LIABILITY ISSUES FOR COMPLIANCE OFFICERS
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Annual Seminar on Risk Management and Regulatory Examination/Compliance Issues
Affecting International Banks

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Compliance Officer Exposure to Personal Risk

“I’ve always felt strongly that you can’t only go after companies. Companies run through individuals, and individuals need to know that they’re at risk when they do bad things under the umbrella of a company.”

- Richard Cordray, Director of the CFPB in 2013

“Many of my colleagues are absolutely terrified.”

- Bob Werner, global head of financial crime compliance at HSBC and former head of FinCEN

- June 2015 – The SEC charged the chief compliance officer of Blackrock with breaches of the Investment Advisers Act for allegedly failing to implement certain compliance policies and procedures
  - The SEC fined the chief compliance officer $60,000 and Blackrock $12 million

- May 2015 – BNP Paribas paid $9 billion in penalties for sanctions offenses. BNP admitted it “knowingly and willfully” moved $8.8 billion through the US financial system on behalf of Sudanese, Iranian, and Cuban entities
  - News accounts report compliance officer concerns routinely dismissed
  - The chief compliance officer retired in August 2014 prior to the penalty

- December 2014 – FinCEN fined the chief compliance officer of MoneyGram $1 million for allegedly not ensuring MoneyGram followed AML laws
  - MoneyGram settled with the DOJ for $100 million in 2012
Personal Risk: “Do the Right Thing. Then Get Fired”*

- In May 2012, the New York Court of Appeals dismissed a suit where a former compliance officer alleged he was fired for uncovering potential improper stock trades in the CEO’s family accounts
  - Joseph Sullivan had served as an EVP, Treasurer, Secretary, COO, and Chief Compliance Officer at Peconic Partners. He was fired in 2008
- The court ruled that Sullivan was an “at-will” employee, and was not protected just because he was a compliance officer
- Chief Judge Jonathan Lippman dissented from the majority opinion:
  - “The message that will be taken from the majority’s decision is self evident: if compliance officers (and others similarly situated) wish to keep their jobs, they should keep their heads down and ignore good-faith suspicions or evidence they may have that their employers have engaged in illegal and unethical behavior, even where such violations could cause or have caused staggering losses to their employers’ clients”

Heightened Regulatory Focus on Personal Misconduct

“Corporations can only commit crimes through flesh-and-blood people. It’s only fair that the people who are responsible for committing those crimes be held accountable. The public needs to have confidence that there is one system of justice and it applies equally regardless of whether that crime occurs on a street corner or in a boardroom.”

- Sally Yates, Deputy Attorney General, from Interview in NYT on September 9, 2015

- Renewed regulatory and enforcement focus on holding bank employees and directors responsible for Bank Compliance failures
- A September 9, 2015 memorandum issued by Deputy Attorney General Sally Yates states that companies will no longer be given credit for cooperation if they do not provide requested information on individuals responsible for bank misconduct:
  - To qualify for cooperation credit, corporations must provide all relevant facts relating to the individuals responsible
  - Absent extraordinary circumstances or approved DOJ policy, culpable individuals not released from civil or criminal liability when resolving a matter with a corporation
  - DOJ attorneys should not resolve matters with a corporation without a clear plan to resolve related individual cases, and should memorialize any declinations as to individuals in such cases
  - Civil attorneys should consistently focus on individuals as well as the company
Role of the Compliance Officer: Factors for Survival (and Success)

- Factors for Survival (and Success):
  - Clear reporting lines and escalation procedures
  - Role and stature
  - Culture/tone at the top
  - Support from headquarters
  - Partnership with business lines

“Bummer of a birthmark, Hal.”
Factor for Success: Reporting Line Within Organization

Statistics from a recent survey conducted by Promontory show that of eighteen large US-based banks, only three, or 17%, have the Compliance function reporting into the Legal function or general counsel’s office.

- Should the general counsel act as the chief compliance officer?
  Should the Compliance department report into Legal?
  Should the functions be separate?
    - No hard-and-fast rule
    - Trend in the US: moving away from embedding Compliance within Legal
    - Legal and Compliance play distinct roles. Compliance should be part of the strategic planning, risk management, and corporate culture, whereas Legal focuses on interpretation and protecting the organization
    - Compliance officers particularly focused on evaluating risks associated with laws and regulations; providing guidance; monitoring, reporting, and testing

- If Compliance does report through Legal, both functions should be conscious of their respective roles
  - Coordination with risk function still crucial

- Headquarters organization structure may dictate reporting lines within regions
Factor for Success: Coordination of Three Lines of Defense

- To be effective, Compliance and Audit should coordinate rather than duplicate efforts
  - Both Audit and Compliance assess compliance risks, but serve different purposes
  - Siloed functions increase likelihood of disagreement on magnitude and nature of risks
- Both Compliance and Audit evaluate the effectiveness of controls in place; however, Compliance must work with the business lines to remediate deficiencies
- Compliance should consider segregating the testing function from the advisory function
Factor for Success: Oversight, Stature, Support

• The chief compliance officer provides oversight but ultimately does not own the actual compliance

• Support from the higher ups: staffing and budget
  – Ensure escalation procedures clearly define processes and accountable parties when breaches occur
  – Challenge: Lost in translation – ‘Mother ship’ support or understanding of US regulatory environment, different (and higher) US compliance standards

• Empowered second line – make sure Compliance can assert itself
Dos for Compliance Officers

• What makes a successful compliance officer?
  – Job One: provides *enterprise* view of compliance risk
  – Looks for solutions and recommendations
  – Oversees but does not own compliance activities
  – Encourages work cultures that uphold the importance of compliance
    • Chief compliance officers must be empowered to escalate issues and potential violations to senior levels
  – Empowered to push for changes before regulators identify issues
  – Casts a wide net in discovering areas of risk (e.g., social media, complaints to identify the trends)
  – Spends time with businesses, rather than just auditing and reviewing
  – Supports the businesses in fixing problems and building controls
Dos for Compliance Officers, cont’d.

• Practical advice:
  – Segregate the testing from the advice functions
  – Coordinate with Audit and the first line for coverage and timing
  – Self-evaluate the compliance program as a whole
  – Ensure defined escalation procedures – *that are actually followed*
  – Utilize risk assessments to properly allocate time/oversight
  – Analyze and correlate complaints to identify root cause and overall behavioral issues in conjunction with risk assessments
Don'ts for Compliance Officers

• What makes an unsuccessful compliance officer?
  – Only identifies problems, not solutions
  – Only audits and reviews businesses, rather than partners
  – Acts with a “gotcha” mentality
  – Fails to build relationships with the business leaders; acts siloed
  – Fails to coordinate with Audit to ensure coverage and remediation
  – Acts constantly with an alarmist attitude or is adversarial
  – Underestimates regulatory expectations
  – Fails to implement sufficient MIS/reporting lines
Successful vs. Unsuccessful Behaviors of Compliance Officers

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<th>Successful Chief Compliance Officers</th>
<th>Unsuccessful Chief Compliance Officers</th>
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<td>• Ability to get the business lines to buy in that they own the risks</td>
<td>• Acting as an adversary</td>
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<td>• The chief compliance officer acted as a partner to the businesses but effectively communicated that he/she did not own the risk as the chief compliance officer</td>
<td>• The chief compliance officer alienated the business lines and antagonized his/her peers, although he/she had the expertise to be an effective officer</td>
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<td>• He/she stressed the business has to identify risks, controls, and take ownership, and he/she would be their partner in doing so</td>
<td>• He/she created a culture where the businesses lines did not own the risks and did not partner with the chief compliance officer to take ownership</td>
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• The successful chief compliance officer looked for solutions; the failed chief compliance officer only tried to identify problems

• The chief compliance officer’s success or failure depends on his/her ability to work with the businesses. In order to be effective, the chief compliance officer:
  • Cannot be seen as the enemy; rather must be viewed as working to keep the business within the risk tolerance of the institution
  • Must build alliances with the businesses so they see the chief compliance officer as enabling their success, rather than blocking business
CFPB Expectations on Compliance Management Systems

• According to its Supervision and Examination Manual, “the CFPB expects every regulated entity under its supervision and enforcement authority to have an **effective compliance management system** adapted to its business strategy and operations”
  – Active oversight of a company’s compliance management activities by its board of directors and management
  – The establishment of a robust compliance program, led by a qualified and experienced chief compliance officer, to set compliance policies and procedures covering all product and service lifecycles, to monitor the company’s business units for and to correct compliance weaknesses, and to train the company’s directors, managers, and employees about their compliance responsibilities
  – The establishment of a system for logging, tracking, and promptly investigating and responding to consumer complaints and for taking both individualized and systemic corrective actions in response to such complaints, as appropriate
  – A periodic independent audit of the company’s compliance with consumer financial laws and adherence to internal policies and procedures

**Regulators are looking for the chief compliance officer to be the internal advocate for consumers within the institution**
Sources


Questions?
About Promontory

• Promontory Financial Group, LLC is a premier strategy, risk management, and regulatory compliance consulting firm focusing primarily on the financial services industry.

• Founded by Eugene Ludwig in 2001, after having served as U.S. Comptroller of the Currency.

• Promontory has nineteen offices in thirteen countries spanning North America, Europe, Asia, Australia, and the Middle East. It has a team of over 500 highly experienced and specialized professionals who support both the in-country and global needs of our clients.

• Many of our professionals have served as senior executives of leading financial institutions, others as senior government officials at the Board of Governors of the Federal Reserve System, the U.S. Department of the Treasury, the Federal Reserve Bank of New York, the Office of the Comptroller of the Currency, the Federal Deposit Insurance Corporation, the Securities and Exchange Commission, as well as the U.K.’s Financial Services Authority, the Bank of England, and various European, Asian and other regulators.

• Our clients include both financial and non-financial firms, governments, and regulatory organizations.
Managing Director, Promontory Financial Group

Peter assists clients in addressing challenging regulatory enforcement and public policy issues. Much of Peter’s practice draws on his extensive international background and experience. His areas of focus include compliance, corporate governance and controls, risk culture and management, internal investigations and forensic reviews, asset/liability management, liquidity planning, and regulatory intelligence. He advises clients on the full range of compliance issues related to anti-money laundering and Bank Secrecy Act provisions, in addition to due diligence, examination, and enforcement remediation. Peter has deep experience in assisting clients with remediation efforts resulting from regulatory enforcement actions and has served as a senior advisor in that capacity to both boards of directors and senior management.

Peter’s career has included service at senior levels of government and roles that focus on the intersection of public policy and finance. In his public service, Peter worked for more than 10 years in senior positions at the Department of State, the United States Trade Representative, and the National Security Council staff (White House), including as Executive Assistant to the National Security Advisor. He has also served as Deputy Assistant Secretary of State for Energy, Sanctions and Commodities, where he was responsible for economic sanctions policy in cooperation with the Department of the Treasury. Immediately prior to joining Promontory, Peter was a vice president at Goldman Sachs & Co., where he was responsible for international policy and regulatory matters. He also served as chief of staff to the firm’s President and Co-Chief Operating Officer.

Peter holds a J.D. from Yale Law School and an A.B. degree from Princeton University. He is a life member of the Council on Foreign Relations; a trustee of Freedom House; director and treasurer of the American Ditchley Foundation; and a director of the Atlantic Council.