Volume 1, Issue 1

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# Bank Director's Guide to Regulatory Compliance

## *Happy New Year and Welcome to more Dodd Frank…...*

**Special points of interest:**

- Where is Your Greatest Risk
- Keep track of required training.
- HMDA deadlines
- Fair Lending- establish standards
- S.A.F.E. Act include HR
- Club Management keep the green clear for the putt.
- Appraisal Management don't forget to include commercial loans


Ask any consumer, they believe their confidential information will be compromised this year.

**Inside this issue:**



*This newsletter is designed to provide information so Board Members can ask questions of bank management about pertinent regulatory issues and to provide some basic insight of their fiduciary responsibilities to the shareholders.*

## Where Is The Greatest Risk To Your Institution?

We used to fear the bank robber, they guy with the gun. We trained our staff how to protect bank assets, we taught them how to react in a robbery, we even trained them multiple times on the in's and out's of bank robbery.

Employees were taught how to identify a person that was casing the bank, how to report suspicious activity and how to spot a robber BEFORE they got to their teller window.

How do we teach them to identify the theft of confidential consumer information? Who do they look for? What characteristics to they look for in an identity thief?

When a robber came into the bank to get money, they got what was in a teller drawer, or even perhaps what was in the vault. If a thief gets into your data systems, what do they get? Customer information, funds from customer accounts, your reputation, the loss is unfathomable, yet we spend less time training our staff about IT related risk than we do about any other area of the bank. Let's be serious if the regulators didn't require it, we probably wouldn't do it at all.

We don't enforce rules about storing customer information during banking hours or after no one but the janitors are in our building after hours.

We don't' enforce the frequency to change passwords, because we agree it is hard to remember new passwords.

We don't lock down the IT equipment room, because the room gets hot and we need to leave the door open rather than invest in a cooling system for the room.

We don't destroy hard drives when we donate old computers, well. In fact, they didn't really work well and we deleted files from the hard drive, right?

Let's talk about cell phones, specifically smart devices. We streamlined Board reports by putting them on web access. Do board members down load reports about the bank? Loan write-ups, reports on NSF activity, past dues, the list goes on and on.

How do we know board members don't let their grandchild load games on that very same device? Games often contain mining viruses.

How do we control when that board member gets a new device? Where is the old one? What bank information was on that device?

If your IT department is not annoying you about controlling data, they may not be doing you a service. Controlling data may just be the greatest area of risk to your institution?

We can't see the data robber come into the lobby!

## Risk Management

What is all the hub bub about Risk Management? If you have had an exam in the last 36 months, it is likely the examiners asked to see your Risk Assessments and to know when the board approved them.

If you haven't approved your institutions risk assessment this year, you should ask why not. What tends to happen is a risk assessment is conducted, approved and then set aside. In reality, the risk assessment should be the road map for the organization, AND it must be dynamic. This means, management should refer to it often and as environments change so should the risk assessment. Let's say you had a low risk rating on debit cards in 2011 because you had never experienced fraud on your cards, if you are located near St. Louis, I bet 2012 was different. Can you say Schnucks?

Each component has to be evaluated and measured, it is not an exact science, but it is a road map that will get you in the "ball park", just maybe not specific enough to find your seat.

Regulators will refer to your risk assessment when things go wrong, so keep it current and somewhere close at hand.

## HMDA

Consumer Financial Protection Bureau

**Makes you stop and go HUMMM! Here's what you need to know about HMDA.**

HMDA is an acronym for Home Mortgage Disclosure Act and it has been around since 1975. So it is not new.

In July 21, 2011, the rule-writing authority of Regulation C was transferred to the Consumer Financial Protection Bureau (CFPB). This regulation provides the public loan data that can be used to assist:

- in determining whether financial institutions are serving the housing needs of their communities;
- public officials in distributing public-sector investments so as to attract private investment to areas where it is needed;
- and in identifying possible discriminatory lending patterns.

The bank is required to report on a register (LAR) applications for loans secured by dwelling and the disposition of these applications; originated, sold, declined, withdrawn or approved and not accepted.

The standardized form outlines all the fields to be reported including the gender of the applicant, amount of the loan, who bought the loan, location of the property. There are two deadlines for completing the LAR. 1– Within 30 days of the end of each calendar quarter, it must be current through the end of the quarter that just ended and 2-it must be submitted by March 1 each year. There is a 5% tolerance for errors, which is does not allow for systematic errors. The book regulators publish each year, "HMDA Getting It Right", says it all!

We recommend an annual HMDA Data report to management and the board reporting results of the LAR and what it tells the organization about their lending practices at the end of each quarter.

**It would be wonderful if regulators and law-makers walked a mile in your shoes, wouldn't it?**

In the St. Louis market-place today, Fair Lending is a HOT HOT HOT button. The heat is turned up not only by your regulators but by community groups that profess to want the best for the underbanked and underserved.

Most bankers take offense to the implication they are biased against any ethnic segment of society. This is not a personal push against any one banker or institution, it is an organized effort to affect the community. It is all about Fair Lending and Reg. B.

## Fair Lending Programs and Controls

What is protected?

The institution must not tolerate discrimination due to:

- Race
- Color
- National Origin
- Sex
- Marital Status
- Age

If the application is related to a home application, it also includes:

- Handicap and
- Familial Status

The institution may not :

- Discourage an applicant from applying
- Refuse to extend credit,
- Use different underwriting standards,
- Vary the terms of credit,
- Use different standards of evaluating the collateral,
- Fail to provide information on products and services

Fair and equal treatment of all is the key to Fair Lending. Be sure you are approving policies and management has strong procedures in place.

### How do you manage Fair Lending?

It must start at the top. The Board and Management set the tone. Then it is all about training. If you write policies and procedures, and do not communicate the message that discrimination is not to be tolerated, you are not getting the message to the troops. It only takes one lender with an attitude toward one of the protected basis to get you for a Fair Lending violation. Lets say, Joe Lender is going through a nasty divorce, he carries a real chip on his shoulder. An applicant comes to the bank to apply for a loan to purchase a new car. She is going through a divorce and her mean, nasty ex-husband got her car in the divorce. Joe Lender is getting lots of push back from his soon to be ex-wife about wanting him to give her the family vehicle. Will Joe's current personal tribulations affect his ability to work with the applicant who is experiencing similar issues? See how easy it might be to discriminate. Or perhaps a lender has very strong opinions about people that are receiving government/public assistance for disabilities. Or mothers that collect Aid for Dependent Children but keep having more children. These are real situations and real attitudes you have to address with your lenders and lending staff. You cannot tolerate even the slightest comment or innuendo regarding these protected basis. Training is how to communicate and lay the groundwork establishing the your expectation.

## S.A.F.E. Act

It has now been five years since we had to implement procedures for S.A.F.E. Act compliance. The S.A.F.E. Act is the regulation that requires mortgage loan officers to register with the National Registry.

We are seeing banks that are not monitoring the renewals, or hiring a lender that was registered and failing to update the NMLS.

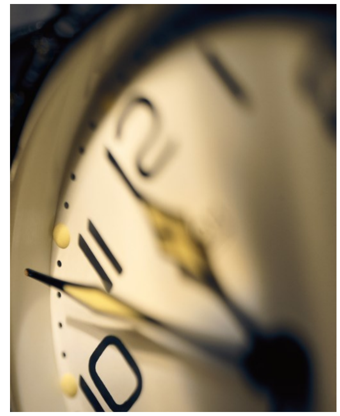
Your HR department should know that before a loan officer is hired, they must be able to be registered, and continue to be registered. If the hiring is taking place without checking the NMLS, you may get caught with a new loan officer that cannot make loans until they can be registered. Worse yet, an officer that cannot pass the background check.

Strong internal controls, hiring practices and job descriptions are going to be important to ongoing compliance to the S.A.F.E. Act.

This process must include identifying mortgage lenders in job descriptions, at the time of hire, and training all loan department employees on what loan activity they can and cannot participate in. Be mindful of those individuals that quote rates, if they are going to participate in the application process, they must be registered.

Fingerprinting and background checks are required and time consuming.

New hires (if registered at their previous employer) have only 30 days to get their information updated in the NMLS. The clock is ticking.



Warning: Ongoing training is a requirement. Don't forget to have it on your required training schedule for mortgage loan officer and staff.

## What Golf Club Do You Manage With

People often ask me why I named my company Ace In The Hole Management. There are several reasons, articles like this is just one. When I started my company my logo was a driver addressing the ball. Why?

It was a visual of my strategic plan, in addressing the ball with the driver, I wanted to get the company up in the air, get my name out there and yes, go far. When I hit my first milestone, then I needed the 7 iron to keep the ball moving toward the green.

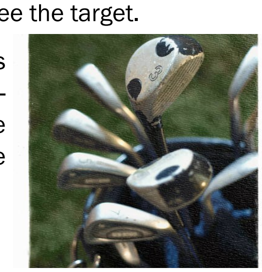
In my game, my driver is my best club.

How does this equate to leading your organization? We can divide the bank into club selection, if we do, the Board is the Driver. Setting the direction the organization is headed. Executive Management is your irons, keeping the organization moving forward, and the employees are the putter, sinking the putt, implementing the strategy.

So I ask, how are your employees at lining up their putt? Are there multiple cups on your green or is the Board and management all focused on the same cup?

If your employees are missing the putt, is the green clear of clutter and can the employees see the cup clearly? If not, perhaps you need to tend the cup more closely, hold the flag up so they can see the target.

To use a St. Louis slang, "I'm just sayin'" all things in life can be analyzed like a golf game, right?



## Appraisal Management

If you make mortgage loans, you should know the guidelines for appraisal management; cannot use an appraisal ordered by the borrower, loan officer cannot order the appraisal, select the appraiser, or conduct the appraisal review. But how do these guidelines carry over to your commercial loans?

It's all about risk management. So ask yourself, if you understand the risk related to appraisal management for mortgage loans, how do you not apply the same rules to commercial loans? Aren't the same risks evident in the commercial appraisal process?

- Lender/Appraiser collusion,
- Borrower/Appraiser collusion,
- inadequate appraiser oversight,
- inadequate review of the appraisal.

All are potential weaknesses that may cause your commercial credit to deteriorate and ultimately, you will have to write down the difference between loan balance and property value.

A best practice is to implement your appraisal procedures across all loan types.

Don't forget to implement rules regarding use of previous appraisals and how to validate those values in today's market.

Market fluctuations, property values, and borrower's income levels, are just a few ways to validate a previous appraisal.

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*Happy New Year*

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Ace In The Hole Management is a full service bank consulting company that serves community banks in the Mid-West.

We are your Partner In Doing Business, whether it is Compliance, Internal Audit , Bank Secrecy Act, Loan Review, IT Audits and Penetration and Vulnerability Tests, Reputation Risk Management, Executive Management consulting, or Training. We can partner with your bank in a customized program that fits your strategic plan. We can write your policies and procedures, create an efficient management strategy, or be your compliance and/or BSA officer.

**Our services are designed to fit your need.**

**Our fees are designed to fit your budget.**

**Our work product is designed to exceed your expectation.**

We have been offering customized compliance and internal audit services since 2007. These services range from acting as the compliance officer on site for specific weeks per month, to quarterly visits. Our clients continue to tell us we exceed their expectation.

***Won't you let us have a chance to do the same for you?***

*Deborah K. Williams*