

THE BANKERS' BULLETIN

Regulatory & Enforcement Insights on Recent Bank Industry Developments

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OCC Semiannual Risk Report Identifies Key Risks in the Banking System

- The OCC beats the drum on proactive risk assessments and sound risk management practices.
- Increased risks from digitalization, new products, fintech partnerships, and AI permeate the report.

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FinCEN Issues Final Rule on Access to Beneficial Ownership Info Database

- The rule permits banks to use BOI to fulfill a broader range of their obligations (suspicious activity monitoring/reporting, sanctions screening), but doesn't resolve remaining CDD Rule compliance questions.

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CFPB Imposes Consent Order and Civil Money Penalty for Overdraft Practices

- The action reinforces the CFPB's focus on overdraft practices and demonstrates a willingness to take enforcement action in an area that has received special attention from Director Chopra.

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OCC Issues Guidance on 'Buy Now, Pay Later' Loans

- Banks are put on notice of the relevant risks from these products, especially regarding credit, consumer compliance, and third-party oversight. To offer BNPL loans, tailoring of existing processes is key.

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SCOTUS Hears Oral Argument That Could Affect Bank Agency Enforcement

- Federal regulators' enforcement procedures could be significantly impacted if SCOTUS objects to the administrative process. The final decision from the Court warrants close monitoring.

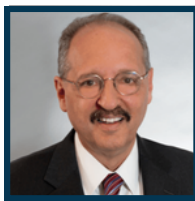
About The Firm

Luse Gorman, PC is a Washington, D.C.-based law firm specializing in mergers, capital raising transactions, regulatory, enforcement, corporate, securities, employee benefits, executive compensation, and tax law for regional and community banks across the United States. Our attorneys have served with the major federal banking and securities agencies, and regularly engage with regulators on a range of novel and complex legal issues.



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Please reach out to any of our regulatory and enforcement attorneys above, or to your primary Luse Gorman contact, if you have any questions related to the topics covered in this edition of *The Banker's Bulletin*.

Summary. On Dec. 7, the OCC published its Fall 2023 Semiannual Risk Perspective, identifying the key risks facing the federal banking system.

Takeaways.

- AI is singled out as an emerging risk, and adoption of AI poses privacy, cybersecurity, third-party, and consumer protection concerns in particular. The OCC will apply existing guidance and principles to banks' use of AI, even if they do not explicitly cover AI.
- The OCC continues to focus on credit quality metrics for CRE and highlights risks in the office market, in both urban and suburban areas, as remote work persists.
- Effective and regular stress testing and sensitivity analyses of deposit assumptions will be vitally important to ascertain true interest rate risk, liquidity risk profiles, and funding costs.
- Cybersecurity risk heads the list of operational risks. The OCC is pushing for the adoption of heightened threat and vulnerability monitoring processes and security measures.
- Effective, specialized oversight of third-party relationships is needed as complexity increases.

Bottom Line. Expect to see these topics become focus areas in the next few cycles. This report is a preview of the agency's exam priorities. Get ahead by assessing these risks.

OCC Semiannual Risk Report Identifies Key Risks in the Banking System



FinCEN Issues Final Rule on Access to Beneficial Ownership Info Database



Summary. On Dec. 21, FinCEN issued its final rule regarding access to beneficial ownership information (BOI), the second of three rulemakings implementing the Corporate Transparency Act. The rule outlines how entities, organizations, and agencies, including banks, can receive the BOI submitted by companies into FinCEN's newly-created BOI database.

Takeaways.

- In a major change from the proposed rule, banks will be permitted to use BOI to comply with a broader range of AML and OFAC obligations, including customer identification, enhanced due diligence, suspicious activity monitoring, SAR filing, and sanctions screening.
- Before obtaining BOI, banks will need to adopt specific procedures related to the handling and dissemination of such information. Personnel will need to be specially trained on the rule.
- The bank agencies stated they don't have an expectation that banks access BOI from FinCEN. So the rule on its own does not require changes to comply with pre-existing requirements.

Bottom Line. FinCEN isn't done. The third rule will modify the existing CDD Rule, which will significantly impact existing BSA/AML programs and compliance requirements for banks.

Summary. On Dec. 7, the CFPB issued a consent order requiring \$5MM in customer redress as well as a civil money penalty of \$1.2MM against Atlantic Union Bank for Regulation E and UDAP violations related to its overdraft programs.

Takeaways.

- Rather than focusing on the *charging* of overdraft fees, the CFPB took aim at the surrounding Bank practices related to disclosing the program terms and obtaining customer consent.
- The consent order requires the Bank to send detailed notices to affected customers, a significant cost over and above the amount put aside to redress the alleged harm to customers.
- The Bank's entire compliance framework around overdraft practices will need an overhaul.
- The order should be read as a blueprint for the CFPB's supervisory expectations around disclosure, training, and monitoring, if a bank wants to continue to offer overdraft programs.

Bottom Line. Director Chopra has targeted so-called "junk fees," including overdrafts, using a variety of tools in the CFPB's arsenal. This action is a warning to the industry that the Bureau will use its enforcement authority to try to rein in practices at banks that have not already voluntarily modified their procedures.

CFPB Imposes Consent Order and Civil Money Penalty for Overdraft Practices



OCC Issues Guidance on ‘Buy Now, Pay Later’ Loans



Summary. On Dec. 6, the OCC issued Bulletin 2023-37, Retail Lending: Risk Management of ‘Buy Now, Pay Later’ Lending, providing guidance to banks for effectively managing the risks associated with BNPL lending. The Bulletin highlights the various risks BNPL lending carries for banks.

Takeaways.

- The OCC clearly establishes its view that a bank’s relationship with a merchant or third-party BNPL provider is subject to recent interagency guidance on third-party risk management. If you partner with BNPL providers, they should be covered by your TPRM program.
- The OCC expects BNPL lending to be integrated into a bank’s larger planning and risk management architecture, including its strategic plan and risk appetite, as well as its CMS, monitoring, reporting, stress testing procedures.

Bottom Line. While the OCC’s expectation for integration is familiar, BNPL loans’ unique features and risks must be considered as the product is integrated into existing frameworks. A one-size-fits-all approach borrowed from other products will not cut it for BNPL loans.

Summary. On Nov. 29, the Supreme Court heard oral arguments in *SEC v. Jarkesy*, a case challenging the SEC’s use of its in-house administrative procedures to take an enforcement action against a hedge fund manager. While the federal banking agencies were not parties to the case, they utilize similar administrative processes in taking enforcement actions against banks, directors, and officers.

Takeaways.

- Deference to federal agencies has come under judicial fire more recently, and the administrative framework that agencies rely on for enforcement actions could be the next domino to fall.
- The Court’s conservative justices appeared to question the constitutionality and propriety of the SEC’s use of administrative law judges in enforcement proceedings.
- If the Court rules against the SEC and finds aspects of the process unconstitutional, the banking agencies may be subject to political or legal pressure to change their own processes.

Bottom Line. The Court’s decision, expected in 2024, could lead to dramatic changes in the agencies’ enforcement approach if they are required to bring their cases in federal court.

SCOTUS Hears Oral Argument in Case That Could Affect Bank Agency Enforcement



Other Developments That You May Have Missed . . .

- **FDIC Issues Guidance Addressing CRE Risks.** On Dec. 18, the FDIC issued an advisory updating and building upon previous guidance. The advisory emphasizes the importance of strong capital, appropriate credit loss allowance levels, reliable funding sources, complete liquidity contingency plans, and robust credit-risk management practices for banks with CRE concentrations. The FDIC views CRE as a significant risk area in the current economic environment, especially after the pandemic’s increase in remote work.
- **Senate Banking Cmte Proposes ILC Legislation.** On Dec. 15, Senator Brown, Chair of the Senate Banking Committee, reintroduced the Close the Shadow Banking Loophole Act, which would impose increased regulation of industrial loan companies (ILCs). The bill has bipartisan support and is a priority of Senator Brown, but similar bills have failed in the recent past. Passage of the bill would significantly effect the future success of any ILC applications.
- **State AGs Push For National Bank Compliance.** On Dec. 7, the NYAG led a coalition of 20 state AGs in urging the OCC and CFPB to ensure that national banks cooperate with investigations into violations of state AGs. The letter confirms state AGs’ interest in pursuing enforcement actions against national banks for state law violations. National banks should consider whether aggressive state AG activity may present reputational, legal, and enforcement risks, especially in those states with aggressive AG offices.
- **FDIC Report Recommends Improvements to Supervision.** On Nov. 28, the FDIC OIG issued its Material Loss Review of First Republic Bank, containing a series of recommendations to improve supervision. FDIC banks should expect the agency to implement changes to its supervisory processes, including to the timing of issuing ratings downgrades and initiating supervisory actions.