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By electronic delivery to:
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The Honorable J. Michael Mulvaney
Acting Director
Bureau of Consumer Financial Protection
1700 G Street, NW
Washington DC 20552

Re: Request for Information Regarding the Bureau's Supervision Program
Docket Number: CFPB-2018-0004
83 Fed. Reg. 7166 (Feb. 20, 2018)

Dear Acting Director Mulvaney:

The American Bankers Association[1] appreciates the opportunity to provide comments and information to assist the Bureau of Consumer Financial Protection (Bureau or BCFP) in assessing the overall efficiency and effectiveness of its supervision program and offer suggestions for improvement. We commend you for seeking suggestions on improving the efficiency and effectiveness of the supervisory process, which is a critically important tool for achieving many of the objectives assigned to the Bureau by the Dodd-Frank Act, including ensuring that "Federal consumer financial law is enforced consistently, without regard to the status of a person as a depository institution, in order to promote fair competition,"[2] and that "markets for consumer financial products and services operate transparently and efficiently to facilitate access and innovation."[3] A supervisory process that works well can help address consumer concerns more expeditiously as well as help individual financial service providers operate successfully and better serve their customers and communities.

ABA's approach throughout the Request for Information (RFI) process will be to provide constructive feedback on the Bureau's policies and procedures. Our intent is that the Bureau implement programs and policies that are transparent, fully consistent with the law, and focused on promoting the interests of financial consumers in a strong, vibrant, and innovative market that offers the variety of financial products and services that consumers want and value.

[1] The American Bankers Association is the voice of the nation's $17 trillion banking industry, which is composed of small, regional, and large banks that together employ more than 2 million people, safeguard $13 trillion in deposits, and extend nearly $10 trillion in loans.
[2] 12 U.S.C. § 5511(b)(4).
[3] 12 U.S.C. § 5511(b)(5).

I. Summary of Comment

Overall, banks report that the Bureau's supervisory process has improved since its establishment and, in many aspects, works well. However, the experience among banks varies, and clear and consistent themes and suggestions for improving the process have emerged. The Bureau's Supervision and Examination Manual[4] already addresses many of these themes and suggestions. However, supervisory practices are not always consistent with the manual's aspirations.

As discussed in ABA's comments to the RFIs on Civil Investigative Demands and Enforcement, key among our recommendations is the need to prioritize the resolution of regulatory violations and compliance management weaknesses through the supervisory process rather than rush to enforcement. Unlike many nonbank regulators, the Bureau is not limited to enforcement actions to promote compliance. Indeed, value-added, effective supervision would minimize the need for enforcement actions. An integral part of supervision — and avoiding unnecessary reliance upon enforcement actions — is identifying weaknesses and potential violations early and working with the bank to resolve them before they become bigger issues and create greater problems. To date, the Bureau's emphasis on enforcement has crowded out supervisory solutions that would be less costly, more certain to benefit consumers, and better for the financial services marketplace as a whole.

Allied with that principle is the need to improve communications, not only between the Bureau and the regulated entity, but also between Bureau examiners and the Bureau's supervisory policy staff in Washington. Improved communications could address concerns related to voluminous but often unused and unread data requests; the length of examinations, particularly with regard to delays in receipt of the final examination report; the lack of specificity and analysis regarding violations; and delays in acknowledging that Matters Requiring Attention (MRAs) have been resolved.

Another important component of improving supervisory efficiency, effectiveness, and consistency is better coordination between the Bureau and prudential regulators with regard to exam scheduling, data requests, sharing of reports, and development of consumer compliance ratings and compliance management system (CMS) evaluations. By avoiding duplication and instead coordinating examinations, valuable synergies may be achieved, enabling the Bureau to allocate more resources to nonbank supervision for the benefit of consumers, fair competition, and economic growth.

Other recommendations include (1) more judicious use of MRAs and Potential Action and Request for Response (PARR) letters, (2) investing in the examination team by providing sufficient resources and training, (3) providing forums to allow regulated entities to understand better the Bureau's *Supervisory Highlights*, and (4) improving the appeals process.

II. Examination Process

Communication between bank and Bureau staff

Continuous communication between the Bureau and the bank throughout the examination process is critical, as the Bureau recognizes, for example, in its Supervision and Examination Manual as well as its "Appeals of Supervisory Matters" document. However, while some banks report that communications are effective and that they have improved over the years, others report dissatisfaction.

[4] Consumer Fin. Protection Bureau, *Supervision and Examination Manual* (Mar. 2018), https://s3.amazonaws.com/files.consumerfinance.gov/f/documents/cfpb_supervision-and-examination-manual.pdf.

Better and more frequent communication between the bank and Bureau staff would improve all areas of its supervisory process, including its efficiency and effectiveness. Continuous discussions throughout the supervision process — prior to, during, after, and in between examination activities— promote banks' understanding of supervisory expectations, identified weaknesses and potential violations, and timelines for resolution. On-going communications also help reduce inaccurate supervisory reports, unnecessary post-examination discussions, revisions and corrections, and confusion.

An illustration of this failure of communication is that some banks have been surprised to learn first about alleged violations *after* examiners had reached a final conclusion. One bank observed that its examiners failed to respond to the bank's requests for compliance direction and guidance, and then cited the bank for violations. Some banks observed that the lack of discussion during the examination process led to inaccurate factual findings in final reports that could have been avoided with on-site discussions. Some banks have found that the Bureau's explanations, whether offered during the examination, in the supervisory report, MRA, or PARR letter, lack specifics with regard to the facts and the legal analysis that would allow the banks to understand the alleged violations and avoid them in the future. A common bank observation was that a lack of prior discussion between the bank and examiner resulted in broad, voluminous, and duplicate requests for data examiners never used.

We also note that some banks reported positively that periodic contacts in between examinations have helped them to anticipate supervisory expectations and to educate examiners about the bank and its products and services. Other banks reported avoiding production of unnecessary data by engaging in discussions about scope and data needs with field managers prior to the formal request.

Failures in communications not only waste the banks' and Bureau's time and resources, they cause frustration and lack of confidence in the process. As noted, the Bureau's Supervision and Examination Manual instructs examiners to communicate at various stages of the process, but examiners are not consistently following those directions. We recommend that the Bureau emphasize to examiners the value and need for frequent communication throughout the examination process. We similarly recommend that the Bureau expand on the examples of constructive communication opportunities in the Supervision and Examination Manual. We also recommend that the Bureau initiate an after-the-exam quality review process to ensure that communication expectations are met.

Bureau headquarters' role in supervision

Supervisory policy staff play a critical role in providing guidance and direction to both examiners and the regulated entities. Their expertise in regulatory interpretations also ensures consistency. Supervisory policy staff are generally responsive and supportive. However, we believe that there are opportunities for improvement of their involvement in examinations and their responses to examiners' and bankers' inquiries.

Banks have raised concerns about headquarters staff involvement in and influence on examinations and their communications with examiners. For example, at a hearing of the Oversight and Investigations Subcommittee of the House Financial Services Committee, Ali Naraghi, a BCFP examiner in the Southeast Region, Division of Supervision, Enforcement and Fair Lending, testified:

> Result-oriented examinations in which the Bureau at the headquarters appears to have decided at the outset to find a violation even if none are identified. I worked on examination for 3 weeks, reviewing 52 mortgage modification applications and did not find any violations. The field manager

> told me that I must not have done my job right because I had not identified any violations. Others in my team were told to expand their sample size if no violations were identified in the initial sample. This is contrary to sampling procedures of the FFIEC and prudential regulations. Furthermore, there is no statistically sound rationale in conducting examinations in this manner.[5]

Mr. Naraghi further stated, "The Enforcement Division joined the examiners and occasionally mentioned plans to bring enforcement actions prior to completion of exam work and of discovering a violation."[6]

In another case, a bank had self-identified an issue and devised a resolution plan. However, Office of Fair Lending and Equal Opportunity staff — not the Supervision Policy examiner — advocated assignment of MRAs, even though the bank had identified, reported, and was already addressing the issue. The bank felt that the participant from the Office of Fair Lending and Equal Opportunity was not following the supervisory process and was inappropriately influencing examination conclusions. For these reasons, we commend Bureau leadership for recent actions changing the Bureau's organizational structure to place the Office of Fair Lending and Equal Opportunity within the Office of Equal Opportunity and Fairness, while combining all enforcement responsibilities within the Supervision, Enforcement, and Fair Lending Division. While the Bureau will continue to enforce fair lending laws, eliminating redundancy will not only reduce government inefficiency and duplication, it will help to minimize inconsistent Bureau direction and inappropriate influence in the supervisory process.

In addition, the Bureau could improve its role in resolving regulatory and supervisory issues and questions. Banks understand that field and regional examiners have to consult Bureau headquarters staff, for example, to interpret a rule for purposes of accuracy and consistency, especially for new regulations and novel questions. However, the process can be unreasonably lengthy, resulting in exam closure delays. In addition, banks may have little or no opportunity to discuss the issue directly with Bureau headquarters staff.

We recommend that the Bureau establish timeframes to ensure faster responses to their field and regional examiners' inquiries. Also, banks should be informed of the opportunity to discuss issues with Bureau headquarters staff directly. Further, Bureau headquarters staff should develop a means to consult formally and regularly with examiners so as to understand banks and the banking business better, thereby Bureau headquarters' directions and responses are more likely to be effective, accurate, and appropriately tailored.

Data requests

Notwithstanding the Bureau's Supervision and Examination Manual's instruction that examiners "customize an Information Request that includes only items that are pertinent to the examination of a particular entity" and "avoid receiving data not relevant to the examination,"[7] the volume and nature of the Bureau's examination data requests drew bank complaints that the requests have been overly broad, voluminous, and duplicative. Indeed, much of the information and data requested is unused by examiners, creating unnecessary expense, wasting both Bureau and bank resources, and frustrating bank compliance staff. Banks also reported that the initial requests may be followed by supplemental requests, sometimes

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5 *Allegations of Discrimination and Retaliation within the Consumer Financial Protection Bureau, Part Three Before the Subcomm. on Oversight and Investigations of the H. Comm. on Financial Services*, 113th Cong. 8 (2014) (statement of Ali Naraghi, Examiner, Southeast Region, Division of Supervision, Enforcement and Fair Lending, Consumer Financial Protection Bureau).

6 *Id.*

7 *Supervision and Examination Manual*, *supra* note 4, at 4.

multiple supplemental requests, often for data that have already been provided. Moreover, overly tight deadlines for responding to these supplemental requests are not uncommon.

Though apparently trending in the right direction, bank reports of their recent experiences underscore the need for further tailoring of data and information requests:

> A regional bank reported that, in 2016, a letter sent 45 days prior to the on-site examination requested 77 items, 32 of which had already been provided. Thirty more items were requested on-site. The bank provided 32,500 pages of information (policies and procedures) and 1 billion data fields for transactions. The response required the work of 50 bank employees over the course of 30 days prior to the examination to gather the requested information.
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> A mid-size bank reported that in 2016 it provided over 25,000 pages of information, excluding the thousands of pages required to respond to supplemental requests, yet the examiners conceded that they had not had time to review the data before they arrived on-site. Supplemental requests for 70 additional items were duplicative of the original request, many with short deadlines. The bank also noted that the composition of the exam team changed from week to week, and too often examiners, with no knowledge of what had been provided previously, would make duplicate requests. In one instance when the bank replied that the information had already been provided, the new examiner insisted it be re-provided over the objections of the team leader.
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> Another mid-size bank reported that for its exam that started in January 2018 it received a request for information involving 137 items relating to a single product. The bank was given only 30 days to deliver the data and, due to the recent concerns about data security, was asked four days before the due date to separate and hold on-site records containing any personally identifiable information. In addition, the bank received over 130 supplemental requests on-site, to which it responded, on average, within 24 hours. In some cases, the supplemental requests asked for information already provided in responses to the initial request.
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> A large bank reported that in the last two or three years, the Bureau has requested between 40 and 130 items, several only 30 days prior to the on-site examination. The request letters arrive between 30 days and 6 months prior to the examination on-site date and are typically due within 30 to 60 days of receipt.
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> A large bank reported that during its 2016 examination, the examiner in charge did not know what data had been provided, argued with his own team managers, and requested that the data be re-produced within 48 hours.

Such broad and voluminous data requests demand the involvement of numerous staff and departments, e.g., information technology, business, operations, and risk management, who must suspend their usual duties to respond in such tight deadlines. It is particularly frustrating after such efforts to find that many Bureau examiners arrive without having the opportunity to review the information and do not use much of the information during the course of the examination. Banks report that the data and data fields requested are not tailored to the bank's products, services, or processes — indeed, many note they are boilerplate requests for information that often has little, if anything, to do with the examination. Such stories do not inspire confidence in Bureau supervision, and the work required to gather unnecessary information and data undermines the efficiency and effectiveness of an exam.

In addition, banks express frustration that the Bureau and prudential regulators do not coordinate data requests. For example, the Bureau and prudential regulators may request the same data (with nonmaterial differences), but in different formats. Banks are then obliged to reformat the data at significant time and cost.

Notwithstanding such accounts, some banks report improvements in the data request process. For example, they indicate that the data requests are better tailored to the examination, and response deadlines are more reasonable and flexible. While encouraged by this trend, ABA recommends that the Bureau work with field managers to implement a data request process that includes—

- Discussions between examiners and the bank prior to issuance of an Information Request to review the scope of the exam. Discussions should also involve how to tailor the requests to promote exam efficiency and effectiveness while limiting the burden on the bank.
- Efforts by examiners to modify data requests to fit the individual exam and the way the bank maintains its records rather than rely on boilerplate forms and formats.
- Sufficient advance notice of data requests to allow adequate time to respond.
- Sufficient time and resources for examiners to review submissions prior to initiation of the on-site exam.
- Minimization of supplemental requests, especially duplicate requests.
- Coordination with prudential regulators to create a single data request that avoids re-formatting the same data.

Schedule and length of examination

The Bureau could improve the scheduling and length of its examinations. It should develop an examination strategy and plan for each of its institutions based upon the complexity and compliance risk profile. After discussing the strategy with the institution, the Bureau should provide reasonable notice (at least six months) of upcoming examinations and other supervisory activities so that banks can prepare, adjust staff schedules, and allocate resources. In addition, the Bureau should coordinate better with the prudential regulators by sharing examination strategies and coordinating examination activities and schedules. We recognize that the agencies currently attempt to coordinate examination schedules, as delineated in its May 16, 2012, Memorandum of Understanding on Supervisory Coordination, and that legitimate challenges preclude perfection. However, we believe it can be improved with more effort and a more formal system that is transparent and reasonably consistent across the regulatory agencies. Coordination will allow agencies to share findings better and avoid duplicative efforts, produce more complete and consistent reports and ratings, and conserve resources for both regulators and banks.

With regard to examination length, which is considered to be the interval between the initial data request to the receipt of the final supervisory report, bank experience varies. One bank reported that over a number of examinations, the average length was 235 days, although if fair lending was a component the average climbed to 476 days.

The time between the completion of the on-site examination and issuance of the final report can be a major factor in examination length, and it is reportedly longer than that of the prudential regulators. For example, one bank reported that it recently waited six months for the Bureau's final supervisory report, compared to 30 days for the Comptroller of the Currency's report. Another reported that the on-site examination finished in December 2017, but the final report arrived mid-April 2018.

Examination length, especially the time between the examiners' departure and bank receipt of the final supervisory report, should be shortened. Prolonged examinations are disruptive, especially if the Bureau actively follows up with questions and requests for information, as bank employees have to neglect their usual responsibilities to focus on the examination demands. Even when the Bureau is not actively communicating with the bank while the exam report is being drafted, an open-examination diverts resources, because bank staff must remain engaged to provide internal updates and be prepared to respond to the Bureau.

To advance efficient and effective allocation of Bureau and bank resources, when determining examination frequency the Bureau should factor more heavily its experience with banks who have strong CMSs and demonstrated records of consumer compliance. The Bureau has indicated its goal to prioritize and focus its resources "where consumers have the greatest potential to be harmed," and that "Relatively higher risk institutional product lines within relatively higher risk markets are [its] highest priority."[8] Because institutions with consistently strong consumer compliance and CMS present lower risk of consumer harm, they should be examined less frequently.

III. Supervisory Reports

As noted above, a significant lag between the end of the on-site examination and bank receipt of the final report is not uncommon. In addition, many supervisory reports do not specify sufficiently the violation and supporting legal analysis. They also may contain surprises and factual inaccuracies. Some banks report that they first learned about a violation through the report. In some cases, factual inaccuracies, if corrected, would have changed the conclusion. Yet, banks have not been afforded a meaningful means to participate in the process.

We recommend that the Bureau emphasize to examiners the importance of communication with the bank throughout the examination process. Examiners should discuss potential violations and concerns as soon as they identify them — and prior to report finalization — through on-site and follow-up discussions. Doing so would enable banks to take corrective steps sooner. In addition, identification of concerns prior to issuance of the final report may, in some cases, permit the bank to correct factual misunderstandings and demonstrate that no violation exists.

The report should also provide detailed information about each alleged violation, including the specific regulation (and citation) violated and the supporting legal and factual analysis. Greater detail will foster bank understanding, bank compliance, and confidence in the examination process.

Moreover, we recommend that examiners share and discuss the draft the report with the bank. This will allow examiners to correct factual inaccuracies and any related incorrect conclusions, will promote confidence in the supervisory process, and allow banks to address compliance issues sooner. We believe sharing a draft report and producing a single, accurate report, rather than, for example, amending a final report, is more efficient and effective. Multiple final reports and amendments can be confusing, and any process for amendment can be inefficient and cumbersome.

IV. Supervisory Evaluations

Explanations and treatment of violations

Banks are concerned that Bureau charges of violations, whether discussed during the examination or contained in the supervisory report, MRA, or PARR letter, do not sufficiently specify the facts and legal analysis to allow the banks to understand the violations and avoid them in the future. Others report that technical or minor violations may be inappropriately escalated into MRAs or PARR letters, distorting the

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8 Consumer Fin. Protection Bureau, Remarks of CFPB Deputy Director Steven Antonakes at the Exchequer Club (Feb. 18, 2015), https://www.consumerfinance.gov/about-us/newsroom/prepared-remarks-of-cfpb-deputy-director-steven-antonakes-at-the-exchequer-club/.

examination findings and creating unnecessary work for matters that do not present significant consumer or compliance risk.

We urge the Bureau to require examiners to provide detailed factual and legal explanations, including specific citations, for any violation, whether noted in discussions, a supervisory report, an MRA, or a PARR letter. Examiners should also not expect perfection, but effective compliance, as demonstrated by the bank's ability to identify, measure, manage, control, and monitor compliance risks. Exam reports should avoid "gotchas" where the violation is minor and poses little, if any, consumer harm.

Consumer compliance and CMS ratings

ABA supported the interagency effort to update the Consumer Compliance Rating System, but we believe that there are opportunities to make the consumer compliance rating and CMS evaluation more efficient, consistent, accurate, and useful. Our members have expressed concern that the Bureau and prudential agencies' consumer compliance ratings may be inconsistent and unpredictable, and, at times, duplicative, indicating ineffective coordination between the Bureau and the prudential agencies. Some banks report that the Bureau and prudential regulators have assigned inconsistent consumer compliance ratings and have reached differing conclusions about the effectiveness of the bank's CMS, which sows confusion and makes it challenging to respond appropriately. In addition, because examination schedules are not well-coordinated and the Bureau's examinations occur less regularly, prudential agencies may be relying on stale evaluations that distort consumer compliance ratings and CMS evaluations.

The situation is complicated by the different examination approaches of the Bureau and the prudential regulators. Prudential regulators tend to conduct comprehensive, enterprise-wide examinations on a regular schedule as the law mandates, and they regularly provide consumer compliance ratings and CMS evaluations based on their broad assessment of the institution's management of its consumer compliance risk. Those ratings and evaluations are critical factors in the "management" component of a bank's CAMELS rating.

In contrast, the Bureau's responsibility to examine both banks and nonbanks makes the prudential regulator's comprehensive, institution-centric approach impractical. Instead, the Bureau conducts examinations by product line, relying on a horizontal review of similar products believed to present the greatest risk to consumers. Depending on the bank and the scope of the examination, Bureau examiners may, but do not always, evaluate the CMS of the product being examined.[9] In cases where, over a period of time, the Bureau has assessed and rated several product lines, it may provide a "roll-up" evaluation reflecting the compilation of the individual product line ratings. In addition, the Bureau's examinations are more sporadic, because regular examinations are not mandated by law, its responsibilities extend to a much broader spectrum of institutions, and as explained above its supervisory resources are allocated to products and market participants deemed to present the greatest risk to consumers.

Experience has shown that these differences in approach have further undermined the Dodd-Frank Act's promise of one consumer compliance regulator. The Bureau's product line approach has opened the door to prudential regulators — who cite their need to evaluate a bank's CMS — conducting examinations of a bank's compliance program. Too often the result has been duplicate examinations with inconsistent ratings, evaluations, and conclusions. Moreover, while the Bureau and prudential regulators share reports, ratings, and evaluations as directed by the Dodd-Frank Act, the degree to which they are incorporated into

[9] The Bureau might not provide consumer compliance ratings and CMS evaluations if, for example, the examination is limited to a single product or the Bureau examiners lack sufficient knowledge of or experience with the bank or market. In addition, it is often not necessary for the Bureau to examine as regularly as the prudential regulators, because consistent satisfactory, targeted examinations have demonstrated little need.

each other's conclusions and final reports is unclear, all of which renders them unpredictable and limited in value.

In addition to concerns related to multiple consumer compliance ratings and CMS evaluations, banks observe that the Bureau's roll-up examination reports may be inappropriate and misleading. Past ratings and evaluations may no longer be relevant or accurate, as issues may have been, and often have been, addressed — and new ones may have developed.

An important objective of the Dodd-Frank Act in creating the Bureau was to eliminate supervisory duplication. That promise has not been fulfilled. The lack of consistent and reliable coordination between the Bureau and prudential regulators, the inconsistency in ratings and evaluations, and the duplication in examinations wastes the time and resources of both regulators and banks.

While banks are strong proponents of a single consumer compliance rating and a single CMS evaluation, there is no consensus on how to achieve it. It is not clear which agency should be the lead and assign the rating, whether this responsibility should be rotated — or even whether a single approach should apply to all banks. Designating a single agency as the examination lead, with input from others, is one option and may, in fact, improve the inter-agency regulatory environment by helping to minimize inter-agency conflict. In some cases, there may be merit to designating the prudential regulator as the lead examining agency, as the prudential regulator's holistic approach and frequency of examinations may better qualify that agency to assign the bank's consumer compliance rating and evaluate its CMS. In addition, the prudential regulatory possesses additional authority to compel compliance with regard to CMS through safety and soundness enforcement authority.[10] Assigning responsibility to the prudential regulators could also allow the Bureau to focus its time and resources on nonbank financial service providers that are not otherwise examined or not examined as frequently or thoroughly as are banks. We recommend that the Bureau and prudential regulators meet with the banking industry to understand concerns and identify reasonable and transparent solutions designed to improve coordination, increase exam effectiveness and efficiency, and free more Bureau supervisory resources to review nonbank compliance programs.

In the interim, while this dialogue is occurring, we recommend that the Bureau only consider current supervisory reports, consumer compliance ratings, and CMS evaluations. This will avoid distortions and inaccuracies in conclusions based on outdated evaluations, and it may provide positive reinforcement for correction of past violations.

Matters Requiring Attention

We believe that the MRA process can be improved to ensure MRAs are judiciously used, clear in their basis and instruction, and promptly closed once resolved.

First, MRAs should be reserved for significant, serious matters that pose actual consumer harm. However, banks report that, too often, Bureau MRAs are written for minor matters, isolated events, and technical violations. Overuse, especially if they relate to minor issues, dilutes their effectiveness and the Bureau's credibility. Moreover, a lengthy list of MRAs offers the Board of Directors and management no indication of the Bureau's priorities or where the bank should focus its attention.

The prudential regulators emphasize in their examination documents that MRAs, matters requiring board attention (MRBAs), and Matters Requiring Immediate Attention (MRIAs) are intended for significant matters. For example, the FDIC's September 2017 Compliance Examination Manual states —

[10] See 12 C.F.R. § 30 (2017).

> The MRBA page is only included in the ROE [report on examination] for items that are *significant and require prompt corrective action and elevated supervisory attention.* MRBAs are intended to clearly convey to an institution's Board and management issues of the *highest degree of supervisory concern*. MRBA could include violations of consumer protection laws, CMS weaknesses that if left unaddressed could adversely affect the institution, activities that resulted in consumer harm, or emerging issues that impact the institution and require proactive attention to mitigate risks.[11] (emphasis added)

Matters that do not rise to the level of MRBAs are addressed elsewhere: "Examiners also provide recommendations to management when issues are identified that have a lower risk of consumer harm and are correctable by management in the normal course of business."[12] Similarly, the Comptroller's Handbook describes MRAs as practices that —

> *Deviate from sound governance, internal control, and risk management principles*, and have the potential to adversely affect the bank's condition, including its financial performance or risk profile, if not addressed; or
>
> Result in *substantive noncompliance* with laws and regulations, enforcement actions, or conditions imposed in writing in connection with approval of any application or other request by the bank.[13] (emphasis added)

The Federal Reserve Board also offers guidance on the definitions of MRIAs and MRAs, stressing that they involve "significant" matters that are intended to focus the attention of Boards of Directors and any executive-level committee on "the most critical and time-sensitive issues." In contrast, the Bureau's guidance on the definition of MRA is cursory, i.e., "Sufficiently serious to bring to the attention of the board of directors," without further explanation.[14]

To ensure that MRAs are effective and useful, the Bureau should state clearly in its manual and other instructions to examiners that MRAs are reserved for significant matters, based on their severity, duration, frequency, and consumer harm. Technical or isolated non-material events should not be addressed through MRAs.

Second, we recommend that the Bureau avoid boilerplate language or over-reliance on forms. Rather, MRAs should be tailored to the bank's specific issue. Banks have reported, for example, Bureau requirements for inappropriate corrective actions that suggest a rote instruction. Also, MRAs should include a clear legal analysis, with specific citations and factual analysis that demonstrate the involvement of Bureau legal staff, where necessary. Clear analysis will promote bank understanding, resolution, and confidence in the supervisory process.

Third, though banks have reported recent improvements, banks have experienced significant delays waiting for the Bureau to close an MRA once the matter has been resolved. Several banks noted that they have waited two years for the Bureau to follow up, despite the banks' prompting. The result is not only frustration and angst but potentially inaccurate reports to the bank boards based on outdated information

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11 Fed. Deposit Ins. Corp., *Compliance Examination Manual*, § II-6.3 to 6.4, https://www.fdic.gov/regulations/compliance/manual/complianceexaminationmanual.pdf (last updated Feb. 2018).

12 *Id.* at § II-6.1.

13 Comptroller of the Currency, *Comptroller's Handbook: Bank Supervision Process*, 104-05 (Sept. 2007), https://www.occ.treas.gov/publications/publications-by-type/comptrollers-handbook/bank-supervision-process/pub-ch-bank-supervision-process.pdf.

14 *Supervision and Examination Manual*, *supra* note 4, at 18.

and circumstances that suggest there are unaddressed MRAs. We urge the Bureau to establish a formal process to close MRAs as promptly as possible and invest in the necessary resources and staff.

Potential Action and Request for Response letters

A PARR letter, a precursor to a potential enforcement action, is a source of concern and alarm to banks. We recommend that the Bureau provide more transparency in the process so that banks are not surprised by receipt of a PARR letter, more detail in the letters, and a more reasonable timeframe for the bank to respond.

Some banks have reported first learning about an issue upon receipt of a PARR letter, with no related prior dialogue with Bureau staff, including supervisory staff. PARR letters should be rare and not a surprise under an effective and transparent supervisory system.

In addition, as we suggest with regard to MRAs, PARR letters should be detailed about the alleged violation, providing specific regulatory citations, the Bureau's understanding of facts, and an element-by-element legal analysis of the Bureau's contention that reflects the Bureau's legal staff involvement and approval. The PARR letter process is far less fair and useful if it does not focus on the precise facts and legal theories on which the Bureau plans to rely. The Bureau staff, including legal staff, should also be prepared to respond to the bank's response and explain in detail reasons for any rejection of the bank's legal and factual argument.

Furthermore, banks should have more time to respond to PARR letters. The default PARR letter response time is only 14 days, an unrealistic timeframe to respond to a long list of demands that requires time to evaluate, circulate with various experts, gather, review, and sort materials and data, develop responses, and obtain internal approvals. While extensions may be granted, they are limited. Banks should have significantly longer time to respond — at a minimum 30 days — especially if the PARR letters require extensive data and document review.

The Bureau also should be more transparent about the PARR letter process, its use, and its effectiveness. For example, the Bureau could provide anonymized reports about the PARR process that describe the issues being addressed and how they are resolved, whether by withdrawal or through supervision or enforcement. The information would shed light on how and whether the process affects the Bureau's decision-making.

Impact of self-reporting

Many banks indicated that, consistent with the Bureau's Supervision and Examination Manual's instruction, Bureau examiners generally recognize and reward self-identification of violations of law and consumer harm. However, there were isolated reports that some have felt penalized nevertheless. For these banks, despite the fact that the banks had identified and reported an issue and were implementing a resolution and resolution schedule, the self-reported issues resulted in several MRAs. The Bureau should reinforce with examiners the value of encouraging banks to self-identify and self-report issues, refraining from unnecessary castigatory actions that appear to penalize self-reporting.

V. Examination Staff

We recommend that the Bureau invest additional resources in its examination staff to improve their expertise and reduce turn-over. The training, experience, and expertise of examiners vary, though overall it has improved in recent years. Given the importance of knowledgeable and experienced examiners for inspiring confidence in the Bureau's competence, effectiveness, and fairness, the Bureau should ensure that Bureau examiners have the necessary training, experience, and resources, including access to legal staff in the supervisory and regulatory divisions, to perform effectively and competently.

VI. Appeals Process

A robust appeals process is a fundamental attribute of a fair regulatory or supervisory regime. The ability of banks to challenge inappropriate supervisory findings and conclusions is critical to a reasonable and transparent supervisory regime. It not only serves as an essential check on examiner excess, but it also serves as a means to address errors — which are inevitable given today's complicated, lengthy, and numerous consumer regulations. Key features of a robust appeals process are independence from the supervisory or enforcement processes, a *de novo* review standard, and transparency.

We see no published data on the Bureau's website about appeals of supervisory matters, but our understanding is that the Bureau's appeals process is infrequently engaged. Though the Bureau states in its "Appeals of Supervisory Matters" that it "will take measures to ensure that an entity's filing of an appeal does not have an adverse effect on the entity's relationship with the CFPB,"[15] banks typically hesitate to file appeals for fear of jeopardizing their important long-term relationship with supervisors. In addition, escalating an issue to the appeals process entails involving senior management, who may lack the compliance expertise to engage effectively.

With these inhibitions and considerations in mind, we recommend that the Bureau adopt a more informal "first resort" process for challenging supervisory conclusions, which might mitigate the need for a formal appeal. Banks would benefit if they were able to access Bureau headquarters regulatory experts directly, without having to engage lawyers, to discuss interpretations of regulations. Such a process could help to resolve issues more quickly and satisfactorily than filing an appeal.

Where a formal appeal is necessary, we recommend the following adjustments which would increase confidence in the appeals process and encourage its use.

First, the Bureau should adopt a clear *de novo* review standard and grant appeals committee members discretion to conduct additional fact-finding. The Bureau's explanation of its appeals process does not identify or articulate a standard of review. A *de novo* review standard, which appellate courts apply to questions of law, rather than one that defers to the judgment of the Bureau staff who made the material supervisory determination, will help to correct errors and promote consistency and fairness.

Second, the Bureau's appeals committee members should be independent from those in the supervision function. Currently, the process excludes from the appeals committee Bureau managers who participated in the supervisory matter,[16] but it includes those who are involved in the supervisory function,[17] who may not be independent. The Bureau's Ombudsman Office serves diligently as an independent, impartial, and confidential resource, but its role is limited to liaison between supervised entities and the Bureau and providing information about the appeals process.[18] We suggest that the Bureau adopt a model similar to that of the Office of the Comptroller of the Currency (OCC), which gives banks the choice to appeal directly to an independent Ombudsman with appropriate expertise, who

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15 Consumer Fin. Protection Bureau, *Appeals of Supervisory Matters*, 2 (Oct. 28, 2015), https://s3.amazonaws.com/files.consumerfinance.gov/f/documents/201508_cfpb_ApprovedSupervisoryAppealsProcess.pdf.

16 *Id.* at 1. (The committee reviewing the appeal will consist of "one member of the Associate Director's staff, one or more representatives from CFPB Headquarters Supervision management, and one or more representatives from CFPB regional management.")

17 *Id.* at 5.

18 *Id*.

reports directly to the Comptroller.[19] An independent appeals entity would help avoid bias, promote confidence in the appeals system, and encourage banks to use the process as needed.

Third, to maximize transparency, the Bureau should make decisions public, balancing confidentiality concerns through appropriate redactions to avoid disclosure of exempt information or, if redaction is deemed insufficient to prevent improper disclosure, in summary form. The Bureau should take care to ensure that summaries and published decisions cannot be used to identify individual institutions that have appealed. We also ask that these publications be posted on a dedicated webpage to make it easy for the public to find them.

VII. *Supervisory Highlights*

The Bureau's publication of *Supervisory Highlights* has provided helpful guidance to industry. Banks find the quarterly publications helpful for understanding compliance and supervisory expectations and for educating bank staff and encouraging compliance internally. Understanding where other financial institutions may be struggling and the Bureau's concerns and priorities help banks to focus compliance efforts and resources.

However, our members would appreciate inclusion of additional detail, including anonymized cases with detailed legal analysis, recognizing that confidentiality constraints may limit publication of some information. In addition, as noted in ABA's May 14, 2018 letter[20] responding to the RFI regarding the Bureau Enforcement Processes, the Bureau rarely uses *Supervisory Highlights* to explain *why* certain matters are resolved through Supervision rather than Enforcement. Providing an explanation of the Bureau's approach to this critical issue would help industry understand how it can work constructively with the Bureau to resolve matters before they require an enforcement action.

We also recommend that the Bureau consider hosting forums to discuss *Supervisory Highlights* and permit banks to ask questions and obtain further insight and guidance about supervisory concerns and solutions. Such forums might inform the Bureau about how to make the publication more useful.

VIII. Risk-focused Supervision

A cornerstone of Title X of the Dodd-Frank Act was the authority given to the Bureau to establish a supervisory program for nondepository institutions to ensure that federal consumer financial law is "enforced consistently, without regard to the status of a person as a depository institution, in order to promote fair competition."[21] As noted in ABA's July 24, 2012, letter to the Bureau regarding the Bureau's proposed procedural rules to supervise certain nonbank covered persons based on risk determination,

> Experience demonstrates that consumer protection laws and regulations must be enforced in a fair, comparable, and rational way if there is to be any hope that the legal and regulatory obligations are observed. ABA believes that establishing comparable

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[19] Julie Andersen Hill, *Improving Appeals of Material Supervisory Determinations*, The Clearing House (2017), https://www.theclearinghouse.org/banking-perspectives/2017/2017-q3-banking-perspectives/articles/improving-supervisory-appeals. (The OCC Ombudsman received more appeal in the periods study than other prudential regulators. Between 1994 and 2012, it received 157. Between 2001 and 2012, the Federal Reserve Board received 25. Between 1995 and 2012, the FDIC received 65.)

[20] Virginia O'Neill, *ABA Response to Request for Information Regarding Bureau Enforcement Processes; Docket No. CFPB-2018-0003* (May 14, 2018), https://www.aba.com/Advocacy/commentletters/Documents/cl-RFI-Enforcement2018May.pdf.

[21] Dodd-Frank Wall Street Reform and Consumer Protection Act of 2010, Pub. L. No. 111-103, 124 Stat. 1337 (codified as amended in scattered sections of 12 U.S.C.).

> accountability across all providers of comparable financial products and services is a fundamental mission of the Bureau.[22]

Accordingly, we supported the procedures by which nondepository financial entities of any size, may become subject to Bureau supervision because the institution is engaging, or has engaged, in conduct that poses risk to consumers with regard to consumer financial products or services. As noted in our letter, establishing procedures to exercise this authority efficiently, expeditiously, and fairly is essential to ensure law abidance and transparency — without creating competitive distortions — for the benefit of consumers.[23]

Similarly, in February 2015, Steve Antonakes, then Deputy Director of the Bureau, explained that the Bureau's approach to prioritizing its supervisory responsibilities involved identifying each product line "based on potential for consumer harm; the size of the product market; the supervised entity's market share; and risks inherent to the supervised entity's operations and offering of financial consumer products within that market."[24] He further noted that some markets have stronger incentives to serve consumers than do others and that "generally when consumers cannot choose their provider of financial products or services, their clout is limited and they lose their most important voice, the ability to 'vote with their feet.'"[25] He continued that such markets present higher risks[26] and are the Bureau's highest priority.[27]

However, to date, the Bureau's supervision efforts have largely focused on depository institutions — with whom consumers have the choice to do business — contrary to the statutory mandate to establish a level playing field. Although the Bureau has issued five rules under its Dodd-Frank Act §1024 authority to define larger participants in particular markets, there are other areas in which it has not defined those larger nonbank participants and therefore does not supervise those nonbank participants. For example, the Bureau has not yet proposed a larger participant rule to define the nonbank installment lenders subject to its jurisdiction, despite the fact that previous Unified Regulatory Agenda filings include it in the proposed rule stage. We urge the Bureau to prioritize that rulemaking.

Similarly, and as recommended in our February 21, 2017, letter to the Bureau regarding its request for information about consumer access to financial records, we urge the Bureau to initiate expeditiously the rulemaking process to define those larger participants in the market for consumer financial data that will be subject to regular reporting to and examination by the Bureau. Once the Bureau has imposed supervisory authority over the larger data aggregators, the Bureau can better monitor — and react to — risks to consumers in this rapidly evolving marketplace. As further explained in that letter:

> Despite the fact that §1024 allocates supervisory resources only to "larger" market participants, we believe that the possibility of oversight should encourage compliance efforts that might otherwise be lacking in entities that currently fall below the applicable larger participant threshold, but believe that their growth may make them subject to the Bureau's supervisory and record-keeping requirements in the future. Moreover, even the smallest data aggregators that choose not to follow existing laws and regulations and are engaged in conduct that poses risk to consumers may be subject to the Bureau's

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[22] Virginia O'Neill, *Proposed procedural rules to establish supervisory authority over certain nonbank covered persons based on risk determination*, 1 (July 24, 2012), https://www.aba.com/Advocacy/commentletters/Documents/72412-Nonbank-Supervision-Risk-Oneill.pdf.

[23] *Id.*

[24] Remarks of CFPB Deputy Director Steven Antonakes at the Exchequer Club, *supra* note 7.

[25] *Id.*

[26] *Id.*

[27] *Id.*

> supervisory authority under Dodd-Frank Act §1024(a)(1)(C). That section provides that a nonbank covered person of any size, operating in any market for consumer financial products and services may become subject to the supervisory authority of the Bureau because it is engaging, or has engaged, in conduct that poses risk to consumers with regard to the offering or provision of consumer financial products or services.[28]

We strongly encourage the Bureau to exercise this authority.

IX. Conclusion

ABA appreciates your leadership in examining the supervisory process to identify opportunities to eliminate redundancies and inefficiencies and to make changes so that the Bureau functions more effectively in its supervisory role. A successful supervisory program that identifies and addresses issues early in the process not only minimizes consumer harm, it minimizes the need for formal enforcement actions. The Bureau should embrace its supervisory responsibility to help banks comply rather than rush to enforcement actions.

To be more effective and efficient, we encourage the Bureau to improve its communications not only between Bureau examiners and banks, but also between Bureau headquarters staff and examiners. It should also improve coordination with the prudential regulators to avoid duplication in efforts and inconsistencies in conclusions. These efforts will not only reduce waste, they also will allow the Bureau to be more successful in meeting its congressional obligation to focus adequate attention on nonbanks, which may not be examined or only lightly examined.

Providing greater clarity about the legal basis for violation assertions, easier access to Bureau headquarters' staff, and a more robust appeal process will promote compliance, consistency, and confidence in the Bureau's supervision. The Bureau should also support its examination staff by ensuring that they have adequate training and resources to perform. We commend the Bureau for its *Supervisory Highlights* and suggest that it provide additional detail, where appropriate. Finally, we strongly urge the Bureau to fulfill its mandate to reduce risk to consumers and ensure that federal consumer protection rules are enforced consistently among all financial institutions, including nondepository institutions, by fully exercising its authority and duty to supervise nondepository institutions.

If you have any questions about these comments or would like additional information, please contact Nessa Feddis (202 663 5433, nfeddis@aba.com) or Rick Freer (202 663 5056, rfreer@aba.com)

Sincerely,

Nessa E. Feddis

Nessa Feddis

Rick Freer

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[28] Rob Morgan, *Request for Information Regarding Consumer Access to Financial Records*, 11-12 (Feb. 21, 2017), https://www.aba.com/Advocacy/commentletters/Documents/ABA-Comment-CFPB-Data-Aggregators.pdf.