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## **Bank Use of Independent Consultants**

Yesterday the Office of the Comptroller of the Currency (the “OCC”) published guidance for bankers on the use of independent consultants. Consultants have become punching bags for regulators and politicians in part due to the outsize fees charged to the banking industry but also a perception that there is a lack of independence that may affect the quality of work performed. The regulators are the architects of the issues because they often require banks to hire consultants or impose such stringent requirements for expertise that bank management turns to outside “experts” instead of bank staff. Internal audit is an example of an area where banks are driven to hire “outside internal” auditors.

### **What does the guidance cover?**

It only covers situations where the OCC requires a bank to employ an independent consultant as part of an enforcement action to address significant violations of law, fraud or harm to consumers. It does not apply when the OCC requires a bank to hire a consultant to provide expertise needed to correct operational or management deficiencies.

### **What do the regulators want banks to do when using consultants generally?**

Always conduct appropriate due diligence to ensure that an independent consultant performing a functional engagement has the necessary expertise and resources to provide the needed services.

### **Does hiring a Consultant insulate Bank Management?**

No, using a consultant does not absolve bank management or a bank's board of directors of their responsibility for ensuring that all needed corrective actions identified in a supervisory action are identified and implemented.

### **How are lawyers treated?**

Lawyers are not mentioned—so banks are free to continue to hire unqualified lawyers.

### **What are the key factors the regulators look at when reviewing a Consultant?**

Once the OCC has determined that a consultant is needed, the OCC requires the bank to submit information regarding the bank's due diligence, including the proposed independent consultant's qualifications and the terms of the engagement. This requirement allows the OCC to assess whether the bank has conducted appropriate due diligence in selecting the consultant and whether the independent consultant has the requisite independence, and whether the work plan is consistent with the consultant's expertise and the enforcement action.

### **What Due Diligence is needed?**

A bank must do extensive due diligence before recommending the use of a consultant. At a minimum this includes: qualifications, independence, resources, expertise, capacity, reputation, information security and document custody practices, risk management and reporting, conflicts of interests, and financial viability of the consultant the bank considered. The bank should also require the independent consultant to disclose any professional disciplinary actions.

### **What is Appropriate Independence of a Consultant?**

The goal is to insure the Consultant's work is done with a high level of objectivity such that the results of the engagement are free of any potential bias and that the work is based on the consultant's own independent and expert judgment. The Consultant may not have any direct conflicts—i.e. the engagement may not involve a review of a policy that the Consultant helped draft. The Bank must insure the

consultant does not have a direct or even indirect conflict of interest. While the OCC does not define such indirect conflicts, they suggest that even a “potential for an appearance of a conflict of interest” could be a disqualifier.

The bank must assess all existing or prior relationships with the bank, including with affiliates or insiders and the amount of fees paid to the consultant and the percentage of total revenue of the Consultant. This includes personal relationships with the Bank’s Board and executive officers. If the Bank has employed any staff of the Consultant, that must be disclosed. The bank must disclose all assignments given to the consultant over the last 3 years. Too many assignments for the same bank may cause an “inherent conflict of interest.”

The Bank has to disclose what other consultants they evaluated for the job. If there were potential independence issues, how would they be mitigated—such as through a “Chinese wall”.

### **What should be in the Engagement Letter?**

A description of the Consultant’s expertise must be included as well as the resources to be deployed by the Consultant. Mandatory provisions in the contract include: privacy protections, record keeping, access by the regulators, what disputed matters will be disclosed to the OCC, how the OCC can have independent access to the Consultant, any material changes have to be approved by the OCC and subcontractors need to be vetted and approved by the OCC.

### **How will the OCC Monitor the Engagement?**

As part of reviewing how the enforcement action is being handled, the OCC will also plan on timely monitoring of the consultant’s work. The extent of oversight will depend on the complexity of the consultant’s engagement.

When the consultant produces the final report to the Bank’s Board, the OCC will review the report to insure that all supervisory matters were adequately addressed.

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