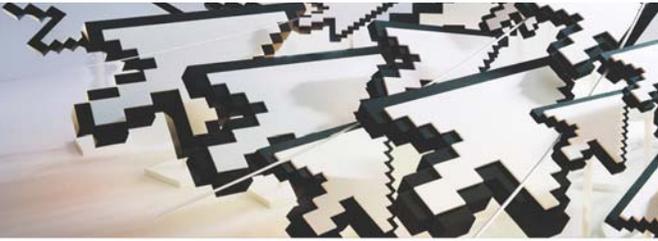


Financial Services Regulatory Update



June, 2017

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

Compliance Risk Management: Adding Value through Compliance Audit

Background

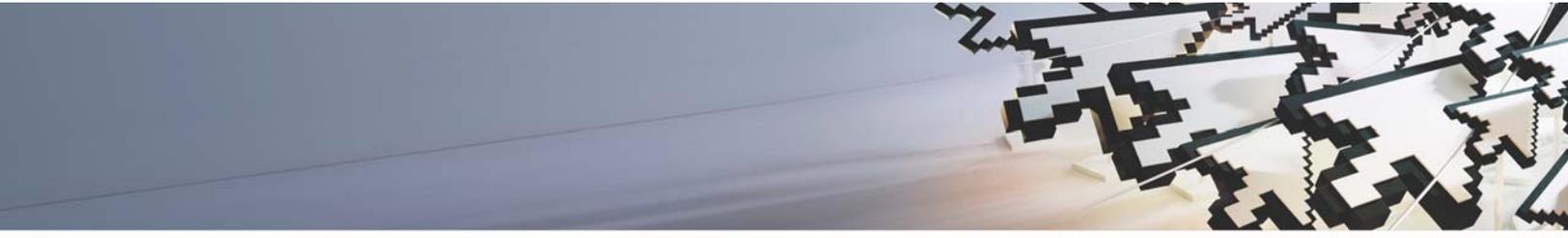
With the recent shift in regulatory supervision toward a focus on the risk of consumer harm in banking practices in addition to numerous regulatory changes on the horizon, financial services organizations are seeking value in controls and processes across the three lines of defense. Most especially, compliance internal audit has become one function management and directors are demanding to see greater value. Whether through process enhancement recommendations, personnel and training evaluations, or assessing control effectiveness, compliance auditors face increasing expectations to justify the time and cost invested to assure control and process effectiveness by adding value to the organization.

Audit Value: Theory and Strategy

Internal Audit methods, whether operational or specific to compliance, have not changed much since the Committee of Sponsoring Organizations (COSO) principles for enterprise risk management were integrated into compliance risk management programs. Still, compliance auditors who excel in their roles are those who look and work beyond work programs, checklists and testing to better understand what they are auditing, how best to conduct the audit in view of the organization's infrastructure and controls, and how audit findings can reveal process inefficiencies or other weaknesses that increase compliance risk.

Process Narratives and Audit Programs gave way in large part to Risk and Control Matrices as compliance audit professionals recalibrated their work and focus toward regulations and business activities posing the greatest risk to their organizations. However, this shift addressed merely the manner in which audits were conducted, ignoring the margin for value-add. And while Process Narratives have been used effectively to summarize the connections between business activities, they presume a keen understanding of the context within which each process operates. Auditors have been adept at drawing conclusions based on Process Narratives and the Audit Programs they drive, but business line management, boards of directors, and strategic managers have a different perspective on the organization and its goals, requiring clearer views of processes and practices, particularly where weaknesses create inefficiencies and higher risk due to ineffectiveness.

The most effective compliance auditors have found a way to bring the benefits of comprehensive Process Narratives for critical activities into risk-driven audits based on a combination of documents and information, beginning with the Compliance Risk Assessment. Once the risk assessment methodology and results have been confirmed, higher risk areas and business activities are targeted for comprehensive compliance audits. These typically are conducted in a way that leverages activity-based information gathered through Process Narratives to build out risk and control matrices specific to broader business lines, such as loan originations, loan servicing, deposit operations, and so on. Part of the process of completing the narratives involves developing a process road map to help identify gaps, duplications of effort, or other weaknesses that increase risk or impede efficiency. One method for revealing these challenges to efficiency is flow charting.



Conducting the Best Compliance Audit: A Case Study

Using the compliance audit function to facilitate regulatory change implementation can also significantly improve board and management reporting, providing the information and illustrations necessary for management to make informed decisions about such questions as where or whether to introduce new systems or replace outdated ones, whether key functions are adequately staffed and sufficiently equipped to perform the work expected, and how to create efficiencies while making the best possible use of limited resources.

For example, when the Truth in Lending Act and Real Estate Settlement Procedures Act Integrated Disclosure rules took effect, organizations discovered quickly that their forms and core origination systems were only part of the answer to implementation. Technical training and reference guides closed some of the knowledge gap, while first- and second-line of defense practices and processes were saddled with multiple check-points to manage the first months of loans originated under the new rules. What many organizations found was that, while hiring additional staff would help manage the burden, few of them had the resources to simply expand their staff. And for those with the budget to hire more resources, doing so created as many problems as it solved. One success story, however, revealed the material and strategic benefit of evaluating business processes in light of the requirements, mapping existing activities and processes to first identify gaps and then making adjustments accordingly to strengthen controls, leveraging systems and highly specialized personnel to target the portions of processes needing change.

In this organization, the compliance internal audit function performed a readiness assessment according to the regulatory guidance from the Consumer Financial Protection Bureau. The audit team conducted interviews, reviewed loan origination system updates and release notes, and worked with sales, processing and pre-closing staff to map the manner in which information and documentation flowed as part of the loan origination process. Creating this road map to the process revealed several activities that were highly duplicative. For instance, Mortgage Loan Originator assistants were comparing system inputs to system outputs for the same system (not surprisingly with a 100% accuracy rate), while loan processors were comparing system outputs to regulatory requirements. The audit team recommended the MLO assistants discontinue the comparison of inputs to outputs in favor of focusing on the accuracy of inputs based on information provided. This minor change resulted in significantly more accurate information being provided to loan processing staff, who in turn became much more productive because they spent less time correcting input errors.

As the compliance audit continued, several more process weaknesses were detected and addressed with minor process adjustments, resulting in a remarkable productivity improvement. This in turn led to a highly efficient process, leading to shorter processing times, faster closings, and happier borrowers. Based on the work flows, Process Narratives, and recommendations by the audit team, management felt confident in making the recommended adjustments because they could clearly see the benefits and, perhaps more importantly, the more effective management of risk. Involving compliance training personnel in mapping the processes and developing recommendations also gave management the opportunity to provide training and communications throughout the initiative and to develop meaningful onboarding training specific to the job expectations.

Finally, compliance auditors provided illustrations to help management create efficiencies and limit impact to business line staff as the new rules were implemented. The report summary and additional information addressing the strategic alignment between business processes, staff and systems provided to the Board gave directors assurance that the organization made the best possible use of the resources available to them while effectively managing compliance risk.



How Experis can help

Experis Finance offers industry experience in all aspects of Financial Services, including:

- Performing objective assessments of compliance risk management practices
- Assessing the adequacy of your organization's compliance control environment
- Developing internal compliance monitoring and audit programs to address unique risks
- Developing and maintaining first-, second- and third-line controls and testing related to compliance

Our Risk Advisory Services practice can evaluate your compliance management program, provide comprehensive recommendations for improvement and help you address those recommendations.

Our team of professionals has extensive experience working with clients to address these issues to help them avoid costly fines and penalties. If you have any questions about or concerns around your implementation of these steps, contact an Experis representative at financialservicesindustry@experis.com or visit our website [Experis Finance](#).