

# Bank Insurance & Securities *Marketing*



## U.S. Bank's 'Up Market Strategy'

Mark Jordahl (l.),  
President, U.S. Bank  
Wealth Management Group

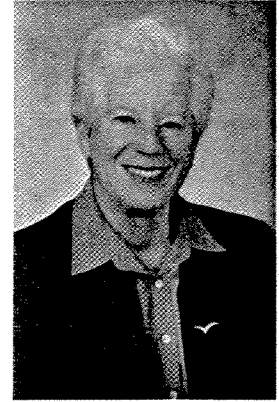
William Benjamin, CEO,  
U.S. Bancorp Investments, Inc., and  
U.S. Bancorp Insurance Services, LLC

Plus!

A 'Frenzy'  
for Hybrid  
Long-Term  
Care Insurance

Commerce  
Bank's B/D  
Embraces  
Managed Accounts,  
Life Insurance

Bank Insurance & Securities Marketing  
is a publication of the  
Bank Insurance & Securities Association



# RISKY BUSINESS

BY KATHLEEN W. COLLINS

**A**SSUMING THAT readers are as tired of reading articles about the Dodd-Frank Act as we are of writing them, this column will take a summer vacation from Dodd-Frank and focus on a seemingly mundane compliance issue – managing third-party risk.

If mounting examination criticism focused on the failure of banks to properly oversee their vendors wasn't enough, the banking agencies have recently cited the failure to effectively manage third-party vendors in several high profile enforcement actions taken against banks as to their foreclosure processing activities. This was not the first, nor will it be the last, time that third-party vendor management issues form the basis for serious regulatory charges.

The regulatory guidance giving rise to these charges has been in place for years, and regulators began examining for compliance with it several years ago. Given the prevalence of third-party vendor relationships in the securities and insurance sales arena, BISA has long focused on the topic at its Legal, Regulatory and Compliance Conferences, as well as in its comments on proposed regulations.

## Establishing standards for third parties

As early as 1994, in the Interagency Statement on Retail Sales of Nondeposit Investment Products, the federal banking agencies warned depository institutions to observe certain standards before and

*Kathleen W. Collins is a partner in Morgan, Lewis & Bockius, and Washington Counsel of the Bank Insurance & Securities Association. She and Richard Starr write the "From Washington" column in alternate issues.*

during arrangements with third parties that might sell or recommend nondeposit investment products on the premises of the institution, or in sales resulting from a referral of retail customers by the institution to a third party when the depository institution receives a benefit for the referral. The Interagency Statement warns banks to (1) conduct an appropriate review of the third party prior to entering into the arrangement; (2) have a written

---

## Three federal banking agencies issued guidance this past decade on managing risks associated with a bank's use of third parties to perform functions on the bank's behalf.

---

agreement with the third party that is approved by the bank's board of directors; (3) include provisions addressing topics like access to records and indemnification in the written agreement; and (4) periodically monitor compliance by the third party with the written agreement.

In 2000, when the federal agencies adopted final regulations addressing Consumer Protections for Bank Sales of Insurance as mandated by the Gramm-Leach-Bliley Act, they included certain third parties as "covered persons" obliged to observe the regulations ("Any other person only when the person sells, solicits, advertises or offers an insurance product or annuity to a consumer at an

office of a bank or on behalf of a bank").

Over time, the banking agencies have refined and broadened the scope of their third-party guidance. Three federal banking agencies issued guidance this past decade on managing risks associated with a bank's use of third parties to perform functions on the bank's behalf, to provide products and services that the bank did not originate, or to "franchise" the bank's attributes. The Office of the Comptroller of the Currency (OCC), the primary regulator for national banks, has issued OCC Bulletin 2001-47; the Office of Thrift Supervision (OTS), the primary regulator for federal thrifts until July 21, 2011, when its responsibilities as to federal thrifts will be assumed by the OCC, has issued Thrift Bulletin 82a; and the Federal Deposit Insurance Corporation (FDIC), the primary federal regulator of state, non-Federal Reserve member banks, and soon-to-be regulator of state savings banks, has issued Financial Institution Letter 44-2008.

## Four phases

The agency guidance basically breaks down into four phases: (i) risk assessment and strategic planning; (ii) due diligence in selecting a third party; (iii) contract structuring and review; and (iv) oversight. Regulators in recent examinations have focused on this fourth element, noting that active oversight of third-party vendors is required by this guidance. Regulators report that many older third-party agreements that have been extended over the years have not been updated and amended to reflect agency guidance, resulting in regulatory criticism. A failure to adhere to this regulatory guidance has been cited in formal regulatory agreements as one

*Continued on page 49*

about new products, strategies, and economic forecasts. These are the keys to engagement.

Much has been written over the years about FAs building relationships with “centers of influence”—attorneys, accountants, and other professionals who are in a good position to make referrals. Engagement is more important with these people than it is with an average client. After all, not only are centers of influence putting their personal reputation at risk when they make a referral, but also their professional standing and their own relationship with the person being referred. It’s unrealistic to think that if an FA gives a stack of business cards to an attorney or accountant that they will just give them to their clients without knowing the FA or the FA’s business. Why would they risk so much?

### The rewards

The Advisor Impact study found that the fundamental reason clients made referrals was the “law of reciprocity”—58 percent of clients gave referrals because the FA had done a good job, and the client wanted to repay the favor. Clients also recommended the FA to friends who had a financial need, and the client wanted to help the friend (not the FA). Sometimes a friend or associate will actually ask your client for a referral. You want your clients to give you an enthusiastic recommendation—not just say, “My advisor’s OK.” And these referrals have a way of expanding. Your client makes a referral, the referred client has a retirement plan and custodial accounts for her kids, and she has a friend with a problem, and so on.

Of course, you get more from an engaged client than just referrals. You get their candor about the job you’re doing, something that helps you to focus and understand what is truly valuable to your clients. You can better spend your time and energy on

what works and stop doing what doesn’t. And you get loyalty. You may change firms some day.

### The obstacles

Time is your constant enemy. There just isn’t enough time to do all the things that must be done each and every day. And clearly time management is a critical skill for successful FAs. But given the importance of having engaged clients, you need to find the time to focus on communicating with clients. Use time management techniques to reserve time every day, week, and month. Research has shown that you’re better off focusing on your best relationships and new ones with potential rather than trying to repair or fix existing relationships with unhappy clients. Memories are long when it comes to errors, mistakes, or hard feelings.

Don’t think that if you’re just nice to your clients, talk to them often and keep them informed, you’ll become fully engaged. It takes time, hard work, and a comprehensive understanding—not just of the client’s needs, but of the products, strategies, and programs that meet and exceed their financial needs.

### Just do it

While it won’t happen overnight, engaged clients will make quality referrals. You can still try the old line with your clients: “You know I’d be happy to help any friends or associates you have that could benefit from my financial guidance, and I am opening my business to a limited number of new clients. Do you know anyone I can contact?”

But the evidence shows this is pretty useless most of the time. Your engaged clients are your best promoters, and given the chance, they will sing your praises. All it takes is someone to ask them. □

---

## FROM THE STATES

*Continued from page 8*

sioners’ regulatory authority and are instead regulated by the Securities & Exchange Commission (SEC) and the Financial Industry Regulatory Authority (FINRA).

It is important to note that the life insurance industry as a whole believes that stranger-owned life insurance damages the reputation of legitimate producers and brokers. Since most life insurance policies lapse and do not result in a claim, the industry also has a financial interest in preventing STOLI contracts—if life insurers pay out more death claims than anticipated, they could be forced to raise premiums. Therefore, associations such as the American Council of Life Insurers (ACLI), National As-

sociation of Insurance and Financial Advisors (NAIFA), and the Association for Advanced Life Underwriting (AALU) are leading the fight to create laws that prohibit these transactions.

### Road Ahead

As over half of the states have already enacted laws prohibiting or restricting STOLI transactions, it appears clear that the scales have decidedly tipped in that direction. What will be more interesting to monitor as time goes on will be whether states begin to test their authority in regulating additional products, such as STOA (mentioned above). While the NAIC has concluded that this would be overreaching, we have seen the states make these attempts in the past, and we should not be surprised if it happens in the future. □

---

## FROM WASHINGTON

*Continued from page 6*

of the justifications for the enforcement action.

As an example of what a bank regulator expects in this regard, here is the OCC’s guidance as to the proper oversight of third-party relationships:

After entering into a contract or agreement with a third party, management should monitor the third party with respect to its activities and performance. Management should dedicate sufficient staff with the necessary expertise to oversee the third party. While the extent of a bank’s oversight activities will vary depending on the nature of the activity, the oversight program should monitor the third party’s financial condition, its controls, and the quality of its service and support.



The OCC expects that a bank's policies and procedures should incorporate its regulator's expectations as to the appropriate oversight of all of its third-party relationships.

The OCC expects a dynamic risk management process over third-party arrangements at the banks it supervises, with the board of directors actively involved in the entire process. Its examiners have been instructed to review business plans for significant new products using third parties, the results of due diligence reviews, material contracts with third parties, management information systems of third parties, and information provided to the board of directors reflecting the results of management's ongoing monitoring activities. Examiners are instructed to criticize banks whose third-party activities pose undue risk or whose risk management systems over such activities are inadequate or ineffective.

The OCC has used its third-party guidance as a partial basis of a Consent Order as early as January 2005 when a national bank's board of directors was ordered to ensure that third-party consultants would be subject to oversight and coordination by bank management and would be subject to appropriate con-

tractual arrangements and OCC guidance related to third-party relationships.

The FDIC has entered an Order to Cease and Desist against a bank for failing to appropriately monitor and/or manage third-party risk, and for operating in contravention of its third-party risk guidance (April 2009). A Consent Order obligated a bank to develop and maintain effective monitoring, training, and audit procedures to ensure proper management of third-party risk in accordance with its risk guidance (November 2009).

In the recent mortgage foreclosure formal enforcement actions, the Federal Reserve, the OCC, and the OTS focused on third-party vendor management, and in an Interagency Review of Foreclosure Policies and Practices found that "Failure to effectively manage third-party vendors resulted in increased reputational, legal, and financial risks to the servicers."

The upshot of these continuing issues with third-party relationships will eventually be the dreaded onset of yet another set of regulations, a set not precipitated by Dodd-Frank, but rather inattention to a building drum beat of concern by bank regulators. □

## U.S. BANK

*Continued from page 14*

life revenues are from "underwritten insurance" (in contrast to simplified issue life insurance) used primarily for wealth transfer purposes—whole life, universal life, and variable universal life insurance.

What percentage of overall B/D revenues is from life insurance? Benjamin wouldn't specify. But if 5 percent is considered good for an active bank program, then U.S. Bank is "significantly above that," Benjamin told us.

### Tapping the mass market

Benjamin's group also supports the institution's "mass market" (i.e., clients with less than \$100,000 in investable assets) brokerage efforts. The bank has been developing a three-pronged strategy for the mass market: a) Internet distribution, b) call center manned by Series 7-licensed advisors, and c) the branch-based platform bankers.

U.S. Bank has 300 licensed bank employees (LBEs) who sell fixed annuities and mutual funds, focusing on retail customers. U.S. Bank once had many more LBEs—closer to 1,200. What happened? In recent years, U.S. Bank has posted some very "aggressive" CD rates in an effort to gather more deposits (unlike many institutions that have been shedding deposits recently), Benjamin recounts. The bank's platform personnel had their hands full with those CDs. Investment product sales became less of a priority.

### An IBM veteran

Financial services is Benjamin's second career. He took a job with IBM out of college, and went through that company's training program. Although he had a "great time" at IBM, when he later attended the University of Minnesota's Carlson School of Management, he became friendly with a classmate who worked at an investment bank, was intrigued by investment banking, and decided to change industries. He went to work for Piper Jaffray after securing his MBA, working mostly on the

BISA Advisory Board			
Dan Overbey, Chairman, BankUnited Investment Services			
Dan Arnold	LPL Financial Institution Services	Kevin Kennedy	AXA Distributors, LLC
Steve Becker	Principal Financial Group	Rich Koll	Essex National Securities, Inc.
Dean Borgh	Wells Real Estate Funds	Mike Korthaus	Protective Life Insurance Company
Wilbur Bullen	Jackson National Life	Rich Lavoie	Symetra
Robert Burnett	MetLife Investors	Frieda Lewis	Broadridge Financial Solutions, Inc.
Keith Burger	SunAmerica Retirement Markets	LeAnn McCool	PrimeVest Financial Services, Inc
Lewis Carlisle	CD Funding Group	Kevin Mummau	CUSO Financial Services, LP
Tyler Carr	John Hancock	Tom Olson	Lincoln Financial Group
Chris Coudret	The State Life Ins. Co., A OneAmerica Co.	Tom Pellowe	Dividend Capital
Steve Dowden	INVEST Financial Corp.	John Phillips	National Financial, a Fidelity Investments Co.
Randy Gabrielson	Allianz Life	Wendy Schmidt	Pershing LLC
Mark Gempler	Forethought Financial Distributors	Craig Simms	Vantislife Insurance Company
Dave Giertz	Nationwide	Peter Stahl	Hartford Life Distributors
John Gies	Prudential Financial	Liza Tyler	New York Life Insurance Company
Tracy Giffen	Sun Life Financial Distributors	Anthony Vossenber	Genworth Financial
Gregg Johnson	Securities America		