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JULY/AUGUST 2020
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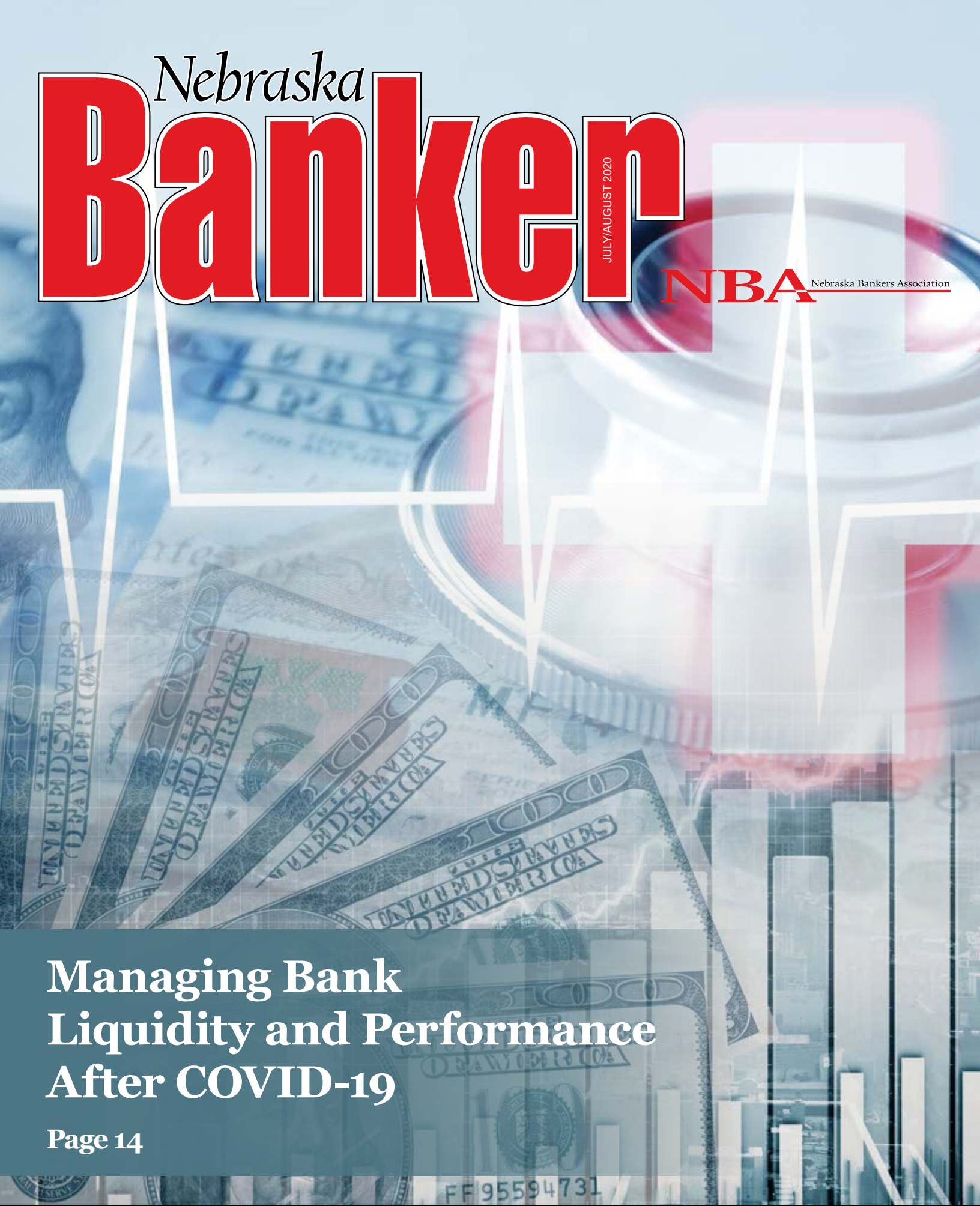

Managing Bank Liquidity and Performance After COVID-19

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Lessons From the Months That Vanished

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

I LOOK BACK ON THE PAST FEW MONTHS AND WONDER WHAT happened to the spring and summer of 2020. Despite the many personal and professional challenges experienced during the COVID-19 pandemic, I have been spending some time each day in my office or at home trying to wrap my brain around lessons we have or should have learned throughout the process; what can we learn as families, bankers and community leaders? For me, the COVID lockdown reinforced the importance of gratitude.

On a personal level, like many families with college-aged children, our daughter returned home to finish the semester online and our medical student's education was placed on hold for an extended period. While their return to our home often stressed our Wi-Fi, it also gave us time to reconnect without the numerous distractions experienced in today's technologically driven world. We suddenly found ourselves eating more family meals, practicing our socially distanced golf game, taking family walks and even enjoying family game night. For these opportunities, our family will be eternally grateful.

At the NBA, COVID gave our team the opportunity to reevaluate operational plans, programs and activities while contemplating how to best represent the banking industry as our economy and country return to a new normal. Your NBA team was able to implement and conduct a real-time test of the NBA's disaster recovery plan. I am pleased to report that our team managed to successfully work from home for more than six weeks with minimal problems. Granted, we also learned some valuable lessons such as the need for additional laptops, with many of those improvements already in process. My staff and our IT partners deserve a great deal of credit for helping us navigate these choppy waters. The reminder in this situation is to thank your partners and vendors for their support!

Another trend that was expedited as a result of the pandemic was the transition of meetings and banker education to more virtual delivery. I was not familiar with Zoom or WebEx a few short years ago. Today, our team has successfully migrated a large number of events to these platforms. I suspect our new normal will include fewer in-person events and more virtual options. Our experiences also reinforced that bankers benefit greatly from personal interactions. Therefore, I am thankful to our team for their innovation and creativity in delivering virtual events, but I will also be thankful to see and interact with our bankers in person. In the meantime, I encourage you to participate in the various NBA virtual events and also to follow the association on social media.

Our NBISCO, legal and finance teams worked with the Nebraska Department of Banking and Finance to kick off the new Single Bank Pooled Collateral Program on July 1. This program allows Nebraska banks to establish a pool of collateralized securities pledged to its aggregate amount of public deposits above FDIC insured limits. First, I am grateful for the 28 Nebraska banks who were part of our user group as the program was developed and implemented. Second, I am also grateful to live and work in a state where the Nebraska Department of Banking worked on this program cooperatively as our partner. Third, I am grateful for the banks who joined the program on July 1 and to those who will be joining on August 1. This program can lower costs and improve efficiency for banks of all sizes. Lastly, I am thankful for a highly talented group of longtime and new staff members who finalized the implementation of this program in a mostly virtual environment.

Finally, watching the pandemic unfold and how my kids relied on video as their source of news, information and entertainment, I was reminded about the importance of proactively marketing our industry in new ways. For example, we know that our industry stepped up to implement the newly created Paycheck Protection Program (PPP) with a focus on helping stabilize the national economy and sustaining our small business customers. While our Nebraska banks received positive regional and national press initially for their work on PPP, we must find ways to leverage this success and promote the importance of personal banking relationships for every generation.

The NBA Board of Directors recently directed resources toward the creation of a video marketing campaign that emphasizes the importance of strong, personal relationships with your Nebraska banker. Younger Nebraskans and those who may not traditionally see the importance of a personal banking relationship are our key target audience. The video will feature testimonials from Nebraska PPP recipients who benefited from their relationship with their bank when securing a PPP loan. Your NBA team engaged redthread, a Lincoln creative agency, to develop the campaign. When the video and related social and radio marketing rolls out, I would strongly encourage you and your marketing representatives to share this message on all your communications channels. Clearly, I am extremely proud of the work our NBA banks did to support PPP lending. I look forward to sharing this story.

Until next time, let's keep working together to promote banking and create a better future for all Nebraskans.

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

Running Toward the Challenge

Rob Nichols, President and CEO, American Bankers Association

IS RACISM BAKED INTO OUR NATION'S SYSTEMS OF JUSTICE, HEALTH and education, or are there disproportionate correlations between race, poverty and crime? Are people too quick to accuse others of racism, or are those in positions of power too slow to recognize their role in perpetuating racial inequities? Is it fair that I posed these as either/or questions, or is all of the above true?

While issues surrounding racial justice and inequities are demanding the nation's attention, honest conversations seem too perilous to hold because of the way some frame the debate as binary. But that ignores the vast common and principled ground on which we all stand and distracts from a focus on meaningful solutions.

Bankers are community leaders, which means you run toward a challenge, not away from it. So as fraught as the situation may feel, ABA is engaging in an open dialogue of how the banking industry, both as employers and as facilitators of wealth creation, can further the principles everyone agrees on: That all Americans should have a truly equal opportunity to prosper and that economic inclusion is essential to creating such opportunity.

Implicit in this discussion is the belief that we each have a role to play in addressing longstanding inequities. Some may feel the problem lies elsewhere — in another community, city or state — and therefore, so must the solution. Others may think they've done all they can with either a great or limited effect. But we are an industry that, in recent years, has developed entirely new ways of banking, and in recent months demonstrated remarkable fortitude and commitment to serving our customers through the pandemic. There is more we can — and must — do to address disparities and promote prosperity for all.

Many banks recognized this long before the pandemic hit and disproportionately harmed Black Americans, and long before the nationwide protests over the killing of George Floyd and others. Some in recent years have built rigorous diversity, equity and inclusion programs that are both inward-facing (focused on employees) and external facing (focused on customers, communities and vendors). Some have pioneered new ways to qualify borrowers and bring those who have been marginalized into the banking system. We celebrate them every year with the ABA Foundation's Community Commitment Awards. Still others

Unacceptable racial disparities in health, wealth, income, education and other measures of opportunity continue to grow — and the pandemic has laid bare these disparities.

have partnered with Minority Depository Institutions and Community Development Financial Institutions to share compliance resources, expertise and more to better enable those institutions to meet the needs of their often underbanked customers.

ABA is tapping the experiences of these banks and leveraging the expertise of our staff experts on diversity, equity and inclusion to provide others with tools and resources to make a difference at their institutions. A new peer group for institutions with robust DE&I programs met for the first time in February and is helping us identify leading industry practices in this space that we can share with members. In April, we convened our Diversity, Equity & Inclusion Advisory Group, which is composed of individuals from banks of all sizes and whose mission is to help us nurture bank DE&I efforts. I was also pleased to announce a strategic partnership this year with the National Bankers Association, the leading trade association for MDIs, to promote the health and well-being of underrepresented communities. And we are collaborating with and promoting MinBanc, which reimburses the educational and professional development expenses of MDI bankers.

This is all to say that both ABA and the industry have a strong foundation upon which to build. And build we must. Unacceptable racial disparities in health, wealth, income, education and other measures of opportunity continue to grow — and the pandemic has laid bare these disparities. Proportionately, two and half times more Black Americans have lost their lives to COVID-19 than white Americans.

We cannot shrug our shoulders and declare these inequities someone else's problem. We cannot fail to engage. We are bankers, we are civic leaders and we must be part of the solution.

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.

AUGUST 2020

Technology Briefings
August 4, 11, 18, 25
Virtual Offering

YBON Annual Conference
August 6-7
Virtual Offering

Opening New Accounts Documentation and Compliance Workshops
August 12, 19, 26
Virtual Offering

Real Estate Lending Compliance Conference
August 18-20
Virtual Offering

School of Banking Fundamentals
August 31-September 4
Grand Island
Ramada Midtown

SEPTEMBER 2020

Fall Agri-business Conference
September 3-4
Virtual Offering

Essential Teller Issues Seminar
September 17
Virtual Offering

Fall IRA Workshops
September 23: Essentials
September 24: Advanced
Virtual Offering

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

Agricultural Lending School
September 21-25
Grand Island
Ramada Midtown

OCTOBER 2020

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
Virtual Offering

Summit on Regulatory Issues
October 30
Virtual Offering

NOVEMBER 2020

Bank Investment, Funding and Economic Outlook Conference
November 5-6
Virtual Offering

Loan Documentation Workshops
November 17-19
Virtual Offering

DECEMBER 2020

Agriculture & Beyond Workshops
December 8
Virtual Offering

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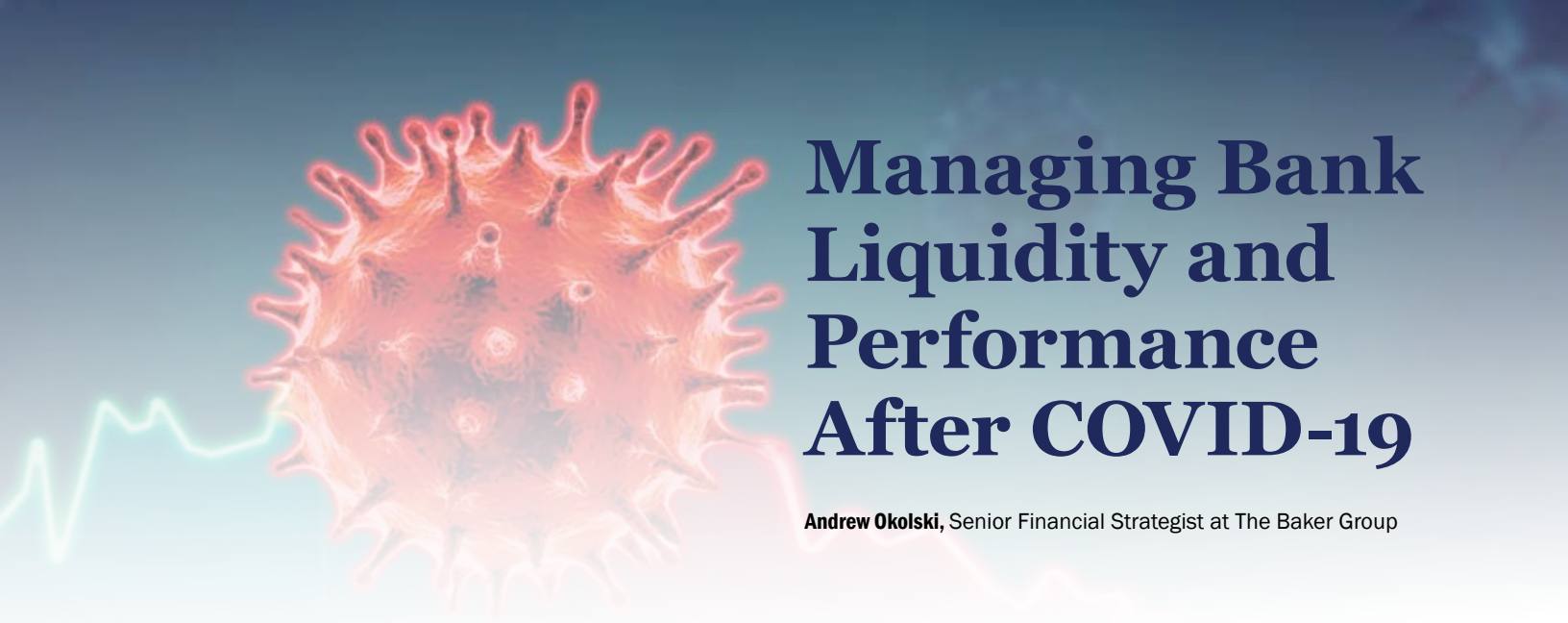
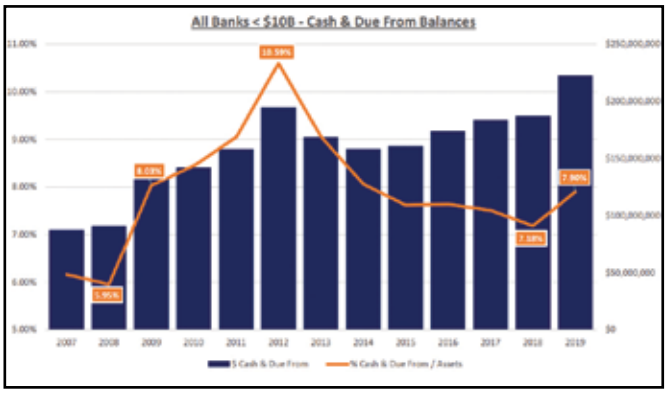
For more information about these live and online education events and training tools, contact the NBA Education Center at (402) 474-1555 or nbaeducation@nebankers.org. You may also visit the NBA website at https://www.nebankers.org/education.html.



Managing Bank Liquidity and Performance After COVID-19

Andrew Okolski, Senior Financial Strategist at The Baker Group

2020 WILL CERTAINLY BE REMEMBERED AS THE YEAR COVID-19 changed the world as we know it. Likewise, the associated "Lockdown Recession" is already changing the way many banks manage their balance sheets. With loan demand dropping in most parts of the country and stimulus deposits adding to already bloated cash positions, proactive strategic planning has never been more crucial. More to the point, proper liquidity management may offer some of the additional margin and income banks desperately need.



Source: FDIC Call Reports

Cash and due from balances as a percentage of total assets reached 7.90% as of year-end 2019. As the chart above illustrates, that level of liquidity was already at or above the average level since 2007. The jump from 7.18% to 7.90%, which occurred 2018 to 2019, very closely mimics the pop in liquidity experienced from 2008 to 2009 (the beginning of the Great Recession). However, it is the three years after 2009 that we are most focused on. Liquidity continued to grow (hitting 10.59% in 2012) as the industry slowly recovered from weakened loan demand and increased deposits from an embattled customer base. The zero-bound range on overnights at the time led to significant drops in overall interest income. As we hit the midpoint of 2020, it appears that the industry must once again prepare to navigate similar waters.

Although we still do not fully understand COVID-19 or the longer-term impact it will have on our economy, we are not completely powerless when it comes to making better-informed decisions. In fact, our performance and trends from past times of crisis can actually become quite useful in a time like this. As we stated earlier, the Great Recession had several important impacts on the overall banking industry. The severe drop in interest rates, mixed with spiking unemployment (sound familiar?), applied extreme pressures on every balance sheet. As we can see below, Loan to Deposit ratios, Investment Yield, and ROA all fell while Provision for Credit Losses and Cash increased leading to lower Return on Equity. Although there isn't a lot we can do about credit issues or lack of demand on the loan side of things, we can do a better job of managing liquidity and specifically cash this time around.

Great Recession Impact			
All Banks < $10B	2007	% Change	2009
Cash & Due From ($Bil) ↑	$86,781	51.44%	$131,420
Loan to Dep ↓	106.10	-8.42%	97.16
PLL ↑	0.27	272.31%	1.02
Investment Yield ↓	4.30	-12.40%	3.77
ROA ↓	1.17	-60.93%	0.46
ROE ↓	11.52	-66.74%	3.83

	75% Impact - COVID			100% Impact - COVID			125% Impact - COVID		
All Banks < $10B	2019Y	75%	2020/2021?	2019Y	100%	2020/2021?	2019Y	125%	2020/2021?
Cash & Due From ($Bil) ↑	221,960	38.58%	$307,590	221,960	51.44%	$336,133	221,960	64.30%	$364,676
Loan to Dep ↓	86.06	-6.32%	78.43	86.06	-8.42%	78.81	86.06	-10.53%	77.00
PLL ↑	0.16	204.23%	0.93	0.16	272.31%	0.61	0.16	340.38%	0.72
Investment Yield ↓	2.73	-9.30%	1.51	2.73	-12.40%	2.39	2.73	-15.50%	2.31
ROA ↓	1.35	-45.70%	0.43	1.35	-60.93%	0.53	1.35	-76.16%	0.32
ROE ↓	10.94	-50.06%	0.10	10.94	-66.74%	3.64	10.94	-83.43%	1.81

Source: FDIC Call Reports

Period in Months	Overnight Rate	Interest Income	Alternative Yield	Interest Income	"Foregone" Income
6	0.05%	$27,750,000	1.10%	$610,500,000	$582,750,000
12	0.05%	$55,500,000	1.10%	$1,221,000,000	$1,165,500,000
24	0.05%	$111,000,000	1.10%	$2,442,000,000	$2,331,000,000
36	0.05%	$166,500,000	1.10%	$3,663,000,000	$3,496,500,000

FHLB Des Moines

Term	1 Mo	3 Mo	6 Mo	1 Yr	2 Yr	3 Yr	5 Yr	7 Yr	10 Yr
Regular Rate	0.45%	0.42%	0.44%	0.47%	0.53%	0.60%	0.84%	1.14%	1.52%
Dividend Adj	0.23%	0.20%	0.22%	0.25%	0.31%	0.38%	0.62%	0.92%	1.30%

Brokered Deposits

Term	1 Mo	3 Mo	6 Mo	1 Yr	2 Yr	3 Yr	5 Yr	7 Yr	10 Yr
"All-In" Rate	0.25%	0.20%	0.25%	0.30%	0.45%	0.60%	0.90%	1.35%	1.60%

The three charts show the potential outcome for our industry assuming a 75%, 100% and 125% magnitude of the impact from 2007-2009. While it can be tempting to "sit on the sidelines" and hope for a V-shaped recovery, we must weigh the potential negative implications from that approach if we end up being wrong. The correct strategy here is not to make a one-way bet in either direction. We can remain positioned for a quicker than expected recovery while also improving our hedge against a longer-term low rate environment like 2007-2012. It all comes down to executable ALM management.

As of 12/31/2019, the industry was carrying just under $222 billion in cash and due from balances earning roughly 1.50% on average. In just one month (March 2020), the return on that cash balance dropped to 0.05%, which equates to an annual interest income shortfall of $3.219 billion. To put it quite simply, we cannot afford to accept an income loss of that magnitude when we do not know how long the current situation could last. In fact, every day that we continue to receive 5bps instead of investing those funds, the foregone income becomes harder and harder to recover. If we assume that we can invest 50% of our cash balance as of year-end ($111 billion) at a yield of 1.10%, the foregone income from waiting in cash builds quickly. In just 6-12 months, we will have already missed out on $580 million to $1.1 billion in additional interest income.

To make matters worse, we ran these figures using cash balances as of the year-end 2019. We all know the first quarter always tends to bring the largest deposit growth. So, if we take that into account and also apply the growth trend in cash from the last crisis (+51%), the industry could be looking at another $100 billion in cash balances near-term. That could potentially double the foregone income figures below. Then we add in the potential windfall of liquidity coming from the forgiveness of PPP loans industrywide. That figure was sitting at $513 billion as of 05/16/2020. Add this all up, and it is not sustainable for earnings or capital.

We fully understand that 1.10% is not the most attractive yield historically; however, income is income in this type of economic environment. If we had the opportunity to add 105bps of additional margin on just about any other asset, we would jump on it. So why does the industry choose to keep additional liquid funds at 0.05% when better earning options are available? The response to this question usually revolves around liquidity concerns in the future. Sure, I have way too much cash now, but what if loan demand picks back up? What if deposits become more competitive?

It is our opinion that with proper balance sheet management, you can have both. We can increase or at least protect margin and earnings through better investment and liquidity management. As for the potential liquidity worries down the road, that is where contingent liquidity comes into play through wholesale liquidity options. In fact, this is exactly why we have these lines of additional liquidity: so that we can put our cash to work at better yields and margins without worrying about funding future loan demand. It's also important to note that the current costs to access these liquidity avenues are at historic lows as well. If we were to invest funds and then have a surprise jump in loan demand, I'm confident we would still be able to earn a healthy spread, funding it with advances or brokered deposits well below 1%. The rule of thumb is that as long as available investment yields are higher than borrowing costs, you will make more money investing your cash and borrowing to fund other liquidity needs.

The next 12-18 months will likely separate those who prepared versus those who chose to wait for it to be over. Current cash balances are already at unsustainable levels with much more likely on the way. There is still time to put together a strategic investment and liquidity management plan based on your specific balance sheet.

Andrew Okolski is a Senior Financial Strategist at The Baker Group. He works directly with clients in a broad range of areas, including ALM, education, portfolio management, interest rate risk management, strategic planning, regulatory issues and wholesale market strategies for financial institutions. Before joining the firm, he spent 15 years building and managing a financial strategies group at a New York broker/dealer. Andy holds a Bachelor of Business Administration Degree from Long Island University — C.W. Post. Contact: 800-937-2257, andyo@GoBaker.com.

Lender Liability — The Basics of a Management Professional Liability Policy

Mitch Florea, Vice President of Marketing, NBISCO

LENDER LIABILITY IS WHEN A LENDER IS ALLEGED TO HAVE violated a duty of good faith and fair dealing owed to the borrower. Approximately 40% of directors and officers (D&O) policy claims paid fall under the lender liability insuring agreement of the policy. Almost half lender liability paid claims are brought forth by commercial borrowers because of the complexity of commercial lending. Most lender liability complaints are filed against the bank entity, but individuals can also be named.

All lender liability policies have different insuring agreements, different triggers, and different exclusions. Perhaps the biggest difference between lender liability policies is between standard and broad-form lender liability policy forms.

- A standard lender liability endorsement form on a bank's Management Professional Liability (D&O) policy covers suits brought by borrowers and guarantors only.
- A broad-form lender liability endorsement form on a bank's Management Professional Liability policy covers suits brought by borrowers, guarantors and other third parties such as other financial institutions, contractors, spouses, etc.

The most common lender liability complaints against a bank involve matters of breach of contract, fraud, breach of the implied covenant of good faith and fair dealing, breach of fiduciary duty, negligence, economic duress and misrepresentation. These claims include:

- Wrongfully refusing to honor a loan commitment.
- Wrongfully refusing to honor an alleged "side deal" that is not clearly spelled out in the loan agreement.
- Wrongfully refusing to renew a loan.
- Negligently processing or administering a loan.
- Misrepresenting information about a borrower in responding to credit inquiries.
- Threatening to take enforcement action which the lender does not carry out, but which causes the customer to act to their detriment.
- Improperly foreclosing a deed, trust, mortgage or security agreement without giving the required notice or otherwise following proper statutory procedures.
- Selling a borrower's collateral for less than its fair market value.
- Interfering, to the borrower's detriment, with a borrower's day to day management or contractual relations with third parties.
- Breaching a fiduciary duty that may have arisen or that a lender may have assumed either purposely or inadvertently with respect to the borrower.
- Violation of consumer lender laws or regulation.

The type and frequency of lender liability claims are constantly increasing, especially in our current economic climate. Many borrowers are no longer accepting foreclosure as a consequence of their inability to repay the loan. Often, a countersuit is filed stating the bank took advantage of the unsophisticated borrower by making them agree to terms they did not understand. In addition, borrowers are also alleging the lender violated certain

federal or state laws that are in place to protect borrowers for illegal lending practices. Even if the bank does everything right, the bank risks a jury empathizing with the borrowers rather than the lender, given banks continue to face an ever-increasing regulatory and public perception challenges.

Here are a few items to review and consider:

1. What is the insurance carrier's definition of lender liability?
2. How many days are required to put a carrier on notice after discovering a potential matter?
3. Are the directors, officers, employees and bank entities covered?
4. Will a paid claim under the lender liability endorsement reduce the future limit for other insuring agreements within your D&O policy?
5. Is it the banks or insurer's duty to defend?
6. In the event the insured wants to settle a claim, but the bank does not agree to the terms, will the bank be responsible for a part or all future defense expense and settlement (Hammer Clause)?
7. Does the lender liability insuring agreement cover complaints brought by guarantors and third parties?

Even if the bank does everything right, the bank risks a jury empathizing with the borrowers rather than the lender, given banks continue to face an ever-increasing regulatory and public perception challenges.

8. Does the lender liability insuring agreement include coverage for loan participations?
9. Is the lender liability limit adequate compared to the bank's legal lending limit and exposure?

Want to know more? Contact Mitch Florea with Nebraska Bankers Insurance and Services Company (NBISCO) at the NBA for a comprehensive discussion and review at mitch.florea@nebankers.org or 402-904-7014.

Information for this article was gathered from Insurance Institute of America (IIA) and American Bankers Association (ABA).

Protection For Lenders — The Effective Financing Statement And Key Court Decisions

Randy Wright, Nick Buda, Partners at Baird Holm LLP, **and Sapphire Andersen,** Law Student and Summer Associate, Baird Holm LLP

IN TIMES OF ECONOMIC STRESS, FARMERS SOMETIMES SELL THEIR crops or livestock without paying their lenders. One of the tools lenders have for protecting their security interest in farm products is to comply with the Food Security Act of 1985 (the FSA) and, in a central filing state such as Nebraska, to file an effective financing statement (EFS) with the Secretary of State. This article will discuss the FSA's impact on Nebraska lenders' security interests in farm products, the filing requirements of an EFS, and select cases.

Security Interests in Farm Products

The Uniform Commercial Code (UCC) provides that when a buyer purchases farm products from a farmer, the buyer buys them subject to the security interest of the farmer's lender. See UCC § 9-320. In other words, the farm products are not purchased "free and clear" of the lender's security interest. Buyers of farm products have objected to this system because, among other things, it was sometimes difficult to ascertain from a UCC search the identity of the lenders who claimed a security interest in particular crops or livestock. Buyers were sometimes subjected to double-payment liability if, for example, they bought farm products from the farmer, but failed to include the lender's name on the check to the farmer.

To address this concern, the FSA was enacted. It pre-empts the UCC, in part, by providing that a buyer, who in the ordinary course of business buys farm products from a farmer, does so free of the lender's security interest unless: (1) within one year before the sale the buyer has received from the secured party written notice of the lender's security interest in the farm products (a direct notice); or (2) for products produced in a state with a central filing system, the secured lender has filed an EFS identifying the farm products. Nebraska adopted a central filing system requiring a lender to file an EFS, with the Secretary of State. Neb. Rev. Stat. § 52-1301, et seq. It is important to understand that filing an EFS or providing direct notice, is not a substitute for the filing of a UCC financing statement. A UCC-1 financing statement still provides the lender with critical protections as to its borrower and others.

Not all lenders choose to file an EFS. Lenders may prefer not to file because doing so requires additional training of its employees and resulting expense. Some lenders may not have realized the serious losses that can result when their borrower becomes insolvent, and therefore feel that the filings are not necessary. However, when a borrower nears insolvency, having an EFS on file, or providing notice in a direct notice state may give the lender important protection. Lenders, from time to time, make mistakes in their EFS filings, which can result in losing the FSA's protections.

EFS Requirements

Nineteen states — including Nebraska — have a central filing system. All other states are, therefore, direct notice states. For central filing states, a lender must provide the following information in its EFS, and then file it with the Secretary of State:

1. The name and address of the secured lender;
2. The name and address of the secured lender's borrower;

3. The social security number or tax identification number of the borrower;

4. A description of the farm products subject to the security interest;

5. Each county in Nebraska where the farm product is produced or located;

6. Crop year, unless every crop of the farm product in question, for the duration of the effective financing statement, is to be subject to the particular security interest; and

7. Additional details of the farm product subject to the lender's security interest if needed to distinguish it from other quantities of such product owned by the same borrower, but not subject to the particular security interest.

Neb. Rev. Stat. § 52-1307(4).

Once filed, an EFS is effective for five years and may be extended for an additional five year period with an additional EFS or continuation statement. If a material change occurs with the lender's borrower, such as a change in the borrower's name, the lender must amend the EFS within three months of that change.

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The key issue was where the cattle were "produced." If they were produced in Missouri, a direct notice state, then the bank would not have complied with the FSA by filing in Oklahoma. If the cattle were found to have been produced in Oklahoma, then the bank would prevail.

Court Decisions — When is an EFS Seriously Misleading?

EFS filings, like traditional UCC-1 financing statements, must not be "seriously misleading." See Lisco State Bank v. McCombs Ranches, Inc., 752 F. Supp. 329, 337 (D. Neb. 1990). One court ruled an EFS that contained a borrower's trade name, instead of the borrower's legal name, was not seriously misleading where the purchaser of farm products also had actual knowledge of the identity of the borrower. See Peoples Bank v. Bryan Bros. Cattle Co., 504 F.3d 549, 559 (5th Cir. 2007); see also Farmers & Merchants State Bank v. Teveldal, 524 N.W.2d 874 (SD 1994) (EFS, which contained an incorrect EFS code number for the collateral — hogs — did not make the statement seriously misleading). According to the Court in Peoples Bank, an EFS will not be "seriously misleading" as long as "the financing statement (EFS) contains sufficient information to put any searcher on inquiry." Peoples Bank, 504 F.3d at 559.

Other courts might disagree with the Peoples Bank decision. In re Borden, the Nebraska Bankruptcy Court determined that a lender's UCC-1 financing statement (not an EFS) was "seriously misleading" where it used the debtor's nickname — "Mike Borden" — instead of the debtor's full legal name — "Michael Borden." In re Borden, 353 BR 886, 892 (Bankr. D. Neb. 2006); see also in re Tyringham Holdings, Inc., 354 BR 363 (Bankr. ED Va. 2006) (holding financing statement was seriously misleading where the lender omitted the "Inc." from the debtor's legal name). Putting the borrowers' full legal name on the EFS, and not a trade name, is most likely the better practice.

When Farm Products Move Across State Lines — EFS or Direct Notice?

Between two systems — direct notice and the central filing — conflicts may arise when products move across state lines. If a lender properly complies with the FSA in a central filing system state by filing an EFS, is their interest still protected if the secured farm products are transported or sold in a state using the direct notice system? The answer is not always clear.

A Colorado court addressed this question in a case involving the purchase of cattle from an Oklahoma debtor, Great Plains Nat'l Bank v. Mount, 280 P.3d 670 (Colo. Ct. App. 2012). The cattle were purchased in Missouri (a direct notice state), transported to and inspected in Oklahoma (a central filing state) for one day, and then shipped to the buyer in Colorado (a central filing state). The debtor's bank filed an EFS in Oklahoma.

The key issue was where the cattle were "produced." If they were produced in Missouri, a direct notice state, then the bank would not have complied with the FSA by filing in Oklahoma. If the cattle were found to have been produced in Oklahoma, then the bank would prevail. The court determined that "produced" meant "the location where farm products are furnished or made available for commerce." The court held that the cattle were produced in Oklahoma because that was where the cattle were furnished for sale. The reason the court gave for this decision was to avoid burdening buyers who might otherwise have to investigate where farm products originated (not an easy task as to livestock) in order to comply with that state's rules.

While this Colorado decision is not binding outside of Colorado, it provides insight for lenders. The court's opinion did not include details about the origin of the cattle, such as where the cattle were born and raised, because the Colorado court interpreted the FSA with a focus on the state in which the sale of farm products occurred. See also Fin-Ag, Inc. v. Pipestone Livestock Auction Market, Inc., 754 N.W.2d 29, 33–37 (SD 2008). This leaves remaining uncertainty about where to file or provide notice if the origins of farm products, like livestock, are unknown. Until further clarification is given, lenders should consider filing or providing direct notice in all states where farm products have been known to be located.

Conclusion

The FSA was enacted to help to protect both lenders and buyers of farm products. In a central filing state like Nebraska, a lender seeking to preserve its security interests in farm products should complete and file an EFS. For products produced in "direct notice" states, a lender should send the required direct notice. Failure to comply with FSA notice requirements may allow a purchaser to buy farm products free and clear of the lender's security interest, leaving the lender with recourse only against its borrower.

A list of central filing systems states is available at: Clear Title (Central Filing Systems), UNITED STATES DEPARTMENT OF AGRICULTURE, https://www.gipsa.usda.gov/laws/cleartitle.aspx (last updated Nov. 16, 2015).

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Should I Test Employee Security Awareness?

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Becoming a Coach

If you've ever volunteered to coach youth sports — especially T-ball — you've probably learned as much as the kids about how to teach and train someone to perform an activity. The first lesson of coaching: it involves repetition. When I helped coach T-ball, our first day of practice involved running to first base over and over and coaching kids to listen to the first base coach. We spent a lot of time on the fundamentals and basics of baseball. When all is said and done, the purpose of T-ball is to provide the kids with a basic knowledge of the game and awareness of what to do when the ball is hit.

The goal of security awareness training should be similar to coaching T-ball. We should understand that the audience is not full of security experts, and we need to provide basic knowledge and appropriate action to take when faced with an incident. We also need to repeatedly test the effectiveness of the training program. Unlike T-ball, however, we need to keep score, not to shame an employee but to measure our coaching. Verifying employees have retained this information and will deploy their training in the future is the key to a successful security awareness program.

Common Testing Methodologies

Quizzes

Administering a quiz after a training session is a common testing approach, but quizzes are ineffective if using a one-and-done approach. Remember, coaching is repetition. Random web-based quizzes throughout the year may provide a better measurement unless employees share answers.

Workplace Security Review

Employees can become desensitized to confidential information in the work area. A great way to test your clean desk policy and physical security policy is to observe your workplace. Take pictures of any security violations — it is the best form of evidence — and share the results of your physical checks during your next security awareness training session.

Dumpster Diving

Dumpster diving can literally be a treasure trove of information for anyone who wants to create a highly successful social engineering campaign. A pair of latex gloves is always recommended for this test. One of the best (cleanest) methods to perform this test is to follow the cleaning crew around after business hours and observe what information is being disposed of as ordinary garbage (not in shred bins; that's where you want employees to put confidential information).

Pretext Phone Calls

In larger organizations, pretext phone calls may be performed by an internal resource that isn't well-known or by an outsourced auditor or consultant. The tester can perform the test via the phone (voice/text) or internet (email/chat) posing as a customer, vendor, or business partner who is requesting confidential information or login credentials. The tester needs to have a good cover story as to why the information is needed. Testers will often use popular spoofing tools to display local area codes, phone numbers, and alias names when impersonating a person or company.

Physical Impersonation

We have all likely performed this test once in our life without realizing it. As an example, when I go to the gym, the attendant is supposed to swipe my card to grant and track my access. However, if I have my earbuds in and stare at my phone, I'm allowed to walk by unchallenged. I look like I belong at the gym; why inconvenience me? If a tester looks like they belong to your organization, will your staff challenge their identity?

Flash Drive Drop Attack Test

Another great test is to bait users with a "lost" USB (Universal Serial Bus) flash drive. How many employees will call IT? How many will plug the device into a company workstation? This test may be performed by capable IT Staff with help from the internet or performed by an outsourced auditor or consultant.

Phishing Attack Simulation

One of the best ways to determine if your employees are aware of the threat posed by a phishing attack is to perform a controlled test (simulated attack) of employee email. Test emails should provide clues covered in training that should tip the recipient of the deception. Directing the recipient to a website link will allow the tester to gather evidence of who opened the email and who followed the link. Such testing may be performed by skilled staff or by a third-party provider. It is recommended that testing be performed throughout the year to maintain employee awareness.

Measuring Results

Share the test results with the management team by documenting your findings using generic terms such as passwords written down and stored within eyesight, confidential information stored in unlocked desk drawers after hours, etc. Avoid using names of employees in the written reports but be prepared to offer details when asked. Keeping in mind the goal is not to demean an employee but improve the organization's security awareness. The risk of social engineering attacks cannot ever be 100% mitigated, but you should strive to improve the results (fewer violations) each year.

Employees should be informed that such testing may occur at random. The results of testing should be shared with employees to emphasize the fundamentals in the test that should have raised a red flag and the actions that users should have taken.

Security awareness and testing methodologies must continue to evolve with attack methods, and the best way to provide evidence of progress is to monitor performance through observation testing.

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.

Foreclosure Protection: Where are We Now?

Chris W. Bell, Associate General Counsel at Compliance Alliance

THE COVID-19 PANDEMIC HAS CHANGED AMERICAN LIFE AS WE know it. As the country continues to deal with the health crisis, the effects of containment measures ripple through the American economy. Unemployment remains high as state economies expand and contract in inverse proportion to the virus's spread. Regulators are in an arms race with rapidly changing markets, forcing banks to adapt to an ever-changing regulatory landscape. Even as we struggle to deal with the immediate concerns, we know the effects of this pandemic will be with us for some time. Economic shocks will continue to reverberate and play out in the housing markets around the country. As we shift into the next phase of operating in the pandemic and consider what options exist to help struggling mortgage borrowers, we should take note of the status of the expansive mortgagor protections passed by Congress, federal agencies, and other government authorities.

Protection for Federally Backed Mortgage Loans

In the early days of the pandemic, Congress passed the Coronavirus Aid, Relief, and Economic Security ("CARES") Act. One of the primary sections of this law established a 60-day moratorium on foreclosure proceedings against homeowners with federally-backed mortgage loans. The CARES Act's mortgage foreclosure moratorium applied to single-family residential mortgage loans secured, guaranteed, or made by FHA, USDA, VA, or Fannie Mae or Freddie Mac. Originally scheduled to expire at the end of June, the various agencies extended the moratorium on foreclosures and evictions until at least August 31, 2020.

The CARES Act also granted federally backed mortgage loan consumers, experiencing financial hardship related to the COVID–19 pandemic, the right to request six months of forbearance (with an option of six additional months), regardless of delinquency status. Congress prohibited servicers from charging any fees related to this forbearance. Mortgage delinquency status is frozen in place during forbearance, even if the bank suspends payments during the forbearance. As it stands today, customers can request forbearance under the CARES Act until the earlier of the end of 2020, or the end-date of the national emergency concerning the novel coronavirus disease outbreak declared by the president on March 13, 2020, under the National Emergencies Act.

State and Local-level Protection

Many state and local authorities enacted policies to protect mortgage borrowers and renters. The details of these state and local foreclosure bans vary. Banks should refer to the official websites for their state and local governments to assess the scope and requirements of applicable prohibitions. While effective dates vary widely, many of these protections remain in effect until respective governors lift statewide emergency declarations.

Private loans

The CARES Act provided no relief for loans that are not federally-backed. Banks should refer to the appropriate investor guidelines for mortgages sold to private investors. Banks should refer to guidance from its regulators concerning their expectations regarding non-federally-back mortgage loans held in portfolio.

Troubled Debt Restructuring ("TDR")

If neither a federal nor state moratorium applies to a residential mortgage you hold in portfolio, you may still be able to exercise your authority to assist pandemic-effected borrowers who are struggling financially. Regulators have urged banks to work with customers and prudently modify loans in a safe and sound manner. Section 4310 of the CARES Act provided banks relief from TDR. In April, regulatory agencies issued revised interagency guidance to help banks sort modification requests into three groups: (1) loan modifications covered by Section 4310 of the CARES Act; (2) those outside of Section 4310 deemed not to be TDRs; and (3) those outside of Section 4310 that may be TDRs. In June, regulators released new interagency safety and soundness examiner guidelines. These guidelines instruct examiners to not criticize institutions for doing so as part of a risk mitigation strategy intended to improve existing loans, even if a restructured loan ultimately results in adverse credit classifications.

To be covered by Section 4310 of the CARES Act, a loan modification must: (1) relate to COVID-19, (2) be executed between March 1st and December 31st (assuming the current national emergency does not end earlier than the end of the year), and (3) the underlying obligation must be not more than 30 days past due. If a loan modification meets these three criteria, financial institutions do not have to report it as a TDR; however, the financial institution should maintain records of the volume of such loan modifications.

If a loan modification fails to meet any of the three criteria for Section 4310 coverage, it does not automatically result in a TDR. Regulators will deem a modification as not to constitute a TDR if it relates to COVID-19, extends no more than six months, and the underlying obligation is not more than 30 days past due. The only subjective criterion is the relationship of the modification to COVID-19. As a best practice, banks should have the borrower certify that the requested change is due to COVID-19. To not raise HIPAA concerns, the certification should be general and not address specific health details. While such a certification is not required to be in the loan file, it would show future examiners that the lender followed the guidance in good faith. If a bank receives a modification request that is outside the scope of Section 4310 and does not meet the described criteria, the bank should assess whether the modification would be a concession to the borrower that the bank would not otherwise consider and act accordingly.

As with everything related to the COVID-19 pandemic, expect mortgage foreclosure protections to change as the country continues to deal with the long-term effects of our national crisis. The federal agencies may extend the protections relating to the loans they back, and Congress will undoubtedly reassess the CARES Act's protections as the end of its covered period draws near. Despite how things change, you can count on the Texas Bankers Association to bring you the most up-to-date information available as we walk hand-in-hand through this crisis.

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