

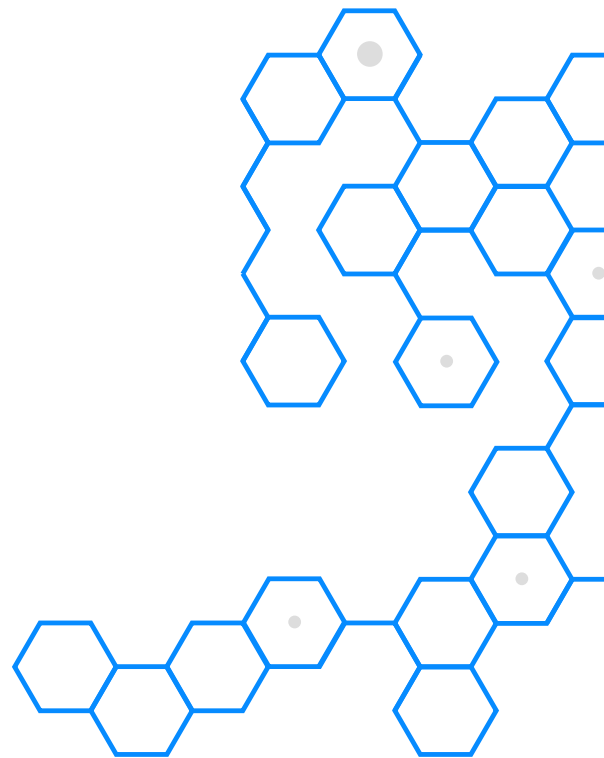
Enforcement Actions: Monitoring Trends, Regulatory Complexity, and Best Practices for Risk Management

Q4 2019

Enforcement Actions: Monitoring Trends and Methods for Improving Compliance Risk Management Practices

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How are financial compliance, risk and crime professionals tracking and monitoring enforcement actions?



Trends in Enforcement Action Monitoring

Regulatory compliance within the financial sector is more complex than ever. Already coping with a massive increase in regulations enacted since the Great Recession, financial institutions must prepare for more complexity, as a wave of new consumer privacy laws begin to take effect in 2020.

The 2010s were a chaotic, stressful decade for corporate compliance teams. Following the Great Recession of 2007-2009, the 2010s saw the enactment of new laws, such as Dodd-Frank; the creation of new regulatory bodies, such as the Consumer Financial Protection Bureau; and the globalization of compliance complexity, as regulatory bodies around the globe rushed to enact their own laws to protect against future meltdowns.

In 2018, the European Union (EU) implemented the General Data Protection Regulation (GDPR), which protects the data privacy of EU citizens. The law has triggered an avalanche of new data privacy regulations that will begin to take effect in 2020. The first to hit will be in California in 2020, but financial institutions must brace for much more complexity as a range of jurisdictions, from individual U.S. states to international regulatory bodies, enact their own consumer data privacy laws.

The California Consumer Protection Act (CCPA) is scheduled to take effect on January 1, 2020, although enforcement

won't begin in earnest until the middle of the year, giving compliance teams a brief window of time to adjust.

Smart organizations will use that window to catch up with the law, if they haven't already. The CCPA is aggressive in how it protects the private information of Californians. Even if your organization does not have so much as a single branch office in California, you may still be liable. If a single one of your customers resides in California, you must comply with the regulation. Moreover, the CCPA protects the privacy of California residents wherever they are in the world, not just in-state.

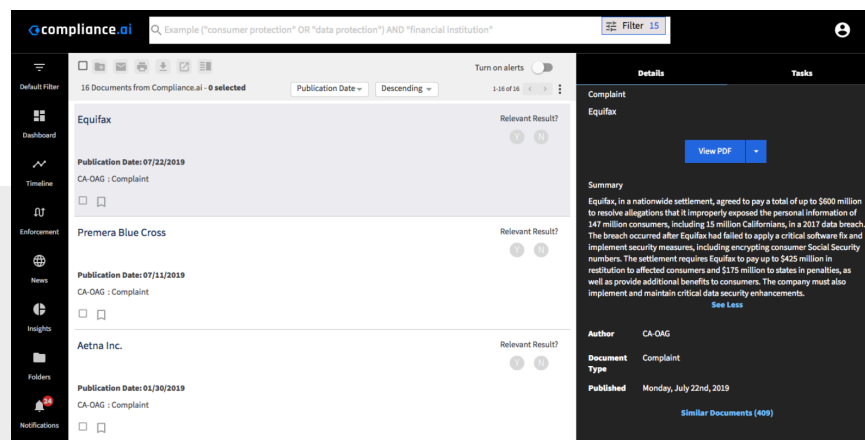
If you don't do business with Californians, you should still expect to face new consumer privacy laws wherever in the world you conduct your business. The EU's

GDPR already offers similar consumer privacy protections in the European Union, and a number of U.S. states, including Maine, Massachusetts and New York, are in the process of introducing their own laws.

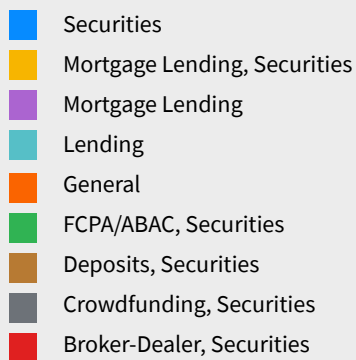
Following the Great Recession, the 2010s were a time of extreme regulatory churn. Governing bodies put extreme pressure on regulatory agencies to enhance supervision and regulations, resulting in new financial requirements and higher standards for risk management practices for institutions the world over.

In the 2020s, new consumer privacy laws could have an even bigger impact, since their effects are more far reaching. For instance, businesses must comply with CCPA, if they collect consumer data from any Californians.

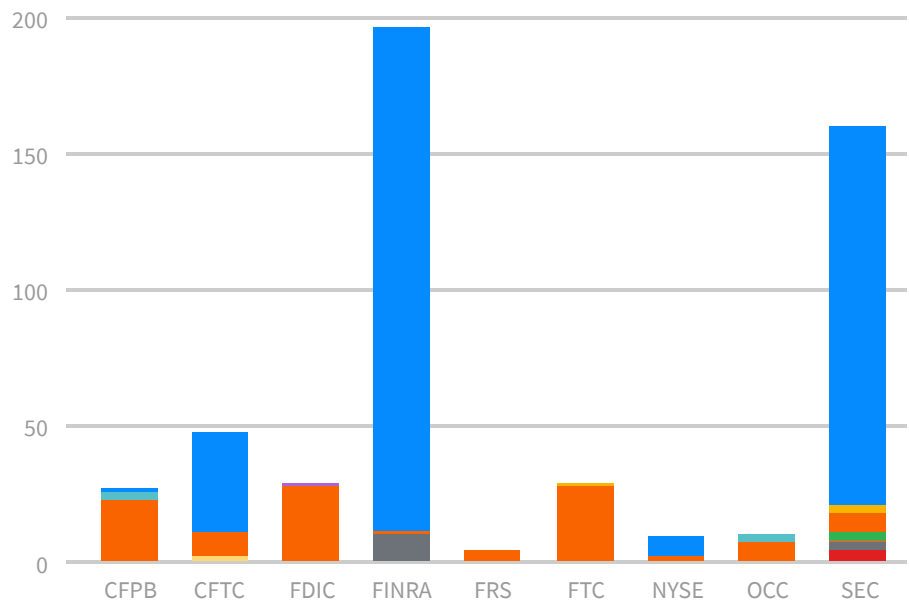
In 2020, we can expect exemplary enforcement actions being issued by CCPA and a possible tendency to settlements due to the fear of uncertainty to litigate previously unlitigated issues. Access to full coverage of California Privacy enforcements (pre-CCPA), can help shed light on future CCPA enforcements.



In the last quarter alone, we've reviewed 500 enforcement actions issued by U.S. federal regulators across various topics, including Securities, Mortgage Lending, FCPA/ABAC, Deposits, Crowd-funding, and Broker-dealer related topics.

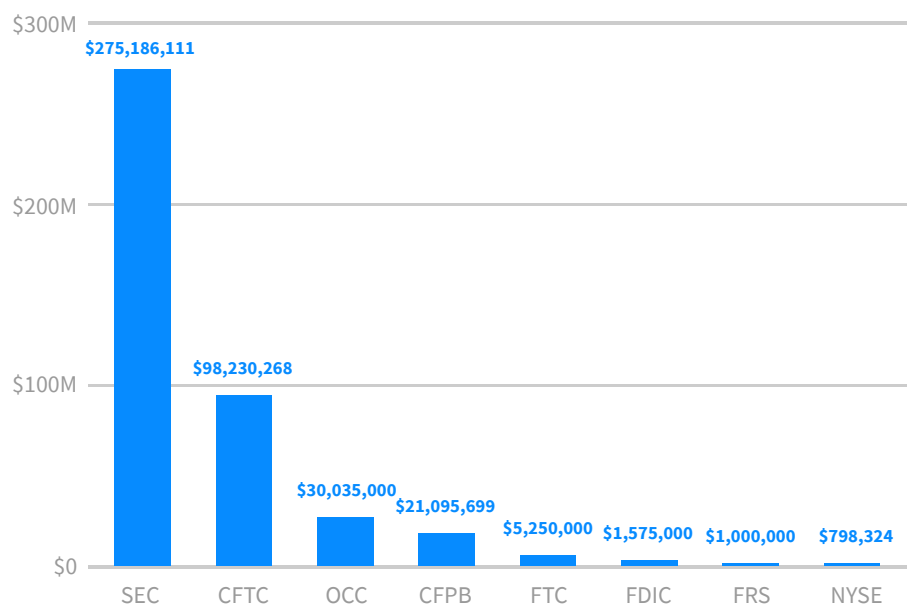


Q4 '19 Enforcement Actions by Topic (US Federal)



A total of over \$450M in monetary penalties were issued with the SEC handing down the lion's share of the penalties.

Q4 '19 Enforcement Actions & Penalties



Monitoring Enforcement Actions: a Time-Consuming, Manual, Error-Prone Process ... If You Don't Have the Right Tools

Ideally, financial institutions would have the time and resources to respond to every single regulation as soon as it is issued; however, this is not realistic... at least not with legacy compliance change management systems (CMS).

Developed before the Great Recession, legacy CMS tools were built as monolithic platforms intended to serve a broad horizontal market. They were designed for consultant-led initiatives and intended to be deployed in such varied sectors as financial services, insurance and health care. A side effect of this monolithic, consultant-led design is that the systems require manual workflows, which means that compliance teams must always play catch-up as regulations change.

Legacy CMS tools fall even further out of step when it comes to enforcement actions. Their monolithic design means that compliance officers tend to default to manual monitoring. They then track their results not in CMS but on spreadsheets.

Manual workflows result in a significant gap between real-time regulatory conditions and institutional responses. The lag-time is even greater with enforcement actions, yet it is business-critical for compliance departments to

proactively track them. Without an accurate view of enforcement actions, the financial institution's strategic planning and risk assessments for new products and services could be grossly misaligned with regulatory priorities. Tracking enforcement actions allows management to identify where regulators are concentrating attention and which compliance areas have been most problematic for the industry.

In a series of two surveys, Compliance.ai polled more than 100 financial compliance, risk and crime professionals at mid-sized to large financial institutions, nearly half of which were C-suite or executive level, to discover how organizations are tracking enforcement actions and how these methods are used to manage risk.

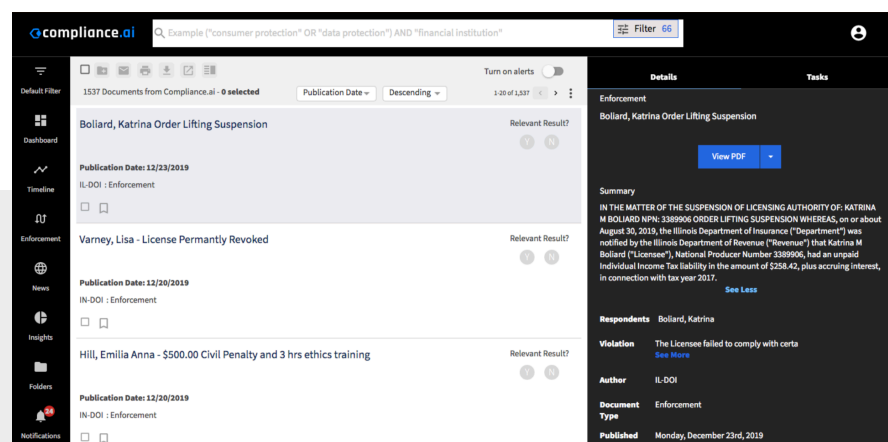
When asked how they track enforcement actions, more than 30% of all respondents reported using manual spreadsheets and/or folders to track enforcement actions, and another 22% stated that they do not yet have a formal process established for tracking enforcement actions.

Over 90% of survey participants stated they track enforcement activity from federal agencies, but when asked how they monitor federal or international enforcement actions, the majority of survey participants pointed to manual and informal processes in reviewing enforcement actions.

The problem with this "informal" approach is that as 2020 brings even more regulatory change, manual, ad-hoc processes will not scale, nor will they be an effective way to address the growing complexity of state, federal and global regulatory activity.

Of all the regulatory changes, enforcement actions are the most time consuming to track due to the wide variations across different jurisdictions. Making matters worse, not all jurisdictions (such as U.S. states) publish enforcement actions in a consistent format. And, enforcement actions issued by state agencies are often the ones that carry the most liability. Lack of compliance with state laws may result in monetary fines or even the revoking of your license to conduct business in the state.

*Compliance.ai has tracked more than 1,500 **State Enforcement actions in 2019** and has extracted key metadata from all of them, making them easy to track and analyze.*



To better understand compliance trends as we enter the 2020s, Compliance.ai conducted a follow-on survey to discover how compliance officers are preparing for this coming decade of global regulatory complexity.

The follow-on survey found that a major reason compliance teams at financial institutions have fallen behind the times is that monitoring enforcement actions is a costly, time-consuming endeavor. Well more than half (64%) of respondents reported spending more than 5 hours a week tracking enforcement actions, while a full fifth (20%) say they spend more than 15 hours a week monitoring enforcement actions.

It is no surprise that the hours stack up, since executives in varying roles, including those within compliance and risk departments, must all monitor trends in enforcement actions in order to accurately assess internal and external risks. A range of institutional leaders must keep up on not only the main regulations that impact their organizations, but they must also continuously review required action items, related violations cited, and the amount of penalties and/or fines issued when institutions fail to comply with them.

However, nearly 40% of survey respondents stated that any enforcement action information that is reviewed and analyzed is not disseminated or reported

to top management or the board of directors, with fewer than a third (30%) communicating this information through quarterly reports. Consequently, these organizations become vulnerable to not just new regulations, but also changing enforcement activities. These organizations tend to be slow to understand changing market trends and industry conditions that impact regulators' areas of emphasis, which exacerbates the already increasing trend of compliance risk management practices that fail to keep up with today's fast-changing regulatory environment.

Frequently, banks choose to manage the risk of enforcement actions on a cost-benefit basis. That is, when assessing the risk of penalties, they must first determine the likelihood of fines considering regulators' ever-changing priorities, and, second, decide whether it is economically justifiable to commit the additional resources needed to avoid enforcement actions. While banks want to do what is right, namely be in full compliance, as with any enterprise, trade-offs must be made.

"Compliance.ai uniquely provides banks the ability to strike a perfect median between the two options of either paying penalties or spending an enormous amount on compliance resources. Compliance.ai allows banks a cost-effective approach to avoiding fines and other regulatory actions and does so effectively and seamlessly."

Drake Ross, U.S. Treasury, Former Regulator at OCC, FDIC and OTS

Tracking enforcement actions across the industry is of utmost importance as it allows financial institutions to assess compliance risk within their own organizations. Deloitte Center for Financial Services reported:

*"Enforcement actions offer some of the most concrete evidence of risk management and compliance issues in the banking industry. In spite of being ex-post measures, they offer a clear view into the problems banking supervisors find in their bank examinations. Many of these issues are likely to be endogenous to particular institutions, where problems occur due to reasons unique to those entities. But in some instances, the number and types of EAs [Enforcement Actions] reflect market conditions and/or supervisory focus at a specific point in time."*¹

¹ The Deloitte Center for Financial Resources, Enforcement Actions in the Banking Industry: Trends and Lessons Learned https://www2.deloitte.com/content/dam/insights/us/articles/bank-enforcement-actions-trends-in-banking-industry/DUP1372_EnforcementActionsBanking_120815.pdf

Fear, Uncertainty and Doubt

Obscure Advances in Change Management

Once senior management and the board establish a formal review and evaluation of relevant enforcement activity, the organization will benefit from an enhanced understanding of possible exposure to new or growing compliance risk and will, therefore, be better able to allocate resources and priorities.

The Board and senior management should establish a consistent review and risk assessment process to determine if enforcement actions issued to other institutions apply to current and planned products, services and strategic initiatives. If they do, senior management must document and report those actions – particularly when expanding into new jurisdictions or introducing new products. The up-front cost of proactively limiting potential exposure to risk can provide significant savings to the institution in the long run.

Yet, while avoiding even a single negative enforcement action could pay for itself, a high percentage of respondents in our follow-on survey remain unaware of the rapid ROI that compliance teams can achieve by formalizing ad-hoc enforcement action monitoring and reporting processes and then automating them through modern RegTech.

Close to half (46%) of respondents cited cost as the biggest obstacle to integrating RegTech into their existing compliance monitoring processes, which runs counter to the rapid ROI modern RegTech is able to deliver.

In contrast to legacy CMS tools, which require massive upfront investments just to get started, RegTech solutions are delivered as a service. Thus, modern RegTech solutions limit both CAPEX and

OPEX expenditures, since RegTech solutions require no upfront investments in hardware or proprietary software, and they also move the expensive management, maintenance, and patching burdens off of the financial institution and over to the service provider.

This finding points to a troubling amount of disinformation in the compliance change management market. The reason isn't difficult to discern: legacy CMS vendors benefit from the confusion.

Facing eroding market shares as they support outdated product lines, legacy CMS vendors have flooded the market with Fear, Uncertainty and Doubt (FUD). They've thrown dirt at newer RegTech tools because disinformation is one of the few competitive tactics they have left.

Despite the fact that RegTech solutions were designed for specific industries (rather than for horizontal markets) and were developed to adapt to a complex, quickly changing regulatory environment, many compliance officers express a hesitancy to change. We believe that FUD from legacy CMS vendors is also confusing compliance teams about the amount of technical expertise needed to modernize compliance management.

Other legacy vendors, however, have seen the writing on the wall and instead of slinging arrows at newer technologies, they have simply slapped the term "RegTech" onto their own outdated products, creating even more confusion. The older CMS tools were designed for consultant-led initiatives, so even if the vendor slaps a "RegTech" label on them, these will still be manual, monolithic tools.

This practice – we call it "RegTech washing"² – sheds light on another head-scratching data point: More than a quarter (26.67%) of follow-on respondents said that their own lack of technical expertise prevented them from adopting RegTech tools.

This is an odd finding, since RegTech tools, as with most modern, best-in-class, cloud-based business tools, abstract complexity away from the end user. RegTech streamlines and simplifies compliance management processes, so even compliance teams with little-to-no technical expertise can begin benefiting the minute they turn the service on.

Disinformation in the market is also likely responsible for the fact that 13% of new respondents said that the biggest obstacle to RegTech adoption is that the tools are "not intuitive enough."

Again, when contrasted against legacy CMS tools, which were designed to be implemented by third-party experts trained in their intricacies, RegTech suites offer intuitive user interfaces that offer several set-it-and-forget-it features, such as automatic alerts and weekly summaries of relevant enforcement actions. RegTech suites also provide personalized dashboards, AI-powered insights, automatic reporting, workflow automation and more.

Best Practices for Regulatory Change Management

While tracking and analyzing enforcement actions is one element of an effective compliance risk management program, organizations must also establish other compliance management processes. Risk and compliance professionals and the board of directors must be proactive, keeping track of new guidance that prefaces future enforcement action trends.

Regulators have communicated that “an effective change management process detects new or amended rules and regulations, evaluates those rules, understands how the new requirements affect the bank’s processes and makes modifications as appropriate.”³

An ineffective change management system can expose a financial institution to increased compliance risk and lead to possible violations, enforcement actions or other penalties. Reputational risk is also often impacted negatively, resulting in potential operational losses and a need for additional marketing and public relations resources to maintain consumer confidence.

Moreover, regulatory agencies have already begun advocating for updated CMS technologies and processes. The U.S.

Treasury Department’s Office of the Comptroller of the Currency (OCC) now believes that a failure to integrate CMS into decision-making processes – a tall task with outdated, manual tools that lag far behind the real-time environment – can have wide-ranging negative consequences.

“The consequences may include missed business opportunities, losses, failure to comply with laws or regulations, or deficient practices (including those that are unsafe or unsound) that could lead to enforcement actions, including CMPs [Civil Money Penalties]” the OCC notes in its latest “Compliance Management Systems” handbook.⁴

To limit those risks, FINRA (Financial Industry Regulatory Authority) has found that industry early adopters have already begun migrating away from legacy CMS to modern tools. “As financial services firms seek to keep pace with regulatory compliance requirements, they are turning to new and innovative regulatory technology (RegTech) tools to assist them in meeting their obligations in an effective and efficient manner,” FINRA notes in its recent RegTech white paper.⁵

“Based on discussions held by FINRA staff with various broker-dealers and other participants in RegTech, surveillance and monitoring is an area where RegTech is gaining substantial traction. Market participants have indicated they are investing significant resources in this area, primarily in RegTech tools that seek to utilize cloud computing, big data analytics or AI / machine learning to obtain more accurate alerts and enhance compliance and supervisory staff efficiencies. Several market participants have noted significant reductions in false alerts generated by surveillance systems after utilizing RegTech tools,” FINRA reports.

What regulators don’t emphasize in their guidance about RegTech tools is that moving away from legacy CMS to modern RegTech often provides a competitive advantage to early adopters, who are now able to systematize, automate and customize their enforcement action monitoring and reporting processes.

² “Remember ‘Cloud Washing?’ It’s Happening in RegTech,” by Kayvan Alikhani, Forbes, October 14, 2019.

<https://www.forbes.com/sites/forbestechcouncil/2019/10/14/remember-cloud-washing-its-happening-in-regtech/#e36b61796cf3>

³ Allison Burns, Examiner, Federal Reserve Bank of Minneapolis, Managing Change Effectively

<https://www.minneapolisfed.org/publications/banking-in-the-ninth/managing-change-effectively>

⁴ Compliance Management Systems, Comptroller’s Handbook, Version 1.0, U.S. Treasury Department Office of the Comptroller of the Currency, June 2018.

<https://www.occ.gov/publications-and-resources/publications/comptrollers-handbook/files/compliance-mgmt-systems/index-compliance-management-systems.html>

⁵ Technology Based Innovations for Regulatory Compliance (“RegTech”) in the Securities Industry, FINRA, September 2018.

<https://www.finra.org/media-center/news-releases/2018/finra-releases-report-rise-regtech>

How Compliance.ai Empowers Compliance Teams

Monitoring, collecting and reporting data through manual or informal processes, such as spreadsheets and email, is prone to errors and omissions. Reports can be neglected due to other urgencies and objectives, or they can even be missed in the flood of other less-urgent emails. As a result, the business-critical information in the reports may not even get the attention of management.

Compliance.ai's RegTech suite empowers compliance professionals to proactively manage the growing volume and velocity of regulatory changes as they occur in real time, making it significantly easier to take proactive measures in order to remain compliant.

Compliance.ai's RegTech suite, delivered as SaaS, automatically provides transparent reporting to all stakeholders. Compliance.ai sifts through regulatory content across multiple jurisdictions and thousands of sources, so you don't have to. Compliance.ai then delivers focused

and timely information tailored to an organization's risk profile, which you can then customize further based on your own unique requirements.

Compliance.ai offers the most efficient way for financial institutions to automatically monitor, analyze, take action and report financial regulatory content. Other features include automatic, customized alerts, so you never miss important compliance deadlines; weekly summaries of enforcement actions, so you don't have to spend 5-15+ hours each week tracking each and every action individually; and summarized insights powered by our expert-in-the-loop AI,⁶ so you can make lightning-quick decisions based on the latest regulatory conditions.

To get an idea of how much modern RegTech can help you trim compliance costs, check out Compliance.ai's compliance change management cost-savings calculator: <https://www.compliance.ai/cost-calculator/>

Plug in a few details about your organization and your current compliance costs, and the calculator will give you a quick assessment of the ROI you should expect through RegTech modernization.

After all, as the 2020's add even more complexity to an already confusing regulatory landscape, you risk more than just fines if you run afoul of regulators. As a wave of new consumer privacy laws hit in the coming years, the risks run beyond the penalties that regulators may impose. Organizations that mishandle consumer data can spend years trying to repair their reputations and recapture market share.

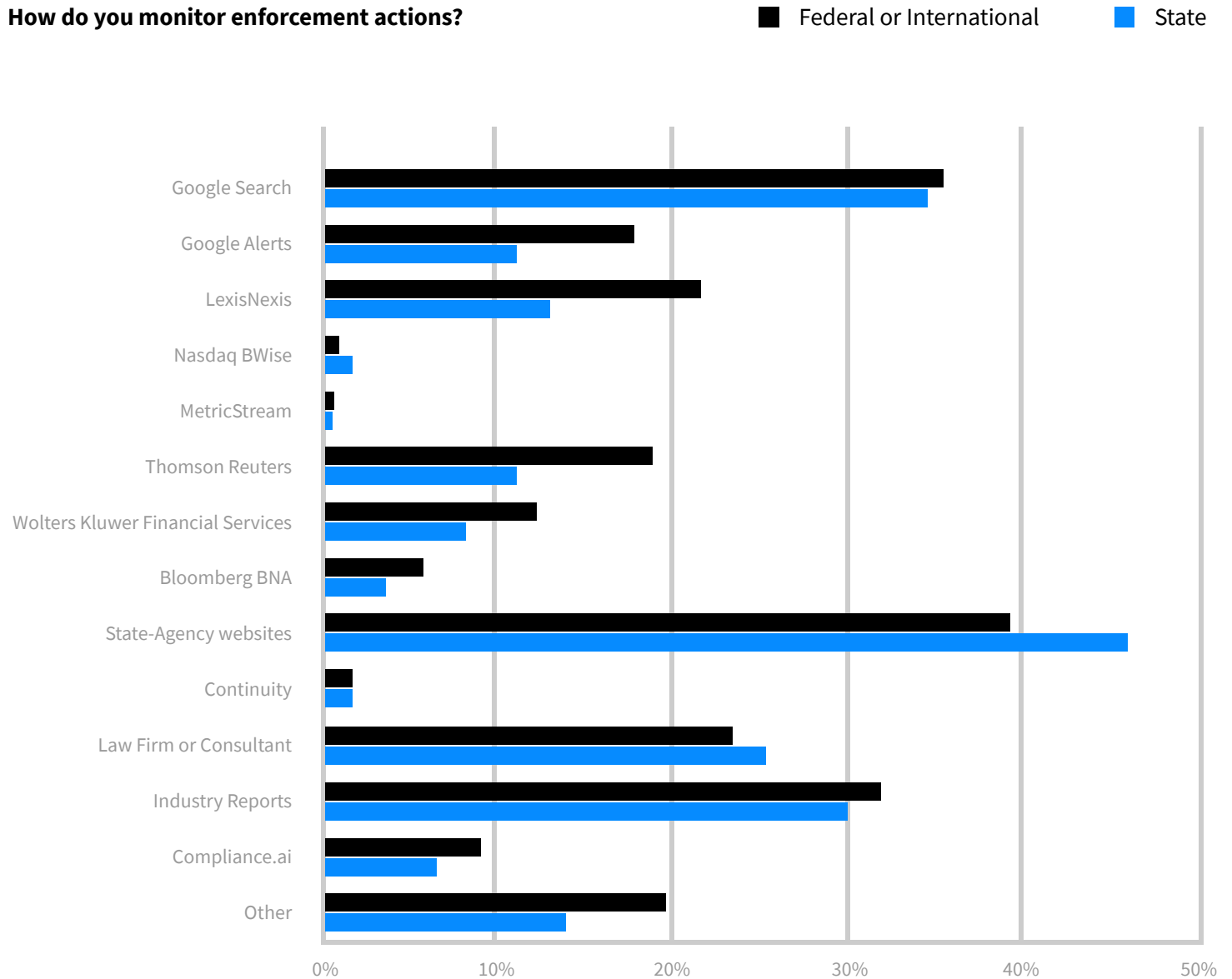
See how much you can save as you modernize compliance management, automate enforcement monitoring and reporting, and mitigate compliance risks: <https://www.compliance.ai/cost-calculator/>

⁶ "Why AI Needs Experts," by Kayvan Alikhani, Forbes, February 5, 2019. <https://www.forbes.com/sites/forbestechcouncil/2019/02/05/why-ai-needs-experts/#339455493360>

Survey Response Data

November 2019 | 122 Survey Participants

How do you monitor enforcement actions?



Survey Participant Profiles

What is your title? (choose the closest option)

Answer Choices	Responses
Auditor	3.74%
Chief Compliance Officer	19.63%
Risk Officer	3.74%
BSA/AML Officer	16.82%
Financial Crimes (Manager, Director, Consultant)	2.80%
Risk and Compliance (Manager, Director, Analyst)	11.21%
BSA/AML (Manager, Director, Analyst)	8.41%
General Counsel / Attorney	7.48%
Legal Specialist	3.74%
Compliance Officer	6.54%
Regulatory Compliance Manager	2.80%
Regulatory Compliance Consultant	5.61%
Other (please specify)	4.67%

Which jurisdiction(s) are important to you? (select all that apply)

Answer Choices	Responses
Federal-level	93.46%
State-level	76.64%
International	28.97%

What is the size of your Compliance and/or Risk Department?

Answer Choices	Responses
less than 5	33.64%
5-10	13.08%
11-20	8.41%
21 - 50	15.89%
more than 50	21.50%
n/a	7.48%

What is your organization's estimated total Assets Under Management (AUM)?

Answer Choices	Responses
Under \$100M	12.15%
\$100 to \$300M	6.54%
\$300M to \$5B	26.17%
\$5B to \$10B	6.54%
\$11B to \$50B	13.08%
More than \$50B	10.28%
N/A	25.23%

Current Methods, Topics and Interests

How do you currently keep track or record of relevant Enforcement Actions? (select all that apply)

Answer Choices	Responses
Spreadsheets/ Folders	28.97%
I rely on a 3rd party summary and/or analysis	35.51%
I do not need to keep track of or record Enforcement Actions.	11.21%
I do not currently keep track of, or record Enforcement Actions, but I would like to.	8.41%
I do not have a formal process established.	29.91%
I have a formal process established.	17.76%
Currently working on establishing a formal process	5.61%

Which aspect of the Enforcement Action do you pay attention to the most?

Answer Choices	Responses
Size of Penalty	43.93%
Regulatory Agency	63.55%
Type of Violations Cited	81.31%
Respondents	16.82%
Related Products or Industries	37.38%
Other (please specify)	2.80%

What patterns or trends would you like to learn from Enforcement Actions? (select all that apply)

Answer Choices	Responses
Size of Penalty Amount	47.66%
Volume of Enforcements by Regulatory Agency	52.34%
Type of Violation Cited	86.92%
Respondent Type	19.63%
Related Product or Industry	50.47%
Other (please specify)	1.87%

Which of the following topics are important to you? (select all that apply)

Answer Choices	Responses
Lending	57.01%
Leasing	6.54%
Commercial Banking	33.64%
Privacy / GDPR	48.60%
Cybersecurity	63.55%
Blockchain/ Cryptocurrency	22.43%
AML/BSA	77.57%
OFAC	65.42%
Insurance	13.08%
Securities	17.76%
Trust	10.28%
FCPA/ABAC	15.89%
Payments	40.19%
Deposits	43.93%
Other (please specify)	7.48%



Modern regulatory change management, made simple.

Resources:

[Enforcement Action Report](#)

[Enforcement Explorer Tool](#)

[Regulatory Activity Reports](#)

Schedule a demo to learn more about how Compliance.ai's modern regulatory change management solution can help your organizations compliance risk management program.

Visit: www.compliance.ai | Email Request: sales@compliance.ai

About Compliance.ai

Compliance.ai is transforming the way highly regulated organizations address compliance risk. Its regulatory change management solution empowers financial institutions to proactively manage the growing volume and velocity of regulatory changes as they occur, and makes it simple to implement the correct steps to remain in compliance. Compliance.ai delivers relevant content with personalized insights, obligation analysis, and risk assessment. With Compliance.ai, organizations can intelligently assess and mitigate their compliance risk, avoid regulatory sanctions and safeguard their corporate reputations—without increasing headcount.