



Strategies for more *effective* supervision and regulation

Technological advances and deregulation are quickly transforming the face of the community banks and bank holding companies we supervise, changing the nature of their operations and introducing new risks. To meet our responsibilities in the face of this change, in 1999 we continued to alter our supervisory processes, exploit new technologies, enhance staff development, and improve communication flows to bankers and the public. We believe the actions we undertook in these areas made our supervision more effective, more efficient, and less burdensome.



A double-edged sword

Technology is a double-edged sword for banks, offering both risks and rewards. New and more cost-effective digital technologies permit banks to provide products and services more economically to a larger and geographically dispersed customer base. And automation breakthroughs, when coupled with advances in financial engineering, permit better risk management.

New technologies can also mean increased operational risks. The century date change was a conspicuous example of this. During the course of several years, culminating on December 31, 1999, our examination and credit and risk management staff worked closely with the region's banking organizations and independent service providers to minimize the potential negative effects of Y2K and instill public confidence in our preparedness. When the new century rolled through international and then district time zones, meticulous preparation paid dividends when none of the region's banks encountered any significant operating problems.

Gramm-Leach-Bliley

New technologies also reduce communication costs and improve information flows, eroding geographic barriers and increasing competition. Intense competition has, in turn, provided an impetus for bank deregulation. Passed in late 1999, the Gramm-Leach-Bliley Act is a major overhaul of the nation's banking laws and the latest in a series of laws passed to reduced restrictions on banking. Gramm-Leach-Bliley expands bank powers and permits affiliation among banks, securities broker/dealers, and insurance companies. Like deposit deregulation and interstate banking legislation

before it, the new law is likely to intensify competition among financial services firms and, in the process, prompt rapid changes for banking organizations. These changes will pose a strategic challenge for banks and holding companies as they seek to identify their role in an evolving industry.

Enhanced processes

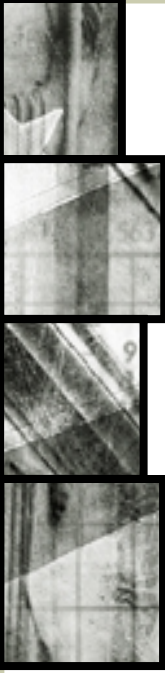
Myriad changes at banking organizations necessitate update of our supervisory processes and continuous staff development. To meet our mandate of promoting a safe and sound banking system, we've continued to integrate "risk-focused" processes into our examinations. Using a risk-focused approach, our examiners identify and review banks' risk exposures and the

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adequacy of their control systems to better determine their ability to manage change and adapt to competitive challenges. In 1999, we continued to integrate these processes with our examinations to obtain a more prospective view of those we supervise.

An important adjunct to on-site examination work is off-site monitoring of individual banks and the industry to help us keep abreast of changing banking conditions. We took steps throughout the year to enhance these efforts by partnering with other Reserve Banks to develop and improve the economic data available to our examiners. In addition, we moved forward with plans to create a supervisory presence at our





Omaha Branch and establish relationship managers as central points of contact for the institutions we supervise.

To assist examiners, we have also continued to refine our use of automated tools. Last year, our examiners utilized improved software to analyze bank-lending patterns, aid in loan reviews, document examinations, record examination findings, and expedite report preparation. We believe that as these tools evolve they will also enhance our efficiency.

Education and outreach

Process improvements alone cannot ensure supervisory success. It also takes a talented, dedicated staff, with the skill set necessary to assess the safety and soundness and compliance of rapidly changing institutions. In 1999, our staff attended numerous schools, seminars, and programs to keep updated on current banking issues, law and regulatory changes, economic conditions, new technologies, accounting pronouncements, financial innovations, and payments system developments. They also shared their expertise by participating as instructors and presenters in Federal Reserve System and interagency schools and in programs sponsored by others in the banking industry.

By sharing our knowledge of banking regulations and management practices with bankers and the public, the Federal Reserve can improve regulatory compliance and bank management, while reducing the demands on our supervisory resources. For this reason, education and outreach are vital components of bank supervision and regulation.

In 1999, we held regional meetings to update bankers on changes in bank regulations and to discuss current operational problem

areas. We also presented a variety of seminars on bank oversight to bank directors and officers and conducted sessions on fair lending for compliance officers. Our staff hosted community development roundtables in each of the district's seven states, sponsored community development workshops, and spoke at forums sponsored by others. And our Community Affairs staff developed 1stSource (www.1stsource.kc.frb.org), an interactive Internet site to provide easy public access to information on federal programs that assist community development projects.

2000

As the banking industry becomes more complex, our supervisory role becomes even more challenging. While it is difficult to predict what the future holds for the banking industry, we must, nevertheless, press forward with the programs and services that will add to our effectiveness in the year to come.

In 2000, we will open a new bank supervision office at the Omaha Branch to expand our service in the region. We will continue to evaluate the impact of the Gramm-Leach-Bliley Act and, where necessary, take actions to adjust our processes and practices to provide a coordinated approach for supervising financial holding companies created under the Act. We will participate in Federal Reserve System initiatives on community bank supervision, bank consumer compliance, supervisory use of information systems and web-based technologies, and development of staff training. And we will continue to promote compliance with banking laws and regulations, as well as economic and community development, through seminars, programs, publications, electronic media, and other outreach efforts.