Nebraska
Banker
MARCH/APRIL 2022
NBA Nebraska Bankers Association

Nebraska Bankers: Past, Present and Future

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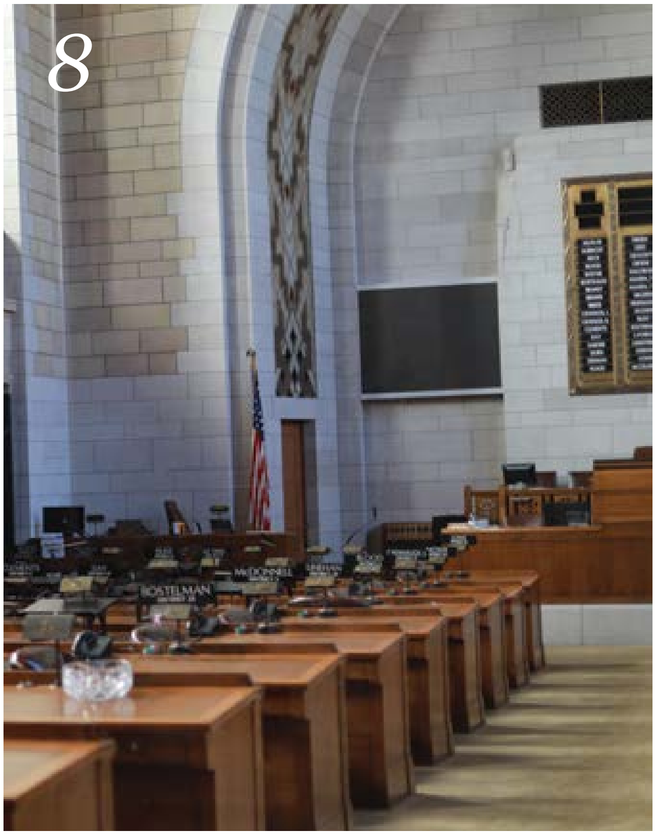
CONTENTS



Nebraska Banker
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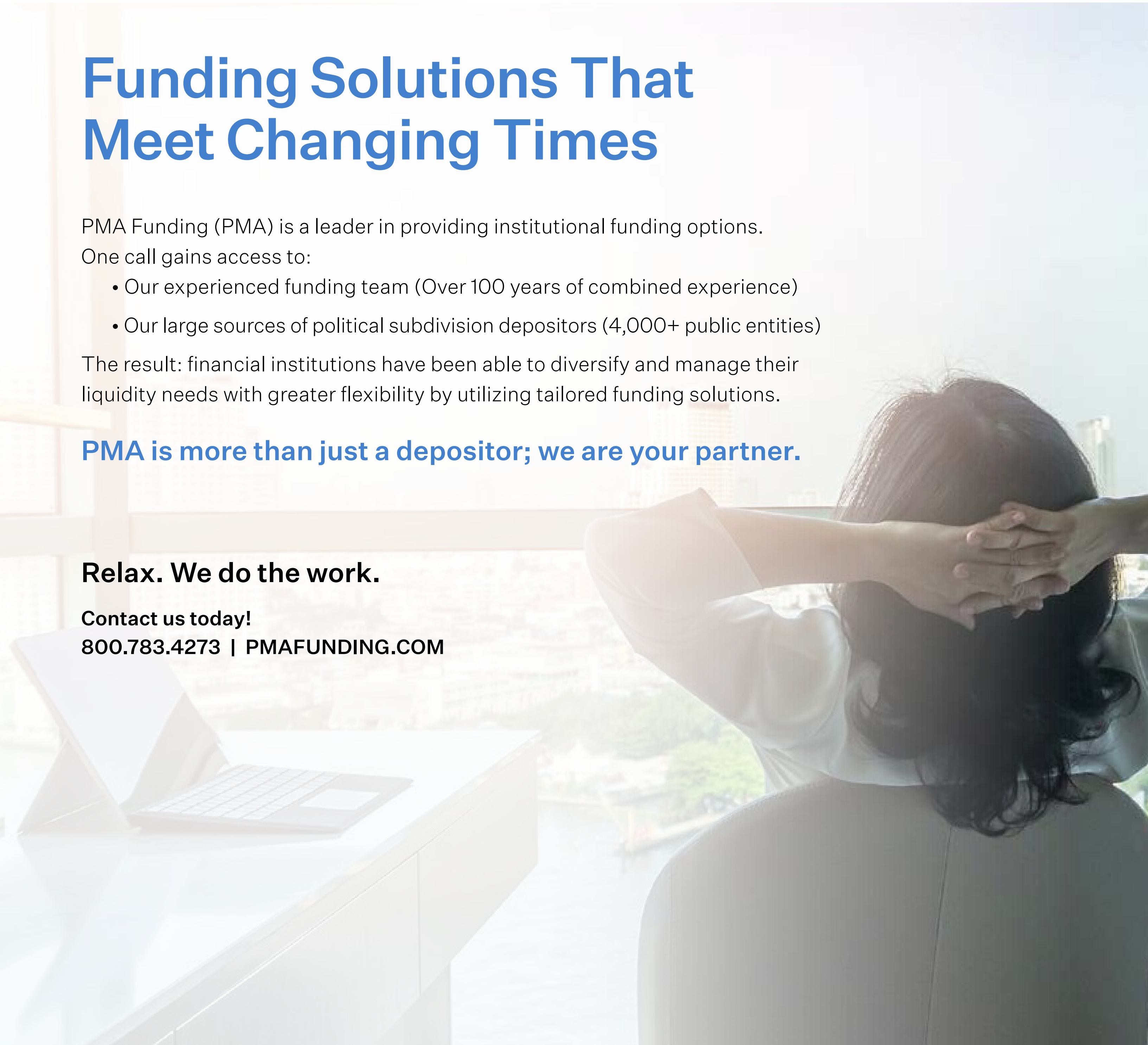

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EDUCATION CALENDAR

APRIL 2022

Demystifying Cryptocurrency Webinar
April 18
Virtual

MAY 2022

NBA Annual Convention
May 4-6
La Vista, NE

Operations School
May 10-12
Lincoln, NE

Small Business Lending Virtual Workshop
May 24-25
Virtual

JUNE 2022

NBA Annual Golf Outing
June 9
Hastings, NE

Preparing for Your Next IT Exam Workshop
June 14
Virtual

Relationship & Business Development School
June 28-30
Manhattan, KS

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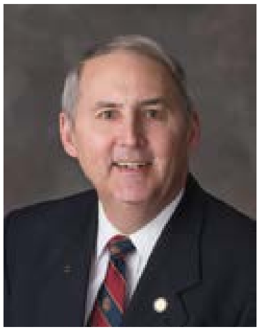
Nebraska Bankers:

Past, Present and Future

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


Sen. Rob Clements


Sen. Mike Jacobson


Sen. John Stinner


Sen. Matt Williams

NBA FRIENDS,

Congratulations to Nebraska Banker and former NBA Chair Mike Jacobson on his recent appointment as the State Senator for Legislative District 42, which includes North Platte. He brings a great deal of knowledge, experience and leadership background to this position.

If you follow Nebraska's government, politics or history, you know that the 49-member unicameral Legislature is the only single-house legislature in the country. The body's nonpartisan structure is also unique. While not perfect, the current system allows for substantial public input, dialogue and collaboration on important public policy issues.

The banking industry is fortunate to have four bankers who hold seats and vital committee and leadership assignments within the Legislature.

Former NBA Chairs John Stinner (District 48) and Matt Williams (District 36) were elected in 2014 and reelected in 2018. Because of term limits, both are serving in their final year at the Legislature.

Sen. Stinner serves as Chair of the Appropriations Committee. He has guided the state's budget through both periods of shortfalls and excessive revenues, including navigating the challenges of the pandemic. He is especially diligent about growing and protecting the state's Cash Reserve Fund and questioning the long-term returns on state program expenditures.

Sen. Williams serves as Chair of the Banking, Commerce and Insurance Committee. He works closely with the banking industry and your NBA government relations team on issues like financial elder abuse protections, creating the state's Single Bank Pooled Collateral Program, cryptocurrency bank

charters, financial literacy standards and workforce housing. His banking experience has proven invaluable in navigating these complicated topics.

Another banker, Sen. Rob Clements (District 2), was appointed and subsequently elected to his position in 2018. He serves as a member of the Appropriations Committee, where his background in budgeting and actuarial science has been a valuable asset. Sen. Clements is currently running for reelection.

I am especially thankful for the past, present and future public service of these bankers. Recruiting and electing competent leaders who can process and analyze complicated issues while seeking win-win scenarios cannot be understated. Voter-implemented legislative term limits have altered the number and experience of the candidates who are willing to put their names on the ballot. Term limits have also reduced the long-term institutional knowledge within the body. In addition, the $12,000 salary for state senators makes pursuing a legislative seat financially impossible for a significant number of potential candidates.

Nebraska bankers must proactively encourage candidates to run for local, state and national elected offices. Bankers can get involved by vetting and recruiting candidates, hosting candidate coffees or fundraisers, putting up campaign signs or flyers and other activities. Your bank and its employees could also contribute to efforts like the NBA BankPAC. At the direction of the NBA BankPAC Committee, these collective banker funds support pro-banking and pro-business candidates.

Finally, as leaders in your community, I strongly encourage you and/or members of your bank's staff to consider running for office like the four bankers currently serving in the Legislature!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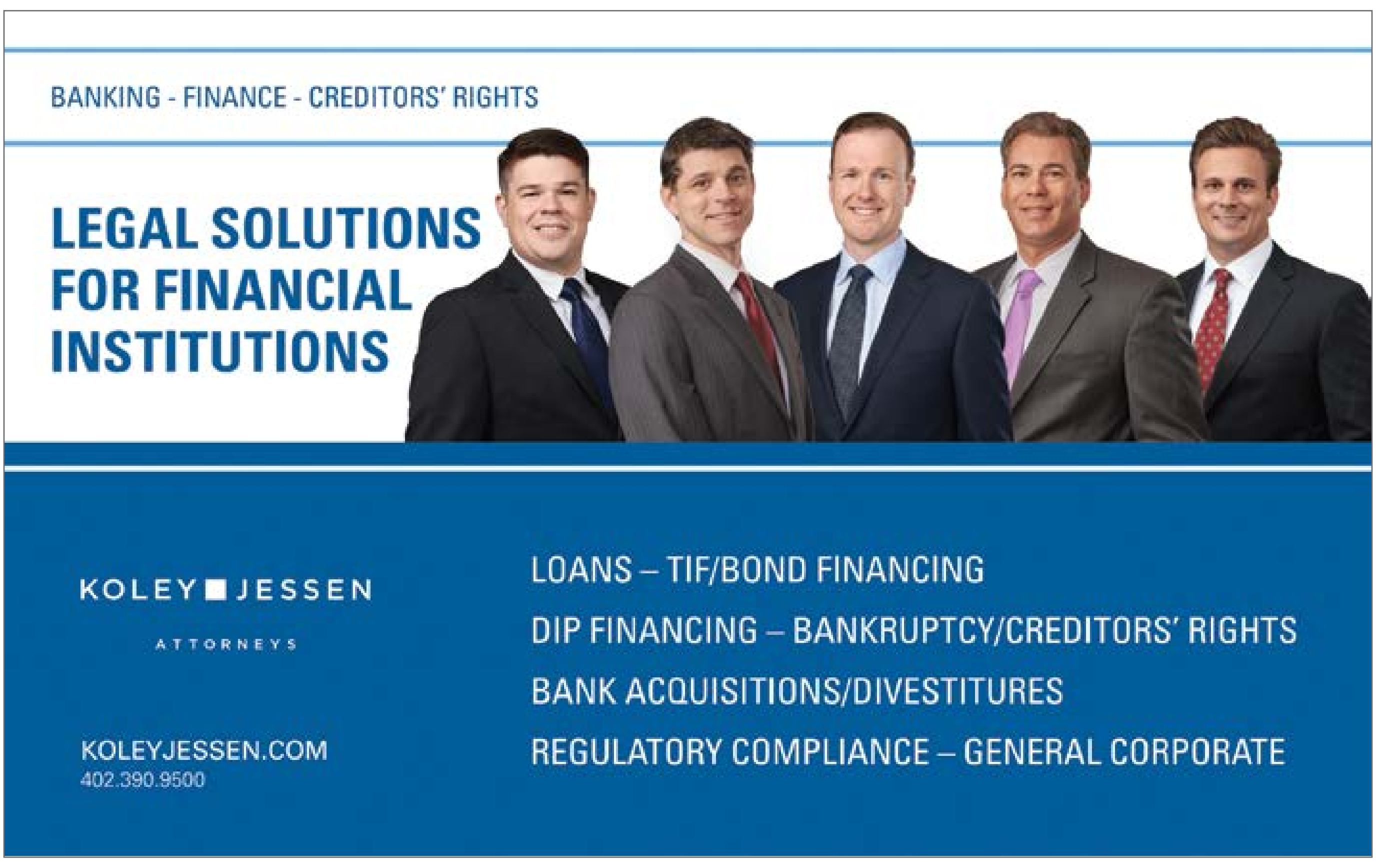
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WASHINGTON UPDATE

Leaders in Financial Literacy:

Bankers Celebrate 25 Years of Teaching Children to Save

Rob Nichols, American Bankers Association

PROVIDING CHILDREN WITH A STRONG BASE OF FINANCIAL knowledge is critical to helping them unlock their financial future and prosper as adults – and bankers are uniquely positioned to play a role in that process.

This year, the ABA Foundation celebrates a major milestone as we commemorate the 25th anniversary of the Teach Children to Save financial literacy initiative. Since 1997, Teach Children to Save has brought students in grades K-8 important lessons about money and real-world financial concepts – from saving and spending to budgeting and keeping their money safe.

With the help of bankers nationwide, Teach Children to Save has reached a total of *9.5 million* students to date. (If you're looking for something to compare that to, it's roughly the number of people who live in the state of New Jersey.) Add in the ABA Foundation's other financial education program for teens and college-age students, Get Smart About Credit, and that number grows to almost 11.8 million children and young adults who have benefitted from the foundation's financial education curriculum (that's a population roughly equivalent to the population of Ohio).

Teach Children to Save began by providing bankers with tools and resources to enable them to take lessons on financial literacy topics into classrooms in their communities. Over the years, it has evolved and adapted to changing needs and preferences of younger generations – including pivoting to be heavily focused on virtual learning during the COVID-19 pandemic.

This year, as the program celebrates its "silver jubilee," the foundation is placing a particular emphasis on bringing financial education to students through video and will be rolling out three short videos this spring designed to deliver engaging, age-appropriate lessons by grade level. (And speaking of video, students also have the opportunity to participate in the foundation's Lights, Camera, Save! program, through which they channel their creativity and produce their own video showcasing their financial knowledge. Learn how your bank can get involved at no cost by visiting aba.com/LightsCameraSave.)

In honor of Financial Literacy Month, the foundation observes Teach Children to Save Day in April, but bankers' efforts to raise awareness about financial education are by no means confined to one day. In fact, Teach Children to Save encourages bankers to advance financial literacy throughout the year in whatever way they choose. To help banks engage on social media channels, the foundation has created a free Teach Children to Save communication toolkit for participating banks to use. The kit includes everything from social media posts, letter templates and graphics – everything your bank needs to spread the word about financial education.

As we work toward the collective goal of increasing financial health in the U.S., reaching out to young people is a great step bankers can take. When bankers engage with the younger members of their communities, it does more than simply provide students with the "nuts and bolts" of financial education – it allows them to interact with their local bank and understand that the two million women and men working in the banking industry are invested in their success. They have the opportunity to see bankers as teachers, experts and as trusted resources in their communities, and they can begin to see the value of having a relationship with a bank.

With all of the financial hardships families have experienced over the past two years, it's more important than ever that the next generation is given the tools and knowledge they need to make prudent financial choices as they grow up. And so, I hope each and every one of you will make the commitment this year to join with the ABA Foundation, take advantage of all the free resources available, and participate in Teach Children to Save and our other financial education initiatives. With your help, we can keep these programs going strong for another 25 years and beyond.

To learn more and register for Teach Children to Save, visit aba.com/teach25. For questions on the ABA Foundation's financial literacy programs, contact ABA's Jeni Pastier at jpastier@aba.com.

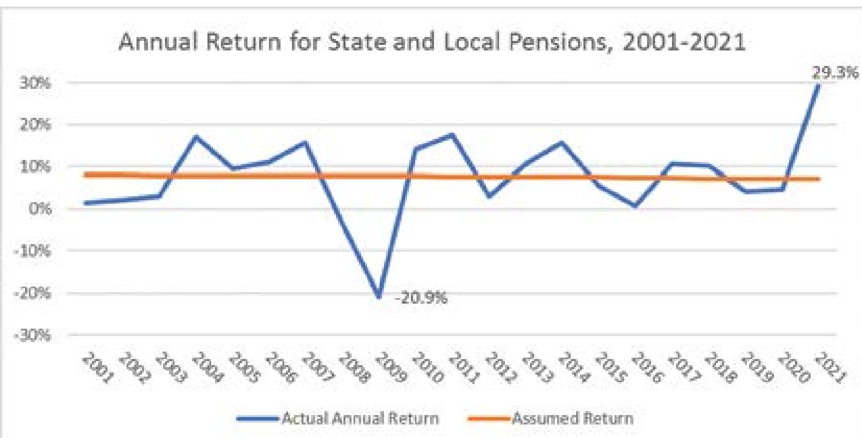
Public Pension Update

Dana Sparkman, CFA, The Baker Group

MUNICIPAL BOND INVESTORS finally have some good news regarding public pension plans after worrying about growing unfunded pension liabilities for many years. The Pew Charitable Trusts reports that aggregate state retirement systems are over 80% funded for the first time since 2008, following record investment returns for the fiscal year ending in 2021.

In an effort to earn higher returns in an era of low-interest rates, pension fund managers have broadly been shifting asset allocations to a higher concentration of risky assets such as private equity and hedge funds. The National Association of State Retirement Administrators (NASRA) reports that alternative investments comprised 21% of the investment portfolios of public pension funds surveyed in 2021 compared to only about 5% in 2005. According to NASRA, investment returns have historically accounted for 61% of public pension fund revenue from 1991 to 2020, making it a large contributor to the overall performance of a pension plan. This strategy of taking on more risk to potentially earn a higher return proved very profitable during 2021 as risky assets outperformed assumed rates of return, and most public pension plans earned returns greater than 25%, with some plans even hitting their highest single-year return in their history.

Many states have enacted reforms to their pension plans to help keep liabilities down in the future, but the impact of those reforms will be felt further down the road because they are often effective only for new hires.



Source: Public Plans Database; Census of Governments

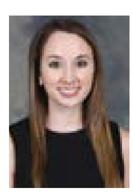
This is great news for municipal employers that participate in those pension plans, especially following investment underperformance in 2020 and a period of increasing annual required contributions. Most public pension plans now have better-funded positions and lower net pension liabilities, which should lead to lower growth in annual required contributions from municipalities and will help to relieve some budget pressure for those municipalities. The Pew Charitable Trusts estimates that contribution levels increased by 8% per year on average over the past 10 years, but the most underwater plans had contributions increase by 16% on average over that same time period. For some municipalities, coming up with funds for those rising contribution levels has become very difficult, and pension contributions have become a significant budget item. However, many state and local governments may be well-positioned today to make excess contributions and pay down some pension liabilities, since 2021 was also generally a year of large budget surpluses and revenue growth. For example, Connecticut has paid $1.7 billion from surplus cash into its state employee and teachers' pension funds in the last two years, and they may add an extra $6.3 billion over the next five years, according to Bloomberg.

While most public pension plans have recently improved financially, investors should remain wary of municipalities that have exposure to troubled pension plans for a few reasons. First, unfortunately, a single year of outstanding investment performance may not be enough to pull underfunded plans out of worrisome territory. The previously discussed increased allocation in highly risky assets makes plan assets sensitive and investment returns volatile. Moody has calculated that, in some instances, it would only take about a 5% loss next year to reverse the positive effects of a 25% return in 2021. Further, Moody anticipates a greater than one-in-six chance that a pension plan with a 7% assumed annual return will suffer a loss of 5% or more in a given year.

Second, unfunded pension liabilities are still very high and represent a large amount of debt. Moody's estimates that net pension liabilities are still above $4 trillion, larger than the municipal bond market, even after the high investment returns realized in 2021 when adjusting for a conservative investment return assumption. Many states have enacted reforms to their pension plans to help keep liabilities down in the future, but the impact of those reforms will be felt further down the road because they are often effective only for new hires.

Lastly, keep in mind that the statistics presented are aggregated to show broad trends. Individual states' plans may differ and may not be as well-positioned as the average plan, and some municipalities even have their own local plans, which could have drastically different funded positions and investment outcomes.

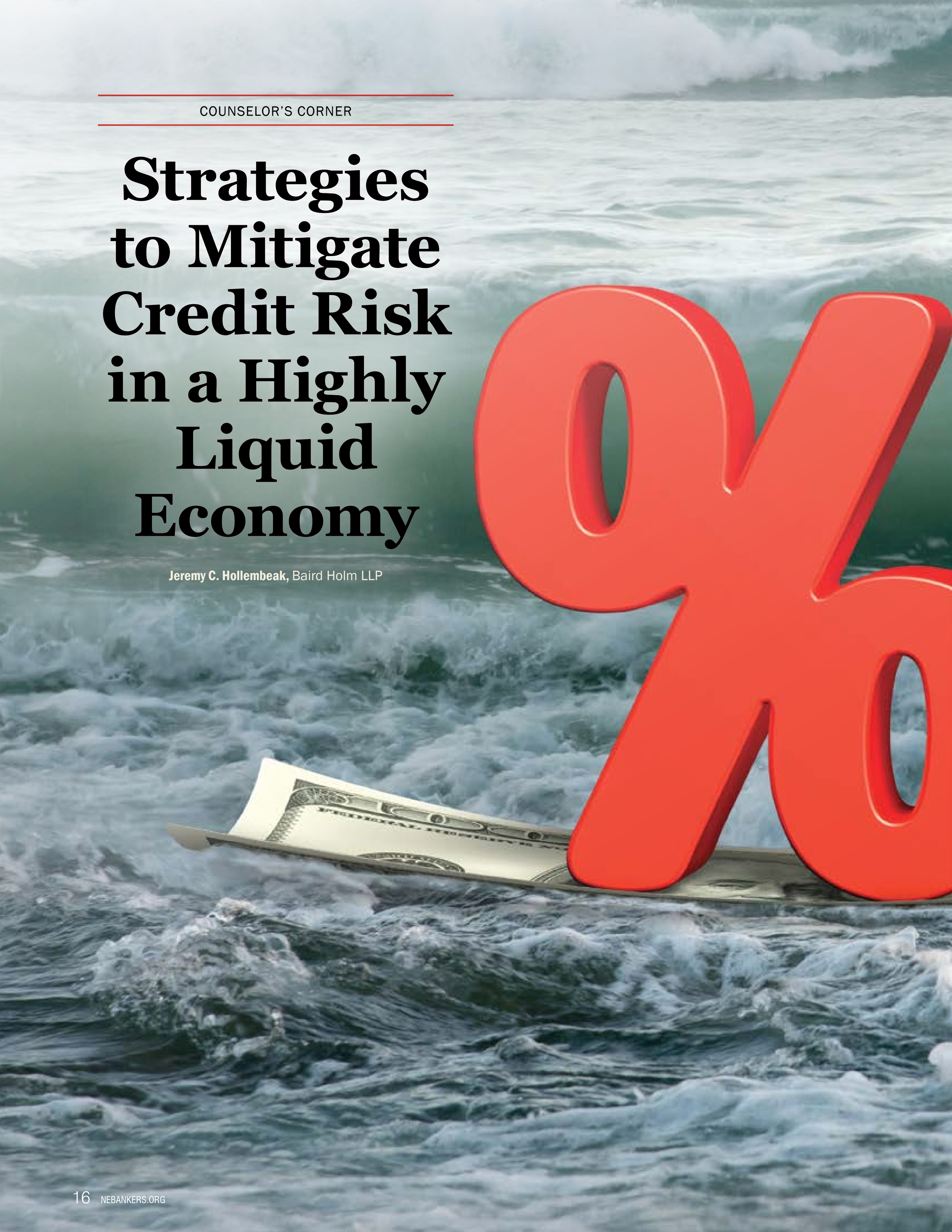
Despite the fact that it is comforting to know that net pension liabilities have generally fallen and that municipalities may benefit from lower pension contributions, prudent municipal bond investors should continue to carefully monitor individual municipalities' specific exposure to pension liabilities.



Dana Sparkman, CFA, is Senior Vice President/Municipal Analyst in The Baker Group's Financial Strategies Group. She manages a municipal credit database that covers more than 150,000 municipal bonds, providing clients with specific credit metrics essential in assessing municipal credit. Dana earned a bachelor's degree in finance from the University of Central Oklahoma as well as the Chartered Financial Analyst designation. Contact: 405-415-7223, dana@GoBaker.com.

Strategies to Mitigate Credit Risk in a Highly Liquid Economy

Jeremy C. Hollembeak, Baird Holm LLP



IF YOU ARE A COMMERCIAL OR agribusiness lender, it's likely been a while since you had a significant number of defaults in your portfolio. I wish I could tell you it's because your borrowers are all financially healthy and operationally disciplined. Unfortunately, borrower distress and problem loans have not been eradicated from commercial and agribusiness lending. They've just become much harder to diagnose.

A much better explanation for the lack of defaults is that a decade-long bull market and historically low-interest rates drove up asset values and created a lot of investor-class wealth. This, in turn, caused a massive influx of private money into the financial system, increasing competition among lenders and shifting the balance of power in favor of borrowers. Eventually, even small- and middle-market businesses found themselves able to borrow more than they ever had before. And borrow they did, with many of these businesses using their increased liquidity for controlled, sustainable growth. Many others, however, used it to cover up the effects of their poor business decisions, personal misfortunes and even fraud.

When the bull market ended in March 2020, it briefly seemed like the jig was up – that borrowers secretly in distress would finally be unmasked. But then, an unprecedented amount of government financial assistance in response to the COVID pandemic was indiscriminately doled out to good and bad businesses alike. The market rebounded and thereafter has remained robust. In short, the jig was not up, there was no unmasking, and to this day, many unprofitable and overleveraged borrowers continue to look from the outside like good businesses with low risks of default.

Now I could tell you a down-cycle is imminent – that it's only a matter of time before you start seeing a sharp increase in defaults as a result of supply chain disruption, interest rate hikes and growing inflation driving up the cost of doing business. But frankly, no one can say with any certainty when the next downturn will happen. Plus, I bet by now someone like me has been telling you "this is the year the music will finally stop" for at least five years running, and you're understandably sick of hearing it.

Instead, let's assume the music keeps playing for a while, and as long as it does, the default rate in your loan portfolio remains very low. This period – from today until the next wave of defaults finally arrives – presents a golden opportunity for you to nip potential problem loans in the bud before they cause you actual problems. The challenge, however, is determining which among all the performing loans in your portfolio should be labeled as "problems" and given your attention. Because of high liquidity levels and greatly appreciated asset values, historical indicators of distress such as payment defaults and blown leverage ratios can no longer be relied on as early warning systems. Without new, more effective strategies for identifying those borrowers most likely to default, commercial and agribusiness lenders are taking on materially greater risk than you were ten, five or even two years ago.

Here are five strategies you can use to effectively mitigate this additional hidden credit risk:

1. **Take advantage of available opportunities to enhance collectability.** To state the obvious, it's not a viable lending practice to start requiring additional credit support from borrowers at a time when they are making all required payments and

Counselor's Corner – continued on page 18

have not triggered serious non-payment defaults. So your best opportunity to identify problem loans and enhance their collectability comes when borrowers request their existing loans be extended, rolled over or consolidated with new extensions of credit. Too many lenders agree to these requests in exchange for little or nothing in return, even though most borrowers would be willing to grant concessions under these circumstances. These opportunities are the doorway to implementing other enhancements discussed below.

2. **Look for signals of distress in non-obvious places.** You don't have to rely on the borrower to give you the information you need. You may be surprised what people make publicly available about themselves, their friends and family members. Investigate and see if you come across anything worth asking the borrower about (e.g., pictures posted on social media showing the borrower driving around town in his new sports car the same day he asked you for a loan extension). Also, if you have access to the borrower's bank statements (e.g., under a deposit account control agreement), have someone review the borrower's recent cash flow activity. In addition to helpful information about the borrower's business relationships and spending priorities with other creditors, you may find undisclosed assets, new business ventures or even evidence of fraud. For example, in a recent lender engagement, I discovered the borrower, who had been in default and not paid my client for several years, had entered into an undisclosed land sale contract that he was using to siphon off and hide my client's cash collateral. Reviewing the borrower's account statements, I noticed small but frequent payments over the last few years, all going to one individual (a relative of the borrower). Upon further investigation, that individual turned out to be the record owner of farmland he was "selling" to the borrower in exchange for payments that should have been used to repay my client. If that had been one of your borrowers and even assuming he was current on his payments, would you agree to roll over his loan? To lend him additional money?

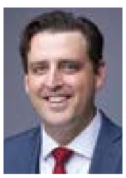
3. **Enhance collectability by fixing mistakes in the original loan documents.** Take the time to have someone carefully go over the original loan documents and check for any mistakes or omissions, whether any assumptions made when the loan was originated need adjustment, and whether you continue to have valid, perfected security interests in all of your original collateral. Then ask the borrower to agree to any amendments needed to correct or adjust the original loan documents. Because these enhancements merely ensure the original intent of the parties is realized, an honest borrower should not push back on this request.

4. **Enhance collectability by securing additional new collateral.** This isn't a novel concept, although lenders already using this strategy don't always benefit from traditional grants of additional collateral (e.g., taking a second lien in assets that would fail to produce enough proceeds to pay off the first lien in an enforcement scenario). Lenders should think "outside the box" when requesting additional collateral. Try requesting a lien in an asset of particular importance to a borrower requesting a rollover or extension, even though the asset itself may have little or no liquidation value in your hands (e.g., trademark and brand assets in a borrower's pet project). Remember, borrowers can only lose assets they pledged as collateral if they are unable or unwilling to fulfill their contractual obligations. If you ask for more collateral and a borrower pushes back too hard, it may mean the rollover or extension they requested involves greater credit risk than you thought before you asked. Finally, those who lend to businesses entitled to receive government assistance payments may be able to take a lien in those payments under certain circumstances. For example, a lender to a farmer receiving federal farm program payments may collect those payments if the farmer previously assigned them to the lender as collateral by executing the proper Farm Service Agency paperwork.

5. **Explore and exploit opportunities to sell loans to distressed investors.** Too many banks and traditional lenders ignore opportunities to get rid of "problem" loans until it is too late. Today's secondary market is saturated with private capital providers looking to invest in distressed situations of virtually all sizes and risk levels. Typically, these investors provide additional rescue financing and turnaround expertise that original lenders can't or won't provide, with an expectation the borrower will return to financial health and payoff both the rescue financing and existing loan in full. As a result, these investors will often purchase existing loans for a price near or even above the returns originating lenders would realistically collect if they retained and worked the

loans themselves. Crucially, however, originating lenders' opportunities to find buyers at these price points comes before a borrower's distress has been compounded. Lenders who mindlessly roll over and consolidate their own positions until their borrowers are completely out of cash flow and unencumbered assets and have no clear paths to rehabilitation cannot then go to the secondary market and expect to find a buyer for their position.

Unprecedented liquidity and asset appreciation may have pushed the day of reckoning for distressed borrowers off into the future, but it is saddling commercial and agribusiness lenders with additional credit risk now. Start using these strategies today to mitigate that risk by identifying which of your borrowers may be in distress and maximizing the collectability of your potential problem loans.



Jeremy C. Hollembeak is an experienced financial restructuring and workout attorney at Baird Holm LLP in Omaha, Nebraska. He concentrates his practice on distressed investment opportunities and related litigation. Jeremy regularly negotiates debt purchase, refinancing and rescue financing transactions. He advises on disputes arising in distressed situations, developing and executing strategies to protect and enforce contract and collateral rights and collect on money judgments. His clients include banks, private capital providers, strategic investment funds and litigation funders.

THE GOLDEN RULE OF EMAIL

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The Golden Rule of Email

Nick Podhradsky, Executive Vice President, SBS CyberSecurity, LLC

ALTHOUGH PHISHING HAS BEEN A PROBLEM FOR YEARS, phishing emails have increased by an estimated 600% over the past two years. Setting a record number of cyber-attacks in that time, phishing continues to be a go-to source for hackers.

Because of the mass amounts of phishing emails targeting victims every day, it is more important now than ever to remember The Golden Rule of Email. This modern version of the well-known principle is to treat every email as if it's a phishing attempt.

The cybersecurity field as a whole has been preaching phishing training for years. October 2021 marked the 18th year for Cybersecurity Awareness Month, yet we still see record-breaking attacks and losses.

To help fix this recurring problem, organizations should consider modifying their training approach to focus on building habits versus one-off lessons. Instead of solely teaching specific details to look for, focusing on building a repeatable process can have a more significant impact. It's not the security awareness training alone that makes the difference, but the repeated process taken while investigating an email.

Implementing The Golden Rule of Email Process

The first step in implementing The Golden Rule of Email is establishing it as part of onboarding techniques and general practices, similar to how employees comprehend the mission or values of a company.

Ultimately, the rule would be adopted by leadership and management teams and woven into training and educational tools to be mastered by every employee.

If every employee was prompted to recite The Golden Rule of Email and the process it takes to spot phishing, with everyone responding promptly and accurately, employers and businesses might get a better sense of just how their company sits when it comes to defending against phishing attacks.

Once the initial concept of the rule is adopted across the company, it's time to start building the skills necessary to support the rule and act against any suspicious activity.

A crucial step in helping employees steer clear of phishing emails is asking the three Ws – who, what, and why.

Ultimately, the rule would be adopted by leadership and management teams and woven into training and educational tools to be mastered by every employee.

Questions similar to the following should be considered for every email received:

Who?

- Do I know the sender?
- Is this someone with whom I usually communicate?
- Is the email sent to an unusual group of people?
- Is the email address spelled correctly?
- Does the email address match the email in the signature?

What?

- What action does the sender want me to take?
- Does the email contain bad grammar, odd styling, or typos?
- Is the email written in style consistent with the sender?
- Is the action something you'd expect from the sender?
- Is it an urgent request?

Why?

- Why do they want me to click on a link, download an attachment, or send information?
- Are they presenting a sense of urgency?
- What is the consequence they are threatening if no action is taken? Is it something I should expect?
- Have they presented an unusual situation? Is it something I should expect?

It's also important to be wary of different phishing types:

- Email phishing – Emails using fake domains to collect private and financial information.
- Spear phishing – A more malicious email targeting specific people. Hackers normally have private

Tech Talk– continued on page 22

Tech Talk– continued from page 21

- information about the individual they're targeting, like their name, job title, and email address.
- Whaling – Emails that aim for senior-level staff and management, using scams and spoofed website links to pry into bank accounts, financial information, and personal details.
- Smishing and vishing – Instead of emails, this form of phishing utilizes texting and over-the-phone conversations where scammers pose as fraud investigators warning individuals of "breached" accounts. Scammers will also ask for payment details to verify identities and attempt to transfer funds.
- Angler phishing – Hackers use social media to gain sensitive information and download malware. They can also use data from social media to create more advanced and targeted attacks.

In addition to warning employees of the various ways to phish, organizations can put technical controls in place to help filter down phishing emails and security controls to ensure emails are coming from valid sources.

The final step in the process is taking accountability. Each employee should know exactly what steps to take when they spot a phishing email. Also, anyone who accidentally clicks on a phishing email and realizes it should immediately report the incident to their respective IT or security department(s) for faster identification and quicker response times.

The goal is for The Golden Rule of Email – treating every email as if it's a phishing attempt – to become second nature for everyone. If you habitually follow this rule, you will instinctively verify certain elements before taking any action on an email. It becomes more than just another rule to follow; it's a habit backed up by a process.

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, auditing, network security, and education. To download a free computer background and poster of "The Golden Rule of Email," please visit sbscyber.com > Education > Free Downloads.

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