Regulatory management as strategy

Perspectives on regulatory engagement

June 2024

Center *for* **Regulatory Strategy** **US**

Introduction

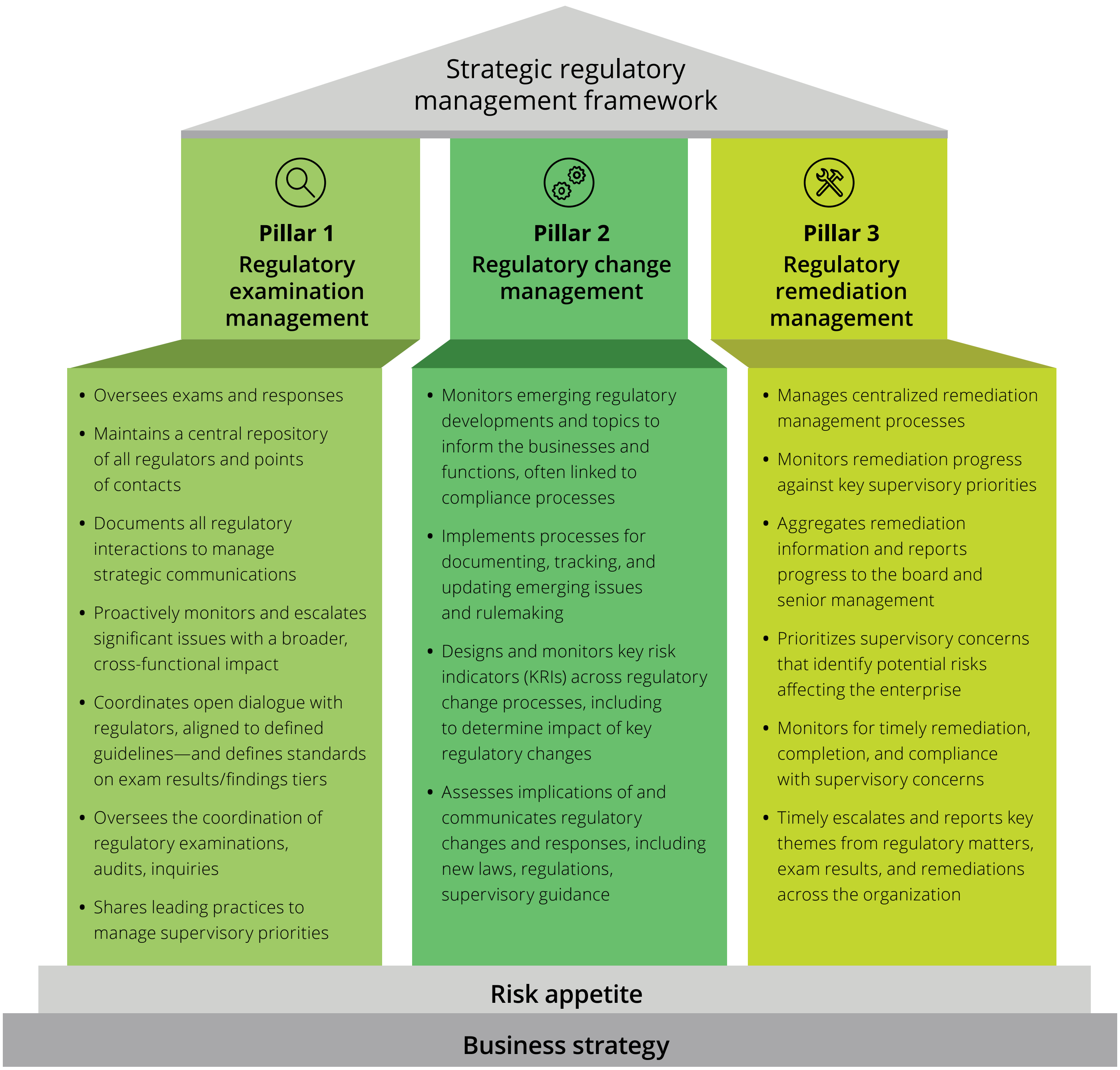
This is the second of four perspectives we are issuing in our "Regulatory management as strategy" series. While this series generally is geared toward more complex and large banking organizations (e.g., Categories I–IV[1]), we believe that many of these practical tips should help inform regulatory engagement by community and regional banks under $100 billion in assets as well.

Our first perspective described our views on an emerging paradigm that calls for a strategic end-to-end regulatory management program across three traditional pillars: regulatory examination management, regulatory change management, and regulatory remediation management (figure 1).[2] In this new paradigm, regulatory management is considered a key strategic imperative, embracing a more integrated and coordinated approach owned by the board and senior management and led by an empowered senior leader.

This edition focuses on the first of the three traditional pillars: regulatory examination management. This edition details considerations and leading practices for regulatory engagement across examination and information request management and its related component parts of regulatory relations and broader regulatory communication.

Future editions of this series will focus on the other two pillars: regulatory change management and regulatory remediation management.

Figure 1. The three pillars of an integrated and strategic regulatory management



The 'regulatory engagement function' and organization

Many firms recognize the importance of managing regulatory engagement as a strategic priority and create a centralized function with a senior leader to coordinate. Titles of regulatory engagement functions may vary from firm to firm (e.g., regulatory affairs, regulatory liaison, regulatory relations), as do their reporting lines and functional alignment.[3] For simplicity, we refer to this function as the regulatory engagement function (REF). Senior leaders of these functions often come to these roles as experienced former regulators, risk and control managers, or compliance or legal professionals. In recent years, it appears organizations have raised the stature of this function and its leaders, along with the standards for who fill these leadership roles. Leaders with broad knowledge of the organization's operations, and who understand regulatory points of interest, have become the top contenders to lead these efforts.

In this perspective, we primarily look at the typical processes this function does as part of a firm's regulatory management strategy. These processes are what the functions use to deal with regulators effectively. We will not focus on the structure or the organization of the REF, but on what they actually do.

Effective communication is critical

The past 15 years have seen a significant increase in US bank and bank holding company regulatory requirements and supervisory expectations.[4] As part of regulatory engagement, the rubber eventually hits the road—examiners and the banking organizations that are supervised and examined engage through choreographed examination processes, starting with first-day letters and ad hoc requests as part of the supervisory cycle, that culminate in the issuance of examination reports, potential supervisory findings (e.g., matters requiring attention [MRA] or matters requiring immediate attention [MRIA]), ratings,[5] and, on a not infrequent basis, formal (public) and informal (nonpublic) enforcement actions.

Engagement with supervisors also occurs outside of the formal examination process. As an example, "non-examination" interactions often take place as part of continuous monitoring or ad hoc meetings focusing on a variety of topics of supervisory interest, including an organization's strategy and initiatives, new product proposals, organizational changes, financial performance, economic impacts, specific risk areas, particular business lines, new processes, external events, remediation progress, and other matters. Senior management are often proactive in arranging discussions with their senior policymaking and supervisory counterparts at their relevant federal and, as applicable, state regulatory agencies.

Getting these communications right i.e., being clear, crisp, consistent, comprehensive, timely, and correct, is critical. There is an old saying when it comes to interactions with US banking regulators: "If it isn't documented, it doesn't exist." We may likely take that expression one step further and say: "If it is not effectively communicated, it does not exist." The stakes are high, as inadequate engagement and communication with supervisors can have significant adverse consequences.

Communication plan—viewing supervisors like your best clients

As a foundational building block, the REF should develop a formal communications plan to facilitate scheduling important meetings with supervisors and promoting information-sharing at all levels of the organization (figure 2). The plan should extend to relevant regulatory agencies, with a focus on local supervisors and policymakers with a central repository of all relevant regulators and points of contact.

A communications plan should cover engagement and communication requirements for the board of directors, executive management, senior risk management, and other senior executives across the organization's three lines model. The planning process also involves establishing a schedule of recurring meetings between the organization and its regulators. These regularly scheduled meetings can send a strong signal to regulators that the organization takes its regulatory obligations seriously.

In creating a communications plan, the REF should map organization contacts from across the institution and senior management to their regulatory counterparts and provide protocols for the frequency and type of communication required. This process can and often does include the identification of banking officers with authority to liaise and communicate with given regulators, as well as the scope of that authority (e.g., subject matter, entity, business line), with these designated executives having the authority to function as chaperones where necessary. In addition, communication protocols outline requirements for overseeing confidential supervisory information (CSI).

Figure 2. REF communication plans map board, senior management, and other regulatory liaison roles to key regulatory contacts and provide protocols for frequency and type of communication

	Key roles	Key regulatory contacts	Representative communications
Board	• Chair, Audit Committee • Chairman • CEO	• Regulatory agency chair/deputy • Central point of contact/supervisory team lead	• Strategic plan and results against plans • Significant and material governance, risk, and control concerns in US/non-US businesses
Senior manager	• Chairman • CEO • COO • General Counsel • CRO • CCO • CFO • Heads of key businesses	• Regulatory agency division lead/deputy • Central point of contact/supervisory team lead • Supervisory team subject matter expert (SME)	• Headline issues/provide escalation regarding significant and material news to key regulatory contacts • Strategy of supervision/evolving holding company strategy • Operating model of bank/key functions • Ongoing financial/operating results • Significant governance, risk, and control concerns in US/non-US businesses • Escalation of items in outstanding applications or approvals • Responding to material examination issues during the examination processes • Business leaders/functional/support group leaders in overviews and governance, control discussions
Regulatory engagement liaisons	• CCO • CRO • Regulatory relations • CFO • Heads of key businesses	• Central point of contact/supervisory team lead/deputy • Bank supervision relationship team members	• Organizing information exchange protocols (e.g., electronic or hard-copy transfers) • Responding to logistical requests • Coordinating ongoing risk and financial reporting with onsite teams • Responding to informal (ad hoc) and formal (information request letters) and first-day letters for targeted examinations • Seeking clarification of requests • Ongoing weekly or biweekly status meetings as protocols are built

CEO = chief executive officer; **COO** = chief operational officer; **CFO** = chief financial officer; **CRO** = chief risk officer; **CCO** = chief compliance officer

A strong communications plan with regulators should be approached in a similar manner of that of a top client—with targeted points of contact, expected frequency, designated officers with authority and accountability for communications, and an integrated approach to delivering the organization's messaging.

The head of the REF also typically serves as the integrator of current regulatory and business developments and is uniquely positioned to analyze, digest, and provide insights to the organization's board and senior leadership on the impact these developments could have on the enterprise's regulatory risk.

The leader's integration and analysis should be supported by data analytics tools that extract historical, real-time, or predictive insights from operational, financial, and other forms of electronic data—either internal or external to the organization.

Tactical foundation for executing the engagement strategy

The REF is also responsible for the day-to-day management of relationships with regulators, including examination coordination. A designated, named contact should be responsible for coordination and oversight of various aspects of the examination, with some delegation as appropriate, depending upon the size and complexity of the review.

In support of its examination oversight responsibility, the REF should establish a formal examination management program, which may be centralized or decentralized depending upon the size of the organization. Regardless of the chosen approach, the following items can be considered to promote a smooth examination process, ranging from administrative to much more substantive tasks.

Figure 3. Considerations to promote a smooth examination process

- Coaching of lines of business on supervisory interaction and examination protocols, including "do's and don'ts"
- Assessing line-of-business preparedness for the examination process (including potentially drawing resources from other parts of the organization in advance of examination kickoff)
- Scheduling meetings with examiners and organizing business/function attendees and content to be covered
- Ensuring REF participation in/gathering follow-ups in meetings with examiners, to the extent practicable, to ensure comprehensive and timely responses
- Overseeing logistics preparation and coordination (e.g., provision of space, location, equipment, and technology connections for examiners)
- Maintaining a comprehensive inventory of regulator requests (from items within first-day letters to follow-up requests made by supervisors during an examination), including implementing processes and training to ensure that all requests are communicated to the REF and catalogued
- Administering process for responding to regulator requests (i.e., review of regulatory requests, assignment of responsibilities for responses, review of proposed responses, tracking progress against submission deadlines)
- Seeking prompt clarification from examiners where a request is not clear or has already been provided
- Providing oversight and monitoring of management information submissions
- Providing general examination response quality control
- Ensuring issue escalation related to regulatory engagement and remediation
- Monitoring across the full life cycle of a regulatory issue that is identified (with the same discipline and rigor of an operational risk or internal audit issue—from identification to response to execution to closure to validation)

Information management

The REF should establish and maintain policies surrounding regulatory interaction and examination management. These policies can help standardize interactions with regulators across different lines of business and regions within the organization. They would typically include processes that protect CSI.

The function should also determine what tools are required to execute its responsibilities. For instance, tracking meetings and information deliverables is critical. Many institutions have in-house systems in place or systems that combine both automated and manual applications. Establishing regulatory portals that house meeting and issue trackers, respectively, are common. Increasingly, workflow and information tools are being implemented to facilitate effective recordkeeping, information management and analytics across the regulatory life cycle and portfolio of examinations, regulatory issues, and tracking.

During ongoing examinations, the REF should use an exam tracker to monitor regulatory requests. This tool would assign ownership, track progress for each request, and keep a record of requests for meetings and interviews that the regulators may want to hold during the examination.

The function may also manage the organization's issue tracker, which captures issues from many different sources of information, including regulators (e.g., MRAs and MRIAs), legal, compliance, audit, individual business lines, or the function itself. The issue tracker can be used to identify systemic problems and underlying causes. In addition, it can help drive single solutions for commonly experienced issues across various lines of business. This topical overview can help the organization understand the impact of risk and any breakdown in compliance and control systems. The issue tracker should assign an issue owner and track remediation responses, remediation progress and milestones, and, if applicable, results from testing and monitoring of controls in place to remediate.

The function can also leverage these various datasets utilizing generative artificial intelligence (GenAI) or other aggregation mechanisms to identify hot spots or areas of focus that the organization can better prepare for.

The continuing role of executive management's accountability

The establishment of the REF does not preclude other members of executive management and selected lines of business from communicating with the organization's regulators. As part of an effective regulatory management strategy, the executive management team should develop its own relationships with regulators and work under a common protocol and standards.

Even in the case of executive management communications, however, the REF can coordinate and weigh in on communications to reduce the possibility of regulatory misunderstanding or inconsistent messaging. Efforts should be made by the organization, however, to avoid the appearance that the REF is "controlling" all communications between executive management and senior supervisors, so as to avoid the possibility of frustrating supervisors and creating a perception that they are not getting as direct and unfettered access to senior leadership as they believe is necessary.

That said, having the REF supporting executive management can help the organization speak with one voice to its regulators—a voice that is consistent and transparent. Working closely with executive management, in turn, can enable the REF to better shape and understand the implications of communications to supervisors from other levels of the organization, and help to interpret and communicate supervisory messaging back to the business at all levels of the organization.

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Endnotes

1. See Board of Governors of the Federal Reserve System (FRB), "Prudential Standards for Large Bank Holding Companies, Savings and Loan Holding Companies, and Foreign Banking Organizations," November 1, 2019.

2. Deloitte, "Regulatory management as strategy," March 2024.

3. Reporting lines for this regulatory engagement function could include reporting lines into the chief operating officer (COO), chief administrative officer (CAO), chief risk officer (CRO), or chief compliance officer (CCO).

4. For example, FRB and Office of the Comptroller of the Currency (OCC), "Regulatory Capital Rules: Regulatory Capital, Implementation of Basel III, Capital Adequacy, Transition Provisions, Prompt Corrective Action, Standardized Approach for Risk-weighted Assets, Market Discipline and Disclosure Requirements, Advanced Approaches Risk-Based Capital Rule, and Market Risk Capital Rule," October 11, 2013 (Basel III); Dodd-Frank Wall Street Reform and Consumer Protection Act, Pub. L. 111-203, 111th Cong., 2010.

5. The Uniform Financial Institutions Rating System (UFIRS) was adopted by the Federal Financial Institutions Examination Council (FFIEC) to provide a uniform basis for evaluating financial institutions. Under the UFIRS, financial institutions are assigned a composite rating based on an evaluation of six financial and operational components, which are also individually rated: capital adequacy, asset quality, management capabilities, earnings sufficiency, liquidity position, and sensitivity to market risk (commonly referred to as CAMELS ratings). Another interagency unform supervisory rating system is used for evaluating branches and agencies of foreign banking organizations, which is composed of risk management, operational controls, compliance, and asset quality (commonly referred to as ROCA ratings). See Federal Deposit Insurance Corporation (FDIC), "Basic Examination Concepts and Guidelines," section 1.1, March 2022, pp. 2–4; OCC, Comptroller's Handbook: Examination Process, September 2019, pp. 69–97, 122–127.

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