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THE CHAMPION FOR MINNESOTA BANKERS

NEWS
MARCH/APRIL 2018

Preview of the 2018 Minnesota Legislative Session

You Are the Voice of Banking - How to Get Involved and Make a Difference

Taking Your Incident Response Plan Testing to the Next Level

Resolve to Get Your Findings Organized in 2018

GOVERNMENT RELATIONS ISSUE

Special Section: Federal Tax Reform

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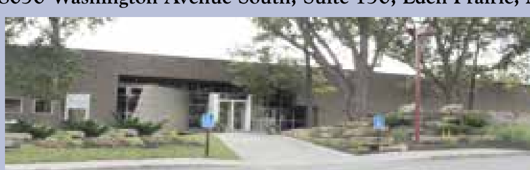

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THE CHAMPION FOR MINNESOTA BANKERS

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New CFPB Acting Director Makes Welcome Changes

Joe Witt
MBA President/CEO
joew@minnbankers.com

Greetings to you. I am writing this column in mid-February, as things are rolling along nicely. From what I saw, the Super Bowl went well for Minnesota. The "Bold North" campaign seemed very positive for our image. The Winter Olympics are taking place, and Team USA is collecting its fair share of medals. Both the Timberwolves and the Wild are looking like playoff teams, and the days are getting noticeably longer as we head towards spring. Yes, things are good.

My wife Kelly likes watching the Sunday morning news shows, like *Meet the Press*. I typically do not watch with her because the shows strike me as being more about entertainment than about reporting the news. They typically have guests on their panels representing the political left and right, and they are mostly from the far left and the far right. During the Obama administration, the people on these shows representing the left said that President Obama could do no wrong, while the other side said that he did nothing right. Now, with the change to the Trump administration, the roles are reversed, and the shows are coming across as more edgy and more divisive than ever.

These news shows rarely showcase anyone representing the middle. They are purposely set up to be confrontational, with a strong "us versus them" mentality. To me it's a lot of noise with no substance. I would welcome hearing someone suggest that it is possible to govern without taking an extreme approach on every issue.

A couple weeks ago a panelist was complaining that some of President Trump's administrative agency heads were changing the focus and the direction of the administrative agencies. Well, of course they have. That situation happens every time a new administration takes over. The policy positions taken by President Obama's agency heads were very different policy positions than those of President Bush's agency heads, too.

Without making a blanket statement about all of the Trump administration's policy changes, one agency pronouncement looks to be very good news for the banking industry. The Acting Director of the Consumer Financial Protection Bureau (CFPB), Mick Mulvaney, sent a memorandum to all CFPB employees. The memorandum was designed to explain how he would manage the CFPB differently than his predecessor, Richard Cordray, had managed the agency.

To explain the differences, Mulvaney referenced a quote by Richard Cordray in *Politico Magazine* to make his point. Cordray said, "We wanted to send a message: There's a new cop on the beat… Pushing the envelope is a loaded phrase, but that's absolutely what we did."

The difference, Mulvaney announced, was that the CFPB would no longer attempt to expand the law by continually "pushing the envelope." Instead, the CFPB will enforce the laws as they are written. Getting back to that fundamental principle is a really significant change.

Acting Director Mulvaney continued by saying that the CFPB does not work for the government; it works for the people, and that means all the people: both those who take out loans and those that make loans; and both those who use credit cards and those who provide the cards. He then said, "All of them deserve to be treated fairly by their government." The CFPB will no longer act as the "new cop on the beat," on a mission to fight the bad guys. (MBA Past Chair Chuck Johnson from Root River State Bank in Chatfield will be very pleased to hear this news, as he was especially troubled by the CFPB's inflammatory rhetoric.)

Acting Director Mulvaney continued by saying that it is not appropriate for any government entity to "push the envelope" because the damage that we can do to people can linger for years. He noted that if the CFPB loses a court case because we "pushed too hard," we simply move on to the next matter. When the CFPB loses a lawsuit, where does the winning party go to get their time, their money or their good names back?

At the same time, Mulvaney signaled a strong enforcement posture when it is warranted. He said, "There will absolutely be times when circumstances dictate that we take dramatic action to protect consumers. And at those appropriate times, I expect us to be vigorous in our enforcement of the law." He then cautioned that "bringing the full weight of the federal government down on the necks of the people we serve should be something that we do only reluctantly, and only when all other attempts at resolution have failed."

This new approach seems thoughtful and reasonable. The CFPB will not be shuttered, as some people would like. The agency will enforce the consumer protection laws as they are written, but it will not attempt to expand the law. When consumers are harmed, the CFPB will vigorously protect them, but they will not make a federal case out of a highly technical regulatory mistake that does not negatively impact consumers.

The people on the Sunday morning talk shows, from both the left and the right, will probably not like what Acting Director Mulvaney has said, which is just fine by me. Let them rant and rave about it. This new direction should mean that our banks will no longer have to spend a ridiculous amount of time and resources defending baseless CFPB claims.

Now we just need the Department of Justice to follow the CFPB's lead.

Thank you very much for your membership in the MBA and for all your support. ■

Joe Witt

Joe Witt, MBA President/CEO

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Look for upcoming GSB classes at www.gsb.org or www.minnbankers.com.

EDUCATION NEWS | by Eric Hauth

Each and every day working at the MBA, I'm reminded of three things:

- First, that banking in today's environment is highly complex, requiring tremendous dedication by bankers to solve problems that help their customers and their communities.
- Second, that despite the challenges they face from regulatory burdens and constant change in the banking landscape, bankers are a resilient and optimistic bunch, willing to tackle new challenges through ongoing professional growth and development.
- Third, that the MBA staff is firmly dedicated to supporting bankers in meeting whatever challenges they face – through advocacy, education, compliance and IT consulting – and hopefully helping our members create new opportunities.

As I look ahead to a much-anticipated spring thaw and summer, I'd like to highlight several upcoming professional development opportunities that speak to all three of these daily reminders.

April 17 & 18 – Operations/Technology Conference
Each year the MBA organizes this conference with the goal of providing bankers the critical information they need to stay current on changing operational opportunities and threats to their bank. This year is no exception. Presentations by leading experts include: continuity planning, disaster preparedness, website design best practices, and tips for educating bank customers on cyber security. The line-up this year is top notch and we're excited for another great conference.

June 10-12 – MBA Annual Summit
Building on the success and energy at last year's Summit in Duluth, the MBA Annual Summit promises to be even bigger and better in 2018! With leadership as the theme, we've pulled together world-class presenters to give bankers practical insights that they can take back and apply to their banks. And, we have one of the highest energy keynote presenters available – P.J. Fleck, the head football coach for the Minnesota Gophers. In addition, we're excited to feature a panel discussion of graduates from the first class of the MBA's new Leadership Development Academy, representing the "next generation" of bank leaders in Minnesota.

2018-19 MBA Leadership Development Academy
Speaking of the Leadership Development Academy, this exciting new program offers a world-class training experience for emerging bank leaders looking to bring their capabilities to a new level. The MBA's board of directors decided to launch this program with the simple idea that the only way to truly future-proof an organization is through the development of great leaders. The application process is now open for the second class, which kicks off immediately following the 2018 Annual Summit in Brainerd. Details can be found at www.minnnbankers.com/leadershipacademy. **The deadline to apply is March 30.**

Spring is right around the corner and, with any luck, we can start thinking about trading our snow shovels for rakes. We look forward to seeing you at a future MBA event, and we invite you to let us know what else we can do to help you succeed. ■

Preview of the 2018 Minnesota Legislative Session –

The Legislative Session began on Tuesday, February 20, with many issues lingering from the end of the 2017 session and additional ones that popped up over the interim. As legislators begin the session, they will have to work at a quicker pace with the Constitutional adjournment date only 13 weeks away on May 21, 2018.

After the Special Session concluded last May, Governor Mark Dayton line-item vetoed the Legislature's funding, sending attorneys for the Governor and legislators to court to debate over whether the Governor has the authority to line-item veto one branch of government. The Minnesota Supreme Court determined that the legislature had enough other sources of funding to use until session began in February and instructed them to use the other funds rather than deciding the issue. Legislative funding will be one of the top priorities for the beginning of session, as the funds are running low.

Another complication in St. Paul comes with the appointment of Lieutenant Governor Tina Smith to the U.S. Senate after the resignation of Senator Al Franken. The appointment of Senator Smith meant that Minnesota Senate President Michelle Fischbach (R-Paynesville) is constitutionally required to assume the position of Lieutenant Governor, raising the question of whether she can hold both positions. Republicans left session last year with a 34-33 majority, but if Senator Fischbach is forced to leave the Senate, her seat would be open. Senator Fischbach's case is currently being debated in court. If she is forced to resign from her seat, the Minnesota Senate will be deadlocked 33-33 until a Special Election can be held in the middle of the Legislative Session.

If that wasn't enough to make your head spin, President Trump and Congress passed a tax bill at the end of 2017 that will require the Minnesota Legislature to pass some type of tax conformity bill this year or Minnesotans' taxes will be confusing and complex, even for TurboTax. Revenue Commissioner Cynthia Bauerly has agreed that something must pass for Minnesotans to help alleviate the confusion. What that something is will be the long discussion this session between legislators and the Governor!

Minnesota is one of a few states that bases state taxes on an income figure pulled from the federal filling called "federal taxable income." In January, it was reported that if Minnesota simply conformed state tax code to federal code, the state would bring in an additional $813 million in taxes in the next fiscal year and $1.49 billion the two years following. Legislators have an opportunity to pass some tax savings on to individuals and businesses; however, getting everyone to agree will be a challenge.

In addition to a tax conformity bill, the February Forecast will be released on February 28 which will result in a supplemental budget. The November budget forecasted a deficit of $188 million for the current biennium. In January, Minnesota Management and Budget gave another update stating that the January numbers were more positive, and revenues were up $349 million. Leadership is anticipating the February forecast will be closer to a $400-500 million surplus, which is considerably better than the November numbers anticipated.

The short session is customarily devoted to passing a bonding bill. Since there was no bonding bill in 2016, the legislature felt they needed to pass a bill last session, resulting in close to $1 billion in capital investment projects. The Governor has already proposed a $1.54 billion bonding package for 2018, which will make for an interesting conversation on the size of a bill. Republicans tend to favor bonding bills under $1 billion. A bonding bill requires a three-fifths majority in each body, meaning the House and Senate majority caucuses will need help from the minority caucuses to pass the bill.

Another Wild Ride

By Therese Kuvaas

Other issues the legislature aims to address this year include fixing the Minnesota Licensing and Registration System (MNLARS) rollout mess, healthcare, sexual harassment and elder abuse reports.

Banking

With such a short session, the MBA is hoping that the legislature keeps the conversation about banking and regulation to a minimum. However, there are always legislators who introduce bills which would impact the banking industry, and this session will be no different.

The MBA has a few legislative issues of interest this year, which include proactively pushing a Residential Property Assessed Clean Energy (PACE) bill that would protect a mortgage's priority lien position and protect homeowners by putting consumer protections and other safeguards in place before a company can offer this type of financing.

Some background: Property Assessed Clean Energy (PACE) legislation began passing in states in 2009 and 2010 to offer additional options for energy financing. Minnesota passed legislation enabling PACE for both commercial and residential projects. Since the legislation passed in Minnesota, only commercial PACE projects have moved forward as the market was still recovering and no one seemed interested in Residential PACE until more recently. The MBA was alerted about two years ago that an energy financing company out of California was looking to move into the Minnesota market, which prompted our research into how residential PACE has worked in other states. Last session, the MBA, along with the Minnesota Realtors, Center for Energy and Environment and Legal Aid passed legislation that would suspend this program in Minnesota until a task force could study the program and provide recommendations.

In the states that have residential PACE, the PACE lien jumps the mortgage and has priority status. The MBA, along with the Minnesota Realtors, Minnesota Credit Union Network, Center for Energy and Environment and Legal Aid spent the past seven months working on the task force and subsequently drafting legislation that would not allow a Residential PACE lien to have priority, require these PACE financing companies to register with the Department of Commerce and require consumer protections to assure the homeowner understands the program.

Some other issues the MBA will be working on include remote notary, agriculture issues, Uniform State Labor Standards, and other topics as they arise throughout the session.

One important point to keep in mind during the upcoming session is that 2018 is an election year for governor, attorney general, secretary of state, auditor, the Minnesota House of Representatives, both U.S. Senate seats and all our members of Congress. Legislators often want to get in and out of session quickly during election years, while other times they want to take a stand. The bottom line is that we expect another lively legislative session and the MBA lobbying team will be working hard to ensure that banking interests are well represented at the Legislature. ■

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You Are the Voice of Banking – How to Get Involved and Make a Difference

By Therese Kuvaas

With the beginning of the 2018 Minnesota legislative session upon us, it's a perfect time to get more involved in the political process. While politics can be a dirty word, lawmakers pass bills and enact new laws based on input from constituents who get involved and move their agendas front and center. Legislators need and want to hear from you concerning how legislation affects you, your business and the community.

Success at the Capitol depends on a multifaceted approach. The MBA is at the Capitol every day during session making sure your voices are heard. MBA staff works hard educating and informing legislators on various banking issues throughout the session and throughout the year. However, that's not enough. Personal contact from you is very influential and helps your legislators understand your position. The voice of a constituent can be much more powerful at the Capitol than a lobbyist's. Legislators and their staff need to hear your perspective on what is going on in today's marketplace. They need to hear that your bank is always working with your customers and that you have been there for your community in both good times and bad. They need to be reminded that you are well managed, heavily regulated, and examined regularly. You need to tell them that you have always provided loans in a thoughtful, conservative manner with an eye toward maintaining long-term relationships. You need to tell them that you are proud to be their local banker!

The legislative process begins with getting involved early and becoming acquainted with your local legislators. The MBA provides several other access points to interact with your policymakers. These include MBA Bank Day at the Capitol, the Washington, D.C. trip, and coordinating letters or emails on important issues. Following is a summary of some of these opportunities.

Stay on Top of Legislative Happenings

Throughout the year, the MBA Government Relations team regularly sends out eNewsletters to keep our members informed on policy issues. During the legislative session, MBA's *Political Insight* eNewsletters arrive in your inbox every Friday with up-to-date information on the session, banking bills and legislative schedules. Please take the time to read these newsletters and contact policymakers to emphasize your stance on issues that impact banking.

What are the Best Ways to Get Involved?

MBA's Annual Bank Day at the Capitol – March 22, 2018: This is an excellent opportunity to begin (or continue) your involvement with the MBA grassroots effort. Bank Day at the Capitol allows you to see the political process in action and gives you the chance to meet in St. Paul with your legislators and educate them on important issues that the financial industry faces.

At Bank Day, not only are you meeting with your local legislators, but you are given the chance to hear from and discuss with leaders of the House and Senate their views on the issues facing our state. Bank Day is not just for CEOs, presidents and senior employees. Every bank employee has an important role in the success of your bank, so encourage every member of your team to participate in Bank Day.

Washington Visit – April 23-25, 2018: MBA will be joining the American Bankers Association's Government Relations Summit at one supercharged conference. During the event, we will hear from congressional and regulatory leaders and make a trip to Capitol Hill to meet with our Members of Congress. We will receive briefings on current rules, regulations and legislation and take the opportunity to discuss issues with those who influence and make the decisions. This is an unparalleled opportunity for bankers to impact national policy and network with other banks throughout the country.

Invite Your Legislators into Your Bank – The best way for a legislator to understand the banking industry is for you to invite them into your bank and have them meet your staff. Most legislators do not comprehend the regulatory burdens placed on banks and businesses. By inviting them into the bank, legislators will get a firsthand look at how banks operate, meet the customers your bank serves and experience the value banks bring to their communities and the economy. This is a great opportunity for you, the bank and the legislator. ■

GET INVOLVED!!

Contact and educate your legislators. Attend Bank Day at the Capitol on March 22nd and the MBA/ABA Spring Government Relations Summit Washington Trip from April 23-25. If you want to get involved in any of these events or if you want more information on MBA's grassroots efforts, contact Therese Kuvaas, MBA's Government Relations Manager, at 952-857-2603 or theresek@minnbankers.com.

who's who

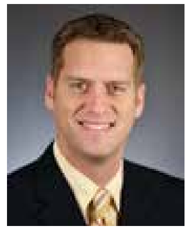
These House and Senate leaders will play key roles in deciding banking related issues this session.

GOVERNOR MARK DAYTON

- Democrat, ***Minneapolis***
- Former U.S. Senator and Minnesota State Auditor

LIEUTENANT GOVERNOR

SPEAKER KURT DAUDT

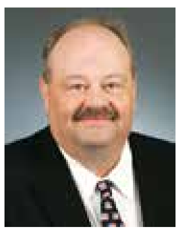


- Republican, ***Crown***
- Speaker of the House
- Most powerful position in Minnesota House of Representatives

REPRESENTATIVE JOYCE PEPPIN

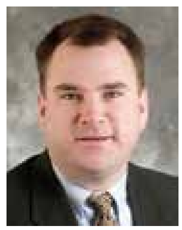
- Republican, ***Rogers***
- Majority Leader
- Number two position in House leadership

REPRESENTATIVE GREG DAVIDS



- Republican, ***Preston***
- Chair of House Tax Committee
- Insurance Agent

REPRESENTATIVE JOE HOPPE



- Republican, ***Chaska***
- Chair of House Commerce and Regulatory Reform Committee

REPRESENTATIVE MELISSA HORTMAN

- Democrat, ***Brooklyn Park***
- Minority Leader
- Attorney

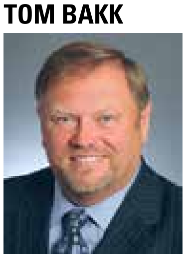
SENATOR PAUL GAZELKA

- Republican, ***Nisswa***
- Majority Leader
- Most Powerful Minnesota State Senator

SENATOR MICHELLE FISCHBACH

- Republican, ***Paynesville***
- President of the Senate
- Chair of Higher Education Committee

SENATOR TOM BAKK



- Democrat, ***Cook***
- Minority Leader
- Former Tax Committee Chair

SENATOR GARY DAHMS

- Republican, ***Redwood Falls***
- Chair of Commerce and Consumer Protection Committee
- Insurance Agent

SENATOR ROGER CHAMBERLAIN

- Republican, ***Lino Lakes***
- Chair of Senate Tax Committee
- Financial Representative

Does S Corporation Status Still Make Sense for My Bank?

By Jason Wimmer

The Tax Cuts and Jobs Act (TCJA) brings sweeping tax reform changes, and many of these changes favor C corporations. The most significant change is a reduction to corporate tax rates. For tax years beginning after December 31, 2017, the corporate tax rate will be reduced to 21 percent (from a maximum tax rate of 35 percent).

The reduction to individual tax rates under the TCJA pales in comparison. The highest individual tax rate will be reduced to 37 percent (from a maximum tax rate of 39.6 percent); therefore, depending on the marginal tax rate of its shareholder group, an S corporation bank will be subject to much higher tax rates than a C corporation bank.

This significant difference in tax rates begs the question: Does S corporation status still make sense for my bank? Tax rates do not tell the entire story. To answer this question, the benefits of C corporation status need to be compared side-by-side to the benefits of S corporation status.

Benefits of C Corporation Status

The obvious benefit of C corporation status is the positive impact of a maximum 21 percent corporate tax rate, compared to a maximum 37 percent individual tax rate for S corporation banks. On a million dollars of taxable earnings, this can translate to permanent tax savings of $160,000 (ignoring the new "pass-through" deduction, discussed below).

Besides reducing corporate tax rates, the TCJA also eliminates the benefit of state tax deductions for most individuals (capped at $10,000 per year). Thus, another ancillary benefit of C corporation status is the fact that C corporations are not limited on their state tax deduction, whereas S corporations will be limited at the shareholder level. On a million dollars of taxable earnings, this can translate to another permanent tax savings of roughly $21,000 for Minnesota banks.

Other benefits of C corporation status for banks include the following:

- **3.8 percent Medicare Tax on Passive Income** – C corporations are not subject to the 3.8 percent Medicare tax on passive income. S corporations, on the other hand, are potentially subject to this tax at the shareholder level, depending on the shareholder's level of involvement at the bank.
- **Deferred Tax Assets** – C corporations can book a deferred tax asset for cumulative book / tax timing differences, thus having a significant positive impact on the bank's capital.
- **Tax Bad Debt Reserve** – Eligible "small" banks are permitted to use a tax reserve method of accounting for bad debts, thus yielding additional tax deductions on their corporate tax return.
- **Dividends Received Deduction** – C corporation banks are permitted to deduct 50 percent (sometimes 65 or 100 percent, depending on percent of ownership) of dividends received from other corporations.
- **Fringe Benefit Treatment** – S corporation shareholders owning more than 2 percent of the outstanding stock must include certain company-provided fringe benefits in their gross income, whereas C corporation shareholders do not.
- **Accrued Expenses to Shareholders** – An accrual basis S corporation cannot deduct accrued expenses to shareholders (e.g. salary, bonus, interest, etc). An accrual basis C corporation can deduct accrued expenses to shareholders owning 50 percent or less of the corporation's stock.
- **Eligibility Issues** – An S corporation can only have one class of stock, cannot have more than 100 shareholders, and must be individuals, certain types of trusts and estates, or qualified nonprofit entities. A C corporation can generally have any number or type of shareholders.
- **Administrative Cost** – A C corporation has fewer administrative costs and professional fees associated with it, as compared to S corporations.

Benefits of S Corporation Status

Many banks have elected S corporation status. In the past, the S corporation election was hugely beneficial, primarily due to two favorable tax provisions: 1) S corporations were not subject to "double tax," and 2) S corporation shareholders received a stock basis increase for undistributed profits.

Double Taxation

Dividends paid by a C corporation are generally subject to double taxation. First, C corporations pay tax on their taxable income, now at a maximum rate of 21 percent. When income is distributed to the shareholders as dividends, the shareholders pay a second tax on the same income, generally at a tax rate of 15 percent or 20 percent (plus another 3.8 percent for the Medicare surcharge).

S corporation earnings are taxed only once - at the shareholder level. Undistributed earnings are recorded in the Accumulated Adjustments Account (AAA), a corporate level account. Because the earnings have previously been "passed-through" to the shareholders and subjected to tax on the shareholders' returns, subsequent distributions of the earnings out of AAA are generally tax-free.

Stock Basis Increase for Undistributed Profits

The shareholders' tax basis in the stock of an S corporation is increased or decreased by the income or loss that is passed through to the shareholders. While generally not taxable, actual distributions of cash out of AAA reduce a shareholder's basis in the stock of the S corporation. Thus, another significant advantage of an S corporation is that undistributed income increases basis in stock and thereby reduces the recognition of gain on the disposition of the S corporation stock.

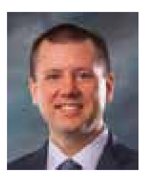
Other benefits of S corporation status for banks include the following:

- Pass-Through Deduction – The TCJA provides a new 20 percent pass-through deduction for "qualified business income." The provision is complicated and subject to numerous limitations and exceptions; however, most well-advised S corporation banks and shareholders should be able to utilize this favorable tax provision. The impact is that 80 percent of the S corporation earnings will be subject to tax, effectively lowering the highest individual tax rate from 37 percent to 29.6 percent.
- Elimination of Double Tax on Sale of Assets or Liquidation – A C corporation must first recognize a gain at the corporate level (and pay tax on the gain) when it sells assets and / or liquidates. If the net proceeds are distributed in liquidation, there is another tax at the shareholder level.

  The gain on the sale of assets (and on subsequent liquidation) by an S corporation is generally taxed only once at the shareholder level, other than gains subject to the Built-in Gains tax. This can be a significant benefit for an S corporation, especially after factoring the basis step-up referenced above. This also makes an S corporation more attractive to a potential buyer.
- Charitable Contribution Limitations – A corporation's charitable contribution deduction is limited to 10 percent of its pre-contribution taxable income. For an S corporation, the limitations are determined at the shareholder level, and are significantly less stringent (a shareholder may deduct cash charitable contributions of up to 60 percent of their AGI).
- Shareholder Interest Expense on Acquisition Debt – When a shareholder purchases the stock of a C corporation and borrows the funds to acquire the stock, the interest expense is classified as "investment interest." In general, investment interest is only deductible against investment income. If the same shareholder borrows funds to purchase S corporation stock, the treatment of the interest expense follows the character of the income passed through from the S corporation (i.e. it generally offsets K-1 ordinary income and is deductible on Schedule E).

Summary

The TCJA brings sweeping tax reform changes. The significant decrease in the C Corporation tax rate has caused many S corporation banks to question whether their choice of entity status still makes sense. To adequately address that question, the benefits of C corporation status should be compared side-by-side with the benefits of S corporation status, while also considering the long-term business plans for the bank. Tax advisors can be consulted to run an analysis over a multi-year period, and to summarize the cost / benefit in a quantifiable manner. The results of this analysis can determine the answer to the question, "Does S corporation status still make sense for my bank?" ■



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MIDWEST BANKERS
Insurance Services

Increased Liquidity? Don't Forget About Excess Deposit Bond Insurance

The FDIC recently released their Supervisory Insights for Summer 2017 stressing liquidity risk. One insurance product that has made its return over the last several years to assist with liquidity is the Excess Deposit Bond (EDB) coverage. This single-policy solution insures depositors in excess of FDIC insurance limits, allowing banks to attract and retain larger deposits without pledging securities, or using letters of credit. Banks can provide EDB to all account and depositor types. Banks electing to use this product will complete a Specified Account Holder form annually, listing the depositor and the amount the bank wishes to insure the customers deposit for. The bank will then receive a master policy which includes an insurance certificate for each depositor. Premiums are calculated based on limits used, rather than limits available, making this a very cost-effective product. A further benefit is the inclusion of pro-rated refunds for the bank, should an insured depositor withdraw some or all of their excess funds prior to the master policy renewal.

We're here to assist Minnesota banks with their insurance needs. Let us know how we can help.

MBIS is owned and operated by the Minnesota Bankers Association and the Wisconsin Bankers Association, while also being endorsed by the North Dakota Bankers Association. As an insurance agency run by those defending and advocating for banking, you can rest assured MBIS will always have your best interests in mind. Further, as an independent agency, MBIS has access to a variety of insurance providers to help them tailor plans to meet the specific needs of banks. To find out more about how MBIS can be the solution to your insurance challenges, please visit www.mbisllc.com, contact MBIS Regional Sales Manager Adam Dawson at 952-857-2604 or adamd@mbisllc.com or Vice President of Sales Jeff Otteson at 608-217-5219 or jeffo@mbisllc.com.

MBA
ASSOCIATE MEMBER

Highlights of the Tax Cuts and Jobs Act for Bankers

By Mike Crabtree

The Tax Cuts and Jobs Act (TCJA) is the biggest change to federal tax law in over 30 years. Some of its provisions have broad application, and some are more narrowly focused, but nearly every United States individual and business will be affected by the Act to some degree. One of the most significant changes is the new income tax rate for C corporations, which is now 21 percent.

The stated goal of achieving tax simplification was not met, but some aspects of the new law may make filing easier for some taxpayers and businesses. The increase in the standard deduction, combined with limitations on state property, sales, and income tax deductions, will increase the number of individual taxpayers that find it more advantageous to claim the standard deduction instead of itemizing. There are several provisions that benefit small businesses (those with less than $25 million in revenues) by allowing them to sidestep certain complicated rules regarding accounting methods, inventory capitalization, and construction contract income.

One provision of the TCJA that directly affects larger banks is the new limitation on the deductibility of FDIC premiums. Under the new law, an "applicable percentage" of a bank's FDIC premiums are not deductible. The formula for determining the "applicable percentage" is to take the total consolidated assets of the bank and subtract $10 billion, then divide the result by $40 billion. For banks with assets under $10 billion, the applicable percentage will be zero, so there is no limitation on the deduction. For banks with assets over $50 billion, the applicable percentage will be 100 percent, so they will get no deduction for their FDIC premiums. Banks with assets between $10 billion and $50 billion will have their tax deduction reduced, but not entirely.

Another provision affecting banks, along with other businesses that have historically entertained clients, is the elimination of the deduction for business entertainment expenses. Under the new law, all expenses for business entertainment are now nondeductible. Twins games, golf outings, and similar activities with clients, prospects, and referral sources can no longer be deducted, regardless of the amount of business discussion involved. There is some debate among the experts on whether all meal expenses involving clients are necessarily nondeductible entertainment expenses, or if there is still some deductibility when a business meeting also includes a meal. Hopefully guidance will be coming from the IRS clarifying the effects of this provision.

Interest Deduction Limitation

In a provision that impacts the customers of banks, the TCJA expands the limitations in the Internal Revenue Code on the deductibility of business interest. Under the new law, all large businesses are generally subject to a disallowance of a deduction for net interest expense in excess of 30 percent of the business's adjusted taxable income. More specifically, the deduction for business interest expense for the year is limited to the sum of: a) business interest income for the year, plus b) floor-plan financing interest expense for the year, plus c) 30 percent of the business's adjusted taxable income (not less than zero) for the year. Amounts disallowed by the limitation are treated as being paid or accrued in the succeeding taxable year (special rules apply for partnerships).

For purposes of this new limitation, "adjusted taxable income" is computed without regard to business interest income or expense, net operating loss (NOL) deductions, the new pass-through deduction for qualified business income, non-business income or loss, and for tax years beginning after December 31, 2017 and before January 1, 2022, without regard to deductions allowable for depreciation, amortization, or depletion. After 2021, depreciation, amortization, and depletion deductions will be part of the adjusted taxable income computation.

An important exemption from these rules applies for taxpayers (other than tax shelters) that have average annual gross receipts for the three-tax year period ending with the prior taxable year that do not exceed $25 million. The new limit does not apply to certain regulated public utilities. Real property trades or businesses (real property development, redevelopment, construction, reconstruction, acquisition, conversion, rental, operation, management, leasing, or brokerage) can elect out of the interest limitation provision if they use the alternative depreciation system (ADS) to depreciate applicable real property used in the trade or business. Farming businesses can also elect out if they use ADS to depreciate any property used in the farming business with a recovery period of ten years or more.

Qualified Business Income Deduction for Pass-Through Entities

Banks that are S corporations, and their clients that are pass-through entities – sole proprietorships, partnerships, and S corporations – may now benefit (or more correctly, their owners may benefit) from a 20 percent deduction from qualified business income, if they meet the requirements. The computation can be complicated and is subject to exceptions and limitations.

One of the limitations is that the deduction cannot exceed the greater of a) 50 percent of the taxpayer's share of W-2 wages from the trade or business, or b) 25 percent of the taxpayer's share of W-2 wages from the trade or business, plus 2.5 percent of the unadjusted basis of the taxpayer's share of qualified property.

Another limitation is that the deduction does not apply to income from a trade or business of being an employee, or from a "specified service trade or business," which includes any activity that involves the performance of services in the fields of health, law, accounting, actuarial services, performing arts, consulting, athletics, financial services, brokerage services, any trades or businesses the principle asset of which is the reputation or skill of one or more of its owners or employees (excluding engineering and architecture), or any business that involves the performance of services that consist of investment and investment management, trading, or dealing in securities, partnership interests, or commodities.

Taxpayers with taxable income that does not exceed $157,500 ($315,000 for married taxpayers filing jointly) are not subject to the W-2 wage or property limits or the exclusion for specified service businesses. Taxpayers with taxable income that exceeds these thresholds will have the limits phase in over the next $50,000 of taxable income ($100,000 for married-filing-joint returns). If the qualified business income for all trades or businesses is a net loss, the amount is treated as a loss from a qualified trade or business in the next year for purposes of calculating the following year's deduction.

Conclusion

These are just some of the many provisions in the TCJA that will impact banks, bankers, and their clients. Some of the changes, like the pass-through deduction and the changes to individual taxes, expire after 2025, while others, like the corporate tax rate and the interest deduction limitation, are permanent. But "permanent" might not be the right word, as the changes brought about by the TCJA show. ■

Graphic by vecteezy.com

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Changing Mortgage Interest Deductions: The Information Bankers Need to Know

By Zachary Thury

The Tax Cuts and Jobs Act (TCJA) signed by the President in December included significant changes to the rules surrounding the deductibility of home mortgage interest. Because of these changes and others included in the recent tax reform package, taxpayers will likely see fewer tax benefits related to their home loans starting in 2018.

Under the previous tax regime, taxpayers were allowed an itemized deduction for mortgage interest on loans with an outstanding principal balance of less than $1,000,000. In addition, taxpayers were able to deduct interest on home equity loans with principal balances up to $100,000. Across the country, many homeowners have historically taken advantage of these deductions.

Changes to Itemized Deductions

Beginning in 2018, taxpayers will be subject to the following changes that will limit the deductibility of home mortgage interest.

1. The maximum outstanding principal balance on home acquisition loans eligible for an interest deduction has been reduced from $1 million to $750,000.
2. The deduction for interest on home equity loans will be eliminated completely.
3. The standard deduction available to taxpayers will be roughly doubled, up to $24,000 for married couples filing jointly and $12,000 for individuals. With this increase, fewer individuals will be eligible to itemize their tax deductions and deduct their home interest.

Definition of a Qualified Residence

To be deductible, loans must be considered to be a "qualified residence." A "qualified residence" can include the taxpayer's principal residence and one other home selected by the taxpayer.

When a taxpayer has more than one home used as a principal residence during the year, the one used most often will typically be considered the primary residence. If there are multiple homes where this simple test may not apply, other key factors to consider include: place of employment; where family members make their place of abode; address shown on tax returns; driver's license; mailing address for correspondence and bills; location of bank accounts; location of doctors/service providers; and location of religious organizations or social clubs.

If the taxpayer owns multiple homes in addition to their primary residence, the taxpayer can designate only one additional qualified residence each year (which can be selected on an original or an amended return). For instance, if a taxpayer owns three homes – a primary residence, a lake home, and a ski home and each had an outstanding mortgage where the proceeds went directly to the acquisition of the property – the taxpayer could deduct the interest on the principal mortgage and either the interest on the lake home or ski home, but not both. The selection for the second home can be changed on an annual basis. This example assumes that the sum of the principal loan balances outstanding is under the $750,000 limitation and none of the properties are rented out.

Mortgage Interest Deductions continued on page 34

Taking Your Incident Response Plan Testing to the Next Level

By Tom Williams

According to the FFIEC, the major testing principles related to your Incident Response Plan (IRP) are as follows:

- Testing should be a continuous cycle and conducted annually at a minimum
- The testing program should be viewed by an independent party
- Test results should be compared against the IRP to identify gaps
- Size and complexity matter in testing
- Results should be reported to the board for approval

Although these are the stated principles, the question remains: What is the best method to truly stress test your IRP? Over the years, I have been directly involved in working with banks on both their IRPs as well as their Business Continuity Plans (BCP). A common challenge for most institutions is determining how to get out of the rut of the basic table-top exercise where team members sit around and discuss what-if scenarios.

To take your testing program to the next level, consider playing out your cyber-attack scenario as if it were a real situation. In other words, re-enact the situation from the time that the virus enters your network/systems, all the way through resolution. I have conducted these types of drills at banks across the country and I, as well as the participants, are amazed at how much more effective and fun they are.

There are five steps to this interactive testing approach:

1. Establish Test Objectives
2. Determine Test Scope
3. Identify Test Participants
4. Conduct the Test
5. Conduct Gap Analysis

Establish Test Objectives

Test objectives should be tied to improving the IRP as well as training employees on their roles prior to, during and after an incident. Another objective is to ensure you are meeting the bank's regulatory requirements. Review your current IRP to identify holes that need to be addressed. For example, a common exposure point for many banks is the process of making a claim with their cyber-insurance company. Although it is listed in the IRP to contact the insurance company, many banks are not aware of the process of making a claim, or what their actual cyber coverage really is. As part of the drill with one bank, the bank learned that their insurance carrier required them to notify the insurance company immediately when the attack presented itself. This way the carrier could get directly involved with assigning a team to assist in resolving the incident. Without the drill, a real incident would lead the bank deep into its response prior to contacting the insurance carrier, which could have jeopardized its ability to file a claim.

Also review the results from your previous tests to address any unresolved issues and to ensure that the proper solutions are now in place. If test objectives from your previous test were not met, they should carry over to this test and be resolved.

Determine Test Scope

This is where we identify the premise of the test and the impact it will have on the bank's customers, employees and shareholders. This is also where we determine our cyber-attack scenario, i.e. ransomware, DDoS, customer information stolen and sold on the dark web, account takeover, social engineering attack, etc. The scenario should be based on real-world potential threats that your bank may encounter based on the risk assessment. Other things to consider in this step include the duration of the incident and whether the attack takes place over one day, or several weeks. Develop a time-line for when the event will occur and when follow-on activities will take place. Determine who will be impacted by the incident, i.e., IT, operations, customers, employees, community, etc. You should also consider how the incident will be resolved. For example, in a ransomware situation will the bank pay the ransom, or will they not pay the ransom and go through the process of rebuilding and recovering from their backups?

Another critical component is to provide situational challenges to the group. The challenges should be based on the business unit that is impacted by the outage. For example, in a ransomware scenario where the domain controller is encrypted and users are unable to log on, a challenge for the call center could be discussing how they would handle customer transfers, or reset passwords for online banking. The call center personnel attending the drill would have to document their response to the challenge and what resources are needed to complete the challenge. This would assist in identifying exposures and what is required to complete a similar challenge in a real-world situation. The challenges should be developed ahead of time and provided on a sheet of paper so that the responses can be documented. Consider 5-10 challenges per department and have a set of challenges for the executive team.

Incident Response Plan Testing continued on page 24

2018 Pioneer Banker Nomination

The MBA is proud to recognize MBA member bankers who have been leaders of the industry for 50 years or more. All eligible nominees will be inducted into the MBA Pioneer Club at a luncheon during the MBA Annual Summit on June 12, 2018, at Madden's Resort in Brainerd, Minnesota.

Who is eligible for induction into the Pioneer Club? Any Minnesota banker working for an MBA member bank who has attained at least 50 years of active service by June 30, 2018, is eligible. U.S. military service counts in the 50-year span if the individual was in banking prior to and subsequent to the time spent in the military. Years after retirement in which the candidate works part-time for a bank as a consultant or as a member of the Board of Directors may be counted toward the 50-year total; however, these must be the principal endeavors of the candidate.

You can find the nomination form on our website or as an insert in this month's *MBA News*. ■

Nominations for MBA Vice Chair/Treasurer

The Minnesota Bankers Association Nominating Committee invites your suggestions for a nominee for MBA Vice Chair/Treasurer for 2018-2019.

For the 2018-2019 year, the Committee will nominate a banker for the position of Vice Chair/Treasurer, to be elected at the Annual Summit on June 12, 2018. The Vice Chair/Treasurer will succeed to the office of Chair, and then to Past Chair.

Enclosed with the *MBA News* is a form for your use in suggesting a candidate for Vice Chair/Treasurer. We have asked that background information be included concerning bankers under consideration by the Committee. As always, past and current involvement with the Minnesota Bankers Association or our industry is important. The Committee will receive nominee suggestions until March 15, 2018.

We appreciate your careful consideration of qualified future leaders for MBA. Feel free to contact any of the Committee members if you have questions or comments.

Members of this year's Committee are Gail Mikolich, Northeast Bank, Minneapolis (Chair); Steve Daggett, Midwest Bank, Detroit Lakes; Steve Huston, BANKWEST, Rockford; Paul Pieschel, Farmers & Merchants State Bank, Springfield; and Dean Toft, HomeTown Bank, Redwood Falls. ■

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2018 MBA ANNUAL SUMMIT

June 10-12, 2018 | Madden's on Gull Lake, Brainerd

SAVE THE DATE!!

Counsel's Corner

Michael Thro
MBA Associate Counsel
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What happens upon the death of the owner of a health savings account?

When opening a health savings account (HSA) a beneficiary should be designated. If the HSA owner's spouse is listed as the beneficiary, then upon the death of the owner it will be treated as the surviving spouse's HSA. If the beneficiary is not a spouse, then upon the death of the HSA owner the account stops being an HSA and the fair market value of the HSA becomes taxable to the beneficiary in the year in which the HSA owner dies. If no beneficiary is listed, then the value is included on the final income tax return for the HSA owner. IRS Publication 969 addresses this.

What should banks do with counterfeit currency?

The bank should contact the local office of the Secret Service. The Minneapolis office can be reached at 612-348-1800.

Is there any way to streamline the process for getting the contents of a safe deposit box to the heirs such as a POD or access upon death document?

Safe deposit box customers rent the box from the bank. Because of this lessee/lessor relationship the customer doesn't actually own the box and cannot convey the contents of the box to a beneficiary. While a few states allow safe deposit box renters to appoint someone to access the box upon the renters' death, Minnesota does not have a law like this.

In the event of a snow storm, or other weather-related emergency, can the bank close early?

Minnesota Statute § 47.0153 states that the officers of a financial institution have the discretion and authority to close early or not even open during an emergency. Minnesota Statute § 47.0151 states that an emergency includes, but is not limited to, fire, flood, earthquake, hurricane, wind, rain or snow storms.

Are banks in Minnesota required to pay interest on escrow accounts?

Interest is only required to be paid on escrow accounts that were established prior to July 1, 1996.

We received a check that had the numerical value of the check, i.e. $100, but it was not written out, i.e. one hundred dollars. Is there a requirement that the amount appear as a number and written out?

There is no requirement for there to be anything written out. Only one of the amounts is required. Generally, most check recognition software can recognize the numerical value. The written value is important when the two values contradict each other. In that instance, the written value is the one used. ■

For more information and members only information on legal matters in banking, log onto minnbankers.com, and click on "Legal and Compliance."

Compliance Query

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How are we supposed to disclose multiple collateral transactions on the TRID forms?

The answer depends on the type of collateral involved in the TRID transaction. For TRID transactions secured by multiple real properties, all such real properties must be included on the TRID forms. If there is insufficient space on page one of the TRID form to identify all real properties securing the loan, then the bank must provide an addendum listing the remaining real properties that could not fit on page one of the TRID form. For TRID transactions secured by real property and personal property, the bank must include all real properties and may include personal property as space allows. In other words, personal property securing a TRID transaction may only be identified on a TRID form if there is sufficient space to do so on page one of the TRID form. Personal property collateral should never be added to any addendum to a TRID form. You can find a discussion of these in comments 2 & 3 to 12 CFR 1026.37(a)(6) and comment 2 to 12 CFR 1026.38(a)(3)(vi).

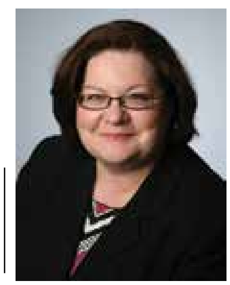
Will the examiners take it easy on us while we implement the extensive data reporting changes under the Home Mortgage Disclosure Act (HMDA) in 2018?

Yes, all four federal banking agencies have committed to a diagnostic mindset for any examinations of 2018 data that will be reported in 2019. This means that their examinations will focus on identifying weaknesses in a bank's program, but not with an eye towards requiring data resubmission and civil money penalties. All four agencies do note that data resubmission may be necessary where the data errors are material. Access the CFPB's announcement online at: https://www.consumerfinance.gov/about-us/newsroom/cfpb-issues-public-statement-home-mortgage-disclosure-act-compliance/. Access the FRB's announcement online at: https://www.federalreserve.gov/supervisionreg/caletters/caltr1704.htm. Access the FDIC's announcement online at: https://www.fdic.gov/news/news/financial/2017/fil17063.pdf. Access the OCC's announcement online at: https://www.occ.gov/news-issuances/bulletins/2017/bulletin-2017-62.html.

Are there any other HMDA-related requirements due to the data reporting change beside the new HMDA Notice of Availability?

Yes, on November 24, 2017, the federal banking agencies published a final rule that, among other things, amended the Community Reinvestment Act (CRA) Public File requirements. For banks that report HMDA data, the CRA Public File must now include a written notice that the bank's HMDA Disclosure Statement may be obtained from the CFPB's website at: www.consumerfinance.gov/hmda. In addition, if the bank elects to have an affiliate's lending considered in its CRA testing, then the bank must include a written notice that the affiliate's HMDA Disclosure Statement may be obtained from the CFPB's website at: www.consumerfinance.gov/hmda. These changes are effective January 1, 2018, and the updates to the CRA Public File requirements should be reflected in bank's CRA Public File by no later than April 1, 2018, as required by 12 CFR 25.43(e), 195.43(e), 228.43(e) and 345.43(e). Access the full final rule online at: https://www.gpo.gov/fdsys/pkg/FR-2017-11-24/pdf/2017-25396.pdf. ■

Ask the Agent



Connie Mack
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I have Basic Life insurance through the MBA Life Plan and would like to know if I can list my minor child as a beneficiary? What happens if I don't name a beneficiary?

If a beneficiary is a minor at the time the insurance proceeds are payable, the proceeds will be disbursed in one of the following ways:

1. To the legal guardian of the minor beneficiary's financial assets;
2. To an adult responsible for the well-being of the minor beneficiary if permitted under any applicable Uniform Transfer to Minor Act; or
3. The insurance proceeds will be held by the carrier until the minor beneficiary is of legal age (based upon state law) to receive the payment.

If there is no named beneficiary, the proceeds will generally be paid to the first of the following: the surviving spouse; surviving children in equal shares; surviving parents in equal shares; surviving siblings in equal shares; the estate. ■

For a full list of MBA's insurance offerings, log on to minnbankers.com and click on the "Group Insurance" button.

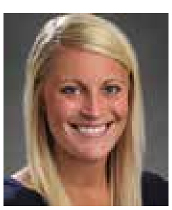
Community Bank Owatonna and its Board of Directors are pleased to announce **Jeff Goergen** as the bank's new Vice President. Goergen began his new role on January 2, 2018. Goergen is an Owatonna native and has over 25 years of banking experience, with the last 21 years serving the Owatonna community. He has a passion for providing community banking services to the Owatonna market. Goergen is actively involved in coaching youth athletics in the Owatonna community where he resides with his wife Rhonda and their two sons, Isaac and Kyle.

Kensington Bank recently announced several promotions and new positions:

The bank announced the promotion of **Dan Robertson** to President and CEO. Robertson is a 17-year veteran of the financial industry. He joined Kensington Bank in 2012 as Bank President in Cokato. Kevin Noble, Chairman of the Board, shared these comments on Robertson's appointment to CEO – "Dan has a unique combination of strengths that make him ideally suited for his expanded role. He is a strategic thinker, has a solid understanding of the financial and technical side of the business and is very driven to succeed. Our Board is very pleased to have Dan Robertson as our new CEO."

Jon Hall was appointed the Bank's Chief Credit Officer. Since 2007, Hall has served as the Bank's CEO. "Jon's leadership and expertise are highly valued by the Bank. In his new role, Jon will utilize his extensive credit knowledge to support the Bank's loan growth goals," said Robertson.

Timothy Stewart joined the Bank as Director of Marketing/Retail/Business Development. Stewart brings over a decade of experience in the financial industry and sales management. "The St. Cloud market is filled with tremendous opportunity," said Robertson. "Tim's knowledge and expertise in financial business development, and in the St. Cloud market area, are great assets to the Bank."



Kensington Bank also welcomed **Kayla Hall** as the new Marketing Specialist/Business Development. Hall has over five years of experience in the financial and marketing industries. "Kayla brings creativity and energy to her position. She will play a key role in continuing our goal of providing best-in-class service and tailored financial solutions to the communities we serve," according to Robertson.

KleinBank recently announced the hiring of **Jeffrey Williamson** as SVP Residential Mortgage Lending. Mr. Williamson has 18 years of mortgage lending experience with financial institutions in the Twin Cities. Mr. Williamson earned a Bachelor of Arts degree from Bethel University in St. Paul. He is the father of three children and resides in Minnetonka with his wife, Joelle.

National Bank of Commerce (NBC) announced the promotion of **Cammy Hansen** to VP – Community Banking Director.

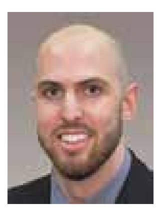
Cammy is a native to Duluth with over 25 years of experience in the banking industry with the last six of those being at NBC. She is involved with Duluth LISC as a board member and chair of the grant and loan review committee, a chair-elect of Safe Haven Shelter and Resource Center board of directors, sustaining member of Junior League of Duluth and a 2005 Leadership Duluth graduate. She also plays a role in other non-profit organizations. In this role, she will be responsible for developing and implementing sales strategies to encourage portfolio growth while managing the sales team of tellers, retail and mortgage bankers.

National Bank of Commerce (NBC) also announced the promotion of **Tim Smith** from Credit Analyst to Commercial Banker. Tim was born and raised in Superior, WI. He attended college at the University of Minnesota Duluth, where he earned his Bachelor's degree in Accounting and Political Science.

Tim joined NBC three years ago as a Credit Analyst where he continued to grow and expand his knowledge of the financial industry.

Eagle Valley Bank in Stillwater is pleased to announce the promotion of **Justine Seidel** to AVP – Commercial Lending.

In her new role, Ms. Seidel will be responsible for helping support the bank's growing loan portfolio by maintaining and developing client relationships. Ms. Seidel has eight total years of banking experience and is a graduate of Metropolitan State University with a degree in Business Administration.



Bridgewater Bank in Bloomington recently welcomed **Jordan Marriott** to its lending team as Vice President. Jordan joins Bridgewater Bank with a strong lending background and has held a variety of positions at local banks in commercial and industrial (C&I) lending, SBA lending and general business lending. Jordan holds a degree in Finance from the University of Minnesota Duluth.

Eagle Valley Bank, a growing Twin Cities bank focused on businesses and entrepreneurs, is pleased to announce the promotion of **Aaron Siegle** to President effective July 1, 2018. In his role as President, Siegle will focus on Sales and Marketing, Shareholder Relations, and assisting John Seidel, the CEO, in the daily operations of the Bank.

Siegle joined Eagle Valley Bank in 2013. Prior to that, he was an examiner for the FDIC where he oversaw financial examinations of banking institutions. Siegle is a graduate of Concordia College, Moorhead, MN, and the University of North Dakota School of Law, Grand Forks, ND.

Gateway Bank announced five promotions at its annual holiday party. President Bruce Downey said "We are extremely blessed to have a great group of associates at Gateway Bank. These promotions reflect the excellent job these associates are doing for our clients. It is very gratifying to continue to promote from within the organization.

Kelly Gibbons to Credit Analyst I. Kelly joined the bank in 2016 as a loan operations associate. He is a graduate of Iowa State University and Eastview High School in Apple Valley.

Felicia Le to Universal Banking Officer. Felicia joined the bank in 2015 as a Universal Banker and moved to the new Edina location in July of 2017. She is a graduate of the University of St. Thomas and Burnsville High School.

Carol Lund to Senior Operations Associate II/ Operations Lead. Carol has been at the bank for 11 years starting as a Teller Operations Associate. Carol lives in Eagan.

Elisa Dabruzzi to Assistant Vice-President Commercial Lending. Elisa joined the bank in 2011 as an Operations Associate. She is a graduate of the University of Wisconsin in Madison and Hastings High School.

Becky Durand to Assistant Vice-President Business Banking. Becky was the first associate to join Gateway Bank when it was being formed in 2003. She has worked her way up from Banking Associate to officer and now this promotion. Becky lives in Eagan.

Stearns Bank National Association announced that **Kelly Skalicky**, daughter of Stearns CEO Norm Skalicky, was recently promoted to President of the organization. Kelly is uniquely qualified to ensure a strong future for Stearns. From spending Saturday mornings with her dad at the bank, to earning her law degree and providing legal counsel to Stearns for more than 20 years, to serving as General Counsel for Stearns Bank for the last six years, Kelly has spent her life learning the intricacies of the banking industry.

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Identify Test Participants

This is the step that sets this type of drill apart from a general table-top drill. There are three pools to consider in selecting participants: (1) bank staff; (2) vendors; and (3) support organizations, e.g., regulators, media, fire, police, etc. Some of the most successful drills that I have conducted with banks are those where vendors and support organizations were involved. At one drill where the disaster scenario was a tornado, the local emergency manager participated and provided critical information on how the local authorities would coordinate rescue efforts and prioritize power restoration. He also provided information on how to develop a family disaster plan for individuals.

I have found that role-playing is another critical element of taking your testing to the next level. Be creative and identify bank personnel to play certain roles during the drill. For example, have someone play the role of an angry customer who has been notified that their Personally Identifiable Information (PII) has been compromised and is now in the hands of a hacker, or being sold on the dark web. The customer is now at the branch demanding to talk with the branch manager. Have someone play the role of a news reporter whose station has been notified that the bank has been compromised. They are now at the main office requesting a response from the CEO. Role playing not only puts individuals in a position that they must deliver, it forces them to want to do better so that in a real-world situation they are better prepared. This also drives buy-in at the individual and business unit level while increasing the fun factor.

Conduct the Test

After the planning has been completed, it is now time to conduct the test. The planning should be limited to just a few individuals and they should not disclose the drill scenario to any of the drill participants. Allow for 2-4 hours to conduct the drill, depending on the number of participants. I would suggest that the 1st round of testing be conducted for the senior team and at least two members from each business unit. When conducting the drill use dates and times to chronologically step the participants through the event. Start out giving the scenario, then provide the challenges based on when they occur on the drill timeline. Do not give out the challenges all at once; rather, give them out based on the events unfolding. Have someone take notes of the drill to review later. The idea is to have fun but remain serious throughout the drill.

Conduct Gap Analysis

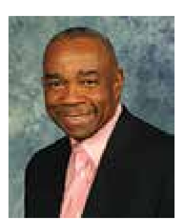
The final step is to compare your test objectives with your test results. For those objectives that were not met be sure to document the reason why and what is required to fix the issue. Review all the completed challenges to determine the required resources associated with each challenge. Because the drill is somewhat fast-paced, there may not be enough time for the participants to complete the challenges with detail. Give the participants an opportunity to take the challenges with them and complete them with their department personnel, and return them to the drill coordinator within a week. Be sure to gain feedback from each participant on what could be done to improve the IRP from their perspective.

The last step is to prepare a report to the board on the results of the test. Include the original test objectives and if the objectives were met. If they were not met list the action plan to get the objectives met. This report could also be used for your examiners as well.

Hopefully, I have provided you with some additional insight on how to enhance your IRP testing. The overall idea is to put some drama to the exercises and to have fun as well. This approach has worked for many banks because they are more interactive and get more people at the bank involved and educated on cyber-security.

Remember, a test that fails might be the most instructive test of all. ■

Editor's Note: This article previews some of the expertise and insights you'll hear from Tom Williams and other great presenters at this year's MBA Operations & Technology Conference on April 17 & 18. For the full agenda and to register, go to www.minnbankers.com and click on the Education tab.



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Resolve to Get Your Findings Organized in 2018 with 3 Easy Tips

By Michael Berman

People love to make New Year's resolutions, but they aren't so good at keeping them. Statistics suggest that as many as 80 percent of New Year's resolutions are broken by the second week of February. That means most resolutions have already fallen by the wayside. But it's not too late to set new goals and try again with a more effective strategy.

There's a lot of reasons resolutions go wrong, but one of the biggest obstacles is that our resolutions require us to actively make changes when we're used to running on autopilot. We're used to eating that afternoon snack, splurging on that cup of coffee, or sitting on the couch when we get home. We're used to running our meetings or handling tasks a certain way. Our habits are ingrained, and our minds are programmed to do what they've always done, good or bad. Life is busy, and our default mode is autopilot.

The secret, then, to keeping a resolution is to make it easy. The less you have to actively do, the more likely you are to succeed. This may not be particularly helpful when it comes to typical resolutions like eating more healthfully, exercising more often, or saving more cash, but it can work in your favor when it comes to getting organized, specifically with your audit and exam findings.

With a little upfront work, 2018 can be the year you get your institution's audit and exam findings organized. Just follow these three tips:

Tip #1 Centralize your findings data.
Is your findings management a pastiche of spreadsheets, documents and emails? Are people across your institution using their own individual approach to findings management? Tracking all these pieces is time consuming, not to mention unreliable. If just one person fails to update the document or if they make different versions of the spreadsheet to keep on their computer, then it can create a mess. Enter the data once and use it everywhere. It's not just more accurate, it's easier and more efficient. One and done.

While implementing a centralized system will take time and effort upfront, requiring you to fight the inertia for a short period, it will ease your workload going forward.

Tip #2 Allocate tasks.
Unless someone really cares about a problem, it won't get fixed. The best way to make someone care is to assign them responsibility. Don't just mention it in a meeting where it might be easily brushed off or forgotten. Communicate it in writing and keep it with your centralized data. Clear lines of responsibility promote action. As an added benefit, delegating tasks will help remove some of the heavy lifting from your own plate, freeing you up to work on big picture items that can be hard to find time for.

Tip #3 Automate task management.
You know when I'm most likely to remember that something needs to be done? It's when I have a few quiet minutes to think. These come to me at the most inconvenient times, like driving to work or in the shower, when there is no easy way to take action, then I forget about it.

Yet I never forget a meeting. That's because I set reminders. Apply that concept to findings management with automation. Find a method that makes it easy to assign, track, and remind task owners what needs to be done and when. It should also make it easy for task owners to log their work. It's hard to find the time to check in with each team member and remember what they are supposed to be doing. It's much easier to find a few minutes to check a centralized, automated task management system to see if you and your team are on track. And it should give you the reminders to make sure you do it instead of forcing you to override your personal autopilot and remember.

Once implemented, these tips will make life simpler and easier, which gives you a real shot at achieving your get-organized resolution. There'll be no more hunting down answers, no more wondering what got done, and no pressure to remember what needs to be done next. It'll all be in one place with proactive reminders of what step is next.

If only all resolutions could be that simple. ■

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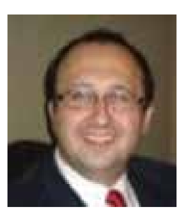

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Best Practices for Bank Websites

By Dawn Koranda

Super Studio is looking forward to presenting website design best practices at the Minnesota Bankers Association Operations and Technology Conference in Alexandria this April. The following is a look into our presentation.

Your website is a combination of many customer experiences happening very quickly or even simultaneously. Many times, you only have a few seconds to show visitors who you are, why you are here, and what they need to do next. That is why it is critical to build trust with your audience. If a customer does not feel a site is secure, they won't do their online banking there. A carefully and strategically designed website can help the customer feel secure by creating a comforting, welcoming and trustworthy environment.

Before a website can be designed, search-engine-optimized website content and a complete information architecture must be strategically created to ensure messaging is clear and users have the best experience possible.

The website design process begins with asking questions. Who is your audience? What are you trying to tell your audience? Do they know who you are, or do you need to introduce yourself? These questions can all revolve around some main themes – brand consistency, clarity of your messaging, security and the power of customer confidence, and the importance of accessibility.

Brand Consistency

Your website is a digital representation of your brand. It should give comfort to visitors that you are trustworthy and clear in your communication. Regardless of whether your customers are interacting with you in your physical location or online, your brand begins and ends with customer relations and satisfaction. Your company brand extends beyond visuals – it's also defined by your messaging. What do you want to say, and how do you say it? How does that message make the customer feel? That message is as unique as your brand. To align with the brand message, the key to building trust and giving a satisfying user experience within the design is brand consistency. The selective use of colors, typefaces, images and content layout is critical in tying the brand message to the visual representation of your brand. By aligning the two, your website will build the trust and comfort necessary for a customer to feel safe and secure while using your site.

Clarity

When writing content and laying out that content for design, the main focus should be on clear messaging and the prioritization of content. Your design must give your customer's eye a place to go. The content should be ordered clearly on the site and with a definitive sense of information hierarchy. For example, you should place important login information and valuable news information near the top of your site. When writing for the web, avoid using loaded language and superfluous words. The idea is to use plain language to guide the users in finding what they need, understanding what they have found and eventually using that information to make a decision. Design helps by placing that important information at high priority – using layouts that help inform the user rather than confuse them. Overall, be clear in telling and showing your customers what they are looking at, what they need, and where (and how) to find it.

Security and the Power of Customer Confidence

A key consideration in web design for financial institutions should be generating trust and a sense of security among users. Customers need to know that they are taking the correct action and that they are safe doing it. The customer should never question whether it's safe to click a button. Avoid using pop-ups or intrusive page overtakes. A consistent and concise design assures the customer that their information is secure and private.

Your brand plays a crucial role in customer security. If the customer feels confident in your brand, and if your brand is represented in a consistent and clear way, customers will have more confidence in their actions. Use clear messaging to inform the user, and use thought-out design to guide the user in understanding the message and what to do with that information. Clarity and consistency build customer confidence.

Accessibility

Another top priority that affects how your content is written and structured is accessibility. In general, web accessibility standards are here to give users the best possible experience no matter their limitations or disabilities. In terms of design, contrast is key. Fonts should be easily readable and line length should be short and digestible. Colors should be used carefully and clear in their utility. Your website should be easy to use by all, and just like your messaging, accessibility depends on clear, thought-out practices. Website accessibility also relates to the responsiveness of your design. Many users will be coming to your site from a mobile device. Knowing how your content will be laid out across different screen sizes will ensure that the prioritized information on your desktop site will be the same across devices.

Designing a website can be a daunting project, but a small understanding of these practices will make a huge difference in the confidence, security and overall experience of your customers. Following these best practices when writing and designing your website will make your site consumable by the widest-possible audience. ■

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Why Taking a Strategic Approach to CECL Will Help Maximize Shareholder Value

By Adam Mustafa

It's time to get ready for the new accounting standard that will be used to calculate loan loss reserves. Even though the current expected credit loss (CECL) model won't go into effect until 2020 for public banks, banks should be preparing already.

And that means all boards of directors and members of the C-Suite should become familiar with the standard and how it will affect their banks going forward. But they shouldn't view CECL simply from a compliance perspective.

The primary goal should be to maximize shareholder value, with compliance serving more as a prerequisite. In other words, the main objective should be making sure the reserve for credit losses is just right – not too large and not too thin.

Every extra dollar in the loan loss reserve on day one is one less dollar of capital and as much as two fewer dollars of shareholder value (using a 2x tangible book value multiple). It gets worse; every excess dollar of loan loss provisions following implementation of CECL is one less dollar of profitability and ten or more fewer dollars of shareholder value (using a 15 to 18x price/earnings multiple and a 35 percent tax rate).

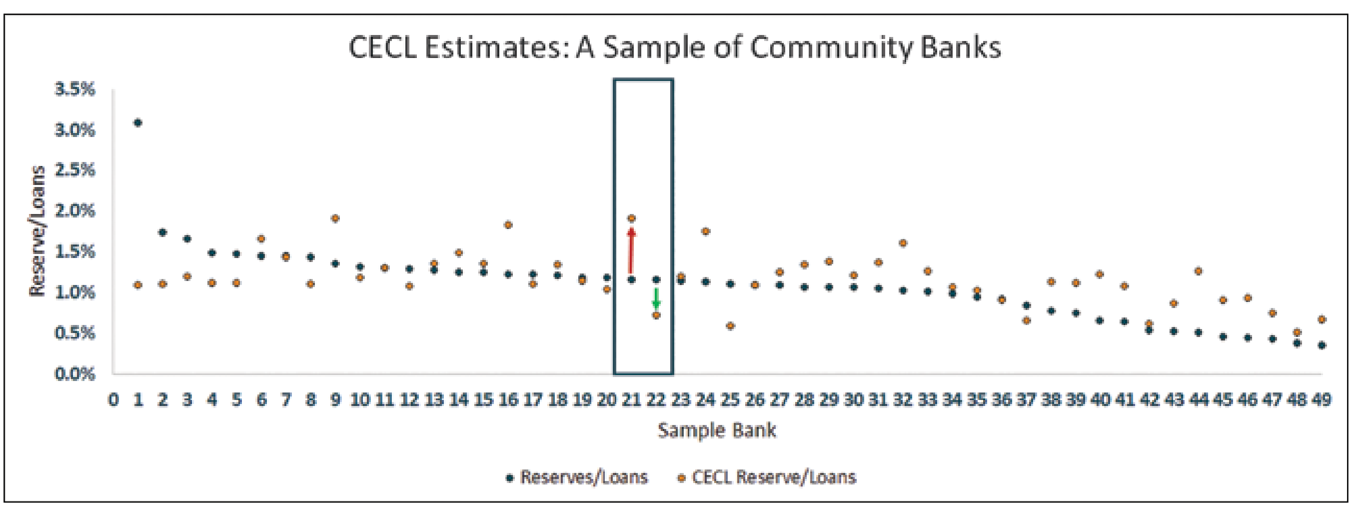
The reality is that community banks are creatures of their own unique footprint, business model, mix of loans and underwriting philosophy. As a result, CECL should affect each community bank's reserve differently; some banks should see no material impact, and perhaps even a decline, while other banks might experience a spike.

To illustrate this, Invictus used BankGenome™, its proprietary bank intelligence, to analyze the potential impact of CECL on the reserves of all banks attending a recent conference. The results, shown in the chart below, demonstrate the impact of CECL on bank loan loss reserves as a percent of gross loans for the quarter ending June 30, 2017.

Notice how Bank 21 and Bank 22 have similar loan loss reserves using today's incurred loss methodology standard. However, under CECL, Bank 21 should see its reserves significantly increase, while Bank 22 should see a decrease. It would be unreasonable for Bank 21 to see its reserve increase at the same rate as Bank 22 under CECL.

Back in 2012, the OCC projected that CECL would increase loan loss reserves by between 30 and 50 percent. Unfortunately, auditors and regulators have embraced that misleading expectation. The OCC analysis was primitive, calculated at a point when the economy was in the early stages of its recovery and the bulk of the loans in banks' portfolios consisted of riskier pre-crisis vintages. Still, the banks that should benefit from CECL implementation are going to be under increased scrutiny to support and defend their calculations, primarily because of those early predictions.

There is a solution. Banks must be aggressive, willing to become an industry leader before there is a consensus on best practices.



In our view, banks should view CECL holistically, taking into account the intersection between strategic planning and capital planning. Community banks have used capital stress testing results to persuade regulators to lower their capital ratios and justify their concentration limits.

They will need to be able to muster similar evidence to optimize their reserves under CECL.

There is a trade-off between simplicity and the strength of a bank's case to defend its reserve levels. Banks that understand the critical implications of CECL on strategic planning will rise to the top, as long as they use a proper, forward-looking methodology that leverages loan data and industry data in the smartest way possible.

In CECL modeling, not all methodologies are created equally. We believe a bank's underwriting standards should be combined with a vintage approach to optimize the CECL calculation. The data must be forward-looking and take into account the unique aspects of each bank's loan portfolio.

Done right, CECL will not require most community banks to increase their loan loss reserves. We believe that the proper approach to CECL is to integrate it with strategic and capital planning, so that banks understand the implications of the standard on everything they do. Compliance isn't good enough. Banks that take an aggressive approach to CECL, and come up with data to support their case, will maximize their shareholder value and gain a competitive advantage. ■

Adam Mustafa is the president of the Invictus Group, a data-driven strategic intelligence firm that specializes in CECL readiness, M&A advisory services, stress testing and capital planning.

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Applications must be received by March 30, 2018.

MBA Honors Thirty-Eight Banks for Their Community Involvement

The MBA recently recognized 38 Minnesota banks for their community involvement. Banks play a vital role in their communities, and to honor and recognize their involvement, the MBA created the Community Champion Recognition program.

The 38 banks recognized as 2018 Community Champions worked with hundreds of organizations in their communities, providing funding, volunteers, materials, supplies, or food for their neighbors. Recipients of the recognition range in size from small community banks to large banks with multiple branches.

In total, these banks donated over $2.2 million to over 900 organizations including the American Red Cross, Habitat for Humanity, United Way, Salvation Army, American Cancer Society, Ronald McDonald House, Special Olympics, Minnesota Business Venture, local schools, churches, and non-profits. 1,941 employees from these banks dedicated over 59,000 hours at a variety of volunteer events and programs.

MBA President/CEO Joe Witt congratulated the recipients. "This extraordinary level of volunteer participation by Minnesota banks demonstrates their deep commitment to the communities they serve," said Witt. "In addition to providing the capital that helps families and local businesses thrive, the banking industry's record of supporting local programs is second to none. The MBA is pleased to recognize these 38 banks for their commitment to making a real difference in their local communities."

2018 Community Champion Recipients

Americana Community Bank
Maple Grove, Sleepy Eye, Chanhassen

Anchor Bank, A Division of Old National Bank
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If you have a positive working relationship with a business that other bankers could benefit from, please have them contact Nicole Hanger at the MBA at nicoleh@minnbankers.com or 952-857-2630.

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AWARDS

Winona National Bank is pleased to announce Teller **Shelby Reinert** as the recipient of its 2017 fourth quarter Community PRIDE Award.

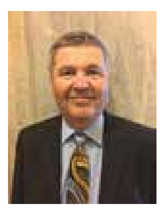
Awarded quarterly by the Bank's Public Relations Committee, Community PRIDE Awards recognize WNB employees for exceptional volunteer service to programs, organizations, and initiatives that contribute to the strength and vitality of the communities served. This includes volunteering efforts made both during and outside of work hours.

In 2017, Reinert dedicated 113 hours to a student through the Miller Mentoring program at Winona Senior High School. Partnered together for two years, Reinert has helped the student with academic goal setting, completing homework, building communication skills, and boosting self-confidence.

As a Community PRIDE Award recipient, Reinert received $100 to donate to the non-profit organization of her choice, which she chose to donate to Miller Mentoring. In addition, she received a certificate of recognition and a Winona National Bank logo shirt.

BOARD APPOINTMENTS

The Bank Holding Company Association (BHCA) is pleased to welcome two new board members, **Michael J. Finley** and **Harry Wahlquist**. They were elected at the 2017 BHCA Fall annual meeting and their three-year terms started on January 2, 2018.



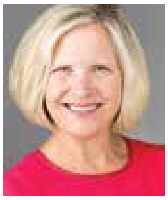
Finley is vice president of Janesville Holding Company, in Janesville, Minnesota, which owns the $70 million Janesville State Bank; Finley is also the bank president.

He graduated from St. John's University, Collegeville, Minnesota, with a Bachelor of Business Administration, and from the Graduate School of Banking at University of Wisconsin – Madison. Finley was an examiner with the Federal Reserve Bank prior to joining Janesville State Bank.

Wahlquist, a graduate of Carleton College, Northfield, Minnesota, is the founder, president and CEO of Midwest Bancorporation, which owns the $260 million Star Bank. The bank's charter is in Maple Lake, Minnesota.

Wahlquist began his banking career at the Northwestern National Bank of Minneapolis, predecessor to Wells Fargo, where he managed the Midwest Banking and Correspondent Banking Departments in the Ninth Federal Reserve District.

First State Bank and Trust is excited to announce the appointment of **Melanie Sullivan** and **Chris Galvin** to its Board of Directors after the retirement of two long serving Directors.



Melanie Sullivan is the Chief People Officer at Constellation Mutual and an Adjunct Professor – Health Services Management at the University of Minnesota. She holds a Doctor of Education, Organization Development degree from the University of St. Thomas and a Masters degree in Business Administration from the University of Phoenix, Denver, CO.

Chris Galvin is Senior Vice President of Manufacturing and Logistics for Andersen Corporation where he is responsible for the company's operational excellence including manufacturing, facilities, logistics and supply chain integration. He holds a Bachelor of Science degree in Finance from the University of Wisconsin-La Crosse and a Masters of Business Management from the University of Minnesota's Carlson School of Management. ■

If you have an announcement you would like to include, please send it to Eric Hauth at erich@minnbankers.com. Also look for *Bankers on the Move* in the "Human Resources" section of minnbankers.com.

Kent Kircher

Kent Kircher of Spicer, formerly from Olivia, died Monday, February 5, at Rice Memorial Hospital at the age of 75.

Kircher was president of the Citizens State Bank of Olivia until 2014, and was a member of the Minnesota Bankers Association Pioneer Banker Club.

A memorial service was held Monday, February 12, at Cross of Calvary Lutheran Church in Olivia. Burial will be at a later date in Olivia Cemetery.

In lieu of flowers, memorials are preferred to the University of Minnesota Foundation for Cancer Research, Rice Health Foundation, and The Bethesda Foundation. ■

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Definition of Acquisition Indebtedness

In addition, to be deducible a loan must be "acquisition indebtedness." This means that the debt is secured by a qualified residence of which the proceeds of the loan are directly traceable to acquiring, constructing, or substantially improving that home. If a taxpayer takes out a first mortgage and uses the proceeds for something other than the purchase of the home (e.g., to buy a boat), then that mortgage interest is not deductible on Schedule A of their tax return.

In order to conform to the law, the debt is considered secured by a qualified residence only if the residence is specific security for payment on the debt; in the event of default, the residence could be foreclosed on to satisfy the debt; and the security interest is recorded or otherwise perfected under state law, whether or not the deed is recorded.

Grandfathered Loans and Larger Dollar Loans

Acquisition loans on qualified residences made prior to January 1, 2018 are grandfathered under the new tax law. Interest on those loans will continue to be deductible going forward on principal balances up to $1 million. This can be an important planning point when taxpayers are determining whether or not to purchase a new home and may be a reason to consult their tax professional.

Under both the old and new laws, having a home mortgage with a principal balance over the limitation does not completely eliminate a taxpayer's ability to deduct their mortgage interest. Instead, taxpayers are able to deduct only a portion of their loan interest representing the interest on the loan principal up to the threshold. There are different methods available for calculating the allowable deduction and taxpayers should consult with their tax advisors regarding their options.

Home equity indebtedness is not grandfathered under the new law and the interest on those notes will be non-deductible starting in 2018 regardless of deductibility in prior years.

Conclusion

These changes can have a significant impact on the taxpayer's treatment of mortgage interest and on their financing decisions going forward. Bankers will want to be well versed in these changes so they can answer customer questions when they arise. Ultimately, it will be up to the taxpayer and their tax professional to determine if the mortgage interest paid qualifies for a deduction on an annual basis. ■

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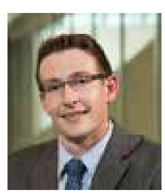

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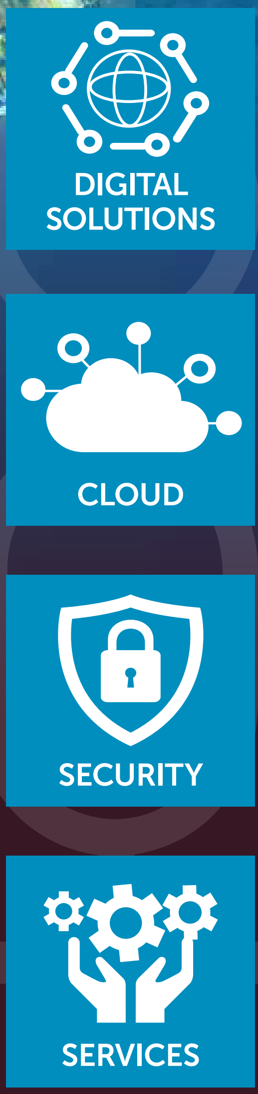

Mid-State Auto Auction
since 1983

We'll sell your repos, so you can get back to banking.

Transportation

We pick up vehicles right at your bank or the impound lot in all of Minnesota, North Dakota, eastern South Dakota, and western Wisconsin.

Selling

We hold an auction every Friday (52 sales/year). To get the best results for our financial institutions, MSAA runs all repos at the top of our busiest lane when buyers are eager to buy, and Dee, our Repo Manager, personally represents each unit during the auction.

Services

- Full detailing and de-identifying department
- Full-time mechanic on staff
- Full condition report with pictures
- Market reports available to estimate values

About Us

With over 34 years in the business, MSAA has built a huge buyer base that will purchase your repos. We pride ourselves on being a family owned and operated business committed to service, integrity, and value. What's more? We have the lowest rates in the state of Minnesota.

Contact us today for an easy process and great results!

Dee Sullivan
Fleet, Lease, and Repo Manager
dee@msaanym.com
800-458-5506

Mid-State Auto Auction | 310 Bach Avenue, New York Mills, MN 56567 | www.msaanym.com

January 1, 2018

Dear Minnesota Banker:

The Minnesota Bankers Association Nominating Committee invites your suggestions for a nominee for **MBA Vice Chair/Treasurer for 2018-2019**.

Association bylaws state that the nomination shall be made by a nominating committee consisting of five Past Chairs of the Association that are active in banking; including the three most recent Past Chairs and two designated by the Board of Directors. As the Immediate Past Chair, I serve as the Nominating Committee Chair. Members of this year's Committee, besides me are Steve Daggett, Midwest Bank, Detroit Lakes; Steve Huston, BANKWEST, Rockford; Paul Pieschel, Farmers & Merchants State Bank, Springfield; and Dean Toft, HomeTown Bank, Redwood Falls.

For the 2018-2019 year, the Committee will nominate a banker for the position of Vice Chair/Treasurer, to be elected at the MBA Annual Summit on June 12, 2018. The Vice Chair/Treasurer will succeed to the office of Chair, and then to Past Chair.

Enclosed is a form for your use in suggesting a candidate for Vice Chair/Treasurer. We have asked that background information be included concerning bankers to be considered by the Committee. As always, past and current involvement with the Minnesota Bankers Association or our industry is important. The Committee will receive nominee suggestions until March 15, 2018.

We will appreciate your careful consideration of qualified future leaders for MBA. Feel free to contact any of the Committee members if you have questions or comments.

Sincerely,

Gail Mikolich
Chair, Nominating Committee
Northeast Bank, Minneapolis

I am pleased to submit:

Banker's name: ____

Title: ____

Bank: ____

for consideration as a candidate for Vice Chair/Treasurer of MBA 2018-2019.

Candidate information to be considered:

1. Current responsibilities in bank:
   ____
   ____
   ____
   ____

2. Banking experience:
   ____
   ____
   ____
   ____

3. Educational background:
   ____
   ____
   ____
   ____

4. MBA or other banking organization experience (committees, board etc.):
   ____
   ____
   ____
   ____

Please fax your nomination to the MBA office:
Attn: Kim Philipson (952) 896-1100 or email kimp@minnbankers.com

Pioneer Banker Nomination Form

The Minnesota Bankers Association (MBA) is proud to recognize MBA member bankers who have been leaders of the industry for 50 years or more. All eligible nominees will be inducted into the MBA Pioneer Club at a luncheon at the MBA Annual Summit on June 12, 2018, at Madden's Resort in Brainerd, Minnesota.

Who is eligible for induction into the Pioneer Club?

Any Minnesota banker working for an MBA member bank who has attained at least 50 years of active service by June 30, 2018, is eligible. U.S. military service counts in the 50-year span if the individual was in banking prior to and subsequent to the time spent in the military. Years after retirement in which the candidate works part-time for a bank as a consultant or as a member of the Board of Directors may be counted toward the 50-year total; however, these endeavors must be the principal endeavors of the candidate.

How many years has the nominee been in banking? ______________

Please include a photo and a short narrative of the individual's banking career (no more than 150 words). MBA will publish brief bios of the Pioneer Bankers at the recognition luncheon, in our *MBA News* magazine, and send press releases to local newspapers.

(Pioneer banker candidates may be nominated or can nominate themselves.)

NOMINATION FORM

Nominee ____

Bank ____

Bank Address ____

City/State/Zip ______________________________ Phone ________________

Submitted by ____

Email ______________________________ Phone ________________

Return form to Kim Philipson at the MBA office **no later than April 1, 2018,** by fax (952-896-1100) or by mail: 8050 Washington Avenue South, Eden Prairie, MN 55344.

Joe Witt

Joseph Witt has served as the President/CEO of the Minnesota Bankers Association (MBA) since 2003. The MBA's motto is "The Champion For Minnesota Bankers," and Joe constantly works to ensure that the association is an effective advocate on behalf of the Minnesota banking industry. Witt is a licensed attorney who began working for the MBA's legal department in 1996. He is recognized as an industry expert and is a frequent lecturer and instructor at various banking and legal functions. Joe also represents the industry at the state legislature and is one of the MBA's primary contacts with the media.

Jeff Kortes

Jeff has more than 25 years experience in human resources. He has worked at companies that specialize in manufacturing, construction, textiles and software development. During his entire career he has worked to recruit, retain and develop employees, at companies including ConAgra Foods, industrial equipment supplier SPX, and automotive retailer Midas International, and more.

Jeff runs his own company, Human Asset Management LLC, which helps organizations to recruit, engage, develop and retain their best people. He is a member of the National Speakers Association (NSA) and a frequent speaker on the topic of retention, engagement, and recruitment to human resources departments, associations and business groups. Jeff is the author of Give Your Employees C.R.A.P...and 7 Other Secrets to Employee Retention and Welcome to Dodge…Tales from the Frontiers of Business. For more information visit http://www.jeffkortes.com and follow Jeff on Twitter @jeffkortes

Conference Sponsored by

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Graduate School of Banking at the University of Wisconsin – Madison

Minnesota Bankers Association
8050 Washington Avenue South, Suite 150 • Eden Prairie, MN 55344
952-835-3900 • www.minnbankers.com

Minnesota Bankers Association

WOMEN'S LEADERSHIP CONFERENCE

April 12, 2018

8:00 AM - 3:15 PM

Marriott Minneapolis West St. Louis Park, MN

This conference is designed to encourage, support, and inspire women to reach for success in their financial careers.

MBA™ MINNESOTA BANKERS ASSOCIATION THE CHAMPION FOR MINNESOTA BANKERS

SCHEDULE OF EVENTS

8:00 - 8:30 **Check-in/Continental Breakfast**

8:30 - 10:30 ***Beyond Grit: Powerful Practices to Reach Your Potential***

Dr. Cindra Kamphoff

In Beyond Grit, Cindra Kamphoff reveals the ten practices that the world's best use to gain the high-performance edge. Kamphoff shares the strategies and tools she's taught executives, entrepreneurs, NFL ProBowl athletes, Olympians, college athletes, and championship teams.

Based on almost twenty years of research and consulting with the world's best, Kamphoff provides a practical, inspiring, and easy-to-use guide to radically accelerate your performance and improve your happiness.

10:30 - 10:45 **Break**

10:45 - 11:45 ***Speed Networking***

Join us for a fast-paced networking session to help you get to know other conference attendees and discuss current issues and trends in banking.

11:45 - 12:45 **Lunch**

12:45 - 1:45 ***State of the Industry***

Joe Witt, MBA President/CEO

Receive an update on the state of the financial industry – both locally and nationally, what issues are on the front burner and hear how the MBA is working for its members followed by Q & A.

1:45 - 2:00 **Break**

2:00 - 3:15 ***Give Your Employees C.R.A.P. - the Success Formula for Building Employee Loyalty***

Jeff Kortes, Human Asset Management LLC

Have you ever wondered why some bosses and organizations have people who are incredibly loyal to them and who will do anything for them while others have a revolving door of employee turnover? Those bosses and organizations that people want to follow, they give their employees lots of C.R.A.P.! (Caring, Respect, Appreciation and Praise). Jeff provides a "headhunter's" insight into why some employees are loyal and others work only to get a paycheck. Through real-life stories and interactive participation, Jeff has created a program which helps participants understand how to demonstrate Caring, Respect, Appreciation, and Praise, so that they can systematically build employee loyalty in their organization.

3:15 **Adjourn**

SPEAKERS

Cindra Kamphoff, Ph.D., CC-AASP

Cindra Kamphoff is a keynote speaker, trainer, entrepreneur, and professor who is a go-to high performance coach for leaders, professional athletes, executives and businesses around the nation.

Based on nearly 20 years of research and consulting, she speaks on how to gain a high performance edge while providing practical strategies that work. Kamphoff is also the founder and director at the Center for Sport & Performance Psychology and professor at Minnesota State University, Mankato.

She has a Ph.D. in sport and performance psychology from the University of North Carolina at Greensboro and a BA in Psychology from the University of Northern Iowa.

Cindra and her husband have two boys and live in Minnesota. You can read more about Cindra's speaking programs and coaching at www.cindrakamphoff.com.

Women's Leadership Conference

PROGRAM	April 12, 2018: 8:00 a.m. – 3:15 p.m.
REGISTRATION FEE (This fee includes materials, continental breakfast, lunch and refreshments)	Member: $299.00 1st registrant $269.00 For each additional registrant from same bank or organization $50.00 For current college students interested in a financial career Qualified Non-Member: $375.00 per person

CANCELLATION POLICY: MBA reserves the right to cancel programs due to insufficient enrollment, instructor illness, or other reasons. Participants wishing to cancel must inform MBA in writing prior to the event. Send cancellation notices to maryh@minnbankers.com. A cancellation fee of 25% of the program cost will be charged for withdrawing, or you may send a substitute. The full program fee will be charged for withdrawing after the event has taken place or a no-show.

NON-MEMBERS: Qualified non-members are encouraged to register. Please call our office for further information.

SPECIAL NEEDS: If you have a disability that may affect your participation in the program, please send MBA a statement regarding any special needs at least two weeks prior to the program. We will contact you to discuss accommodations.

*****Please also let us know if there are dietary issues at least two weeks prior to the program.*****

Lodging: Lodging is not included in the registration fee. A block of rooms has been reserved at the Marriott Minneapolis West for Wednesday, April 11th for $139.00 plus tax per night. Call (952) 544-4400 and ask for the Minnesota Bankers Association block or go to our website www.minnbankers.com for the online reservation link. **Reservations must be made no later than March 22, 2018.**

PLEASE PRINT OR TYPE (One registrant per form - copy form if needed.)

Full Name ______________________ Title ______________________

Company ______________________ Phone ______________________

Address ____

City/State/Zip ______________________ Mail Code/Station ______________________

E-mail ____

Please provide your email address in order to receive a confirmation.

☐ $50.00 Current college student fee School Attending: ______________________

☐ $299.00 First Registrant

☐ $269.00 Each additional registrant from same bank/organization

PAYMENT OPTIONS: Check Enclosed ☐ Bill Bank ☐ Visa/MC/AmEx ☐ Amount Due $__________

Visa/MC/AmEx # ______________________ Exp. Date __________

Signature ____

Name on Card ____

MAIL WITH PAYMENT TO: Minnesota Bankers Association
Attention: Registrar
8050 Washington Avenue South, Suite 150
Eden Prairie, MN 55344

FAX TO: 952-896-1100
EMAIL TO: maryh@minnbankers.com
TO REGISTER ON LINE:
www.minnbankers.com

MarMBANews

MBA's Bank Day at the Capitol: Building Relationships & Creating Connections

Thursday, March 22, 2018
St. Paul** • 10:00 a.m. – 3:00 p.m.

Who should attend and why?
- From CEOs to tellers, your involvement is the key to our strength!

Start the day with:
- Important updates on legislative issues and background information from the MBA Government Relations team
- Speakers, including House and Senate leadership

The afternoon at the Capitol will include:
- Visits with your local legislators
- Committee meetings and hearings

REGISTRATION FORM
(PLEASE PRINT OR TYPE. One registrant per form – copy form if needed.)

Last Name ______________________ First Name ______________________ M.I. *(required)* ________

Bank ______________________ Phone ______________________

Bank Address ______________________ Fax ______________________

City/State/Zip ______________________ Mail Code/Station ______________________

E-mail ______________________

***REQUIRED*: TO SCHEDULE MEETINGS WITH YOUR LOCAL LEGISLATORS, WE NEED YOUR *HOME ADDRESS*:**

____

☐ I will be attending the morning session/luncheon **ONLY**.

PAYMENT OPTIONS: Check enclosed ☐ Bill bank ☐ Visa/MC ☐ Amex ☐ Amount due $________

Account # ______________________ Exp. Date ____________

Signature ______________________

Name on Card ______________________

LODGING: *We have rooms reserved for Wednesday, March 21st, at Hampton Inn & Suites Downtown St. Paul, W 7th Street, St. Paul, for $159 per night + $27 per day valet parking.* **The cut-off date is February 21, 2018.** *Please call 651-224-7400 to reserve a room and identify yourself with the Minnesota Bankers Association.*

CANCELLATION POLICY: MBA reserves the right to cancel programs due to insufficient enrollment, instructor illness, or other reasons. Participants wishing to cancel must inform MBA in writing prior to the event. Send cancellation notices to maryh@minnbankers.com. A cancellation fee of 25% of the program cost will be charged for withdrawing, or you may send a substitute. The full program fee will be charged for withdrawing after the event has taken place or a no-show.

NON-MEMBERS: Qualified non-members are encouraged to apply. Please call our office for further information.

SPECIAL NEEDS: If you have a disability that may affect your participation in the program, please send MBA a statement regarding any special needs at least two weeks prior to the program. We will contact you to discuss accommodations.

**** A confirmation letter will be emailed to registrants including location, agenda, maps, and parking voucher.**

$75.00 Members / $85.00 Non-members / Please remit payment to the MBA, Attn: Registrar

MINNESOTA BANKERS ASSOCIATION
THE CHAMPION FOR MINNESOTA BANKERS

AMERICAN BANKERS ASSOCIATION

The MBA Washington Trip/ABA Government Relations Summit • April 23-25, 2018

We are partnering with the ABA and state associations across the country to make sure our voices are heard at the Capitol!

It's hard to imagine a more important year for bankers to head to Washington, D.C!

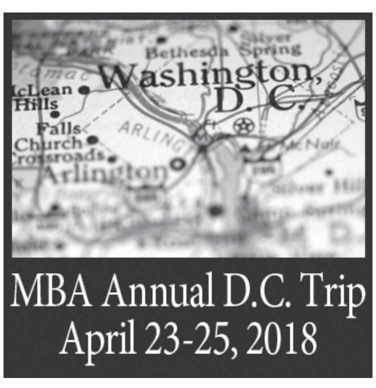
This year the MBA's Washington, D.C. Trip will again be joining the American Bankers Association's (ABA) Government Relations Summit as one supercharged conference.

The ABA will provide briefings on current legislation, regulations and the situation in the U.S. Capitol. During the event, we will hear from Congressional and regulatory leaders and also make a trip to Capitol Hill to meet with your individual member of Congress. This is an excellent opportunity to provide your feedback on the key issues impacting the banking industry.

The MBA Washington Trip/ABA Government Relations Summit is open to all members of the Minnesota Bankers Association (bankers do not have to be a member of the ABA to attend the trip.)

Highlights of the MBA Washington Trip/ ABA Government Relations Summit:

- Meet with Minnesota Senators and U.S. Representatives
- Receive briefings by **Federal Reserve, Federal Deposit Insurance Corporation** (FDIC), **Office of the Comptroller of the Currency** (OCC), and the **Consumer Financial Protection Bureau** (CFPB)
- Hear from other key individuals regarding the banking industry
- Network with bankers from both Minnesota and around the country



Registration Check list:
(please go through the checklist below before registering)

Register with both the MBA and ABA.

- The MBA registration form is attached to this sheet. Please fill it out and fax it back to 952-896-1100 or email to maryh@minnbankers.com.
- The ABA registration must be done online. Please fill it out at aba.com/Summit.

Register for the hotel via the ABA.

- This year's hotel will be the Washington Marriott Marquis. The registration for this hotel should be completed through ABA's online registration form.

Please Note: there is no registration fee with the ABA form

2018 MBA/ABA GOVERNMENT RELATIONS SUMMIT

April 23-25, 2018

Registration Form

MINNESOTA BANKERS ASSOCIATION
THE CHAMPION FOR MINNESOTA BANKERS

Registration Fee

The fee for Washington Conference delegates is $100. This includes the Minnesota Attendee Dinner on Tuesday, April 24, 2018 at Del Frisco.

Due to space limitations, we have been asked that spouses/guests not attend the working sessions. However, they are welcome to attend any receptions or dinners (the cost of these activities is $100 for spouses).

Housing

ABA Convention Services will be handling all hotel reservations (Washington Marriott Marquis) Please make sure to reserve your room through them when you fill out their registration form.

Airlines

Please plan to make your own travel arrangements. We suggest that you plan to arrive in Washington D.C. on the morning of Monday, April 23, or earlier, and depart late afternoon on Wednesday, April 25.

Full Name ______________________________ Spouse ______________________________

Bank ______________________________ Phone ______________________________

Bank Address ____

City/State/Zip ____

E-mail ____

Registration Fee: _____ $ 100 (*Fee is for the Minnesota Dinner on Tuesday, April 24*)

Spouse/Guest Fees: _____ $ 100

Total Due: $______

PAYMENT OPTIONS: Check enclosed ☐ Bill bank ☐ Visa/MC ☐ Amex ☐

Account # ______________________________ Exp. Date ______________

Signature ____

Name on Card ____

Cancellation Policy: Participants wishing to cancel must inform MBA in writing prior to the event. Send cancellation notices to maryh@minnbankers.com. A cancellation fee of 25% of the program cost will be charged for withdrawing, or you may send a substitute. The full program fee will be charged for withdrawing after the event has taken place, or a no-show.

PLEASE RETURN FORM BY APRIL 9, 2018

MAIL WITH PAYMENT TO: Minnesota Bankers Association
Attention: Registrar
8050 Washington Avenue South
Eden Prairie, MN 55344-3821

FAX TO: 952-896-1100

EMAIL TO: maryh@minnbankers.com

*Are **You** the Future of Banking?*

2018-2019

MBA Leadership Development Academy

Why?

The future of banking is now. Cultivating high-performing leaders is the only sure-fire strategy to succeed in today's rapidly changing banking environment. That's why the MBA is so excited to announce the second offering of the **Minnesota Bankers Association Leadership Development Academy.**

As Baby Boomers move into retirement, the banking industry will need to identify and train our next generation of leaders. This world-class leadership development program is designed specifically to hone the leadership skills of high-potential, mid-career bankers in Minnesota. The program instructors, presented below, bring a wealth of experience and an approach that will challenge participants to grow as leaders. This will be an unforgettable experience that will help shape the rest of your career.

The Ideal Candidate

The ideal candidate for this program is:

- A mid-career banker with significant potential for leadership;
- Highly motivated to take your banking career to the next level; and
- Committed to helping your team and your bank succeed.

The Program in Detail

The program consists of four, two-day sessions over the course of 12 months. The class size will be limited to 25 participants. **Tuition for the full year is $3,750.**

In addition to the four in-depth training sessions, participants are highly encouraged to take part in the MBA's Annual Summit and Bank Day at the Capitol.

To help make attendance at these events possible, participants will receive a 50 percent discount on registration for the two Annual Summits that book-end the program and will be allowed to attend Bank Day at the Capitol without charge during the class year. At the 2018 Annual Summit, you will be formally recognized as a member of the new class for the MBA Leadership Development Academy. At the Annual Summit in 2019, you will be recognized as a successful graduate of the program.

Session 1 - It's Simple, But It Isn't Easy

June 12-14, 2018 (Immediately following the MBA Annual Summit)
Madden's on Gull Lake, Brainerd

Leadership of organizations, teams and individuals is based on timeless core principles. These principles are simple to understand but not as easy to implement, maintain and develop into outstanding results. Session 1 will explore these core principles of leadership while also inspiring motivation, discipline and dedication to the pursuit of excellence no matter the leadership challenge.

Content for Session I includes:

- Moving from Manager to Leader
- The Personality Traits, Styles and Potential of Leaders
- Teamwork – The Foundation of Organizational Excellence
- Public Speaking with Confidence and Impact
- Banks of the Future – Leveraging the Inevitable Changes
- The Promises, Challenges and Necessity of the Digital Revolution

Session 2 – Do Something That Scares You

September 25-27, 2018
Location: Sugar Lake Lodge, Grand Rapids

Leaders can emerge on every level of the organizational chart. Often what defines a leader is their willingness to face difficult situations that require courageous decisions or decisive action. In this session, participants will examine their own personal and professional willingness and comfort taking risks, challenging the status quo and engaging in out-of-the-box thinking. In addition, participants will explore how strong, high-performance teams push themselves to take risks and engage as one entity to meet uncertainty and challenge, enabling them to emerge as an even stronger organization.

Content for Session 2 includes:

- Leadership Lessons from the Navy SEALS
- Communication Styles across the Organization
- Pushing the Limits on What You Currently Know and Do at Your Bank
- The Seven Habits of Highly Effective Speaking
- Managing the Stress of Leadership
- Navigating the Challenges of a Strong Team Culture

Session 3 – Limitations are Self Imposed

February 4-6, 2019
Location: Sugar Lake Lodge, Grand Rapids

Often, the limitations that come with change at the bank seem insurmountable. In reality, these limitations are self-imposed because leaders don't have the knowledge, skill or experience to manage change. This session will focus on the inevitability of change in organizations, large or small, and will offer models and practices that will support leaders in taking a pro-active stance in directing that change. Participants will learn to leverage resources and communicate messages that will make any change, from core conversions to mergers to organizational re-structuring and staff turn-over, an event that can be directed for optimal bank outcomes.

Content for Session 3 includes:

- Recognizing and Managing Acute and Chronic Crisis at the Bank
- Peer-to-Peer Problem Solving
- Emotional Intelligence as a Tool for Change
- Crisis Communication
- Leading a Team Under Pressure
- Mission and Project Planning

Session 4 – Who Dares, Wins

May 14-16, 2019
Location: Sugar Lake Lodge, Grand Rapids

The final session focuses on a thorough assessment of the leadership knowledge, skills and experience gained during the year-long leadership development program to guarantee transfer back to the benefit of the bank. In addition, the imperative of "daring" to meet the challenges of bank leaders of the future will be emphasized, along with the understanding that the "win" of becoming a strong leader is beneficial to their banks, their communities and their lives.

Content for Session 4 includes:

- Using Organizational Culture to Drive Business Results
- Recruiting and Hiring the Next Generation of Employees
- Going Beyond – The High Performance Team

- Building a Professional Network for Influencing and Impact
- Becoming an Advocate for the Industry
- Taking it Back – Realizing Personal and Professional Transformation

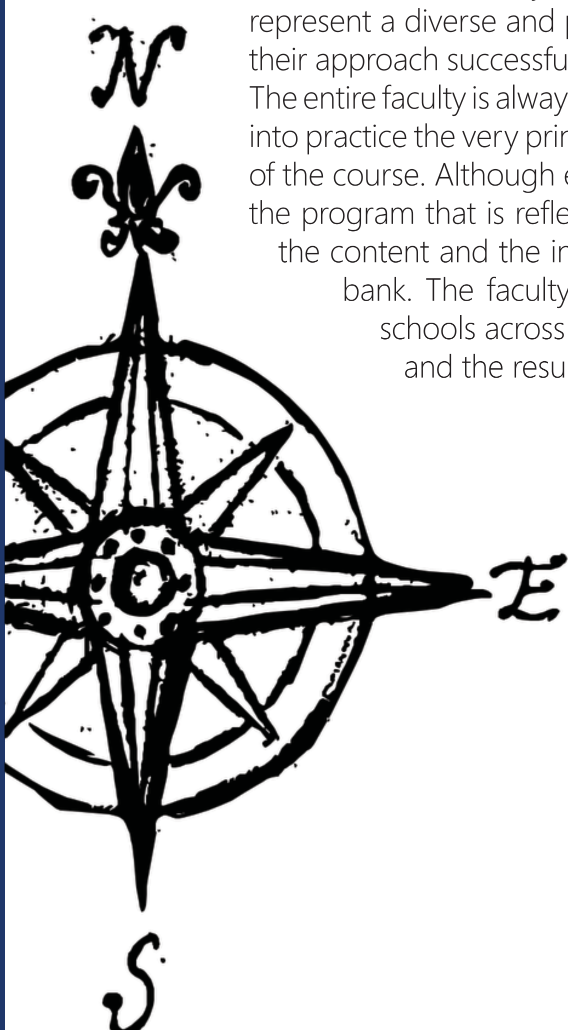
Learning Outcomes

At the conclusion of this program, participants will have the skills to:

- Apply core concepts of – and know the difference between – leadership and management
- Articulate and advocate persuasively for the bank and industry
- Make courageous decisions crucial to the bank's success
- Think, plan and successfully execute bank initiatives
- Deliver compelling business presentations
- Motivate themselves and others to help the bank thrive
- Contribute to the future of banking with innovative, forward thinking
- Build and lead high performance teams
- Develop organizational cultures that sustain success

The Approach

The three core faculty members for the MBA Leadership Development Academy represent a diverse and powerful set of skills and experiences. However, what makes their approach successful is their unique commitment to team teaching and learning. The entire faculty is always with the class, whether in the classroom or outdoors, putting into practice the very principles of leadership and teamwork that are at the foundation of the course. Although each instructor brings a different leadership specialization to the program that is reflected in the content they present, the connections between the content and the instructors are what ultimately provide real value back at the bank. The faculty have implemented this philosophy at banking leadership schools across the country, as well as with companies outside of banking – and the results are always incredible.



The Faculty

Juli Lynch, Ph.D.

Juli Lynch holds a Ph.D. in Human and Organizational Development Psychology. She specializes in personal professional development, leadership and team development and organizational culture alignment and management. Juli has spent 25 years as a consultant and executive coach in the financial services industry, and has also coached executives in the automotive, healthcare and retail industries. She is a regular presenter at the Graduate School of Banking in Madison, and has spoken for more than 25 state banking associations over the past decade. She has led long-term consulting and coaching engagements with 20 banks across the country that have focused on connecting culture and leadership to performance. Prior to her consulting career, Juli was a professional ultra-marathoner and adventure racer, competing around the globe with her teams. She gained incredible insight into enabling teams and leaders to reach new levels of performance in high-stress situations.

Steve Ahlberg
Capt. USN SEAL (Ret.)
MS, MBA

When it comes to stress, Steve Ahlberg understands the reality of facing long odds and devising methods for defeating them. A career spent in the U. S. Navy SEALs, from Platoon Commander to Deputy Commander, Naval Special Warfare Command to Commodore, has empowered Steve to think strategically, plan thoroughly, and take action. The SEALs are arguably the most versatile of the military special operations groups. Known within their community as simply, "The Teams," they achieve the seemingly impossible through Teamwork. Armed with an MBA and MS in Strategic Intelligence, Steve has the ability to wind stories of his military exploits around effective methods of team building, team leadership, and executive training. He has worked to develop high performance teams and leaders in organizations nationally and internationally, large and small.

Jackson Hataway, Ph.D.

All great leaders and teams know that success starts with communication. Jackson holds a Doctorate in Organizational Communication. He specializes in internal and external communication, organizational development, team building, and strategic planning. Jackson works with some of the fastest growing banks in the US to deliver cutting edge innovation that drives positive impact to the bottom line. At the same time, his expertise in communication theory and strategy has led him to work regularly with executives at leading digital technology companies such as Microsoft and Adobe to develop internally and externally facing communication platforms. Through his work facilitating strategic planning sessions and developing innovative strategic initiatives, Jackson has learned to identify the resources that are often forgotten or ignored by organizations – and to hone those resources so that they become invaluable. In addition to his consulting expertise, Jackson is a renowned professional speaker with numerous national awards.

Locations and Lodging Details

The program will kick off at Madden's on Gull Lake. The resort, situated on a lake with peaceful surroundings, offers a truly inspiring location to launch your experience as a participant in the Leadership Development Academy.

The remaining three sessions will take place at The Leadership Lodge at Sugar Lake Lodge near Grand Rapids. The Leadership Lodge is designed specifically to encourage teamwork, inspire creativity and take you to new heights.

Upon acceptance into the program, MBA staff will work with you to arrange accommodations at these two locations. Tuition does not include hotel costs, but does include all onsite meals.

The contracted rate for Madden's is $139 - $199 per night. The contracted rates for the remaining three sessions at the Sugar Lake Lodge range from $129 - $159 per night.

For questions contact
Eric Hauth, Director of Communications and Education
at erich@minnbankers.com.
www.minnbankers.com/leadershipacademy

MBA™
MINNESOTA BANKERS ASSOCIATION
THE CHAMPION FOR MINNESOTA BANKERS

Bert Ely's FARM CREDIT WATCH®

Shedding Light on the Farm Credit System, America's Least Known GSE

To contact Bert Ely: Email: bert@ely-co.com; Fax: 703-836-1403; Phone: 703-836-4101
Mail: P.O. Box 320700, Alexandria, Virginia 22320

January 2018 (No. 238)

Tax bill reduced FCS's competitive edge in real estate lending

One unintended effect of the wide-ranging tax legislation Congress enacted last month was a slight reduction in the competitive edge the FCS has long had for loans secured by real estate. The profits FCS institutions earn on real estate loans have always been exempt from federal and state income taxes while FCS profits on loans **not** secured by real estate, such as equipment and production loans, are subject to federal income tax, but not state and local income taxes. The reduction in the basic federal corporate income tax rate from 35 percent to 21 percent effectively has reduced, but certainly did not eliminate, the tax **disadvantage** bankers have long suffered in competing against the FCS for loans secured by real estate. For banks taxed as corporations, that rate reduction translates into 14 basis points of higher after-tax income for every 100 basis points of pre-tax income on a bank loan secured by farm real estate. The owners of banks taxed as Subchapter S corporations also will enjoy a comparable tax benefit. The FCS, of course, still has a funding cost advantage by virtue of its GSE status, especially for longer term, fixed rate loans, but every basis point of a reduced tax burden helps to lessen the FCS's unfair and unjustifiable tax and funding cost advantages. Unfortunately, the tax bill did not address the FCS's ongoing tax advantages that cost taxpayers $1.61 billion in 2016.

FCS of America letter signals future credit-quality problems?

Last month, FCS of America (FCSA), the largest FCS association, with $27 billion in assets, and serving South Dakota, Iowa, Nebraska, and Wyoming, sent a letter to an undisclosed number of its member/borrowers offering to "defer the principal portion of all payments due in 2018 on your fixed or variable rate real estate loan(s)." FCSA has not posted on its website any announcement about this principal-deferral offer or given any indication as to how widely this deferral option is being offered. While the letter suggests that this offer is being made selectively ("Based on your current status . . ."), it has a very simplistic, shotgun-quality to it, as evidenced by the fact that it offers "to defer the principal portion of <u>all</u> payments due in …" [underlining supplied].

There may be some situations where a 12-month deferral of **all** principal repayment on **all** of a farmer's real estate loans makes sense, but there probably are far more situations when it does **not** make sense from either borrower's or FCSA's perspective. In some cases, only a partial deferral on some loans is needed to help the farmer weather the current outlook for commodity prices and operating expenses while in other cases the farmer's situation is such that his loans need to be restructured or more dramatic action should be taken, such as encouraging the farmer to boost the farm's equity or downsize his operation. It may be, too, that this letter was sent to some borrowers whose projected cash flow will be sufficient to meet their currently scheduled principal repayments. Simplistic, one-size-fits-all solutions seldom are the best. Worse, FCSA may be kicking the can down the road, by not dealing in a timely manner with those situations where a 12-month deferral of all principal payments is not the most appropriate action to take at this time with a potentially troubled loan. The Farm Credit Administration (FCA), FCSA's regulator, should carefully examine the wisdom of this letter. The FCA also should check whether this payment-deferral offer has been extended to the member/borrowers of Frontier Farm Credit, the association serving eastern Kansas that is managed by FCSA.

The FCS Insurance Corporation cuts its premium rate

The FCS Insurance Corporation (FCSIC), an arm of the FCA, announced this month that it had reduced its insurance premium rate for 2018 from 15 basis points to 9 basis points per dollar of Systemwide Debt Securities issued by the Federal Farm Credit Banks Funding Corporation, the primary source of funding for FCS loans and investments. The FCSIC, which is the FCS's counterpart of the FDIC's Deposit Insurance Fund, or DIF, insures the timely payment of the principal and interest on the Systemwide Debt Securities. FCSIC premiums do not reflect the riskiness of the FCS as a whole or of individual FCS institutions, with one exception — the FCSIC assesses a 10-basis point risk surcharge on nonaccrual loans and **other**-than-temporarily impaired investments. FCSIC premiums instead are assessed in an amount sufficient to hold the FCSIC fund balance at two percent of the amount of Systemwide Debt Securities outstanding. Hence, the FCSIC premium rate varies with the rate of growth in outstanding FCS debt, which in turn is largely driven by the rate of FCS loan growth.

What is going on at Lone Star Ag Credit?

As the August 2017 FCW first reported, Lone Star Ag Credit, headquartered in Fort Worth, Texas, in August of last year withdrew its financial reports and call reports back to the beginning of 2016 after Lone Star's management "discovered appraisal and accounting irregularities affecting a segment of [Lone Star's] lending portfolio." These problems appear to be similar to what afflicted FCS Southwest, which served most of Arizona; prior to its acquisition by Farm Credit West in November 2015. In a Nov. 9, 2017, letter posted on its website, Lone Star stated that its investigation of accounting irregularities was "ongoing, with its conclusion anticipated during the fourth quarter of 2017." That means it should soon be issuing audited financial statements for 2017 as well as corrected financial statements back to 2016 as well as filing corrected call reports with the FCA. It will be interesting to see if that occurs as well as whether Lone Star survives or is forced to merge with another FCS association. Perhaps that merger would have to be assisted financially by the FCSIC.

CoBank makes another investment in a private equity fund

In a Jan. 25 press release, CoBank announced that it had made a $7.5 million commitment to a new rural private equity fund, joining five other FCS institutions "to participate in the first round of financing for Open Prairie Rural Opportunities Fund." The fund will invest in "target areas such as crop protection, ingredients, processing, storage, data management and logistics." With the fund's initial commitments of $55 million, CoBank probably is one of its larger investors. The fund will be managed by Open Prairie, which has been licensed by the USDA as a Rural Business Investment Company (RBIC) under USDA's Rural Business Investment Program. As the news release noted, "this is the third time CoBank has invested in a rural-focused equity fund under the [RBIC] since 2014." CoBank has invested a total of $52.5 million in these funds. Leaving aside whether a GSE should be making risky, equity-capital investment, this very reasonable and logical question arises: How well have these RBIC investments performed, both in terms of meeting pre-established objectives as well as profitability? I posed this question to a CoBank representative. His emailed answer: We don't put out a report on the performance of the funds. So much for CoBank transparency.

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Time to rethink the taxation of the FCS and ag co-ops

Hopefully an unintended consequence of the major tax legislation enacted in December will be the triggering of a fundamental review of the taxation of the FCS and agricultural co-ops relative to banks and other investor-owned businesses. The intent of this review should be to eliminate differences in the tax treatment of ag-related businesses due solely to their form of ownership. What should trigger this review was the tax legislation's addition of a new section 199A to the Internal Revenue Code. As a Jan. 9 Wall Street Journal article reported, this new provision "allows farmers to deduct up to 20 percent of their total sales to cooperatives, letting some farmers reduce their taxable income to zero."

According to the Journal article, this provision could sting large agribusinesses, such as Cargill and Archer Daniels Midland, in addition to smaller private operations as farmers increase their grain sales to ag co-ops to capture the tax savings offered by Section 199A. A subsequent Wall Street Journal article (Feb. 15) reported that while investor-owned grain companies are trying to get Section 199A modified so as to reduce its negative impact on them, they may set up their own co-ops so that they can remain competitive with the traditional ag co-ops in purchasing grains from farmers. Although not mentioned in the article, possibly the ag co-ops set up by the grain companies will be able to begin borrowing from CoBank, the only FCS institution authorized to lend to ag co-ops.

Efforts are underway in Congress to modify Section 199A so as to reduce, if not eliminate, the unintended effects it is having on agriculture. However, the longer this section is in effect, the harder it will be to modify or repeal it because grain companies as well as farmers and those who finance agriculture will have adapted to it and therefore will resist efforts to modify it. The furor that Section 199A has created should trigger a congressional review all aspects of agricultural taxation, including the highly favorable tax treatment the FCS has long enjoyed. While the tax-rate reductions Congress just enacted have helped somewhat to reduce the FCS's tax advantages on loans secured by real estate, as reported in last month's FCW, the FCS still enjoys a substantial tax advantage over commercial banks, which is magnified by the FCS's favorable funding-cost advantage by virtue of being a GSE.

FCA chairman okay with deferring loan principal repayments

In last month's FCS, I reported that FCS of America (FCSA), which serves all of South Dakota, Iowa, Nebraska, and Wyoming, had sent a letter to some of its member/borrowers offering to "defer the principal portion of all payments due in 2018 on your fixed or variable rate real estate loan(s)." Several bankers and other ag-finance experts echoed the concern I expressed about the wisdom of FCSA's offer. One banker even suggested that a deferral of a loan's principal repayments should cause the loan to be classified as non-performing or otherwise impaired.

Much to my surprise, Dallas Tonsager, the chairman and CEO of the Farm Credit Administration (FCA), in a Jan. 30 speech to the Farm Credit Council (the FCS trade association), effectively endorsed what FCSA has offered to its borrowers and encouraged other associations to do the same thing. Specifically, Tonsager stated that at a meeting last year, “I learned that some associations are giving some of their borrowers the option to defer the principal portion of their 2018 payments. This gives these producers the chance to re-amortize the outstanding balance over the remaining life of the loan. It also gives them additional working capital, which in turn gives them the flexibility and time to make needed adjustments to their operations.”

It appears that Tonsager is suggesting that FCS associations engage in loan restructuring without calling it that, which would have the effect of underreporting loan-quality issues within the FCS. Given that the USDA has forecast another decline in farm income in 2018, to a level less than half the record income farmers earned in 2013, “there’s a lot of stress and a lot of duress on the farms today,” as Agriculture Secretary Sonny Purdue stated during a recent hearing of the House Agriculture Committee. Has the FCS begun to mask the effect of that stress and distress on its borrowers by encouraging farmers to defer repayment of loan principal? In recent testimony to the House and Senate Agriculture Appropriations Subcommittees, Tonsager noted that four FCS associations “were under supervisory actions,” which suggests that borrower distress is beginning to surface in FCS associations. Encouraging the deferral of principal repayments could unwisely delay the FCA’s recognition and acknowledgement of additional credit-quality problems within the FCS.

FCA chairman again suggests changes in FCS structure

In his Farm Credit Council speech, Tonsager touched on an issue — the structure of the FCS — he previously has addressed, as I have reported in prior FCWs, most recently in the February and May 2017 issues. He asserted that while the FCS “has been in a constant state of renewal since its inception in 1916, as it continues to evolve, we must evaluate how any proposed change could impact the integrity and cooperative structure of the [FCS].” In particular, he stated that “we must consider how the change might affect the relationship between the funding bank and its associations.” What Tonsager is implying, but seems unwilling to state explicitly, is that the FCS’s two-tier structure — four regional banks funding 68 associations of widely varied size — is obsolete. Do the larger associations, for example, need to fund themselves through one of the four banks when they could just as easily deal directly with the Federal Farm Credit Banks Funding Corporation, the FCS’s link to the capital markets? Further consolidation within the FCS, particularly at the bank level, will heighten this issue because the strength of the joint-and-several liability of the FCS banks for debt issued by the Funding Corporation will be questioned if the number of banks — not so long ago there were twelve — shrinks to three or even two.

While Tonsager has repeatedly questioned the FCS’s structure, but noticeably without offering any restructuring proposals, it is most troubling that he views this issue as something to be addressed only within the FCS, as he suggested when he told Council members that “your members and stakeholders must have confidence that structural changes are in the best long-term interests of the [FCS] and those it serves.” By implication, Tonsager said that all others with interests in rural America, including commercial bankers, as well as the taxpayers backing the FCS, should be excluded from any discussions about restructuring the FCS. That should not be the case. Instead, every party with an interest in the health of agriculture and rural America should be involved in a very public discussion of the structure of the FCS, possibly in conjunction with a discussion of its tax status, as suggested above.

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