When You Have to be Right:

The Top 10 Compliance Management Considerations for 2023

Craig Focardi | Elaine Duffus

September 29th 2022

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The Top 10 Compliance Management Considerations for 2023

Welcome to Today's Webinar!

Kyle Brasseur
Editor in Chief
Compliance Week

COMPLIANCE WEEK
FOR THE WELL-INFORMED CHIEF COMPLIANCE OFFICER AND AUDIT EXECUTIVE

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When You Have to be Right:

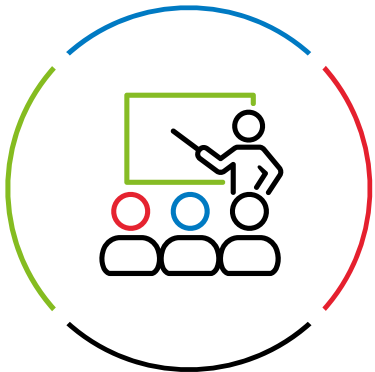# The Top 10 Compliance Management Considerations for 2023

Agenda

1. Welcome and Introduction

2. Highlights from the Wolters Kluwer 2021 Banking Regulatory & Risk Indicator Survey

3. The Top 10 Compliance Management Considerations for 2023

4. Question & Answer Session

5. Wrap up

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The Top 10 Compliance Management Considerations for 2023

Today's Speakers

Craig Focardi
Principal Analyst
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Senior Specialized
Consultant
Wolters Kluwer

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When You Have to be Right:

The Top 10 Compliance Management Considerations for 2023

Polling Slide #1 – What are your organization's major compliance challenges??

1. Keeping up with Regulatory Change
2. Technology and Solutions
3. People and organizational resources
4. Manual Process Inefficiency
5. Budgets
6. Ineffective management and coordination
7. Competing/Conflicting Business Priorities
8. Not certain

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Highlights from the Wolters Kluwer 2021 Banking Regulatory & Risk Indicator Survey

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Wolters Kluwer Banking Regulatory & Risk Management Indicator Survey

The purposes of the Survey are to:

- Collect trend information on the breadth and depth of regulatory/risk concerns
- Determine realized and anticipated regulatory impact on institutions
- Assess sophistication of banks' current risk management efforts
- Gather data inputs to calculate a regulatory and risk management pain index score, which is tracked and reported annually

https://www.wolterskluwer.com/en/know/regulatory-risk-management-indicator

Wolters Kluwer Banking Regulatory & Risk Management Indicator Survey

2021 Indicator Survey: Key Highlights

- **The Main Indicator Score rose to 128 from 103 in 2020.**

- **Primary Drivers:**
  - Managing risk across all lines of business;
  - Navigating significant regulatory changes; and
  - Increase in fines imposed by bank regulators.

- **Keeping current with changing regulations continues to rank consistently as a top challenge, no matter the lender type or size.**

- **Top obstacles to implementing an effective compliance program:**

  - Manual processes (45%);
  - Inadequate staffing (41%);
  - Too many competing business priorities (36%).

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Top Regulatory Compliance Challenges

What do you believe will be your organization's most pressing regulatory compliance challenge over the next 12 months?

Large Banks/CUs (>$1 Bil.)	Medium Banks/CUs ($500M to $999M)	Small Banks/CUs (<$500M)
Consumer protection regs	Keeping up with changes	Keeping up with changes
Keeping up with changes	Consumer protection regs	CECL
CRA	BSA	Tech/Tech compliance

Banks	Credit Unions
Keeping up with changes	Keeping up with changes
Consumer protection regs	CECL
Tech/Tech compliance	Consumer protection regs

Source: Wolters Kluwer 2021 Banking Regulatory & Risk Indicator Survey

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The Top 10 Compliance Management Considerations for 2023:
Hardening your defenses and preparing for the onslaught

1

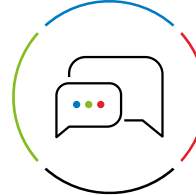EVALUATE YOUR REGULATORY INVENTORY FOR COMPLETENESS

2

ASSESS YOUR REGULATORY CHANGE PROCESS FOR EFFECTIVENESS AND EFFICIENCY
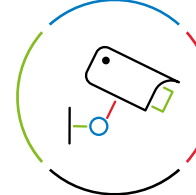
3

TEST YOUR CULTURE OF COMPLIANCE / POLICIES AND PROCEDURES FOR EFFECTIVENESS

4

EVALUATE YOUR COMMUNICATIONS AND TRAINING FOR USEFULNESS

5

MEASURE THE EFFECTIVENESS OF YOUR MONITORING, AUDITING AND REPORTING

6

GAP-ASSESS YOUR THIRD-PARTY MANAGEMENT AND M&A PROCESSES

7

REVIEW YOUR PROCESS FOR PREVENTION, DETECTION, DISCIPLINE AND REPORTING COMPLIANCE VIOLATIONS

8

ENSURE YOUR ASSESSMENTS ARE TAILORED TO YOUR RISKS

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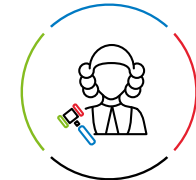
EXAMINE YOUR GOVERNANCE PROCESS FOR RISK AND EFFICACY

10

FOLLOW THE MONEY – UNDERSTAND INCENTIVE AND COMPENSATION SCHEMES

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The Top 10 Compliance Management Considerations for 2023

1 EVALUATE YOUR REGULATORY INVENTORY FOR COMPLETENESS

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Regulatory Compliance is complex and overlaps

Major U.S. Financial Regulators and Organizations

Prudential Bank Regulators
(Depository Regulators)
- FRB
- OCC
- FDIC
- NCUA

Other Regulators
(consumer protection, mortgages and financial crimes)
- CFPB
- FHFB
- FINCEN

Securities and Derivatives Markets
- SEC
- CFTC
- FINRA

Coordinating Forums
- FSOC
- FFIEC
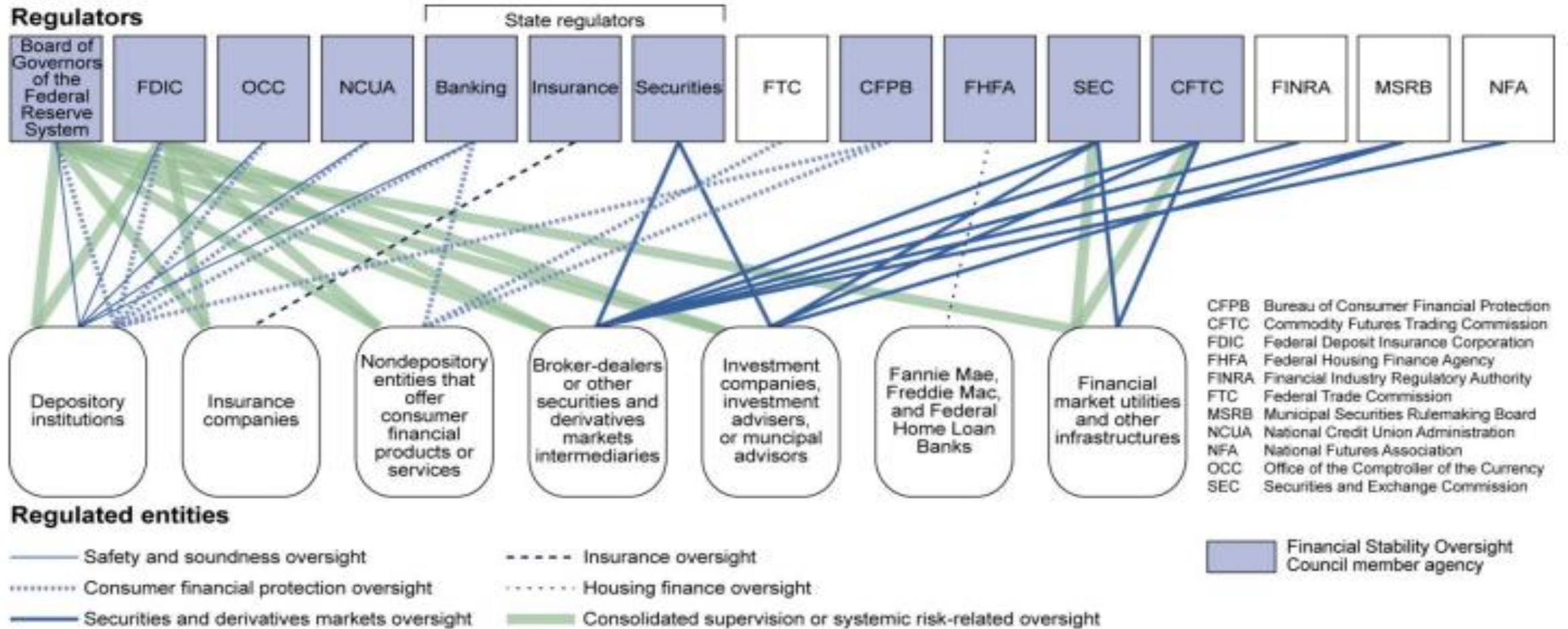- President's Working Group on Capital Markets

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(2) ASSESS YOUR REGULATORY CHANGE PROCESS FOR EFFECTIVENESS AND EFFICIENCY

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An Overview of the U.S. Financial Regulatory Framework

Source: Government Accountability Office (GAO), *Financial Regulation*, GAO-16-175, February 2016, Figure 2.

Regulatory incidence of SEC proposed & final rulemakings

Regulatory Incidence of SEC Proposed & Final Rulemakings (Gensler Chairmanship, April 17, 2021 through July 10, 2022)
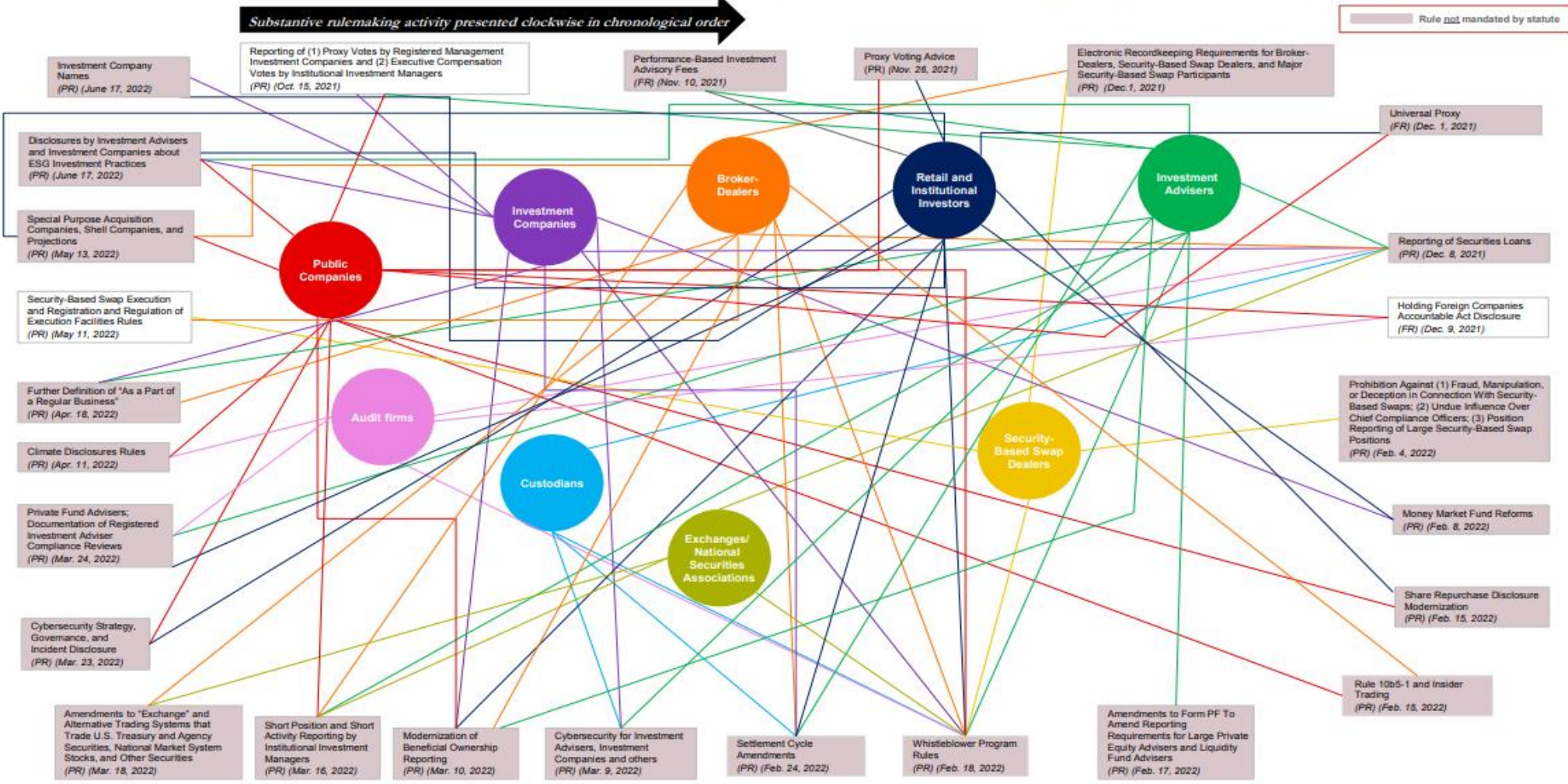
3 TEST YOUR CULTURE OF COMPLIANCE / POLICIES AND PROCEDURES FOR EFFECTIVENESS

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TEST YOUR CULTURE OF COMPLIANCE / POLICIES AND PROCEDURES FOR EFFECTIVENESS

Commitment by Senior and Middle Management
1. Conduct at the top
2. Shared commitment
3. Oversight

Autonomy and Resources
1. Structure
2. Seniority and Stature
3. Experience and qualifications
4. Funding and resources
5. Data resources and access
6. Autonomy
7. Oversight of Outsourced Comp functions

Policies and procedures
1. Design
2. Comprehensiveness
3. Accessibility
4. Responsibility for Operational Integration
5. Gatekeepers

See https://www.justice.gov/criminal-fraud/page/file/937501/download for more information

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September 2022
GAO Report to
Congressional Committees:

BANK SUPERVISION

Lessons Learned from Remote Supervision during Pandemic

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GAO Found Technology Gaps in Smaller Banks/CUs

- Heavy reliance on paper files
- Inability to upload documents/records
- Inability to provide access to internal systems
- Inability to test transactions

Federal Banking Regulators' Actions to Address Pandemic-Related Challenges to Conducting Full Remote Examinations

	Challenge being addressed			
Actions	Pandemic impacts on supervised entitles' risks	Transition to full-time remote examination work	Staff and technology constraints at some supervised institutions	Limitations on examination staff resources
Deferral of examination activities			■	
Expanded off-side monitoring to reassess risk to institutions	■			
Expanded telework and new technology tools		■	■	
Issuance of guidance and communications to examiners		■	■	
Adjustments to examination staffing				■

Source: GAO analysis. | GAO-22-104659

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4 EVALUATE YOUR COMMUNICATIONS AND TRAINING FOR USEFULNESS

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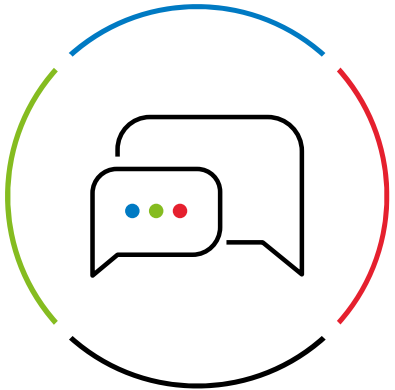
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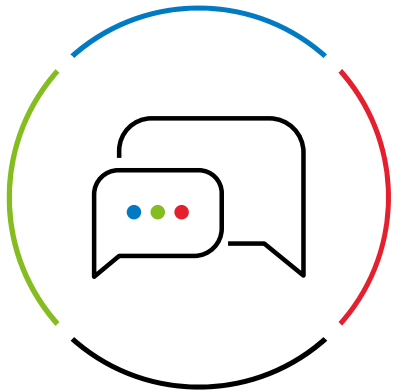
Training and Communication

Risk-based training

Form/Content/Effectiveness of Training

Communications about misconduct

Availability of guidance

See https://www.justice.gov/criminal-fraud/page/file/937501/download for more information

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5 MEASURE THE EFFECTIVENESS OF YOUR MONITORING, AUDITING AND REPORTING

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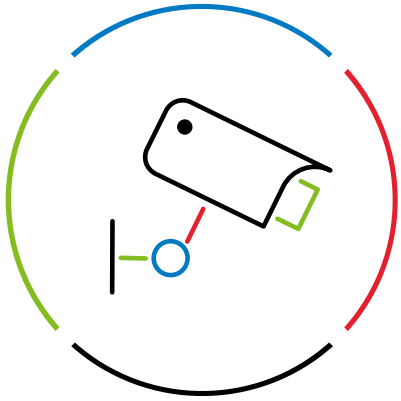
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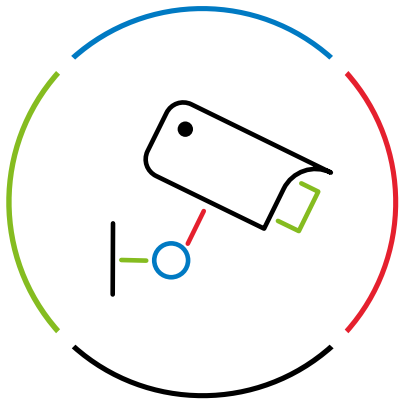
Continuous improvement, periodic testing and review

Internal audit

Control testing

Evolving updates

Culture of compliance

See https://www.justice.gov/criminal-fraud/page/file/937501/download for more information

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Achieving Compliance Effectiveness

PEOPLE

PROCESS

TECHNOLOGY

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Compliance Processes

New Account Transactions	**Account Management**
• Account sales • Account application • Disclosures • Compliance tolerance tests • Compliance data collection • Compliance reporting	• Compliance data management • Compliance analysis • Compliance reporting • Compliance audit support • Compliance management

Technology Components

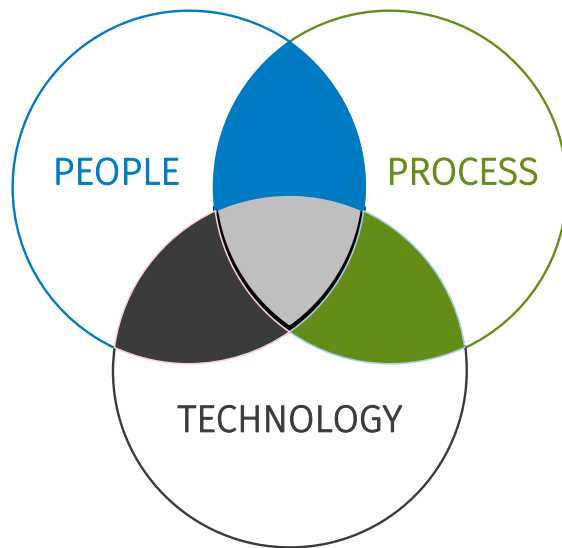| Component	Description
Data	Customer identity, income, asset, credit, and other demographic data
Platform	Transaction processing systems that collect, modify, analyze, and store compliance data and reports
Analytics	Analyze data accuracy, completeness; perform compliance tests, tolerances, calculations, and summaries:
Integration	Integrate processing and services systems with specialized compliance systems and other customer, product, and market data
Reporting	Internal compliance management, operations, and transactional reporting; External regulator, coordinating forum, shareholder, and investor reporting
Presentment	Digital: email, web, mobile in PDF/HTML format; Paper: as required

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Many processes are complex and have compliance embedded within

Mortgage Loan Processing and Compliance Overview Illustrative

Major Processes	Tasks and Compliance Requirements Within Processes				
1.Loan Application	Gather loan application data	Qualifies? Y/N → No / Yes	Pull credit / Request verifications		
2.Loan Processing		Submit for loan underwriting	Approved? Y/N → No / Yes	Draw / review loan documents	Review loan file for compliance; send to Servicer
3.Loan Servicing	Loan onboarding	Billing and payments	Escrow Account Management	Loan Collections and Modification	Repossession

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Automation enhances customer experience, reduces costs, and reduces errors

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Mortgage Loan Processing and Compliance Overview Illustrative

- Compliance requirements complicate and delay nearly every stage of the mortgage loan process, making them a prime target for automation.

Major Processes	Tasks and Compliance Requirements Within Processes				
Compliance	Loan officer compensation and anti-steering	Issue adverse action notice	Issue GFE and TILA disclosures FCRA	Data privacy laws Disclose intent to escrow	Re-issue GFE and TIL; Servicing Transfer Notice
1.Loan Application	Gather loan application data	Qualifies? Y/N — No / Yes	Pull credit / Request verifications		
Compliance	Originator registration/license, appraisal management	Determine if a Qualified Mortgage (QM)	New Ability to Repay (ATR) requirement	Issue declination letter	
2.Loan Processing		Submit for loan underwriting	Approved? Y/N — No / Yes	Draw / review loan documents	Review loan file for compliance; send to Servicer
Compliance	Notice of Servicing Transfer	Design new rate sheets	New underwriting requirements for QM loans		HMDA and CRA reporting requirements
3.Loan Servicing	Loan onboarding	Billing and payments	Escrow Account Management	Loan Collections and Modification	Repossession
Compliance	Notice of Servicing Transfer	New periodic billing statements; prompt payment crediting	interest rate adjustments; RESPA and TILA	FDCPA; FCRA; New continuity of contact law;	New loss mitigation laws; force-placed insurance law

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Automation differentiates leading organizations

Lagging Organizations ··········→ **Leading Organizations** ··········→

Technology
- No or limited/dated standards for technology options
- Freedom to purchase technology, sometimes without due consultation with IT
- Resulting in proliferation of multiple 'flavors' of technology

- Agreed upon standard, with flexibility for innovation
- Effective governance for alternative technology solutions
- Adoption of best practices through common technology solutions, in line with options recognized by the industry
- Dissemination of intended best practice technology

Process
- Inconsistent data sourcing, point-to-point solutions and varying analytical processes across business or functional units
- Inconsistent application of controls, leading to inconsistent views of data
- Redundancies and increased cost

- Consistent, agile processes across business units
- Ability to parse out work based on complexity and level of sophistication
- Dissemination of compliance best practices and results

Data
- Data is collated through different business rules, data guidelines, and integration schema
- Storage of data in multiple places with different levels of control and security assurance
- Differing archiving and reconciliation approaches
- Sourcing or capturing external, often unstructured data, is undertaken on a project or ad hoc basis

- A common, well documented data domain model and dictionary
- Common storage and retention capabilities
- Consistent population of databases, data warehouses, and data lakes
- Well understood data definitions and business logic
- Data broking function that enables acquisition of the right external data, useable on a repeatable basis

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6 GAP-ASSESS YOUR THIRD-PARTY MANAGEMENT AND M&A PROCESSES

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GAP-ASSESS YOUR THIRD-PARTY MANAGEMENT AND M&A PROCESSES

Third-Party Management

1. Risk-based and integrated processes
2. Appropriate Controls
3. Management of relationships
4. Real Actions and Consequences

Mergers and Acquisitions

1. Due diligence process
2. Integration in the M&A process
3. Process connecting due diligence to implementation

See https://www.justice.gov/criminal-fraud/page/file/937501/download for more information

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7 REVIEW YOUR PROCESS FOR PREVENTION, DETECTION, DISCIPLINE AND REPORTING COMPLIANCE VIOLATIONS

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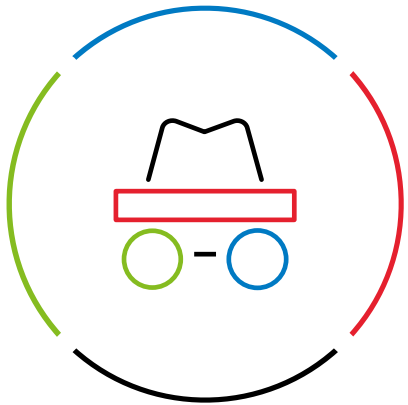
REVIEW YOUR PROCESS FOR PREVENTION, DETECTION, DISCIPLINE AND REPORTING COMPLIANCE VIOLATIONS
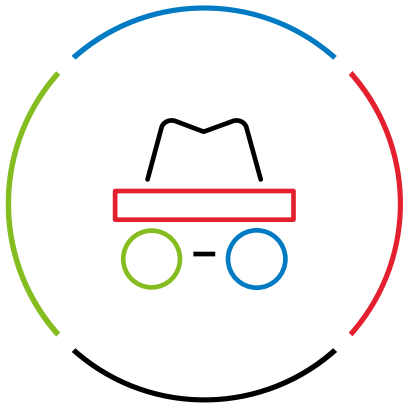
① Investigation of misconduct

1. Properly scoped investigation by qualified personnel
2. Responses to investigations

② Analysis and remediation of any underlying misconduct

1. Root cause analysis
2. Prior weaknesses
3. Payment systems
4. Vendor mgmt.
5. Prior indications
6. Remediation
7. Accountability

③ Confidential Reporting Structure and Investigation Process

1. Effectiveness of the Reporting Mechanism
2. Properly Scoped Investigations by Qualified Personnel
3. Investigation response
4. Resources and tracking of results

See https://www.justice.gov/criminal-fraud/page/file/937501/download for more information

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8 ENSURE YOUR ASSESSMENTS ARE TAILORED TO YOUR RISKS

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ENSURE YOUR ASSESSMENTS ARE TAILORED TO YOUR RISKS

Risk Assessment

Risk management process

Risk-tailored resource allocation

Updates and revisions

Lessons learned

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See https://www.justice.gov/criminal-fraud/page/file/937501/download for more information

Illustrative Example of a Compliance Risk Assessment Framework

Governance
Policies and Procedures | Organizational structure

Input

Inventory of regulatory obligations
- Statutory requirements
- Regulatory guidance
- Rules
- Internal

Understanding of compliance risk / regulatory compliance programs and the business

Key risk assessment components

| Risk taxonomy | Inherent risk / strength of controls |
| Risk units | Residual risk |

Supporting infrastructure
(e.g., Data, IT, analytics, tools, templates)

Key risk activities

Confirm against a top-down view of key risks

Develop action plan (e.g., updates to policies and procedures)

Syndicate assessment results and plan to senior business leaders / exec committee

Improve compliance risk controls

Generate compliance risk reporting to track progress

....

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Compliance life cycle management processes within the framework

1) Governance
(e.g. Organizational structure, Committee oversight)

2) Risk assessment
(e.g. risk identification processes, requirements, business objectives)

3) Rules and regulations
(e.g. inventory, tracking, document changes, assess and rate relevance and criticality, initiating internal updates)

4) Policies and procedures
(e.g. conception, translate changes into business requirements, implementation, documentation, maintenance)

5) Advise
(e.g. compliance/line of business interaction)

6) Communicate and Train
(e.g. onboarding, continuing education for new regulations and internal processes)

7) Control processes
(e.g. Remediation, PA dealing, gifts, entertainment)

8) Monitoring, testing, and surveillance
(e.g. monitoring and testing program)

9) Metrics, reporting and escalation
(e.g. KRIs, dashboards, communications)

Company and Compliance Culture

People

Data / Technology / Infrastructure

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9 EXAMINE YOUR GOVERNANCE PROCESS FOR RISK AND EFFICACY

Industry response to compliance has improved since before the 2008 crisis:

Financial institutions are beginning to align regulatory compliance to their other risk capabilities – market, credit, liquidity, capital, stress and operational risk

Evolution of the approach to managing compliance and governance
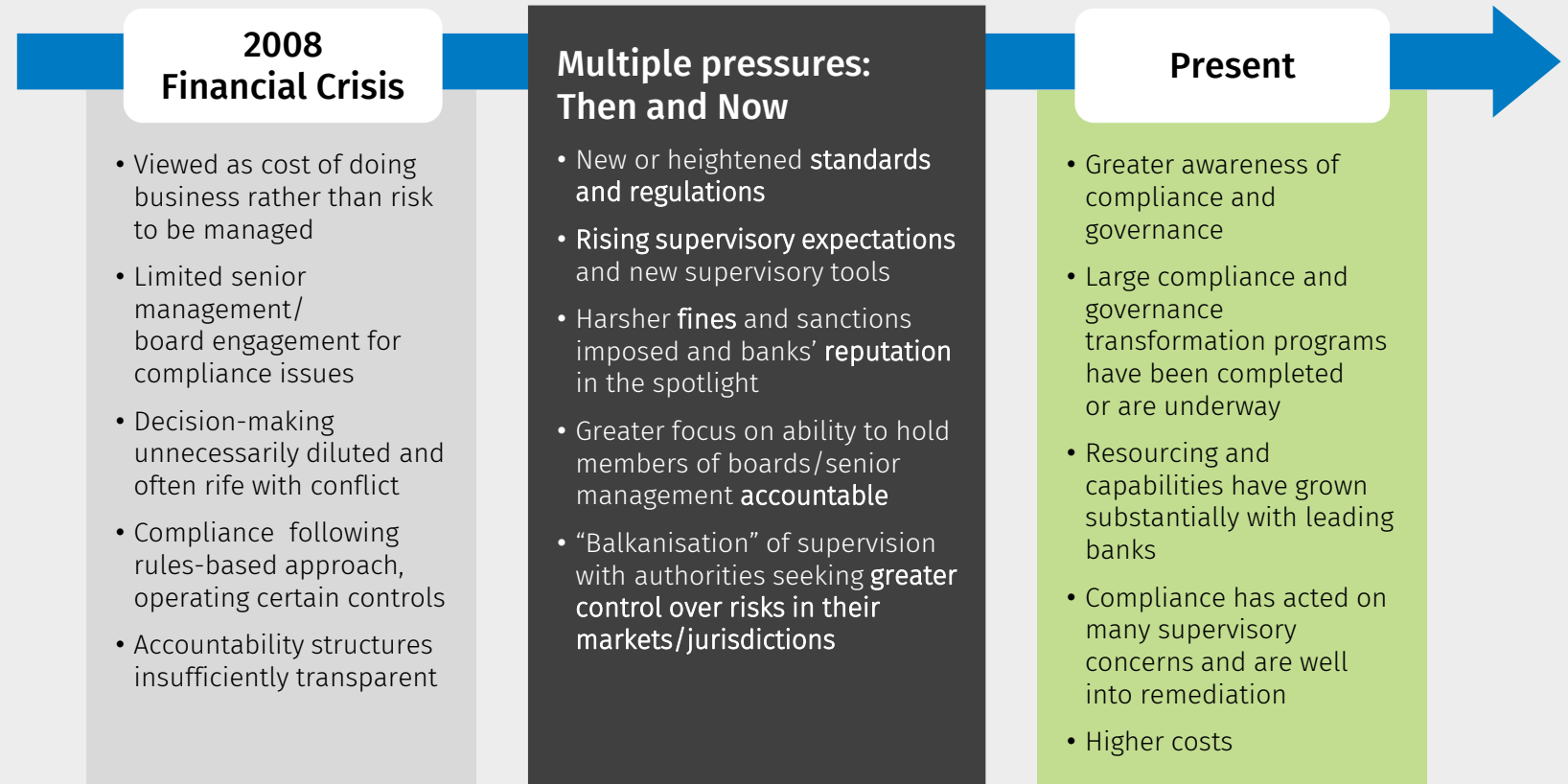
2008 Financial Crisis

- Viewed as cost of doing business rather than risk to be managed
- Limited senior management/ board engagement for compliance issues
- Decision-making unnecessarily diluted and often rife with conflict
- Compliance following rules-based approach, operating certain controls
- Accountability structures insufficiently transparent

Multiple pressures: Then and Now

- New or heightened **standards and regulations**
- **Rising supervisory expectations** and new supervisory tools
- Harsher **fines** and sanctions imposed and banks' **reputation** in the spotlight
- Greater focus on ability to hold members of boards/senior management **accountable**
- "Balkanisation" of supervision with authorities seeking **greater control over risks in their markets/jurisdictions**

Present

- Greater awareness of compliance and governance
- Large compliance and governance transformation programs have been completed or are underway
- Resourcing and capabilities have grown substantially with leading banks
- Compliance has acted on many supervisory concerns and are well into remediation
- Higher costs

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10 FOLLOW THE MONEY – UNDERSTAND INCENTIVE AND COMPENSATION SCHEMES

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FOLLOW THE MONEY – UNDERSTAND INCENTIVE AND COMPENSATION SCHEMES

Incentives and Disciplinary Measures

HR Process

Consistent Application

Incentive System

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Polling Slide #2 – Based upon today's discussion, what will be your organization's major compliance focus area to meet key challenges in 2023?

1. Automation

2. Staffing & People

3. Budget

4. Governance

5. Communications

6. Leadership

7. Not certain

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Question and Answer Session

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The 7 Pillars of Compliance Program Management

Opportunities for Automation and Making Connections

| Regulatory Library | Regulatory Change Management | Compliance & Ethics Governance | Compliance Risk & Controls Assessment | Compliance Testing | Complaint Management | Exam & Inquiry Management |

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Wolters Kluwer offers a unique advantage for your business

Wolters Kluwer provides a comprehensive set of technology, solutions, and services for today's financial institution

Regulatory Compliance

Digital Lending Compliance

Compliance Program Management

Our longevity and proven stability helps us to your strategic partner in compliance

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The Top 10 Compliance Management Considerations for 2023

Resources and More Information

- <u>Wolters Kluwer Expert Insights Spotlight: "Proactively addressing key challenges and enabling success for the Chief Compliance Officer"</u>

- Wolters Kluwer Expert Insights White Paper: "The Top 10 Compliance Management Considerations for 2023"

- <u>Wolters Kluwer Compliance Program Management Solutions</u>

- <u>Celent VendorMatch for Risk and Compliance Management</u>

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Thank You!

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