

WIB/AABD Directors Conference

Compliance: The Role of the Board



Presented by:
Andrew L. Meinhold
Brode Consulting Services
andy@brodeconsulting.com
440-739-0445



Agenda

- Why Compliance is Important
- Director's Role in the Compliance Program
- Discussion of High Risk Compliance Areas
- Tips on Questions to Ask and Red Flags



Regulations

- Reg B, Equal Credit Opportunity
- Reg E, Electronic Funds Transfer
- Reg Z, Truth in Lending
- Reg BB, Community Reinvestment Act
- Reg X, Real Estate Settlement Procedures Act
- Reg DD, Truth in Savings
- Reg P, Privacy of Consumer Financial Information
- Reg F, Interbank Liabilities
- Reg O, Insider Lending
- Reg D, NOW Accounts/MMDA



Regulations

- Reg CC, Funds Availability
- BSA – Bank Secrecy Act
- FACTA – Fair and Accurate Credit Transactions Act
- Fair Housing Act
- Fair Debt Collection
- Information Technology
- Bank Protection Act
- Home Mortgage Disclosure Act (HMDA)
- Lending and Appraisal Policies
- Internal and External Audit Programs



Compliance Program Elements

- Policies
- Compliance Officer
- Procedures
- Training
- Allocation of resources
- Reviews and audits
- Board reporting
- Assessment and monitoring of risks



Compliance Program Questions

- How are compliance requirements and changes monitored?
- How is compliance tested on a transaction basis?
- Is there an independent review of the compliance program or at least of the highest risk areas?
- What kind of compliance training goes on? What is it and who gets it?



Red Flags for Compliance

- Number and severity of audit and review findings
 - Timeliness in responding and correcting
- Staff changes and turnover in compliance
- The lack of compliance topics at board meetings
- Customer dissatisfaction and ***complaints***
- Lack of periodic compliance reports



Product Risk

- Which of the bank's products carry the greatest risk from the standpoint of
 - Materiality – how much do they contribute to the balance sheet
 - Stability – how long has the product been around and how complex is it
 - Product management – how much experience does the bank have in handling the product
 - Overall size of the bank or branch



Regulation Risk

- What is the potential consequence to the public and to the bank of noncompliance
- Includes factors such as
 - Financial harm to consumers
 - Financial harm to the bank
 - Legal harm to the bank
 - Reputation risk to the bank
 - New laws, regulations or amendments
 - The burden of corrective action including civil and financial liability



High Risk Compliance Issues

- BSA
- Insider Lending
- Information Security/BCP
- CRA
- Fair Lending
- Flood Act
- Truth in Lending – APR
- Specific Provisions of RESPA



BSA Program Requirements

- A system of internal controls to assure ongoing compliance with BSA
- Independent testing for BSA/AML compliance
- Designated person(s) responsible
- Training for appropriate personnel (everybody!)
- Customer information program (CIP); risk-based procedures that enable the institution to form a reasonable belief that it knows the true identity of its customers



BSA Red Flags

- Written BSA/AML program
- All required program elements
- Written risk assessment
- SAR reports
- Are BSA/AML changes tracked and implemented
- **Annual testing**
- Training program and schedule in place
 - Should include BOD training



Reg O Actions

- A prohibition on loans to insiders unless a loan
 - is non-preferential **and**
 - does not present a higher-than-normal risk of repayment or other unfavorable features.
- A requirement that prior board approval is obtained for loans to insiders greater than a certain amount.
- A limit on lending to individual insiders and to insiders in aggregate.
- Restrictions on loans to executive officers in other ways.
- Restrictions on the payment of overdrafts for insiders



Reg O Overdraft Prohibition

- Unless there is a pre-approved line of credit or transfer
- Inadvertent
- \$1,000 or less
- Not more than five days
- Charged the same fee as any other customer



Reg O Red Flags

- Insider policy/Conflict of Interest
- Annually pass a resolution specifying the executive officers
- Annually complete form identifying insiders, related interests and immediate family
- Receive reports indicating any loans made to insiders, related interests or immediate family
- Proper overdraft protections put in place



Information Security

- Banks must take steps to:
 - Insure the confidentiality of customer records and information
 - Protect against any anticipated threats or hazards to the security or integrity of such records
 - Protect against unauthorized access to or use of such records that could result in harm or inconvenience
 - Ensure proper disposal of consumer information



Information Security Program

- Address three main components
 - Prevention
 - Detection
 - Response
- Must include
 - Risk assessment
 - Methods of risk control and management
 - Testing
 - Service Provider arrangements
 - Incident response and customer notification
 - Training

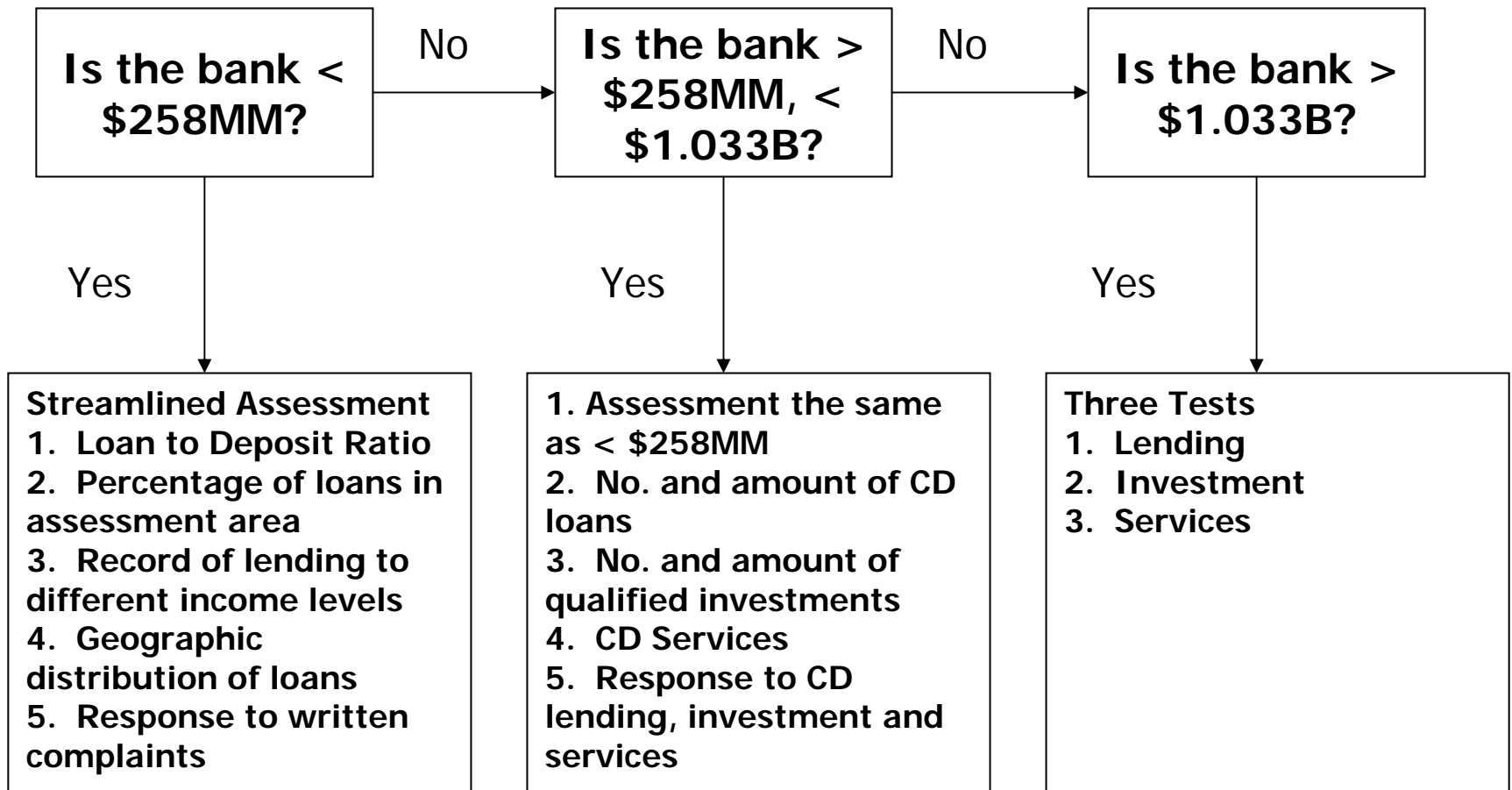


Questions for Info Security

- Does the bank have a written information security program?
- Is it updated at least annually?
- Does it address prevention, detection and response?
- Ask about and understand what steps the bank takes to protect customer information
- Pay attention to both low tech and high tech
- Make sure a process is in place to identify a breach and determine whether a response and notification is needed



CRA Assessment Levels





CRA Reports

- The bank's loan to deposit ratio
- The percentage of the bank's loans within the assessment area
- Dispersion of loans geo-coding report: the percentage of loans within each census tract of the assessment area
- Whether there have been any complaints against the bank



Fair Lending/ECOA Red Flags

- An existing or proposed lending policy whose standards for underwriting, pricing, or setting terms and conditions are vague or unduly subjective, or which allow substantial loan officer discretion.
- Any statements by officers, employees, or agents, indicating a preference, prejudice, or stereotyping on a prohibited basis, or an aversion to doing business in minority areas.



Fair Lending/ECOA Red Flags

- Segmentation of product markets, advertisements, promotions, application channels, or other access to credit along the lines of racial or national origin characteristics of applicants or geographic areas.
- Consumer complaints alleging discrimination in specific transactions.



Fair Lending/ECOA Red Flags

- Substantially fewer loans originated in areas with relatively high concentrations of minority group residents than in areas with comparable income levels, but relatively low concentrations of minority residents.
- Disparities in Home Mortgage Disclosure Act (HMDA) data.



Fair Lending/ECOA Red Flags

- Low levels of minority applicants even though minorities represent a significant part of the service area.
- Use of credit scoring models that have not been validated.



Flood Act

- May not be waived
- Procedures in place to monitor?
- Ability to “force place” insurance



Other Areas of Concern

- Truth in Lending – APR calculation
- RESPA – Settlement statements for covered loans



Regulations Requiring Annual Review

- Bank Secrecy Act
- Bank Security Program
- Community Reinvestment Act (CRA)
- Insider Lending
- Real Estate Lending Standards
- Interbank Liabilities
- External Audit Program
- Information Security Program
- Business Continuity Plan



Thank You

- Questions?
 - andy@brodeconsulting.com
 - 440-739-0445