Disclosures Matter!

A Whitepaper written by Apogee Process Improvement

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1. Introduction

In theory, customer-facing Disclosures are simple – tell your customers what is required by law, regulation, or rule and make certain your processes match your Disclosures. Well, that's theory and as the great philosopher Yogi Berra once said, "In theory, there is no difference between theory and practice – in practice, there is."

When the first Disclosures were mandated as part of the Federal Reserve Act in 1918, there was a single US Banking regulator with a handful of regulations, regulating limited products and customer communications changes. Today, financial institutions have more than a dozen regulators, hundreds of regulations and rules, a plethora of products, and more customer communication channels than could be imagined a century ago including television, ATM screens, internet, mobile/SMS, and social media. In practice, managing Disclosures has not been an easy task for several decades.

2. So why does the present Disclosure situation matter?

It all starts with the customer. Clear and accurate Disclosures matter to our customers. Also, with the creation of the CFPB, confused and angry customers have more power than ever to hold financial services firms accountable.

Since its inception, the CFPB has fined financial institutions for negatively impacting consumers. While these large fines are unfortunate, they seem to be the most effective way to drive operational changes. Since its inception in 2011, the CFPB has levied more than $20 billion in consumer relief and fines – many of which had Disclosure shortcomings identified as part of the fine explanations.

From 2016-2021, the CFPB was relatively quiet, with consumer relief actions totaling $800MM or less per year. However, since the appointment of Rohit Chopra in late 2021, things have changed. In 2022, the CFPB's consumer relief actions totaled $2.4 billion – triple the cost of any of the previous six years. We should expect this level of enforcement action to continue.

Here are a few recent Disclosure-related CFPB headlines:

- *"CFPB Orders Atlantic Union Bank to Pay $6.2 Million for Illegal Overdraft Fee Harvesting" (December 2023)*

  Disclosure reference: "The CFPB found that Atlantic Union misled consumers who enrolled in this overdraft service by phone and failed to provide proper disclosures."

- *"CFPB Orders Leasing Company Tempoe to Provide $36MM in Penalties and Relief for Tricking Consumers and Hiding Contract Terms" (September 2023)*

  Disclosure reference: "…for tricking consumers into expensive leasing agreements by concealing the contract terms and costs, and failing to provide legally required disclosures."

- *"CFPB Orders Installment Lender OneMain to Pay $20 Million for Deceptive Sales Practices" (May 2023)*

  Disclosure reference: "…employees obscured written disclosures from consumers' view, or verbally contradicted them."

Oftentimes, a regulatory fine is a small fraction of the overall cost to the financial institution. A Chief Operations Officer at a $40+ billion bank stated the true cost of their Disclosure issue was at least three times the cost of the regulatory fine. The bank had spent roughly an equal amount to investigate and defend its actions, using internal operational, compliance and legal resources and outside counsel. It also spent an equal amount to remediate its previous actions. The reputational damage was significant, but not quantified.

3. As an industry, what should we do?

Financial services companies need to get a complete handle on the WHAT, WHY and WHERE of Disclosures. It's a simple statement, but very difficult to make happen. Here are the details of the three steps…

1. WHAT are you communicating in your actual Disclosures (not in theory, but in practice)? Identify all Disclosure instances and eliminate unnecessary variations. You don't need ten unique versions of an e-sign agreement. Unnecessary variations increase legal, operational and reputation risk. Identifying and eliminating unnecessary Disclosure variations is known as rationalizing Disclosures. Through rationalization, expect to eliminate two unnecessary Disclosure versions for every one you keep.

2. WHY are you communicating this information to your customers? Link all perceived Disclosures to obligations required by laws, regulations, and rules (LRRs). If you are unable to link text excerpts to LRRs, then they are probably not Disclosures – they are most likely Disclaimers included to proactively avoid legal risk.

3. WHERE are you communicating this to customers? Identify all documents, messages, scripts, and so on containing customer-facing Disclosures. Logging Disclosures to communications is the final step in establishing ongoing traceability.

These three steps are required to create end-to-end control of your Disclosure processes. Similar to the way regulators expect LRR obligations to be mapped to processes, we should expect that in the not-too-distant future, regulators will expect LRR obligations to be mapped to Disclosures.

Unfortunately, many financial institutions do not proactively address the root causes of their Disclosure failures until after major fines are assessed. The tragedy is that customers and shareholders are both damaged in this situation – years of poor customer experience capped off by needless destruction of shareholder value by regulatory fines and unnecessary operational costs. Shareholders and financial institutions would profit if they *proactively* fixed their Disclosure environments and improved customer experience.

4. A Final Word

The complexity of the Disclosure environment continues to increase and so does the likelihood of being fined for non-compliance. As an example of the ever-evolving nature of Disclosures, the US is implementing ESG (Environmental, Social, Governance) Disclosures which will result in more potential fines for non-compliant financial services companies.

Rather than reactively addressing their current Disclosure environment after fines have been levied, companies should invest a fraction of the expected fines to create a world-class Disclosure environment based on rationalization and traceability. Remember, if you don't improve your Disclosure environment, it's not a matter of "if" you'll be fined, but "when" you'll be fined. And that's not theory.

About Apogee

Apogee Process Improvement consulting was formed to address specific needs within the highly regulated financial services industry. Given the continual changes in the regulatory landscape, it has become more important than ever to establish traceability and a solid change management process for all obligations.

At two of the largest four US banks, Apogee team members rationalized and established traceability of hundreds of Disclosures for the most problematic laws, regulations and rules in the US. These laws, regulations and rules were the source of 98% of Disclosure complaints, resulting in millions of dollars wasted on investigation and remediation.

Apogee's mission: **"Reduce reputational, regulatory and operational risk and costs, and improve customer experience for clients in regulated industries by creating world-class Disclosure environments."**

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