

Kansas

Quarterly Interest

The Newsletter of the Office of the State Bank Commissioner

Commissioner's Corner

J. Thomas Thull, Bank Commissioner



The publicity surrounding the sub-prime mortgage dilemma during the last six months has given way to Presidential politics and the greater economy. Although we will continue to monitor foreclosure activity in Kansas, our efforts will also focus on consumer protection and education. Beginning in February of this year, we will place public awareness ads in approximately 144 Kansas newspapers. The message in those ads will encourage Kansans to understand their mortgage documents before they sign them, know their responsibilities and rights under the mortgage, and provide contact information for experts who can answer mortgage and foreclosure

questions. Our goal is to ensure that consumers with mortgage difficulties are not avoiding the problem but instead reaching solutions good for both the consumer and their lender.

During the last part of 2007, Kenneth Torgler was named as the Director of Examinations within the Banking Division, and Scott Hatfield was promoted to replace Ken as the Regional Manager of the East Region covering the Topeka and Lenexa field offices. Adam Courtney was promoted to Regional Manager within the Consumer and Mortgage Lending Division overseeing the Lenexa and Wichita field staff. We are pleased these individuals have assumed these management positions and would encourage you to call on them if you are in need of assistance. Additionally we have hired five additional examiners in the Consumer and Mortgage lending Division, and by mid February, we intend to fill another three vacant examiner positions, which will bring us to the staffing level approved by the legislature.

For 2008 we have a lengthy list of things to consider: completion of a strategic plan; upgrades in the data bases for our agency, including document imaging and more online services to our customers; a request for proposals for office space as our main office location lease expires in 2009; an initiative to increase the number of state chartered banks; expanded training for our examination staff; a review of the staffing levels in our IT area; a commissioner's tour of the state; and an overall review of the salary structure for our agency.

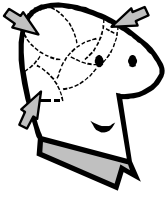
In late March we will attend the CSBS Legislative Fly-In held in Washington, D.C. If you have issues you would like us to bring to the attention of our congressional delegation, please do not hesitate to contact the office and let us know. Our door is always open for this discussion or any other matter.

Winter 2008

Inside This Issue...

- *Barrister's Brain*
- *2007 Summary of Applications*
- *The Sometimes Forgotten C-Capacity*
- *Technology Matters: Top Security Issues in 2008*
- *Employee Spotlight*

Barrister's Brain



As a regular feature in *Quarterly Interest*, our advice columnist, Barry Barrister, will answer a legal question the OSBC has received that we think would be of interest to bankers. Even though he's a fictional lawyer (arguably the best kind), Barry has insisted we include the caveat that the advice he dispenses is general in nature, and is not intended as a substitute for obtaining specific legal advice from counsel when necessary.

Dear Barry,

Questions have recently come up at our bank regarding the reporting requirements for unclaimed property. First, what is the dollar threshold for reporting property? Also, why does the treasurer's office require that we submit a resolution of our board of directors along with the property we report to them?

Signed,

Rapid Reporter Ron

Dear Ron,

Regarding your dollar threshold question, there are two things to look at. First, does your bank hold any individual piece of property over \$100.00 in value? If so, you must report the property. Second, if there is no individual piece of property over \$100.00 in value but there are a number of smaller valued pieces of property that the bank is holding, if the total of that property reaches \$250.00, then all of the property must be reported. The bank must hold the properties under \$100.00 until such time as the total properties reaches \$250.00; the obligation to report the under \$100.00 item never goes away. See K.S.A. 58-3850 (i).

You also asked why the Treasurer's office requires that a board resolution be provided. The answer is fairly straight forward. The law allows the Treasurer to come to your bank and perform examinations of your records to determine compliance with the Unclaimed Property Act. However, the law gives an "out" to certain types of financial institutions, including state banks and trust companies, which provide a letter from an independent CPA, or a resolution of its board of directors, certifying compliance with the act. While a resolution can take some time, it sure sounds better than an examination.

The unclaimed property section of the State Treasurer's website, found at www.kansascash.com/prodweb.up/index.php, is chock-full of useful and interesting information concerning your responsibilities under the Unclaimed Property Act. In my search of the site, for example, I found that the Treasurer apparently does not want the stray animals that show up at your bank to be reported to them as unclaimed property. I guess they let you keep the really valuable stuff! Go figure.

Legally yours,

Barry

Corporate Application Overview for 2007

Dana S. Hampton, Director of Corporate Activities

Currently, 253 state-chartered banks are operating in Kansas. As of December 31, 2007, the total was 255. During 2007 two new banks opened for business and four banks merged out of existence. No changes in state-chartered trust companies were reported during the year; ten companies remain in operation.

Expansion of state chartered banks remained strong in 2007. Twenty-three applications for banks to establish new branch offices were filed during the year. Additionally, merger activity, particularly involving branch office purchases and assumptions, was active, with 11 merger applications filed. Other applications processed during the year included: changes of control involving 15 banks and trust companies; relocation of eight main/branch offices; and name changes of four banks. Also processed were 41 new or renewal applications authorizing companies to conduct money transmitter business in Kansas. A summary of some of the applications and transactions completed during 2007 is provided on the following table. A complete list of application information is available on our Website or will be provided at your request.

(continued on page 6)

The Sometimes Forgotten C-Capacity

Ed Spielbusch, Regional Manager -- Southeast Region

In today's lending environment of elevated asset valuations it becomes exceedingly easy to do quick collateral evaluations, verify the traditional 20 percent margin, and renew for the next go-around feeling quite secure. Wait, haven't we traveled this road before? Does anyone out there remember the agriculture industry in the seventies and the resulting crisis? With the exception of what has been broadly publicized in the residential real estate market, asset valuations are at historical highs. I have always maintained that this is the most

difficult and perilous lending environment that a bank can face. Lending policy margin requirements are applied to these valuations and we still arrive at net positions far in excess of what I can recall those assets selling for a decade or two earlier. Or, more dangerous yet, loans are booked at the cost of the asset relying on the appraisal to create the required margin. In these cases, the borrower is not a party to the risk. Am I taking on "Chicken Little" tendencies and predicting the sky is falling? No, I'm not that smart and didn't pay that close of attention in Economics class. However, margins can sometimes dissipate rapidly from those elevated levels leaving loans under secured, creating loss exposure. Prime examples currently exist in the residential real estate market where foreclosures have escalated, inventories of homes have swelled, and values are coming down. The root of this problem in many cases stems from overextended borrowers drawn in by teaser rates with no attention given to their ongoing repayment capacity. Adjustable rates are driving payments up beyond repayment ability, delinquencies are escalating, and foreclosures are increasing. So when do collateral and collateral values not come into play? The answer is when borrower repayment capacity supports the loans,

payments are made, debt is reduced, and loan customers gain equity and financial strength by appropriately handling their obligations. In the numerous examinations that I have participated in over the past several years one recurring theme

and recommendation continues to reveal itself in almost every case, and finds itself in those Reports of Examination. That theme is the need for repayment analysis and the documentation of such before the lending decision is made. Assessing a borrower's repayment capacity, and

I mean their overall repayment capacity, is one of the basic premises of successful lending. More often than not, in reviewing credit files, evidence of cash flow crunching and debt service capacity is lacking. Many times, there is insufficient information within those files to make a reasonable analysis. Additionally, on occasion, when you find cash flow analysis some institutions forget to capture all of a customer's obligations to assess overall repayment ability. We often refer to this as a "global" cash flow. Just as collateral is one of the "Cs" of credit, so too is capacity or repayment ability. I am not implying that bankers don't intuitively give consideration to the ability to repay given their experience and knowledge. I would suggest, however, that improvements can be made in global cash flow analysis and its documentation in assessing the prospective success in a borrower's ability to meet their obligations.



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Technology



Matters

Glen Caspers, Regional Manager-Technology Division

Top Security Issues in 2008

Is your bank ready for technology changes in 2008? A quick search of the Internet reveals many risks and new waves of technology that could affect your institution. The intent of this article is to provide a brief summary of these predictions. Does your strategic plan and risk assessment address any of these items?

Prediction #1 - The Web evolution will continue

The Web of 2007 became more robust and ready for business, becoming host to a variety of new applications and services. This new generation of sites, generally referred to as Web 2.0, act more like traditional PC software. The sites are responsive and fast. That means web browsers will need to work hard while visiting these sites, pulling data to keep the site current. Combined with market incentives to keep pushing out new features to users, the emerging Web will present a dangerous mix of software flaws ripe for hackers to exploit. These Web-based services, including social networks such as MySpace and Facebook, are becoming prime targets for hackers seeking personal information and for using to distribute malware.

It is anticipated that financial institutions will increasingly tap into Web 2.0, including social networking sites like Facebook and MySpace, to connect with young consumers in the ways they connect with each other. Megabank Wells Fargo (\$540 billion in assets) created Stagecoach Island, which is an interactive site that promotes social networking and financial education. A well-known security firm is predicting that by 2012, 75 percent of banks will use Web 2.0 and social networking technologies in retail delivery and customer relationships.

Prediction #2 - Virtualization will become more popular

Virtualization is and will continue to be a hot topic. VMware appears to be the market leader.

Virtualization refers to the practice of hosting more than one server function on a single host machine. Instead of requiring a separate computer for each server, dozens of virtual servers can coexist on the same computer. In most cases, performance is not affected and each server behaves as if a dedicated machine is hosting it.

Businesses deploying virtualization could see a 40 to 75 percent one-time savings and up to 50 percent in ongoing savings. One organization consolidated 1,000 physical servers into only fifty. Banks that utilize virtualization may also improve business continuity efforts through server redundancy in the virtual server environment. The ability to test new applications and new releases on virtual machines before putting them into production is also a significant advantage. Some sources indicate that many banks will have virtualization in their 2008 plans.

Prediction #3 - Vista will be a catalyst for change in the PC industry

For many years, hardware processing power has exceeded the requirements of operating systems. A reversal of this was seen in 2007 and is expected to continue in 2008 as Vista emerges in the workplace. Vista has hefty hardware requirements, so planning to deploy it on current computers may be unwise. You will want to ensure that 2008 PC purchases are Vista-capable even though you may plan to delay Vista deployment and run XP in the interim. Many businesses have elected not to test and adopt Vista until Service Pack 1 is issued, which will likely be released by the time you read this article. Banks may also need to access their thin-client designs in light of Vista's requirements.

Additionally, Vista and Office 2007 will represent learning curves not seen in recent releases. In particular, Office 2007 will likely require significant

(continued on page 5)

Top Security Issues in 2008 (continued)

training. Banks should be planning for these versions by developing detailed software training and migration plans.

Prediction #4 - Security threats will get personal

Phishing scams and malware will continue to be serious security threats. Cyber criminals are becoming more professional. Attacks are becoming more individualized, focusing on individuals with specific and personal demographic information. Experts say that instead of just credit cards and bank account information, they're going for everything - any and all information that can be used to create an identity. As individuals become savvy to widespread attacks, phishers will target their victims more precisely with highly researched, personal information, known as spearphishing. Also, targeting high-level executives for sensitive company information is referred to as whaling. It is reported that phishing toolkits are becoming more available, making it much easier for cyber predators to engineer their scams. Consumer education and security awareness training will continue to be key factors in mitigating these risks.

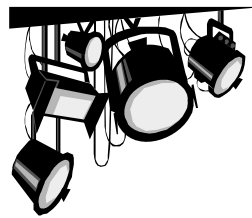
Prediction #5 – Use of smartphones will continue to grow

The use of handheld devices such as smartphones in financial entities is reported to have increased substantially over the past year. The ability for staff to work remotely may increase their productivity, but the risk posed by remotely accessing email and bank networks is higher than ever. Also, smartphones that are running operating systems and e-mail applications can be storing valuable data. This makes them very tempting targets. Security researchers have found ways to break into some mobile-phone platforms. To what extent are they vulnerable to hackers, viruses, theft, and insider abuse, and how can a bank manage their security? Banks that allow employees to use these devices to conduct business will have to learn how to secure and support these devices.

Summary

Other topics worthy of mention for 2008 include pandemic planning, hard drive encryption, and VoIP attacks. Pandemic planning should continue through 2008 and will reinforce current business continuity plans by bringing attention to any disaster that may reduce your workforce.

Data loss due to lost notebook computers and other data-storage medium made up 46 percent of all data losses in 2007. When a computer is lost or stolen, encryption becomes a big deal. While VoIP phones may offer low-price long-distance calling and the ability to place calls from a PC, the communications protocol used by many VoIP providers is vulnerable to attacks, and leaves holes that the hackers could use to hide their identities. Also, some Internet phone carriers have not turned on the technology that can encrypt conversations.



Employee Spotlight

Scott Hatfield, Regional Manager, East Region

The Employee Spotlight is on Scott Hatfield, Regional Manager of the Lenexa and Topeka offices in the East Region. A Kansas State University graduate, Scott began his career with the OSBC in May 2001. He was employed by a community bank in Ottawa, KS, where management gave him opportunities to experience a variety of different duties within the bank. He says that experience gave him a broad understanding of the banking industry and has helped him succeed in his present career.



When asked what he enjoys about the OSBC, Scott's response was "I work with a great group of people at the OSBC. It is really enjoyable getting out in the communities and getting to know the employees of the banks our office regulates and supports". Scott is married with three sons, 5 year old twins and a two year old.

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Corporate Application Overview for 2007

(continued from page 2)

New Bank Charter	Location	Date Opened
Millennium Bank	121 North Washington Street, Junction City	1/16/2007
CROSSPOINT Bank	11225 College Boulevard, Suite 150 Overland Park	10/1/2007
New Branch	Branch Office Location	Date Opened
Commerce Bank & Trust (now known as CoreFirst Bank & Trust), Topeka	2600 NW Rochester Road (inside Wal-Mart), Topeka	1/22/2007
Kansas State Bank of Manhattan, Manhattan	716 North 119 th Street West, Suite 116, Wichita	2/1/2007
Peoples State Bank, McDonald	122 West Laurel, Garden City	2/5/2007
Hillcrest Bank, Overland Park	1600 South Main Street (inside Champions Cove) Duncanville, TX	2/26/2007
Hillcrest Bank, Overland Park	6800 Leetsdale Drive (inside Cherry Creek) Denver, CO	3/28/2007
The First State Bank & Trust Co. of Larned, Larned	7206 College Boulevard, Overland Park	4/23/2007
Cottonwood Valley Bank, Cedar Point	200 Broadway, Cottonwood Falls	5/21/2007
Morrill & Janes Bank and Trust, Merriam (1)	3215 Carnegie Drive, Suite 100, Lee's Summit, MO	5/25/2007
Home Bank and Trust Company, Eureka	1409 North Greenwich, Wichita	6/18/2007
Security Bank of Kansas City, Kansas City	5450 Roberts Street, Shawnee	7/16/2007
SolutionsBank, Overland Park	214 South Main, Pratt	7/23/2007
SolutionsBank, Overland Park	705 NW Woods Chapel Road, Lee's Summit, MO	7/23/2007
First Option Bank, Osawatomie	2110 West 223 rd Street, Spring Hill	9/4/2007
Hillcrest Bank, Overland Park	13800 Metcalf Avenue (inside Tallgrass Creek), Overland Park	10/16/2007
First State Bank & Trust, Tonganoxie	Bank-Owned Courier	10/22/2007
Security State Bank, Wellington	2022 East 16 th (inside Wal-Mart), Wellington	11/7/2007
Emprise Bank, Wichita	63 rd Street South and Rock Road, Derby	11/13/2007
Brotherhood Bank & Trust, Kansas City (2)	708 SE 3 rd Street, Lee's Summit, MO	11/16/2007
Commerce Bank & Trust (now known as CoreFirst Bank & Trust), Topeka	7430 Switzer, Shawnee	12/5/2007
New Branch (through bank merger or P&A of a branch office)	Branch Office Location	Date Opened
United Bank & Trust, Marysville, acquired one branch of Armed Forces Bank, N.A. Ft. Leavenworth	2000 North Tuttle Creek Boulevard, Manhattan	1/8/2007
Security Bank of Kansas City acquired all offices of First Community Bank, Kansas City	1300 North 78 th Street, Kansas City 10950 Parallel Parkway, Kansas City 4400 Shawnee Mission Parkway, Fairway	1/22/2007

Corporate Application Overview for 2007

Bank of Blue Valley, Overland Park, acquired one branch office of Northland National Bank, Gladstone, MO	9500 Lackman Road, Lenexa (the branch was formerly the main office of Western National Bank, Lenexa)	3/29/2007
Scandia State Bank of Scandia, Scandia, acquired all offices of First National Bank, Belleville	1205 18 th Street, Belleville 418 NW 3rd, Abilene 446 North Marshall, Chapman	5/7/2007
State Bank of Downs, Downs, acquired FirstBank of Greeley, Denver, CO	3773 Cherry Creek North Drive, Suite 575, Denver, CO	7/13/2007
CoreFirst Bank & Trust, Topeka, acquired First United Bank, N.A., Englewood, CO	8310 South Valley Highway, 3 rd Floor, Englewood, CO	9/21/2007
The Bank of Protection, Protection, acquired Citizens State Bank, Ashland	722 Main Street, Ashland	9/29/2007
Name Change	New Name	Effective Date
Scandia State Bank, Scandia	Astra Bank	5/10/2007
Commerce Bank & Trust, Topeka	CoreFirst Bank & Trust	9/4/2007
Hartford State Bank, Prairie Village	Bank of Prairie Village	12/13/2007
Main Office Relocations	New Location	Date Opened
Hartford State Bank (now known as Bank of Prairie Village), Hartford	3515 West 75 th Street, Prairie Village (the Hartford office remains a branch)	12/13/2007
Branch Office Relocations	Old and New Location	Date Opened
Hillcrest Bank, Overland Park	2911 Turtle Creek Boulevard, Dallas, TX 2811 McKinney Avenue, Suite 24, Dallas, TX	1/2/2007
Labette Bank, Altamont	119 North Broadway, LaCygne 501 Market, LaCygne	2/20/2007
First State Bank & Trust, Tonganoxie	1106 155 th , Basehor 15505 Pinehurst Drive, Basehor	2/26/2007
First Bank Kansas, Salina	326 NE 14 th , Abilene 1410 North Buckeye, Abilene	2/26/2007
Union State Bank, Arkansas City	321 East 10 th Street, Winfield 2108 Pike Road, Winfield	8/13/2007
Emprise Bank, Wichita	1717 South Rock, Road, Wichita 11111 East Harry Street, Wichita	11/13/2007
Kansas State Bank of Manhattan, Manhattan	716 North 110 th Street West, Wichita 1424 South Maize Road, Wichita	11/19/2007

(1) Prior to establishing the branch, Exchange Bank, Mound City, MO, was merged into the bank. Assets and liabilities of the Missouri bank were later acquired by Nodaway Valley Bank, Maryville, MO.

(2) Prior to establishing the branch, Park Bank, Parkville, MO, was merged into the bank. Assets and liabilities of the Missouri bank were later acquired by Liberty First Bank, Liberty, MO.



Ken Torgler, pictured left, delivers items to this year's recipient.

Volunteer News....

In December, several OSBC employees participated in the "Adopt a Family" Christmas program, which was promoted by KMAJ, a local radio station. In this program, a group of volunteers "adopts" a family or individual in need. Donations of money and food items were collected and delivered. This year, the OSBC adopted an individual. The program is a wonderful opportunity to bring some holiday cheer to a local family or person.

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