

TARP Reporting: With Little Guidance, Institutions Must Balance Simplicity with Effectiveness

Institutions that received equity investments from the U.S. Treasury must now figure out what information they will be required to track and report. In general, TARP agreements do not require recipients to report or track their use of funds, so many institutions are feeling their way along. At this stage, reporting guidance must be divined largely from the objectives for TARP money and could be summarized as follows:

- Documenting how the TARP funds have been and will be used, including programs to continue to meet the needs of creditworthy borrowers, prudently support in-market credit needs, and strengthen bank capital;
- Proving that the recipients have complied with the executive compensation restrictions established by Congress.

While there are few explicit requirements, there are many implied reporting requirements. To comply, institutions will need to:




- Track lending and investing (MBS/ABS) activities and then track changes against TARP funds received and show how these compare to other TARP recipients;
- Recognize how TARP reporting data ties to, or differs from, existing regulatory reporting;
- Think about how to leverage reporting capabilities and processes, such as those developed as part of SOX and/or Basel II initiatives;
- Develop processes for transferring raw data from systems into meaningful and consistent formats to meet new reporting needs; and

- Employ a combination of ongoing internal and external support to meet these new regulatory burdens in a way that minimizes the adverse impact on current operations and profitability.

This is merely the start of the reporting requirements. The largest 20 banks have already been required to provide monthly reports to Treasury on loan activity and mortgage and asset-backed securities. There are numerous federal agencies involved in TARP oversight (e.g., Treasury, the General Accountability Office, the Congressional Oversight Panel, members of Congress, the bank regulatory agencies, etc.), so it is a safe bet that more requirements will be forthcoming.

CPG's Viewpoint: Banking 2.0

A number of new retail banking technologies and applications have been introduced recently. Most of these new tools and services are aimed primarily at Generation Y, whose earnings are expected to outpace Baby Boomers' earnings by over \$500 billion over the next ten years¹. Which innovations should you pay attention to?

Technology	What's to Like	What's Not to Like	CPG's Perspective
<p>Smart Phone Apps: Programs (available for free or for a small fee) that allow customers to access information via a BlackBerry, iPhone, or other smartphone.</p> 	<ul style="list-style-type: none"> • 40% of Gen Y consumers consider mobile banking services when choosing a bank². • 20.5% of smartphone users currently use mobile banking vs. 2.7% of basic cell phone users³. • Through mid 2008, North American smartphone sales we up 79% over 2007⁴. 	<ul style="list-style-type: none"> • Only 18% of cell phones are smartphones⁵. • Mobile banking technology and platforms are continuing to emerge, and focusing attention on smartphone apps may derail or slow other, more urgent technology projects. 	<p>Banks positioning themselves as technology leaders should pursue smartphone apps aggressively; most other institutions should focus on mainstream mobile banking as new technology kinks get resolved.</p>
<p>Widgets: Tools that allow social networking site users to make payments to other individuals, donate to charities, and make online purchases.</p> 	<ul style="list-style-type: none"> • There are over 150 million active Facebook users; approximately 45 million in the US. • Vendor Obopay makes widgets for 10 social sites and has alliances with Citigroup, MasterCard, and Fidelity National Information Services. • Widgets can be bank-branded. 	<ul style="list-style-type: none"> • Technology is very new, so demand is still unclear. • A number of more entrenched, electronic payment technologies exist, such as credit and debit, which may serve to delay payment widget adoption. 	<p>Donation widgets would appear to offer the most initial appeal, as many banks are targeting not-for-profits as deposit rich customers. Banks that offer tools that facilitate non-profit development can distinguish themselves with this segment.</p>
<p>Next Generation Money Management Tools: Tools that help to summarize and track household finances, benchmark spending and budgets against peers, and facilitate savings.</p> 	<ul style="list-style-type: none"> • Budgeting functionality addresses consumers desire to control spending and increase savings. • Fast growing; e.g., Mint.com adding 2,000 users per day. • SmartyPig's goal-oriented accounts make savings more customer-centric. • Sites facilitate sense of community by aligning users with like habits and goals. 	<ul style="list-style-type: none"> • These are standalone applications that overlay bank accounts and activity. • Adoption is still light relative to total online banking users. 	<p>All four websites offer exciting new functionality, but banks still have the upper hand by virtue of their customer account relationships. Banks should look to adopt budgeting capabilities. Wells Fargo and PNC have made noticeable inroads.</p>

¹Deloitte Center for Banking Solutions

²Telecommunications Industry News

³The Kelsey Group

⁴American Banker

⁵Celent

⁶Gartner Group

⁷Facebook

⁸Mint.com

CPG Announcements

- Read Mary Beth Sullivan's Blog, "The Bottom Line" on BAI's online community. Go to <http://bai.org/community>.
- Mary Beth will be speaking at the 14th Annual Source Media Best Practices in Retail Financial Services Symposium, March 15-17, in Naples, FL.
- Mary Beth and Sandy Spring Bank's Jim Burrows will be conducting a webinar "Deposit Growth Strategies That Work In Today's Tough Environment" on April 1. More details will be available soon on our website: www.capitalperform.com.

CPG's TARP Scorecard

Total Number of TARP Capital Purchase Program (CPP) Participants¹:	<ul style="list-style-type: none"> • 311 banks & thrifts (or 4.5% of all eligible institutions). An additional 33 institutions have applied. • Participation is greatest among larger institutions. Just under half of all institutions with assets of \$5B+ are participating in the program.
Government Ownership (CPP funds as a % of risk-weighted assets, or RWA):	The government's total investment to-date amounts to 3.2% of RWA .
Most CPP Funds Received, in \$ooos:	<ul style="list-style-type: none"> • So far, Citigroup has received the largest dollar amount from the program – a total of \$49B or 23% of the total amount distributed. • The government's investments in Bank of America, Citi, JPMorgan Chase, and Wells Fargo amount to \$144B, or 68% of distributed CPP funds.
Least CPP Funds Received, in \$ooos:	Freeport State Bank of East Greenwich, RI (total assets of \$17.8MM) received \$301K , or 3.0% of RWA.
Most CPP Funds Received, as a % of RWA:	Citigroup's CPP funds are equivalent to 4.2% of RWA (as of 9/30/2008). This is well above the government's stated ceiling on TARP investments of 3.0%.
Least CPP Funds Received, as a % of RWA:	The \$4.2MM received by Northeast Bancorp of Lewiston, ME (total assets of \$605.2MM) amounts to only 1.0% of RWA .
Lowest YTD ROAE among CPP Participants, as of 3Qo8²:	OneUnited Bank of Boston, MA (total assets of \$625.3MM) reported an YTD ROAE of -187.88% . The bank received \$12.1MM thru CPP (or 3.0% of RWA).
Highest YTD ROAE among CPP Participants, as of 3Qo8²:	Morrill Bancshares, Inc. of Merriam, KS (total assets of \$659.6MM) posted a YTD ROAE of 17.60% . The bank has received \$13.0MM thru CPP (or 3.0% of RWA).

1. The 311 participants are defined as institutions that are either participating or that have been approved to participate in TARP as of 2/12/2009. The count of institutions that have applied for TARP funds does not include any institutions that may have requested that their application be kept confidential.

2. At press time, the most recent financial data available was as of 9/30/2008.

Source: SNL Financial, LC, 2009.

Regulatory Outlook 2009

The events of 2008 will have a profound impact in 2009 on both the types of regulatory issues that come to the forefront and the regulatory structure itself. At CPG, we believe the most important regulatory issues to be as follows:

1. **An increased emphasis on safety and soundness** – Now that the government's plan for TARP funds has been (mostly) laid out, regulators will be quicker to act against perceived threats to the safety and soundness of the system. This will mean that:
 - a. The regulators will be quicker to “pull the trigger” on failing institutions. During the first month of 2009, six banks and thrifts were closed by the agencies, compared with an average of about two per month in 2008.
 - b. The current regulatory structure will undergo a review – and also an over-
- haul. Legislators have already introduced measures that would create an authority in charge of systemic risk and oversight of industries that are currently not under heavy scrutiny (i.e., hedge funds). The administration wishes to show progress by the time the G-20 meets in April, so a new “blueprint” will likely surface in 1Q09.
2. **Greater capital requirements** – The de facto ratio of total risk-based capital required to be deemed “well-capitalized” has increased from 8% of risk-adjusted assets to around 12% or 15%. If the industry as a whole were to increase its aggregate risk-based capital ratio from 3Q08 levels (the most recent period for which aggregate data is available) to 15%, it would require a 26% increase in capital. TARP Capital Purchase Program funds dispensed to-date have increased capital levels by 17%, leaving a gap that will have to be filled by other sources.
3. **Conflicting pressures on TARP participants** – Banks must hold capital in order to meet the new “well-capitalized” standard previously described; however, institutions that participate in TARP are coming under greater pressure to deploy capital. The administration and Congress (which are now shareholders in most banks) want institutions to increase lending. The Treasury's plan for the final installment of TARP funds (unveiled on February 10, 2009) includes more robust reporting requirements for CPP participants. Future recipients of CPP funds will have to report on how this money has been used to increase lending in their footprint.

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Capital Performance Group, LLC

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