Credit Union Journal, July 19, 2010

www.cujournal.com

5 Steps 1 CU Takes To Cost Cut Its Way To Healthy Bottom Line

Why Even the Obvious Can be A Revelation

By Frank J. Diekmann, Editor

ORLANDO, Fla.-As any CEO or CFO knows, there are two basic means to improve the credit union's bottom line: increase revenues or decrease expenses.

At Tyndall FCU in Panama City, Fla., as EVP/CFO Steve Ravin made clear, "The approach we've taken is to decrease expenses."

Ravin said that "over the years I've found a five-step approach is probably the best way to go" when it comes to cutting those costs. The five steps are:

First: change the corporate culture. "This is easier said than done. If you're used to spending a lot of money and people are used to just paying for everything without much control, it takes a while to change their habits."

Next: know what you're spending your money on. "It seems kind of obvious, but once we had a branch manager saying, 'That's really a revelation to me,'" noted Ravin. The other three steps:

- Considerable analysis is needed across all areas of the credit union.
- The CU needs to PLAN to spend less money.
- A CU must embrace technology and use to best extent it can.

Ravin elaborated on each of those points.

1. Changing Corporate Culture

"Cost control needs to be a daily event," he said. "You need to have a very good expense-approval process in place and should not be approving every invoice that comes through. You want to limit the ability of people to pay invoices, and question what you're spending money on. Preferably, you want to have one person reviewing invoices. At Tyndall, we do it on a daily basis." Ravin said his own reviews over the years have turned up instances in which the CU was paying for Christmas ornaments for employees on behalf of a vendor, and another in which it discovered it had spent more attempting to collect on a loan than the amount that was outstanding.

"In trying to change the culture you need constant reinforcement to the staff," he said. "We preach doing more with less. It took a while, but the managers have embraced it."

It's important, stressed Ravin, that credibility be maintained. "You can't be in ivory tower telling the staff to spend less and you are not doing it yourself. It's a multi-year process to change culture, so you have to keep working it."

As TFCU's CEO Jim Warren had said earlier during the League of Southeastern Credit Unions' annual meeting, Ravin again noted, "We've taken the approach we're not going to use the tax exemption to subsidize operating inefficiencies. We want the members to get the full benefit of the tax exemption we have."

2. Know What You're Spending

Ravin recommended credit unions review and revise their general ledger, taking pains to create a sufficiently detailed chart of accounts that provides an overview of where money is being spent, without creating a document that is overly cumbersome. In particular, Ravin urged CUs create "cost centers, so your managers know where they are spending."

He further urged CUs to pay attention to the "net bills" sent by some vendors, "You need to gross it up so you know what you are actually spending, and what the actual revenue is. Don't let your vendor fool you."

Having a budget in place is insufficient, noted Ravin, unless budget variance reports are also being prepared and distributed to managers so they know where they stand vs. their budget. "The budget should be a working budget," advised Ravin. "You planned to spend a certain amount of money; that's what you should be spending. You want to hold those cost-center managers accountable."

3. Analysis

It is imperative, said Ravin, that every credit union identify and understand its core business. In the case of Tyndall Federal, it's "making loans, and that's our driving force."

The analysis of the credit union must include identifying the competencies of staff members, and it is different for every CU. "We want to take the benefits of those strengths and improve the weaknesses. And then you need to evaluate alternatives and make a decision in the best interests of your members." That means letting go of staff that don't serve those best interests, he reminded.

As an example, Ravin cited a former credit union at which he worked that concluded, after seeing its inability to retain IT staff, that it wasn't in the data processing business. It outsourced that function. At Tyndall, it concluded in 2006 it was not in the item processing business, for which it employed seven full-timers, and contracted with a company to handle that function. "We found that for about $21,000 a month we could move to a third party and save about $700,000 a year. Today, we have three more locations than we did back then, our volumes are down about 23%, and had we stayed with the item processing we'd be paying the same amount for fewer and fewer items. Our bill is now about $13,000 a month."

4. Planning To Spend Less

Talking about reducing spending is the easy part, noted Ravin. The challenge, of course, comes in actually reducing that spending. And how is that done? "Through your budget," Ravin explained. "It's not uncommon for accounting to prepare a budget for a year in advance for the entire organization. Problem with that is it's nobody's budget but accounting's. So what you want to do is accumulate all the micro-budgets into a macro budget. When your staff buys into it first, it's more likely they will watch the budget and hold down their expenses to budget." Ravin said is experience is it takes approximately five years to ingratiate that attitude in a credit union.

The second piece of spending less is to set goals and measure actual performance against those goals, Ravin said. "Goals should be short-term, intermediate, and long-term."

Short term goals include using peer group information, for instance, and targeting certain numbers. "At Tyndall, where we were below average on operating expenses, so our short term goal was to get to average. Our intermediate goal was to hit 3% operating expense ratio by the time we were at $1 billion assets."

5. An Interesting Goal

Tyndall FCU has established an interesting long-term goal: to get down to 100 employees, from its current 254. "Is that realistic? I don't know at this point. There are going to be lots of changes in technology and services, but without that goal we wouldn't have a goal line in sight."

Tyndall has increased spending on individual staff while reducing overall compensation, believing in paying for performance. At end of 2004, its average comp and benefits were about 83% of peer group. In 2009, that figure was approximately 95%. "So staff has benefited from the expense reductions, as have members.

Thirdly, Ravin urged credit unions to "renegotiate everything," even though it may be uncomfortable with long-term vendor relationships. "Vendors in these relationships don't sharpen their pencils as much as they do for new business. So for everything you should be putting it out for bid and getting RFPs to make sure your business partner is taking care of you."

Fourthly, Ravin said CUs must prioritize operating expenses.

Fifth, Ravin reiterated the credit union compare itself to peer group across any number of metrics.

The sixth point in planning to spend less, said Ravin, encompasses technology. "You either utilize (your core system) the way it was designed, and if it doesn't you may need to decide to convert to another system or vendor." Ravin shared that at one previous CU it changed core system twice in four years because vendors were unable to support the promises made.

Other notes related to Tyndall FCU's operations:

• It aggressively promotes online lending, with 80% of new loan apps coming via that channel. TFCU offers a lower rate for online apps. The technology has also helped it to reduce staffing.

• The credit union does productivity tracking for tellers, MSRs, and phone center agents. Using a solution that identifies "Excess Waiting For Work," or the time staff is standing around waiting for a member to come in, Tyndall FCU initially reported a 35% Excess Waiting to Work ratio. It has since reduced that to 20%.

Expense Management Strategies

ORLANDO, Fla.-Steve Ravin, EVP/CFO with Tyndall FCU, offered these additional thoughts about expense management during the League of Southern Credit Unions' annual meeting:

• Branch Profitability/Product Profitability. "I know lot of vendors sell very sophisticated products" in this area. Tyndall FCU had been using such a solution, as well, at a cost of about $30,000 in annual maintenance fees, over and above the initial cost. "One of the biggest stumbling blocks for a lot of people is how to allocate the overhead expenses. It leads to a lot of irrational thinking. You don't need to do that. If you have built the cost centers, you can build out an Excel spreadsheet and know on a macro basis what branches and what products are profitable for you. Then you can make the decision, 'Do you really want to market products that are unprofitable?' "

• Cut Your Losses. "When you ID products or offices that aren't profitable, cut them. It sounds easy, but it's something credit unions aren't very good at. We in management made the decision to open these offices and offer these products. When we did that, we should have laid out in advance the results we expected to achieve. And when we don't, eliminate them and the drain on earnings."