

## Part 2: Strategic Insights into Technology Costs

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In addition to compliance costs in community banks, we also sought to consider other operating costs, including technology or data processing, as well as security and fraud related costs. This article will assess data processing and security/fraud cost trends, the quality of the service provided by these outsourced entities, as well as the prioritization of technology challenges for community banks over the next five years. Our separate compliance cost article examined the magnitude those costs and their impact on the long-term viability of community banks (the results from part one can be referenced in the publications section of Northeast Capital's website).

We distributed the survey to approximately 300 community banks, with an 8.0% response rate. Questions were aimed at measuring the increase in technology and security/fraud costs, as well as assess the banks' satisfaction with these services.

The results from our survey contain data from the past three years (2010, 2011, and 2012) and reflect the responses of twenty-four community banks that are located predominately in New York or New England and have assets between \$50 million and \$1.4 billion.

The responding banks had median total assets of \$422 million, 122 employees and nine branches at year end 2012. The middle 50% of the banks were between \$238 million and \$747 million in total assets, 65 to 187 employees, and 5 to 13 branches.

As shown below, processing and technology costs as a percentage of average assets (in basis points), decreased slightly for banks under \$400 million between 2010 and 2012. However, those same costs increased significantly for banks over \$400 million! This leads us to conclude that while smaller banks spend more overall (as a percentage of assets), larger banks have more frequent technological advancements, which appear in the form of greater costs.

	Median Processing/Tech Costs/Assets (In Basis Points)				
	Number	2010	2011	2012	2012 Range
Banks Under \$400 million	12	31.43	32.25	28.39	8.87-42.58
Banks \$401 million to \$750 million	7	20.86	21.65	22.97	4.04-31.31
Banks \$751 million plus	7	23.12	26.72	25.90	19.20-47.71
<b>TOTALS</b>	<b>24</b>	<b>23.12</b>	<b>23.93</b>	<b>26.24</b>	<b>4.04-47.71</b>

Overall security and fraud costs as a percentage of assets remained fairly constant between 2010 and 2012 as shown in the table below. However, within the three size categories disparities became more pronounced. Organizations less than \$750 million in assets experienced rising fraud and security costs, while larger entities saw substantially lower costs.

	Median Security/Fraud Costs/Assets (in Basis Points)				
	Number	2010	2011	2012	2012 Range
Banks Under \$400 million	12	1.94	2.10	2.13	0.78-5.16
Banks \$401 million to \$750 million	7	1.61	1.79	1.71	0.43-2.48
Banks \$751 million plus	7	2.23	1.70	1.60	1.04-4.24
<b>TOTALS</b>	<b>24</b>	<b>1.89</b>	<b>1.85</b>	<b>1.84</b>	<b>0.43-5.16</b>

With an overall grade of B-, banks were only slightly satisfied with their outsourced providers for tech. When broken down, you can see that the least satisfied group was the middle segment (\$401-\$750 million) with a grade of C. The smallest and largest segments on the other hand were more satisfied, having a grade a B and B- respectively.

<b>Satisfaction with Technology Provider</b>		
	<b>Number</b>	<b>2012</b>
Banks Under \$400 million	11	B
Banks \$401 million to \$750 million	7	C
Banks \$751 million plus	6	B-
<b>TOTALS</b>	24	B-

When looking at security and fraud providers, the results are slightly better with an overall satisfaction rating of B. Breaking this down we see that once again those least satisfied fell in the second segment with a C+; those banks in the smallest and largest segment had a satisfaction rating of B+ and B respectively.

<b>Satisfaction with Security and Fraud Provider</b>		
	<b>Number</b>	<b>2012</b>
Banks Under \$400 million	11	B+
Banks \$401 million to \$750 million	7	C
Banks \$751 million plus	6	B
<b>TOTALS</b>	24	B

In terms of prioritizing technology or security and fraud cost as a future challenge (from a list of 17 challenges) both fall within the top ten, with tech costs being more of a challenge at number five than security and fraud costs, which were deemed eighth in importance.

Based on the survey's responses, it appears that processing or technology costs are a slightly larger concern among community bankers than security and fraud costs.