Federal Financial Analytics, Inc.

TOUGHEN EMBEDDED EXAMINERS, PETROU TELLS REGULATORS

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"Big, bad banks must be disciplined quickly or, like children, they'll just get badder as they get bigger."

Washington, D.C. – In remarks today before a closed-door meeting of bank supervision managers, Federal Financial Analytics' Managing Partner Karen Shaw Petrou warned against the coziness that can occur between big banks and their examiners. "The agencies are taking increasingly tough action against smaller institutions," Petrou said, "but big banks subject to harsh public scrutiny and considerable reputational risk may seem invulnerable to sanction." "Perhaps some of the public attention – including possible actions by non-bank regulators – are wrong-headed," she continued, "but toughness at top levels is vital in big banks when sanctions are warranted. Without meaningful, early action, problems can only get worse in an industry founded on public confidence."

Petrou spoke before the annual session of bank supervision managers at the Office of the Comptroller of the Currency. The OCC supervises many of the nation's largest banks, as examiners wrestle with an array of risks that affect both safety-and-soundness and compliance in such critical areas as money laundering, tying and fair lending. Petrou said, "there is a widespread perception that the agencies – all of them, not just the OCC – are loath to do anything public about the nation's biggest banks because of possible systemic risk. However, the cloak of invincibility can shield institutions from appropriate sanction to the point at which they take undue risk. Smaller, targeted and public action promote the market discipline regulators espouse and they are essential at all banks, including the very biggest ones."

Petrou specifically suggested focusing supervisory action on simple and accountable steps, not burrowing down into the details of examiner handbooks appropriate to more junior-level compliance personnel. "Big bank boards and senior management have to know that acquisitions will be denied, new ventures limited and other franchise-value steps taken if supervisors want effective risk management. This includes basic steps like mandating independence of risk management from business units and requiring compensation structures that promote compliance as well as other corporate priorities."

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