

INSIDER LENDING NONCOMPLIANCE NOW DISCLOSABLE

Revised FDIC rule requires disclosure of errors in insider lending compliance

* * *

Compliance with insider loan restrictions (commonly called Regulation O for national and state member banks) isn't a very hot topic right now. At least, it's not as hot as it was in the pre-Reg O days. But could that change?

Memories of Bert Lance

I'm was thinking of back in the mid-1970's when the insider lending practices of the Calhoun National Bank and Bert Lance, former chairman of the bank, came to light. Lance, at that time the Director of the Office of Management and Budget in the Carter Administration, became front-page headline news. The affair led to changes in the law and new restrictions on insider lending and overdrafts. [Editor's note: Actually, for the record, the matter went to trial and Lance was acquitted on nine counts and a mistrial was declared on three, and later resumed his chairmanship of the bank. But all the hubbub resulted in the insider lending laws and implementing rules.]

You don't typically read news stories about banks found to be in violation of Regulation O lately. Does that mean there are no Regulation O violations in banks anymore? That remains to be seen, as FDIC lawsuits, in the wake of rising failures, have not materialized in a public way just yet. But, the law and regulation still exist and compliance is still required.

And now, if the bank messes up, it won't just be between you and your examiners. The public could find out about it.

A quiet wrinkle that could speak up

A recent development makes me think it would be a very good idea for banks to increase their radar level for Regulation O/Extensions of Credit to Insiders requirements is the FDIC's recent changes to the "Annual Independent Audits and Reporting Requirements Regulation" (12 CFR 363), which became effective Aug. 6, 2009.

FDIC made a number of changes to this regulation. Overall, as revised, the regulation requires banks of a certain size (duties depend on two asset-size thresholds) to have an annual audit of financial statements; to maintain an Audit Committee composed of outside directors; and to disclose a management assessment of the bank's compliance with laws and regulations pertaining to insider loans and dividend restrictions.)

The annual management report must contain an assessment by management of the bank's compliance with the designated safety and soundness laws and regulations (including those relating to extensions of credit to insiders), which includes a public disclosure of any noncompliance with those laws and regulations.

In the explanatory discussion of the audit regulation changes in the July 20, 2009, Federal Register, FDIC noted that the regulators' past experiences with the annual management report requirement has been a lack of adequate disclosure by banks of instances of noncompliance with the applicable laws and regulations. The regulators have found that many bank reports are not disclosing all instances of noncompliance as they should be doing.

Commenters to the proposed audit regulation changes urged FDIC to only require disclosure of "material" noncompliance in the annual report. However, FDIC decided that all noncompliance must be disclosed.

According to FDIC's reasoning: "Public availability of disclosures of instances of noncompliance with these designated laws and regulations should act as a further stimulus to management's efforts to ensure that its policies, procedures, controls, and systems are sound and operating effectively."

These laws and regulations have been in place for a long time and banks should have effective controls and procedures in place to deal with them. Under the revised regulation, banks are not required to identify the specific officers or directors that are the subject of the noncompliance, but they are required to identify "appropriate qualitative and quantitative information to describe the nature, type, and severity of the noncompliance and the dollar amount of the insider loan(s) or dividend(s) involved."

If Regulation O/Insider Loan compliance has not been a high risk segment of a bank's compliance program or monitoring schedule, now is probably a good time to take a closer look at it, before any noncompliance has to be publicly disclosed.

About Nancy Derr-Castiglione

"Lucy and Nancy's Common Sense Compliance" is blogged by both Lucy Griffin and Nancy Derr-Castiglione, both ABA Banking Journal contributing editors on compliance.

Nancy, a Certified Regulatory Compliance Manager, is owner of D-C Compliance Services, an independent regulatory compliance consulting services business that has provided expertise in compliance training, monitoring, risk assessment, and policies and procedures to financial institutions since 2002.

Previously, Nancy held compliance positions with Bank One Corporation and with United Banks of Colorado.

In addition to serving as a Contributing Editor of ABA Banking Journal, Nancy has served on the ABA Compliance Executive Committee; National and Graduate Compliance Schools board; conference planning committees, and the Editorial Advisory Board for the ABA Bank Compliance magazine.

She can be reached at nancycastiglione@comcast.net

Compliance Officers: Don't miss ABA BJ's online coverage of ABA's 2009 Regulatory Compliance Conference. [Click here](#)

Community Bank Compliance Officers: Be sure to check out our other compliance blog, "AML, Fraud, and Other Things." BSA expert John Byrne blogs on money-laundering and related matters with a definite point of view. [Check it out](#)

ABA/ABA Money Laundering Enforcement Conference, Oct. 11-13, Washington, D.C. : How can you evaluate your current AML/BSA program for effectiveness? By attending the 21st annual ABA/ABA Money Laundering Enforcement Conference. o combination of other events -- in-bank or in person -- can equal the quality, scope and value of these three days of practical and current AML/BSA guidance. [Read more.](#)

For ABA Member Banks Only: Get regular compliance news updates with ABA's Compliance Source E-Letter

ABA member-bank employees have access to almost three dozen ABA news and information e-bulletins on important industry topics. One e-bulletin, THE Compliance Source, is dedicated to becoming your source for compliance information in the electronic world. Compliance Source is published each Monday throughout the year. In this changing regulatory environment, every compliance professional should subscribe THE Compliance Source. It will link you to recent compliance developments and alert you to upcoming compliance events. In addition to regular sections on "What's New in Review" and "On the Compliance Horizon," THE Compliance Source will have rotating sections including analysis of compliance issues by ABA staff in the "ABA Reports" section.

For a sample newsletter, [click here.](#)

To subscribe, [click here](#)