



Audit Report



OIG-17-036

SAFETY AND SOUNDNESS

OCC Established Standards for and Provides Oversight of Banks' Use of Independent Consultants

February 14, 2017

Office of
Inspector General

Department of the Treasury

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Abbreviations

OCC	Office of the Comptroller of the Currency
OIG	Office of Inspector General
PPM	Policies and Procedures Manual

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*The Department of the Treasury
Office of Inspector General*

February 14, 2017

Thomas J. Curry
Comptroller of the Currency

This report presents the results of our audit of the Office of the Comptroller of the Currency's (OCC) implementation of OCC Bulletin 2013-33, *Use and Review of Independent Consultants in Enforcement Actions* and Policies and Procedures Manual (PPM) 5310-11, *Use and Review of Independent Consultants in Enforcement Actions*.

Our audit objective was to evaluate OCC's supervision of banks that employ independent consultants required by enforcement actions¹ to address significant violations of law, fraud, or harm to consumers.² To accomplish our objective, we reviewed the above guidance and relevant documentation provided by OCC. In addition, we interviewed OCC personnel with supervisory responsibilities over banks employing independent consultants as part of

¹ Enforcement actions fall into two categories: formal and informal. Formal enforcement actions are authorized by statute (mandated in some cases), generally more severe in nature, and disclosed to the public. They are enforceable through the assessment of civil money penalties and, with the exception of formal agreements, through the Federal court system. Examples of formal enforcement actions include: orders and formal written agreements within the meaning of 12 U.S.C. 1818(b); capital directives under 12 U.S.C. 3907; Prompt Corrective Action directives under 12 U.S.C. 1831o; and safety and soundness orders under 12 U.S.C. 1831p-1.

² Other OCC enforcement actions sometimes require banks to retain independent consultants to provide expertise needed to correct operational and management deficiencies not involving violations of law, fraud, or harm to consumers. These "functional" engagements allow banks to gain the additional knowledge, experience, and resources required to address deficiencies identified through the supervisory process. OCC Bulletin 2013-33 and PPM 5310-11 do not apply to these types of engagements.

enforcement actions. Appendix 1 contains a more detailed description of our objective, scope, and methodology.

In brief, we found that OCC's supervisory offices³ generally complied with Bulletin 2013-33 and PPM 5310-11. There was one instance where a supervisory office did not follow the requirement found in PPM 5310-11 that states "determinations related to the consultant's independence and qualifications should be documented by the supervisory office and reviewed by the responsible Deputy Comptroller."

We recommend that the Comptroller of the Currency determine if a Deputy Comptroller's review of determinations related to the consultant's independence and qualifications is necessary at all times or whether there are circumstances that could warrant an exception to this requirement. If so, we recommend updating the applicable guidance. Supervisory offices should be reminded of the need for a Deputy Comptroller's review in those circumstances where such review is required.

In a written response, which is included as Appendix 2, management stated it reviewed PPM 5310-11 and determined there are no circumstances that would warrant an exception to the requirement for a Deputy Comptroller's review. On January 5, 2017, OCC reminded its supervisory offices of the need for a Deputy Comptroller's review of all determinations of an independent consultant's independence and qualifications in compliance with PPM 5310-11. We consider management's actions responsive to our recommendation.

Background

In April 2011, OCC announced formal enforcement actions against eight national bank mortgage servicers (servicers) and two third-party service providers for unsafe and unsound practices related to

³ Supervisory offices support and oversee the OCC Portfolio Manager/Examiner in Charge for each bank. The supervisory office can be either a field, district, or national office, depending on the bank's size, condition, and risk profile.

residential mortgage loan servicing and foreclosure processing. OCC required each servicer to (1) engage an independent consultant to conduct a multi-faceted review of foreclosure actions between January 1, 2009, and December 31, 2010; and (2) submit a plan to remediate all financial injury to borrowers caused by any errors, misrepresentations, or other deficiencies identified in the independent consultant's findings. Consequently, the servicers hired independent consultants to review their foreclosure files and the servicers were to pay the homeowners based on the harm suffered as determined by the consultants.

By November 2012, the independent consultants had received \$1.9 billion in compensation from the servicers, but no borrower remediation for financial injury had been made by the servicers. As a result, OCC negotiated changes to the enforcement actions that required most review activities by the independent consultants to cease and that payments be made to potentially harmed borrowers.

In April 2013, the Senate Banking Subcommittee on Financial Institutions and Consumer Protection held a hearing focused on the independence, oversight, and quality of services provided by independent consultants, who are hired by banks at the request of regulators. The lawmakers raised doubts about the independence of consultants handpicked by financial firms accused of wrongdoing, and criticized OCC for providing poor oversight of the consultants.

In June 2013, Senator Sherrod Brown urged OCC and the Board of Governors of the Federal Reserve System to enact specific standards for independent consultants and increase efforts to ensure proper oversight when they are hired by banks. In November 2013, OCC issued Bulletin 2013-33 (*Use and Review of Independent Consultants in Enforcement Actions*) and PPM 5310-11 (*Use and Review of Independent Consultants in Enforcement Actions*) to provide guidance and establish standards for OCC examiners to use when banks (national banks, federal savings associations, or federal branches or agencies of foreign banks) are required to employ independent consultants as part of an enforcement action to address significant violations of law, fraud, or harm to customers.

The bulletin describes OCC's:

- assessment of the need to require a bank to hire an independent consultant in an enforcement action;
- expectations for a bank's due diligence process when retaining an independent consultant. A bank's due diligence process should establish that the consultant has sufficient independence, capacity, resources, and expertise and that the proposed engagement contracts and work plans adequately address OCC's supervisory concerns;
- review of the qualifications of the proposed consultant and the proposed contractual terms of the engagement; and
- oversight of the performance of the consultant.

The PPM describes OCC's procedures related to the:

- assessment of the need to require a bank to hire an independent consultant in an enforcement action;
- review of a bank's due diligence when retaining an independent consultant;
- review of the qualifications of the proposed consultant and the proposed contractual terms of the engagement and work plan; and
- oversight of the consultant's engagement.

We obtained a listing of enforcement actions which required the use of an independent consultant to address significant violations of law, fraud, or harm to consumers, from OCC, for the period November 2013 (issuance date of OCC Bulletin 2013-33) through April 2015. We verified the listing and in doing so, identified an additional enforcement action that should have been included in the listing. In total, we identified five enforcement actions for review to determine if OCC supervisory offices were complying with Bulletin 2013-33 and PPM 5310-11. Each enforcement action was issued by a different OCC supervisory office.

Results of Audit

We found that OCC's supervisory offices generally complied with Bulletin 2013-33 and PPM 5310-11 except in one instance where a supervisory office did not follow a requirement found in PPM 5310-11. That is, "determinations related to the consultant's

independence and qualifications should be documented by the supervisory office and reviewed by the responsible Deputy Comptroller.” In this regard, we found that for the determination made by the Mid-Size Supervision supervisory office, the Deputy Comptroller’s review was not obtained.

As part of our evaluation of OCC’s supervision of banks that employ independent consultants, we reviewed OCC Bulletin 2013-33 and PPM 5310-11, and the supervisory offices’ compliance with them.

OCC Established Written Standards for the Oversight of Independent Consultants

In a letter dated June 21, 2013, Senator Brown urged the Comptroller of the Currency and the Chairman of the Board of Governors of the Federal Reserve System to establish written standards in order to increase oversight and transparency of independent consultants hired by the financial agencies under their supervision. These standards were to address:

- requiring additional disclosures of conflict of interest;
- increasing consultant independence;
- requiring additional disclosure of influence by a regulated firm;
- increasing documentation of communications between consultants and a regulated firm;
- improving regulators' direct monitoring of consultants; and
- preventing the disclosure of confidential supervisory information.

We found that OCC Bulletin 2013-33 and PPM 5310-11 addressed each area of concern and provided guidance for the oversight of independent consultants when required as part of an enforcement action to address significant violations of law, fraud, or harm to consumers.

Assessment of the Need to Require Independent Consultants

OCC Bulletin 2013-33 outlines several factors that should be considered by OCC in determining the need to require an

independent consultant as part of an enforcement action. PPM 5310-11 outlines the responsibilities of the supervisory offices and states that the Supervision Review Committee⁴ consider the supervisory office's views in making its recommendation or decision. In the memorandum to the relevant Supervision Review Committee in support of the enforcement action, the supervisory offices are responsible for providing a recommendation regarding whether to require the bank to engage an independent consultant and if so, the scope of the consultant's responsibilities.

For the enforcement actions reviewed, we found 4 of the 5 supervisory offices fulfilled the requirement outlined in PPM 5310-11 to include recommendations to require an independent consultant in memorandums sent to the relevant Supervision Review Committees. However, we found that one supervisory office did not include a recommendation to require the use of an independent consultant in its memorandum. Subsequent to the memorandum being sent to the Supervision Review Committee, the supervisory office, in consultation with the OCC Bank Secrecy Act Senior Counsel, determined that an independent consultant was in fact necessary based on significant examination findings. According to the supervisory office personnel, the recommendation for the use of an independent consultant was discussed and approved in the Supervision Review Committee meeting and was ultimately included in the approved consent order.

For the five enforcement actions reviewed, we found that all the Supervision Review Committees notified the supervisory offices of their approval of the recommendation to engage an independent consultant via email or during the committee meetings.

⁴ The Major Matters Supervision Review Committee's (MMSRC) role is to ensure OCC bank supervision and enforcement policies are applied effectively and consistently in certain enforcement cases that are of heightened importance. MMSRC decides cases by a majority vote of the Committee. Other Supervision Review Committees serve as advisory committees to District, Midsize and Community, and Large Bank Senior Deputy/Deputy Comptrollers by providing recommendations on the proposed supervision and enforcement actions presented to them. They include the Washington Supervision Review Committee, Midsize Supervision Review Committee, and the four District Supervision Review Committees.

Review of the Proposed Consultant

Both OCC Bulletin 2013-33 and PPM 5310-11 state that before issuing a written determination of supervisory objection or no objection to the engagement of an independent consultant, OCC must require the bank to submit information of the following:

- due diligence review of the proposed consultant,
- assessment of the independence and qualifications of the proposed independent consultant, and
- the proposed engagement contracts and work plans.

Furthermore, PPM 5310-11 states that the supervisory office must document its:

- review of the information provided by the bank;
- determination of supervisory objection, or no objection; and
- determinations related to the consultant's independence and qualifications, which should be reviewed by the responsible Deputy Comptroller.

We found that all five supervisory offices documented their review of the information provided by the banks and their determination of supervisory objection or no-objection. However, 2 of the 5 supervisory offices did not provide evidence of a Deputy Comptroller's review of their determinations related to the consultant's independence and qualifications. Specifically, we found that the International Banking Supervision supervisory office did not obtain the Deputy Comptroller's review because, according to the supervisory office's personnel, the independent consultant was hired by the bank before the enforcement action was issued. Based on our understanding of the standards, the Deputy Comptroller's review was not required under this circumstance.

The Mid-Size Supervision supervisory office also did not obtain the Deputy Comptroller's review because, according to the supervisory office's personnel, the Deputy Comptroller's review was not required unless concerns surrounding the independent consultant were identified. In our reading of the applicable standard, we did not see language that provides for this exception to the Deputy Comptroller's review of determinations related to the independence and qualifications of the independent consultant.

Oversight of the Independent Consultant

OCC Bulletin 2013-33 provides that the types and frequency of interactions between OCC, the bank, and the independent consultant depend on the particular facts and circumstances covered by the enforcement action, expertise and resources of bank management, nature of the independent consultant's engagement, and the timeline for completion of the engagement. OCC is responsible for establishing a supervisory strategy for evaluating the bank's compliance with the enforcement action through which OCC evaluates and plans for appropriate and timely monitoring of the independent consultant's work.

PPM 5310-11 states that the supervisory strategy for evaluating a bank's compliance with the enforcement action should outline the supervisory office's plans, including frequency and scope, for periodic meetings or discussions with the independent consultant and for monitoring and reviewing the independent consultant's work. It also states that any ongoing monitoring, meetings, or reviews of the work of the independent consultant should be documented and retained in the supervisory work papers. We found that all five supervisory offices had supervisory strategies that stated when and how OCC would monitor compliance with the consent order. We did note that only one supervisory strategy specifically mentioned an independent consultant but all the strategies included oversight activities related to the consent order which requires the use of an independent consultant.

We found that 4 of the 5 supervisory offices showed evidence of ongoing oversight over the independent consultant, which included reviewing the independent consultant's work papers and report and/or conducting status meetings with the independent consultant. An official from one supervisory office told us that the nature of the independent consultant's engagement did not require ongoing or continuous oversight. This official stated that the independent consultant performed its reviews or audits once per year and OCC examined the work product and results in the month following the issuance of the independent consultant's report. We found this explanation reasonable as there are several factors to

consider in determining the level of oversight required including the nature of the independent consultant's engagement. In addition, we also noted that this supervisory office did have additional oversight activities over the consent order included in its supervisory strategy.

Conclusion

Overall we concluded that OCC's supervisory offices generally complied with Bulletin 2013-33 and PPM 5310-11. There was one instance where a supervisory office did not follow the requirement found in PPM 5310-11 that states "determinations related to the consultant's independence and qualifications should be documented by the supervisory office and reviewed by the responsible Deputy Comptroller."

Recommendation

We recommend that the Comptroller of the Currency determine if a Deputy Comptroller's review of determinations related to the consultant's independence and qualifications is necessary at all times or whether there are circumstances that could warrant an exception to this requirement. If so, we recommend updating the applicable guidance. Supervisory offices should be reminded of the need for a Deputy Comptroller's review in those circumstances where such review is required.

Management Response

OCC reviewed PPM 5310-11 and will retain the requirement that determinations related the consultant's independence and qualifications should be documented by the supervisory office and reviewed by the responsible Deputy Comptroller. OCC determined there are no circumstances that would warrant an exception to the requirement. On January 5, 2017, OCC reminded its supervisory offices of the need for a Deputy Comptroller's review of all

determinations of an independent consultant's independence and qualifications in compliance with PPM 5310-11.

OIG Comments

Management's actions are responsive to our recommendation.

* * * * *

We appreciate the courtesies and cooperation provided to our staff during the audit. If you wish to discuss the report, you may contact me at (202) 927-0384. Major contributors to this report are listed in Appendix 3. A distribution list for this report is provided as Appendix 4.

/s/

Jeffrey Dye
Audit Director

Our audit objective was to evaluate the Office of the Comptroller of the Currency's (OCC) supervision of banks that employ independent consultants required by enforcement actions to address significant violations of law, fraud, or harm to consumers. To accomplish our audit objective, we reviewed applicable OCC policies and procedures and documentation provided by OCC. In addition, we also interviewed key personnel. Specifically, we performed the following procedures.

- Interviewed OCC personnel in order to obtain an understanding of the process followed when requiring the use of an independent consultant to address significant violations of law, fraud, or harm to consumers. This included interviews with the Director for Enforcement and Compliance, Assistant Director for Enforcement and Compliance, Deputy Comptroller for Special Supervision, and the Assistant Deputy Comptroller – Cincinnati.
- Obtained a listing of formal enforcement actions from OCC that required the use of an independent consultant to address significant violations of law, fraud, or harm to consumers, for the period November 2013 (issuance date of OCC Bulletin 2013-33) through April 2015. This listing, which was provided by OCC on April 21, 2015, included four formal enforcement actions that required the use of an independent consultant to address violations of law and ten enforcement actions that included a requirement for an independent consultant for a functional engagement.⁵
- We verified the information on the listing of formal enforcement actions from OCC by conducting a search on the OCC website for formal enforcement actions issued between the issuance of OCC Bulletin 2013-33 (November 2013) and the date OCC provided us with its listing of enforcement actions (April 21, 2015). As a result of our review, we found a total of 242 formal enforcement actions

⁵ Functional engagements allow banks to gain the additional knowledge, experience, and resources required to address operational and management deficiencies identified through the supervisory process.

issued between the aforementioned timeframe. We performed a review of each of those formal enforcement actions looking for those that contained language such as “independent” “independent consultant” and “OCC Bulletin 2013-33”. Out of the 242, we found 40 enforcement actions that contained such language, in addition to those provided by OCC. We provided our listing to OCC for review and verification and were informed that 39 of the 40 requests were functional engagements and were unrelated to OCC Bulletin 2013-33. We found one which specifically referenced “OCC Bulletin 2013-33” which was added to our listing. We concluded that a total of five enforcement actions were issued by OCC during our review period that required the bank to employ an independent consultant to address significant violations of law, fraud, or harm to consumers.

- Provided questionnaires to OCC supervisory offices and Supervision Review Committees responsible for the banks under enforcement actions identified for review in order to obtain information regarding their role and responsibilities.
- Reviewed responses from the questionnaires and documentation provided by the supervisory offices in order to verify compliance with OCC Bulletin 2013-33 and Policies and Procedures Manual 5310-11 regarding the assessment, review and oversight process. This included:
 - memorandums to the Supervision Review Committees in support of the enforcement action;
 - documentation supporting the supervisory office’s review of the banks due diligence process, the independence and qualifications of the independent consultant, and copies of the proposed engagement contract and work plan;
 - documentation supporting the review by the Deputy Comptroller;
 - memorandums to the banks notifying them of the supervisory offices’ determination of supervisory objection and/or no objection; and

- supervisory strategy, for each supervisory office, evaluating the banks' compliance with the enforcement action and the progress of the engagement.

We performed our audit fieldwork in Washington, D.C. from January 2015 through January 2016.

We conducted this performance audit in accordance with generally accepted government auditing standards. Those standards require that we plan and perform the audit to obtain sufficient, appropriate evidence to provide a reasonable basis for our findings and conclusions based on our audit objectives. We believe that the evidence obtained provides a reasonable basis for our findings and conclusions based on our audit objectives.

Appendix 2
Management Response



Office of the Comptroller of the Currency

Washington, DC 20219

January 31, 2017

Jeffrey Dye
Director, Banking Audits
Office of Inspector General
Department of the Treasury
Washington, DC 20220

Subject: Response to Draft Report

Dear Mr. Dye:

We have reviewed the Treasury Office of the Inspector General (OIG) draft report titled "OCC Established Standards for and Provides Oversight of Banks' Use of Independent Consultants." The audit objective was to evaluate the Office of the Comptroller of the Currency's (OCC) supervision of banks that employ independent consultants required by enforcement actions to address significant violations of law, fraud, or harm to consumers. To accomplish the objectives, the OIG reviewed the OCC's implementation of OCC Bulletin 2013-33, Use and Review of Independent Consultants in Enforcement Actions and Policies, and Procedures Manual (PPM) 5310-11, Use and Review of Independent Consultants in Enforcement Actions. In addition, the OIG interviewed OCC personnel with supervisory responsibilities over banks employing independent consultants as part of enforcement actions.

The OIG found that the OCC's supervisory offices generally complied with Bulletin 2013-33 and PPM 5310-11. There was one instance where a supervisory office did not follow the requirement found in PPM 5310-11 that states "determinations related to the consultant's independence and qualifications should be documented by the supervisory office and reviewed by the responsible Deputy Comptroller."

The report recommends that the Comptroller of the Currency determine if a Deputy Comptroller's review of determinations related to the consultant's independence and qualifications is necessary at all times or whether there are circumstances that could warrant an exception to this requirement. If so, the OIG recommends updating the applicable guidance and reminding supervisory offices of the need for a Deputy Comptroller's review in those circumstances where such review is required.

The OCC reviewed PPM 5310-11 and will retain the requirement that determinations related to the consultant's independence and qualifications should be documented by the supervisory office and reviewed by the responsible Deputy Comptroller. The OCC determined there are no circumstances that would warrant an exception to the requirement. On January 5, 2017, the OCC

Appendix 2
Management Response

reminded its supervisory offices of the need for a Deputy Comptroller's review of all determinations of an independent consultant's independence and qualifications in compliance with PPM 5310-11.

If you need additional information, please contact Amy Friend, Senior Deputy Comptroller and Chief Counsel, at 202-649-5276.

Sincerely,

/s/

Thomas J. Curry
Comptroller of the Currency

Appendix 3
Major Contributors to This Report

Olivia Scott, Audit Manager
Clyburn Perry III, Program Analyst
Kiira Hall, Referencer

Department of the Treasury

Deputy Secretary
Office of Strategic Planning and Performance Improvement
Office of the Deputy Chief Financial Officer, Risk and Control
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Comptroller of the Currency
Liaison Officer

Office of Management and Budget

OIG Budget Examiner

United States Senate

Chairman and Ranking Member
Committee on Banking, Housing, and Urban Affairs

U.S. House of Representative

Chairman and Ranking Member
Committee on Financial Services



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