Optimizing Compliance Staffing

Financial institutions, particularly large ones, are responding to a prolonged wave of new rules and regulations by evaluating whether the staffing and skills of their compliance functions are sufficient to meet heightened regulatory expectations.

The industry has made substantial progress in its broad reconsideration of the role of compliance. But in some cases, financial institutions have boosted the size and capability of the compliance function at the corporate level, only to find that its business lines also have critical needs. In other cases, financial institutions have completed multiple iterations of a compliance build-out but still face shortcomings in staffing and skills.

These missteps can be particularly costly given the earnings challenges confronting many financial institutions. As regulatory expenses increase and revenue growth is difficult to find, financial institutions are challenged to ensure that non-interest expenses, including compliance-related costs, are put to best use. Finding the balance between budget constraints and necessary compliance investments is critical to meeting business and regulatory objectives.

Financial institutions can best navigate these challenges by:

- Determining responsibilities and staffing for business-line compliance
- Meeting new skill requirements
- Quantifying workloads and resource needs
- Using benchmarks
- Preparing for internal and external oversight

**DETERMINING RESPONSIBILITIES AND STAFFING FOR BUSINESS-LINE COMPLIANCE**

The compliance function is most effective when corporate and business-line activities are well-coordinated. Many financial institutions are turning their attention to the business line after devoting substantial resources to corporate activities in recent years. Building out business-line compliance capabilities, while re-balancing responsibilities and resources shared at the corporate level, will likely continue in the next several years. That priority is partly due to financial pressure and partly due to regulatory mandate — particularly as laid out in the Office of the Comptroller of the Currency’s

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1 Business line is equivalent to front-line unit as defined by the Office of the Comptroller of the Currency in its final rule establishing heightened standards. This definition includes any unit that generates revenue or reduces expenses, provides support or servicing to units that deliver products or services to customers, or provides technology services to a unit subject to the OCC’s guidelines, provided that such unit is also accountable for risk.
final rule establishing heightened standards. “Banks whose business leaders viewed themselves as accountable for the risks created through their activities fared better in the crisis than banks where accountability for risks were shared among multiple organizational units,” the OCC wrote in its final rule.

Savvy financial institutions have recognized that these first-line-of-defense compliance functions pose their own resource and skill challenges. A critical first step in addressing these challenges is to put together a detailed look at the specific responsibilities that are best handled within the business and those that are best handled at the corporate level (see Exhibit 1 for a high-level perspective on these two lines of defense). This detailed inventory should identify required compliance activities, assign responsibilities, and describe resource allocation. Beyond describing tasks and responsibilities, the inventory should make clear how the lines of defense fit within a logical and consistent framework.

A systematic approach to putting together the inventory supports the best use of a company’s resources. Any gaps between the lines are put in stark relief, pointing the way to needed investment; this approach can also help managers find redundancies and, just as important, determine whether the redundancies are appropriate to make sure risk is mitigated, or represent truly extraneous expenditures that can be eliminated. The inventory will inform resource planning at both the business-line and corporate level.

Implementing this type of responsibility framework may be more difficult than it appears. Business lines are often unprepared to assume more extensive responsibilities for compliance — their procedures, controls, and testing groups tend to focus on operations, and depend upon corporate compliance for regulatory expertise. For its own part, corporate compliance wrestles with its challenge role. How does it remain sufficiently engaged in the details of business-line activities and procedures to challenge them? How much testing and validation is appropriate?

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The right model may require some institutions to make dramatic changes in skills and staffing. Resource-intensive control and testing activities may shift from the second to the first line of defense, while the second line’s challenge role demands more seasoned personnel who can judge when to dig deeper or raise a red flag.

The alignment of business-line and corporate functions depends on individual institutions’ organization models and will evolve as financial institutions experiment and as regulators institute their heightened expectations and standards in examinations.

**MEETING NEW SKILL REQUIREMENTS**

Banks have generally shored up compliance expertise in disciplines that have been of intense interest to regulators, including consumer protection, anti-money-laundering, and fair lending. However, the need for additional competencies has in some cases gone unaddressed, and increasingly, these other functional skills and experience are essential to an effective and cost-efficient compliance function.

For example, regulatory expectations for AML and sanctions compliance have led to significant increases in the number of alerts requiring manual review. Operations managers who are skilled at managing work flows and making just-in-time resource adjustments save money and mitigate risk by handling spikes in alert volumes while maintaining policy-mandated turnaround times and quality standards. Similarly, the scope and volume of compliance testing have expanded as regulators focus on consumer protection. Audit managers with knowledge and experience in statistical sampling, control testing, and test documentation contribute to the design and management of efficient testing programs that work.

Compliance personnel with large-scale project-management experience can lead major efforts and contribute to the effective use of external resources by sharing their organizational and institutional knowledge. Technology-savvy compliance personnel who understand the IT systems architecture, and know how compliance systems integrate with core business applications, can work with IT and external consultants to steer development efforts. IT experience is also increasingly valuable as banks seek to rely more heavily on automated, rather than manual, compliance monitoring and testing.

Business knowledge and experience are also more important than ever. Compliance professionals must advise business leaders on regulatory considerations of the design, marketing, and delivery of products and the development of new businesses and strategies. Compliance partners who know the business and are sensitive to its leaders’ concerns will be the most effective in carrying out the function’s responsibility.

Exhibit 2 highlights typical compliance activities and skills required for their effective execution.

Structured, objective assessments are useful in confirming that the skills of compliance personnel keep up with demanding requirements. Side-by-side comparisons of skills required and skills possessed by specific employees will identify key gaps and help with planning to address them. Financial institutions that have already invested in strengthening skills related to consumer compliance, third-party risk management, and quantitative analytical modeling can use a skill assessment to verify the effectiveness of those investments. Are individuals with specific skills in the jobs that most demand them? Do skill gaps persist, and if so, are they best addressed by hiring, training and development, or by internal transfers?
Skill assessments risk becoming mired in other personnel-management matters; involving the human resources department can be helpful in structuring a fact-based assessment and in assuring a level of independence. Job descriptions and individual biographies provide baseline information about skills required and possessed, and should be supplemented by managers’ first-hand knowledge of skill levels and competencies. Any resulting development plans should be tangible and actionable.

### QUANTIFYING WORKLOADS AND RESOURCE IMPLICATIONS

Determining how many people are needed at each level and explaining the basis for determinations are often the most challenging aspects of compliance staffing. Financial institutions increasingly use staffing models annually to provide a quantitative underpinning to their overall assessment and help executives analyze time spent on similar activities across the organization. Companies typically support these comparisons by breaking down roles and responsibilities for each compliance activity, and estimating the units of work required to complete them. Structuring models in this fashion promotes meaningful discussions about the business or environmental changes that are most likely to drive compliance resource requirements.

For example, resource requirements for compliance testing or quality-assurance work can be quantified by tracking and reviewing time-per-file information and evaluating it against the testing schedule. Some institutions also track volume, as well as time spent on reviewing marketing materials, providing

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<table>
<thead>
<tr>
<th>EXHIBIT 2 — COMPLIANCE RESPONSIBILITY SKILLS</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>RESPONSIBILITIES</strong></td>
</tr>
<tr>
<td><strong>Risk Oversight and Reporting</strong></td>
</tr>
<tr>
<td>• Oversee and support business-line compliance risk management</td>
</tr>
<tr>
<td>• Monitor and report on compliance risk levels and material compliance risks</td>
</tr>
<tr>
<td>• Conduct periodic compliance risk assessments and develop risk mitigation plans</td>
</tr>
</tbody>
</table>

| **Control Processes and Testing**          |
| • Administer enterprisewide compliance risk management and control processes |
| • Advise business-line compliance risk management and control processes |
| • Conduct independent testing of compliance with laws and regulations |

| **Issue and Initiative Management**        |
| • Oversee and support the resolution of compliance issues |
| • Oversee and support the implementation of changes to meet new legal requirements |

| **Compliance Program Administration**      |
| • Manage enterprisewide compliance policies and procedures |
| • Manage enterprisewide compliance training and awareness programs |
| • Support and oversee business-line compliance program activities |

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examination support, and evaluating responses to escalated customer complaints. Institutions can also use the model to perform sensitivity analyses of the resource impact of workload changes such as increases in AML alerts as a result of recalibration, transferring compliance-monitoring activities to the business lines, or expanding the scope of compliance testing. An effective staffing model can also measure how major strategic initiatives — acquisition of a new business line, expansion into new overseas markets, launching a new product, etc. — will affect the compliance functions. Although some compliance activities are difficult to quantify, implementing a resource model can be crucial in making sure that compliance functions are appropriately funded.

Staffing models vary in sophistication. Exhibit 3 is a high-level model that estimates staffing for a business-line compliance function. Within each major work area, the model estimates annual work hours for major activities based on workload assumptions. For example, the model estimates hours required for business self-testing execution based on the number of test scripts, the average number of questions per script, and the annualized hours required to answer an individual question — an estimate based on the frequency of testing, test sample sizes, average answer time, and a productivity factor. It then converts annual work hours into full-time equivalent resources, factoring in vacation days and administrative requirements. The model also distinguishes one-time from ongoing activities so departments can budget appropriately.

EXHIBIT 3 — SAMPLE HIGH-LEVEL STAFFING MODEL

<table>
<thead>
<tr>
<th>Work Area</th>
<th>Work Driver Activities</th>
<th>Workload Assumptions</th>
<th>Estimator Results</th>
<th>Resource Type</th>
</tr>
</thead>
<tbody>
<tr>
<td>Risk Assessment</td>
<td>Risk and Control Mapping (New Business Function)</td>
<td># of Mapping Units</td>
<td>Elapsed Days / Unit</td>
<td>Resources / Unit</td>
</tr>
<tr>
<td></td>
<td></td>
<td>10</td>
<td>8</td>
<td>3</td>
</tr>
<tr>
<td></td>
<td>Risk and Control Mapping (Update)</td>
<td># of Mapping Units</td>
<td>Elapsed Days / Unit</td>
<td>Resources / Unit</td>
</tr>
<tr>
<td></td>
<td></td>
<td>100</td>
<td>8</td>
<td>3</td>
</tr>
<tr>
<td></td>
<td>Risk Assessment Support</td>
<td># of Assessment Units</td>
<td>FTE / Unit</td>
<td>61,013</td>
</tr>
<tr>
<td></td>
<td></td>
<td>110</td>
<td>0.33</td>
<td></td>
</tr>
<tr>
<td>Monitoring</td>
<td>Enhanced Monitoring</td>
<td>2013 FTE</td>
<td>Incremental Volume</td>
<td>9,984</td>
</tr>
<tr>
<td></td>
<td></td>
<td>4</td>
<td>50%</td>
<td></td>
</tr>
<tr>
<td>Business Self-Testing</td>
<td>Test Development (New QA Function)</td>
<td># of New Scripts</td>
<td>Elapsed Days / Script</td>
<td>Resources / Script</td>
</tr>
<tr>
<td></td>
<td></td>
<td>4</td>
<td>30</td>
<td>2</td>
</tr>
<tr>
<td></td>
<td>Test Execution</td>
<td># of Total Scripts</td>
<td>Avg Questions / Script</td>
<td>Hrs / Questions / Yr</td>
</tr>
<tr>
<td></td>
<td></td>
<td>16</td>
<td>10</td>
<td>23</td>
</tr>
<tr>
<td>Other Initiatives</td>
<td>Third-Party Risk Management</td>
<td># of Third Parties</td>
<td>Elapsed Days / Party</td>
<td>Resources / Party</td>
</tr>
<tr>
<td></td>
<td></td>
<td>22</td>
<td>5</td>
<td>1.5</td>
</tr>
<tr>
<td></td>
<td>Lending Disclosures</td>
<td># of Disclosures</td>
<td>Elapsed Days / Unit</td>
<td>Resources / Unit</td>
</tr>
<tr>
<td></td>
<td></td>
<td>100</td>
<td>0.25</td>
<td>2</td>
</tr>
</tbody>
</table>

Total One-Time Resources: 3,840 2
Total Ongoing Resources: 95,651 57
**USING BENCHMARKS**

Benchmarks provide a reality check once preliminary staffing estimates are developed. Internal benchmarking may include comparing the estimates for similar activities (for instance, time or resources dedicated to risk assessments) across different compliance units to find outliers.

Peer benchmarking is also valuable, as long as financial institutions normalize the data and adjust for the differences in organizational models or definitions. For example, corporate compliance at some institutions may include Bank Secrecy Act/AML or legal, while in other institutions those functions may reside elsewhere. Relevant and timely information about peers can be hard to find. Some institutions depend upon industry studies or facts gleaned from other public sources, but information gathered through peer contacts and customized surveys is frequently more useful and current. Confidentiality concerns can typically be overcome by assuring anonymity of survey participants.

**PREPARING FOR INTERNAL AND EXTERNAL OVERSIGHT**

Bank CEOs, enterprise risk committees, and boards are keenly interested in getting compliance staffing right — for both regulatory and financial reasons. Increasingly, inquiries go beyond traditional annual plan and budget information to include documentation of compliance resource plans and information about how the bank’s plans stack up against peers.

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### EXHIBIT 4 — STAFFING ASSESSMENT APPROACH

#### Preassessment Information Gathering

- **Document roles and responsibilities**
  - Current state as well as anticipated changes for each unit

- **Gather baseline staffing information**
  - Current headcount and approved open positions
  - Employee information—rosters and biographies

#### Skills Assessment

- **Identify skill requirements for each task**
  - Consider biographies and first-hand experience
  - Focus on skills rather than performance
  - Identify skill-development plans, where appropriate

- **Assess individuals**
  - Consider biographies and first-hand experience
  - Focus on skills rather than performance
  - Identify skill-development plans, where appropriate

#### Staffing Model Development

- **Determine basis for estimating resources for each task**
  - Create an assumptions-based model
  - Gather work-driver volume, time required, and other information
  - Adjust and refine model; perform sensitivity analysis

#### Benchmarking

- **Checkpoint findings against industry and peer benchmarks**
  - Roles and responsibilities; staffing and skill requirements
  - Even macro comparisons are helpful
Financial institutions should also be prepared to demonstrate to regulators how they have determined the adequacy of their staffing levels and skills. The OCC’s heightened standards and other regulatory guidance regarding enterprise risk management hold senior management and the board accountable for having the right compliance talent, tailored to the size and complexity of their institution’s operations and practices. Given these expectations, supervisors are beginning to strengthen their oversight of compliance staffing to satisfy themselves that institutions have sufficient resources and skill sets to manage their risks.

CONCLUSION

Some financial institutions have built a structured and repeatable compliance staffing assessment linked to the annual compliance planning and budgeting processes. Assessments employ a systematic and rigorous approach as illustrated in Exhibit 4.

These assessments yield valuable information for leaders in the compliance function, as well as for the CEO, enterprise risk committee, board, and regulators. A structured assessment can transform annual budget negotiations from “trust me” conversations based largely on judgment and experience into fact-based discussions about how changes in activities, work drivers, and processing times affect compliance resources. Assessment information, particularly trends in work units and processing times, can also aid budget discussions and, ultimately, help to ensure compliance functions are both right-sized and appropriately skilled.

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