

## **Lingua Franca: Developing a Common Language for Bank Risk Management**

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### **Program Materials**

1. PowerPoint Presentation

### **Reference Materials**

Dorsey Blog: Consumer Financial Services Legal Update  
<https://consumerfinancialserviceslaw.us/>

**Materials are Available on [www.dorsey.com](http://www.dorsey.com) at**  
<https://www.dorsey.com/newsresources/events/event/2018/10/corporate-counsel-symposium-2018-materials>

## Lingua Franca: Developing a Common Language for Bank Risk Management

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Beth Forsythe and Joseph Lynyak, Dorsey & Whitney LLP

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## A Short Introduction

- **Risk Management is in the eyes of the beholder—**
  - It is a very fuzzy term
  - It means different things to different people
  - It often does not align with a legal approach followed by lawyers

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## A Short Introduction

- Yet—it has become the standard methodology for—
  - Operating banks and affiliates
  - Examination and supervision
  - Determining that a bank is operating in an “unsafe and unsound manner...”
- Recently the Banking Regulators have requested/forced banks to revisit their risk management systems

**Bank counsel frequently ask the question: What is risk management and what is my role in the process?**

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## Agenda

- What is risk management?
- What are the “pillars” of risk management?
- What is required by an effective bank risk management program?
  - How is it created?
  - How is it managed?
- What is the role of the attorney in the various stages of the risk management process?
  - The creation of a risk management system
  - The monitoring process
  - When something goes wrong (or terribly wrong)...
- The enhanced (revisited) risk management system currently being required by the Banking Regulators

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## Speaker

### Walter J. Mix



Walter J. Mix III heads the Financial Services practice at BRG. He is a former commissioner of the California Department of Financial Institutions (DFI) and also previously served as a banking executive at Union Bank of California. (DFI is now called the Department of Business Oversight (DBO)).

Mr. Mix advises domestic and international bank clients on corporate governance, risk management, strategic planning, and financial advisory assignments. He has significant experience in Bank Secrecy Act/anti-money laundering, cyber security, fintech, strategic planning, mergers and acquisitions, enterprise risk management, regulatory compliance, and capital planning. He has also advised clients on reengineering and implementing technology to improve profitability. In addition, he performs litigation and expert services based on his extensive expertise in financial services. He speaks frequently before bankers' groups and regulatory seminars.

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## Speaker

### Ann Claire H. Phillips



Ann Claire H. Phillips serves as U.S. Bank's Chief Risk Officer for the Law Division. In this capacity, Ms. Phillips works with the Bank's executives and senior risk officers to manage risk appetite and strategy for the Bank and handles risk management for the Law Division. Ms. Phillips serves on the Bank's Executive Risk Committee, which directs management oversight of the Bank's Risk Management Framework. Ms. Phillips also serves as the Bank's Chief Government Investigations Counsel and is responsible for developing and directing strategy for the Bank with respect to government investigations, enforcement actions, and significant regulatory inquiries.

Ms. Phillips previously served as an Assistant U.S. Attorney for ten years, during which time she prosecuted complex financial crimes and money laundering, organized crime and narcotics trafficking, and associated violent crimes. She began her career as a clerk at National Aeronautics and Space Administration (NASA), followed by four years on active duty as an Assistant Staff Judge Advocate in the U.S. Air Force Judge Advocate General's Department and five years in private practice. Ms. Phillips is a graduate of Washington and Lee University's School of Law and received her B.A. from Tulane University.

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## Speaker



### Beth Forsythe

Beth Forsythe is Co-Chair of Dorsey's Government Enforcement and Corporate Investigations Group. She conducts internal investigations and represents companies and individuals who are under government investigation for various frauds or Foreign Corrupt Practices Act ("FCPA") violations. Beth also draws on her background as a certified public accountant (inactive license) to help clients in litigation involving complex accounting and other financial issues. She frequently represents financial institutions in both litigation and investigations. Beth also routinely provides anti-corruption/FCPA due diligence and compliance advisory services, including risk assessments, program development, board presentations, and employee training. Beth spent four years in Dorsey's Washington, DC, office, but now lives and works here in Minneapolis.

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## Moderator



### Joseph T. Lynyak III

Joe Lynyak is a financial services partner in Dorsey & Whitney's Financial Services Practice. Focusing his practice on the regulation and operation of financial service intermediaries, he provides counsel on strategic planning, application and licensing, legislative strategy, commercial and consumer lending, examination, supervision and enforcement and general corporate matters. He has extensive expertise across a comprehensive range of issues before federal and state regulatory agencies such as the Federal Reserve Board, OCC, FDIC CFPB, SEC, FTC and California and New York Banking Departments. Mr. Lynyak's representative clients include foreign and domestic banks, savings associations, holding companies and mortgage banking companies. He can be contacted via email at [lynjak.joseph@dorsey.com](mailto:lynjak.joseph@dorsey.com) or at 310.386.5554.

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## What is Risk Management?

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## What are the “Pillars” of Risk Management?

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## Identified Risk

- Liquidity risk
- Credit risk
- Residual risk
- Dilution risk
- Settlement/Delivery risk
- Counterparty credit risk
- Market risks
- Interest rate risk
- Foreign exchange risk
- Concentration risk
- Exposure risks
- Investment risk
- Country risk
- Operational risk
- Legal risk
- Compliance risk

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## Two of Our Favorite Risks—

- **Legal Risk—**
  - The risk of loss caused by penalties and sanctions originating from court disputes due to breach of contractual and legal obligations, and penalties and sanctions pronounced by a regulatory body
- **Compliance Risk—**
  - The possibility of occurrence of adverse effects on the bank's financial result and capital as a consequence of failure to comply its operations with the law and other regulations, standards of operations, anti-money laundering and counter-terrorist financing procedures, and other procedures as well as other acts governing the bank's operations, particularly encompassing the risk of sanctions by the regulatory authority, risk of financial losses and reputational risk

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## What is Required for an Effective Risk Management Program?

- How is a program developed?
- How is it managed?

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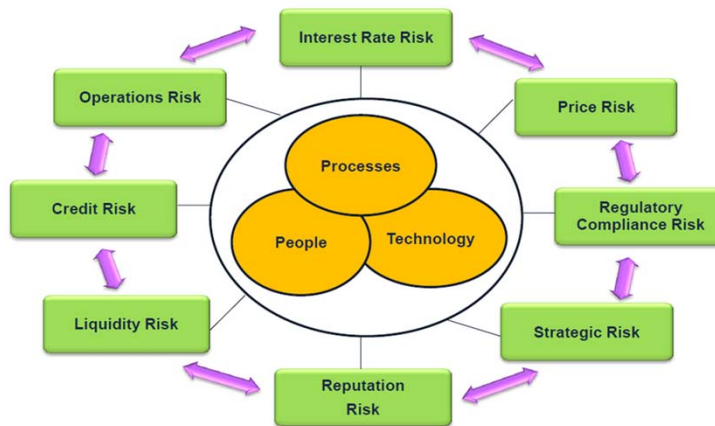
## Risk Management

- Failure to devise and implement proper risk management can lead to:
  - Costly errors, unfavorable consequences and losses
  - Inability to achieve business plan objectives
  - System and control problems
  - Violations of applicable laws and regulations
  - Consent orders and litigation
  - Litigation

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## People, processes and technology



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## Regulation, risk/return and strategy



### *Risk*

The potential that events, expected or unanticipated, may have an adverse impact on the bank's capital or earnings.

### *Risk Management*

The employment of systems and processes to manage the critical tradeoff between risk and return in financial decision-making.

### *Enterprise-wide Risk Management*

The formal mechanism or structure for managing risks across the entire institution on an integrated basis.

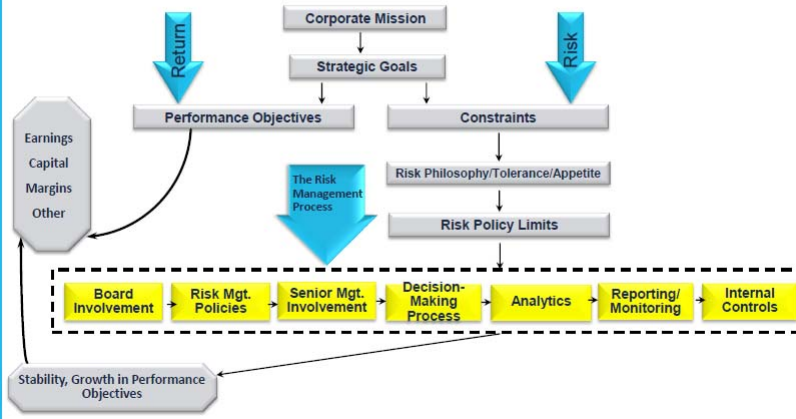
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Regulation, risk/return strategy (cont'd)



Effective Strategic Planning

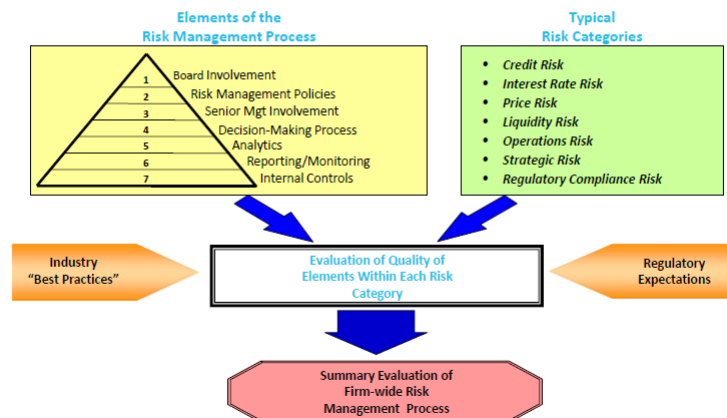


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Regulation, risk/return strategy (cont'd)



A Diagnostic Approach



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Regulation, risk/return strategy (cont'd)



**The Risk Management Rating Matrix**  
A Framework for Assessing the Quality of Risk Management

		1	2	3	4	5	6	7	8	9
		Elements of the Risk Management Process								
Risk Category	Risk Weight	Board Involvement	Senior Mgt Involvement	RM Policies	Decision Process	Analytics	Reporting/Monitoring	Internal Controls		
Credit Risk	20.0%	3	2	2	3	3	4	2		
Interest Rate Risk	5.0%	4	3	1	2	4	2	2		
Liquidity Risk	2.0%	3	2	1	1	1	1	1		
Operations Risk	25.0%	3	2	2	2	3	3	2		
Price Risk	30.0%	4	2	2	2	4	2	2		
Compliance Risk	3.0%	3	3	3	3	3	4	3		
Strategic Risk	2.0%	3	2	2	2	1	4	2		
Reputation Risk	3.0%	2	2	2	2	2	2	2		
Accounting Risk	5.0%	3	3	2	2	3	3	1		
Securitization Risk	5.0%	4	2	2	3	2	2	2		
<b>Totals</b>	<b>100.0%</b>	<b>3.37</b>	<b>2.13</b>	<b>1.96</b>	<b>2.26</b>	<b>3.19</b>	<b>2.78</b>	<b>1.96</b>		

**Overall Rating = 2.52 ("Needs Improvement")**

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## What is the Role of the Attorney in the Various Stages of the Risk Management Process?

- The Creation of a Risk Management System
- The Monitoring Process
- When Something Goes Wrong (or Terribly Wrong)...

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## Case Studies—

- **Dodd-Frank whistleblower authority**
- **The enhanced (revised) risk management system currently being required by the Banking Regulators**
- **Newly identified operational risks**

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  - Audit
  - Business Continuity Planning
  - Development and Acquisition
  - E-Banking
  - Information Security
  - Management
  - Operations
  - Outsourcing Technology Services
  - Retail Payment Systems
  - Supervision of Technology Service Providers
  - Wholesale Payment Systems

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**Questions ???**