



MUTUAL BELT-TIGHTENING

BY RICHARD H. GAMBLE

Amid signs that the economic crisis may be easing on some fronts, strain is starting to show in the inconspicuous but all-important relationship between credit unions and their core processors as hard times take a toll on both parties. “Your processor should be a strong strategic ally,” insists Sabeh Samaha, managing consultant at Samaha & Associates Inc. (www.ssamaha.com), Chino Hills, Calif. Unfortunately, fewer and fewer are able to hold up their end of that partnership, he says.

Samaha divides core processors into three tiers. Tier 1 processors have the development resources and foresight to be investing in future systems. “They should be able to evolve and meet the technological requirements of the times,” he says. He won’t name names, but says Tier 1 processors are becoming rare.

Tier 2 includes most processors, and they stay in business because their products get the job done, but they’re running on present performance, not future development. Tier 3 processors are “facing extinction,” Samaha says. And that’s important to know, even if a CU is not coming up on a contract renewal date when its options would be evaluated anyway. “You don’t want to leave as refugees, having to swim away from a sinking ship. You want to leave while you still have leverage,” he advises.

SHRINKING RESOURCES

Weakness among core processors is bad news. Virtually every CU requires a core processor, and it’s likely to be one of its most important technology partners, notes Michael Wofford, senior technology consultant at Brintech (www.brintech.com), based in Austin, Texas. “The processor has a big impact on the credit union’s cost structure,” he notes. After years of consolidation, the field is dominated by five large providers, which “pretty much offer the same services, but some do some things better than others,” he says.

Here’s how the economy is affecting credit union-core processor relationships.

Hard times are forcing vendors, including core processors, to tighten their belts, which means resources are shrinking at the same time service demands are growing. “Every vendor has been impacted,” reports Kathy Hooker Burress, president of CUES Supplier member Symitar (www.symitar.com), San Diego, the Jack Henry core processing division for CUs. “While most processors have had to lay off some of their workforce, we have avoided layoffs so far and are cutting costs in other ways so that we can both maintain our current service levels and be prepared for the inevitable rebound in the economy.” Many credit unions cut back spending across the board when things fell apart in January, and “that hurts our revenue,” she notes.

“There is no question that credit unions are looking to cut costs,” says David Turner, information officer at CUES Supplier member Fiserv (www.fiserv.com), Brookfield, Wis. “And they’re seeing contract renewal dates with their core processors as a time to do it.”

The premium CUs place on operating efficiency is higher than ever now, Turner reports. “It’s all about how we can make them more efficient,” he notes. Tools to automate account openings can be just as valuable as a lower price on core processing, he adds.

The weak economy has slowed the churn of credit unions changing core processing software or providers and upgrading systems. “The focus has shifted to doing more with what you have,” notes David McConney, EVP/general manager of the credit union core systems group of Harland Financial Solutions (www.harlandfinancialsolutions.com), a CUES Supplier member based in Lake Mary, Fla.

Core processing “is likely to be a tough game to be in



these days,” notes CUES member Doug True, SVP/technology at \$1 billion FORUM Credit Union, Indianapolis, and president of FORUM Solutions, the CU’s technology CUSO. “Regulatory demands continue to increase, technology budgets have been trimmed, and there’s not much new business to go after.

“It takes money to innovate and there is less money in that business these days,” he observes. Putting out regulatory fires takes time and money and could cause processors to delay upgrades, he notes.

Further consolidation among processors might not be a bad thing, True thinks, because having so many different core processors can impede the back-office collaboration

CUs need to cut costs and become more efficient. One solution, already being tried by Open Technology Solutions (www.opentechs.com), Denver, is for CUs to organize a CUSO and get member CUs to use common technology providers to gain collaborative efficiencies, he reports.

TIME TO REINVENT

CUs are cutting back on technology spending to survive, but Samaha thinks that’s a mistake. “Now is the time that they should be reinventing themselves for the next up cycle and making sure they have the tools, including the right



core processor, to capitalize on those opportunities.” CUs that thrive will “cut costs and reinvent themselves at the same time,” he emphasizes.

In this economic climate, it’s hard to push processors to invest in reinvented systems for reinvented CUs, Samaha concedes. “Programming is the heart of systems development,

and programming is not cheap,” he notes. With investor funding scarce and revenue from CU customers shrinking, dealing with new regulatory issues draws scarce resources away from programming. This shortage of investment and revenue funding has dragged several processors from Tier 1 to Tier 2 or from Tier 2 to Tier 3, and those that haven’t fallen are “hanging on by their fingernails,” he says.

The financial condition of the core processor is “absolutely critical,” McConney agrees. “How many dollars you can commit to ongoing development is huge, particularly in light of the regulatory pressures,” he observes. CUs need a processor with the resources to invest in keeping their systems compliant, he emphasizes.

Detecting financial deterioration is critical but difficult, Samaha says. “You have to understand the business model of the mother ship [corporate parent] to deduce the status of the processing vendors,” he explains. “You have to know their strategic plans and what is happening to their

banking relationships.”

They’re mostly public companies, so historical financial information is available. To look ahead, question your sales rep, he advises. “You have to know their financial status and what is in store for the products you depend on. So make them tell you. And then read between the lines.”

Deciding whether and when to switch processors has become a key strategic decision at many CUs. A core processing conversion is “very expensive,” Turner says, “and there’s very little appetite among credit unions to go through a conversion with the economy this way, but they will do it if necessary.”

Switching is often a last resort, for good reason. “It can take up to a year to select a new core processor, and then the conversion can take up to another year,” McConney points out, “so it’s pretty disruptive.” When the value proposition is strong enough, CUs are doing it, but only after they take a long, hard look at the decision, he reports.

But it’s a look they need to take, Wofford says. CUs typically buy core processing under long-term contracts—lasting five, six or even seven years—and those contracts usually include early termination penalties and cost adjustments, he explains. When contracts are about to expire, every credit union should perform due diligence, learn where the market is and renegotiate price and service, paying close attention to penalties, service-level agreements and price adjustment formulas, he says.

STAYING NIMBLE

Accepting status quo core processing is common behavior, but it shouldn’t be, Samaha argues. “Credit unions are nimble and need to stay that way. They need to demand more from their core processors.” Both CUs and processors need to prepare for younger members who may have less wealth but are aggressive users of technology and base their expectations on sites like Facebook, Twitter and YouTube, he points out.

While a conversion is disruptive, this may be a relatively good time to do it since many other initiatives have likely been shelved, Samaha says.

The crisis seems to be producing some market movement. “We picked up 33 new clients in the past year, almost half of them after January,” Burress reports. “In this environment, credit unions feel they have to have technology that doesn’t hinder them. It’s definitely not business as usual this year.”

A peril of coasting is that a CU may depend on a system that a vendor is looking to discontinue, so ask questions. “We always ask our vendor about their vision for the future and we tell them ours to be sure they are in synch. There has to be a level of trust in this conversation,” True notes.

CUs generally know which systems are slated for obsolescence, Wofford notes. If a processor has five systems

VIRTUAL CONFERENCE

With evidence that travel budgets have been cut and that trade show attendance is down as much as 50 percent, Symitar decided to make its August user group meeting a virtual conference, says Kathy Hooker Burress, president of CUES Supplier member Symitar (www.symitar.com), San Diego. “We partnered with a firm that does virtual trade shows. It cost us as much or more, but credit unions could send as many attendees as they wanted and it didn’t cost them anything,” she explains.

Held over two days in August, with 6.5 hours of content each day, the virtual conference mirrored Symitar’s live event as closely as possible. After logging on to a secure Internet site, attendees were able to chose between concurrent educational sessions, and visit a virtual exhibit hall where they could interact with vendors. Attendees also had online access to all content for 90 days after the event. To ensure that only Symitar clients attended, pre-registration was required. The event had 2,400 total registrants, and more than 1,200 people actually logged on for the event.

RESOURCES

Read more about core processors at cues.org/coreprocessorarchive.

Read more about how the CU owners of Open Technology Solutions share IT at cues.org/techcusocreateseconomyofscale. If you need your CUES or CUES Supplier member password or wish to join, please e-mail cues@cues.org.

You may also be interested in "Managing Outside Vendors" at cumanagement.org. Choose "Article Archives" then "Operations" and finally "Compliance."

that serve five distinct market segments, there's a good chance that all will be supported. If a processor has five systems that serve three market segments, there's a good chance one or two will be phased out, he explains.

Core processors generally have user groups, and give users a big voice in what enhancements will be developed and in what order, Wofford says. A processor typically has a multi-year list of what is coming when, he notes. If you are evaluating new processors, ask to see the list and note how well it matches up with your priorities, he advises.

COMPLIANCE CHALLENGES

The strain on core processor resources is exacerbated by all the regulatory compliance issues CUs face and there's no respite in sight, says Scott Hodgins, senior director at Cornerstone Advisors Inc. (www.crnstone.com), a CUES Supplier member in Scottsdale, Ariz., and CUES' partner in creating the monthly *CUES Technology Edge* e-newsletter. CUs are still challenged to comply with the "red flag" rules, anti-money laundering rules and the Bank Secrecy Act, and now they have the credit card "bill of rights" to worry about, with overdraft protection rules coming and a host of mortgage reform measures being batted about.

Regulatory pressure is definitely a key driver in the core processing market, Burress says. "Auditors and the NCUA look at things differently as a result of the economy," she notes. CUs could need a new field on a report or a different way to search through transactions to detect fraud. They could need to report loans differently. "Our clients


are being pushed by regulators, and that pushes us to modify our systems quickly to keep up."

Core processors have to be able to generate the right reports in the right formats to satisfy compliance demands, but they also are asked to serve as compliance consultants. "We got a lot of phone calls last year about red flags compliance, and we're getting a lot of calls this year about compliance with the credit card act," Turner says. To answer compliance questions, Fiserv has a full-time compliance manager, and compliance calls that come in to client services are forwarded to her, he explains.

To avoid robbing development to pay for compliance help, some vendors have separate budgets and staffs, Turner explains. "We're feeling resource pressure like everyone else, but we know we have to invest a certain amount of money in development, so we budget for that. We're not raiding the development budget to fund compliance help, just because demand for that has grown," he says.

Future regulatory challenges are practically a given, although "there's still an awful lot of uncertainty about how the various pieces of legislation and regulatory initiatives will land and the impact they will have on financial institutions," McConney says. "We're already having to respond to issues that weren't even on the radar 12 or 18 months ago."

Most CUs won't leave a core processor just because of compliance difficulties, Hodgins says, but it's becoming a more important component of the relationship and has the potential to sour things. Functionality is less important than the level of confidence and trust a CU has in the compliance output of its core processing system, he explains.

All these pressures mean core processing has to be actively managed. "You can't sit back and ride out the storm," Samaha insists. "You need parallel strategies for staying solvent and reinventing yourself or you will die. You hear a lot of whining now from credit union executives, but they need to snap out of it and get busy preparing for the challenges of the next up cycle." And that means dumping a Tier 3 core processor if you're stuck with one. "You can't reinvent yourself successfully if you can't get support for good services," he points out. 

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COUNTERPOINT

Maybe core processors are not as important as a lot of CU managers think. "Credit unions are way too processing-centric," insists Weldon "Butch" Leonardson, SVP/chief information officer for \$9 billion BECU (www.becu.org) in Seattle. "Most CUs could pick a core processor by throwing a dart at a dart board blindfolded and be fine. We don't have a 'core' processor. We have a processor of record, but that's not 'core' for us."

The job of a core processor is not to cut costs or assist with compliance, Leonardson says. "It's all about the member experience. A processor must help me deliver a dazzling member experience across all channels." How well they do that should alone determine whether a CU stays with its current processor or converts to a new one, he argues. Picking the right processor "has absolutely nothing to do with the economy, prices or regulatory pressures," he says.