Trends in fair, responsible, and inclusive banking

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A majority of chief compliance officers (CCOs) polled by KPMG in 2023 anticipate a heightened emphasis on compliance due to growing regulatory expectations and scrutiny, with the primary push for improvement coming from their boards and regulatory authorities.

53%

Pressure to enhance compliance from boards

49%

Pressure to enhance compliance from regulators/examiners

34%

Pressure to enhance compliance from customers

27%

Pressure to enhance compliance from social policy/public perception

Source: KPMG Chief Compliance Officer Survey (2023)

Evolving regulatory landscape of fair, responsible, and inclusive banking

Over the past decade, regulatory changes, technology, and innovation have heavily shifted how financial services organizations operate, impacting how they offer, market, and service their products. Financial Services organizations have experienced structural transformation driven by digitization, where products and operations have experienced technological advancements. Simultaneously, digitizing and democratizing financial services have resulted in additional socio-political expectations requiring more access to financial information for customers and enhanced focus on social responsibility initiatives. The spotlight on fair, responsible, and inclusive banking practices has never been brighter.

Regulatory pressures

Regulators are increasing their enforcement and scrutiny of organizations, especially regarding consumer protection, accessibility, and discrimination. In October 2023, it was reported that the Consumer Financial Protection Bureau (CFPB) announced an increase in enforcement of 50 percent.[1] Proposed changes to the Unfair, Deceptive, Abusive Acts, and Practices (UDAAP) regulations under the Dodd-Frank Act, Community Reinvestment Act (CRA), Section 1071 of the Dodd-Frank Act, Web Content Accessibility Guidelines (WCAG), Americans with Disabilities Act (ADA) and Limited English Proficiency (LEP) guidelines are designed to enhance and promote equality in the products and services offered by organizations. Regulators have launched multiple initiatives around fairness as part of their emphasis on fair competition, which we highlight later.

73%

CCO's expect level of focus on compliance to increase.

Source: KPMG Chief Compliance Officer Survey (2023)

[1] Source: American Banker "CFPB plans to hire 50% more enforcement attorneys, support staff" (October 5, 2023)

Digitization and automation of processes and services

In parallel to digitizing products and services, the financial industry has increasingly adopted various innovative tools and technologies as cost-efficient methods for streamlining various processes and services offered. Automation has been integrated into decision-making processes, such as the Automated Valuation Model (AVM), which streamlines the home valuation process. Traditional customer support services have also been transformed through chatbots leveraging generative AI. While these algorithm-based technologies have brought many benefits, such as increased processing speeds and additional access to credit through alternative credit models, they also pose potential harm to consumers and create new risks that need to be managed and mitigated.

Digitization of financial products

Digitization of financial products allows financial organizations to expand their products, services, and business practices. As processes and products evolve, financial organizations should be aware of the implications of their new products and services for their customer base, particularly potential new risks that may impact customers disproportionately and/or unfairly. Additionally, demographic shifts lead to a greater consumer demand for financial products and services tailored to their unique needs and preferences. Through digitization, organizations can offer products and services that meet the needs of diverse customer populations, including socio-economic status, geographic location, all generations, all genders, racial and ethnic diversity, and any other considerations to foster greater access, trust, and loyalty.

Need for more accessible information

Consumer expectations have increased to request more control over their financial data. The emergence of open banking and proposed consumer data rights rules under section 1033 of Dodd-Frank have contributed to the changing landscape of organizations in which trust and transparency are critical factors in consumer decision-making. Current trends in consumer behavior suggest that consumers seek innovative and personalized banking options and demand transparency and security in managing their finances. Promoting fair and responsible banking practices and limiting barriers to access while prioritizing equal treatment is crucial so consumers can manage their finances and organizations operate in a way that benefits all consumers.

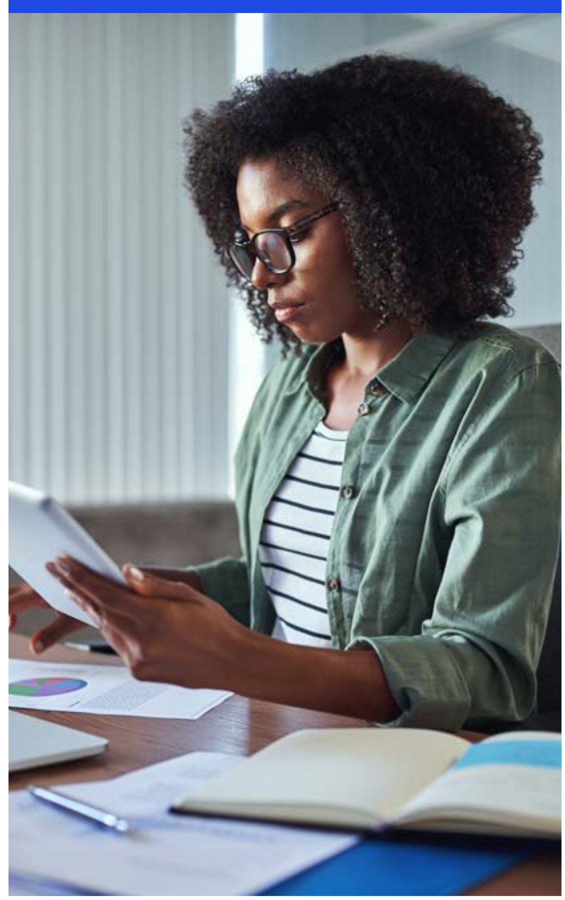
Where will banks invest?

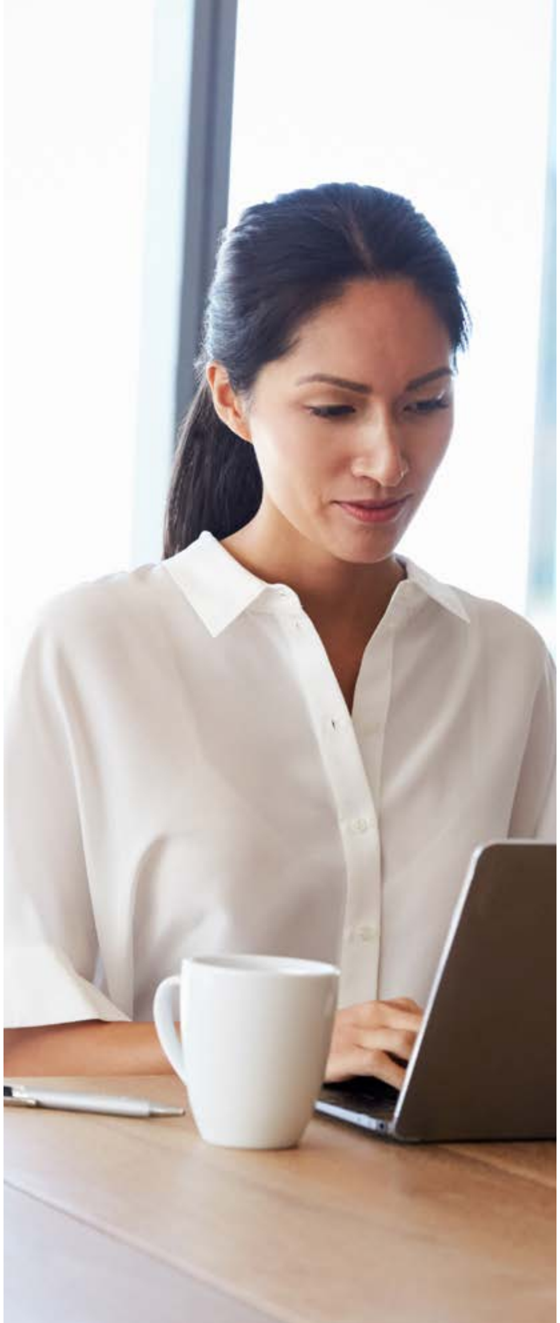
44%
AI/models

50%
Data analytics

61%
cybersecurity and data privacy

Source: KPMG Chief Ethics & Compliance Survey (2023)





71%

of CCOs say that new regulatory requirements and data analytics/predictive modeling for compliance monitoring pose the greatest challenge to their compliance efforts.

Organizations are expected to embody fair banking principles and stand by ethical banking practices. As regulations continue to evolve and the industry experiences digitization of products and services, organizations should consider remaining vigilant in balancing the benefits of technology with the potential harm to consumers. Furthermore, customer-centric approaches that consider the needs and preferences of diverse populations will be a critical success factor. Providing accessible information and promoting transparency and security should remain top priorities to promote consumer trust and foster equitable financial services.

Key areas for organizations to consider

Organizations are turning to artificial intelligence (AI) and other technologies to streamline processes and reduce costs. This creates the need for specific focal points to address concerns around fair, responsible, and inclusive banking practices.
To promote these ideals, organizations should emphasize four principal areas: new technologies, AI, fee and pricing models, and marketing and advertising practices. Regulators have been focusing on these concerns, and organizations should consider prioritizing improving their fair banking practices in these critical areas. Identifying and mitigating potential risks can create a more equitable banking environment while meeting regulatory requirements.

01 AI

02 Fee and pricing models

03 Marketing and advertising practices

04 Access and equal treatment

Fair, responsible, and inclusive banking with new technologies: artificial intelligence

With the financial industry's ever-evolving usage of AI technologies, organizations have seen traditional processes transformed into more efficient alternatives. These technologies have already provided, and promise to further provide, benefits such as:

- **Enhancing efficiency:** Reducing costs and improving productivity by using AI to perform core processes such as finance, compliance, risk management, and administrative tasks
- **Generating revenue:** Using AI to improve segmentation, anticipate customer needs, or create new products and services.
- **Reducing risk:** Applying AI to risk analysis in credit decisions, market risk, or insurance underwriting enhances institutional strength and systemic stability
- **Risk management**: Enhancing fraud detection, trading surveillance, and liquidity or counterparty risk evaluations.
- **Operations streamlining:** Process reengineering of administrative tasks, reporting, or compliance activities
- **Customer acquisition and management:** Accelerating onboarding or improving customer understanding and personalization
- **Customer experiences:** Automating interactions via chatbots or virtual assistants and enhancing existing channels by allowing human advisers to focus on value-added tasks.

Compliance, risk, and business stakeholders should understand the risks associated with these technologies before and after deployment. More importantly, stakeholders should understand potential biases within technology methodologies and should consider implementing appropriate internal controls to identify and mitigate the risk of biases built into their decision-making processes that could lead to possible impact on consumers and regulatory expectations.

63%

increase in technology spend CCOs have recognized technology as a primary area for compliance improvement and anticipate a budget increase for this sector.

$447B

in potential cost savings for organizations with AI implementations

75%

of banks with $100M+ in revenue use AI

AI Bill of Rights

Nonbinding guiding principles issued by the Biden administration for the safe and ethical use of AI

Source: KPMG Chief Compliance Officer Survey (2023)

Some significant risk areas from leveraging AI include poor accountability and transparency, potential bias or discrimination, data misuse or privacy breaches, and financial and operational instability by relying too much on third parties. Like any innovative technology, AI can pose risks if implemented without a suitable governance program and controls.

Examples of current use cases illustrating how AI has raised regulatory commentary include:

- **Automated valuation models:** AI has been embedded into performing home valuations using AVM. The models are created by building algorithms that analyze various data sets to produce an appraisal value, which is then used to underwrite a mortgage. The inaccurate valuation of homes can infringe on a consumer's ability to repay their mortgages and result in digital redlining, enforcing long-standing disparities for marginalized communities. The CFPB recently proposed a rule to uphold fairness in using AVMs by outlining steps organizations can take to prevent bias and discrimination, such as conducting random sample tests and reviewing the valuations produced by the models.[2] By proactively applying the guidance in the proposed rule, organizations that use or plan on using AVMs can gain confidence in their model's accurate and fair decision-making and prevent potential future regulatory scrutiny or disproportionate consumer impact.
- **Credit decisioning models:** The algorithmic models relied upon in credit decisions use data from various sources to fuel decision-making. If decision rationales for adverse action decisions are unclear, organizations risk providing inaccurate adverse action notices. Under the Equal Credit Opportunity Act (ECOA), there are detailed adverse action notice requirements, including a customer's right to an explanation for adverse credit actions. In 2022, the CFPB released a circular that emphasized an organization's obligation to adhere to the rights outlined in ECOA, regardless of how the decision was derived.[3] Organizations that utilize these models should consider reviewing the underlying data for relevance and accuracy while fully understanding the model's decision-making process and assumptions applied to confidently provide a valid rationale for any adverse credit action against a consumer and prevent discriminatory practices.

As organizations continue incorporating algorithmic models, such as chatbots, the importance of consumer rights and regulatory adherence cannot be lost, as it could lead to various regulatory implications and reputational damage. Organizations can follow the following to promote fairness and inclusivity of products and services offered to their customers.

- **Chatbots:** Chatbots are one of the most prominent uses of AI technology. They allow consumers to receive information more quickly by eliminating the need to wait in phone queues. Thanks to the multilingual capabilities of generative AI tools, customers can communicate in their preferred language, helping organizations meet LEP requirements and breaking down communication barriers for consumers who previously had no means of communicating. In a 2023 *Issue Spotlight,* the CFPB highlighted certain chatbot models' inability to distinguish between factual and incorrect data, such as data that is told to be true by users versus the underlying programmed data, as the tool is built to not only utilize the programmed data but also learn from its users. The possibility of misinformation leaves organizations at risk as there is certain critical information regulators require to be accurate. In addition to information reliability, the CFPB has also observed a corresponding increase in security concerns.[4] As organizations are obligated to safeguard personally identifiable information, chatbots without adequate risk management systems and controls pose risks to consumers and the organization. As innovative customer service approaches continue to be deployed, regulatory adherence must remain at the forefront to avoid legal consequences and negative consumer impact.

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[2] Source: Consumer Finance Protection Bureau Site, Rules & Policy Section, "Quality Control Standards for Automated Valuation Models" (June 1, 2023)

[3] Source: Consumer Finance Protection Bureau Site, News Section, "CFPB Acts to Protect the Public from Black-Box Credit Models Using Complex Algorithms" (May 26, 2022)

[4] Source: Consumer Finance Protection Bureau Site, Data & Research Section, "Chatbots in Consumer Finance" (June 6, 2023)

Data validation	Risk assessments	Issue management
Review and validation of the underlying data supporting algorithmic models allows for the detection and prevention of risks that could jeopardize the data's integrity and the model's output.	Organizations should tailor their risk assessment process, scope, and activities to identify the risks posed by using new technologies in their operations and services.	Implementing comprehensive issue management practices allows for remediation of issues and risks identified during the review process, while promoting a strong compliance culture and reducing the impact of unmitigated risks.

Charting a course toward fair, responsible, and inclusive banking

With the changes in technology, there has been a continued democratization of financial services, which has driven a shift in sociopolitical expectations. Acting in concert with the federal government's strategies and directives to promote equity, fairness, and inclusion, federal financial services regulators and state attorneys general have expanded their bank and nonbank supervisory lens on principles of fairness and customer protections to encompass the "whole of the consumer," focusing on impacts, outcomes, and concerns at all touchpoints.

Regulators are scrutinizing the potential adverse impacts of innovative products, services, and technologies that banks utilize on consumers. Further, regulators will continue to assess the fairness of financial market products and services over the "customer journey," including fair treatment focusing on consistency between consumer groups, responsive and fair remediation of disputes, product development, marketing, sales, servicing, and complaints management.

To address these concerns, organizations can focus on a several key areas: fee and pricing models, marketing and disclosure content, and access/equal treatment.

48%

decrease in overdraft/NSF revenue from 2019–2022

12,000

consumer responses to CFPB detailing negative impact of fee practices

Source: Consumer Finance Protection Bureau Overdraft/NSF revenue down nearly 50% versus pre-pandemic levels (May 24, 2023)

Fee and pricing models

Financial Services organizations have long relied on fee income as a revenue driver, transitioning from a supporting role to a major contributor to organizational revenue. This has resulted in increased regulatory scrutiny on how organizations manage fees. Specifically, regulators have focused on what they define as "junk fees," obscured or misleading fees that harm consumers and make it harder for them to afford services. The primary examples of junk fees highlighted by the CFPB include overdraft fees, non-sufficient fund (NSF) fees, returned item deposited fees, and late credit card fees.

To address regulator concerns, the industry has largely begun changing its business models to review and eliminate fees that may harm consumers or otherwise be perceived as misleading. Further, some organizations have started providing financial education to consumers to help them avoid fees, creating and highlighting simple account options with lower fees, and implementing internal controls that strive to make fees fair and transparent.

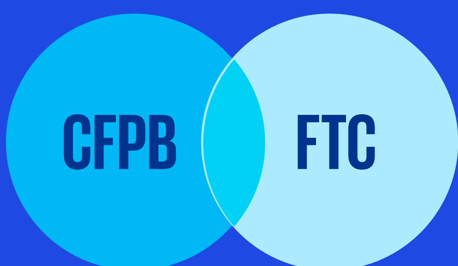
In addition to implementing baseline practices to establish fairness and transparency, financial services organizations should complete the following to develop a framework to allow their stakeholders to review:

- **Understand your fees:** Conduct a comprehensive fee structure review across all products and lifecycles. Organizations should consider whether any fee is commensurate with the cost to the organization and if it is deemed essential to the services/features of the product. Organizations can also reexamine and simplify their fee structures to eliminate confusion and reduce the likelihood of unintended charges.
- **Assess marketing and disclosures:** Organizations should review their marketing materials and disclosures to verify that fees are disclosed clearly and match how they are charged in practice. Clearly disclosing fees up front will enable customers to make informed decisions about the services they use.
- **Examine pricing models:** A targeted review of not just product pricing models, but also their performance, from the lens of how costs may impact vulnerable consumer groups can aid organizations in identifying potential areas of inequality.

Finally, firm adherence to regulatory requirements and maintenance of internal controls can significantly reduce the possibility of violations and enhance compliance with legal and ethical standards.

“When Big Tech firms use sophisticated behavioral targeting techniques to market financial products, they must adhere to federal consumer financial protection laws”

Rohit Chopra,
CFPB Director



Both the CFPB and FTC are putting companies on notice regarding negative-option practices, publishing various legal risks faced when using the marketing tactic.

Marketing and advertising practices

Marketing and advertising tactics have also come under increased scrutiny from regulators who seek to protect consumers from deceptive practices. As many financial services organizations utilize targeted advertising and data-driven marketing to reach potential customers, some of these practices can be seen as misleading, resulting in consumers unknowingly agreeing to products and services they did not want. Regulators have emphasized the importance of transparency in marketing, including requiring explicit consent from consumers before collecting their personal information.

Organizations have begun incorporating digital technologies into their marketing practices, and the arrival of AI has led to greater operating efficiency and effectiveness. However, there have been concerns across agencies over the potential misuse of these algorithms, leading to discriminatory marketing practices. Digital marketing uses harvested personal data to fuel algorithms and AI to identify prospective customers based on spending patterns and select a target audience for marketing campaigns based on who is most interested or likely to convert into a customer. This practice can prevent certain consumers with limited data available or those that do not hold the characteristics of the “target customer” from accessing and viewing certain marketing campaigns that may benefit them. The CFPB passed an interpretive rule in August 2022 to regulate algorithmic marketing and advertising where all customers are provided fair and transparent services.[5] The rule has declared digital marketers as service providers, thus subjecting them to regulation under the Consumer Financial Protection Act (CFPA). This rule is in place to establish guidelines for digital marketers as they use algorithmic models to prevent discriminatory marketing tactics and provide fair product access across all consumers.

Financial services organizations’ use of negative-option practices has also come under scrutiny in the industry as a potentially misleading marketing tactic. Negative-option practices involve the interpretation of a customer’s silence as acceptance of the product/service, leading to recurring charges until the consumer opts out. Product offerings that utilize negative-option practices, such as debt protection and identity protection products, can mislead consumers into commitments that lead to potential financial loss and harm. Regulators have increasingly monitored organizations that use negative-option practices to protect consumers’ financial interests. These guidelines aim to provide transparency and make consumers fully aware of any financial obligations they’re committing to.

[5] Source: Consumer Compliance Protection Bureau, “CFPB Warns that Digital Marketing Providers Must Comply with Federal Consumer Finance Protections” (August 10, 2022)

Financial services organizations can enhance legal and ethical adherence while maintaining customer trust and safety when deploying marketing tactics by conducting the following:

- **Analyze marketing activities and strategy:** Organizations should review and assess their marketing and advertising practices to determine if their product and service offerings are being marketed to different consumers. Organizations should conduct monitoring and testing activities on products targeted to a particular consumer base to detect any unfair or inconsistent treatment.
- **Understand third-party risks:** A review includes the assessment of the digital marketing vendor's compliance with all applicable regulations. The review allows organizations to view vendor risks and the potential impact on business agreements, such as marketing campaigns. Additionally, reviewing the underlying data that marketers use for campaigns will allow an assessment of fair, nondiscriminatory access to the advertised products and services across consumers.
- **Document compliant practices:** Adopt policies that require opt-in consent rather than opt-out to increase transparency and reduce the risk of financial harm to consumers. Further, the monitoring and auditing marketing policies and procedures can aid in strengthening the alignment of internal practices with regulatory expectations.

6%

of American adults remain unbanked

29%

of consumers prefer traditional bank account management methods over mobile and online platforms

Source: Forbes Advisor " U.S. Consumer Banking Statistics 2024" (Jan 31, 2024)

Keys to successful complaint management programs

1 Dynamic data analysis/ reporting

2 Enhanced training programs

3 Robust governance and controls

Access and equal treatment

Despite strides made in access to financial products in recent years, 6 percent of American adults remain unbanked, with African American and Hispanic populations comprising a higher percentage of the population.[6] There are various factors for the marginalization of the unbanked population, including socioeconomic factors and language barriers (i.e., those with LEP.) To address the issue, some organizations have implemented several initiatives to promote financial inclusion, including increasing affordable account options and promoting financial literacy. However, challenges persist in reaching unbanked communities, fair access, and fair and equal treatment. Additionally, organizations are continuing to focus their attention on access and treatment of their customer bases; however, there are three areas where organizations should continue to devote resources:

- **Digital Banking Access:** Although digital banking has benefited millions of people, some populations are still unable to participate due to a lack of internet or mobile access, particularly in low-income or rural areas. To address this issue, organizations can offer alternative forms of digital banking accessibility to allow fair access to the digital economy. Additionally, organizations should prioritize compliance with the ADA and the WCAG to provide accessibility to all customers, including those with disabilities. By taking these steps, organizations can help to reduce financial inequality and increase inclusivity in their services.
- **Access to financial information:** With digitization and diversification of financial market participants, access to their financial data is inconsistent, and even among organizations that share data at a customer's request, the terms of the sharing vary greatly. The CFPB's proposed open banking rule, which would give consumers additional rights in controlling their personal financial data, allows financial organizations to provide personalized experiences to their customers, reduce operational costs, and stay ahead of the curve.
- **Fair and equal treatment:** Regulatory emphasis on fairness principles and related compliance expectations, including consumer protection and equity, continue to take center stage and drive the need for investment. Specifically, the changing regulatory landscape requires organizations to prioritize fairness and responsiveness when dealing with credit decisions, complaints, disputes, and fraud management. Organizations should invest in embedding fairness precepts across the customer's journey, consider the impact of services on society, and deploy internal controls to confirm that consumer commitments are upheld equitably across their customer bases.

[6] Source: The Federal Reserve Board "Report on the Economic Well-Being of U.S. Households in 2022 - May 2023"

Fair and inclusive financial banking relies on equal access to financial products and services. Based on these factors and regulatory emphasis on fairness principles, there is a call to action across the industry for organizations to:

- **Determine social impact strategy:** Consider the impact of services on society and enhance access to a broader range of consumers.
- **Prioritize fairness:** Embed and prioritize fairness controls across consumer and retail products and services.
- **Centralize and simplify:** Execute centralized processes; streamline and simplify customer-focused communications.
- **Amplify fairness:** Enhance complaints, claims, dispute management processes, technology, and data analytics to enhance equitable treatment.
- **Reform risk and approval processes:** Evolve the CMS (across lines) by revisiting the inputs and weights into risk assessments and new product and service reviews and approvals—all to consider inclusion, access, tangible benefit, and consistent and equitable outcomes.

How KPMG can help

KPMG has helped organizations improve and bridge gaps in their processes, products, and services by assisting financial services organization across the industry in understanding and implementing processes and controls to address concerns over fair, responsible, and inclusive practices. Our services include revamping monitoring and testing procedures, helping to optimize risk and controls, identifying and remediating process gaps, performing complaint and trend analysis, and conducting product due diligence. We prioritize the development of fair and responsible practices at every stage of a consumer's journey.

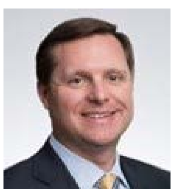
To help, KPMG can assist with:

- **Complaints/disputes trend and root-cause analysis**
- **Marketing advertising reviews**
- **Assessing the customer journey**
- **Tailored compliance program review**
- **Compliance and monitoring testing support**

Conclusion

Financial services organizations should consider embodying fair banking principles and ethical practices as regulations evolve and the industry continues to digitize products and services. Customer-centric approaches prioritizing diverse populations' needs and preferences are critical, as is providing accessible information, transparency, and security to promote consumer trust and foster equitable financial services. To promote fair and responsible banking practices, organizations should focus on implementing fair fee and pricing models, adopting responsible marketing and advertising practices, and providing equal access to treatment. Additionally, as AI and algorithm-based processes become more prevalent, organizations can consider validating any underlying data and algorithms to identify bias or potential discrimination risks and build risk management processes to evaluate the models used for consistency and regulatory compliance. Promoting financial inclusion and addressing the marginalization of unbanked populations, particularly in underserved communities, is also crucial for promoting a more equitable banking environment. Prioritizing fair and responsible practices will improve consumer trust and regulatory compliance, and build a foundation for long-term growth and success.

Contact us



Mike Lamberth
Partner, Financial Services Risk, Regulatory & Compliance
T: 804-241-2795
E: mlamberth@kpmg.com

Todd Semanco
Partner, Financial Services Risk, Regulatory & Compliance
T: 412-232-1601
E: tsemanco@kpmg.com

Damian Plioplys
Principal, Financial Services Risk, Regulatory & Compliance
T: 212-872-7959
E: dplioplys@kpmg.com

Hernando Garcia
Director, Financial Services Risk, Regulatory & Compliance
T: 212-954-3287
E: hernandogarcia@kpmg.com

Authored by Scott Page, Rita Tsafack-Tonleu, and Arianna Haynes

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