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BANK WIRE

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www.acxellrms.com 877.651.1700

UDAAP resurfaces

IS YOUR BANK IN COMPLIANCE?

The Dodd-Frank Act gives the Consumer Financial Protection Bureau (CFPB) broad authority to prosecute unfair, deceptive or abusive acts or practices (UDAAP) by banks and other financial providers. Early last year, the CFPB announced a new policy that gave institutions a reprieve from UDAAP enforcement actions. But in March 2021, it rescinded this policy, signaling a return to more aggressive enforcement. (See "CFPB renews focus on UDAAP enforcement" on page 3.)

UDAAP REFRESHER

During the COVID-19 pandemic, many banks have changed the way they do business — for example, by reducing lobby hours, closing branches, and relying more on mobile banking apps and online transactions — and many of these changes may be here to stay. So, given the CFPB's more aggressive enforcement stance, it's a good idea for banks to review their UDAAP compliance policies and update them to reflect current business practices.

One reason UDAAP might be problematic is that its restrictions are quite broad and, in some cases, vague. Generally, an act or practice is *unfair* if it causes, or is likely to cause, substantial injury to consumers and such injury isn't reasonably avoidable. *Deceptive* acts or practices are those that mislead or are likely to mislead consumers, provided the consumer's interpretation is reasonable under the circumstances and the act or practice is material.

An act or practice is *abusive* if it materially interferes with a consumer's ability to understand a product or service's terms or conditions. Alternatively, abusive acts or practices may take unreasonable advantage of consumers' 1) lack of understanding, 2) inability to protect their interests, or 3) reasonable reliance on banks to act in their interests.

CFPB guidance provides a nonexhaustive list of examples of conduct that may, depending on the facts and circumstances, constitute UDAAPs. They include:

- Collecting or assessing a debt or additional amounts in connection with a debt (for example, interest, fees or charges) not expressly authorized by the agreement or permitted by law,
- Failing to credit a consumer's account with timely submitted payments and then imposing late fees,
- Taking possession of property without the legal right to do so,
- Revealing the consumer's debt, without consent, to the consumer's employer or coworkers,
- Falsely representing the character, amount or legal status of the debt, and
- Threatening any action that isn't intended or authorized, including false threats of lawsuits, arrest, prosecution or imprisonment for nonpayment of debt.

CFPB RENEWS FOCUS ON UDAAP ENFORCEMENT

In January 2020, the Consumer Financial Protection Bureau (CFPB) issued a policy statement providing some relief to banks for unfair, deceptive, or abusive acts or practices (UDAAP). Pursuant to the statement, the CFPB said it wouldn't challenge conduct as *abusive* unless the harm to consumers outweighed the benefits. It also pledged to end "dual pleading" — that is, charging a bank with both abusiveness and unfairness or deception based on the same conduct — and to refrain from seeking monetary relief when a bank made a good-faith effort to comply with the law.

In March 2021, the CFPB rescinded the policy statement, finding it inconsistent with the CFPB's mission. Going forward, it will exercise the "full scope" of its enforcement authority, although it will consider good faith and other relevant factors in using its prosecutorial discretion.

Certain misrepresentations also may qualify as UDAAPs. For instance, a bank can't falsely claim that a debt collection communication is from an attorney or government-affiliated source. Banks also can't lie about whether information about a payment or nonpayment would be furnished to a credit reporting agency — or falsely promise to waive or forgive debts if consumers accept a settlement offer.

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COVID-RELATED UPDATES

The COVID-19 pandemic has caused most businesses, including banks, to change the way they do things — so now's a good time for a review. For example, have you permitted borrowers to skip loan payments under certain circumstances? Will that policy continue even after the pandemic ends? If so, you need to ensure that your policy is designed and communicated in a manner that isn't unfair, deceptive or abusive to your customers.

During the pandemic, many banks have relied more heavily on electronic transactions in light of social distancing guidelines, a practice that may continue post-pandemic. If your bank permits customers to receive disclosures and other documents electronically, be sure that your policies and practices are fair, clearly communicated and don't negatively impact customers without access to the necessary technology.

Even physical access and security practices may raise UDAAP concerns. For example, could reducing branch hours be perceived as unfair or abusive to specific customers? And what about masks or other face coverings? Ordinarily, banks prohibit them. But by necessity, exceptions have made pursuant to mask mandates during the pandemic. In the absence of a mandate, what will your bank's policy be going forward? Will you require customers to remove their masks, even if they're at higher risk or simply feel more comfortable wearing one? Whatever your policy, it should be carefully designed and communicated to avoid UDAAP issues.

TRAINING IS KEY

Any time a bank changes its business practices or establishes new ones, it's important to evaluate whether those changes raise UDAAP concerns. Even if your policies are fair on paper, they can still trigger UDAAP liability if they're not put into practice properly. So be sure that bank staff or other representatives are adequately trained. ■

KEEP YOUR CUSTOMERS SATISFIED

Over the past few years, community banking has withstood rapid technological changes, unprecedented economic challenges during a pandemic and new demands from its customer base. To maintain profitability amidst all this turmoil, you need to ensure that your bank retains its existing customers. After all, studies show that attracting a new customer typically costs five times more than retaining an existing one.

Here are three fundamental questions to help improve customer satisfaction and, ultimately, retention.

1. WHAT'S YOUR CORE DEPOSIT BASE?

A good first step is to identify your core deposits and develop an understanding of customer behaviors. Differentiate loyal, long-term customers from those motivated primarily by interest rates. A core deposit study can help you distinguish between the two types of depositors and predict the impact of fluctuating interest rates on customer retention. Banking regulators strongly encourage banks to conduct these studies as part of their overall asset-liability management efforts.

Core deposit studies assess how much of your bank's deposit base is interest-rate-sensitive by examining past depositor behavior. They also look at factors that tend to predict depositor longevity. For example, customers may be less likely to switch banks if they have higher average deposit balances and use multiple banking products (such as checking and savings accounts, mortgages and auto loans).

2. HOW CAN YOU GET TO KNOW YOUR CUSTOMERS BETTER?

To build customer loyalty, it's critical to ensure that customers are engaged. According to research by Gallup, engaged customers are more loyal, and

they're more likely to recommend the bank to family and friends. They also represent a bigger "share of wallet" (that is, the percentage of a customer's banking business captured by the bank).

Recent retail banking studies show that fewer than half of customers at community banks and small regional banks (less than $40 billion in deposits) are actively engaged. The percentages are even smaller at large regional banks (over $90 billion in deposits) and nationwide banks (over $500 billion in deposits). That's the good news. The bad news is that 50% of customers at online-only banks are fully engaged.

So, how can community banks do a better job of engaging their customers to compete with online banks? The answer lies in leveraging their "local touch" by knowing their customers, delivering superior service, and providing customized solutions and advice. To do that, banks must ensure that their front-line employees — tellers, loan officers, branch managers and call center representatives — are fully engaged in their jobs.

Encouraging employees to engage with customers has little to do with competitive salaries and benefits. Rather, it means providing employees with opportunities for challenging work, responsibility, recognition and personal growth.

3. HOW CAN YOU DEVELOP YOUR ONLINE PRESENCE?

An increasing number of customers — younger people in particular — use multiple channels and devices to interact with their banks. These include online banking, mobile banking applications and two-way texting.

To build loyalty, banks should enable customers to use their preferred channels and ensure that their experiences across channels are seamless. And don't overlook the importance of social media platforms. Younger customers are more likely to use these platforms to recommend your bank to their friends and families.

ASK THE RIGHT QUESTIONS

Your customer retention strategies shouldn't be based on guesswork. Consider periodically engaging with customers concerning their level of satisfaction with your current systems and processes. Ask what they'd like to see improved. A brief survey, or even a short conversation, can provide valuable input on ways to keep your customers satisfied with your bank's services over the long term. ■

MAINTAINING INTERNAL CONTROLS IN A POST-PANDEMIC ENVIRONMENT

Internal controls are the lifeblood of a bank's risk management system. Weak or ineffective controls can lead to operational losses and expose a bank to a higher risk of fraud. As we continue to recover from the COVID-19 pandemic, banks need to assess the pandemic's impact on their internal control systems and make appropriate adjustments.

Many banks continue to rely on remote workers, and it's likely that many employees will continue to work remotely long after the pandemic is behind us. In addition, some banks are operating with reduced workforces. In this environment, maintaining key internal controls — segregation of duties, in particular — can be a challenge. In addition, as workers' duties are adjusted to accommodate remote work and leaner staffs, these changes can inadvertently render some controls ineffective.

EVALUATE THE IMPACT ON SEGREGATION OF DUTIES

Segregation of duties is a simple yet powerful control that substantially reduces the risks of fraud and error. By assigning different people responsibility for authorizing or reviewing transactions, recording transactions and maintaining custody of assets, a bank makes it virtually impossible for a single employee to perpetrate a fraud or make an error *and* conceal it. If workforce changes reduce segregation of duties, they can significantly weaken a bank's internal controls.

Consider this example: ABC Bank has been operating with a reduced staff since early in the pandemic. As lending activity has increased, its staff has struggled to keep up with the growing volume of loan applications. To avoid falling behind, the bank provides Jane Doe, its vice president for loan servicing, with the ability to record transactions on the bank's loan system. Because Jane is also responsible for reviewing loan file maintenance changes, she now lacks independence with respect to her review of loan file maintenance reports. In other words, the duties associated with recording and reviewing transactions are no longer segregated.

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How can your bank avoid this situation? When employees' *operational* responsibilities change, it's important to evaluate any potential conflicts of interest with employees' existing *review* responsibilities.

DIGITAL APPROVALS: HANDLE WITH CARE

A byproduct of the remote work environment is that reviewers may sign off on transactions via email or by typing their initials on an electronic document. This can be risky, as virtually anyone can enter the reviewer's initials.

One solution is to use a digital signature platform, which requires the reviewer to enter a username and password. It also incorporates other protections to verify the signer's identity and otherwise ensure the integrity of the approval process.

REVIEW YOUR CONTROLS

These are just a few examples of how a changing work environment can affect a bank's internal control systems. The consequences aren't always obvious, so be sure to review your internal control policies and procedures and conduct a risk assessment to anticipate the full impact of contemplated changes. Also consider implementing or strengthening other types of controls — such as surprise audits, management or director oversight, mandatory vacations, job rotation, employee support programs and fraud training — to help compensate for a lack of segregation of duties and other internal control weaknesses. ■

BANK WIRE

CFPB ISSUES GUIDANCE ON UNAUTHORIZED EFTs

The Consumer Financial Protection Bureau (CFPB) has issued guidance — in the form of answers to FAQs — on unauthorized electronic fund transfers (EFTs). Here are some of the highlights:

- Unauthorized EFTs include situations in which a third party fraudulently induces a consumer into sharing account access information that's used to initiate an EFT from the consumer's account. And subsequent EFTs initiated using that information are *not* excluded from the definition of unauthorized EFTs as transfers initiated by "a person who was furnished the access device to the consumer's account by the consumer."
- Banks can't consider a consumer's negligence when determining liability for unauthorized EFTs under Regulation E.
- In determining whether an EFT was unauthorized and whether any liability protections apply, a bank can't rely on a consumer agreement that "includes a provision that modifies or waives certain protections granted by Regulation E, such as waiving Regulation E liability protections if a consumer has shared account information with a third party."

You can find the complete FAQs by visiting consumerfinance.gov and typing "EFT FAQs" in the search box. ■

FEDERAL RESERVE TOOL SIMPLIFIES CECL IMPLEMENTATION

For most community banks, the current expected credit loss (CECL) accounting standard will take effect in 2023, and many banks are concerned about the complexity involved in complying with the updated standard. In an effort to simplify the process, the Federal Reserve in July unveiled its Scaled CECL Allowance for Losses Estimator (SCALE), a spreadsheet-based tool that "draws on publicly available regulatory and industry data to aid community banks with assets of less than $1 billion in calculating their CECL allowances."

Your advisors can help you determine whether the SCALE is appropriate for your institution. For more information, visit supervisionoutreach.org/cecl. ■

OCC WILL RESCIND 2020 CRA RULE

In July, the OCC announced its intent to rescind its May 2020 final rule, which was designed to modernize and strengthen the regulatory framework for implementing the Community Reinvestment Act (CRA). Notably, neither the Federal Reserve nor the FDIC joined the OCC in advancing the final rule. In a statement, acting comptroller Michael Hsu said: "To ensure fairness in the face of persistent and rising inequality and changes in banking, the CRA must be strengthened and modernized." He went on to observe that "the disproportionate impacts of the pandemic on low- and moderate-income communities, the comments provided on the [Fed's] Advanced Notice of Proposed Rulemaking, and our experience with implementation of the 2020 rule have highlighted the criticality of strengthening the CRA jointly with the [Fed] and FDIC." ■

acxell ("acxell") has been meeting the specific risk management needs of community banks of all sizes since 1991. As a high quality and affordable alternative to other firms, acxell provides internal audit, regulatory compliance, BSA/AML, information technology, SOX/FDICIA and enterprise risk management review services and software. acxell is exclusively dedicated to the banking industry, providing clients with dedicated, focused and hand-held services reflective of a wide range of skills, experience and industry expertise. As a Firm, we have also been proactive in assisting our clients with the designing, implementation and testing of the internal control environment to assist management with the attestation requirement under the Sarbanes-Oxley Act.

acxell's uniqueness is characterized by its experienced staff and partners. Their hands-on involvement on each engagement provides our clients with a wide range of skills, experience and industry expertise. We employ the use of Subject Matter Experts — designated individuals performing audits in their specific field of expertise. The use of such professionals provides a unique value-added approach that is both efficient and productive.

We believe that a significant aspect of our services is our degree of involvement and responsibility to assist management by making suggestions for improvement, keeping them informed of professional developments and by acting as an independent counsel and sounding board on general business matters and new ideas.

We pride ourselves in our ability to provide effective and practical solutions that are commensurate with our clients' needs by emphasizing high-quality personalized service and attention. Our services are truly customized.

For **Solutions** *to your risk management needs, please contact our service coordinators at (877) 651-1700, or log-on to www.acxellrms.com to learn more.*

www.acxellrms.com

Headquarters:
646 US Highway 18
East Brunswick, NJ 08816

Offices:
New York, NY
Philadelphia, PA
Chicago, IL
Miami, FL