Financial Institution Compliance Update

February 10, 2015

This communication is designed to provide you with quick snapshots and timely perspective on recent regulatory developments.

OCC's Fall 2014 Semiannual Risk Perspective report: Key areas of concern for banks

Background

In December 2014, the Office of the Comptroller of Currency (OCC) issued their Fall 2014 *Semiannual Risk Perspective* report[1] produced by the OCC's National Risk Committee.

The report identifies a number of observations related to the performance of large, midsize, and community banks during 2014 and the points of emphasis that the OCC will focus on in 2015 as part of their examinations and other oversight activities. In the sections below, we share OCC's key areas of concern, their priorities for the next 12 months, and guidelines to help your business prepare for the examinations.

OCC's key areas of concern for 2015

Board members, executive, operating, and all areas of governance, risk and compliance (GRC) management, will be under increased scrutiny to demonstrate that strategic, operational, and compliance risks are being managed effectively. This is a high priority as banks adjust to the current economic environment of low interest rates and competition for sustainability and new business growth. The OCC has cited heightened concerns related to the following risk categories:

Strategic risk continues to be high for banks due to the following:

- Banks are reviewing their business models and risk appetites. They are also expanding to new, less familiar, or higher risk products without the appropriate level of due diligence, risk assessment, and internal controls.
- Banks are lowering overhead expenses through personnel reductions, outsourcing critical control functions to third parties, and other means without appropriate levels of due diligence.
- Banks are seeing more competition from non-banking firms taking on traditional banking activities.
- There is an increasing level of technology risk due to more institutions moving towards cloud computing and mobile banking.
- Bank Secrecy Act (BSA) and anti-money laundering risks (AML) are more frequent as a result of increased sophistication and volume of electronic banking fraud.
- Management succession planning and training are more challenging for banks.
- Execution of strategic and capital plans in the current business environment has also become a struggle for banks.

1 http://www.occ.gov/publications/publications-by-type/other-publications-reports/semiannual-risk-perspective/semiannual-risk-perspective-fall-2014.pdf, Retrieved January 26, 2015.

Operational & compliance risks are high for banks due to the following:

- Business models are under increased pressure as banks attempt to launch new products, increase automation, reduce staff, and re-engineer business processes.
- More institutions are allowing employees and third parties to access banking information through personal mobile devices which can lead to higher security and reputational risks.
- Varying types and complexity of third-party relationships are increasing, requiring effective risk management of such relationships.
- Changing business strategies of organizations may include the bundling of products and services and/or banks taking on new roles as "agents" between consumers and merchants.
- Banks are increasing the use of central counterparties in an effort to reduce foreign counterparty risk.
- Underwriting standards and extension of loan duration are becoming less complex, which in turn help institutions achieve higher returns. This can also cause deterioration of credit risk tolerances.
- The current low interest rate environment is creating an increased risk in asset-liability management, interest rate risk management, liquidity management, and capital sufficiency.

OCC's supervisory priorities for the next 12 months

Given the areas of risk listed above, the OCC has established a set of priorities for 2015. The key areas of focus include:

- **Continued Focus on Governance and Oversight** including risk management practices that address the OCC's "heightened standards guidelines" under 12 CFR Parts 30 and 170
- **Operational Risk Compliance** including areas impacted by foreclosure consent orders, model risk management, liquidity risks, third-party management, cyber security / data protection, and change management initiatives
- **Credit Underwriting** including commercial and retail credit practices with a high emphasis on leveraged loans, auto loans, and commercial loans
- **Compliance** including enhanced coordination of the OCC with the Consumer Financial Protection Bureau (CFPB) to determine compliance with consumer regulatory requirements. Flood Disaster Protection Act, Servicemembers Civil Relief Act, BSA/AML and risks associated with new products, services, and loosening of underwriting standards will be points of emphasis
- **New Regulatory Requirements** related to capital, liquidity, trading, residential mortgages, and risk retention
- **Fair Access** including assessment of compliance with the Community Reinvestment Act (CRA) and other consumer protection laws
- **Enforcement action and MRA Corrective Action follow-up** will also continue to be a part of OCC's area of focus

Guidelines to prepare for the examinations

OCC's priorities are significant and far reaching impacting virtually all aspects of a bank's strategy, operations, and compliance functions. In the following section, we share recommendations to help organizations prepare for these examinations:

1. Make sure your risk management function is comprehensive and is designed and operating effectively. A strong risk management function can serve to reassure management that the strategic, operational, and regulatory compliance controls are in place to protect your organization against financial, reputational, and regulatory compliance risks. Has your risk management function been subjected to an internal / independent audit?
2. Review your *three lines of defense* structure. Is it properly designed, coordinated, and operating effectively with no gaps or redundancies? Is it built on a solid framework such as the Committee of Sponsoring Organizations of the Treadway Commission, the International Standards Organization frameworks for ERM? If reviewed by the OCC, would they be able to conclude that they could place some reliance on your internal risk management function?
3. Review your *risk universe*. Is it up-to-date with reference to the policies and procedures approved by your organization to manage such risks? Do you have *first line of defense* testing protocols (such as Risk Controls Self-Assessments) in place to substantiate that key controls are operating effectively?
4. Assess your key / targeted potential issue areas. Are OCC targeted tactical areas such as BSA/AML, vendor risk management procedures, IT security and vulnerability, credit risk management, and other key areas designed and operating effectively?

How Experis Finance can help?

Experis Finance offers industry experience in all aspects of GRC including: organizational design, infrastructure, governance, program initiation, comprehensive risk assessments, controls and monitoring techniques, management information systems, and board reporting.

In addition, our team of subject matter experts in the areas of vendor risk management, compliance, BSA/AML, IT security, vulnerability, business continuity, and other key areas can help you assess the design and operating effectiveness of your current systems and processes. We can also complete an independent review of your potential vulnerabilities and share recommendations to help close any potential control gaps.

We work with large, midsize, and community banking organizations to support their efforts in complying with the vast amount of regulatory requirements and help guide them to a path of effective risk management and sustainability. We have significant experience in ensuring our clients are meeting OCC expectations and can offer competitive insights as well as industry best practices.

If you have any challenges with preparing for the examinations, **contact** an Experis representative to let us know how we can help you address your specific needs.