

In Touch

Official Publication of the Community Bankers Association of Kansas

2022 Convention & Trade Show

BANKERS HELPING BANKERS



Mortgage Program Assessment

Take this short quiz to assess your bank's mortgage offering

MY BANK DOES NOT OFFER A MORTGAGE PROGRAM

☐ TRUE ☐ FALSE

MY BANK NEEDS MORE PRODUCT VARIETY IN OUR CURRENT MORTGAGE LOAN PROGRAM

☐ TRUE ☐ FALSE

MY BANK DOES NOT HAVE ADEQUATE RESOURCES TO PROCESS AND CLOSE MORTGAGE LOANS

☐ TRUE ☐ FALSE

MY BANK WANTS MORE FLEXIBILITY IN DETERMINING MORTGAGE PRICING AND FEE INCOME EARNED

☐ TRUE ☐ FALSE

MY BANK NEEDS ANOTHER INVESTOR TO OFFER THE MOST COMPETITIVE PRICING TO OUR CUSTOMERS

☐ TRUE ☐ FALSE

If you answered TRUE to any of the questions above:

Bankers' Bank Mortgage can help. If you need support to build a mortgage loan program or an additional resource to add product and pricing options to your existing program, we have easy to implement options designed to fit the needs of your bank. No minimum loan amount or number of loans required.

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————— MORTGAGE —————

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- ✓ Standard Commercial Loan Documentation used in most cases
- ✓ We won't restrict you to unnecessary covenants
- ✓ Limited or no reporting requirements
- ✓ Limited or no origination costs
- ✓ Low interest rates
- ✓ Principal payments often determined with the borrower's input on a year by year basis
- ✓ In many circumstances we accept bank capital growth instead of loan principal reduction
- ✓ We will come to you! Most loans initiated and closed at the borrower's home or office.

Deal directly with lender/owner who is a CPA and understands the banking industry. We have 35 years of industry experience and can make your job far less stressful and time consuming. We understand transactions.

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THE GREAT ESCAPE

THE BOND MARKET BRACES FOR THE FED'S WIND-DOWN OF ITS BALANCE SHEET



BY JIM REBER, ICBA SECURITIES

If bond investors – you – were running low on things to worry about for the rest of the year, I've got some terrific news: the \$9 trillion portfolio owned by our central bank will begin to shrink. Soon. And at a feverish pace, I might add.

We're into new territory for a number of reasons. The most obvious is that the mountain was double its size the last time a wind-down started. Another reason is that inflation, in case it's escaped your notice, is at a 40-year high. Still, another is that consumers no longer believe that prices will get back into the 2%-per-year box they've been confined to for the better part of a decade. So, this high-wire act has some drama attached.

The old playbook

Way back – hyperbole – in 2013, then-Fed Chairman Ben Bernanke announced the last unwinding without much warning and begat the Great Taper Tantrum. Bond yields rose a lot, even though the Fed's balance sheet didn't actually start to shrink for several years. And even when it did, it was a very gradual process.

For example, the initial amounts in 2018 that rolled off were pegged at \$10 billion per month. That's a lot of zeros by most everyone's reckoning but were small enough to be the equivalent of, as then-Fed Chairman Janet Yellen said, "watching paint dry." And while the monthly caps eventually rose to \$50 billion, the market, by and large, shrugged off the wind-down. To be sure, rates rose in absolute terms between 2016 and 2018 as the Fed hiked a total of 10 times, but there were very logical and measured market reactions to these events.

The playbook, 2022-style

What will this time's great escape look like? For starters, the amounts that'll be leaving the party will be much larger even at

the outset. Indications are the number will be around \$95 billion per month. That could increase depending on how quickly inflation behaves to the Federal Open Market Committee (FOMC)'s liking. There's also the matter of the other mandate, maximum employment. What happens if consumption begins to dwindle as consumers can't afford to keep buying goods and services, and the labor market dries up?

At the moment, the overriding concern is that inflation expectations are quite high, spurring the FOMC to act and talk aggressively to get prices under control. And there's a lot of raw material to work with: according to Bloomberg, the Fed owns one-fourth of all Treasury securities and an astonishing 40% of the agency mortgage-backed securities (MBS) market.

Three wind-down strategies

When you get right down to it, there are only three ways to get rid of a bunch of bonds. They are determined by when the bonds will mature, how quickly the investor wants to get rid of them and how much runoff is desired. (For all investors not specifically central banks, the market gain or loss contained in the portfolio can impact which strategy is employed. It's irrelevant to the Fed.)

First, the investor cannot reinvest all the proceeds running off. In the case of the Fed, over \$2 trillion will simply mature in the next two years, so if the objective is to shrink by around \$1.1 trillion per year, it will buy some, but not all, of what is rolling off. Secondly, if it wants to speed up the timetable, the Fed can reinvest none of the proceeds. Both cases are examples of passive Quantitative Tightening (QT).

The third, and potentially the most market-changing, is to actively sell some of the holdings. It's been a while since the Fed used

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this technique, as all of the runoff back in 2018-2019 fell under the passive QT label. This option has been floated because most of the cash flow from its MBS holdings is from prepayments of loans, and since mortgage rates have skyrocketed this year, very few homeowners can now benefit from refinancing. So, actually selling some securities into the open market could be in play, and a seller of the Fed's scale could certainly affect the market.

Where does the Great Escape end? It's anyone's guess, particularly since the Fed will attempt a very public, highly complicated soft landing in the midst of all this. But, if the size of the balance sheet relative to Gross Domestic Product reverts to the pre-pandemic levels, it would settle out at near \$4.5 trillion, around 2026.

Fasten your seat belts. ★

New ICBA Securities endorsed broker

Vining Sparks and Stifel Financial have completed their merger, and for the first time since 1989, ICBA Securities has a new endorsed broker. Stifel representatives will be on-site at a number of ICBA affiliate events later this year. For more information, visit stifel.com.



Jim Reber (jreber@icbasecurities.com) is president and CEO of ICBA Securities, ICBA's institutional, fixed-income broker-dealer for community banks.

An advertisement for First National Bank. The background is a blurred image of a cafe interior with people sitting at tables. In the foreground, a laptop sits on a wooden table, displaying the First National Bank website. The website has a teal header with the bank's logo and a white login box. Overlaid on the left side of the image is the text "ALWAYS OPEN" in large, white, serif capital letters, followed by "Open an account or apply for a loan anywhere, anytime." in a smaller, white, sans-serif font. At the bottom of the image is a dark blue banner containing the First National Bank logo, the website "fnbhutch.bank", social media icons for Facebook, Twitter, Instagram, and LinkedIn, and the phone number "620.663.1521". The text "Member FDIC" is visible in the bottom right corner of the laptop screen.

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Open an account or apply for a loan
anywhere, anytime.

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TO SHARE OR NOT

BY WILLIAM J. SHOWALTER, CRCM, CRP, SENIOR CONSULTANT

The *Uniting and Strengthening America by Providing Appropriate Tools Required to Intercept and Obstruct Terrorism Act* (USA PATRIOT Act) was passed in October 2001 in response to the terrorist acts of September 11. The purpose of the USA PATRIOT Act is to deter and punish terrorist acts in the United States and around the world, to enhance law enforcement investigatory tools, and other purposes.

Section 314(b) of the Act encourages financial institutions and associations to share information on individuals, entities, organizations, and countries suspected of engaging in possible terrorist activity or money laundering. "Financial institution" is any institution required to establish and maintain an anti-money laundering (AML) program, including banks, thrifts, and credit unions regulated by the federal banking agencies.

Section 314(b) also provides a safe harbor from civil liability to financial institutions that appropriately share information within the limitations and requirements specified by the Financial Crimes Enforcement Network (FinCEN) in its implementing regulation [31 CFR 1010.540].

Information subject to the sharing rules includes all forms of "money laundering" and "terrorist financing." FinCEN guidance has made clear that "money laundering" encompasses a wide range of activities defined as specified unlawful activities (SUA) under 18 USC 1956 and 1957. Some of these SUA directly impact financial institutions, such as a number of types of fraud, including those related to banking transactions, loan and credit applications, and bank entries.

Benefits of information sharing

Sharing information about suspected money laundering or fraud can have several benefits for the parties to the information exchange, as well as to law enforcement and the financial industry in general. Sharing information:

- Allows financial firms to significantly expand their information for assessing potential suspicious activity or accounts (e.g., previously unknown accounts, activities, and/or associated entities or individuals) without increased risk. Information received may provide details the requesting institution may not have had, such as the source of a customer's funds.
- Helps the institution receiving information by helping the decision whether to close an existing account or decline opening a new account.
- Allows a financial institution to alert other financial institutions about a customer by proactively using the 314(b) process to share information about which the other institutions might not otherwise have been aware.
- Allows participating institutions to build a more comprehensive and accurate picture of a customer's activities that may involve money laundering by shedding more light on overall financial trails (especially when they are complex and may be layered among a number of financial institutions, jurisdictions, etc.), and allow better decision making in due diligence and transaction monitoring.
- Benefits law enforcement when the information sharing results in filing one or more Suspicious Activity Report(s), particularly since SARs with information derived from more

than one financial institution may provide a more detailed and complete narrative of a particular set of transactions.

- Facilitates more efficient SAR reporting decisions by participating financial institutions by providing them with a more complete picture of activity and informing the decision to file or not file a SAR.
- Benefits law enforcement and the financial industry by identifying and aiding in detecting money laundering and terrorist financing methods and schemes.

How to participate

Sharing of information between financial institutions is entirely voluntary. A “financial institution” or “association of financial institutions” must take action to participate in 314(b) information sharing. A participating institution or association may “transmit, receive, or otherwise share information with any other financial institution or association of financial institutions regarding individuals, entities, organizations, and countries for purposes of identifying and, where appropriate, reporting activities that the financial institution or association suspects may involve possible terrorist activity or money laundering.”

There are four main requirements a participating financial institution or association must fulfill to take advantage of the safe harbor from civil liability for sharing covered information. These requirements are:

- A financial institution or association that intends to share information must submit to FinCEN a notice described on FinCEN’s website, fincen.gov. Each such notice to FinCEN is effective for the one-year period beginning on the date of the notice. To continue to engage in the sharing of information after the end of the one-year period, a financial institution or association must submit a new notice. Completed notices may be submitted to FinCEN by accessing FinCEN’s website and entering the appropriate information as directed. If a financial institution does not have internet access, the notice may be submitted by mail.
- Before sharing such information, a financial institution or an association of financial institutions must take reasonable steps to verify that the other financial institution or association with which it intends to share information has submitted to FinCEN the required notice. A financial institution or association may satisfy this verification requirement by confirming that the other financial institution or association appears on a list that FinCEN will periodically make available to financial institutions or associations of financial institutions that have filed a notice with it or by confirming directly with the other financial institution or association that the requisite notice has been filed with FinCEN.
- Information received by a financial institution or association under this process must not be used for any purpose other than identifying and, where appropriate, reporting on money laundering or terrorist activities; determining whether to establish or maintain an account or to engage in a transaction; or assisting the financial institution in complying with any requirement of the Bank Secrecy Act (BSA) regulation.
- Each financial institution or association that shares information under this process must maintain adequate procedures to protect the security and confidentiality of such shared information. These security requirements will be considered satisfied to the extent that a financial

In situations involving violations that require immediate attention, such as when a reportable violation involves terrorist activity or is ongoing, the financial institution must immediately notify, by telephone, an appropriate law enforcement authority and financial institution supervisory authorities, as well as filing a timely SAR.

institution applies to such information procedures that it has established to satisfy the requirements of section 501 of the Gramm-Leach-Bliley Act (GLBA) and applicable information security regulations issued under the GLBA concerning the protection of its own customers’ nonpublic personal information.

If information sharing under this process causes a financial institution to know, suspect, or have reason to suspect that an individual, entity, or organization is involved in or may be involved in terrorist activity or money laundering, the institution must file a SAR (assuming the institution is subject to SAR requirements). In situations involving violations that require immediate attention, such as when a reportable violation involves terrorist activity or is ongoing, the financial institution must immediately notify, by telephone, an appropriate law enforcement authority and financial institution supervisory authorities, as well as filing a timely SAR.

If a financial institution is interested in taking advantage of the benefits of 314(b) information sharing with other financial institutions to help its BSA/AML compliance, it should be sure that its BSA/AML policies and procedures have appropriate provisions covering this sharing. The bank also needs to designate a point of contact for the sharing and ensure that its affected staff is given relevant training. *



William J. Showalter, CRPM, CRP, is a Senior Consultant with Young & Associates, Inc. (younginc.com), with over 35 years of experience in compliance consulting, advising and assisting financial institutions on consumer compliance and compliance management issues. He also develops and conducts compliance training programs for individual banks and their trade associations and has authored or co-authored numerous

compliance publications and articles. Bill can be reached at wshowalter@younginc.com.



BUILDING GREATER STRENGTH WITH FICO

BY TOM BADOLATO SVP, INSTITUTIONAL RELATIONSHIPS

FICO has been what many consider as the number one stand-alone credit decision model since having been first introduced in 1989 by Fair Isaac Corp. Can we build on that foundation to create a more future-forward way of predicting lending outcomes?

As the world has evolved, so has the way we analyze data. New and exciting technology allows for innovative algorithms that give us a more defined look at an even greater data set. An all-encompassing view of the bigger borrower story can bring today's lenders to a new point of realization – that these new methods of analyzing credit, combined with the FICO mainstay, may lead to even better outcomes.

Many facets make up an individual's credit story beyond payment history and amounts owed. There is data that, once analyzed, can give critical insights to borrower characteristics unable to be categorized by a single number. That is because people are more dynamic than their credit scores.

Think of a traditional consumer credit scoring model as a printed picture. It is a one-dimensional take on a person's whole life in credit. In that static picture, there are balances on debt obligations, utilization of revolving types of credit, like credit cards, delinquency, statuses, etc. As you know, it comes from the three major credit bureaus (EFX, TU, EXP) and represents a vast cross-section of loans originated by banks, credit unions, finance companies, and other lenders across the credit industry. This information adds up to that single definitive score.

In contrast, non-traditional models that build on the foundation of FICO incorporate additional predictive information. Essentially, it is the motion picture version that enables a more dynamic view of consumer creditworthiness. This model gives lenders an ability to assess point-in-time information and the momentum of trended credit data factors, which may help predict the future credit conditions for a potential borrower and allow a lender to make more informed decisions. They see a greater depth – balances increasing or decreasing, utilization



There is data that, once analyzed, can give critical insights to borrower characteristics unable to be categorized by a single number. That is because people are more dynamic than their credit scores.

increasing or decreasing – and capture that relationship with risk outcomes.

Alternative data sources complement static and trended credit history by introducing consumers' checking history, property ownership, and alternative finance activity into credit scoring models. Consumers with comparable credit files can demonstrate vastly different repayment performance; incremental information bearing on creditworthiness equips lenders to optimize risk differentiation when the credit file alone doesn't capture the full story.

It is no small feat to create a new model for calculating and predicting high-performing loans. For example, BHG Financial, a leader in unsecured business and personal loans and creator of one of the country's largest community bank loan networks, once relied on the traditional credit scoring model to help their decision-making. That is until they evolved their credit model to identify a miscategorized set of high-quality borrowers out there most lenders were passing by.

Partnering with TransUnion, BHG Financial's data scientists analyzed over two million consumer loans. Each loan was over \$20,000, had 36+ month terms, and originated between 2015 and 2017. Billions of data points were analyzed and assessed to create their proprietary credit model, the Score.

As a result, they gained faster approvals, identified sub-prime borrowers that perform well and Prime borrowers with high default rates, thereby increasing their originations significantly. This success trickles down to their Bank Network, which is


comprised of over 1400 community banks that purchase their loans. The result – almost \$1 billion in interest earned since 2001.

By working together with the already established success of the FICO score, the chance is lower that good-paying borrowers are labeled as high risk, enabling some lenders to approve pockets of creditworthy consumers others would decline. At the same time, the chance of labeling risky borrowers as low risk is also diminished, enabling lenders to protect the credit quality of their portfolios.

Where does that leave lenders unable to dedicate time and money to develop their own evolved credit scoring model? The simple answer is to work with companies like BHG Financial and skip the extensive research and the costly origination process. This gives them immediate access to purchasing top-quality loans with low risk, which can quickly strengthen their loan portfolio to meet their bank's criteria. This solution is possibly the best answer to finding a more future-forward way of predicting lending outcomes. ★



To learn more about BHG contact: Tom Badolato SVP, Institutional Relationships at (315) 372-4510 or tbadolato@bhgbanks.com. Or visit our website at bhgloanhub.com/Tom.



BEATING THE CECL DEADLINE – WITHOUT ANALYSIS PARALYSIS

BY SHAWN O'BRIEN, PRESIDENT, QWICKRATE

After years of anticipating CECL, January 2023 is within sight. And the compliance deadline won't be moving.

For many banks, the biggest challenge is simply adopting an unfamiliar process for calculating reserves. Fortunately, regulators have made strides toward minimizing possible disruptions. In fact, they've addressed many concerns head-on.

Where should banks start?

Regulators believe a bank's CECL solution should equal the sophistication of its loan portfolio. So they expect different banks to use different solutions to calculate reserves. For banks with fewer losses, overly engineered solutions add no value – one reason solutions based on call report data are popular.

Process complexity can vary greatly among methodologies. When evaluating solutions, don't mistake precision for accuracy. No current or past losses to work with? Future loss forecasts more often come from qualitative adjustments than from quantitative adjustments.

Methodologies such as loss rate, remaining life, migration or vintages are less complicated but generally less precise. Likewise, other methodologies (i.e., probability of default, discounted cash flows) are more precise but more difficult to develop. Is it worth the extra work? Many banks say no, preferring to continue using their Q factors to support or defend CECL as they did for their ALLL reserve.

Practical assistance is available

Among the varying options for CECL compliance is a solution developed with community banks and their challenges in mind. **QwickAnalytics® CECLSolver™ is easy to use, and getting started is simple.**

The tool utilizes a weighted average remaining maturity (WARM) focus to automatically display historical losses over WARM periods. This eliminates the need to compile past information, enabling quick, easy analysis of different loss scenarios. CECLSolver also displays loss histories of selected peer groups (UPBR/state/custom) for identical periods. We'll help you with WARM calculations, whether they're performed by your team (if data is available) or by ours.

We expect that banks will continue to address qualitative factors. Regulatory statements regarding assessing the collectability of cash flows have caused many banks to stress – and there's no need. We believe banks should continue to utilize qualitative adjustments currently conducted as part of their incurred loss calculation. They've been doing this successfully for years. Furthermore, you and your regulators are familiar with and believe in the process.

As for the CECL "forecasting" element, bankers should focus on what might cause future portfolio losses and diminish their ability to collect on loans. Document and quantify your answers, again not mistaking precision for



Request a demo with your data. Find out why hundreds of community banks are already using CECLSolver to address CECL compliance. Schedule at quickrate.com or email info@quickrate.com.

complex loan-level analysis as required. Our approach is to start, monitor, and, if necessary, adjust.

CECL compliance is as complicated as you want to make it – but delaying the inevitable isn't the wisest strategy. Schedule a demo today to see your historical numbers and how CECLSolver can help. ✱



As president of QuickRate, Shawn O'Brien continues to enhance the delivery of direct non-brokered funding and investing through QuickRate's CD Marketplace, while also bringing new offerings to its more than 3,000 institutional subscribers. These newer products and services set industry standards for providing time-saving performance and ease of use to financial institutions: IntelliCredit™ for game-changing loan

review services and a credit intelligence solution that help banks detect risk earlier; QuickAnalytics® for bank research, analysis and regulatory tools including CECLSolver™; and QuickBonds for ease of access to fixed income investments. Shawn currently serves on the board of directors of the National Bank of St. Anne, an Illinois community bank. He holds a B.A. business degree from the University of Notre Dame.

accuracy. Emphasize being directionally accurate, considering your portfolio plus possible scenarios. If your mortgage portfolio is significant, consider housing prices, unemployment levels, etc. Understand how they're trending and the potential negative effect of reversals. We can help you update current qualitative adjustments to reflect forward-looking perspectives.

Designed for community banks like yours
CECLSolver provides banks with a portfolio-level solution based on call report information – plus the ability to perform more

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2022 Convention & Trade Show

BANKERS HELPING BANKERS

The Community Bankers Association is gearing up for its 44th annual convention which will be held July 13 – 15, 2022. The convention will be at the Hyatt Regency, Wichita. The golf tournament will be held on July 13.

You won't want to miss our entertaining emcee, Rich Bratten. The Education and Convention Committee and CBA Staff have lined up a wide variety of outstanding and inspiring speakers, some of which include our OSBC commissioner, the "Millennial Guy" and the inspiring Kim Becking.

Explore fresh, innovative ideas and receive answers for your challenging questions from our guest speakers:

- Shawn O'Brien
- Steve Bench
"The Millennial Guy"
- Jim Reber
- David Herndon
- Scott Green
- Susan Sullivan



JULY 13-15, 2022 • WICHITA, KANSAS • HYATT REGENCY



Wednesday Golf Tournament

The Annual Golf Tournament will be held Wednesday, July 13, at the Rolling Hills Country Club. The tournament will mix men and women golfers. The format is a golf scramble, so even if you haven't had much time to golf this year, you can still have fun and a chance to win some great prizes!



JOIN US FOR AN EXCITING LINE-UP OF EVENTS AND ENTERTAINMENT

Wednesday Night Chairman's Welcome Reception

Join us Wednesday evening for the Chairman's Welcome Reception for an informal get together. The whole family is welcome to attend. Beverages will be available.

Thursday & Friday General Session & Trade Show

CBA's Trade Show is not your average trade show! Take advantage of the focused opportunity to hear our selected and screened demo companies share about their innovations on the General Session Stage. We've carefully chosen the most relevant vendors and presentations, so you're sure to get maximum value for your trade show time.

Networking Reception

Join us Thursday, July 14th from 3:15pm – 5:00pm for a cocktail reception. You don't want to miss this opportunity to network with exhibiting companies and industry peers in the Eagle Ballroom. Name badges are required for this event.

Thursday Entertainment Wichita WindSurge Baseball Game

Bring the whole family to this year's night of fun and entertainment. Join us at the Emprise Bank Pavilion and watch the Wichita WindSurge baseball game. Enjoy all your favorite ballpark foods; hamburgers, hot dogs, bratwursts, pulled pork, baked beans, mac-n-cheese, chips, watermelon, brownies & Cookies, lemonade, water, sweet tea and beer! The WindSurge are becoming one of Wichita's popular attractions, this League has the same enthusiasm and atmosphere as a major league team, but better. CBA has a reserved section...but attendance is limited!

Hotel Reservations

Hotel accommodations at the Hyatt Regency are not included in your convention registration and should be made directly with the hotel. CBA has reserved a block of rooms for Tuesday, Wednesday, Thursday and Friday nights, July 12-15, 2022. This block of rooms consists of hotel guest rooms. The special block price of \$151/night will be held until Friday, June 17, 2022. After June 17, neither price nor room availability will be guaranteed, so make your reservations today! Be sure to mention you are with the Community Bankers Association.



REGISTER TODAY AT CBAK.COM OR CALL (785) 271-1404

Take comfort in the satisfying stack of ICBA Membership.

Supported by exclusively pro-community bank advocacy and grassroots support from bankers like you.

Sticky innovative products and services to attract and retain customers.



Rich, modern educational resources, events, webinars, and online training for your entire team.

High-quality borrowers on demand.

**2021 BHG
borrower:**

WA FICO: **734**

WA Income: **\$287,000**

Avg Loan Size: **\$109,000**

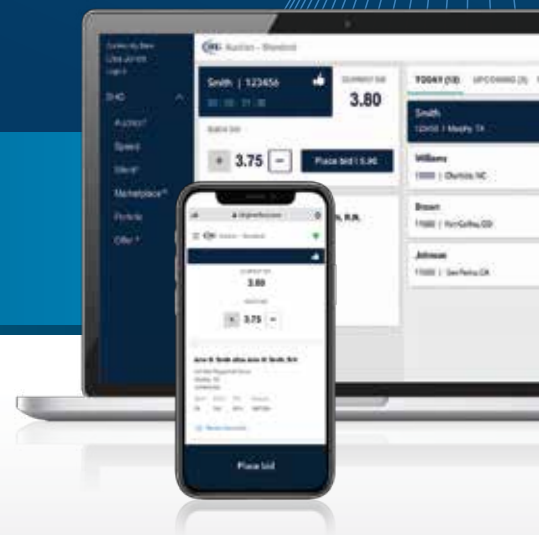
WA Years in Industry: **20**

WA DSCR: **2.6**



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TOP 10 REGULATORY HOT TOPICS FOR 2022— WHAT AML PROFESSIONALS NEED TO KNOW



BY TERRI LUTTRELL, CAMS-AUDIT, COMPLIANCE AND ENGAGEMENT DIRECTOR

The world of FinCrime is more dynamic than ever, with fraud escalating thanks to an increase in mobile payments precipitated by the pandemic and security concerns rising over the Russian conflict in Ukraine. The anti-money laundering (AML) industry waits patiently for further regulations and guidance on the Anti-Money Laundering Act of 2020 (AMLA), specifically expectations for aligning with the eight FinCEN priorities. What does this mean for the current regulatory focus for financial institutions? A panel of experts from top regulatory and supervisory agencies recently spoke at the Hawaii Bankers Association (HBA) BSA/AML Symposium to give insight into what they will be looking for in the 2022 examinations. Below are the top ten regulatory hot topics, in no order of importance.

1. Sanctions

Sanctions are fast becoming the most crucial focus of the year. Be assured that your regulators will look at your sanctions program more closely than at prior exams, and rightly so. Office of Foreign Assets Control (OFAC) compliance should be a high focus as sanctions become more complex and require constant diligence. Pay close attention to added Russian entities and individuals and understand your scanning logic. If your institution does not have automated OFAC scanning, now may be the time to invest in reputable software. Consider adding an enhanced section on Russian sanctions to your OFAC policy to show your regulators that you understand the

magnitude of this situation. The reputational risk alone is significant to your institution if you let a sanctioned Russian transaction fall through the cracks. If your institution needs assistance enhancing your sanctions program, a downloadable “Key Components of a Strong Sanctions Compliance Program” may help.

2. AMLA Preparation

With the passing of AMLA on Jan. 1, 2021, the most sweeping regulatory changes since the USA PATRIOT Act were put into motion. The AML industry is waiting for guidance from FinCEN on regulatory expectations around the requirements, particularly associated with the eight FinCEN priorities. A joint interagency statement issued June 2021 made it clear there were no immediate expectations from the regulators for financial institutions to act until rules and guidance were released. However, the panel suggested thinking and planning around AMLA requirements and informing executive management of expected changes. According to the panel, financial institutions should be prepared to answer the “how are you planning” questions during their 2022 exams.

3. Beneficial Ownership Information

As part of AMLA, the Corporate Transparency Act (CTA) includes enhanced requirements around beneficial ownership information and establishes the beneficial owner database for legal entity customers. There have been three

stages of implementation so far, with a final rule and changes to the 2018 customer due diligence (CDD) legislation still forthcoming. Financial institutions must continue to comply with the CDD rule today but should carefully follow all future changes and be ready to implement them. There will likely be a grace period for implementing any changes, as was given with the 2018 rule, and banks and credit unions must be fully informed when that time comes. It should be noted that CDD is one of the most common regulatory findings and is further discussed in the common deficiencies later in this article.

4. Cryptocurrency

In general, traditional financial institutions have a low-risk tolerance for banking cryptocurrency. Few banks and credit unions are settling cryptocurrency accounts, posing a higher risk for illicit activity. At the most, banks and credit unions may knowingly or unknowingly provide services for cryptocurrency exchanges, such as Coinbase or Binance. The COVID-19 pandemic increased the need to move funds virtually, and cryptocurrency usage filled this need. Regulators advise financial institutions to have risk-based cryptocurrency policies and procedures for their enterprise-wide risk assessment. Once the risk is assessed, create procedures around the residual risk. After all, there is a big difference between financial institutions that purchase cryptocurrency or hold it as a fiduciary and those that process cryptocurrency for customers or act as a clearinghouse for cryptocurrency exchanges. Each scenario has different risks and different due diligence expectations. A financial institution must understand the nature and purpose of each account associated with cryptocurrency and its expected activity and know their customer's customers. Consider this one of the higher risk areas of BSA, and make sure your financial institution's cryptocurrency policies are included in your risk assessment.

5. Marijuana

Speakers on the HBA panel predict that we may not see legislative clarity on the cannabis industry at the federal level for a while due to partisan disagreements. Therefore, continued due diligence is necessary for financial institutions, whether they are knowingly providing traditional services to cannabis-related businesses (CRBs) or not. The Secure and Fair Enforcement Banking Act of 2021 (SAFE Act) will undoubtedly help the AML industry and the regulators by authorizing safe harbor to financial institutions providing services to the cannabis industry and has passed the House for the third time. But with priorities shifting due to current global threats, the cannabis banking topic is not likely to move in Congress anytime soon. Regardless, financial institutions should continue to shore up policies and procedures around CRBs.

6. Non-Bank Financial Institutions

Non-Bank Financial Institutions (NBFI) are under increased regulatory scrutiny. Financial institutions should know which types of NBFIs they provide services to and conduct a thorough risk assessment on each NBFI category. Regulators want to see enhanced due diligence (EDD) on those NBFIs that present a higher risk to the institution, such as money services businesses and other non-depository institutions requiring AML/BSA programs. Banks and credit unions may be asked to provide copies of their NBFI customer's AML

program during their exam, so being proactive in obtaining a copy from each customer at onboarding and updating it throughout the life of the account would be prudent. An NBFI AML program can be lighter than a full-service traditional bank or credit union program. Still, it should address the five BSA pillars and the enhanced due diligence suggestions laid out in the FFIEC BSA Examination Manual. Noted deficiencies for NBFI AML programs include not being robust, not securing an independent audit, failing to do customer due diligence (CDD) on mortgages, and appointing a BSA Officer with no training or expertise. The panel suggests paying close attention to mortgage companies and money transmitters.

7. Innovation and Technology

Another regulatory focus coming out of AMLA is the innovation and technology needs of financial institutions, regardless of asset size. The financial market is rapidly changing regarding payment methods, and AMLA requires financial institutions to modernize their technology to handle new emerging threats. Further rules and guidance will determine the expectations and requirements, but these will undoubtedly be risk-focused. For financial institutions using artificial intelligence (AI), regulators will want to see best practices in place. There should be model validations to ensure AI is working as it should be. After all, AI is developed by humans, and mistakes can happen. Manage with caution and have a good quality assurance process in place.

8. Partnerships with FinTechs

The increased demand and competition for immediate digital payment methods have created opportunities for FinTech firms to partner with traditional financial institutions generally more conservative in developing innovative technologies, or lack expertise and resources for development. From a regulatory perspective, these partnerships can be cloudy at best, which is a new focus during exams. FinTech partners and any third-party vendor management must have an appropriate AML program, including proper CDD, adequate controls and audit function, and suspicious activity referral procedures. Financial institutions should obtain a copy of their partner's AML program and test to be sure they comply with program requirements.

Continued on page 20



For financial institutions using artificial intelligence (AI), regulators will want to see best practices in place. There should be model validations to ensure AI is working as it should be. After all, AI is developed by humans, and mistakes can happen. Manage with caution and have a good quality assurance process in place.

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9. Change management

Change management has been critical during the last two years as the pandemic caused a shift to remote working. Enhanced controls are needed to ensure data security and processes align with expectations, and regulators may ask what steps a financial institution has taken to adapt during the pandemic. Added quality assurance measures may be needed to address the challenges of managing a remote work team. Regulators will also consider how financial institutions have handled the “great resignation.” Retaining talent has proven difficult for some traditional institutions as remote work in the industry has become more acceptable. AML professionals have opportunities nationwide, which include those outside of traditional banking. Experienced BSA professionals have long been in high demand, and this shift has caused a significant strain on financial institutions’ ability to staff their BSA teams with experienced, qualified officers and investigators. Regulators will not want to know why a BSA team is understaffed or underqualified; they want the deficiency corrected. Staffing issues must be addressed, and according to the HBA panel, you may be asked how your institution is attracting and retaining talent within your BSA team. The great resignation has also affected technology talent, which has a significant crossover effect for BSA.

10. Revisiting Common Deficiencies

Wrapping up the top ten hot topics are common deficiencies cited by regulators during recent exams. Be assured that regulatory bodies share information and stay updated on other consent orders. As money laundering and fraud appear to be on the rise in many areas, financial institutions should review these common deficiencies of AML programs and fill in any identified gaps before their next audit or exam.

- Backlogs in BSA related processes, such as processing alerts, cases, and EDD high-risk reviews
- Changes in transaction monitoring systems leading to the backlog described above
- Staffing turnover leads to inadequate or inexperienced staffing
- Lack of adequate controls, either an independent audit function or internal quality assurance processes
- Risk Assessment is not updated with current products/services or markets

- Alerts closed with inadequate or no documentation
- No SAR decision with cut and paste templates – while templates are acceptable, they should always include and support reasons why the activity is not suspicious
- Inadequate analysis for No SAR decisions. Using “known customer” to justify these decisions is insufficient. Each potentially suspicious transaction must be analyzed.

Conclusion

Although there have been drops in regulatory BSA findings for 2020 and into 2021, the panel believes this was primarily due to pandemic restrictions, increased off-site examinations, and a focus shift away from BSA to asset quality and liquidity. Regulators have seen an increase in BSA focus during the first quarter of 2022, and with the Russian invasion of Ukraine, OFAC will be in the spotlight more than ever. Keeping these top ten hot topics in mind will assist your financial institution in passing your next exam with flying colors.

Takeaways

1. Planning now around AMLA requirements and informing executive management of expected changes will put your financial institution in a position to move forward with anticipated rules and guidance.
2. Financial institutions should review the common deficiencies in AML programs that regulators cite and fill gaps identified before their next audit or exam.
3. Regulators have seen an increase in BSA focus during the first quarter of 2022, and now with the crisis with the Russian invasion of Ukraine, OFAC will be in the spotlight more than ever. ✨



Terri Luttrell, Abrigo's Compliance & Engagement Director, is CAMS-Audit certified and has over 20 years in the banking industry. She has worked in both medium and large community banks in compliance/fraud, commercial lending, and deposit operations. As an AML consultant, Terri has helped institutions develop BSA/OFAC programs to ensure all regulatory requirements are met and successfully managed a team of AML investigators for a large cross-border institution, among other engagements.

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Kingman

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Bern

1892
130 Years
Kendall State Bank
Valley Falls

1895
127 Years
State Bank of Canton
Canton

1900
122 Years
Citizens State Bank & Trust Co.
Ellsworth

1901
121 Years
Bison State Bank
Bison

1901
121 Years
Union State Bank
Uniontown

1905
117 Years
Kanza Bank
Kingman

1923
99 Years
First National Bank
Hope

1990
32 Years
The Trust Company of Kansas
Wichita

June

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125 Years
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Manhattan

1901
121 Years
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Clay Center

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