



Banking in the Ninth

March 2014

Ninth District Highlights

Role of Relationship Staff in Banking Supervision

This issue of *Banking in the Ninth* focuses on key employees responsible for the supervisory relationship between the Minneapolis Fed and the banks and holding companies we supervise. A relationship-focused supervisory position may seem out of place. Firms typically have relationship functions to maintain effective connections with customers for the ultimate purpose of meeting profitability and sales goals.

Of course, supervisors do not make sales or earn profits. But building a deep and constructive relationship with the institutions we supervise is entirely appropriate. Establishing an effective relationship with supervised institutions helps us achieve our primary objective: effectively supervising banks and holding companies.

This quarter's article provides a number of examples showing how strong relationships lead to better supervision. One example makes this point clear: Getting to know a bank or holding company well—especially the economy in which the firm operates and the strategy it pursues—typically leads to a strong relationship with firm management.

This same knowledge also leads to better supervision, because the relationship manager or Consumer Affairs contact has a stronger understanding of potential risks that could affect the firm.



Ron Feldman

Therefore, I do not see a conflict between effective supervision and strong relationships between supervisors and banks and holding companies. Rather I see strong relationships facilitating effective supervision. That said, I understand that some people may initially see tension between the two. A strong relationship between the supervisor and the supervised firm may indicate one where the firm “gets off easy.”

Continued inside

SAFETY and SOUNDNESS and CONSUMER AFFAIRS UPDATE

The Role of the Relationship Managers and Consumer Affairs Contacts

Understanding and responding to the unique and local operations of state member banks and bank holding companies and maintaining effective communication with firm management is central to Minneapolis Fed supervision. Relationship Managers (RMs) and Consumer Affairs Contacts (CACs) are critical to achieving

these objectives. These two positions also ensure continuity between examinations and allow for timely exchanges of information with institutions as conditions change. Finally, by providing designated contacts for each institution and assigning responsibility to individuals for maintaining knowledge of each institution's operations,

they eliminate the need for multiple requests for similar information.

Because of the centrality of these roles to our supervision and because we receive questions about the roles, we devote our main article of this newsletter to describing the overall role for these two positions and their day-to-day activities.

Continued inside

SAFETY and SOUNDNESS UPDATE continued

Main Roles: RMs and CACs are primary points of contact and resources for state member banks (and their parent bank holding companies) and large community holding companies in the Ninth District.¹ Each state member bank and large community holding company is assigned an RM and a CAC. The RM is a supervisory examiner responsible for monitoring safety and soundness matters at the assigned institutions. Similarly, the CAC is responsible for monitoring compliance and Community Reinvestment Act (CRA) matters. While the roles are slightly different, the responsibilities are similar. The primary responsibilities of the RM and the CAC are to develop and maintain strong working relationships with supervised institutions; provide effective supervision and risk identification; quickly analyze and respond to identified risks; maintain an understanding of the institution's strategies, operations, and environment; act as a resource for institution management; and facilitate communication between key stakeholders. When RMs and CACs are effective in their roles, the regulatory burden faced by the institution should be less than would be the case without an RM or a CAC assigned.

Day-to-Day Activities: The RM is responsible for developing and ensuring implementation of the safety and soundness supervisory strategy for each assigned institution based on the institution's unique risk profile. In order to be effective, the RM must maintain a solid understanding of each institution and the unique factors that impact its risk profile. This requires periodic contact with senior management and in-depth analysis of regulatory reports. As the RM becomes more familiar with the institution and management, the frequency of contact is typically tailored to meet the supervisory objectives of the Reserve Bank as well as the desires of management.

As with RMs, CACs tailor their activities to the complexity and risk of each supervised institution. CACs conduct monitoring activities, stay informed about developments at the institution, and provide post-examination support. CACs who are responsible for larger,

more complex institutions will also develop a supervisory strategy tailored to the risks of the assigned institution, conduct target examinations, and have frequent and ongoing communication with their assigned institutions.

A Central Contact

RMs and CACs are each assigned a relatively small number of institutions, which allows them to focus on each of these entities and become familiar with the management, business strategy, financial condition, local economy, and compliance-related risks. In addition to serving as a contact for bank management, RMs and CACs serve as a resource for each other as well as other stakeholders, including the staff of the Board of Governors, state and federal regulatory agencies, and Reserve Bank Applications, Statistics, and Credit divisions. This approach often helps limit the need for multiple parties to contact the bank for information. Similarly, the CAC or the RM can assist the banker or bank owner in working with Applications or other Reserve Bank supervision functions by providing background information or by explaining information needs to bank management. The RM and the CAC also have access to a variety of resources within the Reserve Bank and the Federal Reserve System to assist bankers with institution-specific questions, including the specialized, extensive knowledge found with SRC's Risk Group.

Dedicated Resources

The RM is dedicated solely to the ongoing supervision of the assigned institutions. Because RMs travel infrequently, they are generally available to the institutions and Reserve Bank management and can quickly respond to questions and concerns. When an event occurs that may impact regulatory oversight, the RM can quickly analyze the situation, recommend a course of action, and communicate any potential change or resolution to all affected parties. The RMs are available for questions from all institution staff members or directors, not just the chief executive officer or president.

The CAC functions in much the same

way as the RM for the larger, complex, or higher compliance risk profile state member banks. For these entities, the CAC is generally available to respond to questions from the institution, monitors compliance developments, and responds to new situations. For institutions with a lower compliance risk profile, the CAC often works with the Consumer Affairs Hotline (staffed with a dedicated examiner) to provide effective responses to questions received. The CACs also provide input into the supervisory strategy for the institution based on their knowledge of the institution's practices and overall compliance risk profile.

Maintaining Continuity

An important responsibility of the RM and the CAC is to ensure continuity of the supervisory approach at each assigned institution. This responsibility is met through ongoing supervisory contacts detailed previously, but is also important in the context of examinations. In order to maintain a degree of independence and separation of duties in the safety and soundness supervision function, RMs do not serve as the examiner-in-charge (EIC) at safety and soundness examinations and may play only a limited role in the on-site examination. The EIC and examination team conduct the examination, develop the findings, and are responsible for examination conclusions. The RM provides important information to the EIC as part of the scoping process and through ongoing conversations during the examination. RMs are also key players in the post-examination vetting and review processes. These conversations ensure that the examination team has access to information about the bank and its operating environment prior to the examination and that there is continuity in the approach to issues between examinations.

CACs are also responsible for ensuring continuity of the supervisory approach, though they accomplish this mission in a different way than the RM. Because of the nature of compliance examinations and the longer duration between full-scope compliance examinations, CACs are likely to play a more central role in examina-

tions, including sometimes serving as EIC. For banks subject to a more continuous supervision strategy (i.e., subject to periodic target examinations), the CAC is typically the EIC for the target examinations. In addition to being on examinations, CACs monitor developments between examinations and frequently participate in mid-cycle monitoring events.

An Efficient, Routine Support for Banks/BHCs

Although many financial institutions provide similar services, state member banks and large community holding companies to which RMs and CACs are assigned are not all the same. Some offer unique products and services while others stick with traditional community banking products. Some have devised strategies to remain independent; others have determined they need to grow. Each institution has a unique story. Having an RM and a CAC who

know that story helps shape and maintain the supervisory strategy and reduces the need for the banker or owner to explain themselves repeatedly to Reserve Bank supervisory staff. It enables the Reserve Bank to monitor and respond to changes at the institution, whether bank or regulatory driven, in a timely way. The RM also helps ensure consistency among responses and communications.

A unique element of the RM program is its regional focus. Each RM has assigned institutions within a defined territory, usually individual states. As such, the RM is expected to maintain an increased level of knowledge about specific economic conditions, competition, and state law, and can provide that contextual information to examiners or others within the Reserve Bank's supervision division. The regional focus also allows for consistent communication with state supervisors.

A Proactive Approach

The continued communication between the RM, the CAC, and the institutions provides a conduit for updates on key risks, hot topics, or issues affecting the region or a specific economic area. This relationship is particularly helpful in today's changing regulatory environment. RMs and CACs proactively share information that may affect an institution's safety and soundness or compliance risk profile. CACs notify Reserve Bank management when compliance- or CRA-related issues appear to warrant accelerating an examination or conducting a supervisory visit, advisory visit, or other outreach activity. This allows the Reserve Bank to proactively address emerging risks and hopefully prevent serious violations or other issues from occurring.

¹ Large community holding companies are those with consolidated assets between \$1 billion and \$10 billion.

Ninth District Highlights continued

We avoid this concern through several straightforward steps. First, the direct supervision of the firm is facilitated by the relationship staff, but not controlled by it. Second, and, most importantly, supervisory assessments receive multiple reviews by parties that are one step removed from the direct supervision of the firm. Both the Fed and supervised firms benefit from this combination of strong relationship and independent oversight.

A separate challenge is assessing our performance as supervisors on an ongoing basis so that we identify how we can improve our relationship function and our supervision more generally. I noted that supervisors do not make sales or tally profits. Society certainly does not want government supervisors selling their services to the highest bidder. Profits, however, do provide a concrete metric, one that supervisors often lack in assessing their performance.

One concrete measure of assessing our performance is the feedback we receive from supervised entities. I encourage readers to contact me with comments on this issue of *Banking in the Ninth* or any other matter on your mind.

—Ron Feldman
Executive Vice President, SRC

Consumer Affairs Assistance Hotline

The article *The Roles of Relationship Managers and Consumer Affairs Contacts* references our Consumer Affairs hotline, a feature of Federal Reserve Bank consumer supervision mentioned in many *Banking in the Ninth* articles. In this article, we provide a few more details on this hotline.

The Consumer Affairs section within Supervision, Regulation, and Credit offers state member banks a dedicated telephone number to use for compliance questions and concerns. The hotline is monitored by Consumer Affairs staff daily. We provide a timely response to these questions, typically no later than a day.

The hotline report-and-respond process is as one would expect: Typically, a bank employee will leave a voice mail message briefly outlining his/her question. Examiners in the office assigned to monitor and respond to the questions review the message. Examiners then contact the bank to obtain additional information about the specific question or fact pattern.

Call volumes vary; however, we typically see

an increase when new rules and regulations are issued. For example, we received many calls concerning the new mortgage rules in Regulations Z and X. Bankers asked for additional details surrounding documentation they must keep to support their assessment of a borrower's ability to repay under the new regulation. We have also received questions about the small servicer exemptions, qualified mortgages, and rules for escrow accounts.

In addition to questions about new rules, examiners staffing the Consumer Affairs assistance hotline work with bankers on reviewing updated disclosures or questions about aspects of a bank's compliance management program. Finally, we receive heavier call volume in February when compliance officers prepare HMDA data for the March 1 reporting deadline.

We use the information from these calls to reduce examination burden. In particular, the final information provided to the state member bank is documented and shared with the bank's Consumer Affairs Contact and, if appropriate,

the Safety and Soundness relationship manager. This process benefits the bank by ensuring examiners on site or involved in off-site monitoring of the bank are aware of the prior discussion and findings. As a result, they will not need to revisit the issue unless circumstances have changed.

In addition to documenting individual calls, examiners have recently begun compiling a database of questions. We will use trends in calls to offer training and education to bankers. This development fits with our approach to reduce later violations by equipping banks to comply with rules and regulations in advance. For example, some of the articles previously published in *Banking in the Ninth* aimed to answer the common questions we have received on the assistance line for a broad audience.

If you are a state member bank compliance officer and need our assistance, please feel free to call 612-204-6500 or 800-553-9565 and ask for the Consumer Affairs assistance hotline to be connected to the Consumer Affairs assistance voice mail.