



CommunityAmerica Credit Union: Customer-First Profitability

Industry

Financial Services

Problem

CACU needed to better understand customer (member) profitability so they could implement relationship pricing.

Solution

Create a new performance measurement system using Acorn Performance Analyzer.™

Results

Savings Opportunities

Identified to Date:

\$3-4 million annually.

Cost Base: \$63 million

- New pricing for auto loans improved margins
- High cost of debit rewards program resulted in restructuring and eliminating program for new customers



CommunityAmerica Credit Union (CACU) is one of the largest credit unions in the US, with about \$1.7 billion in assets and 168,000 members. Their primary market area includes Missouri and Kansas.

CACU embarked on a profitability initiative to better manage costs and measure customer (member) profitability as the basis for organizational measurement and to support relationship pricing. The credit union had implemented funds transfer pricing concepts along with E-Risk credit management systems, allowing them to understand margin and credit risk by customer.

The goal was to assign non-interest costs to the instrument level to create a full P&L. Once the profitability of each instrument could be determined, CACU could roll up the information to a member and household level. Other views of profitability would then become possible to support organizational measurement, including product and market area profitability.

The ultimate objective was to use the information to improve the profitability of member relationships and organization results while providing a fair pricing mechanism for members.

CACU implemented a time-driven activity-based costing (TDABC) system to determine cost components at an instrument/member level. In April 2008, the company completed implementation of a TDABC solution using Acorn Systems. CACU selected Acorn and their partner DecisionVu, because of their high level of commitment to customer success.



“ If you have it at an instrument level, you can roll it up any way you want to: by customer, household, market segment, product, by anything you can imagine. We can roll it up by the age of our customers, if we want. By driving it to that level and not spending all of your time trying to cascade cost through everything, you get a very good picture of the things you can actually manage. I don't know how to manage organizational profitability. I do know how to manage the profitability of customers. ”

Richard Baumgartner
Chief Financial Officer

CACU's new performance measurement system has two main areas of focus.

Understand profitability. Where does CACU make and lose money?

Why are they doing what they do? How can they segment and crosscut markets to figure out what businesses they should be in? How can they effectively service and deliver for members? On the profit side, CACU focuses on a market area; branch profitability is not relevant to their organizational performance structure.

Cost efficiency. Are branches efficient and well utilized? Are services cost effective? Are resources deployed to manage organizational human capacity?

All costs and revenue are driven to the instrument level.

Branch Profitability - A New Approach

CACU is pioneering new ways of looking at profitability. Branches are no longer considered “profit centers”. Total profit is now measured at the market, relationship and instrument levels. Their new performance measurement system has made this level of detail possible.

Traditionally, banks have focused on branch profitability; if a branch opens an account, or has a customer, they own the balance. CACU's branches do not own balances. Their purpose is to recruit new members, sell products and service members, which can include opening accounts.

CACU does not allocate all costs through the branches, because they are not trying to measure branch profitability. They focus on measuring member profitability. Most costs pass directly to the member instrument instead of passing through an organization hierarchy. For example, costs of using the contact center are not allocated to branches, but rather to the customer accounts serviced in the center. Once instrument level profitability is established CACU can roll up profitability using many different dimensions. They can include member, household, product or market area profitability.

A market area represents a trading area, which can include a branch but does not have to. CACU can measure the profitability of a trading area. The company measures branch level results through this market area approach. In addition, CACU measures capacity utilization by measuring the amount of time spent in a branch to process transactions compared with the available time for all staff in that branch. CACU can measure the efficiency of a branch along with market area profitability.

“ Within 24 hours of presenting our findings to the senior management team, we decided not to roll out a debit card rewards program to about 13,000 customers. At the same time, we created a new pricing program for our indirect auto program and improved the margin. We're in the process of redesigning our checking products, and that will have the potential to strip out as much as \$600,000 of additional costs. I've already paid for my time-driven activity-based costing system and my D-Day to roll out to management was two months ago.”

Andy Tuck
Vice President of Finance

The credit union is in the process of redesigning incentive and pricing plans to recognize this shift of focus to the customer/member level. The goal for branches is to provide efficient service, and the best possible banking experience for members of the credit union. Service is measured by *capability* utilization along with qualitative measures. In addition, branches have requirements for market area growth, which include production targets for new sales. By eliminating a true P & L with costs allocated to branches, CACU managers can focus more on what they can control: their trading area, their capacity and how efficient they are in servicing their members.

Identifying the Cost of Unused Capacity

Using TDABC, CACU can now perform capacity analysis and identify unused capacity. Traditionally, the cost of unused capacity is absorbed in the P&L. CACU needed a way to segregate used and unused capacity. Capacity is one of the key things measured and managed at the branch or operational center level, such as call centers and loan centers.

By using TDABC, the cost of unused capacity is clearly identified and is not passed to the customer view of profitability. CACU uses full absorption to determine product profitability and partial absorption for customer profitability. The difference is that unused capacity is not passed to customers.

Capacity analysis showed pockets of unused capacity, and revealed opportunities for more effective human resource utilization. For example, cross-sharing of employees in different back-office processing units. Other examples include opportunities for channel substitution including better use of IVR technologies, better pricing for fully absorbed costing, and outsource potential savings from process redesign of back office functions.

CACU discovered that capacity levels varied throughout the day. Branches and contact centers were busiest during lunch hours, when staffing is at the lowest levels. They are now looking at ways to solve this problem: more part-time staffing, staggered work hours, sharing work across departments.

Accurate Insight into Product and Transaction Costs

CACU can now see what is driving the cost of each instrument, account and transaction.

About CACU

CommunityAmerica Credit Union (CACU) is one of the largest credit unions in the US with about \$1.7 billion in assets and 168,000 members. Their primary market area includes Missouri and Kansas.
www.cacu.com

About Acorn Systems, Inc.

Acorn combines technology and methodology to improve profitability and increase shareholder value for Global 2000 companies in Financial Services, Retail, Consumer Products, Manufacturing, Distribution, Logistics and Services.
www.acornsys.com

About DecisionVu

DecisionVu is a specialized management consulting practice, focused on delivering measurable performance improvement. Their solutions provide leading companies with innovative tools and capabilities to measure and manage their performance, with a focus on knowledge transfer to deepen organizational capabilities.
www.decisionvu.com

Early results:

| Insight | Action |
|--|---|
| The debit rewards program had high costs. | The program is being restructured and will not be offered to new customers. |
| Discounts on auto loans with low credit risk negatively impacted profitability. For example, 42% of 60-month term loans were unprofitable. | CACU declined to accept loan applications for less than \$8,000, increased loan prices and offered discounts for loans \$30,000+ rather than \$25,000+. Loan volume did not decrease and profitability went up. |
| High costs on some checking accounts were related to high cost to serve. | Plans are under way to encourage changes in customer behavior. |
| Transaction processing of checking accounts varied from \$1 to \$100 per month. WHY? <ul style="list-style-type: none"> • Dormant accounts cost over \$.70 each to mail monthly statements. • Customers choose to be serviced via an IVR, phone number or contact center. Balance inquiries cost \$.07 with an IVR; \$ 3.45 with a live operator or contact center. Some customers called daily to check their balance. The large number of balance inquiries at \$3.45 each was costly and management had no visibility into these high costs. | Clean up dormant accounts. CACU is examining corporate policy that ensures members can talk to a live voice. Calls may be funneled through the IVR first to pick off balance inquiries and easy loan payment questions and then routed to a live person if needed. |

What's Next: Customer-Level RAROC, a Banking Innovation

In the future, CACU will have the capability of calculating risk adjusted return on capital (RAROC) for individual customers and each of their products. This includes the full profitability by instrument calculated through ABC and the cost of risk adjusted capital at the instrument level separately assigned. Customer-level RAROC calculations are an innovation in the industry. Typical RAROC calculations are most commonly done at a portfolio level (customer or LOB portfolio). However, there is significant variation of operational costs based on customer or product profiles. Customer-level RAROC will enable CACU to develop a more accurate “cost-to-risk” profile, and fine tune their product offering accordingly, which is becoming more critical in the current business environment.