

# Community Banker

## Stepping Into the Spotlight

By Charles Keenan

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Community banks set the stage for the future of their institutions by engaging in strategic succession planning.

ROBERT BROSKY SPENDS A LOT OF TIME ON AIRPLANES. THE CHAIRMAN, PRESIDENT, AND CHIEF executive officer of First Federal Savings & Loan Association of Lorain, Ohio, sits on five different boards-one of them ACB's-requiring him to travel extensively. While such an ambitious schedule for a chief executive might leave some companies adrift, Brosky hardly needs to worry. Back at First Federal, the \$398 million-asset thrift is in capable hands.

With Brosky set to retire in June 2008, his second-in-command, John Malanowski, senior vice president and board secretary, has been increasingly handling the day-to-day operations. The heightened responsibility has paved the way for a smooth transition when Brosky steps down. "That, in a sense, has been John's training ground," Brosky said. "It has been going on for the past three to four years. When I get on an airplane, I'm not worried. I know what is going to happen."

### Focused on the Future

Fortunately, more banks are taking a hard look at succession planning than in past years-whether it concerns chief executives, management, board members, or other employees. For one, in the wake of the Sarbanes-Oxley Act of 2002, boards are more conscious of succession planning, and regulators are demanding written plans. Demographics are also playing a role, with a wave of bank chief executives nearing retirement forcing the issue. This has made succession planning a hot topic in boardrooms and company retreats.

"Community banks are becoming increasingly aware of the need to pay closer attention to succession planning and related issues," said Paul Aguggia, chairman of Muldoon, Murphy & Aguggia, a law firm in Washington, D.C. Banks that don't put together succession plans might find themselves in a bind down the road. Succession planning at all levels-from the CEO to management to the board-is necessary to secure a bank's future, bank executives and consultants warn. Without it, the unexpected death of a CEO could lead a bank adrift and plunge management into a power struggle at the top.

A bank that neglects succession planning could also lose its key managers to competitors or fail to have an energized board focused on the future. Ultimately, banks that don't plan may have to sell out of necessity rather than choice, a phenomenon that takes a toll on all: employees, customers, and shareholders.

"I don't want to be in a position where we are forced to sell the company either through poor management or poor planning," said Ronald Martin, chief executive officer of Oak

Valley Community Bank, a \$453 million-asset institution in Oakdale, Calif. "We would like shareholders from a tax planning standpoint to know when they will pay capital gains. The only way to do that is to plan for the company to be here for years. We find that to be our driving force: to protect our shareholders, employees, and customers."

Evidence shows that banks that do have succession plans have a return on assets 13 percent higher than those that don't, according to a 2005 report by the Federal Reserve Bank in Chicago. Nevertheless, many banks are hard pressed to do anything but focus on making it through this tough economic environment. A flat or inverted yield curve over the past few years has crimped margins, preventing many banks from concentrating on long range goals. "Many of them really want to hang on financially right now," said Alexander "Sandy" Salmela, president of AKS Search, an executive search firm in Hingham, Mass. "Succession planning is not even on their radar screens."

While banks have become increasingly engaged in the task of succession planning, many have historically shied away from it. About 36 percent of banks had no written succession plan, according to a survey by the American Bankers Association in 2004, the last time the group surveyed members on the topic. About 32 percent of publicly traded banks had no plan versus 43 percent of family-owned banks.

#### Locked in for Leadership

Many banks have failed to plan at the highest level, the chief executive position. "A lot of the smaller community banks don't have a formal review process for reviewing and identifying the criteria that they are looking for in the CEO," said Stanley Ragalevsky, a partner at the Boston office of K&L Gates, a Boston-based law firm. "That is a major weakness in many community banks. They don't have an ongoing assessment process. They haven't thought about what is going to happen."

Often it is best to identify someone from within management who can assume the reins before the departing chief executive leaves, consultants said. This isn't always easy, as it means the chief executive giving up responsibility little by little, something that might get in the way of ego for some.

Banks, of course, benefit from looking to see if there is a qualified candidate from within to eventually fill the CEO spot. The board of South Shore Savings Bank, a \$910 million-asset thrift in Weymouth, Mass., tapped John Boucher in January to assume the role of president and chief executive officer, succeeding Arthur Connelly, who retained his title of chairman of the bank. (Connelly is also first chairman of ACB). "We made it a very orderly transition," Boucher said. "I am the chief executive for almost two years before Arthur retires. He is actively involved with the bank. That is right out of the FDIC P lay book."

However, banks often need to look beyond their walls for talent. Home Federal Bank, a \$747 million-asset institution in Nampa, Idaho, has anointed a successor well in advance of the retirement date of its chief executive officer, Dan Stevens, who will step down in September 2008. The bank hired Lee Koehn Associates Inc., an executive search firm in Portland, Ore., after a nationwide search. Last year the board selected Len Williams, a commercial banking veteran from Fifth Third Bancorp. Williams comes with the experience Home Federal was looking for, given the thrifts recent move into commercial

lending. That made him a good fit for the thrifts long-term strategic plan, an important factor to consider when a bank looks for a successor.

"We wanted someone with a business banking background who understood the company," Stevens said. "We also wanted someone involved in a strong sales culture. And someone with at least 10 to 15 years left to go before retirement age. Every organization is different from every other," he added. "The logical way to do it is to have an orchestrated succession plan that works over a period of time instead of [proceeding] willy-nilly."

Succession plans also need to name interim successors in case of the sudden death of a chief executive. The late John Sweeney, former chief executive of BankFive, was only a year into his job as chief executive when he died suddenly of a heart attack at age 54 in 2003. An emergency succession plan allowed for the immediate appointment of Thomas Lyons, then head of the thrifts commercial lending business, as interim CEO. Lyons was officially elected CEO a few weeks later. (see Community Ranker, April, 2004). "We continually update our emergency plan," said Lyons, whose bank now has \$602 million in assets. "In case someone becomes incapacitated or dies, everybody knows who will become the emergency president. That gives the board some breathing room."

#### Made for Management

Community banks also need to include management and rank-and-file employees in their succession plans. All too often, banks lose employees because they don't have a plan to help retain them due to a variety of reasons, such as restricting their responsibilities, not paying enough, and failing to extinguish personality conflicts, noted Salmela of AKS Search. "It is very easy for people and boards to talk about succession planning," Salmela said. "It's a whole different matter to make it happen, either to bring people in or give them the opportunity to grow. Good people tend to leave."

"It won't get any easier in the years to come, due to changing demographics," said Terry Saber, president and chief executive officer at Saber & Associates, a consulting firm in Cokato, Minn. With one entrant to the workforce for every three leaving, banks will be competing with not just themselves for talent. "Banks really have to expand their searches in terms of geographic location," Saber said. "They have to get a lot more creative with recruitment and retention packages."

Banks should also take stock of talented employees and anoint potential stars. By doing so, they can motivate them to work harder and give them a greater sense of purpose. Christopher Courtney, president of Oak Valley, started at the bank in 1996. Two years later he was pulled aside one day by chief executive officer Martin and told he had the potential to some day run the bank. At the time, Courtney had his sights set on becoming chief credit officer. At 44, he is now president and heir apparent to Martin. "It led me to think differently," Courtney said. "I had to look further down the line. That was incredibly powerful to me, in how I thought from that day on."

In addition to good compensation and benefits, training is also critical. "We work very hard at that," said David Krebs, senior vice president and director of human resources at Citizens Business Bank, a \$6 billion-asset institution in Ontario, Calif. Citizens tests its

employees to help determine how they can improve themselves and where they might be a good fit in the bank for their next position.

The bank uses a so-called Predictive Index(TM), a model developed by PI Worldwide, a consulting firm based in Wellesley, Mass. The model, which has been used by more than 1,000 financial services clients, measures personality traits such as the need for control, extroversion, patience, and diligence.

Too often, companies rush to evaluate a candidate for a job without sufficient understanding of what the role is about and how well the candidate fits into that job. "Its hard to hit a bull's eye without drawing a bull's eye first," said Todd Harris, director of research at PI Worldwide.

### Directed to Serve

Banks must also consider succession planning for boards, especially those that have ambitions to expand. Oak Valley is well situated in this regard. Population is projected to grow in the region to 15 million during the next 30 years, up from 5.3 million today, according to the banks projections. The bank, 16 years old, determined the best strategy for its shareholders would be to remain independent and capitalize on the growth. It mapped out a 10-year strategic plan, which included succession planning at all levels of the bank, including the board.

"Emotionally and from a people standpoint, one of the things relatively easy to convince the board of was succession management," said Martin. When the bank started, most of the board were in their mid-to-late 40s. That has called for a focus on recruiting new board members. "What happens is most community banks don't plan for this," Martin warned.

Two years ago the bank instituted a board succession plan, later bringing in its first two new directors and retiring two directors with emeritus titles. The new faces bring fresh ideas and new contacts, Martin added. One of the new members is a commercial real estate developer. Another is a Stanford graduate with an MBA who returned to the family business of nut farming. "We're trying to bring on younger, more well-known community members and to expand our sphere of influence," Martin said. "It's best to bring in new blood."

While mandatory retirement ages can help set in place succession planning for the board, banks should still try to harvest the wisdom and expertise of retiring board members, rather than cutting the cord. At North Abington Co-operative Bank, a \$86 million-asset institution in Abington, Mass., directors emeritus still attend meetings, giving five more voices to the official voting board of 10. "It's basically a way for our institution to retain the knowledge and experience of folks who have been on the board for a long time, while still giving us an opportunity to infuse new directors on the board," said Andy Raczka, president and chief executive officer. "It's the best of both worlds."

Whatever the level of the organization, succession planning is key to a bank's ability to prosper in the years to come. "More banks are sitting down and doing this," said Saber of Saber & Associates. "Because of the reality we are facing with the demographic shift and the fiercely competitive nature of finding talent, it is becoming a broader issue on an annual basis with the non-bank competition."

To be sure, banks that do a better job today of having a well-thought out plan will have an edge over their peers. "Succession planning is a necessary part of good management," said Boucher of South Shore Savings Bank. "It gives the board a good road map, and it gives folks internally a good thing to look forward to."

#### SIDEBAR

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#### SIDEBAR

##### Succession Planning Checklist

"Banks could do a better job at planning for the future," said Terry Saber, president and chief executive officer of Saber & Associates. Here are some best practices Saber recommends:

1. Have a well developed strategic plan. Know where the bank is going. Can the bank grow on its own, or will it need to recruit managers from elsewhere?
2. Know the demographics of the workforce. Who are potential retirees? What wisdom does the bank lose when people retire?
3. Know your A-players. Who is the starting line-up? Who must the bank hold onto? Work hardest to maintain and keep this group.
4. Make sure managers are ready. Banks spend a lot of time working on credit quality, but their most valuable asset is the labor force. What training will managers today need for their next position? What skills will they need six to 10 years out?
5. Pay attention to compensation plans. If stock cannot be shared, what are the alternatives to give people some small portion of the increased equity they have helped build?
6. Think about organizational structure. Make sure the human resources director is working with three charts: one for today, one for three years from now, and one for six years out.
7. Conduct assessments of executive management. Typically this is with a good behavioral psychologist. This will give the bank a good picture of what it is getting and what its developing challenges are.

Source: Saber & Associates