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BANK THINK

Five Compliance Priorities for 2012

By Kathlyn L. Farrell

A compliance checklist for CEOs? That almost sounds like an oxymoron. Traditionally, bank CEOs did not give much thought to regulatory compliance unless something went wrong. However, as the regulatory environment continues to be enforcement-focused, bank CEOs must scan not only the economic landscape, but the regulatory one as well.

As CEOs set the priorities for their bank each year, what should be the regulatory compliance priorities for 2012? The problem is – there are so many regulations, and with Dodd-Frank, many more to come, where do you start?

Based on our experience and on recent bank regulatory enforcement actions (both public and private) here is a compliance to-do list for 2012 for banks of all sizes.

1. Establish a UDAAP compliance program:

The concept of unfair, deceptive or abusive acts or practices is perhaps the biggest consumer protection regulatory risk facing banks. Many enforcement actions, both formal and informal, cite UDAAP as the source. Even before the Consumer Financial Protection Bureau was officially up and running, the other banking regulators were aggressively examining

for UDAAP compliance. UDAAP is unusually subjective and very broad, covering most banking transactions. Interpretations are not black and white, and activities that have not previously been criticized are coming under fire. An institution's best compliance defense is to develop a UDAAP compliance program specifically designed to produce fairness and clarity in banking transactions.

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A good UDAAP program, at the minimum, must have the usual compliance elements: policies, procedures, risk assessments, monitoring and testing and a formal governance structure. However, it needs more than this. UDAAP violations are often found deeply embedded in the operations of the institution – areas where compliance departments usually do not venture. Effective UDAAP compliance will need more than just regulatory subject matter expertise (the typical compliance department skill set). For starters, a good UDAAP



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compliance program will need operational and IT experience. Successful regulatory compliance departments of the future will consist of a variety of experts – with the ability to analyze bank products and services holistically – and see them from a consumer perspective. Another essential component to a UDAAP compliance program is a well-managed consumer complaint process that captures all complaints, notes the root causes and tracks complaint trends over time.

2. Do a fair-lending checkup.

Fair-lending compliance pressures have not abated. The Justice Department recently imposed the largest-ever civil money penalty for

fair-lending violations. Prudential bank regulators continue to issue fair-lending enforcement actions; the regulatory emphasis in examinations is as focused as ever.

A fair-lending program must include all bank lending products, not just mortgages. While mortgage lending remains the area of highest scrutiny – especially mortgage servicing, other types of loans can be problematic as well. A fair-lending program must include such products as direct and indirect auto loans, unsecured consumer loans and hybrid products, such as deposit advance loans.

If the bank allows lenders to set prices on any types of loans – even for purposes of meeting the competition – a well-designed risk management program is essential to monitor and test for fair-lending concerns.

3. Do a redlining review.

Redlining claims are making a comeback. Banks should not wait for their regulator to determine where the bank's loans are being made and if the bank is serving all areas of its communities. CEOs should have a complete and thorough understanding of where the bank's loan dollars are going as

well as how their marketing dollars are being spent. Special attention should be paid to low- and moderate-income areas within the bank's assessment areas.

Mortgage lending is not the only type of loans to consider in a redlining review. Take a look at where consumer loans and small-business loans are made. If there are low- or moderate-income geographies within the bank's footprint that are light on loans, determine the reason before your regulator asks. Having a plan and knowing and being able to tell your story (before your examiner does) is one of the best ways to avoid redlining problems.

4. Get your small-business lending in shape for data collection.

One of the new requirements of the Dodd-Frank Act is that banks must collect and report small-business loan data annually – much like HMDA data is now reported. This data collection will enable regulators to determine if an institution is fairly lending to women and minorities. Until the actual regulations are written, data collection is not required. So, in the time available before the rules are in place, banks should take the opportunity to get small-business

portfolios in good shape – from a fair-lending perspective.

One potentially troublesome small-business loan issue is pricing. Many institutions have rate sheets and controls on consumer loan pricing, but not for small-business loans. Regulatory agencies will eventually be able to analyze small-business loan data much like they now review HMDA data, and will be able to compare pricing on loans made to women and minority borrowers. It is crucial to develop and implement effective pricing and underwriting policies and controls for small-business loans. 2012 is the time to get these policies and control elements in place.

5. Make sure your BSA/AML program pillars are still intact and working.

For the last couple of years there has been a prevalent perception that the regulatory agencies were putting less emphasis on Bank Secrecy Act/anti-money-laundering programs. Whether or not that perception was true, BSA compliance enforcement is definitely making a comeback.

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