You *Can* Have It All:

Balancing Fast Banking with Better Compliance

By: Ian Dunn and Ted Goldwyn

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Overview

A discussion on how both mounting compliance burdens and customer expectations for fast, seamless banking create two competing priorities for financial institutions, and how, with the right strategy, institutions can achieve both. Within the agile enterprise, fast banking can actually enable better regulatory compliance. For these two important priorities to work in harmony, financial institutions should consider the following:

- Understand the growing complexities of the regulatory landscape;

- Embrace the business value of risk management and compliance;

- Appreciate customer expectations for faster and more streamlined banking;

- Adopt technology that allows for flexibility, scalability and ease of implementation especially during periods of economic disruption;

- Update data strategy to remove siloes and fractured systems.

Conclusion

The key to achieving both fast banking and better regulatory compliance in concert is pairing the right data management and analysis strategy with an infrastructure flexible enough to allow for adaptations as regulations and expectations change. In doing this, banks and credit unions are empowered to address multiple priorities while operating strategically and proactively even in the midst of unforeseen circumstances.

Executive Summary

As consumers increasingly desire faster banking, more convenient access to their accounts and quicker decisions on their loan requests, financial institutions are hamstrung by a rising wave of new financial regulations. The burden includes new and existing regulatory requirements including the CECL accounting standard, KYC/AML, customer disclosures and fair lending laws, while risks of default, fraud and cybersecurity continue to mount. Financial institutions must also respond and adapt to new federal-issued legislation and customer needs for immediate access to financial services in response to the global health crisis brought on by COVID-19. Financial institutions are stuck between two seemingly mutually exclusive and competing priorities: fast banking and better compliance. Something has to give.

But what if you can have both? This white paper addresses how financial institutions of all sizes can achieve both fast banking and better regulatory compliance through the adoption of secure, emerging and cognitive technology and superior data management. With the right strategy and technology, fast banking can actually enable better regulatory compliance even in the midst of changing and challenging times. Welcome to the new age of agile banking.

Regulations Become More Complex

Regardless of size or charter type, all financial institutions (FIs) must deal with regulatory compliance. Whether overseen by the OCC, FDIC, Federal Reserve, the SBA or NCUA, community banks, credit unions and large banks all face similar challenges when it comes to the burden of regulation.

It is generally accepted that in financial services, a certain level of regulatory oversight is necessary and even desirable to protect consumers, taxpayers and the institutions themselves from a variety of inherent risks. However, since the late-2000s financial crisis prompted the passage of the Dodd-Frank Act, the establishment of the Consumer Financial Protection Bureau (CFPB) and a host of new consumer-friendly regulations in the U.S., the industry has been buried beneath a growing mountain of bureaucratic red tape.

Current regulatory compliance concerns of note include the ongoing implementation of the Financial Accounting Standards Board's (FASB's) Current Expected Credit Losses (CECL) accounting standard; new mortgage disclosure rules enacted under Dodd-Frank, known as the "TILA-RESPA Integrated Disclosure Rule" or "TRID"; and new "qualified mortgage" and "ability to repay" rules. In addition, banks cite compliance with the Community Reinvestment Act (CRA), quarterly call report filing requirements, and the Bank Secrecy Act/anti-money laundering requirements as most burdensome[1].
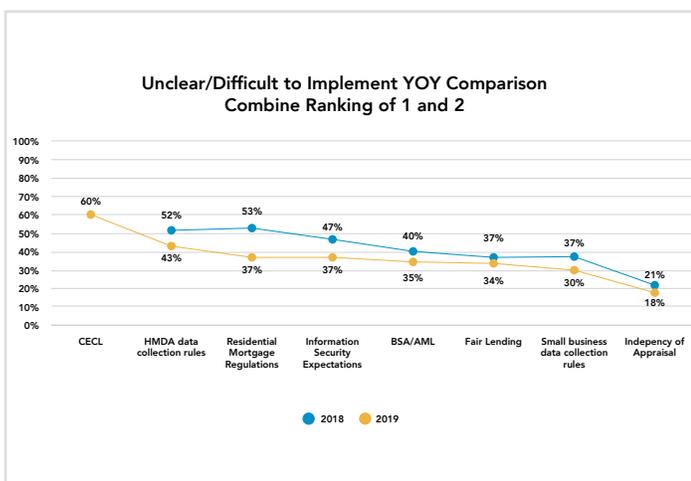
To assess relative compliance costs, the Federal Reserve Bank of St. Louis conducted a survey of community banks in 2017[2]. Respondents cited compliance with the Bank Secrecy Act as most onerous, accounting for 22 percent of their overall compliance expenses.

CECL has rapidly risen to the top of bankers' concerns with regard to compliance expense and difficulty in implementation. It topped the list of concerns in a 2019 Risk Management Association survey of community banks, with 60 percent of respondents ranking it as the most unclear or difficult to implement guidance, above HMDA data collection rules, residential mortgage regulations, information security expectations and Bank Secrecy Act/Anti-money laundering requirements[3].

Although larger institutions have already implemented CECL and required implementation for non-SEC public and private companies has been delayed to January 1, 2023[4], many community banks and credit unions are in an alarming state of unreadiness. The RMA's 2019 survey found that only a quarter of respondents were "close to ready" or "ready for implementation," while 41 percent had barely begun to prepare or were in the early stages of preparation for CECL[5].

In fact, even with the full implementation deadline still years away, both the NCUA and OCC have stated they plan to assess their institutions' CECL readiness in their upcoming exams[6].
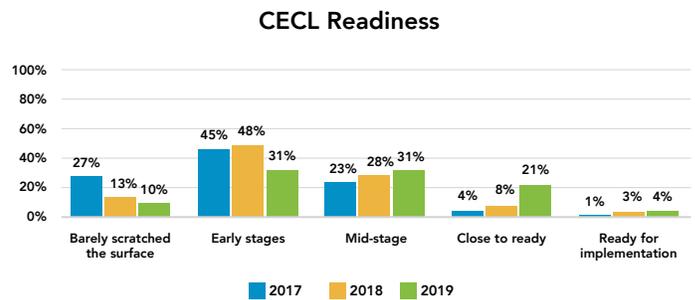
CECL Readiness

Source: "The 2019 Community Bank Regulatory Issues Survey: Results and Analysis," the Risk Management Association, May 6, 2019.

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Another top compliance priority is BSA/AML, which several oversight agencies have cited as an increasing area of scrutiny. For example, the OCC recently expressed concern with inadequate risk assessment and monitoring processes and expressed an urgent need for more modern, robust compliance systems[7].

Banking regulators are reportedly working on updating the FFIEC's examination manual via a "phased approach[8]." They are also focused on monitoring the accuracy, timeliness and thoroughness of suspicious activity report (SAR) and currency transaction report (CTR) filings[9].

Data privacy continues to be a major area of regulatory focus worldwide. The General Data Protection Regulation (GDPR) implemented in May 2018 in the European Union granted individuals expansive rights to their own data. However, it does not only affect European-domiciled companies. Firms in other regions, including the U.S., Canada, Japan and Australia are also subject to GDPR rules if they do business in the EU[10].

The U.S. inches closer to implementing its own national privacy law, with California as the first state out of the gate with passage of the California Consumer Privacy Act (CCPA) in 2018. To date, 26 additional states and Puerto Rico have introduced their own versions of data privacy bills, some of which have already passed. In addition, federal lawmakers introduced two national data privacy law proposals in late 2019, demonstrating that the movement has legs[11].

In the face of a recent global health crisis brought on by COVID-19, government regulations are being rapidly implemented to help preserve the livelihoods and lives of small businesses and households alike. In March 2020 the United States Federal Government issued the Paycheck Protection Program (PPP) under the Coronavirus Aid, Relief and Economic Security (CARES) Act in response to the COVID-19 pandemic. The program requires financial institutions to swiftly adapt and incorporate government-defined requirements into their applications to be processed as quickly as possible.

There are several common factors among these regulatory and enforcement moves. They include regulators' increasing desire to ensure that financial institutions maintain safety and stability, can withstand any future economic or financial downturns and protect the interests of consumers.

A Rising Compliance Burden

In the face of such an increasingly complex and Byzantine regulatory landscape, banks and credit unions are forced to invest more time, resources and money into compliance. Many institutions struggle to establish the operational

and technology infrastructure needed to ensure their compliance needs are met.

As the regulatory compliance burden has grown, the cost to financial institutions is growing as a percentage of overall operating expenses. Just as concerning, the costs of compliance disproportionately impact smaller institutions. According to the Federal Reserve's 2018 study, total compliance expenses averaged 9.8 percent of noninterest expense at banks with assets of less than $100 million yet averaged just 5.3 percent of non-interest expense for banks with assets of $1 billion to $10 billion[12]. Thus, the relative cost of compliance for the smallest institutions is nearly double that of their larger peers.

Total Compliance Expenses as a Percentage of Noninterest Expense by Size Category
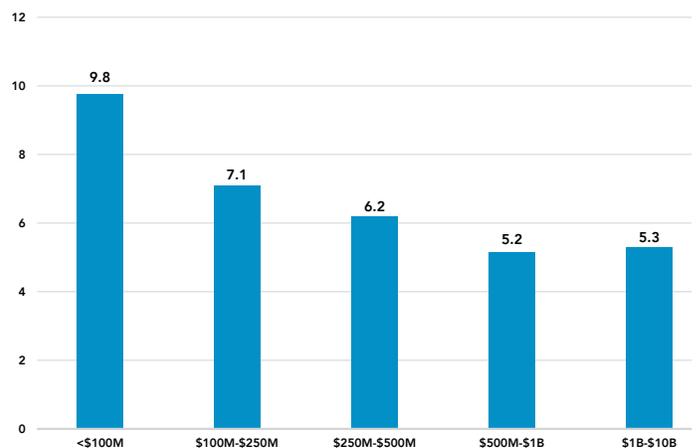
Of course, non-compliance is not a cost-effective option. According to Thomson Reuters, regulatory fines levied against UK and U.S. banks alone is expected to top $400 million by 2020[13]. And while the obvious cost of non-compliance is severe monetary penalties and fines, ignoring regulations can pose deep operational challenges for financial services organizations who fail to comply.

The impact of compliance is felt across the organization, spread among many operational areas of the bank, representing an added financial and personnel burden to manage against competing priorities. The Fed reports that compliance comprises 11.4 percent of total personnel expense, 40.5 percent of total accounting expense and 44.8 percent of consulting spend[14].

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Compliance Expense in Each Category as a Percentage of Total Spending in That Category for All Size Categories
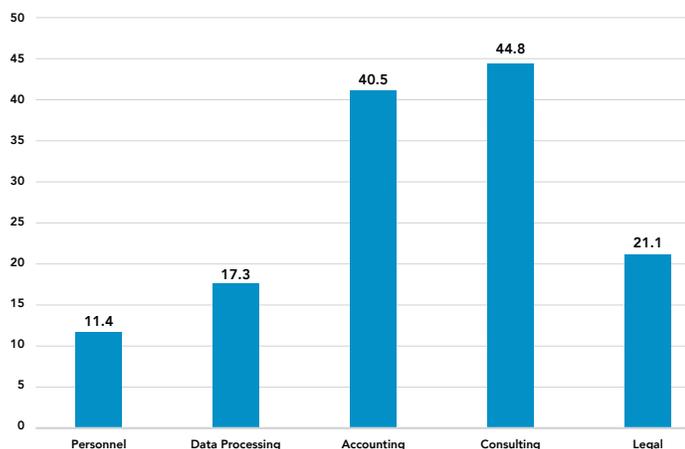
Source: "Compliance Costs, Economies of Scale and Compliance Performance: Evidence from a Survey of Community Banks," April 2018, Community Bank Research & Outreach, Federal Reserve Bank of St. Louis.and Analysis," the Risk Management Association, May 6, 2019.

Moreover, over half of the respondents to the Fed's survey reported increases in regulatory compliance expenditures in 2019[15].

> Evidence shows that as regulatory compliance demands increase, banks and credit unions struggle to serve their customers or members effectively and efficiently.

In the RMA's study, 32 percent of respondents indicated increased regulatory demands resulted in less product flexibility. Twenty-eight percent said this resulted in slower response times to meet consumer requests[16].

As previously shown, the burden and expense hits smaller institutions harder. Among community banks surveyed by RMA, 70 percent reported that the impact of regulatory demands resulted in increased costs, and 66 percent reported it resulted in slower response time to meet customer requests[17].

The Data Dilemma

In addition to the expense and customer impacts of compliance, FIs also face a rising challenge of managing the massive amount of data required to comply with regulation and serve their clientele.

Merger and acquisition activity in the financial sector has increased in recent years, partially in response to the growing burden and expense of regulatory compliance. In turn, the marriage of multiple organizations has increased the complexities of data storage and access. Banks and credit unions now house data in disparate silos, spread among multiple on- and off-site legacy systems and servers. It is difficult to access this data for reporting, regulatory compliance, customer service, sales, marketing and business planning needs. Not to mention data security, which poses more of a challenge as data is spread throughout an organization, and within obsolete, legacy systems that people don't even know how to access, or even that they exist.

With the exponential growth and increasing complexity of the data captured by financial institutions, aging technology stacks cannot keep up. The amount of customer data that institutions aggregate today is greater than anyone ever thought possible. The challenge is in storing, accessing and analyzing this information to help drive profitable business strategies and provide better service to customers.

Customers Demand Speed and Convenience

Institutions confront this growing regulatory burden and urgency of maintaining compliance standards while also facing increasing customer demand for a faster and more convenient banking experience.

Financial services consumers want immediate, round-the-clock access to their funds, anytime and anywhere. This calls for a seamless, fully digital experience across all platforms and touchpoints, whether online, mobile, in the branch or over the phone. In particular, the customer onboarding, loan application and deposit account opening experiences must be smooth and frictionless, as this is often a consumer's first significant interaction with their institution.

Customers also want to feel confident that their chosen financial institution will keep their money and information safe, secure and private.

Complicating financial institutions' response to these evolving demands is the rise of new entrants into the financial services marketplace. As challenger banks, non-bank institutions and even mega-tech firms like Amazon and Facebook pressure incumbent players to up their game,

the stakes have never been higher for traditional players to prove their value to their customers.

According to Juniper Research, the launch of the Apple Card in 2019 has spurred other tech firms such as Google, Stripe and PayPal to start or expand their banking and payment-related offerings. In addition, the requirements of the EU's new privacy regulations (PSD2) have allowed such firms to access a wealth of customer data and share it across multiple platforms using open banking tools[18]. This allows them the opportunity to compete directly with regulated financial institutions without having to be one.

> Banks and credit unions must approach their business differently. No longer can they provide the same old accounts and services, delivered in a paper-intensive, manual way, and expect customers to flock through their door.

A seamless, digital experience is now table stakes. Beyond that, banks must embrace new, emerging technologies like AI and machine learning to develop a deep understanding of their client base like never before. They must take a consistent, continuous approach to testing and introducing new products, adopting proven software development models like Agile to iterate and respond more quickly to changing consumer demands and desires.

Financial institutions must leverage the vast stores of customer and member data they have at their disposal, to ensure they maintain the profitable and loyal client relationships crucial to long-term success and stability.

Speed and Convenience in Times of Disruption

Institutions that are not utilizing an easily adaptable platform will find themselves at a significant disadvantage when the demand for online channels becomes essential as shown by the COVID-19 pandemic. Institutions operating on a digital platform were able to swiftly implement small business solutions and workflows in order to process the large influx of Paycheck Protection Program (PPP) loans to meet their customers' needs. Because the PPP made funds available to small businesses on a first-come first-serve basis, institutions that could not quickly offer compliant digital applications fell short of meeting their customers' needs.

Unleashing Data is the Solution

For incumbent players, particularly community financial institutions faced with rising costs and increased competition, this represents a difficult hill to climb. But what if the solution is right in front of us?

> What if you can have it all: efficient, cost-effective regulatory compliance and fast, convenient banking, working in concert?

Over the past few years, regulatory pressures and rapid advances in technology have spurred innovative banks to address risk and regulatory compliance in a whole new way. Technologies like AI, robotic process automation (RPA) and machine learning (ML) are allowing institutions to leverage advanced data analytics and unleash the goldmine of information stored within the massive caches of customer data at their disposal[19].

For example, more institutions around the world are embracing AI/ML tools to combat cybersecurity attacks and suspicious account activity. The Financial Stability Board and the Monetary Authority of Singapore (MAS) are using natural-language processing (NLP) to identify potential suspicious activity and prioritize based on urgency[20]. Australia's AUSTRAC intelligence agency is taking a similar approach[21].

Large international banks are also taking it on themselves to innovate cloud-based risk management systems to tackle AML risk. One prominent example is HSBC's recent collaboration with Google Cloud to develop a solution to monitor the activity and behavioral data of over 38 million customers[22].

But such solutions aren't available only to the largest banking institutions or central banks. Platforms built on secure cloud platforms like Salesforce can seamlessly integrate with an FI's core accounting and record systems to centralize data and create a single source of truth. The institution can monitor account and portfolio activity, track trends, and act quickly on aberrations and to address market needs. In addition, institutions can provide their examiners with instant access to information, reducing exam times and limiting business process disruption.

These same platforms can be deployed to deliver fast, streamlined services to customers, through the automation of repeated tasks (like required KYC questions) and quicker,

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more intuitive onboarding. With today's leading cloud-based platforms, compliance functions like KYC and AML/BSA are baked right into the solutions.

These technologies are also helping banks to monitor the financial health of their borrowers, and the portfolio as a whole. New credit scoring models that leverage the wealth of customer data banks have at their disposal can not only be used in more accurate and predictive credit decisions but also to proactively monitor borrowers' financial activities and behaviors and anticipate delinquency and defaults well ahead of time.

At the portfolio level, lenders are using analytical "sandboxes" to track changes in portfolio credit quality and determine whether degradation is due to market conditions or the lender's credit policies and practices[23].

> In times of economic disruption like COVID-19, loan analytics tools allow FIs to identify, measure and monitor risks and opportunities by specific portfolio segments, including industry/NAICS code, product type and employer.

Portfolio analytics capabilities also helped FIs understand how the economic conditions coupled with portfolio performance and credit risk could impact reserve amounts to help preserve business continuity and adequately prepare for the future.

A Roadmap for Better Compliance

Financial Institutions operate within a complex, competitive and compliance-driven environment where making timely and data-driven decisions is a key to efficient growth, effective risk management and superior service to customers. Comprehensive cloud-based solutions like the nCino Bank Operating System offer numerous advantages over the old way of managing compliance. Through robust portfolio analytics capabilities, these solutions can provide a bird's eye view of the entire loan and deposit portfolio, as well as drill down to individual relationships, accounts, loans and products.

nCino's Portfolio Analytics Solution – a comprehensive warehousing, analytics and reporting suite built into the Bank Operating System – helps FIs avoid the headache of gathering, verifying and analyzing data from multiple, disparate sources. With nCino, FIs can establish baseline performance metrics across applications, deposits and loans, and set goals to achieve the growth and compliance desired.

> This life-of-loan analytics platform enables managers to better assess today's risks to ensure tomorrow's success.

Platforms like nCino's Portfolio Analytics Solution provides value within three distinct pillars: a data warehouse, robust data analytics and tools, and data reporting and visualization. This offers institutions a clear roadmap for capturing, storing, analyzing and using data to both meet rigorous compliance and risk management activities, and meet customers ever-changing financial needs:

1. Data Warehouse

The first step is to ensure all customer data is captured accurately and warehoused safely and securely in a virtual "vault." nCino accomplishes this by aggregating the data gathered by the institution and stored in their core system. Core systems generally overwrite the data regularly, so it is important to house it somewhere safe, secure and accessible. Through the cloud, this is accomplished efficiently. nCino stores terabytes of data for trending, migration and other types of data analysis.

2. Data Analytics and Tools

Once the information is captured and securely warehoused, nCino provides a wealth of analytical tools to help the institution make effective, well-reasoned, data-driven decisions. Popular tools include predictive analytics, probability of default, probability of prepay, trend analysis, collateral values, forecasts and pricing discrimination analysis for compliance with federal fair Lending laws.

One example of such a tool is nCino's full CECL suite. Users can choose from multiple loss methods, easily incorporate CECL qualitative and environmental (Q&E) and forecast factors, and instantly produce complete disclosure and key reports.

3. Data Reporting and Visualization

The final layer of this comprehensive solution is data reporting and visualization. To provide the data and associated analysis in an easily digestible format for board members, management, ALCO members and examiners, nCino provides a range of standard and custom reporting formats. Reports are seamless and user-friendly and easy to build with a click of the mouse.

Financial institutions obtain numerous tangible benefits from employing a robust data analytics platform like nCino's Portfolio Analytics Solution. These benefits include:

⏱ Time Savings

By automating report creation and other processes, staff and management now have more time to focus on special projects, new product development and providing outstanding service to their customers and members. Some institutions have seen the time it takes to build comprehensive board reporting packages reduced from up to 3 weeks to a single day.

"nCino has freed up so much of the time I was spending doing these manual reports," says Lindsey Hartelroad, Lending and Accounts Control Manager at MountainCrest Credit Union ($105 million assets; Arlington, WA). "With nCino Portfolio Analytics, all of the information is in one area. We can literally run a report in two seconds. The board packets used to take me hours to create — now it's a click of a button. That has streamlined my process significantly."

"I have more time now to work on projects, develop new products to better suit our membership and help staff with the member service aspect."

📝 Better Regulatory Exams

With nCino's robust reporting and data analysis capabilities, institutions can now provide their regulatory examination teams with all the information they need, quickly and efficiently. Whereas exam preparation in the past took up to two weeks, now managers can build and run detailed, customized portfolio reports in a matter of minutes.

"Our examiners require a tremendous amount of reporting," says Mark Morrison, President and CEO of MountainCrest. "When you're a small institution like ours, it's challenging to access the information and generate those reports."

"The examiners want to ensure you have sound underwriting, that you're watching your credit risk migration," says Bennie Haagen, Director of Lending and Accounts Control at MountainCrest. "Every time they come in, that's where they zero in. And now I am able to show them a migration by product type and by credit tier, and drill down to credit lines, if we've closed them. They really want to know that you've got a handle on your delinquency and your future losses.

I don't have the time to generate these manual reports. Instead, I get a packet generated to me each month, and I go in it and I slice and dice what I want to see."

🔍 Reduced Risk

Better access to data can help a lender reduce the risk in their loan portfolio, through deeper trend analysis of leading indicators like credit score degradation and derogatory payment history.

Following its implementation of nCino, Solarity Credit Union ($722.5 million; Yakima, WA) created a dedicated credit quality department, focused "almost exclusively on the health of our portfolio."

"We can do all the analytics for the month on a moment's notice," says Ralph Cumbee, Chief Innovation Officer at Solarity. "We look at performance a lot. Then we stratify by credit score, dealer, loan type and other factors to monitor delinquency and charge-offs."

🙂 An Improved Customer Experience

Most importantly, by streamlining and improving its portfolio analysis, banks and credit unions can focus their attention on developing new products and services to meet their customers' expectations of an outstanding experience.

nCino's superior analytics have helped Solarity develop and launch a variety of new products, faster and with less risk. This has given the Credit Union's Board of Directors enhanced confidence in the ultimate success of new product rollouts.

"The problem when launching a new product or entering a new area is the fact that you don't know exactly when and what the challenges will be," Cumbee says. "With nCino, we make a change, and on the static pool analysis we can see where the change will lead us. We can see how the changes will perform in the real world and see how those changes are affecting our performance. That is invaluable to us."

"Having this kind of technology right in our hands is amazing," says MountainCrest's Hartelroad. "We can run the reports, see what's happening and use the information to build better products that benefit the membership."

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Conclusions

Financial institutions are at a crossroads. Faced with the seemingly opposing dynamics of customers' desire for fast and convenient banking, and an ever-growing and highly complex regulatory regime, banks and credit unions struggle to keep up. Pair these competing priorities with a global health crisis causing disruption in the financial services industry and its clear to see why it is imperative for institutions to deliver on both. The financial services industry is ready for a mindset shift, from an assumption that regulatory compliance is simply a "necessary evil" that restricts growth and profitability, to an understanding of the business value of risk management and compliance.

> The key is to employ the right data management and analysis strategy, coupled with an infrastructure that is flexible enough to allow for easy adoption as regulations change.

Institutions of all sizes can achieve both fast banking and better regulatory compliance, by leveraging emerging cognitive technologies, cloud banking, a superior data management strategy and an iterative, flexible approach to both product development and compliance and risk management.

The age of agile banking has arrived. ■

About the Authors

About Ian Dunn

Ian Dunn is the Director of Portfolio Analytics at nCino, where he oversees the product teams responsible for loans, applications, fair lending, marketing, deposits and CECL. He was a founder of the analytics software company, Visible Equity, prior to its acquisition by nCino in 2019. Previously, he worked in real estate development where he managed the design and construction of projects totaling hundreds of millions of dollars. Ian earned his M.B.A. from the UCLA Anderson School of Management and holds an undergraduate degree in Engineering. He is also a graduate of the Pacific Coast Graduate School of Banking. Ian enjoys skiing, outdoor activities and spending time with his family. He is a former collegiate soccer player and currently coaches a youth team.

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Ted Goldwyn is principal at Ted Goldwyn Writing, a freelance commercial writing firm based in Corning, New York. Ted specializes in marketing, communications, and thought leadership for the financial services industry. He has been published in leading financial journals including Credit Union Magazine and Callahan & Associates. Prior to starting his freelance writing career, Ted spent over 18 years in financial services in a variety of management roles. His experience includes over eight years in senior management as Director of Business Services at Corning Credit Union in Corning, NY, and nearly 10 years in branch management and as Vice President, Product Manager for Small Business Services at The Bank of New York in New York City. Ted holds a BS in Applied Economics and Management from Cornell University, and an MBA in Finance and International Business from New York University's Stern School of Business.

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About nCino

nCino is the worldwide leader in cloud banking. Its Bank Operating System improves employee efficiency while enhancing the customer experience for onboarding, loans and deposits across all lines of business. Transforming how financial institutions operate through innovation, reputation and speed, nCino works with more than 1,100 financial institutions globally whose assets range in size from $30 million to $2 trillion. A proven leader, nCino is part of the Forbes Cloud 100 and was named the #1 "Best Fintech to Work For" by American Banker. Follow @nCino or visit www.ncino.com.

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