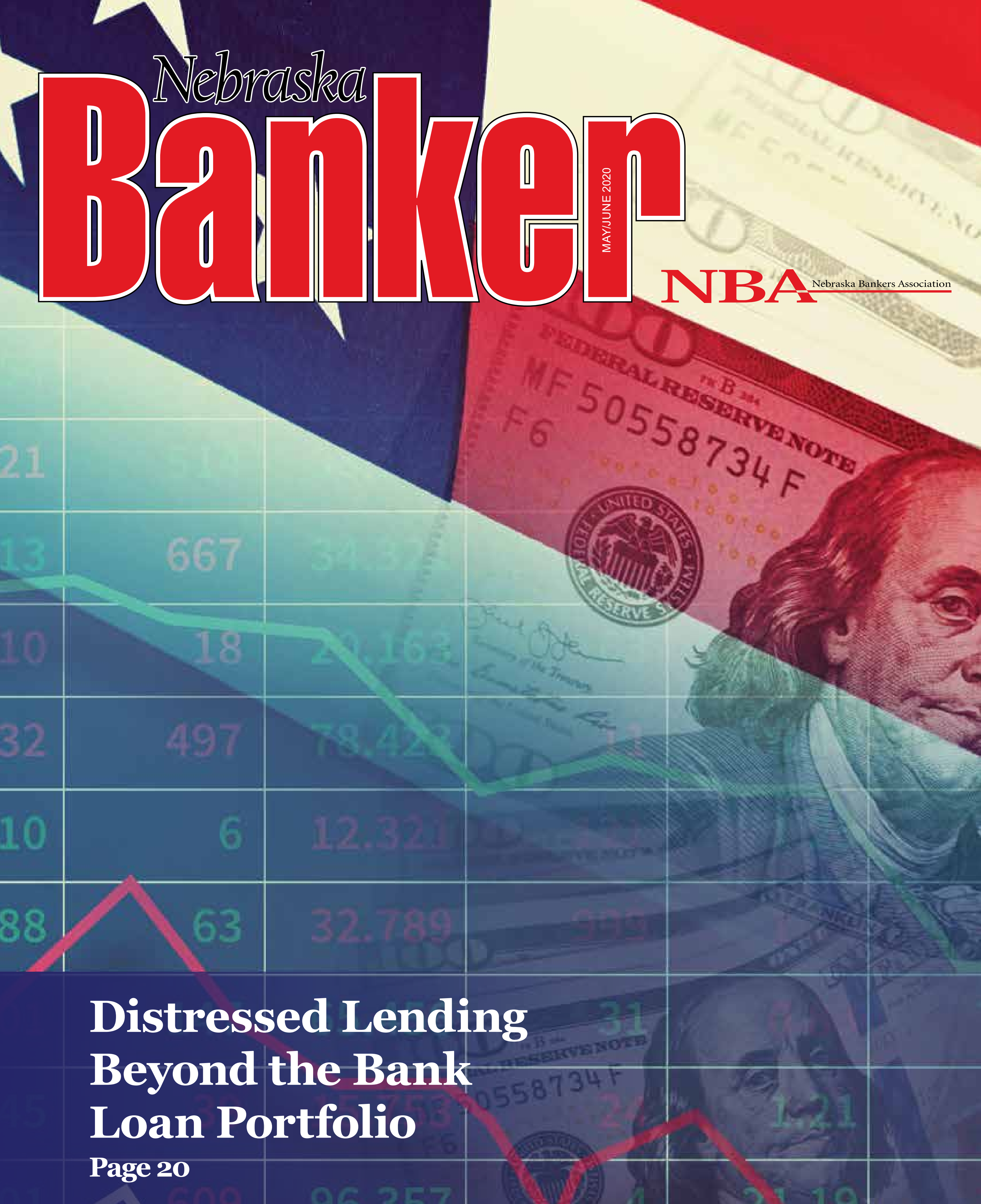
Nebraska
Banker
MAY/JUNE 2020
NBA Nebraska Bankers Association



Distressed Lending Beyond the Bank Loan Portfolio

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OFFICIAL PUBLICATION OF THE NEBRASKA BANKERS ASSOCIATION

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Nebraska Banker

MAY/JUNE 2020

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A Testament of Commitment

Richard J. Baier, President and CEO, Nebraska Bankers Association

THE RISE AND SPREAD OF THE CORONAVIRUS HAS UNDOUBTEDLY brought significant, unplanned hardships and continued change to the Nebraska banking industry. Every aspect of our personal and professional lives has been directly impacted in one way or another. During this challenging time, we have also witnessed our industry step forward and practice what is engrained in our banking DNA: working tirelessly with our customers to help protect and build wealth and support our communities.

I have personally never been more proud to be associated with the banking industry and our NBA member institutions as Nebraska bankers worked to update and implement their pandemic plans, adjust to new travel restrictions, actively alter bank operations, confront mortgage repayment challenges and possible small business closures and proactively rollout new government-approved support programs like the Paycheck Protection Program (PPP).

As I write this column, Nebraska banks have initiated and funded more than 39,000 small business PPP loans totaling more than $3.5 billion. Nebraska bankers worked tirelessly, many of them day and night, to implement the PPP in support of their vulnerable small business customers. These loan commitments were made with little direction or clarity, knowing the loans also placed increased risks on the bank's long-term profitability.

Our member banks repeatedly stepped up and answered the call! As you probably read, Nebraska banks were recognized nationally by numerous news and media outlets for the early successes in securing PPP loans for their customers.

This recognition is truly a testament to the commitment of our Nebraska banks and bankers!

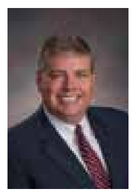
As the PPP loan process and other provisions of the CARES Act play out over the next few months, we know that there will be continued questions and concerns. I would encourage you to reach out to an NBA staff member to discuss these issues. Our team is working directly with representatives from the SBA District Office, the American Bankers Association, various bank regulatory bodies and members of our Nebraska Congressional Delegation to actively raise awareness and seek solutions. With that said, I want to offer a special thanks to our regional SBA staff and our Nebraska Congressional offices for maintaining clear and direct lines of communication throughout this turbulent time. Personally, I can confirm that I and members of our legal/compliance team were on the phone or communicating via email with SBA leadership and our Congressional liaisons almost hourly as the PPP rolled out.

However, PPP is not the only issue where your NBA staff committed time and energy throughout the early stages of the pandemic. Our marketing team constructed a coronavirus webpage for NBA members and managed media relations and interviews, our legal team worked closely on creation of a Governor's Executive Order to expedite remote notary services, the NBISCO and VEBA staff members continued to sell and service bank and health insurance products and our education team managed the cancellation, postponement and rebooking of multiple programs. I want to offer my personal thanks to each of our staff for helping to navigate these unchartered waters.

On an important but non-coronavirus update, the Nebraska Department of Banking and Finance recently announced its intention to designate the Nebraska Bankers Insurance Services Company (NBISCO, the for-profit arm of the NBA) as the Administrator of the Single Bank Pooled Collateral Program (SBPCP) effective July 1, 2020. The SBPCP allows participating banks to aggregate their total public deposits and to pledge collateral against its entire portfolio of public deposits rather than pledging per public entity, thus saving the bank time and money. As the program administrator, NBISCO will collect, confirm and report bank compliance with the mandated pledging requirement, thus streamlining administration for public depositors on a monthly basis. Collateral is pledged to NBISCO. In the event of a bank closure, the pledged collateral would be assigned to NDBF for liquidation and payment to impacted political subdivisions. To learn more about this program, please contact Misty Stoner at misty.stoner@nebankers.org or (402) 474-1555.

Finally, as we begin to return to business as usual, nothing will be like it was before. We are all working in very unique circumstances. Please let our NBA team know how we can help navigate this new normal.

Stay safe!



Contact Richard J. Baier at (402) 474-1555 or richard.baier@nebankers.org.

Coronavirus Strikes. America's Banks Step Up.

Rob Nichols, President and CEO, American Bankers Association

THE WORLD IS GRATEFUL FOR ALL WHO HAVE SERVED ON THE front lines battling the COVID-19 crisis — the doctors and nurses who have put their lives at risk to care for the sick and dying as well as those who have kept our grocery stores and pharmacies stocked. These essential service providers are the pandemic's heroes, putting the needs of others ahead of their own.

There is another category of worker that also fits this bill. It's the women and men who work for America's banks. You, too, are first responders — not to the health crisis but to the economic crisis spawned by it. And if I could drive by your offices (home or otherwise) honking and holding up signs in appreciation, I would.

Whether working from your main office or the kitchen table, in the first several weeks of the pandemic you extended critical lifelines to countless households and small businesses suffering from the loss of income resulting from stay-at-home orders. From the loan officer who learned that the trick to getting into E-Tran (the Small Business Administration's portal for submitting Paycheck Protection Program applications) was to try at 2 a.m., to the staff who put in extra time to help customers needing forbearance or other accommodations and the employee disinfecting the ATM each day, you proved that serving your communities is not just your job, it's your calling.

Your personal efforts, combined with banks' institutional responses—waiving fees, offering low-rate personal loan programs, deferring payments and even effectively fronting customers their economic impact payments—demonstrate that banking is first and foremost about helping others.

America's banks weren't just deemed essential businesses by governors in state after state; they became essential partners in delivering massive amounts of federal government relief. Despite its faults, the SBA's unprecedented PPP program — which in its first phase processed 14 years' worth of SBA loans in less than 14 days — simply could not have been executed without banks acting as the middlemen. And thanks to the sophisticated payment system the industry has built over the years, banks have been key conduits for distributing — safely and quickly — tens of millions of economic stimulus payments to individuals.

ABA has been proud to support you in your efforts and to tout publicly all you have done, as we did through aba.com/CoronavirusResponse and the press statements, media interviews and digital ads that pointed people to that page.

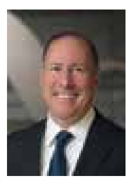
As always, our efforts are carefully coordinated with the ABA-State Association Alliance, which has never been more important or more valuable to the industry as a whole. For the first several weeks of the crisis, state association and ABA leaders held daily conference calls to discuss what banks were reporting from the front lines, identify solutions and relay needed policy fixes or guidance to policymakers. The flow of information was equally important in reverse.

Sometimes the clarity we all needed from Washington was slow to arrive, but policymakers understood and appreciated that our appeals were solutions-focused and made in good faith. In fact, our most effective advocacy often involved direct phone calls, emails and texts to lawmakers, regulators and top Treasury and SBA officials, with public finger-pointing taking a back seat.

America's banks weren't just deemed essential businesses by governors in state after state; they became essential partners in delivering massive amounts of federal government relief.

ABA's efforts throughout the crisis, like your state associations, have been focused on ensuring you have what you need to continue supporting your institutions, customers and communities through these extraordinary times.

We deeply appreciate all of your efforts and are committed to supporting you as we work to rebuild the economy. Because every hero needs a sidekick, and we are proud to be yours.



Email Rob Nichols at rnichols@aba.com.

EDUCATION CALENDAR

Due to the COVID-19 (Coronavirus) event recommendations and related schedule changes, please visit https://www.nebankers.org/education.html or call the NBA Education Center at (402) 474-1555 for the most current event calendar updates.

JUNE 2020

Weekly Ag Briefing
June, 9, 16, 23, 30
Virtual Webinar

Employment Law Compliance for Banks Workshop
June 24, Lincoln
Virtual Webinar

JULY 2020

Protecting Your Bank's Most Valued Assets: Surviving an Incident of Violence
July 8, 2020
Virtual Webinar

Principles of Banking
July 14-15, Lincoln
Cornhusker Marriott Hotel

Agricultural Lending School
July 13-17, Grand Island
Ramada Midtown

Preparing for Your Next IT Examination
July 23, Lincoln
Cornhusker Marriott Hotel

Operations School
July 28-30, Manhattan, Kan.
Bluemont Hotel

AUGUST 2020

YBON Annual Conference
August 6-7, Lincoln
Cornhusker Marriott Hotel

Opening New Accounts Documentation and Compliance Workshops
August 11, Lexington
Holiday Inn Express
August 12, Norfolk
Norfolk Country Club
August 13, Lincoln
Cornhusker Marriott Hotel

Real Estate Lending Compliance Conference
August 18-19, Lincoln
Cornhusker Marriott Hotel

School of Banking Fundamentals
August 31-September 4, Manhattan
Bluemont Hotel

SEPTEMBER 2020

Fall Agri-business Conference
September 3-4, Lincoln
Cornhusker Marriott Hotel

Essential Teller Issues Seminar
September 14, Ogallala
Quality Inn and Conference Center
September 15, Lexington
Holiday Inn Express
September 16, Norfolk
Norfolk Country Club
September 17, Lincoln
Cornhusker Marriott Hotel

Fall IRA Workshops
September 21-22, Lincoln
Cornhusker Marriott Hotel
September 23-24, North Platte
Holiday Inn Express

Bank Compliance School
September 21-25, Grand Island
Ramada Midtown

Fall Group Meetings
September 29, Scottsbluff
Hampton Inn and Suites
September 30, North Platte
Holiday Inn Express

OCTOBER 2020

Fall Group Meetings cont.
October 1, Kearney
Holiday Inn
October 6, Lincoln
Embassy Suites
October 7, La Vista
La Vista Embassy Suites
October 8, Norfolk
Norfolk Country Club

Advanced School of Banking
October 5-9, Manhattan, Kan.
Bluemont Hotel

Commercial Lending Schools
October 19-23, Manhattan, Kan.
Bluemont Hotel

Women in Banking Conference
October 21-22, Lincoln
Cornhusker Marriott Hotel

Summit on Regulatory Issues
October 30, Lincoln
Cornhusker Marriott Hotel

NOVEMBER 2020

Bank Investment, Funding and Economic Outlook Conference
November 5-6, Lincoln
Cornhusker Marriott Hotel

Loan Documentation Workshops
November 17-19, Kearney
Holiday Inn

DECEMBER 2020

Agriculture and Beyond Workshops
December 8, North Platte
Holiday Inn Express
December 9, Norfolk
Northeast Community College

NBA Nebraska Bankers Association

For more information about these live and online education events and training tools, contact the NBA Education Center at (402) 474-1555 or nbaeducation@nebankers.org. You also may visit the NBA website at https://www.nebankers.org/education.html.

PPP Alters Internship

Kara Heideman, Director of Communications and Marketing, Nebraska Bankers Association

IN A NORMAL YEAR, MANY BANK INTERNS BEGIN THEIR SUMMER working at the teller line. This year is certainly not normal and Callie Dethlefs' first banking experience was a little unique. She started her internship by handling Paycheck Protection Program (PPP) loan guarantee paperwork for Town & Country Bank in Ravenna.

Dethlefs, a junior agribusiness major at the University of Nebraska-Lincoln, planned to start her Ag Banking and Finance internship in May. After the university moved classes online, she headed to her parents' home near Rockville. There, she helped her father on the farm, worked on her classes and continued her tutoring job with the Nebraska Athletic Department. An early-morning call from James Friesen, Town & Country president, changed her plans.

Like banks across the country, Town & Country was scrambling to understand and deliver the PPP to customers. Friesen recalled thinking, "We're going to have to basically deliver this program as quickly as possible before the money runs out, while at the same time, we're still trying to interpret the rules."

He asked Senior Vice President Mark Ficek to take the lead on implementing the PPP. Michael Bauer, current Town & Country credit analyst, was brought in to assist. As the roll-out neared, Friesen called Dethlefs and asked if she wanted to start her internship early.

"I think it was 7 a.m.," Dethlefs said of the phone call. She was in the bank two hours later ready to learn how to process the PPP loans.

This was Dethlefs' first experience working in a bank. Friesen knew the tasks she would take on needed to be fairly simple and easy to teach. Friesen taught Dethlefs the ins and outs of putting the files together, creating the closing package and the basics of Town & Country's loan processing software. "Within two hours, she could create the loan package we needed people to sign at closing and she was even researching business entity information on the State of Nebraska corporate information inquiry page," he said.

On her first day, PPP applications were already coming in, so Dethlefs got to work right away. In two weeks, Dethlefs helped Town & Country Bank with over 120 PPP loan packages. "It was honestly a huge help to be able to dedicate her to that specific task," Friesen commented. "She was absolutely a core part of that whole process."

Dethlefs applied what she learned in professor David Aiken's agricultural law class to research and verify business entity information. "She could even put together a draft resolution for these customers to review if we didn't have that information," Friesen said. Dethlefs also credits her agricultural finance class with helping her understand the loan process. "I really enjoy getting experience," Dethlefs said of working on the loans.

Dethlefs balanced working full time at the bank and her classes. During the PPP application period, she needed to take an afternoon off to take a microeconomics exam. When she returned, the pile of folders on her desk had grown substantially.

Despite her busy schedule, Dethlefs appreciated the opportunity to help deliver the PPP loans. As a product of a small town, she understands how important the program is to rural businesses. "It's nice to know these loans are helping these people out, especially during these crazy times when everybody is struggling," she said.

Dethlefs will eventually make her way to the teller line. The teller line will give her an understanding of the core systems of the bank. Her internship will expose her to many aspects of working in a bank like loan support and credit analysis. She's already started working on internal appraisals. Later this summer, she will join loan officers on inspections. Friesen said Dethlefs will also assist with the second part of the PPP, the loan forgiveness.

Approximately 13 interns are working at Nebraska banks this summer through the Ag Banking and Finance program. Dethlefs has some advice for these current and future interns. She noted the importance of paying close attention during training. "If you miss one thing, then you mess up the whole thing," she said. Learning from bankers with years of experience has also been a valuable part of her internship.

Friesen stressed the importance of an internship for career development. He noted that an internship like the ones offered through the Ag Banking and Finance program helps students understand how what they are learning in class applies to the real world. It can be an eye-opening experience he noted. "There's nothing that brings something home to a person like actually having a connection with people who are impacted in either a positive or negative way," said Friesen.

Banks who host an intern also benefit. "We've been fortunate to have young people come in who realize the bank needs something out of this too," Friesen said.

PPP Internship — continued on page 16

PPP Internship — continued from page 15

For Town & Country, the internship program also led to a new employee. Michael Bauer interned there last summer. After graduation, he joined the bank as a credit analyst.

The Ag Banking and Finance program is a partnership between the NBA and the UNL Department of Agricultural Economics. Students in the program receive a scholarship and complete a summer banking internship. Since the program's inception in 2006, nearly $800,000 in scholarships have been awarded to over 500 students.

The program is just one of the Nebraska Bankers Association's initiatives to engage, attract and retain the next generation of Nebraska bankers.

If your bank is interested in being a part of this effort by hosting an intern please contact Kara Heideman or reach out to our NBA Communications and Marketing team at kara.heideman@nebankers.org, 402-474-1555.

Kara Heideman, Director of Communications & Marketing

Fraud and the Economy

Bob Kardell, Baird Holm LLP

THE ASSOCIATION OF CERTIFIED FRAUD Examiners released their biannual survey this year on occupation fraud; the survey again shows the average organization loses 5% of their annual gross revenue to fraud.[1] The issues stemming from fraud can be magnified significantly during an economic crisis such as the one the United States is currently experiencing due to COVID-19. The fraud in such an economy can be categorized into two groups: fraud which has been ongoing and only uncovered due to the drop in the economy, and fraudsters taking advantage of the economic situation.

Ongoing Fraud Revealed

Warren Buffet once said, "Only when the tide goes out do you discover who's been swimming naked."

The latest drop in the market will likely uncover some fraud such as the frauds revealed in the last two recessions. The market drops in 2000 and 2001 resulted in the uncovering of frauds in Enron and World Com and many other "dot com" bubble companies. The market drops in 2008 resulted in the uncovering of Bernie Madoff's Ponzi scheme as well as several other frauds.

The current crisis to hit the economy will uncover a plethora of fraud, waste, and abuse over the next several months to years. This type of fraudulent activity has been there all along; it never really left after the mortgage fraud prosecutions of 2008 had subsided, but the rising economy causes companies to overlook such issues and problems. The companies are then forced to reckon with the issues when the economy declines and budgets get tight.

Several years ago, I worked on a case in which a business manager had been committing fraud. The business manager had

> The fraudsters have an advantage when communication is poor; when we are all separated by distance while working from home and feeling separated from normal support groups, the fraudsters will try to fill that void.

access to the checks, and the checking account, as well as the ability to make entries in general ledger. Shortly after the investigation began, the fraud was uncovered. The business manager admitted to the fraud when confronted with the evidence, but, in spite of the evidence and the admission, the owner decided not to fire the business manager. The reasoning was that the fraud uncovered was not material to the company. Just a few short years later, however, when the economy was tight, the fraud became material, and the business manager was fired. Just as a side note, after they fired him, the company found that he had been stealing from the company in many other ways.

The high tide of the good economy over the past decade has enabled many fraudsters to hide their crimes. The sharp drop in the economy will cause companies to reexamine their budgets, tighten their belts, and cut expenses. As they do so, many will find instances and examples of employee fraud, vendor fraud, poor financial management, and a host of other issues.

Indeed, the next few months and years will be interesting from a financial fraud perspective to see what is uncovered and who has been "swimming naked."

New Fraud Schemes

The drop in the economy has also provided new vectors for fraudsters to create schemes to defraud the government, people, and companies. Just recently it was revealed that charges were being brought against a man in Rhode Island who applied for a PPP loan under the CARES Act.[2] The man did not have any employees, however, and one of the defendants lied to an undercover FBI agent. Fraudulent PPP loan applications are just one of many novel ways in which fraudsters are taking advantage of the novel Corona Virus.

Another fraud taking place includes fake charities seeking donations. A search of the recent registrations for domain names reveals a number of new websites with COVID-19 and charity. Searching for "covid" through "*.com" domain names returned over 42,000 domain names with the word "covid" in them. Limiting the search to names with "covid" and "charity" or "test" or "vaccine" revealed several thousand websites purporting to offer home testing or tests of vaccines.

Many older frauds have made a resurgence. The increase in work-from-home employees means that many employees are now working outside of the protections of their company's firewall or email scanning services. The corporate grade scanning services have allowed the cyber fraudsters to target employees directly. Several weeks ago, I received a number of inquiries from individuals receiving extortion emails — emails in which the cyber fraudster is threatening to reveal embarrassing information until an extortion payment is made. The emails purport to verify the fraudster's threat by including an email address and a password. The passwords are actual passwords used by the email recipient and are from old data breaches like LinkedIn and Marriott and Yahoo. Because the fraudster includes an actual password, the email appears to be a legitimate threat, and the recipients may be tricked into paying the extortion.

Awareness is the Key

Fraud, it seems, is inescapable. It is omnipresent and makes periodic resurgences in tough economies. The fraudsters themselves are looking for money as well. The key for prevention is awareness. Educate your clients and employees as to the possibilities of fraud. Talk early and often about the new types of fraud, and the new ways in which fraudsters are attempting to reach into your network. The fraudsters have an advantage when communication is poor; when we are all separated by distance while working from home and feeling separated from normal support groups, the fraudsters will try to fill that void.

Establish a hotline or webpage for your clients and employees. When employees are working remotely, your clients may be without the communication necessary to find out if an email is legitimate or a BEC fraud.

Update the information regularly and communicate often. Once established, a communication portal should be regularly updated. Ensure that there are regular postings and that information does not become stale. The fraudsters and the schemes evolve almost daily in times such as these and the communications should be constantly updated as well.

Review internal policies and procedures. It is also a good time to review internal business continuity plans, cyber security policies, insurance, and software agreements. Most agreements and policies did not fully anticipate a pandemic with a work from home option. Review those agreements to ensure you and your organization are covered if a phishing scam or ransomware attack occurs at a work from home location.

[1]ACFE Report to the Nations, https://acfepublic.s3-us-west-2.amazonaws.com/2020-Report-to-the-Nations.pdf.
[2]https://www.justice.gov/opa/pr/two-charged-rhode-island-stimulus-fraud

For more information, contact Bob Kardell, J.D., MBA, CISSP, CPA, CFE, CFF, attorney at Baird Holm LLP, 402-636-8313, or bkardell@bairdholm.com. Bob is a member of the Technology and Intellectual Property Section of Baird Holm LLP specializing in cybersecurity and breach response. Bob is also a retired FBI Special Agent with over 27 years of fraud and investigative experience.

Distressed Lending Beyond the Bank Loan Portfolio

Gary Grote, Managing Director, Bridgepoint Investment Banking

BANKERS UNDOUBTEDLY SPENT THE better part of March to May 2020 dealing with stressed, scared and frustrated clients while trying to play mind reader with the SBA. Covid-19 is sure to stress the bank's loan portfolio as businesses face varying impacts of the health crisis. Larger regional banks likely have a special assets group with bankers trained to deal with these special situations. But even for these bankers (and especially for community bankers tasked with wearing both the business development and special asset manager hats), there may come a time where the bank customer is better served by a specialty lender for a period of time. These specialty lenders are happy to work in partnership with a local bank that continues to provide non-credit services like cash management.

Bridge Financing

A liquidity shortfall, pending debt maturity or overleveraged balance sheet does not indicate a failure of leadership. Situations like this are often caused by industry cycles, changing regulations or shifting markets that, as a result, have a negative impact on an organization's financial arrangements. Moreover, situations like this do not have to mean bankruptcy or sale. There are forms of financing — referred to as bridge, stress or rescue — that can be leveraged as a solution to the problem. Understand that a special financing situation can surface in any industry during any point in an economic cycle.

Bridge financing is an interim option primarily used to fulfill a company's short-term working capital needs until a more long-term financial solution can be arranged. This type of loan typically comes with a higher-than-normal interest rate based on investor risk.

Bridge financing is arranged through partnership with an investment bank, which has connections to private debt, institutional capital and alternate source lenders. Additionally, investment banks are able to bring sophisticated systems and deep market knowledge to the table. Think of this type of financing as a bridge that connects a company to capital through short-term borrowings.

Who Provides Bridge Financing?

Bridge financing is available through lenders with substantial amounts of cash who are looking for opportunities to put these funds to work. Here is a list of typical lending sources.

Private Lenders — These are individuals or non-bank companies that are generally considered more aggressive than traditional lenders. Private lenders fund a variety of loans, including those designated as bridge. An advantage is that they tend to have faster approval times than banks due to less regulatory scrutiny.

Family Office Debt Funds — Family offices are privately held wealth management advisory firms that serve individuals and families generally with a net worth skyward of $100 million in investable assets. A primary role of family offices is to seek worthy debt fund investments on behalf of their clients. They often interface with investment banking firms and other outside managers to achieve capital gains for their clients.

Private Debt Funds — Another alternative to traditional banks, private debt funds specialize in raising money from investors and lend it to companies for a variety of purposes including mezzanine financing, distressed financing, growth capital, merger and acquisition and other special situations funds.

Who Qualifies for this Type of Capital?

Forms of bridge financing are not recommended for startup businesses but instead for existing companies that can demonstrate the ability to make it through a temporary downturn. Established companies with good track records and experienced management teams generally can qualify for bridge financing without difficulty. In fact, lenders understand that this sort of capital is needed quickly and for a shorter period time than long-term leveraged debt options.

Bridge financing is meant to alleviate immediate monetary pressures, allowing the company to focus on correcting operational, financial or personnel deficiencies to emerge as a stronger organization and return to traditional financing with a bank.

Gary Grote is a 24-year veteran of Nebraska banking and now a managing director with Bridgepoint Investment Banking. For more information, contact Bridgepoint at 402-817-7940. Bridgepoint is a boutique investment banking firm that provides sophisticated, flexible and creative solutions to middle market companies, which typically are overlooked by Wall Street. In order to offer securities-related investment banking services discussed herein, and to include M&A and institutional capital raising, certain representatives of Bridgepoint Investment Banking are registered representatives of M&A Securities Group, Inc., an unaffiliated broker-dealer and member of FINRA/SIPC. This entity is not affiliated or associated with, authorized or sponsored by Bridgepoint Advisers Limited.

Virtual IT Audit – Not a Novel Idea

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SECURITY AND IT PROFESSIONALS ACROSS THE WORLD HAVE invested a large amount of time and effort transitioning to a remote workforce. At the start of this transition, much of the time was spent on getting the technology up and running, securing remote access, and finding a way to conduct business as normal (or as close to normal as possible). Now that the initial shock to the system is somewhat behind us, it is time to shift our mindset back to proactive security.

It's important to keep in mind that cybersecurity risks grow significantly during a time of uncertainty. In fact, we have seen a massive increase in cyber incidents in recent weeks stemming

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from phishing emails, phone calls, malicious websites' data maps, and ransomware attacks. The spike in malicious activity is so severe that researchers have seen an increase of 667% in phishing email attacks alone in the month of March.

A critical component of proactive security includes continuous process improvement, including regular testing of an organization's people, processes and technology. Many times, an IT audit is how we verify that proper security measures are in place and are effective.

A traditional on-site IT audit has historically required a security firm to send a qualified information security auditor on-site to review policy, procedures and technical controls, as well as to conduct investigative interviews. The auditor typically examines whether the organization is compliant with its own program (and with applicable regulations), as well as identifying possible gaps in the adequacy of controls.

The Future of the IT Audit is Virtual

In response to the COVID-19 virus, regulatory agencies have announced plans to conduct virtual IT examinations. This may seem like a novel idea; however, virtual IT audits have been around for years.

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process. An added bonus of your virtual engagement is that your IT auditor is not spending time traveling, meaning there should be an increase in the efficiency of the audit process from start to finish.

Here are three common questions and solutions to note when conducting a virtual IT audit.

Question 1: Can the IT auditor communicate effectively if the service is performed virtually?

Answer: Communication is important for all services; however, in a virtual IT audit, communication is absolutely vital to the value that the organization gets from the engagement. A virtual IT audit should utilize several different communication channels such as online meetings (with screen sharing and conference call capabilities), video conferencing (when available), email, secure information sharing portals, phone calls, and text messages to ensure the quality of the process. Communication expectations should be set up front with your auditor.

Question 2: What about the availability of the auditor vs. our in-house staff? How does that work?

Answer: When an auditor is on-site it is easy to get access to your team for interviews, questions and concerns. When the auditor is virtual, it's even more important that the auditor gets access to the staff and information needed to conduct the audit.

With a virtual IT audit, a schedule should be created for the duration of the audit that encompasses the topics and ISP components to be reviewed, interview times for your staff members, regular check-ins with your team, and a formal Exit Meeting to discuss findings and recommendations.

Question 3: What about physical security checks? How can you validate physical security controls if you're not on-site?

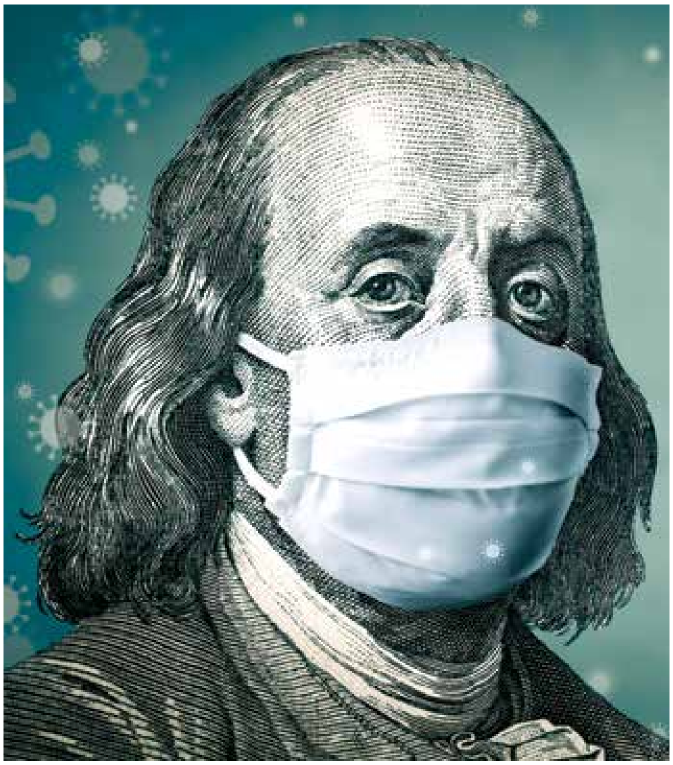
Answer: Physical security is a very important component in an information security program and needs to be addressed even in a virtual IT audit. Physical security can be reviewed and assessed through the use of video or photos of each physical control to ensure the completeness of the audit. If you have the ability to turn on a webcam and walk your IT auditor around your physical premises virtually, that's the preferred option.

Don't push off the your IT audit until later. Stay ahead of cybersecurity threats and incidents with a virtual IT audit.

For more information, contact Reece Simpson at 605-270-3916 or reece.simpson@sbscyber.com. SBS delivers unique, turnkey cybersecurity solutions tailored to each client's needs, including risk management, consulting, on-site and virtual auditing, network security and education. Learn more at www.sbscyber.com.

A Solemn Farewell to Reg. D's Convenient Transfer Restrictions

Michael Perez, Associate General Counsel



EFFECTIVE APRIL 24TH, 2020 THE BOARD OF GOVERNORS OF the Federal Reserve System ("Board") did away with a longstanding, and, in the opinion of some, outdated rule in Regulation D. The Interim Final Rule amended Reg. D by deleting the six convenient transfers and withdrawals restriction that has become synonymous with savings accounts. Additionally, recent guidance has further clarified aspects of the rule change raised by the Interim Final Rule. Because the rule change puts the ball in each depository institution's court, in terms of whether to continue enforcing transfer restrictions, banks are now left at a crossroads with compliance considerations in proceeding down either path.

With the Reg. D restrictions being antiquated for years due to changes in the industry, what precipitated Reg. D's amendments now? In the Interim Final Rule, the Board noted an "ample reserves regime" monetary policy shift, which led to the Board reducing reserve requirement ratios to zero percent effective March 26, 2020. As a result of the elimination of reserve requirements on all transaction accounts, the Board stated that the distinction between transaction accounts and savings deposit accounts was no longer necessary. Lastly, the Board pointed to disruptions caused by COVID-19, which in turn has caused many depositors to have an urgent need for access to their funds by remote means.

Because the Board pointed to recent developments as a bases of the change, as well as its timing amidst the COVID-19 pandemic, has led some to question whether the Reg. D changes are permanent or only temporary in order to provide relief during the current crisis. The Interim Final Rule as currently written did not indicate that these changes are temporary. Additionally, The Federal Reserve Banks ("Banks") further clarified in a recent FAQ that the Board does not have plans to re-impose transfer limits but may make adjustments to the definition of savings accounts in response to comments received regarding the Interim Final Rule as well as potentially in the future, if warranted.

With the question of the Interim Final Rule's permanency being somewhat clearer, it is worth noting that many changes caused by rule are indeed clearly explained. For example, the rule explains that enforcement of the changes is not mandatory. Instead, it is completely up to each bank whether to suspend enforcement of the six transfer limit and even provides that a temporary suspension is an option. Additionally, the rule allows a certain amount of flexibility in that a bank that suspends enforcement of the transfer limits can either continue to report these accounts as savings deposits or alternatively report them as transaction accounts for purposes of the FR 2900. Further, the rule does not require reclassification or name changes for effected accounts.

Because it is up to each bank on whether to suspend enforcement of the six transfer limits, one of the most frequent questions we have received is whether notice is required when suspending enforcement. Neither the Interim Final Rule nor relevant guidance regarding the Reg. D changes have specifically stated notice is required. Additionally, Regulation DD only requires advance notice in certain circumstances which suspension of transfer limits would not trigger. Even though not specifically required by regulation, providing notice is considered a best practice from a customer relationship and UDAAP perspective when significantly changing the terms of an account. Additionally, for those institutions that will be suspending enforcement of the transfer limitations only temporarily, generally Reg. DD would require advance notice when re-implementing the transfer restrictions, as this would adversely affect the consumer. We have heard from many banks that plan to temporarily suspend

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enforcement of restrictions plan on providing a statement notice informing the customer of the change and indicating the date on which the restrictions will be re-implemented.

Another issue presented by the change is whether it is necessary to amend account agreements. While the Interim Final Rule does not specify the manner in which account agreements may be amended, the issue of whether they should be amended remains open. If choosing to suspend enforcement of the restrictions, this would arguably lead to a conflict between the depository institutions practices and the current terms of the account agreement. Additionally, even if not suspending enforcement of the restrictions, it is common to cite Reg. D as a source of the restrictions, which is no longer the case. Either of these issues could cause compliance issues for a depository institution and therefore should be taken into consideration in determining how to proceed.

Lastly, it initially appeared that the Reg. D amendments had caused an unintended consequence concerning Regulation CC. Because Reg. CC defines "account" by referencing Reg. D's amended definition of "transaction account", it appeared that this had caused a conflict within Reg. CC and presented a question of whether saving deposit accounts were now subject to Reg. CC. The Board clarified the impact of the Reg. D amendments on Reg. CC in a recent FAQ. The Board provided that because Reg. CC continues to exclude savings accounts from Reg. CC's "account" definition, the amendments did not result in savings deposits now being covered by Reg. CC.

While banks still have to decide whether they will suspend enforcement of the restrictions as well as tackle compliance considerations either way, ultimately the elimination of the convenient transfer restriction will relieve banks choosing to suspend enforcement the burden of having to monitor for excessive transactions. Additionally, for bank's opting to suspend enforcement, the changes will benefit account holders by providing greater accessibility to funds. While there will be effort and resources required in implementing these changes, overall it appears the Reg. D changes have the potential of providing a net benefit to banks and account holders alike.

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