

How Banks are Addressing New Compliance Challenges

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- Over last 24 months we have seen more regulatory changes with greater impact affecting bank compliance than any other period that I can remember. ABA has tallied 50 new or expanded regulations in this time period.
- Compliance certainly has not been easy lately, but in my opinion it may become even more challenging as a result of regulatory and legislative changes and increased levels of enforcement.

Recent Compliance Challenges

- Sweeping changes in Truth In Lending, both from Congress and the Federal Reserve.
- Complex new RESPA requirements that to some extent turn the Good Faith Estimate into a Good Faith Guaranty.
- Many other changes (SAFE Act, Internet Gambling, etc.)
- UDAP emergence as major compliance issue.

Recent Compliance Challenges

- Regulators are tightening the screws on overdraft protection. But unlike most compliance topics (such as funds availability) no one regulation to assure compliance:
 - Interagency “**guidance**” setting out “best practices”
 - Regulation DD (Truth In Savings)
 - Regulation E Opt in
 - **Unfair and Deceptive Acts and Practices (UDAP)**
 - “New” FDIC guidance stating regulatory “**expectations**”

Recent Compliance Challenges

Visible level of enforcement

- ▶ Many New England CMPs for flood
- ▶ Wells Fargo in class action ruling ordered to pay more than \$200 million to compensate customers charged higher overdraft fees due practice of posting larger checks first.
- ▶ OCC settlement with Woodforest National Bank (\$3.1BN in assets) to reimburse \$32 million (subject to increase) to consumers harmed by bank's overdraft program plus pay a \$1MM CMP.
- ▶ FinCEN assessed \$110 million CMP against Wachovia Bank for BSA violations.

Prospective Challenges

The Dodd–Frank Bill

- ▶ ABA estimated more than 5,000 pages of new regulation for traditional banks.
- ▶ Consumer Financial Protection Bureau
 - Will write rules applicable to all banks regardless of size – Significant New Disclosures & Reporting Requirements anticipated.
 - At discretion can examine community banks on a “sampling basis,
 - Has specific mandate to write rules targeting “unfair, deceptive, or **abusive**” practices.
- ▶ Preemption for national charters weakened.

Prospective Challenges

- ▶ Clearly much has been coming at financial institutions, and many are guessing that a lot more may be on the way!

- ▶ Gone are days when compliance was relatively simple, change infrequent and standards were less prone to informal regulatory interpretation.
- ▶ Institutions can't just assume that business units will on their own fully recognize, understand and discharge their compliance responsibilities.
- ▶ **Key issue** – how management and Board can reasonably assure themselves that compliance responsibilities are being properly discharged.

The Fundamentals

There has been increased emphasis on ensuring that an *effective* compliance management program is in place

- ▶ Compliance program and responsibilities
- ▶ Policies and procedures
- ▶ Independent testing
- ▶ Internal controls
- ▶ Monitoring
- ▶ Issue tracking

- ▶ Many issues being considered as institutions review compliance programs.
- ▶ I will discuss those where I see increased focus.

M&M's Perspective

- ▶ Increasingly we are replacing “general” auditors – Banks want high level of expertise
- ▶ More requests for reviews of compliance management system itself
- ▶ Requests for developing monitoring systems
- ▶ More assistance on policies and procedures.
- ▶ More on site training – **Board** and staff
- ▶ More training overall –(compliance school)
- ▶ Banks see value in risk based approach
- ▶ More Audit committee reporting

Compliance program and responsibilities

- ▶ Does program provide for compliance officer to be “responsible for compliance?”
 - Are responsibilities of “others” articulated, such as line management, the Board, individual performers?
 - Do job descriptions reflect responsibilities?
- ▶ Clear how institution will learn of and react to regulatory changes?
- ▶ Reporting to audit committee?
- ▶ Is there compliance committee? Role? Responsibility?
- ▶ **Effective** complaint mechanism

Policies and procedures

- ▶ Of course everyone has policies/procedures.
 - Are they up to date?
 - Do they reflect exam & audit comments?
 - Do they reflect how **specific** bank operates?
 - Are responsibilities made clear?
 - Are they detailed enough to provide meaningful guidance, particularly in high risk areas?

A Compliance Game Plan

Independent testing

- ▶ At one time, some institutions didn't want auditors to find exceptions on theory that it would tip off examiners.
- ▶ Present dynamic generally is that if institution finds a problem (either on its own, or through audit)– “no harm, no foul.” Management want audits to identify any deficiencies that may exist.
- ▶ Institutions held accountable for failure of audit program to identify deficiencies– sometimes cited as compliance management program deficiency.

A Compliance Game Plan

Independent testing

- ▶ Firm should have significant bank client base and expertise in compliance.
- ▶ Develop a risk based plan.
- ▶ Scopes should be clear.
- ▶ Assure findings go to audit committee.

A Compliance Game Plan

- ▶ **Monitoring** – similar to audit but
 - Done by or on behalf of management
 - Can be done in departments and/or centralized
 - Typically more frequent, focus on fewer items
 - Less formal in term of workpapers
- ▶ Absolutely should be risk based – this means program will change over time.
- ▶ Does monitoring staff have expertise &/or guidance?
- ▶ Are there specific monitoring procedures?
- ▶ Monitoring programs sometimes not effective
 - Process often only corrects individual errors
 - Often limited use of information developed – many missed opportunities

A Compliance Game Plan

Issue tracking system

- an effective tool for managing compliance risk;
- concept originally designed for tracking exceptions, but potential is much greater.

Issue Tracking System

- ▶ Given complexity of regulatory environment, a limited recognition by examiners that banks may not get everything right first time.
- ▶ A lot less understanding when deficiency has already been brought to our attention and we failed to take effective corrective action.
- ▶ Repeat issues tend to result in a strong reaction from examiners– and they are right!

Issue Tracking System

- ▶ Approach is related to Enterprise Wide Risk Management: How does institution get hands around everything material from an oversight perspective?
- ▶ Open issue tracking should not be just about tracking whether issues have been resolved, but should encompass planning to help assure that issues *will be* effectively addressed in a timely manner.

Issue Tracking System

Getting together a plan

- ▶ ID what issues are to be tracked
 - Examination report exceptions
 - Informal comments made at exam exit meeting (someone charged with taking notes?)
 - Audit and compliance review findings
 - Other issues identified by management
 - Changes in regulatory requirements

Issue Tracking System

- Who will administer process?
- How responsibility (senior person) will be affixed?
- When will evaluation of effectiveness of corrective action occur (after/prior to completion)?
- Who will evaluate if corrective action effective?
- Who will determine time frames?
- How to handle “moving” time frames.
- Frequency and visibility of reporting
 - Management committee
 - Audit committee

Issue Tracking System

Important Miscellaneous concerns

- ▶ Capture what has been told examiners will be done; if change of corrective action, document why a different resolution was agreed to.
- ▶ Ascertain up front if “responsible person” is relying on events or resources outside of his/her control to resolve issue in time frame.
- ▶ For complex or significant issues, consider detailed action plan with interim due dates.

Issue Tracking System

- ▶ Specific issue tracking procedures need to address all of the above
- ▶ Objective is not only to assure corrective action is taken, but that corrective action is effective

Thank You!