



Lighthouse

Volume 1, Issue 4

March 16, 2006

By Chesapeake Bay Associates, LLC

Bank Is Buried Under Information Avalanche

In This Issue

Growth from acquisitions is a time-honored strategy. It is a risk, too. Risk management is a business of getting certain things right. This can be very expensive when there are numerous moving parts in a dynamic enterprise. Management can be handicapped by poor coordination and obstacles to sharing information.

In this case, a regional bank holding company's acquisition program failed to integrate cultures, customer service, data center operations and branch platforms. The mounting disconnects threatened the survival of the bank. The vision of an integrated banking company had completely eluded the management, and the regulators were threatening action.



The bank realized a new vision in just one year.

A rapidly growing financial institution had acquired 23 banks. The company grew from a local institution to a major regional bank. They expanded into non traditional banking markets to increase profits, diversify risk and make more loans. Unfortunately, the company was under-achieving and had made several big mistakes. The Comptroller of the Currency, the Securities and Exchange Commission and individual state banking regulators were watching closely and getting more involved.

Mounting customer service problems were caused by 23 independent customer service teams that couldn't communicate with each other. The absence of a common goal was causing problems everywhere for the sprawling bank holding company. In fact, they were embarrassed, having recently cancelled their contract with the major customer satisfaction rating company. The customer complaint volume was too heavy at all branches. Everyone was uncomfortable and angry.

Customers complained they could not access their accounts at the branches where they were opened. Moving accounts to meet capital requirements is not wrong, but the process is usually transparent. Today, depositors can access their accounts and do almost everything from any branch or Internet browser. In this case, the accounting and bookkeeping workload created by the duplication was crushing. The enterprise formed by the 23 previously independent banks and

the holding company operated seven separate bank management systems and separate databases. It took 17 formerly dedicated data centers to keep it running with a much heavier than normal maintenance load. Chesapeake Bay Associates was brought in when the Federal and State Regulators advised management to clean up the mess – or else.

Goal Analysis

The bank holding company was several months behind in their General Ledger bookkeeping. The outside auditors were unwilling to sign the audit letter. Auditors complained management had not provided the financial information needed for the audit. The bank was struggling with sharing information with seven separate and distinct accounting and bank management systems in use across the enterprise. Consolidated reports were produced by hand. Report preparers collected inputs from the regional and divisional level containing a great deal of manually maintained records. Regions and Divisions always phoned-in their figures at the last minute. The financial information was incomplete and often inaccurate.

Operations complained they could not support the new products in Marketing's sales plans. It was far too complicated to install new products and update compliance onto so many diverse systems. Information security and privacy procedures were badly needed. For example, the seven management systems used the same passwords and access keys to process transactions through to

the local general ledger, customer accounts and loan accounts. A simple deposit of a check received from another account at a different branch was a sequence of non-secure transactions with the branches, which risked millions of dollars and customer files. Maintenance budgets burned through hundreds of thousands of dollars to change and verify the independent systems.

The 23 banks had been acquired for the addition of the assets and the income growth. Comparisons of cultures, administration, operations, databases and systems were not considered very important in the evaluation of the target suitability. The resulting sprawl consisted of seven distinct proprietary systems housed in seventeen separate operations facilities across multiple state lines.

Holding company management understood they had severe problems everywhere. We discussed, "How will we manage this," with them. This discussion uncovered four mission critical goals as follows:

1. Integrate the banking operations across one enterprise management platform.
2. Consolidate the data centers.
3. Train all staff on updated branding, positioning, vision and mission.
4. Implement an updated incentive system that establishes new goals for customer satisfaction and compliance along with asset and revenue growth.

Continued on next page ...

“ The review of the situation was bad. Management agreed to ... Implement solutions in two phases: Quick Fix and Strategic Solution ... Aggressive action on the bank’s mission critical goals produced a complete turnaround. ”



“Consolidated the enterprise IT onto five reconfigured operations centers.”

Company Digs Out In Two Steps

Strategy

The review of the situation was bad. Management agreed to a 5-point strategy with a steep ramp:

1. Assign an Integration Program Manager.
2. Specify new criteria for mergers and acquisitions.
3. Rebalance the expectations and goals for each subsidiary.
4. Implement solutions in two phases: Quick Fix and Strategic Solution.
5. Obtain regulatory approval for the restructuring plans.

The Quick Fix

All concerned recognized the scope and complexity of this project. We went to work with operational units on the following tasks:

- ¶ Developed software for global access to customer accounts. Created a customer education program, which spearheaded restored confidence.
- ¶ Customer service produced a list of where people wanted to do business from their analysis of the complaint calls. New banking features were installed to deliver the convenience.
- ¶ Thousands of letters were sent to customers who had phoned in, mailed or visited with complaints.
- ¶ Open houses were hosted for customers at which management appeared in public. At these meetings, complaints were recorded. Management took responsibility, took their beatings, and solicited input.
- ¶ Sent personal letters to everyone who attended meetings.
- ¶ Received extraordinarily favorable press on our efforts to correct a very bad situation.
- ¶ Analyzed capacity, throughput and operations manpower required for every computer system. Identified updates needed for enterprise capability.

- ¶ Completed a performance review for the operations centers. Rated capacity, throughput, and interoperability.
- ¶ Developed specifications for the enterprise solution.
- ¶ Consolidated the enterprise IT onto five reconfigured operations centers. Each center was assigned the responsibility for one mission critical activity, which was backed up at one of the other centers daily.
- ¶ Product lines were hopelessly duplicated across the data centers. Realigning the product lines and data centers according to the performance review conclusions eliminated the duplication.

The centers maintained proprietary databases, and communicated with each other and the branches using a common data format. IT developed a universal data format translator that added a measure of transparency to the process.

Strategic Solutions

Operations centers competed for recognition of best performance and the most rapid deployment of the change over. IT said they expected the Quick Fixes and Strategic Solutions to consume two years of development, an additional year for rollout, and several million dollars including all new equipment and training.

The bank was an experienced M&A partner with an updated target valuation model. So, we proposed a strategic acquisition when the new operation centers were up and running with the branches. We recommended a strategic acquisition that included a corporate computer network that we could plug into. The target management selected also offered most of the best system components called out in the specifications we developed during the Quick Fix phase.

The acquisition closed rapidly. Full integration was completed in less than six months vs. nine years for some of the previous acquisitions.

The new network enabled the imaging of entries onto the enterprise general ledger from the branches. IT and Accounting implemented self-reconciling ledger documents, following procedures developed by the Controller’s office. The streamlined reconciliation process eliminated the transaction backlog and updated the company’s books in four months.

Improvements

Aggressive action on the bank’s mission critical goals produced a complete turnaround. We noted seven improvements in our final report:

1. The regulatory compliance backlog was cleared.
2. The outside auditors signed their letters without qualification, and the regulators were satisfied.
3. The cost of bookkeeping errors vanished.
4. Hundreds of thousands of dollars were recovered from employees who gamed the old system for personal gain.
5. The documented thefts persuaded the regulators to ease some of the restrictions previously imposed on lending.
6. The enterprise restructuring project was completed within one year, slicing two years from IT’s schedule.
7. Customers were pleased and the satisfaction was documented.