring, reporting, and governance over the past several years will really help us prepare for the next downturn, whenever that may be, whether it's six months from now or two years from now.

"We're also dabbling in things like machine learning to help us better identify risks and make changes off that. One big thing with the technology is more automation and efficiency and better identification of risks that will allow us to serve more traditionally underserved segments of our membership and being able to better split risks more precisely."

Professionals who are highly skilled and experienced in risk mitigation must carefully monitor a wide variety of indicators, both internal and external, to continually assess risk levels and make decisions about the right actions to take to protect their institution and their membership. We discovered that even in times of economic strength, the best organizations are always looking at what is coming next as well as peering into every area of their institution to identify and mitigate risk.

This article is the third in a special four-part series focused on various aspects of risk mitigation. If you missed the first two articles ("The Balancing Act of Risk Mitigation — With an Eye on Today's Economy" and "The Many Faces of Risk") and would like to receive them, contact info@StateNational.com.

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Risk Mitigation: Specific steps credit unions can take

Over the past several months, we have explored various aspects of risk mitigation with four experienced credit union professionals from across the U.S.

In the most recent article (the third in the series), these credit union leaders identified and described some of the internal and external factors they monitor to assess risk within their institutions. They also told us about some of the actions they take in response to what they discover.

Here, let's focus on a few of the specific comments our respondents made and take a deeper dive into some of the issues they mentioned.

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"Data security is obviously a huge risk. Especially with the Equifax breach a couple of years ago — I think that should have shocked every financial institution down to its core. Every financial institution has lots of sensitive information and you sure wouldn't want to have something like that happen in your credit union. So your investment in data security and keeping on top of that is a huge deal."

Eric Fuglister
VP Consumer Lending
Wings CU, Apple Valley, MN

FROM ARTICLE 2

"THE MANY FACES OF RISK"

Background

- In 2018, hacking was the most used method of breaching data (482 data breaches with 17 million records exposed). Unauthorized access ranked second (377 breaches affecting 404 million records). Accidental exposure was third (114 breaches with 22 million records exposed).[1]
- The banking, credit, and financial category continues to be the sector most affected. In the first 10 months of 2019, 100.4 million records in this segment were exposed — 62% of all records.[2]
- Data analysis by Juniper Research estimates that cybercrime will cost businesses over $2 trillion in 2019.[3]
- Malicious and criminal attacks are the leading root cause of data breaches, at 51%, but breaches caused by system glitches (25%) and human error (24%) are also serious threats.[4]

One thing that has become glaringly apparent in the past several years is that it's not enough to depend on your IT department to identify and root out security issues — data security awareness is now by necessity the responsibility of everyone in your organization.

What can you do?

- Conduct ongoing training and education of your employees and members.
  - **NAFCU: New Staff Online Training**
  - **NCUA: Cybersecurity Resources**
- Support the NAFCU and the Federal Trade Commission (FTC) in their efforts to advocate for national data and cybersecurity standards.
  - **NAFCU: Data Security**
  - **FTC: Data Security**
- Follow rigorous standards and obtain stringent security certifications. For example, State National has a thorough and proactive Information Security Plan including use of FoundSecure™ to constantly monitor for threats, SSAE 18 (SOC 1) certification, and regular SAS 70 audits. We also keep our systems and data in-house to avoid the possibility of information share transfer that can happen when technology is outsourced to third parties.

“Financial institutions are certainly taking on additional risk by originating auto loans with extended terms. Over the past few years, the percentage of auto loans with terms beyond 72 months has grown quite a bit. While we don’t originate much volume above 75 months, for the small portion that we do, we make sure additional rate premiums are in place to ensure that we are being compensated for the additional risk.”

Dave Brydun
VP Consumer Lending
BCU, Vernon Hills, IL

“THE MANY FACES OF RISK”
Continued

Background

- About a third of auto loans for new vehicles taken in the first half of 2019 had terms of longer than six years; a decade ago, that number was less than 10%.[5]
- The size of the average auto loan has grown by about a third over the past decade and in Q2 of 2019 hit $32,119 for a new car.[6]
- The average loan for a new car stretches for roughly 69 months, a record.[7]
- In the first half of the year, 1.5% of auto loans for new vehicles had terms of 85 months or longer. Five years ago, 8- and 9-year loans were virtually nonexistent.[8]
- Approximately 1 in 8 U.S. drivers is uninsured, and with longer loan terms that means a lender is exposed to risk for a longer period of time.[9]
- The Consumer Financial Protection Bureau found that longer-term auto loans are used by consumers with lower credit scores and have higher rates of default.[10]

What can you do?

As concerns about a possible recession continue to rise, it’s more important than ever for lenders to stay extremely mindful about who they lend to, for how long, and at what rate. Some lenders have chosen to pull back from long-term auto loans, while others are taking advantage of the market opportunity — hopefully with tighter structures in place to compensate for the added risk.

- Invest in sophisticated data and analytics tools that can appropriately price based on quantifiable and detailed borrower attributes and market data.
- Adjust loan-to-value ratios accurately to minimize default losses.
- Monitor your portfolio data to try to catch signs that borrowers are struggling financially — before they reach delinquent or default status.
- Since auto insurance is often one of the first expenses a borrower having financial trouble will drop, implement a rigorous insurance tracking program that includes technology capable of updating records in real time; also consider a portfolio protection insurance program to minimize the risk of unprotected loan collateral.

"We've taken more steps, through both technology and data, in terms of analytical techniques. We've started and economic value-added process as well as risk-adjusted return on capital. We're trying to incorporate more of the potential risks that are out there all together in a holistic approach, and then build that into the pricing so we can adjust our pricing to accurately account for the risks."

Henry Robaszewski
Director of Risk Management/Finance
BCU Vernon Hills, IL

FROM ARTICLE 3

"THE ART, SCIENCE, AND MYSTERY OF MONITORING A WORLD FULL OF RISK"

Background

- From MWCUA's report, *Enterprise Risk Management: An Approach to Implementation in Credit Unions*: "Enterprise Risk Management is a collaborative process to identify, manage and monitor organizational risks and opportunities, both internal and external, to ensure achievement of the credit union's strategic objectives and continued financial stability and viability." One of the benefits of ERM is that it establishes "a philosophy regarding risk and a risk culture, including aligning risk appetite and strategy, allowing for risk optimization within defined risk tolerance levels."[11]
- A comprehensive Enterprise Risk Management (ERM) approach can address myriad types of risk, both financial and non-financial: market risk, credit risk, asset and liability risk, liquidity risk, cybersecurity risk, conduct risk, third-party risk, reputational risk, operational risk, geopolitical risk, and more.[12]
- Eighty-three percent of respondents surveyed by Deloitte in 2019 said their institutions have an ERM program in place, up from 73 percent in the previous survey, with an additional 9 percent saying they were in the process of implementing one.[13]
- The issues cited most often as being an extremely high priority or very high priority were enhancing the quality, availability, and timeliness of risk data (79 percent) and enhancing risk information systems and technology infrastructure (68 percent).
- Advanced digital technologies like Robotic Process Automation (RPA), machine learning, Business Process Modeling (BPM), cognitive analytics, cloud computing, and natural language processing can increase both the efficiency and effectiveness of risk management.[14]

What can you do?

- Consider comprehensively training one or more employees at your institution as a specialist in Enterprise Risk Management.
  - **NAFCU Certified Risk Manager (NCRM) Program**
  - **CUNA Enterprise Risk Management Solutions Specifically Designed for Credit Unions**
- Use a systemic approach to implement capital and liquidity stress tests to continually monitor and assess risk levels in your credit union, including the involvement of your board of directors.
- Make researching and implementing advanced fintech solutions that analyze and address risk one of your institution's highest priorities.
- Attend industry events and conferences centered around risk management and the latest best practices.

"We are trying to develop an enterprise risk management approach to how we deal with risk. Internal to the credit union, we have to monitor our operations for any signs of internal fraud, and we also have to make sure we're training our staff to watch for red flags that indicate any attempted member fraud."

Deborah McRae
VP Risk Management
Five Star CU, Dothan, GA

"THE ART, SCIENCE, AND MYSTERY OF MONITORING A WORLD FULL OF RISK"

Continued

Background:

- The Association of Certified Fraud Examiners (ACFE) found that financial institutions had the highest rate of internal fraud among the industries they analyzed — 17.8 percent, with the median reported dollar cost of $200,000.[15]
- Internal control weaknesses are responsible for nearly half of frauds.[16]
- In 2015, employee fraud was a key contributor to 69 percent of credit union failures.[17]

What can you do?

- The #1 thing you can do in this area is to ensure your employees are well-trained.
  - Provide training and resources such as NCUA's Fraud Overview video series and other learning opportunities:

    NCUA Credit Union Resources & Expansion: Learning

    NAFCU: Lowering the High Cost of Internal Fraud
  - Be sure all employees are aware of the Suspicious Activity reporting requirements in the Bank Secrecy Act.
  - Make all employees aware of NCUA's fraud hotline available for reporting fraudulent or illegal activity; post this resource visibly, in multiple areas, to remind them that they can report any suspicious activity they observe confidentially and anonymously.
- Follow a rigorous data protection protocol as mentioned earlier in this article.
- Be vigilant about keeping a robust prevention program in place with strong internal controls, using best practices approved by regulators.

  NCUA: Regulation and Supervision Manuals and Guides
- Ensure your institution has regular, comprehensive auditing processes in place, and keep up with compliance.

  NAFCU: Compliance Guides & Manuals

Resources

NAFCU: New Staff Online Training
https://www.nafcu.org/newstafftraining

NCUA: Cybersecurity Resources
https://www.ncua.gov/regulation-supervision/regulatory-compliance-resources/cybersecurity-resources

NAFCU: Data Security
https://www.nafcu.org/datasecurity

FTC Data Security
https://www.ftc.gov/datasecurity

NAFCU Certified Risk Manager (NCRM) Program
https://www.nafcu.org/ncrm

CUNA Enterprise Risk Management Solutions Specifically Designed for Credit Unions
https://www.cuna.org/erm/

NCUA Credit Union Resources & Expansion: Learning
https://www.ncua.gov/support-services/credit-union-resources-expansion

NAFCU: Lowering the High Cost of Internal Fraud
https://www.nafcu.org/nafcu-journal-lowering-high-cost-internal-fraud

NCUA: Regulation and Supervision Manuals and Guides
https://www.ncua.gov/regulation-supervision/manuals-guides

NAFCU: Compliance Guides & Manuals
https://www.nafcu.org/compliance/compliance-guides-manuals

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This article is the fourth in a special four-part series focused on various aspects of risk mitigation. If you missed any of the first three articles ("The Balancing Act of Risk Mitigation — With an Eye on Today's Economy," "The Many Faces of Risk," and "The Art, Science, and Mystery of Monitoring a World Full of Risks") and would like to receive them, contact info@StateNational.com.

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