

**UNITED STATES OF AMERICA  
DEPARTMENT OF THE TREASURY  
OFFICE OF THE COMPTROLLER OF THE CURRENCY**

In the Matter of

**Carrie Tolstedt**, Former Head  
of the Community Bank

OCC AA-EC-2019-82

**Claudia Russ Anderson**,  
Former Community Bank Group Risk  
Officer

OCC AA-EC-2019-81

**James Strother**, Former General  
Counsel

OCC AA-EC-2019-70

**David Julian**, Former Chief  
Auditor

OCC AA-EC-2019-71

**Paul McLinko**, Former  
Executive Audit Director

OCC AA-EC-2019-72

Wells Fargo Bank, N.A.  
Sioux Falls, South Dakota

ALJ McNeil

**RECOMMENDED DECISION – PAUL MCLINKO  
Temporarily Sealed until December 30, 2022**

What follows is the Administrative Law Judge’s recommended decision, recommended findings of fact, recommended conclusions of law, and proposed order in the matter of Paul McLinko, who served as the Executive Audit Director assigned to the Community Bank, for Wells Fargo Audit Services at Wells Fargo Bank, N.A. between January 2013 and September 2016.

The recommendations and proposed order are based on proceedings initiated through the OCC’s issuance of a Notice of Charges presented against Mr. McLinko. Among the charges and in the record that has been developed based on those charges are documents and testimony that may include confidential supervisory information and for other reasons may be restricted from

the public. Without making any determination whether those restrictions are applicable here, this Recommended Decision is submitted to the OCC and the parties under temporary seal. The sealing of this Recommended Decision will expire on December 30, 2022, at which point the Recommended Decision will be available as a public record unless the OCC determines that all or part of the Decision may be withheld from the public.

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**1. Nature of the Case**

This is an administrative enforcement action taken by the Office of the Comptroller of the Currency and initiated through a Notice of Charges that was issued on January 23, 2020, by the OCC’s Deputy Comptroller for Large Bank Supervision, Gregory J. Coleman. The enforcement

action was taken against three senior bankers formerly affiliated with Wells Fargo Bank, N.A. (WFB-NA or the Bank). The action was taken pursuant to the federal Administrative Procedure Act as authorized by the Federal Deposit Insurance Act and uniform procedural rules of the Office of the Comptroller of the Currency.

The facts summarized here are based solely on evidence in the record, including testimony and documentary evidence taken during a hearing that began on September 13, 2021 in Sioux Falls, South Dakota and continued through intermittent presentations that concluded on January 6, 2022. After 35 days of sworn testimony and the presentation of documentary evidence, the parties presented their arguments through final briefs filed on June 26, 2022.

Through the Notice of Charges, the OCC identified David Julian as the Bank's Chief Auditor. It identified Claudia Russ Anderson as the Group Risk Officer for the Bank's Community Banking group. It identified Paul McLinko as a direct report of Mr. Julian and the Executive Audit Director for the Bank's Community Banking group.

The Notice advised Ms. Russ Anderson that the OCC contends her conduct as Group Risk Officer constituted violations of law, constituted unsafe or unsound practice, and breached fiduciary duties she owed to the Bank. The Notice seeks an order prohibiting her from engaging in regulated banking activity.

The Notice advised Mr. Julian and Mr. McLinko that the OCC contends their conduct as Chief Auditor and Executive Audit Director (respectively) constituted unsafe or unsound practice and breached the fiduciary duties each owed to the Bank. There is no allegation that either Mr. Julian or Mr. McLinko violated any statute or regulation. The Notice seeks orders that they cease and desist engaging in certain prohibited activity.

The Notice further assessed civil money penalties against each banker.

Mr. McLinko answered the Notice by denying he engaged in unsafe or unsound banking practices, and denying that he breached any fiduciary duties owed to the Bank.

Upon preponderant evidence supporting the factual allegations in the Notice of Charges against Mr. McLinko, I recommend the Comptroller issue a cease and desist order against Mr. McLinko, as proposed in the Notice of Charges as supplemented by the post-hearing submissions by Enforcement Counsel. I also recommend an order that Mr. McLinko pay a \$1.5 million civil money penalty.

## **2. Conditions Leading to the Charges**

Five key conditions led to the presentation of charges against Mr. Julian, Ms. Russ Anderson, and Mr. McLinko.

First, Bank employees working in the Bank's Community Banking unit, who were referred to as team members, engaged in sales practices misconduct throughout the relevant period – which for the purposes of these Reports and this Executive Summary was the beginning of 2013 to the end of 2016. During the relevant period, such misconduct was widespread throughout the Bank's branch system, and materially threatened the safety, soundness, and reputation of Wells Fargo Bank, N.A. and its holding company, Wells Fargo & Company.

Second, as Chief Auditor, Mr. Julian failed to timely identify the root cause of team member sales practices misconduct in the Community Bank, failed to provide credible challenge to Community Bank's risk control managers, failed to timely evaluate the effectiveness of Community Bank's risk management controls, and failed to identify, address, and escalate risk management control failures that threatened the safety, soundness, and reputation of Wells Fargo Bank, N.A.

Third, as Community Bank's Group Risk Officer, Ms. Russ Anderson failed to timely identify the root cause of team member sales practices misconduct in the Community Bank, failed to timely and independently evaluate the effectiveness of Community Bank's risk management controls, and failed to identify, address, and escalate risk management control failures that threatened the safety, soundness, and reputation of Wells Fargo Bank, N.A.

Fourth, as the Community Bank's Executive Audit Director, Mr. McLinko failed to timely identify the root cause of team member sales practices misconduct in the Community Bank, failed to provide credible challenge when evaluating the effectiveness of Community Bank's risk management controls, and failed to identify, address, and escalate risk management control failures that threatened the safety, soundness, and reputation of the Bank.

Fifth, throughout the relevant period, Ms. Russ Anderson, Mr. Julian, and Mr. McLinko separately and collectively engaged in unsafe or unsound banking practices by individually failing to identify and effectively address known issues of risks related to sales goals pressure in the Community Bank, knowingly and purposefully failing to escalate known issues related to those risks, misleading regulators and members of the Bank's Board of Directors regarding the efficacy of controls over risks related to sales goals pressure, and advancing their individual pecuniary interests over the safety, soundness, and reputational interests of Wells Fargo Bank, N.A. and its holding company, Wells Fargo & Company, thereby breaching fiduciary duties each owed to the Bank. Further, Ms. Russ Anderson's efforts to restrict material information from being disseminated among the Bank's senior leaders and the WF&C Board of Directors constituted violation of federal laws.

**1) Community Bank team members engaged in sales practices misconduct that threatened the safety, soundness, and reputation of Wells Fargo Bank, N.A.**

The Community Bank's sales goals and accompanying management pressure during the relevant period led thousands of its employees to engage in: (1) unlawful conduct to attain sales through fraud, identity theft, and the falsification of bank records, and (2) unethical practices to sell products of no or low value to Bank customers, while believing that the customers did not actually need the products.<sup>1</sup>

Collectively, many of these practices were referred to within Wells Fargo as "gaming." "Gaming" was a term generally known at the Bank. It referred to employees' manipulation or misrepresentation of sales to meet sales goals, receive incentive compensation, or avoid negative

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<sup>1</sup> Enforcement Counsel's Motion for Summary Disposition (EC MSD) Ex. 1 (Deferred Prosecution Agreement) at Exhibit A (Statement of Facts) at ¶14.



consequences such as reprimands or termination.<sup>2</sup>

Gaming strategies varied widely, and included using existing customer identities—without the customer’s consent—to open checking and savings, debit card, credit card, bill pay, and global remittance accounts in the customer’s name. Many widespread forms of gaming constituted violations of federal criminal law.<sup>3</sup> Examples of gaming practices engaged in by Wells Fargo employees included:

a. Employees created false records and forged customers’ signatures on account opening documents to open accounts that were not authorized by customers.<sup>4</sup>

b. After opening debit cards using customers’ personal information without consent, employees falsely created a personal identification number (PIN) to activate the unauthorized debit card. Employees often did so because the Community Bank rewarded them for opening online banking profiles, which required a debit card PIN to be activated.<sup>5</sup>

c. In a practice known as “simulated funding,” employees created false records by opening unauthorized checking and savings accounts to hit sales goals. They then transferred funds to the unauthorized account to meet the funding criteria required to receive credit for “selling” the new account. To achieve this “simulated funding,” employees often moved funds from existing accounts of the customers without their consent.<sup>6</sup>

Millions of accounts reflected transfers of funds between two accounts that were equal in amount to the product-specific minimum amount for opening the later account and that thereafter had no further activity on the later account; many of these accounts were subject to simulated funding. In many other instances, employees used their own funds or other methods to simulate actual funding of accounts that they had opened without customer consent.<sup>7</sup>

d. Employees opened unauthorized consumer and business credit card accounts without customer authorization by submitting applications for credit cards in customers’ names using customers’ personal information.<sup>8</sup>

e. Employees opened bill-pay products without customer authorization. Employees also encouraged customers to make test or “token” payments from their bill-pay accounts to obtain employee sales credit (which was only awarded for bill-pay accounts that had made a payment).<sup>9</sup>

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<sup>2</sup> EC MSD Ex. 1 at Ex. A at ¶16.

<sup>3</sup> EC MSD Ex. 1 at Ex. A at ¶16.

<sup>4</sup> EC MSD Ex. 1 at Ex. A at ¶16.

<sup>5</sup> EC MSD Ex. 1 at Ex. A at ¶16.

<sup>6</sup> EC MSD Ex. 1 at Ex. A at ¶16.

<sup>7</sup> EC MSD Ex. 1 at Ex. A at ¶16.

<sup>8</sup> EC MSD Ex. 1 at Ex. A at ¶16.

<sup>9</sup> EC MSD Ex. 1 at Ex. A at ¶16.

f. Employees at times altered the customer phone numbers, email addresses, or physical addresses on account opening documents. In some instances, employees did so to prevent the customers from finding out about unauthorized accounts. They also did so to prevent customers from being contacted by the Company in customer satisfaction surveys.<sup>10</sup>

Millions of customer accounts falsely reflected a Wells Fargo email address as the customer's own personal email address, contained a generic and incorrect customer phone number, or were falsely linked to a Wells Fargo branch or Wells Fargo employee's home address. Employees also intentionally persuaded customers to open accounts and financial products that the customers authorized but which the employees knew the customers did not actually want, need, or intend to use. There were many ways in which employees convinced customers to open these unnecessary accounts, including by opening accounts for friends and family members who did not want them and by encouraging customers to open unnecessary, duplicate checking or savings accounts or credit or debit cards.<sup>11</sup>

**2) Mr. McLinko, as the Community Bank's Executive Audit Director, failed to timely identify the root cause of team member sales practices misconduct in the Community Bank, failed to provide credible challenge when evaluating the effectiveness of Community Bank's risk management controls, and failed to identify, address, and escalate risk management control failures that threatened the safety, soundness, and reputation of the Bank.**

### **3. Summary of the Evidence**

Paul McLinko testified that he has approximately 40 years of experience in internal audit at large national banks.<sup>12</sup> He stated that he served as the Executive Audit Director (EAD) for Wells Fargo Audit Services (WFAS) throughout 2013 to 2016, which is the relevant period in this administrative enforcement action.<sup>13</sup> He holds a Master's Degree in finance and information systems from Pace University and after college worked for Chase Manhattan Bank for fifteen years, starting in branch auditing and thereafter in consumer and corporate lending, with "increasing roles of responsibility in each of those areas."<sup>14</sup>

Mr. McLinko testified that in the mid-1980s he earned the Certified Internal Auditor designation issued by the Institute of Internal Auditors, which he described as the "governing body of audit, internal audit" that is sometimes called the IIA.<sup>15</sup> He described the credentialing process as similar to that of the Certified Public Accountant, which "covers everything from the

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<sup>10</sup> EC MSD Ex. 1 at Ex. A at ¶16.

<sup>11</sup> EC MSD Ex. 1 at Ex. A at ¶17.

<sup>12</sup> Transcript (Tr.) (McLinko) at 8454-55.

<sup>13</sup> Tr. (McLinko) at 7752-53.

<sup>14</sup> Tr. (McLinko) at 7752.

<sup>15</sup> Tr. (McLinko) at 7756.

standards, the objectives, [and] the practice of internal audit.”<sup>16</sup> He said the process requires passing a multipart exam and meeting certain experience requirements.<sup>17</sup> He testified that there are continuing education requirements, including 40 hours a year of such education.<sup>18</sup>

Mr. McLinko testified that he was at Wachovia prior to its merger with Wells Fargo, working as a senior director, and began working in WFAS following the merger, working at WFAS for the entire relevant period.<sup>19</sup> According to Mr. McLinko, WFAS had its own 40-hour continuing education requirements that each member of WFAS was required to complete each year.<sup>20</sup> He testified that he was asked to serve as a member of the IIA Board for the local Charlotte, North Carolina chapter, serving three years as a member and then three years as the chapter’s Chair.<sup>21</sup>

Mr. McLinko testified that he became the Executive Audit Director (EAD) of both the Community Bank and its Operations Group in the middle of 2012, remaining in those positions until 2017.<sup>22</sup> Working within WFAS, Mr. McLinko was EAD for the line of business known as Community Banking throughout the relevant period, in a group referred to as Community Banking and Operations, or CBO.<sup>23</sup> He testified that CBO “was the audit group that was responsible for auditing the Community Bank as well as auditing the operations component of technology and operations group.”<sup>24</sup> In this capacity, the CBO group was “responsible for auditing the Regional Bank, which included the stores” of the retail branch network of the Community Bank.<sup>25</sup>

Mr. McLinko testified that he was an executive vice president of Wells Fargo Bank, N.A. (the Bank); and he also was a member of the Management Committee of Wells Fargo & Company – the Bank’s holding company.<sup>26</sup>

Mr. McLinko testified that during his tenure as EAD for the CBO, he had “leadership roles in our diversity initiatives, in our training initiatives” for WFAS.<sup>27</sup> He testified that beyond working with the CBO staff, he supervised “at least 200 people”, most of whom were on teams

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<sup>16</sup> Tr. (McLinko) at 7756.

<sup>17</sup> Tr. (McLinko) at 7756.

<sup>18</sup> Tr. (McLinko) at 7757.

<sup>19</sup> Tr. (McLinko) at 7752-53.

<sup>20</sup> Tr. (McLinko) at 7758.

<sup>21</sup> Tr. (McLinko) at 7758.

<sup>22</sup> Tr. (McLinko) at 8456.

<sup>23</sup> Tr. (McLinko) at 7753.

<sup>24</sup> Tr. (McLinko) at 7753-54.

<sup>25</sup> Tr. (McLinko) at 8504.

<sup>26</sup> Tr. (McLinko) at 8457-58.

<sup>27</sup> Tr. (McLinko) at 7759.

other than the CBO.<sup>28</sup> He testified that during the relevant period he also was “[p]rofessionally active in the community” including leading WFAS’s efforts in “one of the biggest fundraising events” for the Heart Association in Charlotte.<sup>29</sup>

He testified that he continued in this role until September or December 2017, when – in discussions with David Julian, who was the Bank’s Chief Auditor – Mr. Julian “asked me to take on a role to cover such areas” where there could be “improvements to the effectiveness and the efficiency of the Audit Department”.<sup>30</sup> He denied being fired from his role as EAD for the CBO, testifying that he retired in March-April 2019, adding that he was not asked to retire and has not worked since his retirement.<sup>31</sup>

### **Nature of the Charges against Respondent Paul McLinko**

Through the Notice of Charges, the Comptroller alleged the Community Bank was and is the Bank’s largest line of business and houses the Bank’s retail branch network.<sup>32</sup> The Notice alleged the Community Bank “had a systemic and well-known problem with sales practices misconduct” throughout the relevant period.<sup>33</sup> It alleged the term “sales practices misconduct,” as used in the Notice, refers to “the practices of Bank employees issuing a product or service to a customer without the customer’s consent, transferring customer funds without the customer’s consent, or obtaining a customer’s consent by making false or misleading representations.”<sup>34</sup>

In his testimony, Mr. McLinko denied using the phrase “sales practice misconduct” while employed at Wells Fargo, and testified that this was not a term he heard others using during the relevant period.<sup>35</sup> He testified that he did hear the term “sales integrity” during the relevant period, but denied that “sales integrity” meant the same thing as “sales practices misconduct.”<sup>36</sup> He also testified that he heard the term “sales quality” used at the Bank, but again denied that the “sales quality” meant the same thing as “sales practice misconduct.”<sup>37</sup>

The Notice alleged the root cause of the sales practices misconduct problem was “the Community Bank’s business model, which imposed intentionally unreasonable sales goals and unreasonable pressure on its employees to meet those goals and fostered an atmosphere that

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<sup>28</sup> Tr. (McLinko) at 7760.

<sup>29</sup> Tr. (McLinko) at 7760.

<sup>30</sup> Tr. (McLinko) at 7754.

<sup>31</sup> Tr. (McLinko) at 7754-55.

<sup>32</sup> Notice of Charges at ¶ 2.

<sup>33</sup> *Id.* at ¶ 3.

<sup>34</sup> *Id.* at ¶ 4.

<sup>35</sup> Tr. (McLinko) at 7760-61.

<sup>36</sup> Tr. (McLinko) at 7761.

<sup>37</sup> Tr. (McLinko) at 7762.

perpetuated improper and illegal conduct.”<sup>38</sup> It alleged the Community Bank management “intimidated and badgered employees to meet unattainable sales goals year after year, including by monitoring employees daily or hourly and reporting their sales performance to their managers, subjecting employees to hazing-like abuse, and threatening to terminate and actually terminating employees for failure to meet the goals.”<sup>39</sup>

The Notice alleged the Community Bank’s business model “was highly profitable because it resulted in a greater number of legitimate sales than would have been possible without the unreasonable sales goals and sales pressure.”<sup>40</sup> It alleged the unauthorized products and services that were issued to customers “also resulted in a financial benefit to Respondents and the Bank.” The Notice alleged that the Bank “touted a metric known as ‘cross-sell,’ or the ‘cross-sell ratio,’ that measured the number of products sold per household.”<sup>41</sup>

The Notice of Charges alleged the unauthorized products and services issued to customers inflated the cross-sell metric and “resulted in enhanced stock price.”<sup>42</sup> It alleged the Bank “tolerated pervasive sales practices misconduct as an acceptable side effect of the Community Bank’s profitable sales model, and declined to implement effective controls to catch systemic misconduct. Instead, to avoid upsetting a financially profitable business model, senior executives, including Respondents, turned a blind eye to illegal and improper conduct across the entire Community Bank.”<sup>43</sup>

Mr. McLinko testified that during sworn testimony he gave on March 2, 2018 during the investigation stage of this enforcement action, the OCC provided him with a definition of “systemic”; and stated while the OCC did provide a definition of the term, the definition they gave was not one he ever encountered in any internal audit setting, and it was not one he had ever heard the OCC use prior to giving that testimony.<sup>44</sup>

Through leading questioning provided by his Counsel during direct examination, Mr. McLinko agreed that a “fair definition” of the term systemic was that supplied by Mr. Julian:

At that time period, systemic would have been used in the internal audit language, if you will, when, based on testing, typically statistical sampling or statistical testing, that based on that testing a -- let's say a control weakness

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<sup>38</sup> Notice of Charges at ¶ 5.

<sup>39</sup> *Id.* at ¶ 5.

<sup>40</sup> *Id.* at ¶ 6.

<sup>41</sup> *Id.* at ¶ 6.

<sup>42</sup> *Id.* at ¶ 6.

<sup>43</sup> *Id.* at ¶ 6.

<sup>44</sup> Tr. (McLinko) at 7762.

was identified that was significant in both volume and proportion and -- and also proportionally distributed to the population as a whole.<sup>45</sup>

Mr. McLinko testified that he “especially like the aspect of the proportional that he mentioned there and how it’s proportional to the activities taking place.”<sup>46</sup> In his testimony, Mr. McLinko supplied the following as what he averred to be an example of how he applied the term “systemic” in his role as an internal auditor:

I can think of an example where during this time frame that we're talking about, internal audit, in all the audit teams, began testing something called user access, okay? And what we found during that user access was every area we were going into or most of the areas that we were going into had this user access problem, I'll call it, internal control breakdown. So as the audit teams and, as we started to review and we found this happening across the whole organization, we made the determination to step back and say, Why are we testing this now? Because we know it's throughout the organization, so, therefore, it's systemic as it was built into the processes. So we needed to fix it from a larger perspective.<sup>47</sup>

The Notice alleged that the Bank “had better tools and systems to detect employees who did not meet unreasonable sales goals than it did to catch employees who engaged in sales practices misconduct.”<sup>48</sup> It alleged that “[t]o the extent the Bank did implement controls, the Bank intentionally designed and maintained controls to catch only the most egregious instances of the illegal conduct that was pervasive throughout the Community Bank.”<sup>49</sup> It alleged that Bank senior executives “favored profits and other market rewards over taking action to stop the systemic issuance of unauthorized products and services to customers.”<sup>50</sup>

The Notice alleged that the Bank “had three lines of defense which, together with the Law Department, were tasked with controlling and managing risk. The Community Bank was the first line of defense. Corporate Risk was the second line of defense. Audit was the third line of defense.”<sup>51</sup> It alleged that the systemic sales practices misconduct “persisted for years due to the failures of Bank senior executives and failures in the checks and balances that were supposed to be provided by the Law Department and Audit.”<sup>52</sup> It alleged that Mr. McLinko “had a responsibility to ensure incentive compensation plans were designed and operated in accordance

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<sup>45</sup> Tr. (McLinko) at 7763.

<sup>46</sup> Tr. (McLinko) at 7764.

<sup>47</sup> Tr. (McLinko) at 7764-65.

<sup>48</sup> Notice of Charges at ¶ 6.

<sup>49</sup> *Id.* at ¶ 6.

<sup>50</sup> *Id.* at ¶ 6.

<sup>51</sup> *Id.* at ¶ 10.

<sup>52</sup> *Id.* at ¶ 16.

with Bank policy, evaluate risk and ensure it was adequately managed and escalated, advise whether the Community Bank was operating in conformance with laws and regulations, or identify and detail significant or systemic problems in audit reports.”<sup>53</sup> It alleged that none of the Respondents who held leadership roles in those departments adequately performed their responsibilities with respect to the sales practices misconduct problem.<sup>54</sup>

The Notice alleged that senior executives at the Bank acknowledge what was known or should have been known all along: that sales practices misconduct was a significant and systemic problem, and sales goals were unattainable and a significant part of the root cause of the sales practices misconduct problem.<sup>55</sup> It alleged that in sworn testimony before the OCC, Respondent Julian agreed that the Community Bank “had a serious systemic issue with sales practices misconduct and that he would characterize the root cause of the problem as ‘the goals were unattainable or unreasonable, and the pressure to meet those unattainable goals was severe.’”<sup>56</sup>

The Notice alleged that in sworn testimony before the OCC, Respondent McLinko agreed that there was a systemic sales practices misconduct problem in the branch environment of the Community Bank and “the sales goals and incentive processes were certainly two areas that contributed significantly to the issue, the pressure for the sales goals.”<sup>57</sup>

The Notice alleged that throughout the relevant period, Respondent McLinko was responsible for overseeing all Community Bank audits, which included setting the audit strategy, reviewing and approving draft audit reports, complying with Audit’s charter, and providing credible challenge to Community Bank management.<sup>58</sup> It alleged Respondent McLinko was responsible for ensuring that the Community Bank’s audit team adequately executed their duties consistent with Audit’s responsibilities.<sup>59</sup> It alleged Respondent McLinko was responsible for the accuracy and completeness of the Community Bank’s audits.<sup>60</sup> It alleged Respondent McLinko had access to all functions, records, property, and personnel in the Bank, including sales goals, incentive compensation plans, termination data, customer complaints, and EthicsLine reporting.<sup>61</sup> It alleged that throughout the relevant period, Respondent McLinko knew or should

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<sup>53</sup> *Id.* at ¶ 16.

<sup>54</sup> *Id.* at ¶ 16.

<sup>55</sup> *Id.* at ¶ 17.

<sup>56</sup> *Id.* at ¶ 18.

<sup>57</sup> *Id.* at ¶ 19.

<sup>58</sup> *Id.* at ¶ 444.

<sup>59</sup> *Id.* at ¶ 445.

<sup>60</sup> *Id.* at ¶ 446.

<sup>61</sup> *Id.* at ¶ 447.

have known about the systemic sales practices misconduct problem in the Community Bank and its root cause.<sup>62</sup>

The Notice alleged that Respondent McLinko was a member of the Community Bank's Internal Fraud Committee.<sup>63</sup> It alleged that as part of that committee, he received reporting from Corporate Investigations throughout the relevant period that there were thousands of sales integrity cases each year, including thousands of investigations related to lack of customer consent for products and services.<sup>64</sup>

The Notice alleged that in January 2013, an auditor who reported to Respondent McLinko told him that sales integrity "is still [the Chief Security Officer's] #1 concern."<sup>65</sup> The Notice alleged that in that same email, the auditor wrote: "I questioned [the Chief Security Officer] as to whether they had discussed root cause for some of the items listed above and was it related to sales pressure. He said he felt a lot of it was related to the sales goals and pressure. He feels there's an issue that [Regional Bank] is trying to work through but not a lot of people want to address it with [Respondent Tolstedt]."<sup>66</sup> The Notice alleged that Respondent McLinko took no meaningful action in response to this email.<sup>67</sup>

The Notice alleged that Respondent McLinko was aware of the *Los Angeles Times* articles at the end of 2013.<sup>68</sup> The Notice alleged that the Chief Security Officer and Head of Corporate Investigations emailed him the first article and explained it was a "big deal[.]"<sup>69</sup> It alleged that Respondent McLinko took no meaningful action in response to the *Los Angeles Times* articles.<sup>70</sup>

The Notice alleged that Respondent McLinko failed to identify and escalate the sales practices misconduct problem in audit reports.<sup>71</sup> The Notice alleged Respondent McLinko failed to fulfill his audit responsibilities with respect to the sales practices misconduct problem.<sup>72</sup> It alleged that Respondent McLinko admitted in sworn testimony before the OCC that the Community Bank had a systemic problem with sales practices misconduct.<sup>73</sup> The Notice alleged

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<sup>62</sup> *Id.* at ¶ 448.

<sup>63</sup> *Id.* at ¶ 449.

<sup>64</sup> *Id.* at ¶ 449.

<sup>65</sup> *Id.* at ¶ 456.

<sup>66</sup> *Id.* at ¶ 456.

<sup>67</sup> *Id.* at ¶ 456.

<sup>68</sup> *Id.* at ¶ 457.

<sup>69</sup> *Id.* at ¶ 457.

<sup>70</sup> *Id.* at ¶ 457.

<sup>71</sup> *Id.* at 95.

<sup>72</sup> *Id.* at ¶ 458.

<sup>73</sup> *Id.* at ¶ 459.



Respondent McLinko further admitted in his sworn testimony before the OCC that “this systemic sales practices misconduct problem persisted until sales goals were eliminated in October 2016.”<sup>74</sup>

The Notice alleged Respondent McLinko admitted that although the systemic sales practices misconduct problem existed throughout his tenure as Executive Audit Director with responsibility for auditing the Community Bank, “none of the Community Bank’s audits identified this problem.”<sup>75</sup> The Notice alleged that when asked whether Audit ever rated *anything* in Community Bank as unsatisfactory, Respondent McLinko replied, “Nothing I can think of.”<sup>76</sup>

The Notice alleged that under Respondent McLinko’s leadership, the Community Bank audit team never criticized the Community Bank for its systemic sales practices misconduct problem or identified its root cause in any audit report and that in doing so Respondent McLinko allowed the Community Bank’s systemic sales practices misconduct problem to persist.<sup>77</sup>

The Notice alleged that in audits conducted during the relevant period that involved aspects of sales practices misconduct, the Community Bank audit team under Respondent McLinko’s leadership awarded high ratings to the Community Bank.<sup>78</sup> It alleged that in December 2013, the Community Bank received an “effective” rating—the highest possible rating—for its sales quality / sales integrity internal controls.<sup>79</sup>

The Notice alleged that in June 2015, the OCC issued five Matters Requiring Attention related to sales practices and that one Matter Requiring Attention required Audit to “reassess their coverage of sales practices and provide an enterprise view.”<sup>80</sup> It alleged that in response to the Matter Requiring Attention, “Audit indicated that it was committed to maintaining independence and developing a comprehensive audit approach with respect to sales practices.”<sup>81</sup> It alleged that the response to the Matter Requiring Attention designated Respondent McLinko as the “accountable executive.”<sup>82</sup>

The Notice alleged that the commitments for which Respondent McLinko was the “accountable executive” included being “engaged with the various LOBs (lines of business) as they develop and implement corrective actions to the Enterprise Sales Practices MRA’s. . . . Issue

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<sup>74</sup> *Id.* at ¶ 460.

<sup>75</sup> *Id.* at ¶ 461.

<sup>76</sup> *Id.* at ¶ 461.

<sup>77</sup> *Id.* at ¶ 462.

<sup>78</sup> *Id.* at ¶ 463.

<sup>79</sup> *Id.* at ¶ 465.

<sup>80</sup> *Id.* at ¶ 466.

<sup>81</sup> *Id.* at ¶ 467.

<sup>82</sup> *Id.* at ¶ 467.

monitoring and validation, reviewing governance processes and enhanced policy, monitoring of projects/initiatives to enhance Enterprise Sales Practices compliance, and obtaining an understanding of key activities and functions performed to ensure compliance with enterprise sales practices along with their sustainability.”<sup>83</sup> The Notice alleged that notwithstanding all of the commitments that Audit made and for which Respondent McLinko was the “accountable executive,” the Community Bank audit team under Respondent McLinko’s leadership “continued to award high ratings to the Community Bank.”<sup>84</sup>

The Notice alleged that in March 2016, following the Los Angeles City Attorney’s lawsuit and the five Matters Requiring Attention from the OCC, Audit rated the Community Bank’s system of internal controls related to customer account opening as “effective.”<sup>85</sup> (470) The Notice alleged that “Far from identifying and escalating the sales practices misconduct problem in the Community Bank in audit reports, Respondent McLinko personally praised Respondent Tolstedt for her and the Community Bank’s quality of risk management.”<sup>86</sup>

The Notice alleged that in March 2016, Respondent McLinko told Respondent Tolstedt that “[w]hile many groups talk about risk management, [Respondent Tolstedt] and [her] team live it.”<sup>87</sup> And in July 2016, Respondent McLinko told Respondent Tolstedt: “[i]t’s rare to find a business leader who takes risk management as seriously as you do.”<sup>88</sup> The Notice alleged that in April 2016, Respondent McLinko told Respondent Russ Anderson: “I’d appreciate it if you don’t mention audit and the risk culture topic together when and if you approach the subject with the regulators.”<sup>89</sup>

The Notice alleged that in a September 2016 email about sales practices misconduct, Respondent Julian asked his staff, including Respondent McLinko: “Where was audit while this activity was taking place? To be honest, I’m not sure how to answer this but am sure the A[udit and] E[xamination] Committee will and should be asking.”<sup>90</sup> Neither Respondent McLinko, nor anyone else in Audit, was able to provide Respondent Julian with an adequate answer to the question: “Where was audit while this activity was taking place?”<sup>91</sup>

### **Known Weaknesses of WFAS**

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<sup>83</sup> *Id.* at ¶ 468.

<sup>84</sup> *Id.* at ¶ 468.

<sup>85</sup> *Id.* at ¶ 469.

<sup>86</sup> *Id.* at ¶ 470.

<sup>87</sup> *Id.* at ¶ 470.

<sup>88</sup> *Id.* at ¶ 470.

<sup>89</sup> *Id.* at ¶ 471.

<sup>90</sup> Notice of Charges at ¶ 472.

<sup>91</sup> *Id.* at ¶ 472.

When Mr. Julian became Chief Auditor for WFAS, the Bank’s holding company, WF&C, was a “diversified financial services company providing banking, insurance, investments, mortgage, and consumer and commercial finance through more than 9,000 stores, 12,000 ATMs, the Internet, and other customer-facing locations across North America and internationally.”<sup>92</sup> At that time, “[o]ne in three households in America” did business with Wells Fargo, and the holding company had “\$1.3 trillion in assets and more than 270,000 team members across its 80+ businesses.”<sup>93</sup>

Mr. Julian testified that upon commencing his service as Chief Auditor in 2012, “management had expressed concern with the current direction of Wells Fargo Audit Services and the leadership that was being provided to it.”<sup>94</sup> He emphasized, “[t]here was certainly pressure from the Board as well as the regulators to enhance Wells Fargo Audit Services’ stature within the heightened standards.”<sup>95</sup> He added, “Management and the Board had concerns about the current leadership’s ability to lead into that effort.”<sup>96</sup>

Mr. Julian testified that he replaced Kevin McCabe as Chief Auditor.<sup>97</sup> He said that at the time of this transition, the OCC expressed concerns about Mr. McCabe’s leadership.<sup>98</sup> He recalled the OCC communicating to him that they did not feel that under Mr. McCabe’s leadership that WFAS “was meeting their expectations with respect to Internal Audit function, nor did they feel that Kevin had the ability to confidently lead the group to achieve such – as the standards were heightening.”<sup>99</sup> He recalled the OCC Examiners, notably Examiner in Charge Scott Wilson, expressing their expectation that “appropriate credible challenge would be applied. That the Audit Plan would reflect and include significant risks.”<sup>100</sup> He said they also were concerned that the Audit staff “have the appropriate expertise to execute their responsibilities.”<sup>101</sup>

Wells Fargo & Company – through its Corporate Risk unit – explained the role of “credible challenge” in its November 2015 Sales Practices Risk Governance Document in these terms:

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<sup>92</sup> R. Ex. 3560 at 23.

<sup>93</sup> *Id.*

<sup>94</sup> Tr. (Julian) at 5926.

<sup>95</sup> Tr. (Julian) at 5928.

<sup>96</sup> Tr. (Julian) at 5929.

<sup>97</sup> Tr. (Julian) at 6094.

<sup>98</sup> Tr. (Julian) at 6094-95.

<sup>99</sup> Tr. (Julian) at 6095.

<sup>100</sup> Tr. (Julian) at 6095-96.

<sup>101</sup> Tr. (Julian) at 6095.

A hallmark of an independent, effective, informed, and engaged sales practices risk management function is the degree to which team members at all levels, and across all areas, feel empowered to prudently question the propriety of business, support and risk management decisions as well as key strategic initiatives with a view towards ensuring the appropriate balance of risk-taking and reward. Credible challenge is the communication of an alternative view, opinion, or strategy developed through expertise and professional judgement to challenge business or enterprise strategies, policies, products, practices and controls. Credible challenge may also take the form of the offering of ideas or alternative strategies that may be equally or more effective in mitigating risk. Credible challenge is critical to the success of each of Wells Fargo's three lines of defense. To be successful, credible challenge requires team members to have the necessary expertise, understand the company's sales practices risk-generating activities, build relationships, be good listeners, be informed about risks and issues, and communicate openly, honestly, and directly.<sup>102</sup>

The Governance Document provided guidance specifically directed towards the function of Group Risk Officers like Ms. Russ Anderson:

Group Risk Officers ("GROs"), who lead the Group Risk organizations embedded in the Company's sales practices risk-generating Groups, exercise credible challenge through various means, including by raising concerns to Group management and escalating issues to CERG [Corporate Enterprise Risk Group] in a timely manner, and in particular its SPO [Sales Practices Oversight] unit in addition to certain components of the Chief Administrative Office, the Law Department, and certain Corporate Risk functions. [Footnote omitted.]

Within the second-line of defenses, the SPO unit has primary organizational responsibility for exercising and coordinating credible challenge with respect to sales practices risk management. It does so through a number of methods, including maintaining a clear understanding of sales practices risks and risk drivers, which allows the SPO unit to independently assess sales practice risk exposures and information and work closely with the first-line to refine its perspective and ensure that concerns and questions are raised in a timely and appropriate manner. To credibly challenge the first-line of defense, the SPO unit applies its risk management skills and deep understanding of the nature of appropriate sales practices. If the SPO unit does not consider that its

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<sup>102</sup> OCC Ex. 1477 at 9.

concerns have been appropriately or adequately addressed, it utilizes established escalation structures and protocols.<sup>103</sup>

Mr. Julian testified that he shared the OCC's concerns about the state of WFAS at the time he took over as its Chief Auditor.<sup>104</sup> He elaborated on this answer by stating there had been a time in a prior role where he had been audited by WFAS and had "seen the work."<sup>105</sup> From this experience, he "came to appreciate that there were opportunities to enhance" WFAS.<sup>106</sup> No one, however, raised any concerns to him about the Community Bank's business model in general or its sales practices in particular.<sup>107</sup>

Mr. McLinko testified that by January 2013 he had been the EAD assigned to Community Banking for about six months, and that it was his opinion that throughout the relevant period the CBO team competently and in good faith audited those processes and controls relating to sales in the Community Bank.<sup>108</sup> He testified that early in his tenure he "sat down with my SAMs, each of the SAMs, and to understand the work they did, the activities, try to get understanding of the businesses."<sup>109</sup> He stated he joined his team "in their business monitoring in some cases, I sat down with senior leaders of Community Bank to hear what they said, how they said it, what about their . . . groups."<sup>110</sup> He stated he did the same with the Risk Management Group "to hear their perspective on the business."<sup>111</sup> He testified he also met in person – either in December 2012 or January 2013 – with Ms. Tolstedt and her leadership team to gain "insight to help me understand the . . . Community Bank" while getting up to speed in his new role as the WFAS EAD assigned to Community Banking.<sup>112</sup> He testified he met with Ms. Tolstedt on an on-going basis after that, meeting with her in person every six months.<sup>113</sup>

Mr. McLinko described the scope of these meetings in these terms:

The -- basically I would go through -- depending on the timing, if it was at the beginning of an audit plan year, I would review with her the actual audit plan that we were going to be embarking upon for the year and go through what we're doing, why we're doing it, those sorts of -- those sorts of things.

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<sup>103</sup> *Id.* at 9-10.

<sup>104</sup> Tr. (Julian) at 6096.

<sup>105</sup> Tr. (Julian) at 6096.

<sup>106</sup> Tr. (Julian) at 6096.

<sup>107</sup> Tr. (Julian) at 6096-97.

<sup>108</sup> Tr. (McLinko) at 7856.

<sup>109</sup> Tr. (McLinko) at 7857.

<sup>110</sup> Tr. (McLinko) at 7857.

<sup>111</sup> Tr. (McLinko) at 7858.

<sup>112</sup> Tr. (McLinko) at 7858.

<sup>113</sup> Tr. (McLinko) at 7859.

If it was in the middle of the year, I would give her results of the performing audit work for the first six months of the year, for example, and give her -- excuse me -- any updates to our plan that we may be doing. And then I would then have -- there would be dialogue.<sup>114</sup>

Mr. McLinko testified that in addition to the twice yearly meetings, his team would prepare and deliver to Ms. Tolstedt a packet of documents every quarter, “that talked about the activities that took place within Community Bank.”<sup>115</sup>

Mr. McLinko denied that he and Ms. Tolstedt were friends, testifying, “[s]he was engaged in the conversations that I had with her. She certainly had an interest in what I was saying. Very professional was another way I would describe it.”<sup>116</sup>

Mr. McLinko testified early in his position as EAD for Community Banking he reached out and established a relationship with Claudia Russ Anderson, stating, “it was important to get her perspective on where she felt the risks were”, describing this as “a way to make our audit process more efficient at that time.”<sup>117</sup> He denied that he and Ms. Russ Anderson were friends, and opined through leading questioning by his Counsel during direct examination that he had an appropriate professional relationship with both Ms. Russ Anderson and Ms. Tolstedt.<sup>118</sup> He added that he directed his team members on the CBO to do the same, and stated that in his career, which “spans many banks over many years, this practice of establishing business relationships happened in every one of them.”<sup>119</sup> He denied that this practice of having good working relationships with Community Banking leadership impaired his professional independence.<sup>120</sup>

In 2013, WFAS “transitioned to a new methodology to increase transparency in audit work and results, as well as ensure coverage of all businesses and their associated activities.”<sup>121</sup> In February 2014, there were 116 RABUs [Risk Assessable Business Units] in the business hierarchy – and WFAS “aligns the RABUs to the corresponding Operating Committee Group.”<sup>122</sup> Under the process framework implemented in 2013, WFAS reported it would be able to “identify common business activities which may warrant cross-enterprise reviews as well as

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<sup>114</sup> Tr. (McLinko) at 7860.

<sup>115</sup> Tr. (McLinko) at 7861.

<sup>116</sup> Tr. (McLinko) at 7860.

<sup>117</sup> Tr. (McLinko) at 7861-62.

<sup>118</sup> Tr. (McLinko) at 7862.

<sup>119</sup> Tr. (McLinko) at 7863-64.

<sup>120</sup> Tr. (McLinko) at 7864.

<sup>121</sup> OCC Ex. 2107 at 6.

<sup>122</sup> *Id.* at 3.

provide the ability to analyze trend data throughout the enterprise.”<sup>123</sup> The “process level represents the business activities performed and really defines the point at which audit work can be performed.”<sup>124</sup> WFAS uses the process level “in defining the ‘auditable’ segments of the company and for reporting and analytics.”<sup>125</sup>

Under the “process level,” once the business unit or RABU has been identified and the company’s business activities have been confirmed, WFAS “begins building the comprehensive inventory of which activities/processes are performed within each business unit. It is at this individual process level that WFAS can most easily measure and understand the risks that an activity poses to the business.”<sup>126</sup> In 2014, WFAS had 2,159 RABU-processes within its audit universe, and within this universe it performs a risk assessment “to determine the level of risk and frequency in which the business activity should be audited.”<sup>127</sup>

Mr. Julian testified that although no one – from the Board, from the OCC, from WFAS – raised concerns about the sales practices of the Community Bank, his focus upon assuming the role of Chief Auditor was to “focus very initially [on] recognizing that there was an expectation that I brought [WFAS] from what was described to me as a weak audit function to a function that would meet or exceed regulatory and industry practice standards.”<sup>128</sup> To this end, Mr. Julian stated he was focused on “assuring that we had the right level of resources to execute and Audit Plan, that the Audit Plan was focused on the right areas, that we had the right, not only level of resources, but also the right qualified resources to execute the work.”<sup>129</sup>

Mr. Julian testified that to address staffing issues, he “reorganized in certain instances new leadership, brought on new leadership . . . to make sure that Audit was structured in a way that I felt made the most sense to address and be responsive to our responsibilities.”<sup>130</sup> He said to this end he added “a senior level person within [WFAS] to take over the development of the talent management program,” in conjunction with Human Resources.<sup>131</sup>

Mr. Julian testified that he also made changes to improve WFAS use of technology, reporting that WFAS “enhanced and actually implemented a new technology system which

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<sup>123</sup> *Id.* at 4.

<sup>124</sup> OCC Ex. 2107 at 4.

<sup>125</sup> *Id.*

<sup>126</sup> *Id.* at 5.

<sup>127</sup> *Id.* at 6.

<sup>128</sup> Tr. (Julian) at 6101.

<sup>129</sup> Tr. (Julian) at 6103.

<sup>130</sup> Tr. (Julian) at 6105.

<sup>131</sup> Tr. (Julian) at 6105.

allowed the Audit Group to, again, better track and better execute audits that were being performed, the ability to track themes that might be coming up throughout various audits.”<sup>132</sup>

Mr. Julian testified that steps he took enhanced Audit’s stature within the company, by assuring that “Audit was providing appropriate level critical challenge and credible challenge.”<sup>133</sup> His own actions, according to Mr. Julian, increased WFAS’s stature: “My involvement on the Operating Committee and my inclusion on the Operating Committee alone provided stature to [WFAS] organization because now they saw that the leader of their Group had a seat at the table.”<sup>134</sup> He added that the OCC and the Federal Reserve “constantly” provided “favorable feedback” that he had “stature within the organization. That I provided credible challenge. That I provided appropriate leadership to the [WFAS] group.”<sup>135</sup>

One specific area of concern, according to Mr. Julian, was that “Management wanted to make sure that I had appropriate time to focus on Wells Fargo Audit Services and enhancing [WFAS’s] stature and compliance with the Heightened Standards.”<sup>136</sup> In furtherance of this objective, the Corporate Security (or Corporate Investigations) team, headed at the time by Michael Bacon, was removed from WFAS’s direction and relocated, where Mr. Bacon would thenceforth report to the head of Human Resources.<sup>137</sup> He also included in the 2013 Audit Plan a request for more staff, observing that when he started as Chief Auditor, there was a staff of approximately 500, and when he retired there were nearly 1,200 WFAS employees.<sup>138</sup> This, according to Mr. Julian, precipitated a doubling of the dollars that WF&C devoted to Internal Audit between 2012 and 2017.<sup>139</sup>



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<sup>132</sup> Tr. (Julian) at 6110.

<sup>133</sup> Tr. (Julian) at 6111.

<sup>134</sup> Tr. (Julian) at 6112.

<sup>135</sup> Tr. (Julian) at 6114; R. Ex. 19770 at 15; R. Ex. 4095 at 11; see also OCC Ex. 4266 at 7.

<sup>136</sup> Tr. (Julian) at 5966.

<sup>137</sup> Tr. (Julian) at 5965-66.

<sup>138</sup> Tr. (Julian) at 6106.

<sup>139</sup> Tr. (Julian) at 6109.

<sup>140</sup> R. Ex. 740.

<sup>141</sup> *Id.* at 1.



[REDACTED]

[REDACTED]

[REDACTED]

[REDACTED]

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<sup>142</sup> *Id.* at 1.

<sup>143</sup> R. Ex. 740 at 1.

<sup>144</sup> *Id.*

<sup>145</sup> *Id.* at 3.

<sup>146</sup> *Id.*

<sup>147</sup> *Id.*

<sup>148</sup> *Id.*

<sup>149</sup> *Id.*

<sup>150</sup> *Id.* at 5.

<sup>151</sup> *Id.* at 6.



### **Known Weaknesses in 2013 regarding Community Banking’s Sales Integrity and Team Member Fraud**

Mr. McLinko identified a January 3, 2013 email exchange among Bart Deese, Mark Teuschler, Janet Malvitz and himself regarding a January 2, 2013 meeting with Mr. Deese, Mr. Teuschler, and Michael Bacon, who was head of Corporate Investigations.<sup>155</sup>

Summarizing the January 2, 2013 meeting for the benefit of Mr. McLinko, Mr. Deese wrote that Mr. Bacon was “entertaining as always” and provided bullet points from the meeting, including the following:

- Sales Integrity is still his #1 concern. During mid-year 2012 the case numbers leveled out, but they saw an uptick in the last half of 2012.
- He feels Claudia’s group has done some good work around new reporting; however, he still feels they have some opportunities (which he has shared with Claudia) regarding being more proactive in some areas of reporting such as (Note: Michael stated this was not all related to Sales Integrity but compliance as well):
  - Accounts opened by team members for other team members including both personal and business type accounts. Many were found to be unfunded.

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<sup>152</sup> *Id.* at 6.

<sup>153</sup> R. Ex. 12120 at 5.

<sup>154</sup> *Id.* at 6.

<sup>155</sup> Tr. (McLinko) at 7879; R. Ex. 3635

- Non-resident alien accounts . . . there was a historical issue with these types of accounts being opened to meet goals; however, it was addressed, but he feels more proactive monitoring is warranted.
- Duplicate addresses across customers and accounts.
- Duplicate SSNs.
- Suspicious Driver Licenses #s/No ID listed.
- Non-college individuals set up with college accounts.

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- His general thoughts on [Community Banking] were as follows:
  - Business Banking . . . they have a good program detecting issues in other areas such as [Regional Banking], etc. (i.e., improperly opened BB accounts); however, he feels they could do more with their own division.
  - RB . . . clearly some ongoing challenges as outlined in this summary.
  - WFCC . . . Diana has some opportunities to improve processes.
  - DSSG . . . not a lot of activity, but did terminate a few folks in 2012 related to falsifying or encouraging falsification of SOCR information.
  - Debit/Prepaid products . . . some opportunities here.
  - Rest of [Community Banking] . . . not a lot of activity or trends.
- Now that he attends the Senior HR Meetings, he finds out a lot of good information. Here is what he shared off the record (verbal information he remembered from a recent meeting):
  - RB turnover is higher than it has ever been.
  - RB engagement scores are lower.
  - Employee Relations issues as well as RB ethics line calls are at an all-time high.
  - Michael feels the year-end Sales Integrity cases and terminations in RB will be an all-time high as well.
- I questioned Michael as to whether they had discussed root cause for some of the items listed above and was it related to sales pressure. He said he felt a lot of it was related to the sales goals and pressure. He feels there's an issue that RB is trying to work through, but not a lot of people want to address it with Carrie [Tolstedt]. He mentioned that on a recent call, Mike Loughlin mentioned his wife went into a store to do a transaction and came out with 5 products.
- CBO Offsite . . . we talked with Michael about coming to the offsite (he or one of his managers). He's glad to arrange it, and they'll have a lot of good information to share (e.g., trends, new Fraud Comm process, year-end numbers, etc.). After the meeting Michael arranged for Marty Weber to come to our offsite.<sup>156</sup>

During cross-examination, when asked whether he ever sought from Mr. Bacon more information about the falsification of SOCR information, Mr. McLinko responded, "I was not

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<sup>156</sup> R. Ex. 3635 at 1-2.

part of this meeting, so I did not”, nor did he ask his team to track down more information related to the falsification of this information, and was not able to determine how employees were able to falsify those records.<sup>157</sup>

During cross-examination, when asked about the bullet point regarding root cause – that it was “an issue that [Regional Banking] is trying to work through,” when presented with the premise that if employees in the Community Bank did not want to discuss the root cause of sales integrity violations with the head of the Community Bank, Ms. Tolstedt, wouldn’t that be important information for him as the EAD to know? Mr. McLinko responded, “It’s certainly a data point.”<sup>158</sup>

Without identifying any evidence to support this testimony, Mr. McLinko testified that Mr. Deese’s use of the term “sales integrity” was not the same as “sales practice misconduct,” and that “as I understood it, [sales integrity] was a much larger component” and “encompasses many more things.”<sup>159</sup> Further, where Mr. Bacon is reported as referring to “the case numbers”, Mr. McLinko testified that this did not refer to instances of confirmed sales integrity violations – only “cases that were being researched.”<sup>160</sup>

Notwithstanding Mr. Bacon’s stated concern that Mr. Bacon identified Sales Integrity to be his “No.1 concern”, when asked by his Counsel during direct examination whether this statement caused him any concerns from an audit perspective, Mr. McLinko responded, “when you’re talking about sales integrity, you need to have a more prescriptive [*sic*] around what that actually means. So undue concern, no.”<sup>161</sup> Through leading questioning by his Counsel during direct examination, Mr. McLinko testified further that neither Mr. Deese nor Mr. Teuschler (who, along with Ms. Malvitz were Senior Audit Managers who reported to Mr. McLinko) came out of their meeting with Mr. Bacon having any concerns about sales integrity issues in the Community Bank.<sup>162</sup>

Testimony given by a witness during direct examination generally should not be based on leading questions. The test of a "leading question" is whether it suggests the answer desired by the examiner.<sup>163</sup> The examiner in this case was Mr. Crudo, Mr. McLinko’s trial counsel. The essential test of a leading question is whether it so suggests to the witness the specific tenor of

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<sup>157</sup> Tr. (McLinko) at 8556-57.

<sup>158</sup> Tr. (McLinko) at 8558.

<sup>159</sup> Tr. (McLinko) at 7884.

<sup>160</sup> Tr. (McLinko) at 7884.

<sup>161</sup> Tr. (McLinko) at 7885; see also “22-03-07 Respondents’ Amended Revised Errata Days 9 -38” at page 68. Ordered through Second Supplemental Order Regarding Hearing Transcript Errata.

<sup>162</sup> Tr. (McLinko) at 7885.

<sup>163</sup> *U.S. v. Hansen*, 256 F. Supp. 2d 65 (D. Mass. 2003), *aff’d*, 434 F.3d 92, 69 Fed. R. Evid. Serv. 262 (1st Cir. 2006).

the reply desired by counsel that such a reply is likely to be given irrespective of an actual memory; the evil to be avoided is that of supplying a false memory for the witness.<sup>164</sup>

There are three possible consequences of the leading question: (1) it can be very helpful in expediting the trial on matters that are indisputably preliminary or uncontested, or for refreshing memory or facilitating clear testimony from witnesses with language limitations; (2) it can amount to a minor and harmless violation of the prohibition against leading in that the answers elicited are not dispositive or otherwise critical; or (3) it can be unfair in that it supplies the witness with dispositive or otherwise critical answers, and usurps the elements of credibility the jury should be entitled to assess.<sup>165</sup>

Given that the leading question here would have the witness assume he knew what reaction or concerns either Mr. Deese or Mr. Teuschler had after their meeting with Mr. Bacon, the consequence of this question falls within the third of the three possible consequences: Mr. Crudo's question supplied Mr. McLinko with dispositive and otherwise critical answers to material questions, and usurped the elements of credibility. There is little evidentiary substance to be gained by this form of questioning, yet it is a form repeatedly used, particularly with respect to the testimony of Mr. McLinko by Mr. Crudo.

Similarly, notwithstanding Mr. Bacon's stated concern that "year-end Sales Integrity cases and terminations in [Regional Banking] will be at an all-time high", when asked during direct examination by his Counsel whether he found this statement concerning, Mr. McLinko responded, "When I read this, again it's all of a meeting that the Senior Audit Managers were having with Michael. Again, no undue concern here, because we had a lot of audit activities that were taking place in this area that we could – we would be testing" and added that neither Mr. Teuschler nor Mr. Deese expressed any concerns about the number of terminations or cases cited in this report.<sup>166</sup> He did not, however, support this statement with any documentary evidence.

Similarly, where Mr. Teuschler reportedly asked Mr. Bacon whether they had discussed root causes for some of the items listed here, to inquire whether it was related to sales pressure, and Mr. Bacon reportedly responded that he felt a lot of it was related to the sales goals and pressure, Mr. McLinko was asked whether this concerned him when he read it, and Mr. McLinko responded, "Again, there was no undue concern noted", adding his team was "in the process of analyzing the sales practices for the Community Bank, looking at our audit coverage to confirm that we had the right coverage."<sup>167</sup>

When asked whether he understood that someone was looking into root causes, Mr. McLinko responded only, "Well, that someone being that someone within [Mr. Bacon's] area or

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<sup>164</sup> *U. S. v. O'Brien*, 618 F.2d 1234, 5 Fed. R. Evid. Serv. 1236 (7th Cir. 1980)

<sup>165</sup> A Minnesota CLE Deskbook, Judge Gordon Shumaker (Ret.) Rulings on Evidence An Evidentiary Manual for Minnesota Trial Judges and Judicial Officers (and Attorneys!) 2013 last accessed on November 16, 2022 at <https://blogpendleton.files.wordpress.com/2020/04/schmaker-on-evidence.pdf>

<sup>166</sup> Tr. (McLinko) at 7887-88.

<sup>167</sup> Tr. (McLinko) at 7889.

in the Community Bank or the Risk Group of Community Bank”, without directly answering the question – and denied that Mr. Bacon was inferring that it was the responsibility of Mr. McLinko’s CBO team to look into the root cause.<sup>168</sup>

Notwithstanding the data and inferences presented by Mr. Bacon during the meeting as reported by Mr. Teuschler in this January 3, 2013 email message, when asked through leading questioning by his Counsel during direct examination whether the message led him to believe there was a widespread or systemic sales practices misconduct problem or sales integrity problem in the Community Bank, Mr. McLinko replied simply, “No”, without elaboration – other than to state that neither Mr. Deese nor Mr. Teuschler ever told him they had concerns about a widespread or systemic problem.<sup>169</sup>

Mr. McLinko testified that later in January 2013 he attended an off-site meeting in Phoenix with all of his Senior Audit Managers.<sup>170</sup> He testified that Marty Weber, one of Mr. Bacon’s direct reports, also attended.<sup>171</sup> Mr. McLinko identified a one-page flow chart titled “Sales Quality (SQ) Overview/Coverage Overlay” as having been prepared by Mr. Teuschler and Stephanie Wardlaw at his direction and presented during the January 2013 off-site meeting with Mr. Weber.<sup>172</sup> When asked, however, whether he recalled anything about Mr. Weber’s presentation at the off-site meeting, Mr. McLinko responded, “I really don’t know.”<sup>173</sup> After providing this answer, when asked whether Mr. Weber said anything to suggest that he believed the CBO team’s coverage of sales processes and controls in the Community Bank was deficient, Mr. McLinko responded only “Not that I recall”, without offering any documentation reflecting what was said during the meeting.<sup>174</sup> When asked whether anyone from his own team expressed any concerns about the CBO group’s audit coverage of sales in the Community Bank, Mr. McLinko responded, “No”, without elaboration.<sup>175</sup>

Noteworthy in the Overlay presented during the off-site meeting in Phoenix in January 2013 is the attention given to Incentive Compensation Programs.<sup>176</sup> The narrative at the top of the flow chart regarding incentive compensation programs is, “Create a level playing field to incent TMs to succeed within the rules while doing what’s right for the customer.”<sup>177</sup> The chart indicates that there will be Business Monitoring of EKIs (Enterprise Key Indicators) and Control

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<sup>168</sup> Tr. (McLinko) at 7889.

<sup>169</sup> Tr. (McLinko) at 7891,

<sup>170</sup> Tr. (McLinko) at 7892, 7897.

<sup>171</sup> Tr. (McLinko) at 7892.

<sup>172</sup> Tr. (McLinko) at 7898; R. Ex. 3745; transmittal email at R. Ex. 3744.

<sup>173</sup> Tr. (McLinko) at 7893.

<sup>174</sup> Tr. (McLinko) at 7894-95.

<sup>175</sup> Tr. (McLinko) at 7893.

<sup>176</sup> R. Ex. 3745.

<sup>177</sup> *Id.*

Testing of the HR and Incentive Compensation functions; and Control Testing of both the Risk Council and “Minding the Store” functions.<sup>178</sup> The chart indicates the Sales Quality Team (and not Audit) will be responsible for researching allegations for Regional Bank team members, customer polling based on allegation findings, “refer to [Corporate Security] for further investigations (as necessary)”, and “SQ Report Card on activations, signatures, funding.”<sup>179</sup>

The chart indicates Regional Banking Senior Leadership will “establish sales goals” and an “execution strategy”, directing that strategy to Store (including teller, banker, and customer service), followed by “Management Monitoring/Assessment”.<sup>180</sup> In between the senior leadership’s execution strategy and the direction to tellers and bankers at the stores, there would be control testing of SOCR – Store Operations Control Review.<sup>181</sup>

The chart indicated that Sales Quality “becomes involved when allegations [are] received from phone bank, [team members]/Management, [Human Resources], Ethics Line, and Investigations.”<sup>182</sup>

The chart provided this narrative regarding the Sales Quality Team of Regional Banking:

Sales Quality – Sales and referral related concerns stemming from general product design considerations, training needs and even serious ethical violations behaviors can range from individual team member level to enterprise-wide.

Sales Integrity – Subset of sales quality issues which typically involve the manipulation and/or misrepresentation of sales or referrals in order to receive compensation or to meet sales goals; including unethical and/or illegal behavior.<sup>183</sup>

Thus, under the definition of Sales Integrity used in this presentation, Community Bank employees engaged in “sales integrity” violations if they manipulated or misrepresented sales or referrals in order to receive compensation or to meet sales goals.<sup>184</sup>

The chart also described the role of Corporate Security,<sup>185</sup> as “Investigates/interviews when evidence supports allegation. Reports results to RB Mgmt./HR. SQ informed of final

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<sup>178</sup> Tr. (McLinko) at 7911; R. Ex. 3745.

<sup>179</sup> Tr. (McLinko) at 7911-12; R. Ex. 4009 at 1.

<sup>180</sup> R. Ex. 3745.

<sup>181</sup> *Id.*

<sup>182</sup> *Id.*

<sup>183</sup> *Id.*; see also R. Ex. 4009 (similar chart, with identical definitions for Sales Quality and Sales Integrity).

<sup>184</sup> R. Ex. 4009 at 1.

<sup>185</sup> Tr. (McLinko) at 7906, stating Corporate Security is the same as Corporate Investigations.

results.”<sup>186</sup> It provides for Control Testing of Sales Quality and Sales Integrity functions and Business Monitoring for “[Business Monitoring Program] BMP – [Corporate Security or Corporate Investigations] & RP [Regional Presidents] Meetings.”<sup>187</sup>

Mr. McLinko also identified an email exchange dated March 4, 2013 initiated by David Julian, regarding team member fraud in Community Banking.<sup>188</sup> Mr. Julian asked Mr. McLinko “What work do we do related to team member fraud?”<sup>189</sup> Through cross-examination, Mr. McLinko agreed that an employee opening an account without customer consent would be considered fraud.<sup>190</sup> He reported that Mr. Bacon “is presenting some data and Community Banking has a lot of issues each year.”<sup>191</sup>

In response, Mr. McLinko wrote, “Interesting that you asked this. Over the last month I had my managers put together a picture (1 pager) of a Sales Quality Overview, which includes coverage of Fraud. I will find 30 minutes on your calendar to review the picture.”<sup>192</sup> Mr. McLinko testified that the “1 pager” was the flow chart described above.<sup>193</sup> Mr. McLinko testified that nothing in this email chain gave him the impression that Mr. Julian was confused by Mr. Bacon’s data, or that Mr. Julian questioned the accuracy of Mr. Bacon’s data.<sup>194</sup>

In his email response on March 4, 2013, Mr. McLinko wrote the following in response to Mr. Julian’s question:

The short answer is:

- We do a control testing audit of the Store Operations Control Review (SOCR) where elements of fraud would be covered (audit was performed last year)
- We also do a control testing audit of Sales Quality/Sales Integrity where elements of fraud would be covered (audit will be performed this year)
- Both of these reviews were done on approximately 24 month cycle (thus touching something every year)

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<sup>186</sup> R. Ex. 3745.

<sup>187</sup> Tr. (McLinko) at 7910; R. Ex. 3745.

<sup>188</sup> Tr. (McLinko) at 7899; R. Ex. 3881.

<sup>189</sup> R. Ex. 3881 at 2.

<sup>190</sup> Tr. (McLinko) at 8531.

<sup>191</sup> R. Ex. 3881 at 2.

<sup>192</sup> *Id.*

<sup>193</sup> Tr. (McLinko) at 7903.

<sup>194</sup> Tr. (McLinko) at 8530.



- There are some other indirect reviews where we may find potential fraud (Customer Complaints, Incentive Compensation), but unlikely.<sup>195</sup>

Mr. McLinko identified the December 16, 2013 WFAS Community Banking, Regional Banking Sales Quality/Sales Integrity Audit Engagement Report as an example of a “control testing” audit.<sup>196</sup> He testified that the Regional Sales Quality/Sales Integrity Group reported up through Ms. Russ Anderson, and that later the Group was called SSCOT.<sup>197</sup>

The objective of this internal audit was “to determine if the risk management, system of controls, and governance processes are adequate and functioning as intended.”<sup>198</sup> In its Executive Summary, the Report stated:

Based on audit work performed, the system of internal controls within Regional Banking Sales Quality/Sales Integrity is **Effective**. This rating reflects our opinion that controls in place adequately mitigate the risks associated with sales quality allegation, case management, service management and reporting processes.<sup>199</sup>

Upon his review of the Audit Engagement Report, Mr. McLinko was unable to say whether the CBO audit team tested SSCOT’s Quality of Sales Report Card (QSRC).<sup>200</sup> He confirmed, however, that the internal control processes around the proactive monitoring and behavioral trends analysis were tested as part of the audit – and there were no issues identified in the Report related to SSCOT’s proactive monitoring or behavioral trend analysis processes.<sup>201</sup>

Mr. McLinko testified that the description found in the Report “clarifies that the team performed a design review and not effectiveness testing.”<sup>202</sup>

The Report identified the role of polling as reviewed by CBO auditors:

The RB Sales Quality (SQ) group consists of the SQ Analyst team and the Service Quality Polling Analyst team. The SQ Case Analyst team is responsible for researching allegations of inappropriate store sales practices received from the following sources: Phone Bank, Ethics Line, Human Resources, Regional Management, Corporate Investigations, and internal/proactive monitoring activities. Based on the research conducted by

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<sup>195</sup> R. Ex. 3881 at 1.

<sup>196</sup> Tr. (McLinko) at 8705-06; OCC Ex. 1328.

<sup>197</sup> Tr. (McLinko) at 8706.

<sup>198</sup> OCC Ex. 1328 at 5.

<sup>199</sup> *Id.* at 2, emphasis in original.

<sup>200</sup> Tr. (McLinko) at 8708.

<sup>201</sup> Tr. (McLinko) at 8708.

<sup>202</sup> Tr. (McLinko) at 8709.

the SQ Case Analyst team, the cases are closed as a non-issue, sent to the Polling Analyst team for customer follow-up, sent to Corporate Investigations, and/or emailed to management for training recommendations. The RB Sales Quality Group also produces sales quality reporting on a monthly basis via regional reports and Quality of Sales Report Cards (QSRC) and quarterly via RB Risk Council reports. RB Sales Quality is currently implementing a stronger proactive monitoring/behavioral trend analysis process. Historical inputs to the allegations process have been primarily reactive in nature and relied on observations/communication of concerns by team members, managers or customers. The proactive monitoring/behavioral trend analysis identifies potential sales quality concerns through the use of data analysis. The team identifies data analysis opportunities through trends identified during the sales allegation and case management process. Outliers identified within the data analysis reporting process are then fed into the sales allegations process for research, polling (if necessary) and resolution.<sup>203</sup>

Mr. McLinko testified that he believed “the control processes around the polling process, how all of that information flowed through the system and went to the right areas would – I believe would have been tested.”<sup>204</sup> Mr. McLinko confirmed that there were no issues identified in this Sales Quality/Sales Integrity Audit Report related to SSCOT’s customer polling process.<sup>205</sup>

Although the Report rated Regional Banking’s Sales Quality and Sales Integrity internal controls “Effective”, the auditors opined that the Sales Quality team “needs to strengthen the training notification process to ensure regional management performs all necessary team member coaching.”<sup>206</sup>

Elaborating, the Report held:

When the Regional Banking Sales Quality team closes a case, there are instances where the allegation or case does not warrant reporting to Corporate Investigations, but there is evidence of banker non-compliance with proper sales procedures. In these instances, the Sales Quality team issues emails to regional management instructing them to perform coaching/provide training to the applicable team member. During the previous twelve months, approximately 48% of allegations worked by the Sales Quality team resulted in training emails. Our review of this notification process revealed:

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<sup>203</sup> *Id.* at 2.

<sup>204</sup> Tr. (McLinko) at 8710.

<sup>205</sup> Tr. (McLinko) at 8710.

<sup>206</sup> OCC Ex. 1328 at 3.

- Sales Quality does not have a process in place to ensure management received the email and provided the coaching/training.
- The monthly regional sales reports including metrics on cases resulting in training email notifications does not differentiate between first time and second time training notifications.<sup>207</sup>

Mr. McLinko was asked during cross-examination that – if there was a pervasive and widespread sales practices misconduct problem in the Community Bank at this time – whether he would agree that if they were intended to be *sales practices controls*, SSCOT’s proactive monitoring and behavioral trend processes were not very effective, Mr. McLinko responded, “I would agree that this control that was in place was not fully effective in this scenario that you’re talking about”.<sup>208</sup>

Similarly, and based on the same assumptions as the prior scenario, when asked if he would agree that SSCOT’s customer polling process was not an effective one if intended to be a sales practices control, “with what you stated as the background, the polling – the analyst team, that process was not working as effectively as you indicated.”<sup>209</sup>

Mr. McLinko also confirmed that WFAS did not do another control testing of SSCOT’s proactive monitoring process before the sales goals were eliminated in October 2016.<sup>210</sup>

Although Mr. Julian asked what Audit did related to team member fraud, and Mr. McLinko gave the response shown in this email chain, Mr. McLinko denied that it was Audit’s responsibility to find fraud.<sup>211</sup> Elaborating on this answer, Mr. McLinko testified, “There are other groups within the businesses, including areas like Corporate Investigations, which has that role.”<sup>212</sup> Mr. McLinko testified that it was Audit’s responsibility “to put a program in place to monitor – or to audit for – for the control activities around fraud.”<sup>213</sup> Mr. McLinko agreed on cross-examination that part of WFAS’s job was to evaluate independently the internal controls over the fraud and fraud program, opining that “to ensure that the controls around fraud was definitely part of the job.”<sup>214</sup>

Mr. McLinko testified that he never told Mr. Julian that the audit procedures set forth in the email exchange were insufficient in order for Mr. McLinko to execute his responsibilities with respect to those audits related to team member fraud in the Community Bank, nor had Mr.

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<sup>207</sup> *Id.*

<sup>208</sup> Tr. (McLinko) at 8713.

<sup>209</sup> Tr. (McLinko) at 8714.

<sup>210</sup> Tr. (McLinko) at 8714.

<sup>211</sup> Tr. (McLinko) at 7902.

<sup>212</sup> Tr. (McLinko) at 7902.

<sup>213</sup> Tr. (McLinko) at 7902.

<sup>214</sup> Tr. (McLinko) at 8532.

Julian ever told him that additional procedures were needed besides what Mr. McLinko had listed.<sup>215</sup>

During direct examination, Mr. McLinko was asked by his Counsel, “How does SOCR relate to team member fraud?” and Mr. McLinko responded, “It relates to team member fraud in the aspects of where they do their work in relation to deposit transaction openings, that sort of thing.”<sup>216</sup> Asked how the Sales Quality group related to team member fraud, Mr. McLinko responded, “They are a conduit to review information relating to complaints, EthicsLine and monitor activities.”<sup>217</sup>

The record reflects, with respect to the last bulleted item, that the “1 pager” has as its title “Sales Quality (SQ) Overview/Coverage Overlay” regarding “Incentive Compensation Programs”.<sup>218</sup> There is thus some reason to question the reliability of both Mr. McLinko’s testimony regarding the flow chart and the reliability of the chart itself – where Mr. McLinko told Mr. Julian reviews of incentive compensation would not likely be a source of fraud, but where the response he gave Mr. Julian was to rely on a chart depicting incentive compensation programs.

Mr. McLinko added no clarity to his answer when, upon further questioning by his Counsel during direct examination he testified “the audit teams are reviewing the control processes around these types of activities, so you’re not specifically looking at how the controls are in place and operating. You’re not looking . . . for specific instances.”<sup>219</sup> He also added no clarity to the reliability of the chart by testifying that the list of items he presented to Mr. Julian was not the only work that Audit was doing that touched on fraud – that through this list Mr. McLinko was “trying to be responsive to David and I – I would have included things that came to my head immediately.”<sup>220</sup>

Audits focusing on Community Banking’s sales integrity continued to be discussed between Mr. Julian and Mr. McLinko. In an email chain that preceded a meeting with Mr. McLinko, Mr. Julian, Mr. Teuschler, and Ms. Wardlaw, the participants reviewed a three-page slide deck that included the 1 pager and a slide for sales integrity definitions, and an allegation resolutions pie chart.<sup>221</sup>

Mr. McLinko testified that he recalled Mr. Julian attended the meeting at which the three-page deck was presented, that Mr. McLinko’s team “went through the three pages in some

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<sup>215</sup> Tr. (McLinko) at 8533-34.

<sup>216</sup> Tr. (McLinko) at 7900-01; see also, “EC’s 2d Revised Hrg Transcript Errata Sheet” at page 24. Ordered through Second Supplemental Order Regarding Hearing Transcript Errata.

<sup>217</sup> Tr. (McLinko) at 7901.

<sup>218</sup> R. Ex. 3745.

<sup>219</sup> Tr. (McLinko) at 7901-02.

<sup>220</sup> Tr. (McLinko) at 7903.

<sup>221</sup> R. Ex. 4008 (email transmission) and 4009 (three slide deck).

detail,” that Mr. Julian “was engaged” and “appreciated the meeting”, but that Mr. McLinko did not recall anything else from that meeting – other than to state through responding to leading questioning by his Counsel during direct examination that Mr. Julian did not express at that meeting any concerns about the CBO’s group coverage of sales in the Community Bank.<sup>222</sup>

Through the 1 pager, there are arrows “trying to show that you go from the goals are established, they execute the strategy, which includes the goals, who does it, the stores, the tellers and the bankers do that, management then monitors the information.”<sup>223</sup> Mr. McLinko testified that those were not activities the CBO team conducted – “these are activities that are done either by the store, Community – the risk group within Community Bank, or – you’ll see a box at the very bottom – Corporate Security.”<sup>224</sup>

Through another set of arrows, in green, the picture identified the “actual control testing that is performed by . . . either the Community Bank group or potentially [other audit groups within WFAS] that would do control testing over these various activities.”<sup>225</sup>

The three-page slide deck included a March 2013 list of definitions provided by Corporate Security.<sup>226</sup> Under the broad heading of “Sales Integrity Violations,” Corporate Investigations identified eight specific categories of what CI tracks:

- Customer Consent – allegations of the booking or sale of any banking product without the knowledge or official direct consent of the primary customer and joint account/product holder.
- False Entries/CIP Violations – allegations of entering false identification, expiration dates, or other false information in order to open accounts; with or without customer consent.
- Fictitious Customer – Includes any product application where a falsified identification and or social security number is used to mask the true identity of the account holder.
- Online Banking – Pinning online banking with or without customer consent and activating online banking and/or ID Theft Protection.
- Product Manipulation – Waiving fees or adjusting products to open sales for unqualified customers. Steering customers into products they are not qualified for or it is not in their best interest to have.
- Funding Manipulation – Allegations of team members funding new or existing accounts for the purpose of sales goals.

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<sup>222</sup> Tr. (McLinko) at 7915-16.

<sup>223</sup> Tr. (McLinko) at 7908.

<sup>224</sup> Tr. (McLinko) at 7908-09.

<sup>225</sup> Tr. (McLinko) at 7909.

<sup>226</sup> R. Ex. 4009 at 2.

- Reassignment of Sales Credit – Includes allegations of one team member making referral contacts or product sales and reassigning the credit(s) to another team member in need of sales.
- Referrals – Invalid sales referrals gained by directing traffic, or inappropriately received by another team member when an actual sales referral was not made.<sup>227</sup>
- A final category recognized the possibility of sales integrity matters that do not “easily fall into one of the other categories.”<sup>228</sup>

Mr. McLinko acknowledged that for at least part of the relevant period he was a Wells Fargo Code of Ethics Administrator.<sup>229</sup> He acknowledged that in this position, he had the duty to “review different types of information that came to us,” and as such it was important for him to be familiar with the Wells Fargo Code of Ethics.<sup>230</sup>

During cross-examination, Mr. McLinko was presented with the Corporate Security Activities Report to Regional Banking Presidents (March 2013), which included the list of Sales Integrity Violations referred to above – including categories for “Customer Consent”, “False Entries/CIP Violations”, and “Fictitious Customer”.<sup>231</sup> When asked which of the listed categories were consistent with Wells Fargo’s Code of Ethics, Mr. McLinko responded: “I just don’t recall”, adding:

I was the Code of Ethics Administrator six, seven years ago. I don't remember the time frame. I don't remember what was in that Code of Ethics document. I don't remember specifically in that; and in my role, it was not a role of looking at the details of the -- of the Code, specific necessarily Code of Ethics violation. So I'm having difficulty answering which one of these apply to that Code of Ethics because I just don't remember the Code of Ethics at this point.<sup>232</sup>

Mr. McLinko was similarly unable to identify any of the listed behaviors as being “completely legal”; and when asked whether the conduct listed in these categories were in line with bank policies, Mr. McLinko responded:

In line with bank policies, I can't -- I don't know what "other" means. The rest of them, you'd almost have to see the individual circumstances to know that. I wouldn't think that -- as I look at this, though, in the various -- some of the

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<sup>227</sup> *Id.*

<sup>228</sup> *Id.*. Note that the pie chart included in this exhibit provided graphic interpretation of data from beyond the relevant period and thus is not included in this analysis. R. Ex. 4009 at 3.

<sup>229</sup> Tr. (McLinko) at 8458.

<sup>230</sup> Tr. (McLinko) at 8458.

<sup>231</sup> Tr. (McLinko) at 8546; R. Ex. 4009 at 2.

<sup>232</sup> Tr. (McLinko) at 8551.

definitions, the bank policy -- I don't know the bank policy, but it wouldn't seem to align with it.<sup>233</sup>

During cross-examination, Mr. McLinko was asked whether – at the time this presentation was made to Mr. Julian – he was familiar with the processes employed by the Sales Quality team to determine whether to refer an allegation to Corporate Investigations, and he responded that he was not familiar with that process, adding, “my team may have been.”<sup>234</sup>

Ms. Russ Anderson testified that she agreed that during the relevant period, “operational risk” was defined as “all risks excluding credit and market, inclusive of risks we have traditionally viewed as loss prevention and team member behavior (sales quality/sales integrity, internal fraud, ethics violations, etc.).”<sup>235</sup> Ms. Russ Anderson testified that when employees engaged in sales practices misconduct during the relevant period, this posed operational risk, reputational risk, regulatory risk, and compliance risk for the Bank.<sup>236</sup>

Through the 2013 performance review, Ms. Russ Anderson reported that it was her responsibility to “[f]ocus on reputation management and keep the Community Banking lines of business out of trouble by identifying and mitigating key operating risks in the businesses.”<sup>237</sup> She further identified her responsibility to “[b]uild a culture of accountability with strong controls that help ensure no material operational losses.”<sup>238</sup>

One of the events that occurred during the 2013 performance year started with a May 9, 2013 letter sent anonymously [under the name “Mule”] to CEO John Stumpf and head of Community Banking, Ms. Tolstedt.<sup>239</sup> Once received, Ms. Tolstedt forwarded the emailed letter to Ms. Russ Anderson, and Ms. Russ Anderson forwarded it to Michael Bacon (for Corporate Security) and Cindy Walker (SVP – Manager, Sales Quality), with a request that both look at what had been sent.<sup>240</sup>

The letter from Mule reads as follows:

Good morning Mr. Stumpf,

I am a current Branch Manager in the North Ocean District in New Jersey. I have some serious concerns about the leadership in our market. There is a huge amount of unethical practices going on within the market. We are being

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<sup>233</sup> Tr. (McLinko) at 8552-53.

<sup>234</sup> Tr. (McLinko) at 8555.

<sup>235</sup> Tr. (Russ Anderson) at 9520; R. Ex. 7256 at 1.

<sup>236</sup> Tr. (Russ Anderson) at 9520-22.

<sup>237</sup> Tr. (Russ Anderson) at 9536; R. Ex. 5214 at 3.

<sup>238</sup> R. Ex. 5214 at 3.

<sup>239</sup> Tr. (Russ Anderson) at 10118; OCC Ex. 261.

<sup>240</sup> OCC Ex. 261 at 4.

coerced to open checking accounts so the market is at goal, when the branches are closed. I have emails printed out, showing the threats of being placed on corrective action and showing that we must put a DDA on the system and to call when we get it. Until then I assume, we would just keep working into the night? It is my understanding that we cannot open any DDAs without customers being present with signatures and [sic] funding. There are branches where bankers are falsifying Drivers Licenses for customers just to get an account. I could go on for hours with the knowledge and things I have seen.

It's amusing that the upper leadership within South Jersey cannot understand why the Sales Quality can't be brought under control, when they are the ones driving the train off the tracks. I do not know what direction to take anymore. I know of so many things going on in the market it's scary. There are managers leaving for lunch and coming back drunk, and working at a car dealership during Wells Fargo time. Over time I have accumulated quite some evidence and reported it to the ethics line.

I am a proud employee of Wells Fargo. I put Wells Fargo before my family sometimes. However, I am questioning would Wells Fargo have my back? From what I see I do not believe so. I am looking into contacting the media to let customers be aware of the predatory sales practices. I believe that most of the employees will do the same if I spoke with them about it.

I respect Wells Fargo and yourself, Mr. Stumpf – make the change.<sup>241</sup>

Presented with this correspondence, Mr. Bacon wrote in response to Ms. Russ Anderson's email.<sup>242</sup> He reported, "We have had significant issues in this market, so not a total surprise. Cases are 2 to 1 compared to rest of the northeast, and up 36% since same time period last year. We will research EthicsLine reports and we will send an email to the address to see if we can't get more specifics."<sup>243</sup>

When questioned during cross-examination about her reaction to this letter, Ms. Russ Anderson responded, "I didn't know what to think since this came from an unknown person, which is why I forwarded it up the chain to Michael Bacon and Cindy Walker to do some research."<sup>244</sup> She testified, however, that she did consider Mr. Bacon's information to be truthful.<sup>245</sup>

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<sup>241</sup> *Id.* at 5. The May 9, 2013 message from Mule is also present in the record at OCC Ex. 989 at 1-2.

<sup>242</sup> OCC Ex. 261 at 4.

<sup>243</sup> *Id.*

<sup>244</sup> Tr. (Russ Anderson) at 10120.

<sup>245</sup> Tr. (Russ Anderson) at 10121.



Elaborating, Ms. Russ Anderson testified:

As is shown in the rest of the email, there was a lot of work done around this particular complaint in addition to reaching back out through systems to speak to the Mule, who didn't provide any further information, never responded back to corporate investigations or the SSCOT team.<sup>246</sup>

Ms. Walker responded as well, suggesting:

Let's have Glen and Mike touch base to work out a game plan. We can start some research regarding pattern of EL allegations and analysis from the respective area. Mike can convey any additional detail he acquires from the letter writer – 'mule' – interesting!

I am aware that we continue to have issues specific to the NJ footprint and in fact were in the process of partnering with Mike to discuss with Michelle Lee SQ and CI trends. Before we do that I would like to see what surfaces from the analysis relevant to this letter.<sup>247</sup>

After Ms. Russ Anderson expressed support for Ms. Walker's plan, a follow up message indicated that an investigator had spoken with Mule. Notwithstanding Ms. Russ Anderson's averment that she did not know what to think about the letter because it came from an unknown person, there is nothing in the record suggesting the correspondent was anything other than what he claimed to be – a Branch Manager in the North Ocean District in New Jersey. The investigator reported, however, that she did not receive such documentation from Mule.<sup>248</sup>

Glen Najvar, Project Management Manager, reported that Sales Quality "conducted a comprehensive overview of all 11 stores in the Northern Ocean District (S NJ Region), and data findings "yielded potential consent concerns in 6 of the 11 stores (products ranging from checking/savings, Debit Cards, Credit Cards, and Online Banking)."<sup>249</sup>

When presented with the May 9, 2013 email from Mule during cross-examination, Mr. McLinko testified that Enforcement Counsel was correct in understanding that this email did not lead him to conclude there was a systemic problem with sales practices in the Community Bank.<sup>250</sup>

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<sup>246</sup> Tr. (Russ Anderson) at 10122.

<sup>247</sup> OCC Ex. 261 at 4.

<sup>248</sup> *Id.* at 1.

<sup>249</sup> *Id.*

<sup>250</sup> Tr. (McLinko) at 8854; OCC Ex. 989 at 1-2.

Mr. McLinko identified an August 20, 2013 email from Marty Weber of Corporate Investigations regarding Sales Integrity Case Update – with data through August 15, 2013.<sup>251</sup> Data included with the email reflected Corporate Investigations by Region were widespread – with double-digit increases in Sales Integrity Violations and double-digit increases in investigations generally throughout the nation.<sup>252</sup>

In his transmittal email from Corporate Investigations, Mr. Weber wrote, “There is a lot of data, 51 pages, but there are clearly some good news stories and some areas which are in need of attention.”<sup>253</sup> When asked during cross-examination whether the data and the substantial report presented by Corporate Investigations led him to conclude there was a systemic problem with Sales Practices misconduct in the Community Bank, Mr. McLinko responded:

I don't recall what I said about reviewing these documents or not, so I can't tell you if I reviewed the documents. I see my Senior Audit Manager responsible for this area had also received it, and he would have had that as part of his role and responsibilities to look at this documentation and inform me if he felt there were issues.<sup>254</sup>

Evidence of similar increases in the West Coast Region was included in an August 19, 2013 email transmission from Stephanie Wardlaw to Mr. McLinko and others.<sup>255</sup> Among Sales Integrity Violation cases reported in North Central California, False Entries/CIP violations increased 73%; Customer Consent violations increased 83% in Oregon; Code of Ethics violations increased 117% in the San Francisco Bay area.<sup>256</sup>

Mr. McLinko was asked during cross-examination whether any of the data reported in this transmission led him to believe there was a systemic sales practices misconduct with the

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<sup>251</sup> Tr. (McLinko) at 8855-56; OCC Ex. 273 (email); OCC Ex. 274 (summary of reported cases); OCC Ex. 275 (2013 Mid-Year EthicsLine Update, Regional Banking – August 20, 2013, by Marty Weber, Corporate Investigations).

<sup>252</sup> OCC Ex. 274 at 1. Examples include: 38% increase in Customer Consent violations in San Francisco, OCC Ex. 274 at 7; 114% increase in Customer Consent violations in Oregon, *id.* at 9; 34% increase in Sales Integrity Violations in All Northeast Regions, *id.* at 10; 52% increase in Customer Consent violations in New Jersey, *id.* at 11; 160% increase in Referrals violations in Arizona, *id.* at 16; 40% increase in Sales Integrity Violations in Washington State, *id.* at 19; 19% increase in Sales Integrity Violations in All Florida Regions, *id.* at 21; 16% increase in Sales Integrity Violations in All Mountain Midwest Regions, *id.* at 27; and 38% increase in Sales Integrity Violations in Iowa-Illinois, *id.* at 30.

<sup>253</sup> OCC Ex. 273 at 1.

<sup>254</sup> Tr. (McLinko) at 8856.

<sup>255</sup> Tr. (McLinko) at 8858; OCC Ex. 1174 (email transmission); OCC Ex. 1175 (Summary of cases reported).

<sup>256</sup> OCC Ex. 1175 at 4-9.

Community Bank, and he responded that he did not believe he would even read the report, and “since I don’t recall reviewing it, I don’t know that it would have” led to such a belief.<sup>257</sup>

Evidence of similar increases in the Pacific Midwest Region was included in an April 2, 2014 email transmission from Gregory Harmon to Mr. McLinko and others.<sup>258</sup> A 21% increase in Sales Integrity violations (including a 49% increase in Customer Consent violations) was reported in the LA Metro/Orange County areas;<sup>259</sup> a 13% increase in Ethics Code violations was reported in Colorado;<sup>260</sup> a 29% increase in Customer Consent violations was reported in Minnesota;<sup>261</sup> a 400% increase in Referrals violations was reported in Iowa-Illinois;<sup>262</sup> and a 67% increase in False Entries/CIP violations was reported in Wisconsin-Michigan.<sup>263</sup>

When asked whether any of the data contained in this transmission led him to believe that there was a systemic sales practices misconduct problem with the Community Bank, Mr. McLinko responded by testifying that he did not read the information when he received it, so nothing in the transmission would have led to him reaching such a conclusion.<sup>264</sup>

In 2013, WFAS “transitioned to a new methodology to increase transparency in audit work and results, as well as ensure coverage of all businesses and their associated activities.”<sup>265</sup> In February 2014, there were 116 risk-assessable business units (RABUs) in the business hierarchy – and WFAS “aligns the RABUs to the corresponding Operating Committee Group.”<sup>266</sup> Under the process framework implemented in 2013, WFAS reported it would be able to “identify common business activities which may warrant cross-enterprise reviews as well as provide the ability to analyze trend data throughout the enterprise.”<sup>267</sup> The “process level” “represents the business activities performed and really defines the point at which audit work can

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<sup>257</sup> Tr. (McLinko) at 8858-59.

<sup>258</sup> Tr. (McLinko) at 8863-64; R. Ex. 5651 (email transmission); R. Ex. 5657 (Summary of Reported Cases).

<sup>259</sup> R. Ex. 5657 at 3.

<sup>260</sup> *Id.* at 5.

<sup>261</sup> *Id.* at 8.

<sup>262</sup> *Id.* at 12.

<sup>263</sup> *Id.* at 14.

<sup>264</sup> Tr. (McLinko) at 8864-65. The record reflects that Respondents’ Exhibits 5651 and 5657 were not admitted, based on a finding that the contents were repetitive; accordingly, the two exhibits are in the record as proffered evidence only. Tr. (McLinko) at 8866. There was, however, no motion to strike PM’s testimony related to those exhibits, and as such the testimony remains as evidence in the record.

<sup>265</sup> OCC Ex. 2107 at 6.

<sup>266</sup> *Id.*

<sup>267</sup> *Id.* at 7.

be performed.”<sup>268</sup> WFAS uses the process level “in defining the ‘auditable’ segments of the company and for reporting and analytics.”<sup>269</sup>

Under the “process level,” once the business unit or RABU has been identified and the company’s business activities have been confirmed, WFAS “begins building the comprehensive inventory of which activities/processes are performed within each business unit. It is at this individual process level that WFAS can most easily measure and understand the risks that an activity poses to the business.”<sup>270</sup> In 2014, WFAS had 2,159 RABU-processes within its audit universe, and within this universe it performs a risk assessment “to determine the level of risk and frequency in which the business activity should be audited.”<sup>271</sup>

### **Mr. McLinko’s Reporting Relationships**

Mr. McLinko identified organization charts dated December 10, 2012, which identified him as one of nine direct reports to Chief Auditor David Julian during the relevant period.<sup>272</sup> He testified that as EAD responsible for Community Banking and Operations, his audit responsibilities extended to all of the business units in CBO – including Deposit Products, Virtual Channels (the Bank’s online portal), Regional Banking, Customer Connections (the Bank’s call center), Business Banking, and Global Remittance.<sup>273</sup> He explained that credit cards “could be sold at the branch” but that CBO did not have responsibility for auditing credit card services.<sup>274</sup> He estimated that 60 to 70 percent of all audit work under his direction was devoted to the Community Bank versus the operations group.<sup>275</sup>

Mr. McLinko testified that as one of WFAS’s executive audit directors, he was part of the Audit Management Committee (AMC), which was responsible for setting WFAS’s strategy, including “what is our resourcing plan, what is our audit methodology plan, training, things along those lines.”<sup>276</sup> He testified that all EADs for WFAS were on the Committee, as was Chief Auditor David Julian.<sup>277</sup> He testified that included in the AMC during the relevant period was Andrew Shipley, whom Mr. McLinko stated, “had responsibilities for corporate finance”, which

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<sup>268</sup> *Id.* at 7.

<sup>269</sup> *Id.*

<sup>270</sup> *Id.* at 8.

<sup>271</sup> *Id.* at 9.

<sup>272</sup> Tr. (McLinko) at 7765, 7880; R. Ex. 18305 at 2. See also OCC Ex. 2107 (WFAS 2014 Audit Plan, February 25, 2014) at 30, WFAS leadership chart.

<sup>273</sup> Tr. (McLinko) at 7766-68.

<sup>274</sup> Tr. (McLinko) at 7768.

<sup>275</sup> Tr. (McLinko) at 7769.

<sup>276</sup> Tr. (McLinko) at 7770.

<sup>277</sup> Tr. (McLinko) at 7770.

included HR activities.<sup>278</sup> He testified that during the relevant period Mr. Shipley's group "took over the responsibilities for auditing incentive compensation Wells Fargo-wide."<sup>279</sup> He said he thought Mr. Shipley's group also was responsible for auditing EthicsLine, but did not know this for certain – but knew CBO was not responsible for auditing EthicsLine.<sup>280</sup> According to Mr. McLinko, the CBO also was not responsible for auditing Corporate Investigations.<sup>281</sup>

Mr. McLinko testified that between 30 and 35 auditors worked in the CBO group in 2013, and identified employees who reported directly to him – including Senior Audit Managers (SAM) – Bart Deese, Janet Malvitz, and Mark Teuschler.<sup>282</sup> He testified this number grew to between 40 and 45 between 2013 and 2016.<sup>283</sup> According to Mr. McLinko, SAMs "had the responsibility for developing the annual audit plan around their business units that they had responsibility for auditing."<sup>284</sup> He testified that once that plan was developed, "they then would be involved in the planning, the execution and the reporting on the audit work that was done."<sup>285</sup>

Mr. McLinko testified that an Auditor in Charge would be responsible for one audit at a time; a supervisor would have two or more audits going on at the time; the supervisor then reported to a Senior Audit Manager.<sup>286</sup> When asked whether he was involved with actually performing any audit work, Mr. McLinko responded, "I was not involved with performing the work. . . . That was not my role."<sup>287</sup> He added he had no responsibility for scoping audits – where scoping means "that when you have -- when the team, the audit team, goes into the area that they're auditing, they make a decision on what it is they wish to audit, so they're scoping the work right there."<sup>288</sup>

Mr. McLinko said he neither completed nor reviewed workpapers – where workpapers "are the documentation that supports the audit activities for the audit . . . being performed", adding that workpapers "needed to be reviewed by at least an AIC or supervisor, and . . . then

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<sup>278</sup> Tr. (McLinko) at 7771.

<sup>279</sup> Tr. (McLinko) at 7771; see also, "22-03-07 Respondents' Amended Revised Errata Days 9 -38" at page 67. Ordered through Second Supplemental Order Regarding Hearing Transcript Errata.

<sup>280</sup> Tr. (McLinko) at 7772.

<sup>281</sup> Tr. (McLinko) at 7772.

<sup>282</sup> Tr. (McLinko) at 7774-76; R. Ex. 18305 at 9.

<sup>283</sup> Tr. (McLinko) at 7776.

<sup>284</sup> Tr. (McLinko) at 7774.

<sup>285</sup> Tr. (McLinko) at 7774-75.

<sup>286</sup> Tr. (McLinko) at 7790.

<sup>287</sup> Tr. (McLinko) at 7791.

<sup>288</sup> Tr. (McLinko) at 7792.

there was a sample of workpapers that also needed to be secondarily reviewed by the Senior Audit Manager.”<sup>289</sup>

Mr. McLinko said the same was true with audit reports – that he “had full reliance” on the work of the auditors working below him and was “very much” comfortable doing that.<sup>290</sup> His reasoning for having this level of comfort was – notwithstanding the concerns Mr. Julian reported regarding the quality of the auditors at WFAS in 2013 – WFAS auditors “were highly credentialed with CIA, CPAs, other sorts of designations. They had the appropriate training that they were required to have, and many of them had spent numerous years in auditing the Community Bank operations areas.”<sup>291</sup>

### **Mr. McLinko’s Roles and Responsibilities – Committee Membership**

Mr. McLinko testified that in addition to his duties as an Executive Audit Director at WFAS, and beyond his work “including training, methodology development, diversity, as well as running the charter Charlotte office”, he was a member of the Audit Management Committee, that starting in 2014 he was a member of the Community Bank Risk Management Committee, and was a nonvoting member of the Community Bank Internal Fraud Committee.<sup>292</sup> He testified that his was a nonvoting position on the Committee because “basically the bottom line is,” “as an auditor, we need to maintain our independence” and serving in a voting capacity “would be impacting your independence.”<sup>293</sup> Nothing in the record, however, supports Mr. McLinko’s testimony that under the Committee’s Charter or through records of Committee meetings that his position was non-voting.<sup>294</sup>

#### *Audit Management Committee*

Mr. McLinko identified the January 24, 2014 WFAS Policy Manual and testified that as Executive Audit Director for Community Banking, he was a member of the Audit Management Committee (AMC).<sup>295</sup> The Manual provides that the AMC “uses the top down assessment at the OCG [Operating Committee Group] level to assist in determining resource allocations for audit activities related to each OCG.”<sup>296</sup> Mr. McLinko testified that in 2013 he was responsible for the Community Bank Operating Committee Group, such that this portion of the Policy Manual

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<sup>289</sup> Tr. (McLinko) at 7792-93.

<sup>290</sup> Tr. (McLinko) at 7793.

<sup>291</sup> Tr. (McLinko) at 7794.

<sup>292</sup> Tr. (McLinko) at 7788.

<sup>293</sup> Tr. (McLinko) at 7789.

<sup>294</sup> See OCC Ex. 1272, which provides for dual roles applicable to PM: as a member of the IFC, and as a member of WFAS; and provides no indication of a non-voting status for either role.

<sup>295</sup> Tr. (McLinko) at 8471; OCC Ex. 1694 (same as R. Ex. 12281) – WFAS Policy Manual.

<sup>296</sup> Tr. (McLinko) at 8474; R. Ex. 12281 at 27.

should describe his responsibilities.<sup>297</sup> He testified that he would assist in determining resource allocations for audit activities in the Community Bank’s OCG, as he was the OCG’s “owner” at the time covered by this Policy Manual.<sup>298</sup>

Under the Policy Manual, OCG Owner Responsibilities included:

- Complete the Strategic Risk and Enterprise Risk Management Assessments for the OCG.
- Determine resource allocation for the OCG with the collective Audit Management Committee (AMC).
- Escalate significant deficiencies and changes in resource allocation to the AMC for decisioning [*sic*].
- Assess applicable processes, risks, and controls to the OCG support functions.
- Create an audit plan based on the OCG and enterprise risk profiles.
- Establish business monitoring and A&E related reporting associated with the OCG.<sup>299</sup>

During cross-examination while referring to the Policy Manual, Enforcement Counsel asked Mr. McLinko whether, per the Policy, “Resource Deployment” was one of the responsibilities he had at the time covered by the Manual, and Mr. McLinko responded, “it’s a combined responsibility” of his and the Senior Audit Manager to “determine[] how many resources you need to complete that work. That would be resource allocation, I think.”<sup>300</sup>

During cross-examination, when presented with the Policy language that provided: “The Executive Audit Director/Audit Director and Senior Audit Managers (SAMs) are responsible for determining how the WFAS resources are deployed by identifying the specific RABUs and processes to be scheduled for the OCG”,<sup>301</sup> concerning the determination of what to audit in any given year, Enforcement Counsel asked, “per this Policy that was one of your responsibilities along with the SAMs, is that correct?” and Mr. McLinko responded, “Per the Policy, the SAM is the individual who determined the resource and they combined it for me for the overall team.”<sup>302</sup> There is, however, no support for Mr. McLinko’s testimony that “the SAM is the individual who determined the resource” – where the Policy Manual directs these responsibilities to both the EAD and the SAM.<sup>303</sup>

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<sup>297</sup> Tr. (McLinko) at 8474-75.

<sup>298</sup> Tr. (McLinko) at 8475; R. Ex. 12281 at 27-29.

<sup>299</sup> Tr. (McLinko) at 8476; R. Ex. 12281 at 29.

<sup>300</sup> Tr. (McLinko) at 8477-78.

<sup>301</sup> R. Ex. 12281 at 29.

<sup>302</sup> Tr. (McLinko) at 8477-78.

<sup>303</sup> R. Ex. 12281 at 29.

Under the Policy Manual regarding “Supervision and Review”, “[t]he Chief Audit Executive is accountable for the execution of audit work. Responsibility for the accuracy and completeness of audit work is delegated to the Executive Audit Director/Audit Director and Senior Audit Manager, but cannot be delegated further.”<sup>304</sup> When asked during cross-examination if this described his responsibilities as of the date of the Policy Manual, Mr. McLinko responded, “It describes the overall responsibility, but not how it was actually completed.”<sup>305</sup>

The Policy Manual provides that during the course of an engagement, “auditors analyze identified exceptions to determine if there is a lack of controls, and any systemic, material control weaknesses or deficiencies. An Audit Issue form is created/written if an exception/issue is:

- Significant enough to report to management
- Documented by facts or empirical data, not opinions, and by evidence that is sufficient, competent, and relevant
- Objectively developed without bias or preconceived ideas
- Convincing enough to compel action to correct the exception<sup>306</sup>

As part of “Issue Identification”, the Policy Manual provides the following set of standards:

Auditors are diligent in developing the issue so it is logical, reasonable, compelling, and will motivate corrective action. All Issues, when fully developed, include or have considered the elements of a well-designed Issue: Background, Criteria, Condition, Root Cause, Risk (Effect), and Recommendation.<sup>307</sup>

With respect to root cause, the Policy Manual provides, “[t]his element may or may not be appropriate because it may be self-evident. The reason for the difference between the expected and actual conditions (why the difference exists).”<sup>308</sup>

With respect to “Risk”, the Policy Manual provides:

The risk of exposure the auditable unit and/or others encounter because the condition exists (the probability and impact of the difference). This is the portion of the Issue that convinces the business partner and higher management that the issue, if permitted to continue, will or has the potential to cause serious harm and cost more than the action needed to correct the

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<sup>304</sup> R. Ex. 12281 at 87.

<sup>305</sup> Tr. (McLinko) at 8479.

<sup>306</sup> R. Ex. 12281 at 73.

<sup>307</sup> *Id.*

<sup>308</sup> *Id.*



problem. In economy and efficiency issues, the risk is usually measured in dollars. In adequacy and effectiveness issues, the risk is usually the inability to accomplish some desired or mandated end result.<sup>309</sup>

The Policy Manual then provides that “[a]ll potential issues are communicated to the business partner as soon as they are detected. Timely escalation of issues is critical to the audit process.”<sup>310</sup>

Mr. McLinko identified WFAS Policy Manuals dated January 24, 2013,<sup>311</sup> April 2014,<sup>312</sup> December 31, 2014,<sup>313</sup> December 10, 2015,<sup>314</sup> February 2016,<sup>315</sup> and March 31, 2016<sup>316</sup> and testified that his answers to questions presented regarding the 2013 Manual would be the same with respect to the same provisions found in the subsequent Manuals, “as long as it’s understood that it commented in there about the delegation of responsibilities – either – and/or – so, yes.”<sup>317</sup>

When during cross-examination he was asked by Enforcement Counsel whether throughout the period from 2013 to 2016 he was, under Audit’s own policies, always responsible for the accuracy of the audit work performed by his team, Mr. McLinko answered, “Yes, in combination myself with my Senior Audit Managers per what the Policy says as . . . far as delegation, yes, I was.”<sup>318</sup> He said the same was true regarding being responsible for the completeness of the audit work performed by his team.<sup>319</sup>

When asked, however, whether (throughout the relevant period) he ever believed that he was not responsible for assessing the risks in the Community Bank, including the risk posed by the Community Bank sales practices, Mr. McLinko answered: “It was my team’s responsibility for assessing those risks under my guidance.”<sup>320</sup> Pressed to provide a direct answer to the question presented, Mr. McLinko responded, “Yes, I believe I had that responsibility, along with the delegation to my Senior Audit Managers” and had the responsibilities for assessing the risks

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<sup>309</sup> R. Ex. 12281 at 73.

<sup>310</sup> *Id.*

<sup>311</sup> Tr. (McLinko) at 8474; R. Ex. 12281.

<sup>312</sup> Tr. (McLinko) at 8480-81; OCC Ex. 2091.

<sup>313</sup> Tr. (McLinko) at 8483; OCC Ex. 2093.

<sup>314</sup> Tr. (McLinko) at 8490; OCC Ex. 2092.

<sup>315</sup> Tr. (McLinko) at 8493; OCC Ex. 2090.

<sup>316</sup> Tr. (McLinko) at 8483-84; OCC Ex. 2092.

<sup>317</sup> Tr. (McLinko) at 8491-92.

<sup>318</sup> Tr. (McLinko) at 8497-98.

<sup>319</sup> Tr. (McLinko) at 8498.

<sup>320</sup> Tr. (McLinko) at 8499.

in the Community Bank, including Community Bank sales practices.<sup>321</sup> He also acknowledged that as part of the Audit Management Committee he had responsibility for allocating WFAS's resources in the various Operating Committee Groups, including the Community Bank OCG.<sup>322</sup>

Mr. McLinko testified that at no time during the relevant period did he feel he could not ask Mr. Julian or the Audit Management Committee for more resources if necessary to effectively execute his responsibilities as Executive Audit Director for the Community Bank.<sup>323</sup>

### ***Community Banking Internal Fraud Committee***

Ms. Russ Anderson testified that she was on the Fraud Risk Committee.<sup>324</sup> She testified that it was her practice to review reporting she received on the Internal Fraud Committee, and opined that the Committee was a helpful and important committee.<sup>325</sup> She testified that, "broadly speaking," she understood that as a member of the Internal Fraud Committee she was charged with ensuring that internal fraud risks were appropriately managed in the Community Bank.<sup>326</sup> As a Group Risk Officer, Ms. Russ Anderson had specific duties under the Policy: "Group Risk Officers (GROs) and their delegates are responsible for opining on the adequacy of internal and external fraud risk management and providing credible challenge to the businesses they oversee."<sup>327</sup>

Mr. McLinko testified that he was a member of the Community Bank's Internal Fraud Committee.<sup>328</sup> With respect to his membership in the Committee, Mr. McLinko testified, "most . . . of the senior leaders within Community Bank were there."<sup>329</sup> He testified that the Committee was established by the Corporate Investigations group in 2013 – so it was not a Committee of WFAS – and that it met twice a year and Mr. Bacon "led the meeting."<sup>330</sup>

Mr. McLinko identified the Corporate Fraud Risk Management Policy, dated August 1, 2013.<sup>331</sup> The Policy's stated purpose "is to promote accountability, measurability, partnership, and transparency of fraud risk management at Wells Fargo by setting the structure and

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<sup>321</sup> Tr. (McLinko) at 8500-01.

<sup>322</sup> Tr. (McLinko) at 8502.

<sup>323</sup> Tr. (McLinko) at 8503-04.

<sup>324</sup> Tr. (Russ Anderson) at 9275.

<sup>325</sup> Tr. (Russ Anderson) at 9547-48.

<sup>326</sup> Tr. (Russ Anderson) at 9548.

<sup>327</sup> OCC Ex. 1272 at 7.

<sup>328</sup> Tr. (McLinko) at 8461.

<sup>329</sup> Tr. (McLinko) at 7919.

<sup>330</sup> Tr. (McLinko) at 7918-19.

<sup>331</sup> OCC Ex. 1272.

expectations for business fraud risk management programs.”<sup>332</sup> It identified those “particularly responsible for its implementation” to include “business, fraud, and operational risk managers at the business, group, and corporate levels.”<sup>333</sup> Under the Policy, “[e]ach Wells Fargo business is responsible for managing internal and external fraud risk in a consistent and effective manner, in order to protect our customers, shareholders, and the company.”<sup>334</sup> “[S]tandards and requirements for the businesses” are set by Corporate Fraud Risk Management (CFRM), a part of Financial Crimes Risk Management (FCRM).<sup>335</sup> CFRM “monitors and oversees the management of these risks on a company-wide basis.”<sup>336</sup>

Mr. McLinko had distinct responsibilities both as a member of Community Banking’s Internal Fraud Committee (IFC), and as an auditor in Wells Fargo Audit Services.<sup>337</sup> As a Business Internal Fraud Committee, the Policy directed members in Community Banking’s IFC to “ensure that all stakeholders who share responsibility for internal fraud risk management receive appropriate reporting and have a forum to address broad team member misconduct matters. The IFC assists the GRO [Group Risk Officer] in addressing internal fraud matters specific to business practices and processes.”<sup>338</sup> The Policy provides that IFCs “are accountable to the Team Member Misconduct Executive Committee (TMMEC).” CSI (Corporate Security Investigations) “chairs each IFC, facilitates meetings held at least semi-annually, and provides the committee with Internal Fraud reporting.”<sup>339</sup>

As a member of WFAS, Mr. McLinko had duties “[i]n addition to general operational risk management roles and responsibilities”.<sup>340</sup> As the CBO leader for WFAS, the Policy provided that WFAS:

- Provides independent evaluation of the fraud controls that management has designed and implemented, including direct business controls
- Performs direct audits of business fraud programs and controls
- Communicates fraud-related audit findings to Corporate Fraud Risk Management

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<sup>332</sup> *Id.* at 1.

<sup>333</sup> *Id.*

<sup>334</sup> *Id.*

<sup>335</sup> *Id.*

<sup>336</sup> *Id.*

<sup>337</sup> *Id.* at 5, 7.

<sup>338</sup> *Id.* at 5.

<sup>339</sup> *Id.*

<sup>340</sup> *Id.* at 7.

- Consults with Corporate Fraud Risk Management as necessary, during the annual audit planning cycle as well as during individual audits, regarding information that may address fraud risk or controls<sup>341</sup>

The Policy addressed “Escalation” in these terms:

Policy cannot account for every possible situation. To address situations not covered by policy, request a change to this policy or the related standards, or recommend and [sic] alternative practice, fraud managers contact the policy manager indicated on the last page of this document [Jim Richards, Chief Operational Risk Officer at Revision Date 8/1/2013]. The policy manager will work with the requesting business to address the business’s needs and escalate the request as necessary.

The chief operational risk officer may approve policy changes or alternative implementation practices for certain businesses after consulting with senior executive business management, GROs and appropriate corporate and business subject matter experts. If needed, matters will be escalated to the Enterprise Risk Management Committee or Wells Fargo’s Operating Committee for resolution.<sup>342</sup>

The Policy defined “Fraud” as “[a] deliberate misrepresentation which may cause another person or entity to suffer damages, usually monetary loss. Wells Fargo distinguishes between two major types of fraud: internal and external.”<sup>343</sup> It defines “Misrepresentation” as “false or misleading representation or concealment of a fact”, it defines “True Name Fraud” as “fraud that occurs when an individual materially misrepresents his or her identity by using identifying information that is the valid identity of another real individual”, and defines “Internal Fraud” thus:

An event in which any suspected or known fraud operator is a team member or managed resources hired by Wells Fargo, who:

- Commits misconduct meeting the definition of fraud, during the course of his or her employment
- Is a customer who may have committed fraud
- Colludes with a customer who may have committed fraud
- Conducts, enables, or contributes to fraud<sup>344</sup>

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<sup>341</sup> OCC Ex. 1272 at 7.

<sup>342</sup> *Id.* at 8, 10.

<sup>343</sup> *Id.* at 9.

<sup>344</sup> *Id.*

During cross-examination by Enforcement Counsel, Mr. McLinko was asked whether he believed it was incumbent upon him as a member of the Community Bank’s IFC to pay attention to the reporting that he received.<sup>345</sup> Although the question seeks a yes or no answer, Mr. McLinko deflected, responding: “As a member of the Committee, along with the other individuals who were part of that Committee, you were . . . you looked at information that was presented”, avoiding answering whether it was important that he pay attention to that information.<sup>346</sup>

When asked in further cross-examination, “Did you believe that it was incumbent upon you as a member of the Community Bank Internal Fraud Committee to pay attention to that reporting [of emails related to his membership in the Community Bank IFC that included attached presentations] that you received, Mr. McLinko again avoided answering directly, responding: “I believe that as the EAD responsible for Community Bank and Operations, that either myself or the . . . other individuals who were on that Committee, which included my SAMs, would – could and would review some of the data.”<sup>347</sup>

When asked specifically about his own responsibility – not that of CBO’s SAMs – to pay attention to the reporting that he received, Mr. McLinko responded: “[W]hen you say, ‘pay attention’, can you just explain that, please?” and then stated “[t]hen the information that is presented as part of the Committee, I would at least review or scan some of it, yes”.<sup>348</sup> When asked whether he believed it was incumbent upon him to pay attention to all of the reporting that he received, Mr. McLinko responded, “No.”<sup>349</sup>

Mr. McLinko identified the Meeting Agenda showing that in February 2013 Mr. Bacon facilitated the inaugural meeting of the Committee.<sup>350</sup> He testified that he attended the meeting, held on February 21, 2013, as did his Senior Audit Managers.<sup>351</sup>

According to the Agenda, Mr. Bacon anticipated covering numerous topics and set aside time for discussion, a line-of-business update, and the identification of required action items.<sup>352</sup> The topics included the presentation of an overview of corporate fraud policy objectives, goals and objectives specific to lines of business, a description of the responsibilities of Committee members, a report on the Team Member Executive Committee at the Corporate level, a

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<sup>345</sup> Tr. (McLinko) at 8462.

<sup>346</sup> Tr. (McLinko) at 8462.

<sup>347</sup> Tr. (McLinko) at 8463.

<sup>348</sup> Tr. (McLinko) at 8464.

<sup>349</sup> Tr. (McLinko) at 8464.

<sup>350</sup> R. Ex. 3817 (transmittal email to Ms. Russ Anderson, Mr. McLinko, and others); R. Ex. 3818 (Meeting Agenda); R. Ex. 3819 (Corporate Securities Activities attachment). Note that R. Ex. 3819 concerned data outside of the relevant period and thus is not included in this analysis.

<sup>351</sup> Tr. (McLinko) at 7921-22.

<sup>352</sup> R. Ex. 3818 at 1-2.

discussion of “[n]umerous committees, teams, processes, specific functions”, the identification of team member – as team member, as Customers, and as Individuals, and a review of 2013 Corporate Investigation Key Activities related to the Community Bank and Regional Banking.<sup>353</sup>

Mr. McLinko also identified documents relating to the August 12, 2013 meeting of the Community Banking Internal Fraud Committee.<sup>354</sup> Included in the attachments provided in advance of the meeting were dashboard presentations showing Corporate Investigations activities, including those concerning Sales Integrity violations.<sup>355</sup> The data presented through these attachments indicated an increase in sales integrity violations as well as an increase in Code of Ethics violations in Community Banking and Regional Banking between March and June 2013.<sup>356</sup>

When asked during direct examination whether he attended the August 12, 2013 Committee meeting, Mr. McLinko responded, “I don’t recall.”<sup>357</sup> He testified, however, that it was his practice “to review . . . the meeting agenda for this type of a meeting”.<sup>358</sup>

Through leading questioning by his Counsel during direct examination, Mr. McLinko testified that it was his understanding that information from Corporate Investigations was reported up to the Board of Directors.<sup>359</sup> He testified that although neither he nor anyone on his team had any role in drafting the information that Corporate Investigations provided to the A&E Committee, he understood that information “was reported on a quarterly basis through a separate section in the [Audit & Examination] Committee package.”<sup>360</sup>

***Wells Fargo Code of Ethics Administrator  
Community Bank’s Risk Management Committee***

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<sup>353</sup> Tr. (McLinko) at 7923; R. Ex. 3818 at 1. Note the record includes R. Ex. 3923 (transmittal email to Mr. Julian, Mr. McLinko, and others) and R. Ex. 3924 (Corporate Investigation General Update: 2012 Year End Key Activities Overview, [Audit Management Committee] Meeting). The latter exhibit concerned data outside of the relevant period and thus is not included in this analysis.

<sup>354</sup> Tr. (McLinko) at 7926; R. Ex. 4427 (email from Mr. Bacon to Ms. Russ Anderson, Mr. McLinko, and others); R. Ex. 4229 (Corporate Investigations Dashboard, 2Q2013 DSSG); R. Ex. 4430 (Corporate Investigations Dashboard 2Q2013 Digital Channels Group); R. Ex. 4431 (Corporate Investigations Dashboard 2Q2013 Regional Banking); R. Ex. 4432 (Corporate Investigations Dashboard 2Q2013 Phone Bank); R. Ex. 4433 (Corporate Investigations Dashboard 2Q2013 Business Banking); and R. Ex. 4434 (Corporate Investigations Dashboard 2Q2013 Community Banking).

<sup>355</sup> See, e.g., R. Ex. 4229 (Corporate Investigations Dashboard, 2Q2013 DSSG) at 3.

<sup>356</sup> R. Ex. 4434 (Corporate Investigations Dashboard 2Q2013 Community Banking) at 2-3; R. Ex. 4431 (Corporate Investigations Dashboard 2Q2013 Regional Banking) at 2-3.

<sup>357</sup> Tr. (McLinko) at 7928.

<sup>358</sup> Tr. (McLinko) at 7929.

<sup>359</sup> Tr. (McLinko) at 7929.

<sup>360</sup> Tr. (McLinko) at 7929.

Ms. Russ Anderson testified that as Community Banking’s Chief Risk Officer, she was Chair of the Community Banking Risk Management Committee (CBRMC).<sup>361</sup> Under the 2013 Charter, the purpose of the CBRMC was “to oversee the management of operational and compliance risks inherent in the Community Banking lines of business. This includes the development of appropriate risk identification, measurement and mitigation strategies and reporting, consistent with Wells Fargo’s policies, processes and procedures.”<sup>362</sup>

Membership under the 2013 Charter included the head of Community Banking (Ms. Tolstedt), the Community Banking Chief Risk Officer (Ms. Russ Anderson) as Chairperson, and eight other members – there was no mention of the presence of a representative from Wells Fargo Audit Services in this list of Committee members.<sup>363</sup>

Effective January 2013, the Committee’s primary responsibility during the relevant period was to “understand Community Banking’s operational risk profile and to work with management across Community Banking to ensure risks are managed effectively.”<sup>364</sup>

Ms. Russ Anderson testified that in her role as Chair of the Community Banking RMC, it was her responsibility to inform members of the Committee about both systemic problems and control breakdowns in the Community Bank.<sup>365</sup> She testified that she considered the CBRMC an important committee at the Bank, but testified it was her responsibility to inform the Committee about pervasive and widespread misconduct in the Community Bank only “[i]f I believed there was some”.<sup>366</sup>

Under its 2013 Charter the Community Banking RMC was to meet quarterly “or as frequently as the Committee will deem necessary.”<sup>367</sup> As GRO for Community Banking, Ms. Russ Anderson presided over meetings of the CBRMC, would establish the content of meeting agendas, would ensure that “responsibility is assigned for each initiative undertaken” by the CBRMC, and would ensure that the CBRMC “reviews and assesses the adequacy of the Community Banking RMC charter annually.”<sup>368</sup>

Pursuant to its 2013 Charter, members of the Community Banking RMC were required to understand and evaluate “current and emerging material risks”, “examine trends”, and “assess the strategic implications for business objectives and risk management practices”.<sup>369</sup> Each

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<sup>361</sup> Tr. (Russ Anderson) at 9275, 9769; R. Ex. 5214 at 8; OCC Ex. 660 at 1.

<sup>362</sup> OCC Ex. 660 at 1.

<sup>363</sup> *Id.* at 2.

<sup>364</sup> *Id.* at 1.

<sup>365</sup> Tr. (Russ Anderson) at 9770.

<sup>366</sup> Tr. (Russ Anderson) at 9771.

<sup>367</sup> OCC Ex. 660 at 2.

<sup>368</sup> *Id.*

<sup>369</sup> *Id.* at 1.

member was required to “[w]eigh the relationship between risks; identify combinations of exposures that may change the operational risk portfolio and determine whether an appropriate balance exists between risks and rewards”.<sup>370</sup> They also needed to review and evaluate “risk appetite metrics” and direct action “for metrics out of tolerance”.<sup>371</sup>

Pursuant to its 2013 Charter, the Committee was required to “[i]nitiate or direct the initiation of discussion, escalation or other measures with the appropriate person or forum about any current or emerging risk, trend, business practice or other business or environmental factors” and require that “corrective actions be taken to address any material breakdown of internal controls and assign monitoring responsibility through resolution.”<sup>372</sup>

Pursuant to its 2013 Charter, the Committee was required to oversee and approve “acceptance for high-risk activities, products and markets”.<sup>373</sup> Member of the Committee “[s]erve as the ultimate approval authority for new high-risk products and material changes to existing products, as defined and required by Wells Fargo’s policy.”<sup>374</sup> The Committee had the authority to establish, modify or eliminate Community Banking risk management programs as needed, “in collaboration with the corporate Operational Risk Group.”<sup>375</sup> It was required to ensure that appropriate policies, procedures and processes “exist for adequately identifying, measuring, managing and reporting risks across Community Banking”, and review, validate, interpret and provide guidance to Community Banking business unit “regarding regulatory and operational risk requirements.”<sup>376</sup>

Pursuant to the 2013 Charter:

The scope of reviews and oversight would include, but not be limited to significant new strategies, vendors, business continuity planning, losses, major projects (including implementation and readiness assessment), risk self-assessments, key regulatory and legal issues, conflicts of interest, security, privacy and reputational risk.”<sup>377</sup>

The 2013 Charter also required Committee members to review the status of previously identified risk management concerns and initiatives” and “[i]nform, advise and educate the

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<sup>370</sup> OCC Ex. 660 at 1.

<sup>371</sup> *Id.*

<sup>372</sup> *Id.*

<sup>373</sup> *Id.*

<sup>374</sup> *Id.*

<sup>375</sup> *Id.*

<sup>376</sup> *Id.*

<sup>377</sup> *Id.*



Community Banking leadership about risk management strategies, initiatives and related matters”.<sup>378</sup>

Mr. McLinko identified the March 24, 2015 Community Banking Risk Management Committee Charter, and testified that he was a non-voting member of the Community Bank Risk Management Committee.<sup>379</sup> When asked during cross-examination whether as a member of the Committee he believed it was incumbent upon him to ensure that the Community Bank’s risks were managed effectively, he responded that it was his responsibility to “understand the risk and ensure that Internal Audit . . . had the audit programs for that.”<sup>380</sup>

Under the 2015 Community Banking Risk Management Committee (CBRMC) Charter, the Committee is identified as a “risk governance committee the purpose of which is to oversee the management of key Risk Types to which the Group is exposed, in particular: credit, compliance, operational, BSA/AML, model, strategic, emerging, reputational, and cross-functional risks.”<sup>381</sup> The 2015 Charter provides that the Committee “shall serve as the primary management-level forum for the consideration of the highest priority risk issues resident in Community Banking.”<sup>382</sup>

The 2015 Charter states, “critically, the Committee shall support and assist Wells Fargo’s Enterprise Risk Management Committee (ERMC) in carrying out its risk oversight responsibilities.”<sup>383</sup> The CBRMC’s primary responsibility “is to understand Community Banking’s risk profile and to work with management across Community Banking to ensure risks are managed effectively.”<sup>384</sup> The 2015 Charter provides that this includes, “oversight of the development of appropriate risk identification, measurement and mitigation strategies and reporting, consistent with Wells Fargo’s policies, processes, and procedures.”<sup>385</sup>

The 2015 Charter expressly identified Mr. McLinko as Community Banking’s Executive Audit Director, as a non-voting member of the Committee.<sup>386</sup> It identified Ms. Russ Anderson as Chair and a voting member, as Community Banking Group Risk Officer.<sup>387</sup> It identified Ms. Tolstedt as a voting member, as Head of Community Banking. It prohibits delegation of member

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<sup>378</sup> *Id.*

<sup>379</sup> Tr. (McLinko) at 8467, 8471; R. Ex. 11556.

<sup>380</sup> Tr. (McLinko) at 8471.

<sup>381</sup> R. Ex. 11556 at 1.

<sup>382</sup> *Id.*

<sup>383</sup> *Id.*

<sup>384</sup> *Id.*

<sup>385</sup> *Id.*

<sup>386</sup> *Id.* at 4-5.

<sup>387</sup> *Id.* at 5.

participation “except for occasional instances when a member is unable to attend a meeting and an agenda item requires specific representation from the member’s area.”<sup>388</sup>

Under the 2015 Charter, issues that may be escalated to the Committee include but are not limited to:

- Triggers of Community Banking’s risk appetite metric boundaries, as required
- Violations of Community Banking’s risk management limits, as required
- Violations of Group-level policies, as required;
- Events likely to cause material adverse impact to customers, or to the Company’s reputation or financial results, as required;
- Issues that are likely to be discussed with the Company’s regulators as well as potentially new issues identified by the Company’s supervisors (e.g., forthcoming/potential MRAs and MRIAs), as required; and
- Other matters that, based upon a reasonable manager’s judgment, may adversely impact the Company.<sup>389</sup>

Under the 2015 Charter, the Committee “shall initiate or direct the initiation of discussion, escalation or other measures with the appropriate person or forum about any current or emerging risk, trend, business practice, or other business or environmental factors.”<sup>390</sup>

Under the 2015 Charter, the Committee “shall require that corrective actions be taken to address any material breakdown of internal controls and assign monitoring responsibility through resolution.”<sup>391</sup>

The Committee is required to “escalate matters that require decision-making from a more senior level of the Company to the Head of Community Banking, the Chief Risk Officer, and the relevant member of Corporate Risk, or to the ERMC as appropriate.”<sup>392</sup> The Committee “may further escalate issues that require decision-making from a more senior level of the Company, at its discretion”.<sup>393</sup>

For each escalated issue, the 2015 Charter provides that the Committee “shall have the authority to assess the degree to which the risk owner has identified, assessed, controlled, and mitigated the issue at hand” and “may require further actions to be taken by the risk owner and may require oversight of the issue by the Committee or a designated individual.”<sup>394</sup> The 2015

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<sup>388</sup> *Id.* at 4.

<sup>389</sup> *Id.* at 2.

<sup>390</sup> *Id.*

<sup>391</sup> *Id.*

<sup>392</sup> *Id.* at 3.

<sup>393</sup> *Id.* at 2.

<sup>394</sup> *Id.*

Charter provides that the Committee may “[i]nform, advise, and educate the Community Banking leadership about risk management strategies, initiatives and related matters.”<sup>395</sup>

The 2015 Charter provides that the Committee “shall aggregate and report regularly to the Head of Community Banking and the ERMC information that is sufficient to understand (a) the risk position of the Group, and (b) the performance of Community Banking’s Group Risk Organization.”<sup>396</sup> The 2015 Charter provides further that “periodic and/or ad hoc reports to the Committee on the risk types it oversees are provided by varying committees/forums and/or team members, each of which may escalate key issues and/or issue remediation plans to the Committee for its consideration and/or further escalation. Additional reporting or information on risk issues may be requested by voting members or the Chairperson as needed.”<sup>397</sup>

### **Mr. McLinko’s Application of the Dynamic Audit Planning Process**

Mr. McLinko testified that the CBO followed what he called a dynamic audit planning process, in which “every year the audit teams were tasked with reviewing . . . their operating committee group, their RABUs that they had, and the associated processes that were associated with those to ensure that those were the right processes to be involved.”<sup>398</sup> He testified that having a dynamic audit plan meant that Audit’s annual audit plan could be adjusted after it was approved to address changes in the risk environment.<sup>399</sup> He testified that he felt he could make changes “as long as I could support them whenever I needed to.”<sup>400</sup>

With respect to risk analysis, Mr. McLinko testified that WFAS employed a “risk-based audit approach” as “part of the scope that was done by the senior audit managers and their team. And part of that analysis”. He said, “there was methodology that was part of our standard operating procedures . . . rating a process, what would be high, medium or low. And based on that criteria, the auditors would select a risk.”<sup>401</sup>

Responding to leading questioning by his Counsel during direct examination, Mr. McLinko testified that in 2013 his team performed audits that related to sales controls and processes related to sales practices in the Community Bank.<sup>402</sup> He denied, however, doing any of the testing in connection with those audits, stating that such testing “was led by the Senior Audit Managers” and that the same was true with respect to scoping for the audits.<sup>403</sup>

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<sup>395</sup> R. Ex. 11556 at 2.

<sup>396</sup> *Id.* at 3.

<sup>397</sup> *Id.*

<sup>398</sup> Tr. (McLinko) at 7794-95.

<sup>399</sup> Tr. (McLinko) at 8619.

<sup>400</sup> Tr. (McLinko) at 8619.

<sup>401</sup> Tr. (McLinko) at 7795-96

<sup>402</sup> Tr. (McLinko) at 7930.

<sup>403</sup> Tr. (McLinko) at 7931.

## **Mr. McLinko's Interaction with Regulators**

Mr. McLinko testified that Internal Audit also plays “a critical role” regarding laws and regulations, in “reviewing the controls over the design of it and the effectiveness of the controls over the regulations. . . . Internal Audit is a function that reviews for the system of internal control around regulatory compliance.”<sup>404</sup>

Similarly, Mr. McLinko testified that Internal Audit plays a critical role in informing the Board about the effectiveness of the Bank's internal controls and risk management.<sup>405</sup> He also confirmed that it is important for Internal Audit to be able to have open and frank communications with the bank's regulators.<sup>406</sup>

## **Mr. Julian's Roles and Responsibilities – Committee Membership**

There is evidence in the record that as Chief Auditor, Mr. Julian a member of seven management committees.<sup>407</sup> As a direct report, Mr. McLinko would have access to these committees through Mr. Julian.

### ***Operating Committee Group***

Wells Fargo & Company maintained a leadership group – the Operating Committee Group (OCG) – that was made up of senior Bank employees who directly reported to the holding company's Chief Executive Officer (John Stumpf at the start of the relevant period, and Tim Sloan thereafter).<sup>408</sup> These direct reports, “were responsible for managing their Operating Committee Group” so, for example, Carrie Tolstedt was the head of the Community Bank's Operating Committee Group.<sup>409</sup> Mr. Julian was a member of the Operating Committee Group.<sup>410</sup>

CRO Loughlin reported that the OCG “is an executive-level committee that meets weekly and consists of direct reports of the CEO. The committee provides strategic leadership and has high-level decision-making authority. This committee is chaired by the CEO.”<sup>411</sup>

The WFAS Audit Groups generally aligned with the Operating Committee Groups for the Bank's Lines of Business (including Community Bank) – but, according to Mr. Julian, “[t]here were a couple risk types within Wells Fargo & Company that [WFAS] organized ourselves to specifically audit where there wasn't a specific operating committee member.”<sup>412</sup> As an example,

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<sup>404</sup> Tr. (McLinko) at 8517-18.

<sup>405</sup> Tr. (McLinko) at 8528.

<sup>406</sup> Tr. (McLinko) at 8529.

<sup>407</sup> R. Ex. 740 at 6.

<sup>408</sup> Tr. (Julian) at 5977.

<sup>409</sup> Tr. (Julian) at 5978.

<sup>410</sup> Tr. (Julian) at 6059.

<sup>411</sup> OCC Ex. 1553 at 8.

<sup>412</sup> Tr. (Julian) at 5978-79.

he identified the risk group relating to group responsible for the Bank's Bank Secrecy/Anti-Money Laundering (BSA/AML) function.<sup>413</sup> He explained that because the BSA/AML risks are "enterprise-wide and prevalent throughout the organization, [WFAS] determined it was better to manage from an audit function – not manage the function, but manage the audit accountabilities with one audit leader rather than having that risk audited throughout the organization."<sup>414</sup>

### ***Team Member Misconduct Committee***

The purpose of the Team Member Misconduct Executive Committee (TMMEC) was to "provide a forum for Wells Fargo executive management to provide leadership, oversight and direction related to team member misconduct and internal fraud risk management."<sup>415</sup> In the Committee Charter, dated May 31, 2012, the Committee was to "ensure that the enterprise has appropriate team member misconduct related policies, business processes, and program components that are designed to identify and mitigate associated risks and ensure that misconduct incidents are appropriately investigated and resolved."<sup>416</sup>

Mr. Julian was one of seven voting members of the Team Member Misconduct Committee (which he also referred to as the Team Member Engagement Committee and Executive Committee).<sup>417</sup> He testified that his role in this committee was limited and that he was "not permitted to in any way act as management, make management-type decisions for the Committee."<sup>418</sup> His role was to "listen for information that would be valuable to share back" with WFAS, and to "share information with the Committee that I was aware of" as Chief Auditor.<sup>419</sup>

The record does not support Mr. Julian's representation that his role in the Committee was limited to listening for information that would be valuable to share with WFAS and sharing information with the Committee.

Pursuant to the Charter, each member of the Committee was responsible on a semi-annual basis to "[r]eview team member misconduct trending reports to include enterprise and line of business specific investigative key activity" and "determine any required action items."<sup>420</sup> He also was required to "[r]eview specific team member misconduct or fraud occurrences which have been deemed significant by Corporate Investigations," "[r]eview and resolve any

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<sup>413</sup> Tr. (Julian) at 5979.

<sup>414</sup> Tr. (Julian) at 5979.

<sup>415</sup> R. Ex. 760 at 1.

<sup>416</sup> *Id.*

<sup>417</sup> Tr. (Julian) at 6059; R. Ex. 760 at 1; see also "22-03-07 Respondents' Amended Revised Errata Days 9 - 38" at page 42. Ordered through Second Supplemental Order Regarding Hearing Transcript Errata.

<sup>418</sup> Tr. (Julian) at 6060.

<sup>419</sup> Tr. (Julian) at 6060.

<sup>420</sup> R. Ex. 760 at 1. See also OCC Ex. 893 reflecting mapping of functions of the Committee through 9/21/2015; and Tr. (Julian) at 6158, where Mr. Julian testified the Team Member Misconduct Executive Committee was later subsumed by the Ethics and Integrity Oversight Committee. Tr. at 6158.

outstanding investigation resolution issues escalated by the line of business senior leadership,” “[r]eview emerging trends [and determine] any required action items,” and [r]eview any concerns or issues identified by committee membership, Audit or the Financial Crimes Corporate Risk Management Program” and determine any required action items.<sup>421</sup>

Further the Committee annually had the obligation to review and reassess the adequacy of the Committee’s Charter, the “adequacy of the team member misconduct and internal fraud investigations program,” ensure that there are “policies and processes” in place for adequately responding to the results of investigations, ensure that there are polices and processes in place “for incidents to be appropriately categorized as isolated or indicative of prevalent control breakdowns,” ensure that “periodic review of policies and procedures are performed”, and ensure that there are policies and procedures in place “for quarterly risk assessments to be adequately performed by qualified personnel independent of the business lines.”<sup>422</sup>

Mr. Julian testified that the Committee met on March 4, 2013 at which time they considered a report showing reports of enterprise-wide sales practices misconduct.<sup>423</sup> He noted, however, that the report did not separate misconduct from with the Community Bank – it was a corporate-wide reporting of investigations involving sales integrity violations.<sup>424</sup> He understood sales integrity violations to be “a much broader group of types of violations or cases of violations whereas sales practices misconduct . . . could be one subset of sales integrity violations, but not the whole entirety of it.”<sup>425</sup>

Mr. Julian testified that at no time during the March 4, 2013 meeting did Mr. Bacon say anything about customer consent being obtained through false or misleading representations, nor about customer funds being transferred in the Community Bank without customer consent, or about products or services being issued to Community Bank customers without customer consent.<sup>426</sup> He added that no one at the meeting tell him that any of Audit’s work had identified systemic risk with regard to either sales integrity or sales practices misconduct.<sup>427</sup>

However, Mr. Julian testified that as a result of seeing this information, he “wanted to understand more,” so he “reached out to Paul McLinko, who was the EAD, executive audit director, over the Community Bank to inquire as to what work the Community Bank . . . Audit Group was doing specific to sales integrity-type activity within the Community Bank.”<sup>428</sup> He

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<sup>421</sup> R. Ex. 760 at 1-2.

<sup>422</sup> *Id.* at 2.

<sup>423</sup> Tr. (Julian) at 6159-64; OCC Ex. 2943; R. Ex. 800.

<sup>424</sup> Tr. (Julian) at 6163.

<sup>425</sup> Tr. (Julian) at 6164.

<sup>426</sup> Tr. (Julian) at 6168.

<sup>427</sup> Tr. (Julian) at 6184.

<sup>428</sup> Tr. (Julian) at 6170-71.

asked Mr. McLinko “What work do we do related to team member fraud? Michael Bacon is presenting some data and Community Banking has a lot of issues each year.”<sup>429</sup>

Within hours after the Committee meeting, Mr. McLinko responded to Mr. Julian’s inquiry.<sup>430</sup> Mr. Julian testified that it “gave me comfort that the topic was top of mind for Paul. He was familiar with the issue and familiar with the work that his team was doing around the issue.”<sup>431</sup> Mr. McLinko reported that every 24 months his team does a “control testing audit of the Store Operations Control Review (SOCR) where elements of fraud would be covered;” and every 24 months his team does a “control testing audit of Sales Quality/Sales Integrity where elements of fraud would be covered”.<sup>432</sup> He added that there “are some other indirect reviews where we may find potential fraud (Customer Complaints, Incentive Compensation), but unlikely.”<sup>433</sup>

Mr. Julian testified that Mr. McLinko’s response “gave me comfort” and described the half-page response as “very thorough, very responsive.”<sup>434</sup> He said he also “took a great deal of comfort” in reading, several days later, a one-page “Sales Quality (SQ) Overview Coverage Overlay,” a half-page chart defining what Corporate Investigations tracks, and a half-page pie chart showing YTD 2012 Regional Banking Allegation Resolutions.<sup>435</sup> Mr. Julian testified that the Coverage Overlay established that only a small portion of investigations – 7 percent – resulted in disciplinary action.<sup>436</sup>

Mr. Julian said the half-page chart defining what Corporate Investigations tracks “broke out the types of sales integrity violations that Corporate Investigations was tracking,” but noted that not every type of sales integrity violation tracked by Corporate Investigations involved customer consent issues.<sup>437</sup> Mr. Julian said the pie chart, chart of definitions, and Coverage Overlay did not only refer to Internal Audit activities but instead “conveys to the extent that other control activities outside of [WFAS] [are] being leveraged as part of the overall risk management and being used by the [WFAS] folks in their assessment of the management of sales quality risk.”<sup>438</sup>

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<sup>429</sup> R. Ex. 766 at 1.

<sup>430</sup> Tr. (Julian) at 6174; R. Ex. 766.

<sup>431</sup> Tr. (Julian) at 6174.

<sup>432</sup> R. Ex. 766 at 1.

<sup>433</sup> *Id.*

<sup>434</sup> Tr. (Julian) at 6176.

<sup>435</sup> Tr. (Julian) at 6177-78; R. Ex. 4009.

<sup>436</sup> Tr. (Julian) at 6186; R. Ex. 4009 at 2.

<sup>437</sup> Tr. (Julian) at 6185.

<sup>438</sup> Tr. (Julian) at 6180-81.

He said he took comfort in knowing that WFAS “was aware of the issue, was performing various activities, both testing and business monitoring, in assessing the various control activities that were in place to govern sales quality activities.”<sup>439</sup> Mr. Julian considered these documents to be “comprehensive, well thought out, inclusive of relevant matters that ought to be assessed when assessing sales quality,” and that he “took comfort that this wasn’t something they had to prepare for me, meaning they were using this in their management of their responsibilities over at Community Bank.”<sup>440</sup>

Mr. Julian testified that on March 11, 2013, he convened a meeting with the Audit Management Committee (AMC) and used that meeting to “talk about the management of the audit function, any issues, resources, anything that seemed and would be appropriate to share with that entire group.”<sup>441</sup> At Mr. Julian’s invitation, Corporate Investigations made a presentation through Mr. Bacon, who presented the data previously presented to Mr. Julian at the March 3, 2013 meeting.<sup>442</sup> According to Mr. Julian, no one from Corporate Investigations raised any concerns specifically about customer funds being transferred without the customer’s consent, or accounts being obtained by false or misleading representations.<sup>443</sup> Further, he said that because the presentation was about “unsubstantiated” cases, nothing Corporate Investigations presented during this meeting indicated to him that sales integrity violations or sales practices misconduct in the Community Bank was either widespread or systemic.<sup>444</sup>

### *Ethics Committee*

Mr. Julian was a member of the Ethics Committee.<sup>445</sup> Mr. Julian identified the Ethics Committee Charter as being set forth in the Code Administration Responsibilities section of the WF&C Code of Ethics & Business Conduct, which was effective January 2014.<sup>446</sup> He described the Ethics Committee as a WF&C management committee “intended to provide oversight on governance activities of ethics program.”<sup>447</sup>

CRO Loughlin reported that the Ethics Committee “is responsible for administering and interpreting the Wells Fargo Code of Ethics and Business Conduct, as well as approving its

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<sup>439</sup> Tr. (Julian) at 6183.

<sup>440</sup> Tr. (Julian) at 6180; see also “22-03-07 Respondents’ Amended Revised Errata Days 9 -38” at page 43. Ordered through Second Supplemental Order Regarding Hearing Transcript Errata.

<sup>441</sup> Tr. (Julian) at 6189; R. Ex. 323.

<sup>442</sup> Tr. (Julian) at 6189-90.

<sup>443</sup> Tr. (Julian) at 6190-91.

<sup>444</sup> Tr. (Julian) at 6191.

<sup>445</sup> Tr. (Julian) at 6226.

<sup>446</sup> Tr. (Julian) at 6222-24; R. Ex. 6638 at 24.

<sup>447</sup> Tr. (Julian) at 6228.



content. The chairmanship of this committee rotates every three years among the members of the committee.”<sup>448</sup>

Mr. Julian testified that he limited this role on the Committee “to listen for information that would have been discussed or come out of the meeting that I felt was necessary or could be necessary to communicate to” WFAS’s leadership team “so that they were aware of any issues that were being raised.”<sup>449</sup> In addition, his role was to “ask questions on information that was being presented and to share information that I may have related to the topic of the meeting that I would have learned through my role on other committees or as Chief Auditor.”<sup>450</sup> He testified, however, that in accordance with professional standards, “it was important that I maintain independence and objectivity with respect to my engagement in the work of the Committee so that I wasn’t impairing my independence or objectivity.”<sup>451</sup>

Mr. Julian identified the agenda that had been circulated in advance of the December 2, 2013 meeting of the Ethics Committee.<sup>452</sup> He testified that he personally did not set the agenda, stating that the agenda “would have been set by the Ethics Committee group” of which he was a member.<sup>453</sup> He acknowledged that the agenda made no mention of sales integrity or sales practices misconduct by team member of the Community Bank – notwithstanding the information that was known to him by December 2013.<sup>454</sup>

Asked whether he was surprised that the agenda included no mention of the sales integrity or sales practices misconduct issue, Mr. Julian responded that he was not surprised – “not at the time.”<sup>455</sup> He acknowledged that by that meeting the LA Times article had come out, but justified his reaction by stating that “[i]t was known that work was being performed by the Community Bank to address the issue or look into the issue.”<sup>456</sup> From this, Mr. Julian concluded that members of the Ethics Committee “were already informed of the matter and knew that work was going on by December 2 of 2013.”<sup>457</sup>

There is, however, nothing in the record establishing that by December 2, 2013 the members of the Ethics Committee knew of any issue regarding sales practices misconduct, nor that either WFAS or the Community Bank were taking steps to address the issue.

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<sup>448</sup> OCC Ex. 1553 at 10.

<sup>449</sup> Tr. (Julian) at 6228-29.

<sup>450</sup> Tr. (Julian) at 6229.

<sup>451</sup> Tr. (Julian) at 6229.

<sup>452</sup> Tr. (Julian) at 6304, R. Ex. 6014.

<sup>453</sup> Tr. (Julian) at 6303, 6226.

<sup>454</sup> Tr. (Julian) at 6305; R. Ex. 6014.

<sup>455</sup> Tr. (Julian) at 6305.

<sup>456</sup> Tr. (Julian) at 6305.

<sup>457</sup> Tr. (Julian) at 6305-06.

Mr. Julian identified the meeting minutes for the December 2, 2013 Ethic Committee meeting, which he attended.<sup>458</sup> Notwithstanding the information that was then available to Mr. Julian by December 2, 2013 regarding sales practices misconduct by team member of the Community Bank, he identified nothing during his testimony that indicated through the meeting minutes that he shared any of that knowledge with other members of the Committee.<sup>459</sup>

The 2014 Charter established that members of the Committee would be appointed by the chief executive officer of WF&C and would be “responsible for the content of the Code and overseeing the policy and interpretation of the Code.”<sup>460</sup> Each member of the Operating Committee “is responsible for Code administration for all team members in the business groups that report to him or her.”<sup>461</sup>

Mr. Julian testified that the WF&C Ethics Committee was later subsumed by the Ethics and Integrity Oversight Committee, and he identified the April 13, 2016 Charter for that Committee as well.<sup>462</sup>

Mr. Julian testified that during the relevant time when serving as a member of the Ethics Committee and then the Ethics and Integrity Oversight Committee, he limited his role consistent with the professional standards, including independent standards applicable to Internal Auditors.<sup>463</sup> He identified the meeting agenda for the August 22, 2013 Ethic Committee meeting and stated that he was present at that meeting.<sup>464</sup> Through the Meeting Agenda for the 2013 meeting, Corporate Security reported that out of 6,841 cases investigated by Corporate Investigations YTD end of 2Q 2013, 5,862 cases were from the Community Bank line of business, reflecting a 5% increase from the same period in 2012.<sup>465</sup>

Equally significant, year to date through the end of the second quarter 2103, Community Banking generated 3,516 EthicsLine reports – constituting 83.44% of all the reports received.<sup>466</sup> The report reflected there were 105,185 team member in the Community Bank line of business, such that the reports identified 37.7% of all team member working for the Community Bank – or 33 reports per 1,000 team member (contrasting with 1 report per 1,000 team member for the Wealth Management, Wholesale Banking, and Technology and Operations lines of business).<sup>467</sup>

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<sup>458</sup> Tr. (Julian) at 6301-02; R. Ex. 6322.

<sup>459</sup> Tr. (Julian) at 6301-03; see also R. Ex. 6322.

<sup>460</sup> R. Ex. 6638 at 24.

<sup>461</sup> *Id.*

<sup>462</sup> Tr. (Julian) at 6225; R. Ex. 12528.

<sup>463</sup> Tr. (Julian) at 6226.

<sup>464</sup> Tr. (Julian) at 6229-30; R. Ex. 4479.

<sup>465</sup> R. Ex. 4479 at 5.

<sup>466</sup> *Id.* at 8.

<sup>467</sup> *Id.*

Minutes from the August 22, 2013 Ethic Committee meeting reflect the contents of the materials supplied in advance of the meeting. Mr. Bacon, head of Corporate Investigations, reported that “misconduct and ethics violations are up,” but “EthicsLine reports are down 4%” marking the “first time that’s happened since the Wachovia merger.”<sup>468</sup> He noted that March “tends to be the highest month for reports,” opining that this might be “associated with sales campaign activity.”<sup>469</sup>

Mr. Bacon reported that while Community Banking numbers “are decreasing,” they were still the “highest number of reports per 1,000 Team Members and most associated with Sales Integrity issues.”<sup>470</sup> He reported, “Claudia Russ Anderson’s team is aware of the metrics and is working on this. Some Regional Banking areas have seen marked improvement in metrics while others still need to improve.”<sup>471</sup> Mr. Bacon made two points in summary: first, “CFPB and Sales Integrity issues are most prevalent – there needs to be continued focus in this area;” and second – this in response to a question from a member of the Committee – Mr. Bacon reported that “while he is not seeing regulatory inquiries to date, he anticipates the trend is heading toward more inquiry and we need to be prepared for it. There is more prevalence of Team Members going to regulators with reports and complaints.”<sup>472</sup>

Mr. Julian testified that from Mr. Bacon’s presentation during the August 2013 Ethics Committee meeting, his understanding of Mr. Bacon’s data regarding cases investigated by Corporate Investigations, “the majority were unsubstantiated” and that the same was true of EthicsLine complaints during the first half of 2013, and that in the place allotted for describing “Action” Mr. Bacon indicated “none”.<sup>473</sup> Mr. Julian testified that recalling the presentation during this meeting, Mr. Bacon said nothing about products or services being issued to Community Bank customers without customer consent or where customer consent was obtained through false or misleading representations.<sup>474</sup> Nothing in the 2013 report by Mr. Bacon indicated to Mr. Julian that sales integrity violations or sales practice misconduct in the Community Bank were widespread or systemic.<sup>475</sup> Notwithstanding the written comments from Mr. Bacon noting the trend that would lead to more regulatory inquiry and that the highest number of reports per 1,000 Team Members were in cases associated with sales integrity issues, Mr. Julian testified that the report was “absolutely” reassuring to him and that his takeaway from

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<sup>468</sup> R. Ex. 4501 at 1.

<sup>469</sup> *Id.* at 1-2.

<sup>470</sup> *Id.* at 2.

<sup>471</sup> *Id.*

<sup>472</sup> *Id.*

<sup>473</sup> Tr. (Julian) at 6232-24. R. Ex. 4501 at 2.

<sup>474</sup> Tr. (Julian) at 6236.

<sup>475</sup> Tr. (Julian) at 6237-38.

Mr. Bacon's presentation was that "certain metrics were improving across the organization," and that Ms. Russ Anderson "was aware and working on the issues."<sup>476</sup>

Mr. Julian testified that he was present at the Ethics Committee meeting of December 8, 2014.<sup>477</sup> The minutes of that meeting, however, do not indicate Mr. Julian had anything to say.<sup>478</sup> The minutes reflect the Committee took no action of record.<sup>479</sup> In his review of the meeting minutes, Mr. Julian testified that Ms. Meuers, in reporting about the direction of sales quality issues, informed those present that regarding "Code Administrator and EthicsLine Updates, "incidents were up slightly, but specific to sales quality issues, that they had decreased."<sup>480</sup> Asked whether he had any reason to disagree with Ms. Meuers' report, Mr. Julian answered in the negative.<sup>481</sup>

Nothing in this report established that the sales quality issues that decreased were within the Community Bank; and nothing in the report established whether the sales quality issues included issues regarding sales practices misconduct. As such, there is nothing in this report that advanced either issues presented by the pleadings or defenses raised by Respondents.

Notwithstanding that the document contained no material evidence relating to issues or defenses, Counsel for Mr. Julian sought to introduce evidence establishing "whether or not Enforcement Counsel asked him about this document or this meeting, the December 8 Ethics Committee meeting in either his investigative testimony or his deposition."<sup>482</sup>

Finding no material relevance to whatever answer would be given (and Counsel proffered the answer would be that Enforcement Counsel did not ask Mr. Julian about the meeting or the minutes), the objection to admission of the line of questioning was sustained on the grounds that the evidence lacked material relevance.<sup>483</sup> If anything, the relevance of the document tends to show Mr. Julian's continued failure to fully disclose material information he had possessed since at least late 2013 regarding complaints indicating management's improper pressure to meet unreasonable sales goals that were being applied to the Community Bank's Team Members.<sup>484</sup>

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<sup>476</sup> Tr. (Julian) at 6238.

<sup>477</sup> Tr. (Julian) at 6604.

<sup>478</sup> Tr. (Julian) at 6604; R. Ex. 9981.

<sup>479</sup> R. Ex. 9981 at 1-4.

<sup>480</sup> Tr. (Julian) at 6607; R. Ex. 9981 at

<sup>481</sup> Tr. (Julian) at 6608.

<sup>482</sup> Tr. (Julian) at 6605.

<sup>483</sup> Tr. (Julian) at 6604-05

<sup>484</sup> See Mr. Julian's testimony at Tr. p. 6148 acknowledging his receipt of a 1/28/13 customer report that a personal banker opened an account without the customer's consent (OCC Ex. 1588); the 1/28/13 EthicsLine report that sales services representative opened a customer's account without the customer's consent (OCC Ex. 1571); a 10/28/13 EthicsLine web report that a Community Banking District Manager in Deltona, Florida may be encouraging an unethical and stressful sales environment by personally setting district sales goals that exceed stated

According to the Charter, the 2016 iteration of the Committee “is sponsored by and operates under the authority of the Audit & Examination Committee of WFC’s Board of Directors, as well as the Operating Committee, which collectively authorize it to perform the oversight responsibilities described in this Charter.”<sup>485</sup>

Included in the Charter for the 2016 Committee, members were required to provide “significant issue management oversight,” to include the review of “significant ethical and business conduct issues that may have a material impact on the Company’s operations and/or reputation, including oversight of resolution, proposed corrective actions and identified program gaps or other control weaknesses; review and ensure appropriate management resolution of allegations involving significant violations of business conduct law or regulation”.<sup>486</sup> Whereas the 2014 Charter was silent with respect to the Chief Auditor’s voting status within the Committee, the 2016 Charter expressly identified the Chief Auditor as a non-voting member.<sup>487</sup>

Included in the 2016 Charter was the provision that Committee members were to review and evaluate “emerging ethics, business conduct and conflicts of interest issues and trends in response to changes in business strategy, risk and regulatory and legal requirements to assess the implications for business objectives, strategies, and practices.”<sup>488</sup>

Also included in the 2016 Charter was the provision that Committee members periodically review and advise the Head of Global Ethics & Integrity “on the adequacy and effectiveness of the Company’s ethics, business conduct and conflicts of interest risk management program, including policies, programs, applicable Global Ethics & Integrity risk management practices and the awareness and promotion of an ethical culture across the enterprise.”<sup>489</sup>

Also included in the 2016 Charter was the requirement that Committee members review business conduct activity “to include enterprise and line of business specific investigative key

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sales goals in personal banker and CSSR sale matrices (OCC Ex. 1586); and in the same email, Katie Hall noted further that she “was able to locate five additional EthicsLine reports for Deltona, FL related to sales integrity concerns received between 9/10/2013 and 10/14/2013.” She wrote that three of the five “have been referred to Sales Quality for research,” and two “have been referred to Corporate Investigations and are currently being investigated” (OCC Ex. 1586); a 10/29/13 report that two customers with the knowledge of a Community Banking District Manager in Pasadena, Texas (OCC Ex. 1587); a 1/14/14 report that a banker in Hockessin, Delaware opened accounts for a customer without the customer’s consent (OCC Ex. 1589); and a 3/3/14 report that a president in a Long Beach, New Jersey branch “‘threatens’ the Team and tells them they must hit 200% of their sales goal at any cost on a daily basis” (OCC Ex. 1590).

<sup>485</sup> R. Ex. 12528 at 1.

<sup>486</sup> *Id.* at 2.

<sup>487</sup> *Id.* at 3.

<sup>488</sup> *Id.* at 1.

<sup>489</sup> *Id.*

activity (case totals, case type activity, related terminations/resignations) and EthicsLine activities, which includes issues related to sales practices.”<sup>490</sup>

Also included in the 2016 Charter was the requirement that Committee members review “specific business conduct or fraud incidents, to include cases involving EthicsLine allegations, whistleblower complaints, issues escalated by the business compliance teams and unethical or misconduct identified by Global Ethics & Integrity oversight activities.”<sup>491</sup>

The 2016 Charter described Committee members as “the most senior management-level risk governance committee to which key ethics, business conduct and conflicts of interest risk issues are escalated”.<sup>492</sup> These issues included business conduct that was “likely to cause material adverse impact to customers, or to the Company’s reputation,” and issues “likely to be discussed with the Company’s regulators”.<sup>493</sup> The issues also included those, “based upon a reasonable manager’s judgment, may adversely impact the Company,” as well as “[b]udget and resource issues.”<sup>494</sup>

The 2016 Charter provided that for each escalated issue, the Committee “shall have the authority to assess the degree to which the owner has identified, assessed, controlled, and mitigated the issue at hand,” and may require “further actions to be taken by the owner and may require oversight of the issue by the Committee”.<sup>495</sup>

#### ***The Role of the WF&C Ethics Line***

Mr. Julian testified that the WF&C EthicsLine was a “process by which Team Members could either anonymously or, if they so choose, identify themselves, but to raise concerns they may have with respect to ethics allegations.”<sup>496</sup>

#### ***Incentive Compensation Committee***

Mr. Julian was a member of the Incentive Compensation Committee.<sup>497</sup> Until June 15, 2015 Mr. Julian served as a voting member of the Incentive Compensation Steering Committee (which later became known as the Incentive Compensation Committee), which was a WF&C committee.<sup>498</sup>

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<sup>490</sup> R. Ex. 12528 at 2.

<sup>491</sup> *Id.*

<sup>492</sup> *Id.*

<sup>493</sup> *Id.*

<sup>494</sup> *Id.*

<sup>495</sup> *Id.*

<sup>496</sup> Tr. (Julian) at 6144.

<sup>497</sup> Tr. (Julian) at 6060.

<sup>498</sup> Tr. (Julian) at 6143; OCC Ex. 1722 at 1; OCC Ex. 1724 at 3.

CRO Loughlin reported that the ICC (formerly known as the Incentive Compensation Steering Committee) “leads Wells Fargo’s efforts to enhance incentive compensation practices throughout the company. This committee is chaired by the head of Corporate Human Resources.”<sup>499</sup>

Mr. Julian testified that his role in this committee was limited and that he was “not permitted to in any way act as management, make management-type decisions for the Committee.”<sup>500</sup> He testified that his role was limited: that all he could or would do as Chief Auditor was “listen for information that would be valuable to share back” with WFAS, and to “share information with the committee that I was aware of”.<sup>501</sup>

There is, however, nothing in the description of the oversight and decision-making authority of the Committee that limited Mr. Julian’s role to listening for information - The oversight and decision-making authority of the Committee included overseeing the “development of enterprise-wide standards for the design and administration of the Company’s incentive compensation plans”, and monitoring the implementation of appropriate actions for enhancing the Company’s incentive compensation programs “to better align with the Federal Reserve Guidance.”<sup>502</sup>

The minutes of the July 8, 2015 meeting of the Incentive Compensation Committee reflect that as part of the reviews conducted under the Incentive Compensation Risk Management (ICRM) Program, “enhancement opportunities were identified, including adding rigor around risk metrics and identifying opportunities for further improvement to address new risks and increased regulatory scrutiny.”<sup>503</sup>

Notwithstanding this evidence, Mr. Julian testified that he was never during his tenure as Chief Auditor involved in managing incentive compensation at Wells Fargo.<sup>504</sup> He also denied that the Incentive Compensation Steering Committee was ever responsible for directing or managing changes to incentive compensation plans.<sup>505</sup>

Mr. Julian identified the February 18, 2014 Summary of Risk Assessments relating to the compensation of senior executives.<sup>506</sup> The Summary was prepared by Justin Thornton, a direct report of the head of HR, Hope Hardison.<sup>507</sup> Mr. Julian participated in the February 2014

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<sup>499</sup> OCC Ex. 1553 at 9.

<sup>500</sup> Tr. (Julian) at 6060.

<sup>501</sup> Tr. (Julian) at 6060.

<sup>502</sup> OCC Ex. 1722 at 1.

<sup>503</sup> OCC Ex. 1700 at 1.

<sup>504</sup> Tr. (Julian) at 6135.

<sup>505</sup> Tr. (Julian) at 6140.

<sup>506</sup> Tr. (Julian) at 6380; OCC Ex. 640.

<sup>507</sup> Tr. (Julian) at 6381.

meeting of the group reviewing the Summary, which included Ms. Hardison for HR and Chief Risk Officer Michael Loughlin.<sup>508</sup>

For 2013, 75 members of senior management were “covered employees” about whom the Summary pertained.<sup>509</sup> Covered employees “represented the major business line heads, corporate functional heads, and line of business control function heads (finance, HR and risk). This group includes all the members of the Operating Committee (OC) and Management Committee Review Group (MCRG), and selected members of the Management Committee (MC).”<sup>510</sup> Mr. Julian was a covered employee, as was Ms. Russ Anderson.<sup>511</sup>

Mr. Julian described himself as an active participant in the February 2014 meeting.<sup>512</sup> Unlike his description of the role he played during meetings of other committees on which he served, in the case of this meeting Mr. Julian described his role as Chief Auditor “was to assure that I credibly challenged and was actually recognized, as that was one of my strengths. So it’s not something that I would have shied away from.”<sup>513</sup>

Mr. Julian testified that he had no role in the ultimate decisions regarding specific compensation, “but with regard to the extent that I felt that any of the information that I mentioned was in the package that we reviewed, to the extent any of that information should be taken into consideration by senior management in the determination of a particular person, covered employee’s compensation, I would have been engaged in that discussion.”<sup>514</sup>

Mr. Julian testified that he would not be involved in the “ultimate, actual compensation” of a covered employee because it “wasn’t a responsibility or role of me as Chief Auditor to be involved in compensation decisions.”<sup>515</sup> Instead, his role “was to assure that the folks who were responsible for making those decisions, in my opinion, had my view with respect to risk matters that ought to be taken into consideration.”<sup>516</sup>

Mr. Julian identified a similar memo from February 16, 2015, featuring reports by Ms. Hardison and Mr. Loughlin regarding risk assessments relating to compensation of senior executives.<sup>517</sup> He testified that he had nothing to do with preparing the memo and that as of

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<sup>508</sup> Tr. (Julian) at 6381; OCC Ex. 640 at 1.

<sup>509</sup> OCC Ex. 640 at 1.

<sup>510</sup> Tr. (Julian) at 6565-66; R. Ex. 774 at 8; OCC Ex. 640 at 1.

<sup>511</sup> OCC Ex. 640 at Appendix A, OCC-WF-SP-07373931-32.

<sup>512</sup> Tr. (Julian) at 6382.

<sup>513</sup> Tr. (Julian) at 6383.

<sup>514</sup> Tr. (Julian) at 6383.

<sup>515</sup> Tr. (Julian) at 6384.

<sup>516</sup> Tr. (Julian) at 6384.

<sup>517</sup> Tr. (Julian) at 6621; OCC Ex. 2819.



February 2015 he was not aware of any other information regarding sales practices risk that needed to be escalated to the Board of Directors.<sup>518</sup>

As part of the Summary he prepared for the February 2014 meeting, Mr. Thornton identified within the Summary of Q4 Breaches and other Recent Risk Issues Requiring Attention in 2014 the following regarding sales integrity:

In addition, we also recommend monitoring in 2014 for sales integrity in Community Banking, specifically ongoing monitoring and review of store level quality processes. This issue presents potential operational and reputational risk. Action plans are in progress including: heightened monitoring processes; communication of sales quality expectations; strengthening of control function review of incentive plans, goals, and performance management programs; and continued focused attention on consistent and high-touch communications strategies.<sup>519</sup>

Mr. Julian denied that he ever saw Mr. Thornton's summary prior to the present enforcement litigation.<sup>520</sup> He testified that he recalled, "[g]enerally the discussion was that . . . work was being performed by folks who had responsibility for performing the work related to sales practices and that folks in the room and my view of – based on what I had heard, was that work was being performed with a good faith effort."<sup>521</sup>

Mr. McLinko identified a March 13, 2015 WFAS Audit Engagement Report for the Enterprise on Incentive Compensation, prepared by the Financial Controls Audit (FCA) audit team, led by Andrew Shipley.<sup>522</sup> He testified that during the 2013 to 2016 period the FCA was the group responsible for auditing the process and controls related to incentive compensation in the Community Bank.<sup>523</sup>

Mr. McLinko testified that Mr. Shipley's group scoped and performed the audit, but that the FCA team "would reach out to the other audit teams" when performing an Enterprise audit.<sup>524</sup> When asked, however, whether during the 2013 to 2016 period auditors under the direction of the FCA ever looked into the reasonableness of sales goals in the Community Bank, Mr. McLinko responded, "I really don't know."<sup>525</sup>

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<sup>518</sup> Tr. (Julian) at 6621.

<sup>519</sup> OCC Ex. 640 at 3.

<sup>520</sup> Tr. (Julian) at 6385.

<sup>521</sup> Tr. (Julian) at 6384-85.

<sup>522</sup> Tr. (McLinko) at 8071; OCC Ex. 2068.

<sup>523</sup> Tr. (McLinko) at 8443.

<sup>524</sup> Tr. (McLinko) at 8072.

<sup>525</sup> Tr. (McLinko) at 8443.

Mr. McLinko denied that he had any involvement in creating the standard audit program that FCA used for Incentive Compensation audits, and stated he had no role in either conducting or managing the audit.<sup>526</sup> (When asked whether he had any involvement in the 2017 Enterprise Incentive Compensation audit, Mr. McLinko responded, “I don’t believe I would. I just don’t remember that audit.”<sup>527</sup>) He added that from 2013 to 2016, he was not involved in any Incentive Compensation audits covering the Regional Bank.<sup>528</sup>

Through the March 13, 2015 Enterprise Incentive Compensation Audit Engagement Report, WFAS auditors completed an “enterprise-wide audit of Incentive Compensation that included significant control design and effectiveness testing in both Corporate Compensation and each line of business (LOB) Human Resources (HR) group.”<sup>529</sup> It covered the period from January 1, 2013 through June 30, 2014 and found “several moderate-rated issues” but concluded, “that compensation processes and the overall system of internal control of this engagement scope are Effective.”<sup>530</sup>

Through the Executive Summary, the Bank’s Incentive Compensation responsibilities were described thus:

The responsibilities for incentive compensation governance and control rest with both the LOB HR groups and Corporate Compensation. Specifically, the LOBs are responsible for incentive compensation plan design, risk balancing, and payout administration. Corporate Compensation is responsible for the Incentive Compensation Risk Management (ICRM) program, which provides governance and oversight of incentive compensation (either at the LOB or Corporate level) and executive compensation administration.<sup>531</sup>

The March 13, 2015 Engagement Report identified issues and the need to take corrective actions regarding the documentation of reviews and outcomes of risk scorecards and performance-based vesting; the documentation of discretion to support the long term cash incentive program; the documentation and guidance for the Model Risk Compensation framework; the need to implement a review process for supplemental compensation agreement renewals; and the need to enhance process documentation guidelines to ensure evidence of key reviews and approvals are maintained.<sup>532</sup>

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<sup>526</sup> Tr. (McLinko) at 8074.

<sup>527</sup> Tr. (McLinko) at 8074.

<sup>528</sup> Tr. (McLinko) at 8075.

<sup>529</sup> OCC Ex. 2068 at 2.

<sup>530</sup> *Id.* at 2, 14.

<sup>531</sup> *Id.* at 2.

<sup>532</sup> *Id.* at 5-13.

Mr. Julian identified the Incentive Compensation Risk Management Policy, published May 7, 2015.<sup>533</sup> Through this Policy, WF&C established four compensation objectives – “pay for performance,” the promotion of “a culture of risk management that avoids unnecessary or excessive risk taking,” the goal of “attract[ing] and retain[ing] talent with competitive pay,” and aligning “employee interests with shareholders.”<sup>534</sup>

The Policy statement also provides that Wells Fargo “ensures it has effective incentive compensation arrangements that support the long-term strength of the organization by providing team member incentives “that appropriately balance risk and financial results,” ensure that “incentive arrangements are compatible with effective controls and risk management,” enforce “strong corporate governance, including active and effective oversight by the company’s Board of Directors,” and disclose “the structure of its incentive-based compensation arrangements to governance bodies and regulators in accordance with applicable law and regulation.”<sup>535</sup>

Mr. Julian identified the Incentive Compensation Committee Meeting Minutes dated July 8, 2015.<sup>536</sup> The minutes reflect that Mr. Julian was present at the meeting, and that included in the materials presented during the meeting was the Governance Review and Program Update of the Incentive Compensation Risk Management (ICRM) Program of the Incentive Compensation Committee, dated July 8, 2015.<sup>537</sup>

The Program Update included a report indicating that five MRAs the Bank received related to “broader Enterprise Sales Practices, including compensation-related requirements”.<sup>538</sup> The Enterprise Sales Practices MRA provided: that compensation programs “need[ed] to be reviewed to protect against incenting inappropriate behavior”; that Corporate HR was identified “as part of development” of first and second line of defense governance; and that Corporate Risk “reviews the reasonableness of [incentive compensation] program for all Enterprise Sales activities”.<sup>539</sup>

Mr. Julian identified a Risk Assessment Summary provided to CEO Stumpf on February 12, 2016 by Hope Hardison (Director of Human Resources) and Michael Loughlin (Chief Risk Officer).<sup>540</sup>

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<sup>533</sup> Tr. (Julian) at 6795-96; R. Ex. 10012.

<sup>534</sup> R. Ex. 10012 at 1.

<sup>535</sup> *Id.*

<sup>536</sup> Tr. (Julian) at 6796; OCC Ex. 1700.

<sup>537</sup> OCC Ex. 1700 at 2.

<sup>538</sup> *Id.* at 22.

<sup>539</sup> *Id.*

<sup>540</sup> OCC Ex. 689.

The Risk Assessment Summary included a list of “key risk issues” as of 2016, one of which related to Sales Practices (without limiting the risks to the Community Bank).<sup>541</sup> Mr. Julian testified that while he recognized the Summary he did not see it other than as part of this enforcement litigation, and had no role in either reviewing or approving the Summary.<sup>542</sup>

The Summary identified Claudia Russ Anderson among those with accountability for the sales practices issue.<sup>543</sup> The Summary rated the sales practices issue at Community Bank as “improvement needed”, describing the issue as “Top OCC issue with 5 MRAs related to Tone at the Top, FLOD, SLOD, and Customer Complaint. Current litigation related to Community Banking, ongoing customer remediation.”<sup>544</sup>

The Summary described the impact as “reputational and regulatory risks for Wells Fargo resulting from this issue.”<sup>545</sup> It identified the resolution as follows: “Significant work has been accomplished to address the MRAs, but a lot still needs to be completed in a short timeframe for completion. Acceptable and steady progress is evidenced with all open corrective actions.”<sup>546</sup> There is no indication WFAS was participating in addressing the issues raised in this Summary.

### **May 2014: WFAS’s Relationship (Third Line of Defense) with Corporate Risk (Second Line of Defense)**

Mr. Julian testified that acting on his own initiative and without apparent support or approval by WF&C’s Board of Directors, he convened “quarterly management meeting[s]” between Audit and Corporate Risk, starting in May 2014.<sup>547</sup> He testified that through these meetings, he sought to meet what he perceived to be a need to “have the senior leaders of WFAS and Corporate Risk meet on a quarterly basis to discuss recent trends, significant issues, emerging risks, recent Audit results, and key areas of focus.”<sup>548</sup>

Asked why he made the suggestion for such meetings, Mr. Julian responded that he believed “there had been a report previously that had talked about communications between Corporate Audit and Corporate Risk and that those were important types of dialogue. And I felt that this would just enhance further the communications and somewhat formalize the communications between the two groups.”<sup>549</sup>

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<sup>541</sup> *Id.* at 2.

<sup>542</sup> Tr. (Julian) at 6942-43.

<sup>543</sup> OCC Ex. 689 at 7.

<sup>544</sup> *Id.*

<sup>545</sup> *Id.*

<sup>546</sup> *Id.*

<sup>547</sup> Tr. (Julian) at 6555; R. Ex. 958 at 2.

<sup>548</sup> Tr. (Julian) at 6555; R. Ex. 958 at 2.

<sup>549</sup> Tr. (Julian) at 6555.

Mr. McLinko testified that he participated in the initial meeting of “the direct reports of Mike Loughlin and the direct reports of David Julian” convened under the title “Audit & Corporate Risk Quarterly Management.”<sup>550</sup> Using two separate exhibits, both Mr. McLinko and Mr. Julian identified the same report titled “Audit & Corporate Risk Quarterly Management Meeting” dated May 2014 – without acknowledging that the two exhibits are the same.<sup>551</sup>

In his testimony regarding these quarterly meetings, Mr. Julian made no mention of the professional standards concerning the need for independence between the Third Line of Defense and Corporate Risk, which is part of the second line of defense.<sup>552</sup> Instead, the stated objectives of this quarterly discussion were, *inter alia*, to “[u]nderstand recent Audit results and upcoming coverage and how that reflects on the quality of risk management across the enterprise”; discuss “key areas of focus of the Corporate Risk Officers and their groups”; and review “the Noteworthy Risk Issues report that is shared with the Board.”<sup>553</sup>

Under the terms of the May 2014 Audit & Corporate Risk Quarterly Management Meeting, the Chief Auditor directed meetings be held quarterly and directed participants to “[m]ake these meetings a priority as poor attendance will affect the quality of the discussions,” and anticipated each participant would “[s]hare the perspectives coming out of these meetings with your teams to help cascade the information throughout each organization.”<sup>554</sup> The May 2014 “Key Areas of Coverage” for this group had ten upcoming audit coverage areas – but made no mention of sales practices misconduct by Team Members of the Community Bank in the description of “key areas of Audit coverage areas occurring in the coming 90 days.”<sup>555</sup>

Operating now under the name “Corporate Risk & Audit” the agenda for the May 13, 2014 meeting was inexplicably contained in the same document that contained the minutes for the same meeting.<sup>556</sup> In what are described as “Minutes for this Meeting,” Mr. Julian and Kris Klos stated that the “objective [of this quarterly meeting series between Corporate Risk and Audit] is to share perspectives on significant and emerging risks and issues facing the organization to help understand the current state of risk management. In addition, discussions will highlight key areas of coverage by WFAS in the upcoming quarter.”<sup>557</sup>

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<sup>550</sup> Tr. (McLinko) at 8008.

<sup>551</sup> Tr. (McLinko) at 8009; R. Ex. 6147; *cf* Tr. (Julian) at 6555-63; R. Ex. 958.

<sup>552</sup> Tr. (Julian) at 6555-63; R. Ex. 958 at 2.

<sup>553</sup> R. Ex. 958 at 3.

<sup>554</sup> *Id.* at 4.

<sup>555</sup> *Id.* at 5.

<sup>556</sup> See R. Ex. 684 at 1.

<sup>557</sup> *Id.*

Included in the Minutes is an update about WFAS presented by Mr. Julian.<sup>558</sup> The update included “specific trends” detailed in the 1Q14 A&E Committee report.<sup>559</sup> Those trends included the “[l]ack of clear definitions of roles and responsibilities between the first and second lines of defense”, and “[r]esource constraints and limited knowledge transfer” that “have resulted in oversight concerns and control ineffectiveness.”<sup>560</sup> Mr. Julian is reported to have stated that the “primary goal of sharing this report was to highlight areas where Corporate Risk may want to focus attention as well as allow Corporate Risk to weigh in on areas WFAS may want to focus on during their audits.”<sup>561</sup> Also reported in the Minutes:

The group discussed emerging risk reporting. Currently, both areas report separately, and there may be an opportunity for further collaboration on reporting to the Board and senior management. Considering Audit’s need for independence, separate reporting may continue to make sense. However, certain reporting may be able to be combined but allow for differences between views of each respective group to be called out. Currently, WFAS uses the Noteworthy Issues Report to comment on audit coverage of these key risk topics instead of creating their own emerging risk report.<sup>562</sup>

The Minutes reflect that Yvette Hollingsworth, whom Mr. Julian identified as “the Chief Compliance Officer for Wells Fargo Corporation [*sic*] reporting to Mike Loughlin, the Chief Risk Officer,”<sup>563</sup> discussed “sales practices and the need for the second and third lines of defense to focus on this area considering the number of whistleblower complaints and regulatory scrutiny.”<sup>564</sup> She also is reported as stating that “Audit is currently validating the cross sell numbers (Wholesale and Community Banking), per the direction of the OCC.”<sup>565</sup> The Minutes report that in response, Paul McLinko “noted this is considered in Audit coverage, more so from the incentive side.”<sup>566</sup>

Asked what his reaction was to Ms. Hollingsworth’s report, Mr. Julian responded, “I didn’t disagree. Sales practices risk was well known by this time by both groups. Both groups were engaged in activity related to it, so I didn’t disagree with her comment.”<sup>567</sup>

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<sup>558</sup> R. Ex. 684 at 1.

<sup>559</sup> *Id.*

<sup>560</sup> *Id.*

<sup>561</sup> *Id.* at 2.

<sup>562</sup> *Id.*

<sup>563</sup> Tr. (Julian) at 6560.

<sup>564</sup> R. Ex. 684 at 3.

<sup>565</sup> *Id.*

<sup>566</sup> *Id.*

<sup>567</sup> Tr. (Julian) at 6561.

As noted, Ms. Hollingsworth represented the Second Line of Defense, reporting directly to the Chief Risk Officer. For reasons that are not clear in the record, during direct examination Mr. Julian was asked by his attorney whether Ms. Hollingsworth, from whom he should be independent in his role as Chief Auditor, ever suggested that Audit's coverage of sales practices needed to be broader.<sup>568</sup> Mr. Julian answered in the negative.<sup>569</sup>

Predating the May 13, 2014 meeting by more than four months, Ms. Hollingsworth wrote to Mr. Loughlin raising her concerns about information that had been reported in the LA Times December 23, 2013 article "Wells Fargo's Pressure-Cooker Sales Culture Comes at a Cost".<sup>570</sup> In a December 30, 2013 email, Ms. Hollingsworth asked Mr. Loughlin and Caryl Athanasiu "how are we responding to this allegation as a company? I'm certain discussions or even decisions are already underway [or] have been made, but an independent review of the perception of the sales culture by those on the front line will be very helpful."<sup>571</sup>

She wrote:

From an oversight perspective, as a second line of defense, we need management information to monitor sales performance, similar to how one monitors traders. This is not in place yet on my team; however, we can begin to build such a process under the responsible banking policy but I will need a forum to vet the idea and to structure this correctly – if you agree- perhaps we can raise this with the Consumer Council?<sup>572</sup>

During his testimony, Mr. Julian denied being aware that Ms. Hollingsworth recommended that the Company engage an independent investigation of sales practices issues in the Community Bank.<sup>573</sup> Mr. McLinko testified that he understood the risk issues presented in the Noteworthy Risk Issues – April 2014 included a reference to sales practices, and through leading questioning presented by his Counsel during direct examination testified that he understood this memo was going to be sent to the Board or a committee of the Board.<sup>574</sup>

### **Mr. Julian's Reporting Relationship with Respondent McLinko**

During the relevant period, Respondent McLinko led the audit function of the WFAS's Audit Group over the Community Bank Line of Business.<sup>575</sup> Mr. McLinko was one of "nine to ten direct reports who were typically Executive Audit Directors who reported directly" to Mr.

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<sup>568</sup> Tr. (Julian) at 6562.

<sup>569</sup> Tr. (Julian) at 6562.

<sup>570</sup> OCC Ex. 1437.

<sup>571</sup> *Id.* at 1.

<sup>572</sup> *Id.*

<sup>573</sup> Tr. (Julian) at 6563.

<sup>574</sup> Tr. (McLinko) at 8009; R. Ex. 6149.

<sup>575</sup> Tr. (Julian) at 5971.

Julian.<sup>576</sup> In this context, an Audit Group “is a group who has primary responsibilities for auditing the specific either First or Second Line of [Defense].”<sup>577</sup>

As the Executive Audit Director responsible for the Community Bank Line of Business, Mr. McLinko “had primary responsibility for managing the activities within that Audit Group.”<sup>578</sup>

The Audit Group for which Mr. McLinko was EAD was the only group that was focused on the Community Bank.<sup>579</sup> Mr. Julian testified that throughout the relevant period, as one of his direct reports, Mr. Julian found Mr. McLinko to be well qualified to execute the role of EAD.<sup>580</sup> He opined that Mr. McLinko was competent, professional, and had significant internal audit experience.<sup>581</sup> He said that at no time did he have any concerns about Mr. McLinko’s performance, nor did he identify any red flags about Mr. McLinko’s work.<sup>582</sup>

Mr. Julian explained that given the size of the Community Bank, Mr. McLinko “divided that into subgroups for purposes of being able to appropriately provide oversight – or to provide audit activities over.”<sup>583</sup>

Mr. Julian testified that the purpose of the WFAS Policy Manual was to assure that the members of WFAS “understood their accountabilities, responsibilities and so forth, the various policies that were implemented for oversight for how [WFAS] executed its work.”<sup>584</sup> Mr. McLinko testified that the WFAS Policy Manual “is the guidance, the manual for how internal auditors and the internal audit department” is run, the “policies and procedures.”<sup>585</sup>

Mr. McLinko testified that under the Policy he was responsible to communicate with the Operating Committee Group (OCG).<sup>586</sup> According to Mr. McLinko, Carrie Tolstedt was the OCG member for Community Banking in 2013.<sup>587</sup> He testified that during 2013, he

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<sup>576</sup> Tr. (Julian) at 5971.

<sup>577</sup> Tr. (Julian) at 5976-77.

<sup>578</sup> Tr. (Julian) at 5979.

<sup>579</sup> Tr. (Julian) at 5977.

<sup>580</sup> Tr. (Julian) at 5977.

<sup>581</sup> Tr. (Julian) at 5977.

<sup>582</sup> Tr. (Julian) at 5974-75.

<sup>583</sup> Tr. (Julian) at 5988-89.

<sup>584</sup> Tr. (Julian) at 5981, citing R. Ex. 12281 at 44.

<sup>585</sup> Tr. (McLinko) at 7778.

<sup>586</sup> Tr. (McLinko) at 7779, citing R. Ex. 12281 at 44.

<sup>587</sup> Tr. (McLinko) at 7780.



communicated and met regularly with Ms. Tolsted, through formal in-person meetings held twice a year, and at other times in other settings.<sup>588</sup>

### **Mr. McLinko's Interaction with the OCC's Examiners and External Auditors**

Mr. McLinko testified that although his office was in Charlotte, North Carolina, he and his team “would travel to San Francisco, since that is where the majority of the regulators were.”<sup>589</sup> He testified that during these meetings, “I would go through at a high-level overview of what . . . the team had done since the last time we met, audit activities, audit reports issued, issue validation activities, staffing, things along those lines.”<sup>590</sup>

Mr. McLinko stated his Senior Audit Managers then would “talk about the actual audit work, audit reports that moved into planning, review work that had been reported, what issues we had, anything like that.”<sup>591</sup> He added, “If there was any special things the regulators wanted, we would talk about that, and then we would turn it over to them to provide us information about their activities.”<sup>592</sup> He denied, however, that this meant he was relying on the OCC to tell him how to do his job or to do his job for him.<sup>593</sup>

Mr. McLinko testified that while the chart indicated he would meet with external auditors if applicable, this task did not much apply to him: “Since this was external auditors and the fact that they're dealing with the finance side of the bank, that was mostly under the auspices of Andrew Shipley and his team.”<sup>594</sup>

Mr. McLinko also explained his responsibility regarding risk assessable business units (RABUs)<sup>595</sup> – which he described as “the area basically that you have selected to audit or could be a component of that RABU” – per this chart, his role basically that “I was aware of the activities.”<sup>596</sup> He testified that per this chart, drafts of audits would be shared with the line of business being audited because “we wanted to confirm the factual data about the business to ensure that it was accurate” but that it “had nothing to do about our findings or anything like that.”<sup>597</sup>

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<sup>588</sup> Tr. (McLinko) at 7780.

<sup>589</sup> Tr. (McLinko) at 7783.

<sup>590</sup> Tr. (McLinko) at 7783.

<sup>591</sup> Tr. (McLinko) at 7783-84.

<sup>592</sup> Tr. (McLinko) at 7784.

<sup>593</sup> Tr. (McLinko) at 7784.

<sup>594</sup> Tr. (McLinko) at 7784.

<sup>595</sup> Per errata reported by Respondents, where the court reporter transcribed PM's testimony as identifying RABUs as “Risk Accessible Business Units,” the correct transcription of testimony from PM was “Risk Assessable Business Units”. See Respondents Amended Revised Errata to Transcripts of Hearing Days 9 through 38 at 68.

<sup>596</sup> Tr. (McLinko) at 7785-86.

<sup>597</sup> Tr. (McLinko) at 7786.

Mr. McLinko testified that like the previous line item, his responsibility for finalizing and releasing the audit report was limited: this line meant “my either senior audit manager or supervisor would inform me that the report was completed.”<sup>598</sup>

Mr. McLinko testified that throughout the relevant period OCC examiners frequently would attend bimonthly meetings with him and his team “to improve the communication flow . . . for information to be shared, both me and my team to the regulators, the regulators back to us, so that they have an understanding of our audit activities.”<sup>599</sup>

According to Mr. McLinko, in addition to these regularly scheduled meetings, “[i]t was possible that if the OCC was beginning one of their examinations in an area, they would reach out and ask us what our audit activities were there so we could share that work with them so they could make a determination, help them learn about the area.”<sup>600</sup>

Through leading questioning by his Counsel during direct examination, Mr. McLinko testified that in early 2013 his team made an effort to analyze its coverage of processes and controls relating to sales in the Community Bank.<sup>601</sup> He testified that his team members “documented the sales process . . . as they understood it and then overlaid the audit activities that – over the three – over the groups that were done.”<sup>602</sup>

Mr. McLinko identified the Regional Banking RABU Overview, and stated this “was a good way for the senior audit manager to provide me with the perspective on how they arrive at their decisions to audit the things that they wish to audit.”<sup>603</sup>

Mr. McLinko testified that the Overview included information about the “methodology behind how the senior audit managers and their teams prepared this documentation” and identified “Sales Quality/Integrity” as a high priority section.<sup>604</sup> This section of the Overview contained the following bullet point:

Sales Quality/Integrity: Focused on high level sales integrity monitoring and analysis performed by this GRO group. Includes review of the Sales Quality Report Card (signatures, activations, etc.) and sales integrity processes (allegations, reporting, ethics line, etc.).<sup>605</sup>

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<sup>598</sup> Tr. (McLinko) at 7786-87.

<sup>599</sup> Tr. (McLinko) at 7865,

<sup>600</sup> Tr. (McLinko) at 7866.

<sup>601</sup> Tr. (McLinko) at 7867.

<sup>602</sup> Tr. (McLinko) at 7868.

<sup>603</sup> Tr. (McLinko) at 7870; R. Ex. 3534.

<sup>604</sup> Tr. (McLinko) at 7871; R. Ex. 3534 at 2.

<sup>605</sup> R. Ex. 3534 at 2.

Mr. McLinko confirmed that Ms. Russ Anderson led the referenced GRO; and testified that it was his understanding that her group “performs monitoring of types of information that they receive on allegations, ethics, things along those lines.”<sup>606</sup> Mr. McLinko testified that through reading this Overview, he became familiar with the Sales Quality Report Card: that it was a report “that was produced for the Risk Council”; that it “listed a large number of metrics, and on those metrics, it also listed thresholds”; and that it “was a document that could be reviewed by the senior leaders of the Community Bank for branch activities, sales-type activities at the branch.”<sup>607</sup>

When asked by his Counsel during direct examination, “What can you tell me about the CBO group’s review around the quality of sales report card in 2013?” Mr. McLinko responded, “I can tell you that it was performed” but offered no details about how it was performed or what results were reported.<sup>608</sup>

Similarly, when asked whether he was familiar with the “regional bank call program”, Mr. McLinko was able to state that “from what I recall, the QSRC was part of the monitoring program” and that the program involved “audit work that would go into various areas periodically, normally quarterly, to review various types of activities, meet with management, understand what is happening in the area, confirming certain activities that are taking place”; but that he did not review the QSRC reporting, having delegated that to “either the senior audit manager or someone on his team that was assigned to it.”<sup>609</sup> He testified that no one from the CBO team expressed any concerns about the QSRC data that they were reviewing.<sup>610</sup>

Similarly, Mr. McLinko testified that the CBO group he led did not cover EthicsLine reporting, notwithstanding the Overview included in the “Sales Quality/Integrity” report: He stated the processes referred to in the Overview had been “put into place in working with Corporate Investigations on the referral of allegations and the reporting with the EthicsLine area” and the Sales Quality Group “would get information from those groups” and “determine what the next steps were with it.”<sup>611</sup>

When asked by his Counsel during direct examination why this information was included in this document, Mr. McLinko responded, “Well, it’s what the business unit, in this case the Sales Quality Group, was using. Just because . . . it’s an area that [the CBO group doesn’t] audit, it doesn’t mean that it’s information that wouldn’t be appropriate to be used by that group.”<sup>612</sup>

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<sup>606</sup> Tr. (McLinko) at 7872.

<sup>607</sup> Tr. (McLinko) at 7873.

<sup>608</sup> Tr. (McLinko) at 7873.

<sup>609</sup> Tr. (McLinko) at 7873-74.

<sup>610</sup> Tr. (McLinko) at 7874.

<sup>611</sup> Tr. (McLinko) at 7875.

<sup>612</sup> Tr. (McLinko) at 7875-76.

The Overview also included “Supporting Notes” regarding Regional Banking Incentive Compensation: “Regional banking conducted an audit of incentive compensation as part of the 2012 audit plan. Related [Regional Bank] management compensation practices will be considered within the scope of the 2013 [Community Bank Human Resources] Compensation audit.”<sup>613</sup>

Again, Mr. McLinko testified during direct examination by his Counsel that the CBO team was not responsible for the audit listed here: “At that time, the practices for auditing incentive compensation were transitioning over to the [Financial Controls Activity] team” led by Andrew Shipley, and that the listing appeared in the Overview only for “information purposes.”<sup>614</sup>

Included in the Overview was a chart describing “the business where audit work is going to be performed” by the CBO group he led.<sup>615</sup> Mr. McLinko testified, “this is the actual audit activity that was going to take place.”<sup>616</sup>

Elaborating, Mr. McLinko testified:

The audit type is what we reviewed before, whether control testing, monitoring, project auditing, that sort of thing. And then the hours -- the hours that the senior audit manager felt they needed to get this work done. And then the plan driver is – while it's in capitals, you can refer these plan drivers back to things like you said, high priority before, HP. The driver for these first three audits of the audit forms that you see was the high priority.<sup>617</sup>

The Overview reported that the 2013 audit coverage strategy “is influenced by the following risk drivers:

- Regulatory Change – Regulatory scrutiny and resulting changes to products/requirements/processes place additional pressure on Regional banking to ensure customers have a positive experience through all channels, but specifically through the store and ATM channels for regional banking.
- Reputation Risk/Customer Experience – Maintaining high customer service quality levels is imperative to managing reputation risk in the current environment; ensuring the customer is not presented with unsuitable products or other behaviors not in the best interest of the customer.

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<sup>613</sup> R. Ex. 3534 at 3.

<sup>614</sup> Tr. (McLinko) at 7877.

<sup>615</sup> Tr. (McLinko) at 7877; R. Ex. 3534 at 3.

<sup>616</sup> Tr. (McLinko) at 7877.

<sup>617</sup> Tr. (McLinko) at 7878.

- New/Enhanced Product Offerings: Pricing and sales strategies must ensure a positive customer experience in helping them to achieve their financial goals, while adhering to applicable consumer protection requirements.
- Customer Complaints: As noted above, heightened reputation risk has brought additional scrutiny on the bank’s customer complaints process, ensuring that customers are provided appropriate and timely attention.
- Incentive Compensation – There is increased focus on compensation incentives, particularly on those that may drive inappropriate/unethical practices resulting in poor sales quality and ultimately harm to the customer.<sup>618</sup>

The Overview identified “a mix of assurance engagements (monitoring, project audits, control testing) focused on key risk drivers within high risk processes.”<sup>619</sup>

Regarding the Group Risk Office – led by Ms. Russ Anderson, zero hours were allocated for the GRO’s Regulatory Reform project, 800 hours of Control Testing for “RM – Sales Quality/Integrity,” and 200 hours of Business Monitoring for the GRO Business Segment regarding “RB Compliance – program/CRAS/Governance”.<sup>620</sup> “Key Risks” that “Must be Covered” included “Ongoing monitoring of Regional Bank’s progress and compliance to enterprise-established reporting requirements” regarding Customer Complaints.<sup>621</sup>

Mr. McLinko identified a presentation that was shared with the regulators for the October 2013 bimonthly meeting.<sup>622</sup> He testified that he presented the Community Bank and TOG Operations Team Update to regulators, including the OCC examiners, and identified the section entitled, “2013 Plan Changes” as a report on “whether we are adding something to our Plan or removing something from the Plan.”<sup>623</sup>

The changes reported in October 2013 included the addition of Control Testing in the Operations Fraud Program (due to “enterprise requirements of fraud coverage across WFAS”) and the Regional Bank Fraud Program (again, due to “enterprise requirements of fraud coverage across WFAS”).<sup>624</sup> Mr. McLinko testified that the changes were in response to “guidance provided to the . . . audit teams . . . on what they should do to monitor for the implementation”

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<sup>618</sup> R. Ex. 3534 at 1.

<sup>619</sup> *Id.*

<sup>620</sup> *Id.* at 3.

<sup>621</sup> *Id.* at 1.

<sup>622</sup> Tr. (McLinko) at 7964; R. Ex. 4740.

<sup>623</sup> Tr. (McLinko) at 7965; R. Ex. 4740 at 5.

<sup>624</sup> R. Ex. 4740 at 5.

of a corporate-wide fraud program.<sup>625</sup> These changes were “the way to assign those resources to perform that.”<sup>626</sup>

The October 2013 Update also reported on the cancellation of two Control Testing audits – both of which related to Community Banking.<sup>627</sup> First, there had been an audit as part of the “2013 Product & Service Management Policy” through which Mr. McLinko’s team “performed a detailed design evaluation on the DCG program with no concerns noted.”<sup>628</sup> Although the Update referred to business monitoring after the cancellation of this audit,<sup>629</sup> Mr. McLinko offered no evidence indicating his review of any business monitoring reports relating to this canceled audit.

Second, the existing Control Testing of Regional Bank’s “In-Store Customer Complaint process” was canceled.<sup>630</sup> The October 2013 Update provided this rationale for canceling the Customer Complaint audit:

The [Regional Bank] In-Store Customer Complaint process is currently in “pilot” mode and has only been rolled out to 4 states. Additional roll-out will continue through March 2014. As this process is the focus of the RB-Customer Complaint audit, this review has been canceled until full implementation and evidence of sustainability of the new in-house customer complaint process. The majority of Regional Banking customer complaint risk is managed within WFCC. Coverage of WFCC complaint processes was performed in 2013 with an effective rating, therefore, mitigating the overall exposure and supporting the delay of this audit.<sup>631</sup>

Elaborating on this justification for canceling the Regional Bank customer complaint audit, Mr. McLinko testified:

This audit – when this plan was put together, which would have been, at this stage, maybe nine months ago, there was a customer complaints policy being implemented again at the corporate level and being driven down to all of the lines of business. At that point during the annual planning, the opinion was

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<sup>625</sup> Tr. (McLinko) at 7966.

<sup>626</sup> Tr. (McLinko) at 7966.

<sup>627</sup> R. Ex. 4740 at 5.

<sup>628</sup> *Id.*

<sup>629</sup> *Id.*: “As part of the 2013 Product & Service Management Policy Implementation Review . . . Audit performed a detailed design evaluation on the DCG program with no concerns noted. In addition, limited product/service modifications will be executed using the new tool in 2013. Finally, the process does not require coverage until 2014. For the remainder of 2013, Audit will continue to monitor the pipeline and create independent assessments of all projects that are executed to determine if project audits are warranted.”

<sup>630</sup> R. Ex. 4740 at 5.

<sup>631</sup> *Id.*

that we thought there would be enough audit evidence to be able to do work to see how the process was working. As we do our dynamic audit plan, as we continued to monitor this through business monitoring, we determined that their pilot hadn't gotten far enough along. As a result, there was really not enough to test to provide good audit evidence on the effectiveness of the controls.<sup>632</sup>

Mr. McLinko opined that the decision to cancel this audit was consistent with IIA standards because:

one of the main reasons is the aspect of doing audit work over an area that's -- you know, over a business unit that has control processes that are changing does not add any value to . . . Wells Fargo or to the business unit, because you're auditing something that's changing. So you wait until that work is completed, and then you do the audit work.<sup>633</sup>

Mr. McLinko offered no suggestion that there would be business monitoring over these control processes following this Control Testing cancellation, but testified that no one from the OCC raised any concerns about the change in audit coverage or the cancellation of audits reported in the October 2013 Update.<sup>634</sup>

#### **Mr. McLinko's Appointment as a Wells Fargo Code of Ethics Administrator**

Mr. McLinko testified that for at least part of the relevant period he was also a Wells Fargo Code of Ethics Administrator.<sup>635</sup> He acknowledged that in this position, he had the duty to "review different types of information that came to us," and as such it was important for him to be familiar with the Wells Fargo Code of Ethics.<sup>636</sup>

The record reflects that on August 25, 2013, Julie Grotnes sent to both Mr. McLinko and Mr. Julian and others the Wells Fargo Code of Ethics Administrator Annual Training, dated August 26, 2013.<sup>637</sup> Ms. Grotnes wrote that the attachment held the meeting materials for the Code of Ethics Administrators quarterly meeting for the third quarter of 2013.<sup>638</sup>

In the meeting materials, Corporate Security through Mr. Bacon provided an Update reporting on "Investigation Trends" that included the following:

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<sup>632</sup> Tr. (McLinko) at 7968.

<sup>633</sup> Tr. (McLinko) at 7969.

<sup>634</sup> Tr. (McLinko) at 7969.

<sup>635</sup> Tr. (McLinko) at 8458.

<sup>636</sup> Tr. (McLinko) at 8458.

<sup>637</sup> Tr. (McLinko) at 8860-61; R. Ex. 4498 at 1-2 (transmittal email); R. Ex. 4499 (Code of Ethics Code Administrator Annual Training – 2013).

<sup>638</sup> R. Ex. 4498 at 2.

General increase in allegations of TM misconduct across most all LOBs and within most all case types

- 6,841 cases opened thru end of June, up 7% over same time period last year (Heightened awareness and increased monitoring & detection driving some of the increases)
- Increases in allegations involving potential Sales Integrity Violations, Falsification of Records, General Code of Ethics Issues and Information Security Policy Violations
  - Within Code of Ethics, an increase in allegations involving potential Conflicts of Interest and Borrowing/Lending with Customer or Team Member<sup>639</sup>

Mr. McLinko was asked during cross-examination whether the data being reported in this Update led him to believe that there was a systemic sales practices misconduct problem in the Community Bank, and he responded that without looking through “the training involved and the types of details and stuff like that in it” he “can’t really comment on it”.<sup>640</sup>

Included in the training was a description of the role of Line of Business Code Administrators, including Mr. McLinko:

- Code Administrators play a key role as SMEs [Subject Matter Experts] on the COE [Code of Ethics]
- Ensure oversight of the processes by which the Code is administered with their:
  - broad perspective of their business
  - awareness of the ethics-related issues typical to their LOB
  - ability to exercise independent judgment when faced with an ethics question
- Code Administrators must be accessible to team members<sup>641</sup>

Included in the training was an articulation of “Primary Principles of the Code of Ethics”:

There are four fundamental principles of the Wells Fargo Code of Ethics and Business Conduct that guide our company:

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<sup>639</sup> R. Ex. 4499 at 3.

<sup>640</sup> Tr. (McLinko) at 8862. Note that Enforcement Counsel sought the introduction of R. Exs. 7243 (transmittal email) and 7244 (Code of Ethics Code Administrator 2014 3<sup>rd</sup> Quarter Meeting with EthicsLine Update), and R. Exs. 11404 (transmittal email) and 11405 (Code Administrator’s Bi-Annual Meeting, December 11, 2015). Tr. (McLinko) at 8868. Upon objection and finding the evidence cumulative and repetitive and thus lacking in material relevance, Respondents’ objections to the introduction of these four of their proposed exhibits was sustained, such that the exhibits are in the record as proffers only. Tr. (McLinko) at 8868.

<sup>641</sup> R. Ex. 4499 at 10.



1. **Serve Wells Fargo's Best Interests**<sup>642</sup>

- Knowing and understanding your job
- Acting in an honest, ethical and legal manner
- Conducting Wells Fargo's business and community involvement in compliance with all applicable laws, rules and regulations
- Complying with Wells Fargo's policies and procedures
- Using good judgment and common sense in your decision-making and dealings with others
- Reporting any actual or potential problems in Wells Fargo's services, operations, relationships with vendors, or in Wells Fargo's business relationships with domestic or foreign customers or officials
- Promptly reporting any violations or potential violations of this Code, applicable laws, rules or regulations, or of accounting standards or controls
- Protecting and ensuring efficient use of Wells Fargo's assets<sup>643</sup>

2. **Act with Honesty, Integrity and Trustworthiness**<sup>644</sup>

Acting with integrity requires:

- Providing complete and accurate information
- Maintaining accurate records
- Following incentive program guidelines
- Avoiding undue influence
- Verifying payments promptly<sup>645</sup>

3. **Preserve Confidentiality**<sup>646</sup>

Wells Fargo is committed to protecting the private, personal and proprietary information of all customers, vendors and team members.

- You may ONLY disclose confidential customer information outside of Wells Fargo when required by law or in accordance with Wells Fargo's privacy policies and customer agreements

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<sup>642</sup> *Id.* at 13.

<sup>643</sup> *Id.* at 14.

<sup>644</sup> *Id.* at 10.

<sup>645</sup> *Id.* at 15.

<sup>646</sup> *Id.* at 13.

- Be aware of and honor Wells Fargo's confidentiality and nondisclosure agreements with third parties
- Do not access confidential customer information without a specific business purpose
- Safeguard Wells Fargo's proprietary information<sup>647</sup>

4. **Avoid Conflicts of Interest**<sup>648</sup>

Areas where conflicts of interest may occur include:

- Personal finance and investments
- Transactions with Wells Fargo, either your personal transactions or those of friends and family members
- Borrowing and lending practices
- Business expenses
- Outside business opportunities and referrals
- Activities outside the company, either for profit or in your community
- Fiduciary activities, or customers' wills, trusts and estates
- Accepting or giving gifts, or activities with customers or vendors<sup>649</sup>

The training materials included a description of the Code Administrator's roles and responsibilities, regarding both documentation and escalation:

**Documentation and Record Keeping**

- Maintain files (whether electronic or paper) documenting consultations and inquiries about Code issues to help ensure consistency in how matters are addressed for the business group.
- Ensure that a copy of each disclosure, request for approval or request for exception, noting the approval or disapproval by the Code Administrator, or the OC member, or the Ethics Committee
  - Must be returned to the team member
  - A copy forwarded to Employee Records for placement in the TM's Official Personnel File<sup>650</sup>

**Escalation Process**

- Partner as needed with other Code Administrator(s) within your LOB, HR, ER, HR Policy, the Law Department and/or your LOB Compliance &

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<sup>647</sup> *Id.* at 16.

<sup>648</sup> *Id.* at 13.

<sup>649</sup> *Id.* at 17.

<sup>650</sup> *Id.* at 11.

Operational Risk Manager to ensure consistent interpretation and application of the Code

- When escalating to an OC member, consider additional communication channels within your line of business as appropriate.<sup>651</sup>

During cross-examination, Mr. McLinko was asked whether he read the training materials when he received them, and he responded: “I don’t really recall this meeting at this point and attending the meeting. So I’m not sure if I read it or not.”<sup>652</sup>

### ***Ethics Committee***

Mr. Julian was a member of the Ethics Committee.<sup>653</sup> Mr. Julian identified the Ethics Committee Charter as being set forth in the Code Administration Responsibilities section of the WF&C Code of Ethics & Business Conduct, which was effective January 2014.<sup>654</sup> He described the Ethics Committee as a WF&C management committee “intended to provide oversight on governance activities of [the] ethics program.”<sup>655</sup>

CRO Loughlin reported that the Ethics Committee “is responsible for administering and interpreting the Wells Fargo Code of Ethics and Business Conduct, as well as approving its content. The chairmanship of this committee rotates every three years among the members of the committee.”<sup>656</sup>

Mr. Julian identified the agenda that had been circulated in advance of the December 2, 2013 meeting of the Ethics Committee.<sup>657</sup> He acknowledged that the agenda made no mention of sales integrity or sales practices misconduct by team members of the Community Bank – notwithstanding the information that was known to him by December 2013.<sup>658</sup> Asked whether he was surprised that the agenda included no mention of the sales integrity or sales practices misconduct issue, Mr. Julian responded that he was not surprise – “not at the time.”<sup>659</sup> He acknowledged that by that meeting the L.A. Times article had come out, but justified his reaction by stating that “[i]t was known that work was being performed by the Community Bank to address the issue or look into the issue.”<sup>660</sup> From this, Mr. Julian concluded that members of the

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<sup>651</sup> *Id.* at 11.

<sup>652</sup> Tr. (McLinko) at 8861.

<sup>653</sup> Tr. (Julian) at 6226.

<sup>654</sup> Tr. (Julian) at 6222-24; R. Ex. 6638 at 24.

<sup>655</sup> Tr. (Julian) at 6228.

<sup>656</sup> OCC Ex. 1553 at 10.

<sup>657</sup> Tr. (Julian) at 6304, R. Ex. 6014.

<sup>658</sup> Tr. (Julian) at 6305; R. Ex. 6014.

<sup>659</sup> Tr. (Julian) at 6305.

<sup>660</sup> Tr. (Julian) at 6305.

Ethics Committee “were already informed of the matter and knew that work was going on by December 2 of 2013.”<sup>661</sup>

Mr. Julian identified the meeting minutes for the December 2, 2013 Ethic Committee meeting, which he attended.<sup>662</sup> Notwithstanding the information that was then available to Mr. Julian by December 2, 2013 regarding sales practices misconduct by team members of the Community Bank, he identified nothing during his testimony that indicated through the meeting minutes that he shared any of that knowledge with other members of the Committee.<sup>663</sup>

The 2014 Charter established that members of the Committee would be appointed by the chief executive officer of WF&C and would be “responsible for the content of the Code and overseeing the policy and interpretation of the Code.”<sup>664</sup> Each member of the Operating Committee “is responsible for Code administration for all team members in the business groups that report to him or her.”<sup>665</sup>

Mr. Julian testified that the WF&C Ethics Committee was later subsumed by the Ethics and Integrity Oversight Committee, and he identified the April 13, 2016 Charter for that Committee as well.<sup>666</sup>

Mr. Julian identified the meeting agenda for the August 22, 2013 Ethic Committee meeting and stated that he was present at that meeting.<sup>667</sup> Through the Meeting Agenda for the 2013 meeting, Corporate Security reported that out of 6,841 cases investigated by Corporate Investigations YTD end of 2Q 2013, 5,862 cases were from the Community Bank line of business, reflecting a 5% increase from the same period in 2012.<sup>668</sup>

Equally significant, year to date through the end of the second quarter 2103, Community Banking generated 3,516 EthicsLine reports – constituting 83.44% of all the reports received.<sup>669</sup> The report reflected there were 105,185 team members in the Community Bank line of business, such that the reports identified 37.7 percent of all team members working for the Community Bank – or 33 reports per 1,000 team members (contrasting with 1 report per 1,000 team members

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<sup>661</sup> Tr. (Julian) at 6305-06.

<sup>662</sup> Tr. (Julian) at 6301-02; R. Ex. 6322.

<sup>663</sup> Tr. (Julian) at 6301-03; see also R. Ex. 6322.

<sup>664</sup> R. Ex. 6638 at 24.

<sup>665</sup> *Id.*

<sup>666</sup> Tr. (Julian) at 6225; R. Ex. 12528.

<sup>667</sup> Tr. (Julian) at 6229-30; R. Ex. 4479.

<sup>668</sup> R. Ex. 4479 at 5.

<sup>669</sup> *Id.* at 8.

for the Wealth Management, Wholesale Banking, and Technology and Operations lines of business).<sup>670</sup>

Minutes from the August 22, 2013 Ethic Committee meeting reflect the contents of the materials supplied in advance of the meeting.<sup>671</sup> Mr. Bacon, head of Corporate Investigations, reported that “misconduct and ethics violations are up,” but “EthicsLine reports are down 4%” marking the “first time that’s happened since the Wachovia merger.”<sup>672</sup> He noted that March “tends to be the highest month for reports,” opining that this might be “associated with sales campaign activity.”<sup>673</sup>

Mr. Bacon reported that while Community Banking numbers “are decreasing,” they were still the “highest number of reports per 1,000 Team Members and most associated with Sales Integrity issues.”<sup>674</sup> He reported, “Claudia Russ Anderson’s team is aware of the metrics and is working on this. Some Regional Banking areas have seen marked improvement in metrics while others still need to improve”.<sup>675</sup>

Mr. Bacon made two points: first, “CFPB and Sales Integrity issues are most prevalent – there needs to be continued focus in this area;” and second – this in response to a question from a member of the Committee – Mr. Bacon reported that “while he is not seeing regulatory inquiries to date, he anticipates the trend is heading toward more inquiry and we need to be prepared for it. There is more prevalence of Team Members going to regulators with reports and complaints.”<sup>676</sup>

Notwithstanding the written comments from Mr. Bacon noting the trend that would lead to more regulatory inquiry and that the highest number of reports per 1,000 team members were in cases associated with sales integrity issues, Mr. Julian testified that the report was “absolutely” reassuring to him and that his takeaway from Mr. Bacon’s presentation was that “certain metrics were improving across the organization,” and that Ms. Russ Anderson “was aware and working on the issues.”<sup>677</sup>

According to the Charter, the 2016 iteration of the Committee “is sponsored by and operates under the authority of the Audit & Examination Committee of WFC’s Board of Directors, as well as the Operating Committee, which collectively authorize it to perform the oversight responsibilities described in this Charter.”<sup>678</sup>

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<sup>670</sup> R. Ex. 4479 at 8.

<sup>671</sup> R. Ex. 4501.

<sup>672</sup> *Id.* at 1.

<sup>673</sup> *Id.* at 1-2.

<sup>674</sup> *Id.* at 2.

<sup>675</sup> *Id.*

<sup>676</sup> *Id.*

<sup>677</sup> Tr. (Julian) at 6238.

<sup>678</sup> R. Ex. 12528 at 1.

Included in the Charter for the 2016 Committee, members were required to provide “significant issue management oversight,” to include the review of “significant ethical and business conduct issues that may have a material impact on the Company’s operations and/or reputation, including oversight of resolution, proposed corrective actions and identified program gaps or other control weaknesses; review and ensure appropriate management resolution of allegations involving significant violations of business conduct law or regulation”.<sup>679</sup>

Included in the 2016 Charter was the provision that Committee members were to review and evaluate “emerging ethics, business conduct and conflicts of interest issues and trends in response to changes in business strategy, risk and regulatory and legal requirements to assess the implications for business objectives, strategies, and practices.”<sup>680</sup>

Also included in the 2016 Charter was the provision that Committee members periodically review and advise the Head of Global Ethics & Integrity “on the adequacy and effectiveness of the Company’s ethics, business conduct and conflicts of interest risk management program, including policies, programs, applicable Global Ethics & Integrity risk management practices and the awareness and promotion of an ethical culture across the enterprise”.<sup>681</sup>

Also included in the 2016 Charter was the requirement that Committee members review business conduct activity “to include enterprise and line of business specific investigative key activity (case totals, case type activity, related terminations/resignations) and EthicsLine activities, which includes issues related to sales practices”.<sup>682</sup>

Also included in the 2016 Charter was the requirement that Committee members review “specific business conduct or fraud incidents, to include cases involving EthicsLine allegations, whistleblower complaints, issues escalated by the business compliance teams and unethical or misconduct identified by Global Ethics & Integrity oversight activities.”<sup>683</sup>

The 2016 Charter described Committee members as “the most senior management-level risk governance committee to which key ethics, business conduct and conflicts of interest risk issues are escalated”.<sup>684</sup> These issues included business conduct that was “likely to cause material adverse impact to customers, or to the Company’s reputation,” and issues “likely to be discussed with the Company’s regulators”.<sup>685</sup> The issues also included those that “based on a

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<sup>679</sup> *Id.* at 1-2.

<sup>680</sup> *Id.* at 1.

<sup>681</sup> *Id.*

<sup>682</sup> *Id.* at 2.

<sup>683</sup> *Id.*

<sup>684</sup> *Id.*

<sup>685</sup> *Id.*

reasonable manager’s judgment, may adversely impact the Company,” as well as “[b]udget and resource issues.”<sup>686</sup>

The 2016 Charter provided that for each escalated issue, the Committee “shall have the authority to assess the degree to which the owner has identified, assessed, controlled, and mitigated the issue at hand,” and may require “further actions to be taken by the owner and may require oversight of the issue by the Committee”.<sup>687</sup> Thus, Mr. McLinko had the ability to escalate through Mr. Julian any issue presented by the Community Bank regarding the mitigation of risks associated with team member sales practices misconduct.

As of 2016, Committee members constituted the most senior management-level risk governance committee to which key ethics, business conduct and conflicts of interest risk issues were to be escalated. These issues included business conduct that was likely to cause material adverse impact to customers, or to the Company’s reputation, and issues likely to be discussed with the Company’s regulators. The issues also included those that, based on a reasonable manager’s judgment, could adversely affect the Company. **Mr. McLinko’s failure to promptly report to the Ethics Committee known control issues related to sales practices misconduct by Community Bank team members constituted unsafe or unsound banking practices and a breach of the fiduciary duty he owed to the Bank.**

#### *Incentive Compensation Committee*

Mr. Julian was a member of the Incentive Compensation Committee.<sup>688</sup> Until June 15, 2015 Mr. Julian served as a voting member of the Incentive Compensation Steering Committee (which later became known as the Incentive Compensation Committee), which was a WF&C committee.<sup>689</sup>

CRO Loughlin reported that the ICC (formerly known as the Incentive Compensation Steering Committee) “leads Wells Fargo’s efforts to enhance incentive compensation practices throughout the company. This committee is chaired by the head of Corporate Human Resources.”<sup>690</sup>

Mr. Julian testified that his role in this committee was limited and that he was “not permitted to in any way act as management, make management-type decisions for the Committee.”<sup>691</sup> He testified that his role was limited – that all he could or would do as Chief

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<sup>686</sup> *Id.* at 2.

<sup>687</sup> *Id.*

<sup>688</sup> Tr. (Julian) at 6060.

<sup>689</sup> Tr. (Julian) at 6143; OCC Ex. 1722 at 1; OCC Ex. 1724 at 3.

<sup>690</sup> OCC Ex. 1553 at 9.

<sup>691</sup> Tr. (Julian) at 6060.

Auditor was “listen for information that would be valuable to share back” with WFAS, and to “share information with the committee that I was aware of”.<sup>692</sup>

There is, however, nothing in the description of the oversight and decision-making authority of the Committee that limited Mr. Julian’s role to listening for information. The oversight and decision-making authority of the Committee included overseeing the “development of enterprise-wide standards for the design and administration of the Company’s incentive compensation plans”, and monitoring the implementation of appropriate actions for enhancing the Company’s incentive compensation programs “to better align with the Federal Reserve Guidance.”<sup>693</sup>

As a direct report, Mr. McLinko thus had direct access to the Committee through Mr. Julian to escalate risk-control issues in the design of the Community Bank’s management of the risks associated with team member sales practices misconduct.

The minutes of the July 8, 2015 meeting of the Incentive Compensation Committee reflect that as part of the reviews conducted under the Incentive Compensation Risk Management (ICRM) Program, “enhancement opportunities were identified, including adding rigor around risk metrics and identifying opportunities for further improvement to address new risks and increased regulatory scrutiny.”<sup>694</sup> During its July 8, 2015 meeting, the Committee received a report that the OCC had issued five Matters Requiring Attention (MRA) that related to Enterprise Sales Practices, including compensation-related requirements.

The Enterprise Sales Practices MRA provided that compensation programs needed to be reviewed to protect against incenting inappropriate behavior and that Corporate Risk needed to review the reasonableness of incentive compensation programs for all Enterprise Sales activities. **Mr. McLinko’s failure to escalate risk-management control issues related to incentive compensation, through Mr. Julian to the Incentive Compensation Committee, on known issues related to inadequate and ineffective risk management controls over the Community Bank’s sales incentives program as it related to sales practices misconduct by Community Bank team members during this meeting constituted unsafe or unsound banking practices and a breach of the fiduciary duty he owed to the Bank.**

Under Mr. McLinko’s leadership, the CBO audit team was expected to assure there was an appropriate governance model – that is, a model in which the people who should be designing compensation incentive programs were designing them, assuring that there were effective review programs in place, and assuring that there was a governance structure through which the programs incented appropriate behavior. Where sales goals incented inappropriate behavior by Community Bank’s team members, Mr. McLinko had a duty to determine the adequacy of the governance structure that supported those incentives, so that, acting through his reports to Mr. Julian, he and Mr. Julian could assure the A&E Committee members that sales goals did not

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<sup>692</sup> Tr. (Julian) at 6060.

<sup>693</sup> OCC Ex. 1722 at 1.

<sup>694</sup> OCC Ex. 1700 at 1.



encourage sales practices misconduct.

Mr. Julian identified the Incentive Compensation Risk Management Policy, published May 7, 2015.<sup>695</sup> Through this Policy, WF&C established four compensation objectives – “pay for performance,” the promotion of “a culture of risk management that avoids unnecessary or excessive risk taking,” the goal of “attract[ing] and retain[ing] talent with competitive pay,” and aligning “employee interests with shareholders.”<sup>696</sup>

The Policy statement also provides that Wells Fargo “ensures it has effective incentive compensation arrangements that support the long-term strength of the organization” by providing team member incentives “that appropriately balance risk and financial results,” ensure that “incentive arrangements are compatible with effective controls and risk management,” enforce “strong corporate governance, including active and effective oversight by the company’s Board of Directors,” and disclose “the structure of its incentive-based compensation arrangements to governance bodies and regulators in accordance with applicable law and regulation”.<sup>697</sup>

**Mr. McLinko’s failure to promptly report, through Mr. Julian, to the Incentive Compensation Committee on known issues related to the Community Bank’s risk management control failures related to sales goals pressure and sales practices misconduct by Community Bank team members during this meeting constituted unsafe or unsound banking practices and a breach of the fiduciary duty he owed to the Bank.**

Mr. Julian identified the Incentive Compensation Committee Meeting Minutes dated July 8, 2015.<sup>698</sup> The minutes reflect that Mr. Julian was present at the meeting, and that included in the materials presented during the meeting was the Governance Review and Program Update of the Incentive Compensation Risk Management (ICRM) Program of the Incentive Compensation Committee, dated July 8, 2015.<sup>699</sup>

The Program Update included a report indicating that five MRAs the Bank received related to “broader Enterprise Sales Practices, including compensation-related requirements”.<sup>700</sup> The Enterprise Sales Practices MRA provided that compensation programs “need to be reviewed to protect against incenting inappropriate behavior”; that Corporate HR was identified “as part of development” of first and second line of defense governance; and that Corporate Risk “reviews the reasonableness of [incentive compensation] programs for all Enterprise Sales activities”.<sup>701</sup>

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<sup>695</sup> Tr. (Julian) at 6795-96; R. Ex. 10012.

<sup>696</sup> R. Ex. 10012 at 1.

<sup>697</sup> *Id.*

<sup>698</sup> Tr. (Julian) at 6796-97; OCC Ex. 1700.

<sup>699</sup> OCC Ex. 1700 at 2.

<sup>700</sup> *Id.* at 22.

<sup>701</sup> *Id.*

Mr. Julian identified a Risk Assessment Summary provided to CEO Stumpf on February 12, 2016 by Hope Hardison (Director of Human Resources) and Michael Loughlin (Chief Risk Officer).<sup>702</sup>

The Risk Assessment Summary included a list of “key risk issues” as of 2016, one of which related to Sales Practices (without limiting the risks to the Community Bank).<sup>703</sup> Mr. Julian testified that while he recognized the Summary he did not see it other than as part of this enforcement litigation, and had no role in either reviewing or approving the Summary.<sup>704</sup>

The Summary identified Claudia Russ Anderson among those with accountability for the sales practices issue.<sup>705</sup> The Summary rated the sales practices issue at Community Bank as “improvement needed”, describing the issue as “Top OCC issue with 5 MRAs related to Tone at the Top, FLOD, SLOD, and Customer Complaint. Current litigation related to Community Banking, ongoing customer remediation.”<sup>706</sup> It described the impact as “reputational and regulatory risks for Wells Fargo resulting from this issue.”<sup>707</sup> It identified the resolution as follows: “Significant work has been accomplished to address the MRAs, but a lot still needs to be completed in a short timeframe for completion. Acceptable and steady progress is evidenced with all open corrective actions.”<sup>708</sup>

Reputation risk with respect to a control environment of the management of risk was a byproduct of how well functioning the controls worked. WFAS’s role at the enterprise level (for Mr. Julian) and at Community Banking (for Mr. McLinko) was assuring that controls were designed appropriately and were working as intended. There is no indication, however, that WFAS or the CBO audit team contemporaneously participated in addressing the issues raised in this Summary.

### **The OCC’s May 5, 2014 Supervisory Letter**

Mr. Julian identified the OCC’s May 5, 2014 Supervisory Letter addressed to Mr. Quigley for the WF&C A&E Committee.<sup>709</sup> The Letter summarized the results of the OCC’s March 10, 2014 Target Examination of WFAS.<sup>710</sup> Mr. Julian’s takeaway from reading this letter was that the OCC had concluded WFAS “continued to make reasonable progress towards achieving the heightened expectations,” and that he personally “had positively influenced Audit

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<sup>702</sup> Tr. (Julian) at 6942; OCC Ex. 689.

<sup>703</sup> OCC Ex. 689.

<sup>704</sup> Tr. (Julian) at 6942-43.

<sup>705</sup> OCC Ex. 689 at 7.

<sup>706</sup> *Id.*

<sup>707</sup> *Id.*

<sup>708</sup> *Id.*

<sup>709</sup> Tr. (Julian) at 6511; R. Ex. 1613.

<sup>710</sup> R. Ex. 1613 at 1.

stature and the ability to provide credible challenge.”<sup>711</sup> He said the Letter also concluded he personally “had made enhancements to the Audit senior leadership management team as well as . . . what they refer to as production staff to strengthen the talent and skill sets within WFAS.”<sup>712</sup>

Through this Supervisory Letter, the OCC put Mr. Julian on notice that improvement was needed in several areas. The OCC found that “[t]he overall audit plan, including scope, coverage, talent and resources, may not be adequate in light of the MRAs identified during this review related to model development and validation.”<sup>713</sup>

The Letter specifically addressed WFAS’s Business Monitoring Program.<sup>714</sup> It described the Program as a “relationship oriented program where audit team members meet regularly with business line management to monitor emerging risks and adjust audit coverage as appropriate.”<sup>715</sup> It noted there were at least two audit teams that have implemented either continuous auditing or testing programs, and found “there is no standard definition as to what constitutes either program or how they should inform and support audit management and processes or WFAS’ Audit Strategy.”<sup>716</sup>

Further weaknesses were identified regarding the sampling processes WFAS relied upon in its Quality Assurance program: “We requested QA to evaluate the sampling methodologies and sample sizes being used across the various lines of business audit teams in the scope of work in 2014 to ensure the sampling approaches are reasonable and consistent with audit policy.”<sup>717</sup>

### **The OCC’s January 7, 2015 Request Letter Regarding the Operational Risk Management Examination**

Mr. Julian identified the January 7, 2015 Request Letter addressed to Carrie Tolstedt as Senior Executive Vice President of Community Banking, sent from National Bank Examiner Christine Moses of the OCC.<sup>718</sup> The Letter announced the OCC’s intention to conduct an examination of Community Banking operational risk management to begin on February 2, 2015.<sup>719</sup> The scope of the examination was to include an assessment of the level of oversight and reporting within the first line of defense, an evaluation of the appropriateness of governance policies and procedures, business processes, quality and sufficiency of staff to monitor,

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<sup>711</sup> Tr. (Julian) at 6512.

<sup>712</sup> Tr. (Julian) at 6512-13.

<sup>713</sup> R. Ex. 1613 at 2.

<sup>714</sup> *Id.* at 3.

<sup>715</sup> *Id.* at 3-4.

<sup>716</sup> *Id.* at 4.

<sup>717</sup> *Id.* at 3.

<sup>718</sup> Tr. (Julian) at 662-23; R. Ex. 7383.

<sup>719</sup> R. Ex. 7383 at 1.

challenge, and conduct controls testing, and a review of the Community Bank’s cross sell oversight activities.<sup>720</sup>

Asked what the term “cross-sell” means, Mr. Julian responded that “[c]ross-sell within Wells Fargo was the practice of providing customers with different products . . . that the company offered, offering customers different products that was [sic] believed that would be valuable to them.”<sup>721</sup> He described the “cross-sell metric” as a metric “by which the number of products that a customer had or had . . . obtained were provided across various lines or within a line of business.”<sup>722</sup>

Asked how, during the relevant time, cross-sell related to the Community Bank’s revenue, Mr. Julian responded:

Well, it was really inherent in the entire business. So when you think of the Community Bank and the Community Bank's customers, the business of the Community Bank was providing customers with various products that would be useful and valuable to the customer. So it was really a -- somewhat at core of the Community Bank's business.<sup>723</sup>

Mr. Julian added that during the relevant period, WFAS lacked the ability to distinguish cross-sell from the Community Bank’s overall sales activities – because cross-sell “was inherent in the business practice.”<sup>724</sup> He testified that as a result, WFAS could not conduct a cross-sell specific review of the Community Bank analogous to audits conducted for other businesses.<sup>725</sup>

The inability of WFAS to conduct an analogous cross-sell specific review of the Community Bank was discussed between the OCC and Claudia Russ Andersons, as Operations Risk and Compliance Manager.<sup>726</sup> The Supporting Comments for the February 23, 2015 Conclusion Memo reflects the initial meeting on cross sell took place on February 4, 2014.<sup>727</sup> During that meeting, Ms. Russ Anderson explained to the OCC that in the Community Bank, “the focus is on selling customers additional products to enhance the ‘mutual exchange of value’ between customers and the bank. Customers benefit through additional utility, service, and convenience; the bank benefits through increased revenue and customer retention.”<sup>728</sup>

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<sup>720</sup> R. Ex. 7383 at 1.

<sup>721</sup> Tr. (Julian) at 6624.

<sup>722</sup> Tr. (Julian) at 6624.

<sup>723</sup> Tr. (Julian) at 6625.

<sup>724</sup> Tr. (Julian) at 6625.

<sup>725</sup> Tr. (Julian) at 6625-26.

<sup>726</sup> R. Ex. 18918 at 2.

<sup>727</sup> *Id.*

<sup>728</sup> *Id.*

The notes from that meeting reflect that Ms. Russ Anderson told the OCC, “team members do have referral and sales goals but meeting these is only part of the review and evaluation process.”<sup>729</sup> Referral fees paid to team members are capped to keep incentive to sell products in check and keep the focus on customer service.”<sup>730</sup> She identified the “number of WFB products per household” as “the key metric” and reported the “most common products are checking accounts and debit cards.”<sup>731</sup> Other products included credit cards, loans, on-line bill pay, and investment products.<sup>732</sup>

The Conclusion Memorandum reported that as of “4Q14, the retail bank cross-sell metric was 6.17 (number of WFB products held/number of WFB retail bank households).”<sup>733</sup> The “Retail Bank Cross Sell Steering Committee oversees metric data and calculation,” and the Conclusion Memorandum described the work of the Committee – notably its data governance – as “critical” because “the metric is disclosed in SEC filings and is closely watched by investors, analysts, etc.”<sup>734</sup> Notwithstanding the importance of the work of the Committee, the Committee “is not a governance committee and does not have a charter or keep minutes.”<sup>735</sup>

The Conclusion Memorandum lacked audit reports of the Community Bank’s cross sell; it had, however, audit reports of cross sell done in the Wholesale group and the Wealth, Brokerage, and Retirement (WBR) group.<sup>736</sup> Although it lacked an audit report from the Community Bank, the Memorandum reflected that the OCC held a conference call on February 9, 2015 with WFAS personnel, including the Executive Audit Director Paul McLinko and Senior Audit Manager Bart Dees, to review WFAS Community Bank Sales Coverage.<sup>737</sup>

The Memorandum noted that WFAS’s audit reports regarding cross sell in both the Wholesale and WBR groups “focused on cross sell as a separate activity, assessing governance, internal controls, oversight, revenue derived from cross sell, etc.”<sup>738</sup> The Memo reported, “WFAS has not conducted a similarly structured review” of cross sell in the Community Bank.<sup>739</sup> According to Mr. Swanson and Mr. Declue, at this point in the February 9, 2015 conference call, Ms. Russ Anderson and Mr. MacDuff “interjected and reiterated that in CB,

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<sup>729</sup> R. Ex. 18918 at 3.

<sup>730</sup> *Id.*

<sup>731</sup> *Id.*

<sup>732</sup> *Id.*

<sup>733</sup> *Id.*

<sup>734</sup> *Id.*

<sup>735</sup> *Id.*

<sup>736</sup> *Id.*

<sup>737</sup> *Id.*

<sup>738</sup> *Id.*

<sup>739</sup> *Id.*

cross sell is not a separate activity that can be broken out and governed as a stand-alone activity. CB is the bank's main distribution channel and governance over cross sell is part of overall governance over products. Messrs. McLinko and Deese did not disagree or offer additional comments on this subject."<sup>740</sup>

The Conclusions identified four main areas of WFAS's sales coverage for the Community Bank: sales and account opening, incentive compensation, sales quality (monitoring conduct and handling complaints), and the accuracy of reporting the cross sell metric.<sup>741</sup>

In their Conclusions, Mr. Swanson and Mr. Declue report that while the Community Bank's oversight processes "provide generally effective oversight of the [Community Bank's] cross sell activities," the current process "lacks transparency and needs to be formalized in a governing framework that describes roles and responsibilities, lines of reporting, escalation protocols, incentive compensation oversight, and quality assurance processes."<sup>742</sup> Further, the Memo concludes that the "[l]ack of a comprehensive governance framework can expose the CB to heightened reputation risk through negative publicity. Without a more formal structure it is more difficult to ensure compliance with the firm's values and goals for achieving customer satisfaction and strategic and financial objectives."<sup>743</sup>

Business monitoring engagements were assurance engagements that were a collection of ongoing activities conducted to validate issue remediation, to monitor ongoing and emerging risk activities, and to achieve general awareness of the businesses being audited. The results of business monitoring were to be used in ongoing annual dynamic audit plan analysis.<sup>744</sup> A written engagement report was required whenever an activity advances the coverage horizon.<sup>745</sup>

There were five types of business-monitoring activities: Continuous Risk Assessment (CRA), Risk-Assessable Business Unit (RABU) Risk Review, Issue Validation, Call/Awareness Program, and Leverage.<sup>746</sup>

Continuous Risk Assessments were performed on a more continuous or continual basis. They refer to activities to identify and assess risks by examining trends and comparisons within a single process or system, as compared to its own past performance or against other established targets. CRA testing was linked to a specific Process, Risk, or Control and was to be documented on the Documentation workpaper.<sup>747</sup>

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<sup>740</sup> *Id.* at 3.

<sup>741</sup> *Id.* at 3-4.

<sup>742</sup> *Id.* at 1.

<sup>743</sup> *Id.* at 1.

<sup>744</sup> R. Ex. 3560 at 29.

<sup>745</sup> R. Ex. 12281 at 54.

<sup>746</sup> *Id.* at 53-54.

<sup>747</sup> *Id.* at 53.

RABU Risk Review business monitoring was a semi-annual review where the RABU Owner was responsible for evaluating the risk profile and other activities related to the RABU. The RABU Risk Review Checklist was to be used to guide the RABU Owner through the required activities and to document comments and conclusion from those activities.<sup>748</sup>

Issue Validation business monitoring involved validation of prior audit issues and could be performed as part of the business monitoring engagement. Issue Validation testing was to be documented on the Issue form in Issue Track.<sup>749</sup>

Call/Awareness Program business monitoring was established for most RABUs and was designed to monitor activities and maintain an understanding of the risks in a RABU. The nature and extent of business monitoring activities was different for each RABU and took into account the RABU risk ratings and other planned engagements. It could involve business-partner awareness meetings, committee meetings, and analyses of business reporting and metrics. Call/Awareness activities were linked to the Audit Call Program form and were to be documented on the Meeting/Awareness workpaper.<sup>750</sup>

Leveraging in this context was the process where the results of testing performed by Risk Management/Control Testing groups throughout Wells Fargo could be relied upon and leveraged or used by WFAS without WFAS auditors having to do the work. Leveraging was permissible only if specific requirements are met. Policies governing the leveraging of Risk Management or Control Testing groups were available in a separate Policy Manual document.

Leverage testing was linked to a specific Process, Risk, or Control audit, and was to be documented on a Documentation workpaper.<sup>751</sup> “WFAS will report any negative conditions identified during a business monitoring engagement using its Issue & Corrective Action policy.”<sup>752</sup>

None of the Respondents offered any documentation of their reporting of negative conditions identified during the business monitoring of Community Banking’s risk-management controls.

Notwithstanding that WFAS did not audit Community Bank’s branches directly, Mr. Julian denied the claim – attributed to OCC’s Senior Deputy Comptroller Gregory Coleman – that WFAS audit scopes were specifically not designed to audit the sales practices issue.<sup>753</sup> The assertion by the OCC is also related to the Conclusion Memorandum of February 23, 2015, which reported that WFAS has not conducted a structured review of cross sell in the Community

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<sup>748</sup> R. Ex. 12281 at 53.

<sup>749</sup> *Id.*

<sup>750</sup> *Id.* at 53-54.

<sup>751</sup> *Id.* at 54.

<sup>752</sup> R. Ex. 3560 at 29.

<sup>753</sup> Tr. (Julian) at 6632.

Bank (like the ones performed for Wholesale and WRB)<sup>754</sup> and noted Ms. Russ Anderson's insistence during the February 9, 2015 conference call that Community Bank's "cross sell is not a separate activity that can be broken out and governed as a stand-alone activity" and noted no disagreement from WFAS's Mr. McLinko.<sup>755</sup>

The record reflects that at least as of April 2015, the OCC recognized that Community Bank "is the Bank's main distribution channel, thus sales of products are an integral part of the group's activities."<sup>756</sup> This was the stated reason the OCC "evaluated CB sales practices oversight instead of cross sell."<sup>757</sup>

Mr. Julian pointed to the OCC's presentation appearing in the Wells Fargo Bank, N.A. Community Banking Operational Risk Examination Exit Discussion document, dated April 2, 2015. Through a series of leading questions by his attorney, Mr. Julian agreed that given the presentation, there "seem[s] to be some confusion on the OCC's part as to the different meanings as you've discussed of the term 'cross-sell'".<sup>758</sup>

Elaborating, he testified:

I believe that they refer to cross-sell as sales practices activity versus the fact that within the Community Bank, as I've described, the activity of providing customers with products that they needed and wanted was inherent in the business. So there's a difference between how I would think a cross-sell – especially the discussions around cross-sell and the metric and the reporting of cross-sell versus the way the OCC has implied its use.<sup>759</sup>

Notwithstanding the need to assess independently the effectiveness of controls related to enterprise-wide sales practices misconduct, and without identifying work WFAS had done on its own in this regard, Mr. Julian considered the OCC's April 2, 2015 Exit Discussion permitted him to "take confidence that the Community Bank operational risk management activities were . . . effective and consistent with what I was hearing from my own audit folks."<sup>760</sup> He reached this conclusion despite the OCC's conclusion that opportunities exist "to strengthen oversight of CB offshoring activities and sales practices."<sup>761</sup>

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<sup>754</sup> *Id.* at 3.

<sup>755</sup> *Id.*

<sup>756</sup> Tr. (Julian) at 6636; R. ex. 8347 at 3.

<sup>757</sup> R. ex. 8347 at 3.

<sup>758</sup> Tr. (Julian) at 6638.

<sup>759</sup> Tr. (Julian) at 6638-39.

<sup>760</sup> Tr. (Julian) at 6640.

<sup>761</sup> Tr. (Julian) at 6640; R. Ex. 8347 at 4.



Without providing specifics, Mr. Julian testified, “the audit scopes were specifically laid out here to audit controls and activities that were related to sales practices.”<sup>762</sup> He said, “there’s not one control related to sales practices. There’s a series of controls that manage sales practice activities, and these audits within the scopes of these audits were designed to audit specific activities.”<sup>763</sup> He said, “Audit would audit the controls with respect to sales integrity-type activities, which sales practices was one of. So one is auditing the controls around managing risks. The other is, to . . . my understanding, would be Corporate Investigations-type activity where they’re investigating sales practices activity.”<sup>764</sup>

### Three Lines of Defense

Wells Fargo & Company and Wells Fargo Bank, N.A. employed a “Three Lines of Defense” risk management system throughout the relevant period.<sup>765</sup> WFAS’s Internal Audit was the Third Line of Defense.<sup>766</sup> The First Line of Defense refers to the Line of Business (LOB) organizations, including Community Bank.<sup>767</sup> The Second Line of Business refers to “the corporate risk function as well as a few other second line of defense activities, like HR and Legal.”<sup>768</sup>

The First Line of Defense – “Lines of Business & Administrative Functions” – is responsible “for taking, identifying, assessing, managing, and controlling the risks it generates.”<sup>769</sup> It “owns” risk and is accountable to Senior Management and the WF&C Board of Directors.<sup>770</sup> This principle requires “adherence to risk framework, risk appetite and concentration limits, etc.”<sup>771</sup>

Through the March 4, 2013 report, “Wells Fargo’s Risk Management Framework,” CRO Loughlin described the first line of defense in these terms:

First line of defense: Lines of business.

We believe placing risk identification, assessment, monitoring, ownership, management, and mitigation as close as possible to the source of risk improves risk management effectiveness and efficiencies. . . . To be effective,

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<sup>762</sup> Tr. (Julian) at 6632.

<sup>763</sup> Tr. (Julian) at 6632.

<sup>764</sup> Tr. (Julian) at 6632-33

<sup>765</sup> Tr. (Julian) at 5936.

<sup>766</sup> Tr. (Julian) at 5936.

<sup>767</sup> Tr. (Julian) at 5936.

<sup>768</sup> Tr. (Julian) at 5936.

<sup>769</sup> R. Ex. 1780 at 41.

<sup>770</sup> *Id.*

<sup>771</sup> *Id.*

the line-of-business risk management process must recognize good risk management behaviors and also hold individuals accountable for poor risk management behaviors.<sup>772</sup>

The Second Line of Defense – “Corporate Risk” – is responsible for “establishing and enforcing Wells Fargo’s Risk Management Framework.”<sup>773</sup> It “oversees risk” and is “[a]ccountable to the Board, with day-to-day oversight” from the CEO.<sup>774</sup> It established and enforced risk management policies, standards, tools, methodologies and programs, provides oversight of risks across all businesses and functions, and performs “independent risk monitoring and reporting.”<sup>775</sup>

CRO Loughlin described the second line of defense in these terms:

Second line of defense: Corporate functions.

Corporate Risk, Human Resources, the Law Department, Social Responsibility, Public Relations, and Corporate Controllers provide company-wide leadership, standards, support, and oversight to ensure effective understanding and management of all risk, including associated strategic and reputation risks, across Wells Fargo.<sup>776</sup>

The Third Line of Defense – “Audit” or “Audit and Examination” – is responsible “for providing an independent assessment of the risk framework and internal control systems to the Board.”<sup>777</sup> It is accountable to the Board, with day-to-day oversight from the CEO.<sup>778</sup> The scope of Audit includes “[c]ompliance with policies and standards,” the “effectiveness of the independent risk management function,” and “[c]ompleteness and accuracy of information.”<sup>779</sup>

CRO Loughlin described the third line of defense in these terms:

Third line of defense: Wells Fargo Audit Services

[WFAS] is an independent assurance and advisory function that reports directly to the Audit & Examination (A&E) Committee of the Board of Directors. Through its assurance and advisory work, WFAS helps the company accomplish its objectives by bringing a systematic, disciplined

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<sup>772</sup> OCC Ex. 1553 at 7-8.

<sup>773</sup> R. Ex. 1780 at 41.

<sup>774</sup> *Id.*

<sup>775</sup> *Id.*

<sup>776</sup> OCC Ex. 1553 at 8.

<sup>777</sup> R. Ex. 1780 at 41.

<sup>778</sup> *Id.*

<sup>779</sup> *Id.*

approach to evaluate and improve the effectiveness of enterprise governance, risk management, and control processes across the enterprise.<sup>780</sup>

Mr. Julian testified that the Wells Fargo Community Bank LOB was one of the Bank's First Lines of Defense, and Paul McLinko was the head of the Audit Group that had responsibilities for providing audit oversight for that line of business.<sup>781</sup>

Mr. Julian described the Internal Audit function served by WFAS in these terms:

Principally, the role of Audit -- especially within an organization the size of Wells Fargo Corporation [*sic*], the role of Audit was to perform audit work to provide assurance to management and to the Board that the controls that management oversaw were, in fact, working as intended or as designed.<sup>782</sup>

Mr. Julian testified that the first line of defense (and not WFAS) was expected to design risk management controls for the Community Bank.<sup>783</sup> In this context, risk management controls "are intended to be designed to assure that the risks are being managed within the parameters of the risk appetite that the line of business has adopted."<sup>784</sup> Mr. Julian testified that the Community Bank, and not WFAS, was expected to set the "risk appetite" for the Community Bank line of business.<sup>785</sup>

### **Risk Appetite**

Risk appetite "means the aggregate level and types of risk the board of directors and management are willing to assume to achieve a covered bank's strategic objectives and business plan, consistent with applicable capital, liquidity, and other regulatory requirements."<sup>786</sup>

According to its Risk Management Framework, the holding company's Board of Directors and its seven standing committees "play an active role in overseeing and guiding the company's overall approach to risk management."<sup>787</sup> The Framework provides that a key component of this approach is its Statement of Risk Appetite, "which is developed and refined by senior management, with updates reviewed and approved at least annually by the Board."<sup>788</sup>

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<sup>780</sup> OCC Ex. 1553 at 8.

<sup>781</sup> Tr. (Julian) at 5988.

<sup>782</sup> Tr. (Julian) at 5936.

<sup>783</sup> Tr. (Julian) at 5937.

<sup>784</sup> Tr. (Julian) at 5938.

<sup>785</sup> Tr. (Julian) at 5938.

<sup>786</sup> OCC Ex. 931 at 114 (12 CFR Ch. 1, Pt. 30, App. D at I(E)(10)).

<sup>787</sup> Resp. Ex. 482, Wells Fargo & Company, Corporate Risk, Wells Fargo Risk Management Framework, Second Edition, published July 2014, at 12.

<sup>788</sup> *Id.*

The Framework provides thus with respect to risk appetite:

Generally, the statement of risk appetite serves to guide business and risk leaders as they manage risk on a daily basis. It describes the nature and magnitude of risks that the company is willing to assume in pursuit of its strategic objectives, and is composed of qualitative and quantitative parameters for certain individual risk types (*e.g.* financial, capital, liquidity, credit, counterparty, market, model, operational, compliance, reputational). It also contains specific financial ranges which the company does not want to exceed or fall below over time (*e.g.*, ROE, ROA, efficiency ratio). Moreover, the enterprise statement of risk appetite informs individual legal entity, group, and in some cases LOB-specific statements of risk appetite, which the company has developed for its five risk-generating groups and Wells Fargo Bank, N.A., the company's principle banking subsidiary. The metrics included in the group and legal entity statements are harmonized with the enterprise level metrics to ensure consistency, where appropriate.<sup>789</sup>

Mr. Julian testified, "risk appetite" is "a level of risk that the line of business is willing to accept and the level of risk which they're expected to build controls to mitigate down to."<sup>790</sup> He testified that although the "lines of business were responsible for developing risk appetite metrics," by as late as April 2015 he was aware that the Community Bank had not set a risk appetite.<sup>791</sup>

Through the OCC's Supervisory Letter WFC 2015-07, the OCC directed Carrie Tolstedt, Senior Executive Vice President for Community Banking to "establish risk appetite metrics specific to monitoring the sales practices activities as well as appropriately reporting and escalating as needed."<sup>792</sup> Mr. Julian reiterated that WFAS played no role in setting the risk appetite for the Community Bank.<sup>793</sup> Elaborating on this point, Mr. Julian testified that "[i]t would be inappropriate for WFAS to set the appetite, because WFAS was providing audit work and testing the controls against such appetite".<sup>794</sup>

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<sup>789</sup> *Id.*

<sup>790</sup> Tr. (Julian) at 5945.

<sup>791</sup> Tr. (Julian) at 6643-44; R. Ex. 654 at 3.

<sup>792</sup> Tr. (Julian) at 6644.

<sup>793</sup> Tr. (Julian) at 5943-44, citing R. Ex. 482, Wells Fargo & Company, Corporate Risk, Wells Fargo Risk Management Framework, Second Edition, published July 2014: "The Board is also responsible for the oversight of Wells Fargo's risk management organization. In this capacity, the Board oversees senior management's efforts to ensure that the risk management organization and Wells Fargo Audit Services are adequately staffed and maintain the appropriate stature within the company. Accordingly, the Board reviews senior management reports on staffing levels and expertise in these areas and requires that both the CRO and Chief Auditor report directly to Board-level committees." *Id.* at 13.

<sup>794</sup> Tr. (Julian) at 5938.

Risk appetite for the Community Bank was supposed to be set by the line of business – in this case, by Carrie Tolstedt for the Community Bank’s First Line of Defense.<sup>795</sup> While WFAS would not set Community Bank’s risk appetite, it was responsible for “the testing of the controls and the testing of the risks that are being managed,” and would “evaluate the effectiveness of those controls against the stated risk appetite of the line of business.”<sup>796</sup>

Mr. Julian testified that it would be inappropriate for WFAS to *design* the internal controls for the Community Bank: “[O]ne of the critical aspects of Wells Fargo Audit Services’ role and the audit profession in general is that of independence and objectivity. And it would not have been appropriate for Audit to design controls that they would then turn it around in testing compliance with and the effectiveness of them.”<sup>797</sup>

Similarly, Mr. Julian stated that WFAS was not responsible for developing or implementing enterprise-wide risk management frameworks across the Bank’s several lines of business.<sup>798</sup> According to Mr. Julian, the responsibility for such framework during the relevant period was with Mike Loughlin as head of Corporate Risk within the Second Line of Defense.<sup>799</sup>

Mr. Julian testified during his direct examination that having attended Board meetings, he was qualified to opine that members of the holding company’s Board of Directors were “aware of the overall risk appetites. Risk appetite would have been a discussion at various times with the Board with management as the management of risk was being discussed.”<sup>800</sup> Offering no evidence to support the factual claim, Mr. Julian testified further that it “would not have been the norm” for a specific risk appetite to be defined for a particular activity like sales practices.<sup>801</sup>

Elaborating on this answer but without offering any evidence establishing the existence of such a norm, Mr. Julian stated, “Well, risk appetite statements or metrics were really done at a higher level with respect to broader risks. This is requiring the line of business to set a risk appetite level at a specific risk-type activity, which is just not the norm within the risk appetite framework at the time.”<sup>802</sup>

## **Professional Standards: Comptroller’s Handbook**

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<sup>795</sup> Tr. (Julian) at 5944, 5959, citing Resp. Exhibit 482 (Wells Fargo & Company, Corporate Risk, Wells Fargo Risk Management Framework), at 24 - Organizational Structure of the First Line of Defense.

<sup>796</sup> Tr. (Julian) at 5944.

<sup>797</sup> Tr. (Julian) at 5938-39.

<sup>798</sup> Tr. (Julian) at 5960.

<sup>799</sup> Tr. (Julian) at 5960.

<sup>800</sup> Tr. (Julian) at 5958-59.

<sup>801</sup> Tr. (Julian) at 6644.

<sup>802</sup> Tr. (Julian) at 6645.

Identifying one source of authority relevant to the work of WFAS's Internal Audit group, Mr. Julian cited the April 2013 version of the Comptroller's Handbook.<sup>803</sup> The Handbook includes a section on "Independence and Competence"<sup>804</sup> that according to Mr. Julian makes clear that "Internal Auditors must be independent of the activities that they audit so that they can carry out the work freely and objectively."<sup>805</sup>

More completely stated the Handbook provides the following on the point Mr. Julian testified to:

Internal auditors must be independent of the activities they audit so that they can carry out their work freely and objectively. They must render impartial and unbiased judgments. The internal auditor or the manager (director) of internal audit should report directly and regularly to the board of directors. In some banks, the internal audit function may be part of a group that manages or controls the bank's overall risk-taking activities. This arrangement may be satisfactory as long as the audit function functionally reports directly to the board and retains its independence. If the internal audit manager reports to a senior executive on day-to-day administrative issues, the board must take extra measures to ensure that the relationship does not impair the auditor's independence or unduly influence the auditor's work.

The board is responsible for delegating the authority necessary to effectively allow internal auditors to perform their job. Auditors must have the power to act on their own initiative in all departments, divisions, and functions in the bank; to communicate directly with any bank personnel; and to gain access to all records, files or data necessary for the proper conduct of the audit. Clear communication between the board, the internal auditors, and management is critical to timely identification and correction of weaknesses in internal controls and operations.<sup>806</sup>

Mr. Julian referred to provisions in the Comptroller's Handbook pertaining to "Safety and Soundness" related to internal and external audits.<sup>807</sup> He cited this authority in support of the proposition that it would not have been appropriate for Internal Audit to design internal controls

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<sup>803</sup> Tr. (Julian) at 5939, citing OCC Exhibit 1909, Comptroller's Handbook, Internal and External Audits, April 2003 at 25.

<sup>804</sup> Tr. (Julian) at 5939, citing OCC Exhibit 1909, Comptroller's Handbook, Internal and External Audits, April 2003 at 25.

<sup>805</sup> Tr. (Julian) at 5940, citing OCC Exhibit 1909, Comptroller's Handbook, Internal and External Audits, April 2003 at 25.

<sup>806</sup> OCC Exhibit 1909 at 25 (page 23 of the Comptroller's Handbook).

<sup>807</sup> Tr. (Julian) at 5940-41, citing Resp. Exhibit 18844, Comptroller's Handbook, Safety and Soundness, Internal and External Audits, Version 1.0, December 2016 (replaced by version 1.1 of the booklet of the same title published July 2019).

for the Community Bank line of business.<sup>808</sup> Relevant to this premise is the following language: “The internal audit function should not be involved in designing, selecting, implementing, or operating specific internal control measures.”<sup>809</sup>

Mr. Julian also supported this position by referring to provisions in the Comptroller’s Handbook related to Corporate and Risk Governance.<sup>810</sup> From this section, Mr. Julian posited that the OCC’s Handbook is “consistent that WFAS had no responsibilities and should have no responsibilities for implementing internal controls.”<sup>811</sup> According to Mr. Julian, the Corporate and Risk Governance section of the OCC’s Handbook places on Community Bank’s first line of defense, rather than the third line of defense, the responsibility for identifying, assessing, controlling and mitigating the risks associated with the Community Bank’s business activities consistent with the established risk appetite.<sup>812</sup>

### **Professional Standards: International Standards for the Professional Practice of Internal Auditing**

The Internal Audit Department under Mr. Julian recognized the definition of Internal Audit and adhered to the International Standards for the Professional Practice of Internal Auditing and the Code of Ethics of the Institute of Internal Auditors. Pursuant to the WFAS Audit Charter, the mission and purpose of Internal Audit was to serve as a provider of independent, objective assurance and consulting services delivered through a highly competent and diverse team.

Mr. Julian stated that the Institute of Internal Auditors (IIA) is “a governing body that develops and issues standards by which the audit professional must . . . adhere to.”<sup>813</sup> He referred to the IIA standards in support of the premise that as one of the Bank’s several lines of business, Community Bank – and not WFAS – was responsible to set risk appetite levels for the Community Bank.<sup>814</sup> Similarly, he testified that Community Bank and not WFAS was responsible for implementing internal controls: “It was critical that [WFAS] remained independent and ‘independent’ meaning the ability to assess and be objective on its – performing

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<sup>808</sup> Tr. (Julian) at 5941-42.

<sup>809</sup> Resp. Exhibit 18844, Comptroller’s Handbook, Safety and Soundness, Internal and External Audits, Version 1.0, December 2016, at 36 (page 34 of the Handbook).

<sup>810</sup> Tr. (Julian) at 5955, citing Resp. Exhibit 705, Comptroller’s Handbook, Safety and Soundness, Corporate and Risk Governance, version 1.0, July 2016 (replaced by version 2.0 of the booklet of the same title published July 2019).

<sup>811</sup> Tr. (Julian) at 5955.

<sup>812</sup> Tr. (Julian) at 5955-56.

<sup>813</sup> Tr. (Julian) at 5946.

<sup>814</sup> Tr. (Julian) at 5946, citing Resp. Ex. 533, International Standards for the Professional Practice of Internal Auditing (Standards) at 12 (page 9 of the Standards).

its work.”<sup>815</sup> He averred that under the IIA Standards, WFAS “couldn’t have then designed those controls or implemented those controls. It would have been inappropriate.”<sup>816</sup> He testified that the Community Bank’s first line of defense, rather than WFAS, “owned the management of the risks” and thus was responsible for designing and implementing those controls.<sup>817</sup>

Mr. Julian cited the IIA Standards for the proposition that while internal auditors “must apply care and the skill expected of a reasonably prudent and competent internal auditor . . . that professional care doesn’t imply that the work of internal audit will catch every instance of, say, control breakdown or a risk issue.”<sup>818</sup>

Similarly, Mr. Julian cited the IIA Standards regarding Due Professional Care for the proposition that internal auditors must “have an understanding of the significant risks that might affect the work being performed and the controls being tested,” but that even when performed appropriately or with due professional care, there are “possibilities that issues won’t be identified.”<sup>819</sup>

### ***IIA Standards – Engagement Supervision and Business Monitoring***

Under WFAS’s Charter, business monitoring was expected to be a vital part of the ongoing risk identification activity. Such monitoring was supposed to include continuous risk assessments, analyses of business reporting and metrics, and issue follow-up. It also was expected to include a call-awareness program from a variety of internal and external sources to keep apprised of new and emerging risks. Documentation was required for all forms of business monitoring.

During direct examination, Mr. Julian testified that an “audit engagement” generally “is where an audit group would identify a set of controls that they would scope in to be tested and then execute those controls and execute the testing of those controls and provide an opinion based on their findings.”<sup>820</sup> He added that an audit engagement “can also reflect other activities that audit would have performed, be it specific project-related, business monitoring where it was a formal business monitoring engagement.”<sup>821</sup>

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<sup>815</sup> Tr. (Julian) at 5947.

<sup>816</sup> Tr. (Julian) at 5947.

<sup>817</sup> Tr. (Julian) at 5947.

<sup>818</sup> Tr. (Julian) at 5951, citing Resp. Ex. 533, International Standards for the Professional Practice of Internal Auditing (Standards) at 9 (page 6 of the Standards).

<sup>819</sup> Tr. (Julian) at 5952, citing Resp. Ex. 533, International Standards for the Professional Practice of Internal Auditing (Standards) at 9 (page 6 of the Standards), which states: “1220.A3 Internal auditors must be alert to the significant risk that might affect objectives, operations, or resources. However, assurance procedures alone, even when performed with due professional care, do not guarantee that all significant risks will be identified.”

<sup>820</sup> Tr. (Julian) at 5982.

<sup>821</sup> Tr. (Julian) at 5982.



Mr. McLinko testified that he was aware of independent assessments being made to determine whether WFAS conformed to applicable professional standards, although he did not identify who or what made those assessments.<sup>822</sup> Through leading questioning by his Counsel during direct examination, Mr. McLinko testified that he was also aware that he and the CBO team were subject to internal assessments by the Quality Assurance Audit Team at WFAS.<sup>823</sup>

Again without identifying the source of the assessment, Mr. McLinko testified that “the external exams were done by an independent accounting firm, if I recall, that came in following the guidelines for external assessments to review the audit work that was performed by WFAS, which my team was part of.”<sup>824</sup> He testified that the external assessors “would come in and select workpapers and have quite an extensive deep dive into the workpapers and working with the Senior Audit Managers.”<sup>825</sup> He said he believed WFAS attained “the highest rating” and that this, “gave me some comfort.”<sup>826</sup>

Referring specifically to Senior Audit Manager Bart Deese, Mr. McLinko testified Mr. Deese, “was one of the most professional auditors that you can ever deal with. He had CPA credentials. He had extensive experience in audit . . . provided training, things along those lines. So he was highly competent.”<sup>827</sup>

### **Risks Associated with Sales Practices Misconduct**

Mr. Julian testified that the risks associated with sales practices misconduct were not limited to the Community Bank.<sup>828</sup> He explained, “sales practices activities or the risk of sales practices activities also has the potential or the risk across other lines of business groups outside the Community Bank business group.”<sup>829</sup>

Mr. Julian said his role as Chief Auditor during the relevant time was to engage with EADs (including Mr. McLinko) “over the various lines of business to understand the engagement that they were performing with respect to sales practices”.<sup>830</sup> His reason for doing so was that he needed to “have an understanding and a level of assurance that they were aware of the sales practice risk”.<sup>831</sup> With that understanding, Mr. Julian said he expected the EADs to

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<sup>822</sup> Tr. (McLinko) at 8430.

<sup>823</sup> Tr. (McLinko) at 8431.

<sup>824</sup> Tr. (McLinko) at 8432.

<sup>825</sup> Tr. (McLinko) at 8432.

<sup>826</sup> Tr. (McLinko) at 8432.

<sup>827</sup> Tr. (McLinko) at 8434.

<sup>828</sup> Tr. (Julian) at 5989.

<sup>829</sup> Tr. (Julian) at 5989.

<sup>830</sup> Tr. (Julian) at 5990.

<sup>831</sup> Tr. (Julian) at 5990.

incorporate that risk “into their various audit plans.”<sup>832</sup> He added, however, that during the relevant period, none of the EADs personally executed any audit engagements.<sup>833</sup>

### **The Role of the Audit Plan**

In this context, the Audit Plan “lays out specifically how Audit would be allocating its resources, where Audit would be spending its time, what significant risks Audit would be focused on and factored into the development of that Plan.”<sup>834</sup> As Chief Auditor, Mr. Julian testified that he had the responsibility to assure the Bank that “Audit had a reliable approach for developing an Audit Plan,” using a “reliable methodology.”<sup>835</sup> Further, he stated he needed to understand “that methodology and that it was being applied.”<sup>836</sup>

Mr. Julian explained that an Audit Plan would be developed once a year for the upcoming year.<sup>837</sup> He added that during his tenure WFAS employed a “dynamic audit approach,” and elaborated thus:

Formally, an Audit Plan was developed once a year for that upcoming year. However, the Audit Plan throughout the year, we employed what I implemented early on in my tenure as a dynamic audit approach. Which meant that, while we were responsible for executing the Audit Plan that the audit committee of Wells Fargo Corporation approved, we were also -- it was important to make sure that we assessed that Audit Plan throughout the year based on any emerging risks or any other relevant information that should be taken into account in determining should we continue with that portion of an Audit Plan. For instance, should we execute a certain audit? If certain changes occurred, did it make sense to execute that audit? So it was dynamic, but the formal plan was developed once a year.<sup>838</sup>

Throughout the relevant period, WFAS employed a dynamic audit program in order to accomplish its mission. Under its Charter, WFAS was expected to assure that the Board’s governance system had been adequately designed and was in compliance with all regulatory requirements. This included assuring that the Board adhered to key governance documents and was receiving appropriate, accurate, and timely information.

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<sup>832</sup> Tr. (Julian) at 5990.

<sup>833</sup> Tr. (Julian) at 5990.

<sup>834</sup> Tr. (Julian) at 5994.

<sup>835</sup> Tr. (Julian) at 5995.

<sup>836</sup> Tr. (Julian) at 5995.

<sup>837</sup> Tr. (Julian) at 5996.

<sup>838</sup> Tr. (Julian) at 5996.

Mr. Julian described the “dynamic” approach began only after he became Chief Auditor – that the prior Chief Auditor “was very focused on executing the Audit Plan as it was designed,” but that it was Mr. Julian’s impression in 2013 that a dynamic approach was warranted.<sup>839</sup>

As I came in, I observed that the Audit Plan, for instance, for 2013, let's say, would have been developed as early as October-November of 2012. Well, if work's going on late in 2013, work's being performed based on risks that were assessed as much as 12 months prior. Risks change. The company organizations change. The businesses change. So it didn't make sense to me to audit what I thought of as a stagnant audit plan but, rather, felt it was important that it was dynamic and took into account changes that were important to consider.<sup>840</sup>

He said that he “had ongoing dialogues while the Plan was being developed.”<sup>841</sup> Without offering any documentary evidence to identify such dialogues, Mr. Julian averred the process of developing the Plan was “probably a three- to four-month process” for the upcoming year; and that during this period he would have “various dialogues, both individually with the EADs specific to their Audit Plan and to understand where their primary focus was going to be.”<sup>842</sup>

According to Mr. Julian, the process of developing the Bank’s Audit Plan consisted of “two primary streams being worked.”<sup>843</sup> One stream called for the audit group’s Chief Operating Officer to “look at prior audits that had been performed around controls,” and then look “at our cyclical basis to ensure that the upcoming Audit Plan scoped in those audits of those controls and processes that were due to be tested based on the risk assessment of those.”<sup>844</sup>

The second “stream” happened while the first stream was taking place.<sup>845</sup> Through this process, “the individual Audit Groups were performing bottom-up risk assessments of all of the processes within . . . their specific audit line of business group[s]”.<sup>846</sup> He said these assessments were to assess “the risk relevant to the processes and the businesses within their purview to determine whether the risks have increased, decreased, so forth, so that those risk assessments could be utilized in the cyclical audit approach.”<sup>847</sup>

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<sup>839</sup> Tr. (Julian) at 5997.

<sup>840</sup> Tr. (Julian) at 5997-98; see also, “22-03-07 Respondents’ Amended Revised Errata Days 9 -38” at page 39. Ordered through Second Supplemental Order Regarding Hearing Transcript Errata.

<sup>841</sup> Tr. (Julian) at 5995.

<sup>842</sup> Tr. (Julian) at 5995.

<sup>843</sup> Tr. (Julian) at 5998.

<sup>844</sup> Tr. (Julian) at 5998.

<sup>845</sup> Tr. (Julian) at 5998.

<sup>846</sup> Tr. (Julian) at 5998-99.

<sup>847</sup> Tr. (Julian) at 5999.

## **Nature of the Relationship between Audit (the Third Line of Defense) and Risk Management (the Second Line of Defense)**

Mr. McLinko identified an “Issue and Recommendation Memo” prepared by Regina McCadney, a Senior Audit Manager in the Community Banking & Operations Group (CBO) of WFAS, a direct report of Mr. McLinko and a group Mr. McLinko directed as part of the Bank’s Third Line of Defense.<sup>848</sup> The Memo was addressed to Katherine Noakes, Operational Risk Consultant, RBCOR, and the subject was “[Regional Banking] Account Opening (150618)”.<sup>849</sup>

The Regional Banking Compliance and Operational Risk (RBCOR) group is part of the Bank’s Second Line of Defense and provides oversight of the Fraud Risk Management Program (FRMP).<sup>850</sup> The objective of the Program is to ensure controls are in place to detect and prevent fraud in connection with opening accounts or servicing/maintenance of existing accounts.<sup>851</sup> The Program defines roles and responsibilities, document Regional Banking’s (RB) approach to fraud risk management, and outlines fraud-reporting requirements to meet the objectives.<sup>852</sup>

RBCOR is responsible for understanding its internal and external fraud risks and maintaining a FRMP to address these risks and ensure compliance with Corporate Fraud policy.<sup>853</sup> The RB Fraud Risk Management Program applies to all Regional Banking business units, including Community Banking.<sup>854</sup> It also includes Business Banking areas involved in deposit and credit activities, to include account opening, account servicing or maintenance, and service provider/contractor relationships of the businesses.<sup>855</sup>

Through leading questioning by his Counsel during direct examination, Mr. McLinko testified that the distribution of the draft Memo was an example of the process where WFAS would share draft Issues and Recommendations (I&R) memos with the line of business being audited to make sure WFAS had the facts right.<sup>856</sup>

Through this I&R Memo, Senior Audit Manager McCadney, along with an Audit Manager and an Audit Leader under Mr. McLinko’s direction, described two issues which

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<sup>848</sup> Tr. (McLinko) at 8400; R. Ex. 11812 (Memo) and R. Ex. 11811 (1/26/16 transmittal email from Regina McGriff (McCadney) to PM).

<sup>849</sup> R. Ex. 11812 at 1.

<sup>850</sup> R. Ex. 1459 at 2.

<sup>851</sup> *Id.*

<sup>852</sup> *Id.*

<sup>853</sup> *Id.*

<sup>854</sup> *Id.*

<sup>855</sup> *Id.*

<sup>856</sup> Tr. (McLinko) at 8402.

required the attention of Ms. Noakes and RBCOR.<sup>857</sup> The issues both were rated “Moderate”.<sup>858</sup> First, under the heading, “Enforce Quality Customer Override Approval Requirements”, the I&R described the issue in these terms:

### **Issue**

Before opening a customer deposit account, the individual(s) with transaction authority must be risk screened using the Qualify Customer Process on Store Vision Platform (SVP). The Qualify Customer Process consists of DDA history and fraud screening, credit bureau risk screening, and internal Wells [Fargo] Bank screening.

If a negative Quality Customer response is returned, the new account or relationship maintenance request must be denied, with the exception of a new opportunity account which may be opened if the customer is eligible for an Opportunity Account.

A new, non-Opportunity account may be opened with negative Qualify Customer results if approval is obtained from a Business Banking Manager or from one level or more above a Store Manager. The approval must be documented by the addition of a permanent remark that includes an approval reason and the approver’s name. The approval is documented in the Hogan ACRM screen.

Qualify Customer overrides are recorded in the Consumer DDA Overrides Account Summary Report maintained on Distribution Strategies and Services Group’s Minding the Store (MTS) website. The report information page states that Management should review the report to ensure approvals are document on ACRM.

WFAS selected a sample of 46 Qualify Customer overrides from the reports to verify the approval was documented on the ACRM screen and included a permanent remark with approval reason and approver’s name.

In 11 of the first 20 (55%) sampled customers with risk screen overrides, no management approval was documented in the Hogan ACRM screen. Due to the rate of exceptions, WFAS stopped testing at 20 samples, rather than reviewing the entire sample of 46.

Management was not reviewing the report to confirm appropriate approvals and documentation. Additionally, some Bankers were not aware of, or did not understand, the override approval procedures.<sup>859</sup>

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<sup>857</sup> R. Ex. 11812 at 1.

<sup>858</sup> *Id.*

<sup>859</sup> *Id.* at 1-2.

The “Issue” thus first identified Bank policies relevant to the process being audited, then described how the auditors sought to verify team member compliance with those policies; and when it became clear that a significant number of examples revealed noncompliance with those policies the auditor stopped gathering data and made very direct findings regarding management’s noncompliance.

By providing a draft of the Memo to the subject of the audit, CBO auditors thus provided the line of business with a timely opportunity to correct any misstatements of fact in the Memo. Through leading questioning by his Counsel during direct examination, Mr. McLinko testified that the Line of Business could provide feedback that supports changes to the draft I&R – but that this does not mean the audit is not independent.<sup>860</sup>

The I&R had six other components for each Issue: the auditor provided a “Root Cause” finding (here the root cause was describe thus: “Override procedures were not consistently communicated to Bankers. Bankers [may be] disregarding the risk screen message because they are motivated to open accounts in order to meet their sales goals.”).<sup>861</sup>

The auditor then described the “Risk” associated with the issue. In this case, the auditor wrote: “Failure to obtain approvals before opening an account for a customer with a negative Qualify Customer leads to an increased number of poor quality accounts resulting in financial losses.”<sup>862</sup>

The auditor then provided a “Recommendation” (here: “Modify SVP to require Qualify Customer overrides to be approved and documented within SVP. In the interim, require Management to certify that they have reviewed the Consumer DDA Overrides Account Summary Report.”)<sup>863</sup>

The I&R then had a space for “Management Response”, “Responsible Person”, and “Expected completion date”.<sup>864</sup>

The same format was used for the second “Issue” – “Follow up with Customers who have Unfunded Accounts”.<sup>865</sup> Summarized, the issue addressed the auditor’s concern about customers who have “provided all necessary information and signed all required documentation to obtain an account with Wells Fargo but have not yet deposited the minimum funds required for their

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<sup>860</sup> Tr. (McLinko) at 8404.

<sup>861</sup> R. Ex. 11812 at 2.

<sup>862</sup> *Id.*

<sup>863</sup> *Id.*

<sup>864</sup> *Id.*

<sup>865</sup> *Id.* at 2-4.

account.”<sup>866</sup> The auditors noted that if the minimum deposit amount is not obtained, “the account is ultimately closed” at least 60 days after account opening.<sup>867</sup>

The auditors noted that the Rolling Funding Rate (RFR) report “provides information about customers who have not funded new accounts” but found that the information on the RFR “is not used to perform follow up. No effort is made to follow up with the customer to obtain the minimum funding amount.”<sup>868</sup>

The auditors reported, “Bankers receive incentives when they provide a customer with a product/solution. Bankers are credited with a solution even if the account is not funded.”<sup>869</sup>

The “Risk” reported by the auditors was this:

Closure of accounts because minimum funding requirements were not met results in a loss of potential revenue and does not support corporate priorities related to growing revenue and reducing expenses. The current incentive structure may result in a negative impact on customer experience and Wells Fargo’s reputation.<sup>870</sup>

The “Root Cause” for this risk was: “Crediting Bankers for opening unfunded accounts limits the motivation to follow-up with the potential customer and obtain the minimum funding amount.”<sup>871</sup>

The auditors recommended, “Credit the Banker for a solution only when the deposit account product meets the minimum funding requirements. Follow up with a customer to obtain minimum funding or confirmation that they do not want the product.”<sup>872</sup>

Following the issuance of the final Issue and Recommendation Memo, the audited party is required to provide a written response to each issue by a date set forth in the Memo.<sup>873</sup> Here too, the response is subject to a specific protocol expressed directly in the Memo.

According to the Memo, the response should:

1. Be specific and responsive to the entire issue,
2. Be complete in addressing all material aspects of the reported issue,
3. Include reasonable and achievable target dates for the completion of each corrective action,

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<sup>866</sup> *Id.* at 3.

<sup>867</sup> *Id.*

<sup>868</sup> *Id.*

<sup>869</sup> *Id.*

<sup>870</sup> *Id.*

<sup>871</sup> *Id.*

<sup>872</sup> *Id.*

<sup>873</sup> *Id.* at 1.

4. Include achievable actions that will prevent a recurrence of the generic control issue and also document any actions to address the specific exceptions identified during testing, and include designated individuals to “own” the corrective actions.<sup>874</sup>

Through this interaction, the auditors, as the Bank’s Third Line of Defense, examine activities – in this case, actions of RBCOR in the Second Line of Defense – and exercise independent judgment to guard against noncompliance with Bank policies. This constitutes the “credible challenge” needed for the Third Line of Defense to guide actors in the Second Line of Defense, as they monitor the actions of team member Bankers in the First Line of Defense.

Mr. McLinko also identified a draft March 2016 Audit Engagement Report, citing WFAS Audit #150618 and rating Community Banking – Regional Banking “Effective”.<sup>875</sup> Notwithstanding the two issues reported in the I&R related to WFAS Audit #150618, the Audit Engagement Report “reflects our opinion that the Originate and Set Up Account and User Access processes and controls are effective to manage corresponding risks.”<sup>876</sup> Under the draft Audit Engagement Report, the recommended “Corrective Actions” were to “Eliminate the Risk Screen Override Approval Documentation Requirement”.<sup>877</sup> The following rationale was provided in support of this recommendation:

Risk screen overrides are monitored as an Enterprise Key Indicator (EKI) and all groups and super groups are under threshold. This represents monitoring of appropriate risk screening. As the requirement for adding approval comments to the Hogan ACRM screen is a perceived control and does not equate to less risk we will make changes to elevate the monitoring. Each manager will be required to review and certify the risk screen override reporting monthly and document trends noted with their store control tasks.<sup>878</sup>

Although the WFAS I&R for Audit #150618 addressed two issues (management’s noncompliance with the customer override approval requirements and the need for follow up with customers who have unfunded accounts), the draft Audit Engagement Report concerning this Audit addressed only the former issue, deleting findings regarding customers who have unfunded accounts.<sup>879</sup> Although he admitted receiving the I&R and both draft Audit Engagement

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<sup>874</sup> R. Ex. 11812 at 1.

<sup>875</sup> Tr. (McLinko) at 8405, 8413; R. Ex. 12065 (Audit Engagement Report) and R. Ex. 12064 (2/29/16 transmittal email from Regina McGriff, SAM – Community Banking and Operations – to PM).

<sup>876</sup> R. Ex. 12065 at 2.

<sup>877</sup> *Id.* at 4.

<sup>878</sup> *Id.*

<sup>879</sup> R. Ex. 11812 *cf.* R. Ex. 12065 and R. Ex. 12067.



Reports, Mr. McLinko expressed no concern that there was only one issue reported in the Reports, testifying that “No one brought it up to me.”<sup>880</sup>

One of the purposes of an evidentiary hearing is to “enable the finder of fact to evaluate the credibility of witnesses by seeing ‘the witness's physical reactions to questions, to assess the witness's demeanor, and to hear the tone of the witness's voice’”.<sup>881</sup> Further, “factors other than demeanor and inflection go into the decision whether or not to believe a witness. Documents or objective evidence may contradict the witness’ story; or the story itself may be so internally inconsistent or implausible on its face that a reasonable factfinder would not credit it.”<sup>882</sup>

Factors for assessing the credibility of a witness include (1) the opportunity and ability of the witness to see or hear or know the things testified to; (2) the witness's memory; (3) the witness's manner while testifying; (4) the witness's interest in the outcome of the case, if any; (5) the witness's bias or prejudice, if any; (6) whether other evidence contradicted the witness's testimony; (7) the reasonableness of the witness's testimony in light of all the evidence; and (8) any other factors that bear on believability.<sup>883</sup>

Mr. McLinko denied that the removal of the issue meant that the scope of the audit was somehow narrowed retroactively; but then admitted to writing to Ms. Tolstedt that, reporting to her that given the pending LA County lawsuit, “we concentrated on the processes of setting up an account. We purposely stayed away from how the account was obtained.”<sup>884</sup>

The Community Bank and Operations Team Update he prepared and shared with the OCC acknowledged only one issue presented through the March 18, 2016 Engagement regarding Regional Banking Account Opening – and disclosed only “one moderate rated issue related to enforcing qualify customer override approval requirements.”<sup>885</sup>

Given this evidence, I give no weight to Mr. McLinko’s claim that no one brought to his attention the removal of one of the two issues addressed through Audit #150618, nor to his claim that the scope of the audit report was not narrowed retroactively. Both of his averments appear to be false statements and are contradicted by the preponderant weight of reliable evidence; and both statements erode the reliability and credibility of Mr. McLinko’s testimony regarding his

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<sup>880</sup> Tr. (McLinko) at 8417.

<sup>881</sup> *Vickers v. Smith*, No. 115CV00129SABPC, 2019 WL 1367784, at \*5 (E.D. Cal. Mar. 26, 2019) (quoting *United States v. Mejia*, 69 F.3d 309, 315 (9th Cir. 1995); *Conservation Cong. v. United States Forest Serv.*, No. CV 2:15-00249 WBS AC, 2016 WL 3126116, at \*5 (E.D. Cal. June 2, 2016) (evidentiary hearings “enable the court to listen to the witnesses’ testimony, observe their demeanor, assess their credibility, and resolve the disputed issues of fact regarding defendant's motivations based on the totality of the evidence”).

<sup>882</sup> *Anderson v. City of Bessemer City*, 470 U.S. 564, 575 (1985).

<sup>883</sup> *Cuevas Espinoza v. Hatton*, No. 10CV397-WQH-BGS, 2020 WL 434269, at \*32 (S.D. Cal. Jan. 28, 2020), citing Ninth Circuit Manual of Model Civil Jury Instructions 1.14 (2017 ed.).

<sup>884</sup> Tr. (McLinko) at 8419, 8423; OCC Ex. 1019 at 1.

<sup>885</sup> Tr. (McLinko) at 8425; R. Ex. 12934 at 6. See also OCC Ex. 697, WFAS Audit Engagement Report, RB Account Opening, March 18, 2016; and R. Ex. 382 (same document).

role in limiting the scope of audit findings presented through the Audit Engagement Report concerning Audit #150618.

Through leading questioning by his Counsel during direct examination, Mr. McLinko testified that it would not have concerned him if he knew at the time that the funding issue that was included in the draft I&R had been removed specifically from the final audit report.<sup>886</sup>

Elaborating on this answer, Mr. McLinko testified:

Again, the audit team responsible for this work are competent in what they do. They pass the I&Rs on to the business. The business will reply either with additional control information, whatever it may be. So if for some reason the audit team made the determination that it was no longer an issue and recommendation, I rely on the team.<sup>887</sup>

Knowing that the OCC had just issued five MRAs in the prior June, when asked how he could justify the “Effective” rating for this Audit Engagement Report from Audit #150618, Mr. McLinko responded:

One has to step back and look at what was the scope of this audit, which we talked about including those two processes that were included within the scope. The testing of the internal controls around the scope of the audit found that those controls were in place and operating effectively.<sup>888</sup>

Although Mr. McLinko testified that the CBO team under his direction shared the results of the Regional Banking Account Opening Audit with the OCC, the email transmittal copy does not reflect that an attachment accompanied the email.<sup>889</sup> Mr. McLinko testified that he attended the June 2016 meeting, that the PowerPoint deck referred to in the transmittal email was discussed, but acknowledged that he did not know specifically the OCC received a copy of the Audit Engagement Report from Audit #150618.<sup>890</sup> He denied, however, instructing anyone to not provide the OCC with the Report.<sup>891</sup>

### **Audit Plan Development and Evaluation**

Mr. Julian testified that under his leadership WFAS Internal Audit relied on a “Chief Operating Officer Group” within Audit that was responsible for “preparing all the reports, the

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<sup>886</sup> Tr. (McLinko) at 8418.

<sup>887</sup> Tr. (McLinko) at 8418.

<sup>888</sup> Tr. (McLinko) at 8419.

<sup>889</sup> Tr. (McLinko) at 8424; R. Ex. 12933 (transmittal dated 6/20/16 from Bartley Deese to Examiner Grover and others); R. Ex. 12934 (Community Bank and Operations Team Update, June 2016).

<sup>890</sup> Tr. (McLinko) at 8427.

<sup>891</sup> Tr. (McLinko) at 8428.

process of developing the [Audit] Plan, meaning pulling the Plan together.”<sup>892</sup> He said the Group also would review “each of the individual line of business Audit Group Plans . . . to assure that the plans took into account [that the] cyclical approach was in accordance with our methodology”.<sup>893</sup>

It is significant to note that under Mr. Julian’s leadership, one of the participants in the review conducted by the Chief Operating Officer Group was the business group of the Audit team for whom the Team was preparing the Audit Plan. Under this approach, “the Audit Leadership Group, typically the EAD of a specific audit group, would meet with the business head.”<sup>894</sup> In the case of the Community Bank line of business, this meant that a member of the Audit Leadership Group, typically the WFAS EAD assigned to audit the Community Bank, Mr. McLinko, would meet with Carrie Tolstedt, the head of the Community Bank, and Claudia Russ Anderson, the Community Bank’s Chief Risk Officer.<sup>895</sup>

During these meetings Mr. McLinko, would meet with Ms. Tolstedt and Ms. Russ Anderson, to “go through the [Plan], the draft Plan, to discuss what Audit identified as significant areas [they] felt ought to be included in the plan”.<sup>896</sup> Thus, there was an “ongoing dialogue” between the Third Line of Defense (WFAS), the Second Line of Defense (Ms. Russ Anderson), and the First Line of Defense (the Community Bank).<sup>897</sup> The stated purpose of this dialogue was to “get feedback from the business as to any aspects of the Plan that ought to be enhanced, changed, areas that ought to be looked at based on information that business knew.”<sup>898</sup>

Mr. Julian testified the “OCC folks who were assigned to the various audit groups would meet with the Audit Leadership team,” to review the draft Plan.<sup>899</sup> The purpose of these meetings was to share with the OCC “the areas of focus that Audit had identified as appropriate to include in the Plan”.<sup>900</sup> The dialogue also permitted the OCC to provide feedback “as to what, if any, information they have that they felt was relevant and should be incorporated into the Plan.”<sup>901</sup>

Mr. Julian testified that while the CBO audit team was putting together the Community Bank’s Audit Plan, “the respective leadership team within the Audit Group would meet with

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<sup>892</sup> Tr. (Julian) at 6005.

<sup>893</sup> Tr. (Julian) at 6005.

<sup>894</sup> Tr. (Julian) at 6006.

<sup>895</sup> Tr. (Julian) at 6006.

<sup>896</sup> Tr. (Julian) at 6006; see also “22-03-07 Respondents’ Amended Revised Errata Days 9 -38” at page 40. Ordered through Second Supplemental Order Regarding Hearing Transcript Errata.

<sup>897</sup> Tr. (Julian) at 6006.

<sup>898</sup> Tr. (Julian) at 6006.

<sup>899</sup> Tr. (Julian) at 6006.

<sup>900</sup> Tr. (Julian) at 6007.

<sup>901</sup> Tr. (Julian) at 6007.

their counterparts within the OCC to discuss the plan”.<sup>902</sup> He said this allowed the WFAS auditors to “inform the OCC as to what information the Audit Group felt relevant to include in the Plan, what work was going to be performed.”<sup>903</sup> It also allowed the OCC “to provide any feedback specific to any areas of concern or risks that the OCC felt that the Plan was not incorporating and perhaps should.”<sup>904</sup>

Unclear from the record is whether WFAS or Mr. Julian ever disclosed to the OCC the extent to which the First and Second Lines of Defense influenced what should have been the independent decisions of the Third Line of Defense in drawing up the Community Bank’s Audit Plan.

Mr. Julian denied, however, that there was anything inconsistent with applicable audit professional standards with respect to the meetings WFAS had with the First and Second Lines of Defense.<sup>905</sup> He said, “it was absolutely critical that Audit had the information available,” including information available from “the business unit who owned managing the risk within their business.”<sup>906</sup> Further, he could recall no instance where Internal Audit ever declined to do an audit because of some objection from the Community Bank with regard to sales practices.<sup>907</sup>

Mr. Julian opined that there could be valid business reasons for WFAS Internal Auditors adjusting an Audit Plan based on such a dialogue with the First or Second Line of Defense.<sup>908</sup> Asked what he would do if information came to him through such a dialogue, Mr. Julian responded thus:

I would have addressed it first with the Audit Leader to understand the perspective, to make sure I had the information. I would have then engaged in discussions with the business group to understand their perspectives. And unless there was a truly valid business reason for not performing that audit, I would have -- I would have declined their request and told Audit to engage in the work.<sup>909</sup>

#### **Relevant Features of the 2013 Audit Plan**<sup>910</sup>

The 2013 Audit Plan Mr. Julian presented to the A&E Committee addressed the expectation that WFAS would provide the “independent assurance function of the company” by

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<sup>902</sup> Tr. (Julian) at 6012.

<sup>903</sup> Tr. (Julian) at 6012.

<sup>904</sup> Tr. (Julian) at 6013.

<sup>905</sup> Tr. (Julian) at 6007.

<sup>906</sup> Tr. (Julian) at 6007-08.

<sup>907</sup> Tr. (Julian) at 6008.

<sup>908</sup> Tr. (Julian) at 6008.

<sup>909</sup> Tr. (Julian) at 6008.

<sup>910</sup> R. Ex. 3560.

developing a “coverage plan that provides an appropriate level of testing of core business processes over a four year coverage horizon.”<sup>911</sup> The Plan represented that it will “ensure coverage for the top enterprise risks,” and that other risks “will continue to be monitored throughout 2013 through business monitoring programs and dialogue with business partners.”<sup>912</sup> It reported that as “the risk profile changes or risks emerge, it may be necessary for us to gauge our need to be dynamic and adjust our intended approach and/or resources.”<sup>913</sup>

As a business partner, Internal Audit was required to help the Company accomplish its objectives by bringing a systematic disciplined approach to evaluate and improve the effectiveness of risk management, control, and governance processes.

The 2013 Audit Plan addressed leveraging by stating WFAS will “utilize our process-centric Audit Management Platform and enhanced reporting tools to more effectively link our audit activities, and the results thereof, to support strong conclusions regarding the overall process effectiveness.”<sup>914</sup> The Plan identified specifically leveraging “the Enterprise Risk Management Committee top enterprise risk summary and assessing our audit coverage.”<sup>915</sup>

The 2013 Audit Plan stated it would utilize “our ‘seat at the table’ to be aware of strategic initiatives and industry trends that our business partners are facing”.<sup>916</sup>

The 2013 Audit Plan identified Wholesale Banking and Consumer Lending as the top two Operating Committee Groups “from a resource priority standpoint,” and made no mention of the OGC related to the Community Bank line of business.<sup>917</sup> The Plan represented, however, that its “dynamic audit plan promotes shifting priorities in alignment with changing risk or risk management environment.”<sup>918</sup>

The 2013 Audit Plan represented WFAS had approximately 510 team members across North America, and that “we will have sufficient resources to complete the plan and an appropriate level of expertise and competency to meet our 2013 Audit Plan needs.”<sup>919</sup> It represented, however, that if “a need to supplement proficiency is noted in an area, we will take the appropriate steps to ensure this expertise is obtained.”<sup>920</sup>

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<sup>911</sup> R. Ex. 3560 at 4.

<sup>912</sup> *Id.*

<sup>913</sup> *Id.*

<sup>914</sup> *Id.*

<sup>915</sup> *Id.*

<sup>916</sup> *Id.* at 5.

<sup>917</sup> *Id.*

<sup>918</sup> *Id.*

<sup>919</sup> *Id.* at 5-6.

<sup>920</sup> *Id.* at 5-6.

The 2013 Audit Plan reiterated six core principles that inform the “rational approach” as they “manage risk real time,” including taking “only as much risk as is necessary to efficiently, effectively, and prudently serve our consumers, small business, commercial, and wealth customers.”<sup>921</sup>

The Plan expressly stated “[w]e do not offer products that do not serve our customers’ best interests or are not appropriate for their needs and circumstances.”<sup>922</sup> It expressly stated that under the Plan, “Our reputation is paramount” and “[w]e will not engage in activities or business practices that could cause permanent or irreparable damage to our reputation.”<sup>923</sup> It expressly provided that “[w]e are prepared to refrain from businesses and activities that do not conform to our risk principles and will give up market share rather than accept unsuitable risks (as we did when competitors were offering more exotic mortgages).”<sup>924</sup>

The 2013 Audit Plan provided that WFAS would “identify specific engagements for the Plan year, along with the quarter in which the engagement is projected to begin fieldwork.”<sup>925</sup> “Risks associated with each [risk-assessable business unit] process are evaluated semi-annually for changes in the RABU profile.”<sup>926</sup>

The 2013 Audit Plan provided for multiple engagement types, each with an “administrative checklist that describes the actions required to successfully perform the work.”<sup>927</sup> Mr. McLinko, as the Community Bank’s Executive Audit Director, was the head of Community Banking and Operations (CBO), the audit group assigned to the Community Bank line of business, and he reported directly to Mr. Julian.

Whether through control testing, project engagements, or business monitoring activities, WFAS and the CBO were required to provide assurance to the Wells Fargo & Company Board of Directors that the Community Bank’s management was addressing the risk issues and that Community Banking’s controls were working appropriately.

“Project engagements” are assurance audits “which focus on significant changes in the business environment.”<sup>928</sup> Such engagements are distinguished from control testing engagements “by their focus on design or evolution of the system of controls.”<sup>929</sup>

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<sup>921</sup> R. Ex. 3560 at 23.

<sup>922</sup> *Id.*

<sup>923</sup> *Id.*

<sup>924</sup> *Id.*

<sup>925</sup> *Id.* at 27.

<sup>926</sup> *Id.*

<sup>927</sup> *Id.* at 28.

<sup>928</sup> *Id.*

<sup>929</sup> *Id.*

“Control testing engagements” are assurance audits “which result in an objective and independent opinion of the adequacy of internal controls and the effectiveness of the primary control(s) designed to reduce risk of business processes to a prudent level.”<sup>930</sup>

“Business monitoring engagements” are a “collection of ongoing activities conducted to provide assurance coverage of business processes.” Such engagements include “continuous risk assessments as well as reviews of business metrics, monitoring of key risk/control indicators, and issue follow-up.”<sup>931</sup> Under the 2013 Audit Plan, WFAS “will report any negative conditions identified during a business monitoring engagement using its Issue & Corrective Action policy.”<sup>932</sup>

Under the 2013 Audit Plan’s Issue & Corrective Action policy, “the business partners are expected to provide a corrective action plan that addresses the identified risk or to formally assume the risk.”<sup>933</sup> If a business partner assumes the risk, “the rationale must be reviewed and approved by the appropriate Director and the condition is summarized for the A&E.”<sup>934</sup> High-risk issues “are validated within 90 days of completion of the business partner’s indicating it is resolved.”<sup>935</sup>

Under the 2013 Audit Plan, the Chief Auditor, “is accountable for the execution of audit work. Responsibility for the accuracy and completeness of audit work is delegated to the audit leadership, but cannot be delegated further.”<sup>936</sup> The Chief Auditor “delegates the responsibility for ensuring accuracy and completeness of each engagement report to the Director and SAM. This responsibility cannot be delegated further.”<sup>937</sup>

### **Presentation of the 2013 Audit Plan to the WF&C Audit and Examination Committee – February 26, 2013**

The Audit and Examination Committee of the Wells Fargo & Company Board of Directors met in San Francisco on February 26, 2013.<sup>938</sup> During the meeting, Mr. Julian presented his report in three stages: he provided an Internal Audit update, presented the 2013

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<sup>930</sup> *Id.*

<sup>931</sup> *Id.* at 29.

<sup>932</sup> *Id.*

<sup>933</sup> *Id.* at 31.

<sup>934</sup> *Id.*

<sup>935</sup> *Id.*

<sup>936</sup> *Id.* at 32.

<sup>937</sup> *Id.*

<sup>938</sup> R. Ex. 20591.

Audit Plan updated, and presented the WFAS Charter, including management's proposed amendments.<sup>939</sup>

According to the meeting minutes, Mr. Julian reported, "overall risk management, systems of controls, and governance processes are Generally Effective."<sup>940</sup>

The minutes reflect Mr. Julian reviewed recent guidance of the Federal Reserve Board regarding the "characteristics, governance and operational effectiveness of the internal audit function." The minutes state Mr. Julian "said the guidance includes prescriptive requirements regarding reporting to the Committee and requires audit coverage of high risk areas every 12-18 months."<sup>942</sup>

The minutes reflect that Mr. Julian "addressed staffing for WFAS and noted the high level of turnover" and the "potential impact the turnover could have on the ability of WFAS to execute the 2013 audit plan and the actions WFAS is taking to address the turnover and current shortfall in staffing."<sup>943</sup>

The minutes reflect that Mr. Julian's "chief operating officer" at WFAS, Elizabeth C. Laudun, "presented a report providing more detail to the Committee about the changes in the 2013 Audit Plan."<sup>944</sup> Specifically, the minutes reflect Ms. Laudun "explained that, although the fundamental testing of risks, processes and controls has not changed, the manner of defining the audit universe has become process-based rather than business-line based."<sup>945</sup> Further, "audit coverage would have to be adjusted due to the new regulatory guidance that high risk areas must be reviewed every 12-18 months."<sup>946</sup>

### **Publication of the L.A. Times Articles in 2013**

Mr. Julian testified that he was aware of the publication by the L.A. Times of articles concerning Wells Fargo sales practices in the Los Angeles and Orange County region.<sup>947</sup> In an email chain that began on October 3 and ended on October 4, 2013, Mr. Bacon alerted Mr. Julian

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<sup>939</sup> Tr. (Julian) at 6195; R. Ex. 20591 at 1-2.

<sup>940</sup> R. Ex. 20591 at 1.

<sup>941</sup> *Id.*

<sup>942</sup> *Id.* at 2.

<sup>943</sup> *Id.*

<sup>944</sup> Tr. (Julian) at 6196; R. Ex. 20591 at 2.

<sup>945</sup> R. Ex. 20591 at 2.

<sup>946</sup> *Id.*

<sup>947</sup> Tr. (Julian) at 6244-45.



and others, including Ms. Russ Anderson, that the newspaper had published an article (providing a copy of the same, dated October 3, 2013 by E. Scott Reckard) about Wells Fargo's termination of the employment of about 30 branch employees in the L.A. area "who tried to meet sales goals by opening accounts that were never used."<sup>948</sup>

The October 3, 2013 article quoted a Bank representative, Gary Kishner, as stating, "We found a breakdown in a small number of our team members" who were "trying to take shortcuts to meet sales goals".<sup>949</sup> "One of the fired employees said that in some cases signatures were forged and customers had accounts opened in their names without their knowledge."<sup>950</sup> "The employee, who spoke to The Times on condition of anonymity pending a meeting with an attorney, said the pressure to meet sales goals was intense at Wells Fargo. At times, managers required workers to stay late calling their friends and family members if they failed to open enough accounts during the day".<sup>951</sup>

In her response to Mr. Bacon's initial email, Respondent Russ Anderson asked Mr. Bacon to "give me some context. I wasn't aware of this situation."<sup>952</sup> In responding to Ms. Russ Anderson (copied later that day to Mr. Julian), Mr. Bacon wrote:

I am shocked that this is already out. I thought terms would occur today or next week. This is an interesting one – it started with RP running some reports with SQ and identifying they had a regional issue with simulated funding then it expanded into more. I believe they detected that TMs were falsifying the customers [*sic*] preferences, primarily putting in false phone numbers do [*sic*] they couldn't be contacted by [G]allop. I will get you more details shortly.<sup>953</sup>

In his forwarding of the email chain to Mr. Julian on October 4, 2013, Mr. Bacon wrote, "FYI only – big deal and very interesting article at bottom of chain."<sup>954</sup> Mr. Julian testified that his takeaway from reading the article and Mr. Bacon's email chain was that "essentially based on what I understood at this time, the controls identified the behavior. It's what prompted the investigations and ultimately resulted in terminations of team members for the wrongdoing. So my impression was that the controls were working to identify the behavior."<sup>955</sup>

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<sup>948</sup> R. Ex. 330 at 2.

<sup>949</sup> *Id.* at 3.

<sup>950</sup> *Id.*

<sup>951</sup> *Id.*

<sup>952</sup> *Id.* at 2.

<sup>953</sup> *Id.* at 1.

<sup>954</sup> *Id.*

<sup>955</sup> Tr. (Julian) at 6247-48.

Within the email chain, Mr. Bacon wrote to Justin Richards, with copies to Patrick Russ and Bart Deese, writing that a team member “went to media during the investigation.”<sup>956</sup> Mr. Bacon advised Mr. Richards to “keep this on the radar, since what we found in LA may be found elsewhere, so at some point we will be asking SQ to review other regions.”<sup>957</sup> Mr. Julian testified that from this he concluded that it had not yet been confirmed that the same kind of misconduct was happening at locations other than LA/OC, but that “it had potential to be outside of the L.A./Orange County region and at some point future work would be undertaken.”<sup>958</sup>

Asked what his reaction was to the article, Mr. Julian responded that his was “[o]ne of disappointment that it had been made public.”<sup>959</sup> Asked to elaborate, he testified, “nobody wants to read negative information about a company they work for. So, you know, you never want to read negative information.”<sup>960</sup> He added that nothing he read in this email chain led him to understand that Mr. Bacon was communicating that sales integrity violations or sales practices misconduct at the Community Bank was widespread.<sup>961</sup> Instead, Mr. Julian described the report as “isolated to a specific region within southern L.A., specifically Orange County.”<sup>962</sup> Taking that fact into account, “that didn’t leave me to believe that it was either systemic or widespread.”<sup>963</sup> He added that when the article came out, his reaction was to “take a pause and think about it, that ‘did we have an issue related to it?’ So it certainly provided me an opportunity to step back and think about the issue.”<sup>964</sup>

According to Mr. Julian, WF&C had a mechanism to escalate issues that received significant press attention to the Board of Directors.<sup>965</sup> He identified a weekly communications update communicated by Alex Ball, who was in the corporate communications administrative group.<sup>966</sup> According to Mr. Julian, the weekly update “would include information that corporate communications or management felt was important or useful to make sure that it was distributed amongst both the Board as well as the Operating Committee.”<sup>967</sup> This response made no reference

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<sup>956</sup> R. Ex. 330 at 1.

<sup>957</sup> *Id.*

<sup>958</sup> Tr. (Julian) at 6249.

<sup>959</sup> Tr. (Julian) at 6249.

<sup>960</sup> Tr. (Julian) at 6249.

<sup>961</sup> Tr. (Julian) at 6250.

<sup>962</sup> Tr. (Julian) at 6250.

<sup>963</sup> Tr. (Julian) at 6251.

<sup>964</sup> Tr. (Julian) at 6258.

<sup>965</sup> Tr. (Julian) at 6251.

<sup>966</sup> Tr. (Julian) at 6251; R. Ex. 4806.

<sup>967</sup> Tr. (Julian) at 6251.

to Mr. Julian's duty to escalate issues, including emerging issues, to the Board or its A&E committee.

Mr. Julian also described the role of Significant Investigation Notifications (SIN).<sup>968</sup> He described these as a formal notification that Corporate Investigations would use "to notify internally certain specific management of potential issues that they were investigating or had investigated."<sup>969</sup> He identified a SIN dated October 9, 2013 regarding a September 13, 2013 receipt by Corporate Investigations of an email referral from Sales Quality regarding allegations of "25 Team Members from various AU's located in Southern CA for possible Simulated Funding" and noting that further research "was conducted by Sales Quality that was requested by Regional President John Sotoodeh which identified 177 bankers for possible Simulated Funding at various AUs mostly in the San Fernando Valley."<sup>970</sup>

The report included the allegations that "Simulated Funding falsified entries were made to meet individual and store sales goals" and "phone number changes were made to avoid a negative rating from Gallup poll surveys."<sup>971</sup> Upon conducting 35 interviews the report found that "most confessed" to Simulated Funding and knew "their actions were against WFB policy" and occurred "to meet quarterly sales goals."<sup>972</sup>

The report noted:

A high number on [*sic*] phone number and preference changes were also identified by Sales Quality and additional research was requested by the LOB. Initial research discovered 9 stores that had over 100 telephone number changes for May-July. One store was identified to have over 1,000 phone number changes.<sup>973</sup>

Further, the report stated the team members were "[f]ollowing manager and/or prior manager's guidance", that they "learned from observing/talking to other team members", that they "had customer's [*sic*] fund accounts with a \$50 deposit and then withdraw from atm", and that they attempted to "contact customer with unfunded accounts but would resort to auto transfers w/o customer consent to meet goals timely".<sup>974</sup>

Investigators found that most of the interviewees confessed to changing phone numbers and preference changes to avoid negative surveys, and that they had "developed a signal to alert management on a possible negative customer experience", and "posted stickies on monitors with

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<sup>968</sup> Tr. (Julian) at 6259.

<sup>969</sup> Tr. (Julian) at 6259.

<sup>970</sup> Tr. (Julian) at 6259; R. Ex. 866 at 1.

<sup>971</sup> R. Ex. 866 at 2.

<sup>972</sup> *Id.*

<sup>973</sup> *Id.*

<sup>974</sup> *Id.* at 3.

customer's name/account number [and at the] end of [the] day management would collect stickies and change digits on phone number," with an average of 15-40 per day, and with new tellers being "coached to explain, if asked" (noting there was a "large population of agricultural workers that change phone numbers often").<sup>975</sup>

Findings reported in the SIN included that "Management instructed them that it was acceptable", "there was a big emphasis on obtaining a perfect score", "one bad score out of the five categories equaled a bad survey and he felt he would lose his job", "not obtaining perfect scores would mess with everyone's bonuses and recognition", "co-workers would know if someone received a bad score and would say things like you're messing with my money", members would "chang[e] the numbers trying to protect the branch", and "bad surveys equal a manager talking to you and sending you to training".<sup>976</sup>

One team member reported that he knew the conduct was wrong "but did not report it because he knew it would not be confidential."<sup>977</sup> Elaborating, the team member "explained that he reported policy issues to MSC who informed the branch that he reported issues [and he] felt betrayed and his trust was taken for granted."<sup>978</sup> The investigators emphasized, "we are now seeing a **pattern of denials despite the significant facts**".<sup>979</sup>

The investigation identified two store managers and one district manager as being implicated by the team members who were interviewed.<sup>980</sup>

Mr. Julian testified that the conduct described in the article did not threaten the Bank's safety or soundness – based first on the fact that it related to only "35 team members" – not a significant number "given the size of Wells Fargo."<sup>981</sup> Further, he said that the report was "specific to a specific region within Southern California, Orange County."<sup>982</sup> Further, he "knew from background of the article that it was the controls that identified the behavior, and it was self-identified by Wells Fargo, the behavior, and, therefore, it provide me some assurance that the controls were working appropriately."<sup>983</sup>

After describing the process in place for Corporate Investigations to notify relevant leaders in Audit if there were material issues or findings, Mr. Julian stated there were "also opportunities in various committee meetings that we've gone over where I participated with

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<sup>975</sup> R. Ex. 866 at 3.

<sup>976</sup> *Id.* at 4.

<sup>977</sup> *Id.* at 5.

<sup>978</sup> *Id.*

<sup>979</sup> *Id.*, emphasis *sic*.

<sup>980</sup> *Id.* at 4.

<sup>981</sup> Tr. (Julian) at 6256.

<sup>982</sup> Tr. (Julian) at 6256.

<sup>983</sup> Tr. (Julian) at 6256.

Michael Bacon where he could have raised any of those types of issues that he might have had.”<sup>984</sup>

Despite espousing these convictions regarding the import of the content of the two articles, Mr. Julian testified that he nevertheless participated in the Enterprise Risk Management Committee shortly after the first article’s publication and at that meeting raised the existence of this risk as a risk that the Committee should discuss and escalate to the Operating Committee and the Board of Directors.<sup>985</sup> He identified the minutes from the October 9, 2013 ERMC meeting, which he attended by telephone.<sup>986</sup> He testified that the Committee Chair, Mr. Loughlin, would “go one by one,” calling on “each of the members to provide their thoughts and engagement.”<sup>987</sup>

Despite the substantial information available to him, both through the email reports regarding sales practices misconduct and the public reports disseminated through the L.A. Times article, and despite testifying that he was not at all shy about raising issues on the phone during these meetings, according to the minutes of the October 9, 2013 ERMC meeting, Mr. Julian raised no issue concerning Community Bank or its sales practices misconduct during this meeting of the ERCM.<sup>988</sup> There was no evidence in the record indicating that Mr. McLinko escalated to Mr. Julian any issues presented by the October L.A. Times article.

The record reflects that indeed, there is no mention of the topic reportedly raised by Mr. Julian in the minutes of the October 9, 2013 meeting presented to the ERMC.<sup>989</sup> And there is no documentary evidence in the record – in the email chain, or in the meeting’s agenda or minutes – to support Mr. Julian’s claim that on October 9, 2013 he reported to Committee members that the Community Bank’s sales practices misconduct issue ought to be escalated from the ERMC.

The L.A. Times published a second article on December 21, 2013.<sup>990</sup> Through this article the reporter, E. Scott Reckard, presented the results of interviews he conducted with 28 former and seven current Wells Fargo employees, “who worked at bank branches in nine states, including California.”<sup>991</sup>

The lede for the article was “Wells Fargo branch manager Rita Murillo came to dread the phone calls.”<sup>992</sup> Mr. Reckard reported, “Regional bosses required hourly conferences on her Florida branch’s progress toward daily quotas for opening accounts and selling customers extras

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<sup>984</sup> Tr. (Julian) at 6257.

<sup>985</sup> Tr. (Julian) at 6261.

<sup>986</sup> Tr. (Julian) at 6274; R. Ex. 16271.

<sup>987</sup> Tr. (Julian) at 6275.

<sup>988</sup> R. Ex. 16271 at 3-4.

<sup>989</sup> *Id.*

<sup>990</sup> Tr. (Julian) at 6312, R. Ex. 5250.

<sup>991</sup> R. Ex. 5250 at 1.

<sup>992</sup> *Id.*

such as overdraft protection. Employees who lagged behind had to stay late and work weekends to meet goals, Murillo said.”<sup>993</sup> “Then came the threats: Anyone falling short after two months would be fired.”<sup>994</sup> Murillo reported that she resigned from her Wells Fargo branch in the Ft. Myers area in 2010, even though she had no other job and her husband wasn’t working at the time. The couple ended up losing their home. She told the Times: “It all seemed worth the chance and the risk, rather than to deal with the mental abuse. Just thinking about it gives me palpitations and a stomachache.”<sup>995</sup>

The reporter wrote:

Wells Fargo & Co. is the nation’s leader in selling add-on services to its customers. The giant San Francisco bank brags in earnings reports of its prowess in ‘cross-selling’ financial products such as checking and savings accounts, credit cards, mortgages and wealth management. In addition to generating fees and profits, those services keep customers tied to the bank and less likely to jump to competitors.<sup>996</sup>

The Times investigation found that the “relentless pressure to sell has battered employee morale and led to ethical breaches, customer complaints and labor lawsuits”.<sup>997</sup> It found that to meet quotas, “employees have opened unneeded accounts for customers, ordered credit cards without customers’ permission and forged client signatures on paperwork.”<sup>998</sup> A former business specialist said, “employees would open premium checking accounts for Latino immigrants, enabling them to send money across the border at no charge. Those accounts could be opened with just \$50, but customers were supposed to have at least \$25,000 on deposit within three months or pay a \$30 monthly charge.”<sup>999</sup>

One former business manager at a Canoga Park, California branch said, “managers there coached workers on how to inflate sales numbers.”<sup>1000</sup> He told the Times, “the manager would greet the staff each morning with a daily quota for products such as credit cards or direct-deposit accounts. To fail meant staying after hours, begging friends and family to sign up for services”.<sup>1001</sup> He told the Times his manager “would say: ‘I don’t care how you do it – but do it,

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<sup>993</sup> R. Ex. 5250 at 1.

<sup>994</sup> *Id.*

<sup>995</sup> *Id.* at 3.

<sup>996</sup> *Id.* at 1.

<sup>997</sup> *Id.*

<sup>998</sup> *Id.*

<sup>999</sup> *Id.* at 4.

<sup>1000</sup> *Id.* at 1.

<sup>1001</sup> *Id.* at 4.

or else you're not going home.”<sup>1002</sup> He said branch and district managers “told him to falsify the phone numbers of angry customers so they couldn't be reached for the bank's satisfaction surveys.”<sup>1003</sup>

In addition to opening duplicate accounts, workers “used a bank database to identify customers who had been pre-approved for credit cards – then ordered the plastic without asking them”.<sup>1004</sup> One former branch manager who worked in the Pacific Northwest discovered that employees “had talked a homeless woman into opening six checking and savings accounts with fees totaling \$39 a month.”<sup>1005</sup> The manager told the Times “It's all manipulation. We are taught exactly how to sell multiple accounts. . . . It sounds good, but in reality it doesn't benefit most customers.”<sup>1006</sup>

A branch manager with 14 years of service with Wells Fargo quit in February 2013, reporting, “she retired early because employees were expected to force ‘unneeded and unwanted’ products on customers to satisfy sales targets.”<sup>1007</sup> She is quoted as saying, “I could no longer do these unethical practices nor coach my team to do them either”.<sup>1008</sup>

The article reported that the Bank “expects staffers to sell at least four financial products to 80% of their customers,” but “top Wells Fargo executives exhort employees to shoot for the Great 8 – an average of eight financial products per household.”<sup>1009</sup> The former branch manager from the Pacific Northwest told the Times that “branch managers are expected to commit to 120% of the daily quotas,” and the results “were reviewed at day's end on a conference call with managers from across the region.”<sup>1010</sup> He told the Times, “If you do not make your goal, you are severely chastised and embarrassed in front of 60-plus managers in your area by the Community Banking president”.<sup>1011</sup>

The article said that by some measures, Wells Fargo is “the nation's biggest retail bank, with more than 6,300 offices and a market valuation of \$237 billion.”<sup>1012</sup> The article reported that the Bank's branch employees “receive ethics training and are compensated mainly in salary, not bonuses,” but that “tellers earn about 3% in incentive pay linked to sales and customer service, . .

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<sup>1002</sup> *Id.* at 4.

<sup>1003</sup> *Id.*

<sup>1004</sup> *Id.* at 1.

<sup>1005</sup> R. Ex. 5250 at 2.

<sup>1006</sup> *Id.*

<sup>1007</sup> *Id.* at 3.

<sup>1008</sup> *Id.*

<sup>1009</sup> *Id.*

<sup>1010</sup> *Id.*

<sup>1011</sup> *Id.*

<sup>1012</sup> *Id.*

. while personal bankers typically derive about 15% to 20% of total earning from these payments.”<sup>1013</sup>

The article quoted an independent bank consultant, Michael Moebs, who said that Wells Fargo “is a master at this, . . . No other bank can touch them.”<sup>1014</sup> The article reported the “pressure to meet goals starts with supervisors,” and that that branch managers in California “have filed five related lawsuits alleging that the bank failed to pay them overtime. The extra hours were spent laboring to meet sales targets”.<sup>1015</sup> Two other recently filed lawsuits alleged that Wells Fargo employees “opened accounts or credit lines without their authorization.”<sup>1016</sup>

One former customer filed suit on September 11, 2013 in Los Angeles County Superior Court alleging that three Wells Fargo employees “used his birth date and Social Security number to open accounts in his name and those of fictitious businesses. At least one employee forged his signature several times”.<sup>1017</sup> The customer alleged that the employees “put their own addresses on the accounts so he wouldn’t know about it. . . . It showed up on his credit report – that’s how he found out.”<sup>1018</sup>

A former bank employee filed suit on October 3, 2013, alleging that she was wrongfully fired “after following her manager’s directions to open accounts in the names of family members.”<sup>1019</sup>

The article reported that Wells Fargo carefully tracks account openings and “lucrative add-ons.”<sup>1020</sup> The documents, dated from 2011 through October 2013, “include a 10-page report tracking sales of overdraft protection at more than 300 Southland branches from Ventura to Victorville; a spreadsheet of daily performance by personal bankers in 21 sales categories, and widely distributed emails urging laggard branches to boost sales and require employees to stay after hours for telemarketing sessions.”<sup>1021</sup>

Mr. Julian testified that he read the December 2013 article and found it to be “[c]oncerning to the extent that, if true, you don’t want leadership – that type of pressure being placed on Team Members or that type of activity.”<sup>1022</sup> He added that it was concerning “to the

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<sup>1013</sup> *Id.* at 2.

<sup>1014</sup> *Id.* at 3.

<sup>1015</sup> *Id.* at 2.

<sup>1016</sup> *Id.*

<sup>1017</sup> R. Ex. 5250 at 4.

<sup>1018</sup> *Id.*

<sup>1019</sup> *Id.*

<sup>1020</sup> *Id.* at 3.

<sup>1021</sup> *Id.*

<sup>1022</sup> Tr. (Julian) at 6312.



extent that there were allegations being made that needed to be further investigated,” but that he believed those allegations were being investigated.<sup>1023</sup>

### **WFAS’s Presentation to the A&E Committee: Fourth Quarter 2013 Summary**

Mr. Julian identified the WFAS Summary dated February 25, 2014 as presented to the WF&C A&E Committee members, and as distributed to the Board of Directors of WF&C, the OCC, and the Federal Reserve.<sup>1024</sup>

Mr. Julian testified that at this time Corporate Investigations, acting through Michael Bacon, provided information that was included in the Summary.<sup>1025</sup> Upon his review of the Corporate Investigations report, Mr. Julian concluded that of allegations reported as EthicsLine cases, “the 13,000 that were Team Member allegations, I had heard – had been informed that approximately 80 to 85 percent of Team Member allegations through the EthicsLine ultimately were found to be unsubstantiated.”<sup>1026</sup>

The data in Mr. Bacon’s report concerned *all* internal fraud and *all* forms of misconduct – and thus was not limited to reporting on sales practices misconduct.<sup>1027</sup> The report, indeed, does not indicate whether *any* of the 13,799 cases concerned allegations of sales practices misconduct.

Nevertheless, Mr. Julian testified that the “remainder of the cases, of the 13,779, I think it is, cases that were not a result of Team Member allegations through EthicsLine but, in fact, were identified through the proactive and detective controls, a large portion of those cases, once investigated, were confirmed.”<sup>1028</sup>

Mr. Julian described a “detective control” as a type of control to identify when there has been a control breakdown.<sup>1029</sup> He denied that a detective control was in any way less effective than proactive controls, opining,

Detective controls are just one type of control. And depending on the control that you -- or the risk that is trying to be mitigated, certain controls were detective, meaning that they would identify to some extent after the fact, and proactive would identify or try to prevent. But it really depended upon the type of risk what type of control needed to be put in place or even could be put in place to manage the risk it's trying to mitigate.<sup>1030</sup>

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<sup>1023</sup> Tr. (Julian) at 6313.

<sup>1024</sup> Tr. (Julian) at 6398-99; R. Ex. 5624; and the transmittal email at R. Ex. 5623.

<sup>1025</sup> Tr. (Julian) at 6402-03.

<sup>1026</sup> Tr. (Julian) at 6407.

<sup>1027</sup> R. Ex. 5624 at 47.

<sup>1028</sup> Tr. (Julian) at 6407.

<sup>1029</sup> Tr. (Julian) at 6471.

<sup>1030</sup> Tr. (Julian) at 6471-72.

Based on these points, Mr. Julian stated that he understands now that Wells Fargo Bank had “both detective controls in place that I was probably more aware of during the time, but also proactive controls that were in place, such as proactive monitoring.”<sup>1031</sup>

Mr. Julian concluded, “the proactive and detective controls in place to identify those cases that ultimately would be investigated, the large portion of the 13,700 and something, that those controls, in fact, were . . . significantly identifying cases that ultimately were confirmed. So the controls were appropriately, in my mind, identifying cases that ultimately, when investigated, were confirmed.”<sup>1032</sup> He said this perspective was different from the view he had in 2018 when he testified that there was too much reliance on detective controls.<sup>1033</sup> He further testified in 2018 that in his opinion the controls to manage the risk of sales practices misconduct “could have been” unsatisfactory.<sup>1034</sup>

Mr. Julian accounted for this material change in his testimony by stating that in 2018 he was “familiar somewhat with controls related to sales practices,” but “didn’t have a full appreciation at the time of the type of proactive monitoring that I’ve heard since my testimony” during these proceedings – specifically testimony from others regarding what he believes are called “thresholds”.<sup>1035</sup> Through a series of leading questions by his Counsel during direct examination, Mr. Julian testified that although he personally did not have a “full appreciation” of this type of monitoring, the WFAS Community Bank Audit Group members did have a general understanding of the detective controls relevant to their assigned areas of responsibility sufficient to design and perform audits.<sup>1036</sup>

Irrespective of which version of Mr. Julian’s testimony is given weight regarding thresholds and detective controls, little weight can be given to Mr. Julian’s conclusion that the CI Summary reflected positively on Internal Audit’s actions related to the Fourth Quarter Summary to the A&E Committee.

The record reflects that the CI Summary was *not* designed to identify sales practices misconduct and does not support Mr. Julian’s determination that this report permitted the conclusion that the controls testing related to the allegations in the L.A. Times article “appeared to be working based on the results of the investigative . . . work,” and that “Audit could rely on Corporate Investigations to perform investigative work appropriately and rely on them – on the proactive and detective controls that, in fact, identified the cases in the first place.”<sup>1037</sup> Nothing in the record supports this conclusion.

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<sup>1031</sup> Tr. (Julian) at 6472.

<sup>1032</sup> Tr. (Julian) at 6407-08.

<sup>1033</sup> Tr. (Julian) at 6473.

<sup>1034</sup> Tr. (Julian) at 6478.

<sup>1035</sup> Tr. (Julian) at 6473.

<sup>1036</sup> Tr. (Julian) at 6474-77.

<sup>1037</sup> Tr. (Julian) at 6408-09.

More to the point, the Summary of 2013 Audit plan focus and results provides substantial evidence that WFAS had *no basis* to conclude Community Bank’s controls testing was working.

In its report on annual fiduciary activities, the Summary noted that that Internal Audit “is required to report annually to the A&E Committee the results of each audit performed, including the significant actions taken as a result of the audit.”<sup>1038</sup> Issued four months after the publication of the first L.A. Times article, the annual fiduciary activities report is silent regarding any activity by WFAS Internal Audit concerning Audit’s testing of either detective or proactive controls regarding Community Bank’s sales practices misconduct issues.<sup>1039</sup>

The Corporate Security Results section of the 2013 Summary speaks not to issues arising from sales practices misconduct, but to issues within the scope of Wells Fargo’s obligations under the Bank Protection Act.<sup>1040</sup> The Act requires “each member bank of the Federal Reserve System to adopt and maintain appropriate security procedures to discourage robberies, burglaries, larcenies, and to assist in the identification and prosecution of persons who commit such acts.”<sup>1041</sup> The data relied upon by Mr. Julian in his testimony – that Corporate Investigations reported 13,799 cases of internal fraud or misconduct – has not been shown to pertain to sales practices misconduct being attributed to Community Bank team members.<sup>1042</sup>

The report states that for a case to be included in this count, all that was required was the allegation be against a team member and that the allegation be about “misconduct involving a possible violation of law or a code of ethics policy violation or information security policy violation, which has resulted in a financial loss and/or exposure or represents a significant compliance or occupational risk.”<sup>1043</sup>

The cases counted in this report were not limited to Community Bank team members, and the report appears to not have been designed to report on sales practices misconduct allegations as a distinct cohort. Further, while portions of the CI report do identify the separate Operating Committee Groups by name (and reports, for example, that 12 open issues concerned Community Bank team members in its “Open Issues” report<sup>1044</sup>) there is no evidence establishing the correlation relied upon by Mr. Julian<sup>1045</sup> – that is, nothing in the report permits a finding that Audit could have or should have relied on *Corporate Investigations* to test the effectiveness of the Community Bank’s proactive or detective controls in light of the factual claims presented by third parties through the L.A. Times articles. In turn, nothing in the report

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<sup>1038</sup> R. Ex. 5624 at Appendix D (p. 76 of report).

<sup>1039</sup> *Id.* at Appendix D, pp. 76-84.

<sup>1040</sup> R. Ex. 5624 at 47, citing 12 U.S.C. § 1882, and 12 C.F.R. Part 21.

<sup>1041</sup> R. Ex. 5624 at 47.

<sup>1042</sup> *Id.*

<sup>1043</sup> *Id.*

<sup>1044</sup> *Id.*

<sup>1045</sup> Tr. (Julian) at 6407.

supported Mr. Julian's self-proclaimed determination that there was no need to escalate any additional information related to sales practices to the Board.<sup>1046</sup>

Apart from providing conflicting testimony regarding whether there was too much reliance in WFAS on detective controls,<sup>1047</sup> Mr. Julian also provided conflicting testimony regarding whether the controls to manage the risk of sales practices misconduct was or was not satisfactory. During his testimony in 2018, Mr. Julian was asked whether the controls to manage the risk of sales practices misconduct were unsatisfactory, and he testified at that time that based on what he knew at the time, yes.<sup>1048</sup>

In his testimony during the hearing, Mr. Julian changed his answer: he stated “[t]o the extent prior to the L.A. Times article, the controls could have been unsatisfactory. But certainly subsequent to the L.A. Time article, based on what I knew . . . work was being done to evaluate the controls, to improve the controls.”<sup>1049</sup> Even with this answer, however, Mr. Julian does not materially change his response to the prior question – he deflects by testifying that efforts were underway to improve the controls, but does not dispute that even after the publication of the article controls to manage the risk of sales practices misconduct remained unsatisfactory.<sup>1050</sup>

#### **WFAS's Presentation to the A&E Committee: May 5, 2014**

Mr. Julian testified that he attended the May 5, 2014 WF&C A&E Committee meeting, and “presented on key activities” that WFAS had conducted during the first quarter of 2014.<sup>1051</sup> Through the WFAS First Quarter 2014 Summary (May 5, 2014), Mr. Julian reported to the A&E Committee WFAS's involvement with key risks.<sup>1052</sup> Mr. Julian testified that this was WFAS's “method for escalating to the A&E Committee” any “new or significant risks that would not have been identified in the RMC memo previously.”<sup>1053</sup>

Mr. Julian confirmed that through this Summary, WFAS identified two business activities related to sales practices that were “escalated” to the A&E Committee: “specifically, [WFAS] was performing two audits, one being in the Wells Fargo Customer Connection business group as well as one in the Digital Channels group. That's in addition to the ongoing

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<sup>1046</sup> Tr. (Julian) at 6409.

<sup>1047</sup> Tr. (Julian) at 6471-77.

<sup>1048</sup> Tr. (Julian) at 6478.

<sup>1049</sup> Tr. (Julian) at 6478.

<sup>1050</sup> Tr. (Julian) at 6478.

<sup>1051</sup> Tr. (Julian) at 6515-16; R. Ex. 20600; R. Exs. 400, 6123 (distribution of WFAS First Quarter 2014 Summary, A&E Reports for April and May 2014 by email transmission to the Board and to the OCC).

<sup>1052</sup> R. Ex. 400 at 31.

<sup>1053</sup> Tr. (Julian) at 6519; see also “22-03-07 Respondents' Amended Revised Errata Days 9 -38” at page 49. Ordered through Second Supplemental Order Regarding Hearing Transcript Errata.

Business Monitoring that had been occurring.”<sup>1054</sup> Neither of these businesses were related to the businesses within the Community Bank that were the subject of sales practices misconduct issues raised by the Times articles. “Digital Channels” is the “online account opening process,” and Customer Connections “is the business unit where telephone sales occurred”.<sup>1055</sup> The Times article raised issues not with respect to either of these businesses within the Community Bank, but instead with respect to activity occurring with Bank branches.<sup>1056</sup>

Mr. Julian justified WFAS’s auditing of these two businesses, rather than the business activity identified in the Times article, in these terms:

At this point in 2014 -- first quarter of 2014, Wells Fargo Audit Services was aware of the work that was going on within the retail banking by both the line of business, first line of [defense], that being the Community Bank risk group as well as by the corporate risk group, who was looking at the activity that had been identified in the L.A. Times article. So while that work was going on, Wells Fargo Audit Services thought it was important to look elsewhere outside of the retail-banking channel but within areas like Customer Connection as well as Digital Channels to determine if any sales activity -- sales practices misconduct activity was going on in those lines of business.<sup>1057</sup>

Mr. Julian testified that WFAS made changes to the 2014 Audit Plan after the Times articles were published.<sup>1058</sup> The Plan Adjustments presented with the WFAS First Quarter 2014 Summary (Appendix B) identified thirteen plan additions, seven plan cancellations or deferrals, and five “carryovers”.<sup>1059</sup>

Mr. Julian testified that because the Audit Plan followed a “dynamic audit approach,” the formal Plan would periodically be changed during the audit year “based on emerging risks, based on relevant information” that WFAS learned.<sup>1060</sup> Such changes were to be presented to the A&E Committee for its approval, so “it was our practice to communicate that to the A&E Committee so they could be aware of any changes being made to the Plan that they had previously approved.”<sup>1061</sup> Mr. Julian later testified, however, that changes to the Audit Plan could be made by WFAS without approval by the A&E Committee: “They were not required to approve the

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<sup>1054</sup> Tr. (Julian) at 6519.

<sup>1055</sup> Tr. (Julian) at 6519-20.

<sup>1056</sup> Tr. (Julian) at 6520-21.

<sup>1057</sup> Tr. (Julian) at 6521.

<sup>1058</sup> Tr. (Julian) at 6522.

<sup>1059</sup> R. Ex. 400 at 60-61.

<sup>1060</sup> Tr. (Julian) at 6523.

<sup>1061</sup> Tr. (Julian) at 6523-24.

changes, just to be made aware of them, and provided an opportunity to discuss and challenge, to the extent they disagreed with Audit's recommendations for Plan changes.<sup>1062</sup>

The changes Mr. Julian identified through this Summary were that WFAS would engage in with the Community Bank were "additional continuous Business Monitoring both on [Store Operations Control Review (SOCR)] and [Business Banking Operations Control Review (BOCR)] as well as participation in Business Monitoring of the Regional Banks' Risk Council. So it identifies that the additional work is now going to be occurring."<sup>1063</sup>

The record reflects that prior to the issuance of the May 5, 2014 Quarterly Summary, Mr. Julian had personally been provided guidance by the OCC regarding weaknesses in the WFAS Business Monitoring Program. The OCC's May 5, 2014 Supervisory Letter specifically addressed WFAS's Business Monitoring Program.<sup>1064</sup> The Letter, which followed a May 1, 2014 Exit Interview between Mr. Julian and the OCC covering the contents of the Letter, noted there were at least two audit teams that have implemented either continuous auditing or testing programs, and found "there is no standard definition as to what constitutes either program or how they should inform and support audit management and processes or WFAS' Audit Strategy."<sup>1065</sup>

Despite being aware of the weaknesses of the WFAS Business Monitoring Plan, Mr. Julian testified that Business Monitoring, rather than control testing, was the appropriate activity for WFAS at this time. In support, he gave the following rationale:

Well, because Corporate Risk as well as the Community Bank line of business had been tasked with investigating and determining the issues -- any issues related to the team member misconduct that had been identified. And so while that work was going on, because that work -- some of that work was new and, you know, it had just been directed by the board, it was important for Wells Fargo Audit Services to be informed of that work, to be able to assess the work and the pace in which that work was going on. So this activity was added to the plan, meaning resources were now allocated to performing this level of work.<sup>1066</sup>

There is nothing in the record, however, that supports a finding that the investigations by Corporate Risk or the Community Bank itself divested WFAS of its responsibility to provide credible challenge and independent audit services – and nothing that would permit WFAS to limit its audit function to the use of Business Monitoring.

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<sup>1062</sup> Tr. (Julian) at 6526.

<sup>1063</sup> Tr. (Julian) at 6524; R. Ex. 400 at 60.

<sup>1064</sup> R. Ex. 1613 at 3.

<sup>1065</sup> *Id.* at 2, 4.

<sup>1066</sup> Tr. (Julian) at 6524-25.

Mr. Julian disputed testimony from OCC Examiner Smith with respect to her statement that while WFAS had “a lot of information” beginning with the L.A. Times articles, “nothing is happening in the Audit in Wells Fargo Audit Services to really look at sales practices misconduct in the Branch Banking System.”<sup>1067</sup> He described this as “misinformed” – either that or she “didn’t know about all this work that was going on.”<sup>1068</sup>

In this context, the work Mr. Julian was referring to was that “Audit was performing continuous business monitoring. The Plan itself identified two audits that were going on specific to sales practices. So there was a significant amount of work going on by Audit.”<sup>1069</sup> In their testimony, however, neither Mr. McLinko nor Mr. Julian identified documentation supporting the assertion that there was continuous business monitoring by WFAS and the CBO audit team directed by Mr. McLinko during the relevant period.

The record reflects that Examiner Smith was not misinformed, nor does it suggest she did not know about all of the work that was going on. The record reflects the two control-testing audits conducted by WFAS were for activities (telephone banking and online banking) that Mr. Julian admitted were not related to the issues relating to sales practices misconduct at the branch banking level as reported by the Times articles. The record further offers virtually no evidence of what “Business Monitoring” was taking place, and as the OCC had previously told Mr. Julian, the Business Monitoring Program lacked a standard definition as to what constitutes “Business Monitoring” or how WFAS auditors should inform and support audit management and WFAS’ Audit Strategy.<sup>1070</sup>

Further, nothing in the Summary for 1Q2014 reflected that WFAS had identified the risks presented through the Times article: the Summary states only, “an assessment of cross sell audit coverage is included in the Community Banking audit plan. Focus of these reviews is on the sales practices and conduct to ensure customers are sold products meeting their financial needs.”<sup>1071</sup> The Plan is silent with respect to the nature of the assessment and there is no indication that Audit will be testing Community Bank controls for efficacy.

Reference to the minutes of the May 5, 2014 A&E Committee meeting leads to the conclusion that nothing Mr. Julian presented during that meeting adequately informed the Committee members of the risks identified through the Times article. When asked by a Committee member for details “regarding the risk rating of open issues,” Mr. Julian said, “he would enhance the report next quarter” to provide that information.<sup>1072</sup>

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<sup>1067</sup> Tr. (Julian) at 6625-26.

<sup>1068</sup> Tr. (Julian) at 6526.

<sup>1069</sup> Tr. (Julian) at 6526.

<sup>1070</sup> R. Ex. 1613 at 2, 4.

<sup>1071</sup> R. Ex. 400 at 31.

<sup>1072</sup> R. Ex. 20600 at 3.

When asked about the “increase in repeat and protracted issues,” Mr. Julian responded that the “increase resulted from heightened expectations and increased scrutiny with WFAS’s review of open items.”<sup>1073</sup> When asked about the “increase in the time taken to validate issues,” Mr. Julian responded he “expects the amount of time to decrease in the future.”<sup>1074</sup> When asked about the number of Suspicious Activity Reports (SARs) related to activity by team members, Mr. Julian recommended that “the head of Corporate Security speak to the Committee regarding SARs at a future meeting,” while expressing the view that “it is generally better to file [them] than not if there is a suspicion of criminal activity.”<sup>1075</sup>

Mr. Julian said nothing directly addressing the issues presented by the Times article or audits WFAS was performing regarding risk management controls being used by the Community Bank, and made no mention of anything regarding sales practices misconduct by Community Bank team members.<sup>1076</sup> Further, there is no evidence establishing that Mr. McLinko sought to include in Mr. Julian’s reporting any audit issues related to the efficacy of risk-management tools being used by the Community Bank to address risks related to sales practices misconduct.

#### **WFAS’s Presentation to the Board’s Risk Committee: July 2014**

Mr. Julian identified the July 2014 Noteworthy Risk Issues memo as the product of the ERM brainstorming process.<sup>1077</sup> Without identifying the Community Bank as the line of business being described, the “Sales Conduct, Practices and the Consumer Business Model” risk issue in the report of July 2014 stated the following:

With heightened focus on consumer customers, management is discussing the risks associated with sales practices, our cross sell strategy, and team member conduct. Ensuring we are providing products that provide real benefit to the customer, are sold in the appropriate manner with the proper sales incentives, and are delivered with high operational excellence is key in this environment to reducing our risk.<sup>1078</sup>

The July 2014 memo is silent with respect to any responsive initiatives by WFAS or the CBO to determine the adequacy of controls regarding the issues presented by the L.A. Times articles, and fails to indicate that the root cause of sales practices misconduct had yet to be named by either the Community Bank or WFAS. Nevertheless, Mr. Julian testified that as of July

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<sup>1073</sup> R. Ex. 20600 at 3.

<sup>1074</sup> *Id.* at 4.

<sup>1075</sup> Tr. (Julian) at 6528; R. Ex. 20600 at 4.

<sup>1076</sup> R. Ex. 20600 at 3-4.

<sup>1077</sup> Tr. (Julian) at 6590; OCC Ex. 1103.

<sup>1078</sup> OCC Ex. 1103 at 2.



2014, he was not aware of any other information regarding sales practices risk that needed to be escalated to the Board of Directors.<sup>1079</sup>

Mr. Julian testified that the substance of the July 2014 Noteworthy Risk Issues memo from ERMC was discussed during Mr. Loughlin's presentation to the Board's Risk Committee on August 4, 2014.<sup>1080</sup> Nothing in the Committee's minutes from this meeting identified risks arising from sales practices misconduct by team members of the Community Bank or the efficacy of controls used by the first line of defense to address the risks of such misconduct.<sup>1081</sup> Instead, Mr. Loughlin is recorded as identifying "risks associated with changes in the Federal Reserve's monetary policy and the resulting potential impacts to asset values and customers, cyber security threats, regulatory focus on the growth of Wells Fargo Securities, and sales conduct practices", making no mention of the Community Bank.<sup>1082</sup>

In response to a Committee member's question about "cross-sell risk issues," Mr. Loughlin is reported to have discussed with Mr. Stumpf "the Company's focus on ensuring its cross-sell strategies are consistent with the development of long-term customer relationships."<sup>1083</sup> There is no reported discussion regarding sales practices misconduct by team members of the Community Bank. Nor is it disclosed that during the relevant period, WFAS lacked the ability to distinguish cross-sell from the Community Bank's overall sales activities – because (according to Ms. Russ Anderson and Mr. Julian) cross-sell "was inherent in the business practice."<sup>1084</sup> During the hearing, Mr. Julian testified – without offering any documentary support for the claim – that as a result, WFAS could not conduct a cross-sell specific review of the Community Bank analogous to audits conducted for other businesses.<sup>1085</sup>

Asked what he understood, as of August 2014, the Risk Committee's response to be to the sales practices issues that had been raised in the L.A. Times articles, Mr. Julian testified:

As of August of 2014, the Risk Committee had specifically directed Mike Loughlin, who was the chief risk officer, to work with the Community Bank business group to investigate the allegations that were made and to work with the Community Bank to understand the issues, including sizing the issue, understanding the root cause of the issue and so forth.<sup>1086</sup>

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<sup>1079</sup> Tr. (Julian) at 6590.

<sup>1080</sup> Tr. (Julian) at 6592; OCC Ex. 1967 at 4.

<sup>1081</sup> OCC Ex. 1967 at 4.

<sup>1082</sup> *Id.*

<sup>1083</sup> *Id.*

<sup>1084</sup> Tr. (Julian) at 6625.

<sup>1085</sup> Tr. (Julian) at 6625-26.

<sup>1086</sup> Tr. (Julian) at 6592.

There is, however, nothing in the minutes of the Risk Committee’s August 2014 meeting suggesting or establishing that the Board or the Board’s Risk Committee sought to limit in any way Audit’s response to the issues raised in the Times articles. Further, there is no evidence establishing that Mr. McLinko sought to include in Mr. Julian’s reporting any audit issues related to the efficacy of risk-management tools being used by the Community Bank to address risks related to sales practices misconduct.

#### **WFAS’s Presentation to the Board’s Risk Committee: October 2014**

Mr. Julian identified that part of the October 2014 Noteworthy Risk Issues memo pertaining to Sales Conduct, Practices and the Consumer Business Model. The language in the October 2014 memo is identical to the August 2014 Noteworthy Risk Issues memo.<sup>1087</sup>

Like the July 2014 memo, the October 2014 memo is silent with respect to any initiatives by WFAS to determine the adequacy of controls regarding the issues presented by the L.A. Times articles, and fails to indicate that the root cause of sales practices misconduct has yet to be publicly identified. Nevertheless, Mr. Julian testified that as of October 2014, he was not aware of any other information regarding sales practices risk that needed to be escalated to the Board of Directors.<sup>1088</sup> Further, there is no evidence establishing that Mr. McLinko sought to include in Mr. Julian’s reporting any audit issues related to the efficacy of risk-management tools being used by the Community Bank to address risks related to sales practices misconduct.

#### **Execution of the 2013 Audit Plan**

Although the 2013 Audit Plan did not identify sales practices misconduct as an existing or emerging risk, Mr. Julian testified that it “gave me comfort that the OCC had evaluated the plan.”<sup>1089</sup> Elaborating, he stated, “[c]ertainly they had been performing work across the company to assess risks and to identify any material or significant risks that they thought ought to be addressed.”<sup>1090</sup> He regarded the OCC’s examination as “just yet another opportunity for me to take comfort that the Plan, the [WFAS] Audit Services 2013 Plan, incorporated the right level of risks and was . . . to be executed on the right types of risk.”<sup>1091</sup> Through this response, Mr. Julian exhibited no appreciation for the distinction existing between WFAS’s role as the Bank’s third line of defense – with its affirmative obligation to understand deeply the line of business and its emergent risks – and the OCC’s role as a regulatory supervisor.

Mr. Julian stated that after the WF&C Board of Directors adopted the 2013 Audit Plan presented by WFAS through Mr. Julian, the WFAS Audit Groups would “begin the detailed

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<sup>1087</sup> Tr. (Julian) at 6590; OCC Ex. 1103 at 2, cf. OCC Ex. 739 at 2.

<sup>1088</sup> Tr. (Julian) at 6593.

<sup>1089</sup> Tr. (Julian) at 6288.

<sup>1090</sup> Tr. (Julian) at 6288.

<sup>1091</sup> Tr. (Julian) at 6289.

scoping of the Audit Plan [and] assign[] various resources.”<sup>1092</sup> Mr. Julian stated, however, that he was not involved in the scoping of the audits that were to be executed as part of the Audit Plan.<sup>1093</sup> He also was not involved in any part of an individual Audit Plan execution; nor in any of the scheduling of audits called for under the Audit Plan.<sup>1094</sup>

### **Transmission of the January 22, 2014 Significant Risk Memo to the Board of Directors and the Operating Committee**

Mr. Julian testified that on January 22, 2014, the ERM, through its Chair, Mike Loughlin, made its quarterly report to the WF&C Operating Committee and Board of Directors.<sup>1095</sup> That report described the “overall state of risk is high and rising.”<sup>1096</sup>

The January 2014 report to the WF&C Board of Directors was silent with respect to issues raised by the L.A. Times article; it was silent about issues related to fraudulent conduct by team members; it was silent regarding the failure of the first line of defense to publicly name the root cause of this misconduct; and it was silent regarding tangible evidence of pressure to engage in abusive and illegal sales practices placed on team members by supervisors.<sup>1097</sup>

The Risk Memo obliquely described the issue in the following terms:

**Sales Conduct, Practices and the Consumer Business Model.** With heightened focus on consumer customers, management is discussing the risks associated with sales practices, our cross sell strategy, and team member conduct. Ensuring we are providing products that provide real benefit to the customer, are sold in the appropriate manner with the proper sales incentives, and are delivered with high operational excellence is key in this environment to reducing our risk.<sup>1098</sup>

According to Mr. Julian, the memo presented by the ERM to the OCC, the WF&C Board of Directors, and the WF&C Operating Committee, was the product of the ERM brainstorming process.<sup>1099</sup> He testified that the text presented above “was included as a result of the dialogue that occurred at the prior [October 9, 2013] ERM meeting where I raised sales practices as a significant risk and an issue that ought to be discussed and disclosed.”<sup>1100</sup> He

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<sup>1092</sup> Tr. (Julian) at 6013.

<sup>1093</sup> Tr. (Julian) at 6013.

<sup>1094</sup> Tr. (Julian) at 6013-14.

<sup>1095</sup> Tr. (Julian) at 6285; R. Ex. 19357.

<sup>1096</sup> R. Ex. 19357 at 1.

<sup>1097</sup> *Id.*

<sup>1098</sup> *Id.*

<sup>1099</sup> Tr. (Julian) at 6352-53.

<sup>1100</sup> Tr. (Julian) at 6354; see also, “22-03-07 Respondents’ Amended Revised Errata Days 9 -38” at page 46. Ordered through Second Supplemental Order Regarding Hearing Transcript Errata.

acknowledged criticism of the text – which does not identify sales practices misconduct as a systemic problem – but said as of January 2014 he had not received data or information indicating that the sales conduct issue was either widespread or systemic.<sup>1101</sup> There is no evidence establishing that Mr. McLinko sought to include in Mr. Julian’s reporting any audit issues related to the efficacy of risk-management tools being used by the Community Bank to address risks related to sales practices misconduct.

Mr. Julian also acknowledged criticism by the OCC based on the premise that escalation should include details in regards to the significant risk issue, the root cause of that issue, how the issue could affect the Bank, and what recommended actions management needed to take to remediate the issue.<sup>1102</sup> He said the January 2104 memo had none of these things because “at this time, the root cause wasn’t known” – to him, and to others;<sup>1103</sup> neither was the impact of sales practices issues on the Community Bank.<sup>1104</sup> Nothing in the documentary evidence introduced during the hearing indicated that Mr. Julian escalated to the Bank’s Risk Committee that WFAS had not determined the root cause of team member misconduct.

Mr. Julian acknowledged that WFAS had responsibilities specific to finding the root cause of the sales practices misconduct issue. He testified:

WFAS was responsible for identifying root cause when that root -- when the issue, underlying issue was identified in the course of WFAS's audit work. So to the extent WFAS in the execution of its audit plan would identify an audit issue, at that time, WFAS was also responsible for determining root cause so that it could present the issue and the underlying root cause to the business unit who was responsible for addressing the issue. In this case, to the extent issues are identified outside of audit's work, such as self-identified by a business unit or in this case identified through . . . the Corporate Investigations work, when issues are identified like that, it's the responsibility of the business unit to own the identification of the root cause.<sup>1105</sup>

Mr. Julian gave this description of how little he knew about these issues as of January 2014:

Again, at the time, what was known from the L.A. Times article was that approximately 35 team members had been terminated for sales practices misconduct. At that time, I was aware that the controls that were in place

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<sup>1101</sup> Tr. (Julian) at 6354-55.

<sup>1102</sup> Tr. (Julian) at 6355.

<sup>1103</sup> Tr. (Julian) at 6355-56.

<sup>1104</sup> Tr. (Julian) at 6356.

<sup>1105</sup> Tr. (Julian) at 6364-65.

actually identified that conduct. And as well, I wasn't aware of any further steps at that time that needed to be taken -- needed to be put in place.<sup>1106</sup>

This response failed to account for the wealth of information supplied by Mr. Bacon for Corporate Investigations and the EthicsLine documents that he had reviewed indicating the scope and nature of the risks associated with team member misconduct and the possible failure of risk management controls by the Community Bank's first line of defense.

Mr. Julian denied having any responsibility for investigating the issues that had been raised in the L.A. Times articles.<sup>1107</sup> Elaborating on that answer, he testified that,

this issue was identified not through Audit's work but rather through . . . the Corporate Investigations work that was performed and then was escalated, if you will – or not escalated, but at least identified also through the L.A. Times article. In that sense, when issues are raised outside of Audit's work, as I mentioned before, it's the responsibility of the business unit to investigate the root cause, the business unit who owns the underlying management of the risk".<sup>1108</sup>

Mr. Julian distinguished between determining the root cause of a control failure and determining the root cause of sales practices misconduct:

Well, a control failure is a specific control activity that is in place to manage a risk. And to the extent that that control fails, it's possible to go and determine the root cause of that control failure, what caused that control not to work. Sales practices misconduct in the -- you know, as the Enforcement Counsel describes it, isn't a control. There's not one control that manages sales practices misconduct. It's a series of controls and, therefore, it's just different in nature when you're talking about root cause of a control issue versus root cause of something of a nature, for instance, of sales practices misconduct as the OCC defines it in this matter.<sup>1109</sup>

Mr. Julian testified that once the above-quoted ERMC report was sent to the Board, responsibility for overseeing the Company's response addressing that risk was with the members of the Risk Committee of the Board.<sup>1110</sup> He identified the agenda for the February 24, 2014 meeting of the WF&C Risk Committee – which makes no mention of any of the risks described by the two L.A. Times articles.<sup>1111</sup>

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<sup>1106</sup> Tr. (Julian) at 6357.

<sup>1107</sup> Tr. (Julian) at 6365.

<sup>1108</sup> Tr. (Julian) at 6366.

<sup>1109</sup> Tr. (Julian) at 6366-67.

<sup>1110</sup> Tr. (Julian) at 6360.

<sup>1111</sup> R. Ex. 1780 at 3.

Instead, among the “Noteworthy Risk Issues” included in the February 2014 report, the following entry appears under the subheading “Sales Conduct, Practices and the Consumer Business Model”:

With heightened focus on consumer customers, management is discussing the risk associated with sales practices, our cross sell strategy, and team member conduct. Ensuring we are providing products that provide real benefit to the customer, are sold in the appropriate manner with the proper sales incentives, and are delivered with high operational excellence is key in this environment to reducing our risk.<sup>1112</sup>

Notably absent from this description is any acknowledgement of the failure to identify or disclose to the Bank’s risk managers the root cause of the issues presented in the L.A. Times articles.

Mr. Julian explained that the Noteworthy Risk Issues described in this section of the February 2014 report lacked any claim that the risks were either systemic or widespread “because at that time, I had no information to indicate that the issue was systemic or widespread,” and lacked any description of the root cause of the issue because at the time, “I didn’t know the root cause for the sales conduct practices and consumer model issue raised.”<sup>1113</sup> This answer fails to disclose the information provided to Mr. Julian that had been escalated to him through the delivery of EthicsLine reports raising concerns about the scope and nature of sales practices misconduct throughout 2013 and into 2014.

Similarly, the report is silent with respect to the impact of sales practices misconduct because, according to Mr. Julian, “I didn’t know the impact – that that work was being performed to determine the impact”.<sup>1114</sup> Further, the report did not identify recommended actions that management must take because “work was being – was ongoing with respect to determining – with respect to determining corrective actions that might be necessary.”<sup>1115</sup>

In this context, Mr. Julian said that the ongoing work was being performed by “a core group in place” and the Community Bank “was looking at - at the issue and looking at the controls and so forth” and “Corporate Risk had been tasked with taking the lead and looking at the effort and investigating the matters. All that work was ongoing at the time” this report was issued.<sup>1116</sup> This response makes no reference to any credible challenge by WFAS generally or by Mr. McLinko specifically, regarding the efficacy of risk management controls in place in the Community Bank’s first line of defense.

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<sup>1112</sup> *Id.* at 67. See also OCC Ex. 1107 at 1.

<sup>1113</sup> Tr. (Julian) at 6393.

<sup>1114</sup> Tr. (Julian) at 6393-94.

<sup>1115</sup> Tr. (Julian) at 6394.

<sup>1116</sup> Tr. (Julian) at 6394.

Mr. Julian described the process by which the “Noteworthy Risk Issues” were developed for the February 2014 report: “The process for creating this would have been with Mike Loughlin and his Corporate Risk team” and the “dialogues that occurred at the Enterprise Risk Management Committee meeting,” of which Mr. Julian was a member.<sup>1117</sup> He added the same process was followed quarterly throughout the relevant period.<sup>1118</sup>

Mr. Julian identified the April 2014 Noteworthy Risk Issues, which copies verbatim the description of “Sales Conduct, Practices and the Consumer Business Model”<sup>1119</sup> presented in the February 2014 report.<sup>1120</sup> Asked what he had been personally doing with regard to WFAS’s audit work relating to Wells Fargo’s response to sales practices issues raised in the L.A. Times, Mr. Julian responded that he was having “one-on-one meetings with . . . various WFAS leadership as well as the Audit Management Committee,” along with “routine updates from WFAS personnel with respect to business monitoring that was going on,” and he “continued to be engaged in dialogues with all levels of management, participation in various committees, discussions with regulators. And so ongoing discussions with various stakeholders around the issues.”<sup>1121</sup> During his testimony, however, Mr. Julian identified no documentary support for this set of factual premises, and identified no documentation of business monitoring by WFAS relating to the risks associated with team member misconduct.

Although the report now had the benefit of information presented to WFAS and Mr. Julian between February and April 2014, Mr. Julian testified that he was not aware of any information beyond that which is shown in the April 2014 report that needed to be escalated to the Board of Directors of Wells Fargo.<sup>1122</sup> And he said no one inside or outside of WFAS raised with him any issues regarding the pace or substance of the Community Bank’s response to the sales practices misconduct issues identified in the L.A. Times article.<sup>1123</sup>

Mr. Julian identified the minutes of the April 28, 2014 meeting of WF&C’s A&E Committee, and acknowledged he made the presentation described in the Audit Update section of the minutes.<sup>1124</sup> There are two noteworthy features of the Update: first, Mr. Julian – apparently not for the first time – reported that WFAS would be relying on “the activities of other business lines” [REDACTED] – and that he was “working with

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<sup>1117</sup> Tr. (Julian) at 6387-88; OCC Ex. 1107 at 1.

<sup>1118</sup> Tr. (Julian) at 6388-89.

<sup>1119</sup> Tr. (Julian) at 6482; OCC Ex. 2162.

<sup>1120</sup> Cf. OCC Ex. 1107 (February 2014) and OCC Ex. 2162 (April 2014).

<sup>1121</sup> Tr. (Julian) at 6483-84.

<sup>1122</sup> Tr. (Julian) at 6482.

<sup>1123</sup> Tr. (Julian) at 6484.

<sup>1124</sup> Tr. (Julian) at 6487; R. Ex. 19525 at 6.

management of those lines of business to ensure their work is completed in a timely and comprehensive manner that WFAS can leverage.”<sup>1125</sup>

Second, the Update is remarkable for its lack of information regarding the issues presented through the third party reporting found in the EthicsLine reports or the articles of the L.A. Times. Mr. Julian is reported to have “presented a report on the Company’s approach to retrospective reviews of adverse events,” with no mention that the two articles from the Times were adverse events. The example reported in the minutes had nothing to do with sales practices misconduct but instead was one regarding the “first quarter write-down of an equity investment in the Company’s renewable energy portfolio.”<sup>1126</sup>

In his report on the WFAS 2013 Enterprise Risk Management (ERM) Assessment, there is no indication that either Mr. Julian or Mr. McLinko raised any of the risks associated with sales practices misconduct in the Community Bank. Instead, he attributed the fact that WFAS rated ERM as “Needs Improvement” to the fact that “the rating was the result of heightened expectations, not a degradation in ERM.”<sup>1127</sup> While the minutes indicate Mr. Julian “reviewed the line of defense ratings by risk area,” there is nothing in the minutes suggesting he had escalated to the A&E Committee concerns relating to either the Community Bank generally or its sales practices misconduct problem in particular.<sup>1128</sup> Nothing in his testimony suggests otherwise.<sup>1129</sup> After identifying the WFAS 2013 Enterprise Risk Management Assessment presented to the A&E Committee on April 28, 2014, Mr. Julian defended the lack of information specific to the Community Bank by deflecting, stating that the Report “is an enterprise-wide Enterprise Risk Management Assessment, so . . . it’s specific to the entire corporation, all the entities within Wells Fargo & Company.”<sup>1130</sup>

According to Mr. Julian, his role in reporting this Assessment was to “assure that there was a methodology for developing this ERMA that could be relied upon.”<sup>1131</sup>

And then I was engaged -- as the enterprise-wide ERMA was being prepared and pulled together, I would engage in dialogues both with individual senior leaders within Wells Fargo Audit Services to understand their perspectives on their individual line of business, but also with the Audit Management Committee group to discuss and understand what the

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<sup>1125</sup> R. Ex. 19525 at 6.

<sup>1126</sup> *Id.*

<sup>1127</sup> *Id.*

<sup>1128</sup> *Id.*

<sup>1129</sup> Tr. (Julian) at 6487-88.

<sup>1130</sup> Tr. (Julian) at 6489; R. Ex. 1157.

<sup>1131</sup> Tr. (Julian) at 6491; R. Ex. 1157.



audit management leadership was ultimately recommending as it relates to the enterprise-wide opinions.<sup>1132</sup>

The record does not establish that Mr. Julian actually understood the methodology used in developing the ERMA: Mr. Julian testified that he formed his belief about the reliability of the process for the creation of the ERMA “based on discussions I had with the leadership group as well as the Audit Group that was pulling it all together”.<sup>1133</sup>

The Assessment is silent with respect to issues raised by the L. A. Times articles, and makes no mention of the issues relating to sales practices misconduct by team members of the Community Bank. Instead, the Assessment reported that the enterprise-wide first lines of defense – the lines of business – all, without exception, “have established satisfactory risk management frameworks.”<sup>1134</sup> It found the second line of defense “needs improvement primarily in the space of operational risk management.”<sup>1135</sup>

Mr. Julian testified that the “needs improvement” grade in this sector would have an impact on sales practices risk – as the risk is an operational risk, as well as a compliance risk.<sup>1136</sup> While the Assessment never discloses this relationship between operational risk and sales practices misconduct, Mr. Julian opined that “because sales practices risk was a type of operational risk” WFAS “was concluding that the environment with respect to managing operational risk as a whole needed to be improved,” and as such, that would “encompass activities related to sales practices.”<sup>1137</sup>

In its focus on culture, as expressed through the company’s Vision and Values and its Employee Handbook, the Assessment reported the culture is “communicated in team member meetings and publications,” and found Community Bank’s culture to be “Strong,” its highest rating.<sup>1138</sup> Mr. Julian testified that “from a risk management standpoint,” culture “involved, from WFAS’s view, an assessment of the management, the tone at the top. Meaning were they attentive to risk management issues? Were they – did they address them in a timely manner?”<sup>1139</sup>

Asked for his reaction to these April 2014 ratings in light of the L.A. Times articles that had been published in October and December 2013, Mr. Julian testified:

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<sup>1132</sup> Tr. (Julian) at 6491.

<sup>1133</sup> Tr. (Julian) at 6493.

<sup>1134</sup> R. Ex. 1157 at 2.

<sup>1135</sup> *Id.*

<sup>1136</sup> Tr. (Julian) at 6496; R. Ex. 1157 at 4.

<sup>1137</sup> Tr. (Julian) at 6496.

<sup>1138</sup> R. Ex. 1157 at 9, 12.

<sup>1139</sup> Tr. (Julian) at 6499-500.

Well, first of all, this rating on the Community Bank is a reflection of their management of controls across the Community Bank, not just specific to one type of activity such as sales practices activity. So this is a reflection of all the work across the Community Bank's controls. It's important to also understand that at this time, you know, the L.A. Times article, as I had mentioned before, identified the 35 team members had been terminated as a result of -- well, I was aware that it was as a result of controls in place to identify such behavior. So the L.A. Times article at the time didn't lead me to believe that -- didn't give me any indication that a rating of satisfactory for the Community Bank overall was an inappropriate rating based on what I understood.<sup>1140</sup>

In the report on Culture, the Assessment reports that WF&C “does not have robust processes in place to identify areas misaligned with the company’s desired risk and ethical culture.”<sup>1141</sup> Mr. Julian testified, without providing details or a specific timeline, that in early 2014 WF&C was taking steps to improve its processes to detect outlier areas.<sup>1142</sup>

In its focus on risk identification, assessment and analysis, the Assessment reported, “Operational risk lacks a comprehensive enterprise risk assessment framework in respect to broader operational risk areas for capturing, assessing, and reporting risks across the enterprise.”<sup>1143</sup> It continued: “WFC’s ability to aggregate risk information is hindered by data that is difficult to collect, manipulate, and share. In addition, it is not always possible to ensure data accuracy due to the lack of standard data definitions and agreement on source data.”<sup>1144</sup>

Asked how WFAS could have issued a “Strong” rating for Culture in the 2013 ERMA given the L.A. Times article and issues raised therein in late 2013, Mr. Julian responded:

Well, again, at the time that this was issued, and it was reflective of a full year of 2013, I had not been made aware, other than late in 2013, that there were some allegations -- again, the L.A. Times article in late 2013 identified a few team members who were raising concerns around undue sales pressure. But I had not seen information at that time or wasn't aware of information at that time that caused me to believe that that was -- that

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<sup>1140</sup> Tr. (Julian) at 6498-99.

<sup>1141</sup> R. Ex. 1157 at 13.

<sup>1142</sup> Tr. (Julian) at 6500-01

<sup>1143</sup> R. Ex. 1157 at 13.

<sup>1144</sup> *Id.* at 14.

behavior was widespread or systemic, per se, across the -- across Community Bank.<sup>1145</sup>

### **2014 Audit Plan and Plan Update**

Mr. Julian testified that he participated in the February 25, 2014 meeting of WF&C's A&E Committee.<sup>1146</sup> He confirmed that Mr. Hernandez and Mr. Quigley were still members of the Committee.<sup>1147</sup>

Notwithstanding the issues presented by Mr. Bacon and by the presentation of the L.A. Times articles at the end of 2013, Mr. Julian reported to the members of the A&E Committee that "overall, controls are functioning as intended."<sup>1148</sup>

Mr. Julian testified he presented the 2014 Audit Plan to the A&E Committee at this meeting.<sup>1149</sup> Through this Audit Plan, Mr. Julian reported that "current staffing levels are adequate to execute the 2014 Audit Plan," the Plan "represents an increase of 30% over the hours utilized in 2013"; appropriate coverage of high risk areas within required 12-18 months"; "69% of the Audit Plan is allocated to control testing, the core activity for WFAS"; and "65% of our audit focus is on those Operating Committee Groups which we have determined to have heightened risk. Those areas are Corporate Risk Group, Consumer Lending Group, Wholesale Banking Group, and Technology and Operations Group."<sup>1150</sup> There is no mention of the sales practices issues raised by the articles in Mr. Julian's Internal Audit Update.<sup>1151</sup> There is no indication that Mr. McLinko sought to have Mr. Julian escalate issues related to the possible ineffectiveness of risk-management audit controls by WFAS over the Community Bank.

Mr. Julian testified that he also presented the 2014 Audit Plan Update during this meeting.<sup>1152</sup> In the 2014 Audit Plan Update, the minutes reflect that Mr. Julian said, "he believes the audit plan provides appropriate coverage and that staffing is at an adequate level to support the plan."<sup>1153</sup> There is no mention of the sales practices issues raised by Mr. Bacon, the EthicsLine reports, or the 2013 articles in the 2014 Audit Plan Update.<sup>1154</sup> When asked whether his conclusion that "controls are functioning as intended" was a reference specifically to the

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<sup>1145</sup> Tr. (Julian) at 6501-02.

<sup>1146</sup> Tr. (Julian) at 6409; R. Ex. 20701.

<sup>1147</sup> Tr. (Julian) at 6412.

<sup>1148</sup> Tr. (Julian) at 6412; R. Ex. 20701 at 1.

<sup>1149</sup> Tr. (Julian) at 6435; OCC Ex. 2107; Resp. Ex. 734.

<sup>1150</sup> OCC Ex. 2107 at 4.

<sup>1151</sup> R. Ex. 20701 at 1.

<sup>1152</sup> Tr. (Julian) at 6412-13.

<sup>1153</sup> R. Ex. 20701 at 2.

<sup>1154</sup> R. Ex. 20701 at 2.

Community Bank, Mr. Julian said, “No, it wasn’t.”<sup>1155</sup> He said he could make this report “based on the work that had been conducted during the prior period,” and that “a significant portion of the audits that had been executed received ‘Effective’ ratings” so “it was concluded that . . . the overall system of controls were [*sic*] functioning as intended.”<sup>1156</sup>

During direct examination, Mr. Julian was asked whether, as of February 2014 he had received information indicating that the internal controls were not functioning as intended at the Community Bank, and he responded, “No, I did not.”<sup>1157</sup> He did not mention the information provided by Mr. Bacon and denied that the L.A. Times articles indicated any problems with the Community Bank’s internal controls.<sup>1158</sup> He testified that based on the information he had at the time, “and with respect to the L.A. Times article and the 35 Team Members that had been terminated, actually, the controls are what identified that behavior.”<sup>1159</sup> He asserted, “action then was taken to terminate the Team Members that participated in that activity. So actually the controls are what identified it.”<sup>1160</sup>

One feature of the 2014 Audit Plan is its dynamic nature:

Based on the dynamic nature of the plan, changes to the Audit Plan are expected to occur during the year. These changes are driven by new/emerging risks, changes in the current organization, and/or processes issues and/or concerns arising through ongoing business monitoring, thematic trend results, and inclusion in various proactive risk discussions such as new products committees, quarterly meetings with Corporate Risk, and the Emerging Risk Management Committee (ERMC).<sup>1161</sup>

The 2014 Audit Plan called for 647,000 hours of “control testing” versus 145,000 hours of “business monitoring” and 62,500 hours of “project audit”.<sup>1162</sup> Despite identifying Community Banking in the upper left quadrant of the 2014 OGC Strategic Risk Assessment – denoting its “heightened strategic risk,”<sup>1163</sup> and despite Mr. Julian’s knowledge of issues reported by Mr. Bacon, the EthicsLine reports, and the L.A. Times concerning sales practices misconduct in the Community Bank, the 2014 Audit Plan he presented to the A&E Committee

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<sup>1155</sup> Tr. (Julian) at 6412.

<sup>1156</sup> Tr. (Julian) at 6414.

<sup>1157</sup> Tr. (Julian) at 6414.

<sup>1158</sup> Tr. (Julian) at 6414.

<sup>1159</sup> Tr. (Julian) at 6414.

<sup>1160</sup> Tr. (Julian) at 6414-15.

<sup>1161</sup> OCC Ex. 2107 at 20 (page 17 of the Plan).

<sup>1162</sup> *Id.* at 21 (page 18 of the Plan).

<sup>1163</sup> *Id.* at 10 (page 7 of the Plan)

allocated only 51,500 Audit Plan hours to the Community Bank – representing 5% of the 2014 Audit Team hours provided by WFAS – the lowest percentage of all Audit teams.<sup>1164</sup>

This was at a time where WFAS staffing had a shortfall of 15 team members, but through Mr. Julian reported to the A&E Committee that it “does not anticipate this staffing gap to be problematic as it is a small percentage (<2%) of our overall team” and the staffing need “was identified early in the year”.<sup>1165</sup> At the time of the distribution of the 2014 Audit Plan, WFAS had only one open staffing position to be filled for the Community Banking and TOG Operations Team.<sup>1166</sup> It also reported that there were no material gaps in skill sets – and the gaps “will not have an impact on WFAS’ ability to complete its 2014 Audit Plan with quality.”<sup>1167</sup>

Also of note in the 2014 Audit Plan is the decision by WFAS and Mr. Julian to emphasize business monitoring rather than control testing for the Community Bank during the Audit Plan. Business monitoring activities include “continuous risk assessment, analyses of business reporting and metrics, and issue validation.”<sup>1168</sup>

Noteworthy, according to Mr. Julian, is that these monitoring activities “typically do not result in any formal audit reports or audit conclusions but instead are integral to WFAS responding to unexpected changes in strategic risk factors, risk profiles, and enterprise events and being able to quickly redirect audit resources to areas of emerging risk as needed.”<sup>1169</sup> As noted above, the record does not support the proposition that business monitoring results in no formal audit reports or audit conclusions.

Although the record established that each form of Business Monitoring was to be reported through written documentation, Mr. Julian testified that “at my level, business monitoring included activities such as my participation in a management level committee such as the Operating Committee, the ERMC and other committees we’ve discussed, my engagement . . . at Board meetings as well as committee meetings of the Board, my engagement with regulators with respect to the OCC and the Federal Reserve, what information did they have that I felt was important that should influence our plan and work being done, as well as individual dialogues with various leaders across Wells Fargo Corporation [*sic*].”<sup>1170</sup> Nothing in the record confirmed that Mr. Julian’s business monitoring was exempt from the requirement of written documentation.

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<sup>1164</sup> *Id.* at 22 (page 19 of the Plan).

<sup>1165</sup> *Id.* at 30-31 (page 27 of the Plan).

<sup>1166</sup> *Id.* at 31 (page 28 of the Plan).

<sup>1167</sup> *Id.* at 32 (page 29 of the Plan).

<sup>1168</sup> *Id.* at 19 (page 16 of the Plan).

<sup>1169</sup> *Id.*

<sup>1170</sup> Tr. (Julian) at 6419-20.

During the February 25, 2014 A&E Committee meeting, Mr. Julian also presented the 2014 WFAS Audit Charter, which the Committee approved.<sup>1171</sup> Asked whether the 2014 Audit Plan addressed sales practices in any way, Mr. Julian responded that it did, but offered no specifics. Instead, he testified: “So there were various audits of controls that were performed across the organization that address controls related to sales practices. It also incorporated a significant level of business monitoring on the work that was being performed with respect to sales practices.”<sup>1172</sup>

Mr. Julian testified that the 2014 Audit Plan included a report about “High Risk Areas” and noted the Plan provided quantitative criteria regarding enterprise high-risk process and enterprise high risk RABU.<sup>1173</sup> He said, “to the extent that a process is deemed to be high risk is [*sic*] associated with 10 or more RABUs, meaning risk assessed business areas, then because of the nature and the prevalence of it across multiple RABUs, it would be deemed to be a high-risk process.”<sup>1174</sup>

Mr. Julian identified no part of the Audit Plan that indicated the Plan was designed to address sales practices misconduct at the Community Bank. Instead, he stated the Plan touched on sales practices that WFAS identified as high-risk – like Digital Channels, which “would have been an area with sales practices that was high-risk – or potential sales practices that was high risk. Regional banking, I think [it] would have an impact.”<sup>1175</sup>

Upon leading questioning by his attorney during direct examination, Mr. Julian was able to identify Wells Fargo Customer Connection as another RABU that was rated high-risk that had sales practices-type activities.<sup>1176</sup> There is in the record, however, no evidence suggesting that Community Bank’s sales practices misconduct were in any way related to Digital Sales or Wells Fargo Customer Connection.

Mr. Julian testified that under the 2014 Audit Plan, as Chief Auditor he “would have spent more of my time engaging in discussions and understanding the work being done.”<sup>1177</sup> He said the individual WFAS line of business audit groups would “identify key areas of focus within their line of business” and “would also take into account the significant risks identified through the ERM, regulatory matters that the regulators may have . . . raised during the course of their work and our dialogues.”<sup>1178</sup>

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<sup>1171</sup> Tr. (Julian) at 6444; R. Ex. 423.

<sup>1172</sup> Tr. (Julian) at 6420.

<sup>1173</sup> Tr. (Julian) at 6421-22; OCC Ex. 2107 at 17 (page 14 of the Plan).

<sup>1174</sup> Tr. (Julian) at 6422.

<sup>1175</sup> Tr. (Julian) at 6424-25.

<sup>1176</sup> Tr. (Julian) at 6425.

<sup>1177</sup> Tr. (Julian) at 6429.

<sup>1178</sup> Tr. (Julian) at 6429.

In the 2014 Audit Plan, key areas of focus included BSA/AML/OFAC compliance programs, corporate risk and regulatory reform, “model governance,” regulatory reporting, and “Third Party Change Management”.<sup>1179</sup> None of the key areas of focus referred to sales practices misconduct related to Community Bank team members. The only audits that arguably touched on the allegations in the L.A. Times article, according to Mr. Julian, were audits regarding Digital Channels and Customer Connections – and those were related only because they concerned activities by team members in the Community Bank – but were not related to the sales practices misconduct that is the focus of this administrative enforcement action.

Asked whether there was audit work – other than control testing – that WFAS was performing that touched upon the allegations in the L.A. Times article, Mr. Julian responded that “business monitoring was the critical aspect of audit’s work” and the 2014 Audit Plan “had enhanced or increased the activity with respect to business monitoring” in areas like “the Risk Committee of the Community Bank where Audit would be participating in discussions” and “other types of business monitoring.”<sup>1180</sup> Mr. Julian identified no documentation regarding these “other types” of business monitoring.

Although there is a paucity of evidence establishing that the 2014 Audit Plan addressed the risk issues presented by Mr. Bacon’s presentations or the third parties in the L.A. Times articles, Mr. Julian testified that as of the first quarter of 2014 the WFAS’s actions aligned with the relevant professional standards.

Well, the professional standards required that audit perform work based on, you know, risks, address significant risks, the work that's going on by the company to address those risks. Audit's plan was both to – included the performance of specific rated audits with respect to sales activity -- sales practices activity in certain lines of business as well as incorporated significant amount of businesses monitoring which, combined, that is responsive and in line with what the professional standards would require.<sup>1181</sup>

Under the 2014 Audit Plan, internal company growth was a factor when Internal Audit determined whether business monitoring rather than control testing was appropriate. Among the posted internal factors, the Plan stated that the “company continues to grow, evolve, and invest in new technologies and tools which lead to a high degree of change. This level of ongoing change has a significant impact on our audit plan decisions for deciding where to focus resources and the type of audit coverage to provide.”<sup>1182</sup>

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<sup>1179</sup> OCC Ex. 2107 at 26-27(pages 23-24 of the Plan).

<sup>1180</sup> Tr. (Julian) at 6431.

<sup>1181</sup> Tr. (Julian) at 6432.

<sup>1182</sup> OCC Ex. 2107 at 14 (page 11 of the Plan).

When such change is present, the Plan states that “[i]n many cases WFAS will engage in business monitoring or project audit activities as this more appropriately aligns with the life cycle of the project or initiative.”<sup>1183</sup>

In providing examples of internal factors – those reflecting key initiatives and changes – that “influenced our 2014 Audit Plan,” there is no mention of issues relating to sales practices misconduct like those issues presented by Mr. Bacon’s presentations or the 2013 L.A. Times article.<sup>1184</sup> The one oblique reference to “common processes within an individual Operating Committee Group” was a review of “cross-selling,” but that reference makes no mention of whether the Community Bank’s experiences with sales practices misconduct influenced the 2014 Audit Plan.

One point made very clear in the 2014 Audit Plan concerned the need to determine root causes of issues presented to Internal Audit. Among six “internal factors” that influenced the 2014 Audit Plan was the need for “[i]ssue monitoring for timely closure by business management and independent validation of 500+ open issues to ensure issues and root causes have been effectively addressed by business management, risk has been mitigated and actions are sustainable.”<sup>1185</sup>

Media focus, too, appears to be one of factors that influenced the 2014 Audit Plan – however, the Plan makes no mention of the issues raised by Mr. Bacon or the L.A. Times article. Instead, the Plan identified as an influence “[h]eightedened scrutiny from a regulatory and media focus has increased attention on indirect auto products and processes along with education financial services.”<sup>1186</sup>

Given that there clearly was heightened scrutiny from both regulators and from the media following the publication of the L.A. Times article in October through December 2013, WFAS’s failure in general and Mr. McLinko’s failure in particular to note such scrutiny as an influence into the 2014 Audit Plan is particularly troubling.

Asked during direct examination about the steps the OCC would take upon receipt of the 2014 Audit Plan, Mr. Julian described his understanding that “members of the OCC would meet with members of [WFAS’s] Operating Committee Groups. So those OCC members that had responsibilities for providing oversight over” for example, the Community Bank Operating Audit Group, “would meet with the leadership of the Line of Business Audit Group during the process of the development of plan where the Audit folks would share with the OCC progress being made in the development of the Plan, meaning what areas of focus, what audits were going to be performed.”<sup>1187</sup>

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<sup>1183</sup> OCC Ex. 2107 at 14 (page 11 of the Plan).

<sup>1184</sup> *Id.*

<sup>1185</sup> *Id.* at 15 (page 12 of the Plan).

<sup>1186</sup> *Id.* at 16 (page 13 of the Plan).

<sup>1187</sup> Tr. (Julian) at 6439.



The Supervisory Reviews section of the OCC’s Internal and External Audits from the Comptroller’s Handbook of April 2003 describes how its Examiners develop the appropriate scope for audit reviews.<sup>1188</sup> The Handbook instructs that the review of a bank’s audit function “should focus first on the internal audit program.”<sup>1189</sup> Examiners should “determine the program’s adequacy and effectiveness in assessing controls and following up on management’s actions to correct any noted control weaknesses.”<sup>1190</sup>

In order to undertake these preliminary reviews – in order to effectively determine the scope of the Examiner’s internal audit reviews, the Handbook requires that the Examiners review in-house and co-sourced internal audit activities – including the policies and processes in place, staffing resources, risk and control assessments, annual audit plans, schedules and budgets, the frequency of audits and audit cycles, individual audit work programs and audit reports, follow-up activities, and reports submitted to the audit committee.<sup>1191</sup>

Where, as here, the evidence reflects a lack of information material to sales practices misconduct being provided to the audit committees – particularly information known to Mr. McLinko and not disclosed to the A&E Committee following the publication of the October 2013 L.A. Times article – the risk of the OCC’s Examiners accepting the proposed and unduly limited scope of the 2014 Audit Plan is substantial. Applied to the record in this case, although it is clear Mr. Julian and Mr. McLinko both had the opportunity for “several dialogues” with the OCC Examiners,<sup>1192</sup> there is no evidence that either banker discussed with OCC Examiners the substantial and troubling evidence of sales practices misconduct reported both before and after the publication of the Times article.

#### **WFAS’s Presentation to the A&E Committee: August 4, 2014**

As noted above, during the March 4, 2013 TMMEC meeting, Michael Bacon, as head of Corporate Investigations, provided a corporation-wide report of investigations involving sales integrity violations.<sup>1193</sup> Mr. Julian testified that because that report was not limited to the Community Bank, and because he understood sales integrity violations to be “a much broader group of types of violations” than sales practices misconduct,<sup>1194</sup> he “reached out to Paul McLinko, who was the EAD, executive audit director, over the Community Bank to inquire as to what work the Community Bank . . . Audit Group was doing specific to sales integrity-type

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<sup>1188</sup> OCC Ex. 1909 at 49 (page 47 of the Handbook).

<sup>1189</sup> *Id.*, emphasis *sic*.

<sup>1190</sup> *Id.*

<sup>1191</sup> *Id.*

<sup>1192</sup> Tr. (Julian) at 6439.

<sup>1193</sup> OCC Ex. 2943; R. Ex. 800.

<sup>1194</sup> Tr. (Julian) at 6164.

activity within the Community Bank.”<sup>1195</sup> He asked Mr. McLinko “What work do we do related to team member fraud?”<sup>1196</sup>

Eighteen months after recognizing the need to determine whether controls by the Community Bank regarding team member sales practices misconduct were effective, Mr. Julian reported to the A&E Committee regarding compliance and financial crimes risks in Community Bank.<sup>1197</sup> Drawing from the prior ERM report of “noteworthy risks” (having evolved its nomenclature from what had been referred to as “significant enterprise risks”), the WFAS Second Quarter 2014 Summary presented to the A&E Committee made *no mention* of risks associated with team member misconduct in branch locations (i.e., the risks identified through the L.A. Times articles), but identified risks associated with Community Banking “in Wells Fargo Customer Connection and the Digital Channels Group.”<sup>1198</sup>

The focus of WFAS’s reviews “was on the sales practices and conduct to ensure customers are sold products meeting their financial needs. Both audits were rated Effective with no reportable issues.”<sup>1199</sup> A&E committee members also were told that “an assessment of cross-sell audit coverage is underway as part of the 2014 Community Bank audit plan.”<sup>1200</sup>

There is nothing in the record indicating that Mr. Julian disclosed that WFAS lacked the ability to distinguish cross-sell from the Community Bank’s overall sales activities – because, according to Ms. Russ Anderson, cross-sell “was inherent in the business practice.”<sup>1201</sup> During the hearing, Mr. Julian testified – without documentary support – that as a result, WFAS could not conduct a cross-sell specific review of the Community Bank analogous to audits conducted for other businesses.<sup>1202</sup> Preponderant evidence in the record does not support this factual claim.

Separately, there was no reference in the report to WFAS’s efforts to determine the root cause of the sales practices misconduct related to the L.A. Times article in the Executive Overview for the Second Quarter 2014.<sup>1203</sup> EthicsLine activity – reports by team members regarding violations of law or corporate policy – increased by eight percent (from 4,214 in 2013YTD to 4,536 in 2014YTD) – with 42% being referred to Community Bank Sales Quality.<sup>1204</sup>

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<sup>1195</sup> Tr. (Julian) at 6170-71.

<sup>1196</sup> R. Ex. 766 at 1.

<sup>1197</sup> R. Ex. 6584 at 52.

<sup>1198</sup> *Id.*

<sup>1199</sup> *Id.*

<sup>1200</sup> *Id.*

<sup>1201</sup> Tr. (Julian) at 6625.

<sup>1202</sup> Tr. (Julian) at 6625-26.

<sup>1203</sup> R. Ex. 6584 at 4-5.

<sup>1204</sup> *Id.* at 68.

One of the “Recurring themes” reported was “a lack of clear definition and understanding of roles and responsibilities between first and second lines of defense”.<sup>1205</sup> “Incentive compensation” was identified as an “emerging” trend, but nothing in the report suggested incentive compensation was related to sales practices misconduct in the Community Bank.<sup>1206</sup> “Customer complaints” were placed on the “Watch List” – without context or definition.<sup>1207</sup>

When asked during direct examination as of August 2014 what the Board of Directors for WF&C been advised about what was being done in response to the L.A. Times articles (beyond firing people), Mr. Julian responded without actually answering the question:

They had been advised and actually directed, Corporate Risk, to work with the Community Bank line of business to look into the issue, to identify root cause, to size the matter. So they were well aware of work that was going on by both Corporate Risk as well as the first line as well as work that was being performed by audit through our Wells Fargo Audit Services updates.<sup>1208</sup>

Taking that answer at face value, the record reflects that the Board of Directors gave instructions to Corporate Risk – as the Second Line of Defense – to work with the Community Bank line of business – as the First Line of Defense – to “look into the issue”.<sup>1209</sup> Nothing in this answer, however, responded to the question asked, as the response makes no reference to what advice had been given to the Board by August 2014, or by whom.

With no reference to the failure of Mr. McLinko, WFAS, or the Community Bank to identify the root cause of sales practices misconduct by Community Bank team members reported by the Times article, the August 2014 Quarterly Report included the following:

Community Banking risk remains heightened related to reputation and regulatory change. Ongoing media and regulatory scrutiny place additional pressure to ensure customers have a positive experience in all channels including stores, call centers, digital channels, and ATMs. This includes meeting the technology needs of the millennial generation as well as competing with non-bank entities.

The risk trend is stable, and Community Bank has taken appropriate measures to continuously evaluate and enhance channel usability to meet the needs of the customer. Additionally, Community Banking continues to evaluate product offerings, pricing, and sales strategies to ensure customers are

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<sup>1205</sup> *Id.* at 14.

<sup>1206</sup> *Id.*

<sup>1207</sup> *Id.*

<sup>1208</sup> Tr. (Julian) at 6588.

<sup>1209</sup> Tr. (Julian) at 6588.

obtaining the products and services that help them achieve their financial goals.<sup>1210</sup>

The Report noted that all audit reports issued throughout 2014 regarding the Community Bank have been rated “Effective”, and states that WFAS “has been actively monitoring various projects including Full Image Capture, Project ICE, Project EMV, Global Remittance Services Remittance Network, and Digital Channels Group Online Wires.”<sup>1211</sup> Nothing in this report suggests monitoring of controls the Community Bank put in place regarding the efficacy of risk-management controls addressing team member sales practices misconduct.

Mr. Julian testified that the reference to ERMC noteworthy risks in the WFAS Quarterly Report for the Second Quarter of 2014 “was an opportunity to, one, continue to escalate that information up to the A&E Committee, but also to provide the A&E Committee with some level of understanding around what activities [WFAS] was doing with respect to these risks.”<sup>1212</sup>

Notwithstanding that the L.A. Times articles did not address any team member misconduct arising out of either Customer Connection and the Digital Channels Group, Mr. Julian testified that WFAS was performing audit work with regard to sales practices issues identified in the L.A. Times articles.<sup>1213</sup> He testified that the reference presented in the August 2014 report to the A&E Committee “specifically identifies that two audits we had discussed previously, one in Customer Connection and the other in Digital Channels group had been completed.”<sup>1214</sup>

Mr. Julian testified that as of August 2014, WFAS was responding to issues raised in the L.A. Times articles: “there was a significant amount of business monitoring also going on with respect to sales practices activity and the work that was being performed . . . within the Community Bank as well as within the Corporate Risk area to address issues that have been raised.”<sup>1215</sup> He admitted, however, that even by August 2014 he did not inform the A&E Committee that the sales practices misconduct by Community Bank team members was either widespread or systemic.<sup>1216</sup>

Mr. Julian testified that by this time he still “had not seen evidence to support that.”<sup>1217</sup> He also offered no documentary evidence establishing that there was, in fact, a significant amount of business monitoring going on with respect to sales practices activity. Apart from this

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<sup>1210</sup> R. Ex. 6584 at 20.

<sup>1211</sup> *Id.* at 21.

<sup>1212</sup> Tr. (Julian) at 6574.

<sup>1213</sup> Tr. (Julian) at 6574-75.

<sup>1214</sup> Tr. (Julian) at 6575.

<sup>1215</sup> Tr. (Julian) at 6576-77.

<sup>1216</sup> Tr. (Julian) at 6579.

<sup>1217</sup> Tr. (Julian) at 6579.

testimony, which I found to be less than fully reliable with respect to his averments regarding business monitoring, the record does not by a preponderance establish a meaningful business monitoring effort was underway during the relevant period.

Mr. Julian noted that the Corporate Security results that were included in the August 2014 Quarterly Report showed a reduction in all forms of internal fraud and misconduct cases reported by Corporate Investigations – from 6,841 2013YTD cases to 6,555 2015YTD cases (a 4% reduction).<sup>1218</sup> The report also showed, however, that for all major lines of business, cases involving Community Bank’s team members *far exceeded* all other lines of business (Community Bank had 5,724 cases – including 1,540 for Sales Integrity Violations; Consumer Lending had 487 cases; Wealth, Brokerage and Retirement had 188 cases; Wholesale had 71 cases; and Technology and Operations had 63 cases).<sup>1219</sup>

Mr. Julian testified that in construing the data presented in this report, he “understood it to be an implication, if you will, of what I understood that there was more work going on around the controls and the awareness of the issues. And that the cases were improving, in part, I believed as a result of additional focus in controls – enhanced controls.”<sup>1220</sup> Nothing in the data, however, supported the understanding that “there was more work going on” regarding risk-management controls.

Similarly, where the data reflected a seven percent increase in terminations and resignations, Mr. Julian testified that, while they were increasing, “they weren’t increasing significantly”, and

while they were increasing, I didn’t know whether potentially that was just a timing issue, meaning were some of those terminations a result of investigations that had happened in the prior year. But, nonetheless, it indicated that while – that while cases were going down, terminations were continuing, and the work was being done to identify and root out the issues that were identified.<sup>1221</sup>

He did not, however, identify *which controls* were responsible for the cases identified in this Quarterly report, nor is there evidence in the record that there was a causal relationship between whatever controls may have been in place and either the reduction in cases or the increase in terminations and resignations.

**WFAS’s Presentation to the A&E Committee: November 18, 2014**

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<sup>1218</sup> R. Ex. 6584 at 64.

<sup>1219</sup> *Id.* at 67.

<sup>1220</sup> Tr. (Julian) at 6581.

<sup>1221</sup> Tr. (Julian) at 6581-82.

Mr. Julian made a presentation during the November 18, 2014 meeting of the A&E Committee.<sup>1222</sup> Nothing in the minutes of this meeting, however, suggest or report any presentation by Audit concerning issues arising from the L.A. Times articles.<sup>1223</sup>

The meeting minutes do reflect that Mr. Julian distributed in advance of the meeting WFAS's Third Quarter 2014 Summary.<sup>1224</sup> When asked to describe the audit work WFAS was doing at this time with respect to sales practices issues at the Community Bank, Mr. Julian testified that the Summary described risk within the Community Bank as "heightened and increasing relative to reputation and regulatory environment."<sup>1225</sup> The report stated that "[c]hanging products, delivery methods, and technology, along with ongoing media and regulatory scrutiny, place additional pressure on management to ensure customers have a positive experience in all channels (including stores, call centers, digital channels, and ATMs)."<sup>1226</sup>

Mr. Julian testified that given the sales practices misconduct allegations that had been made in the L.A. Times article, "the work that was going on to understand the issues that were raised, [and] the regulators were involved in discussions around that activity."<sup>1227</sup> As such, WFAS "determined that it was heightened and increasing, the risk within the Community Bank."<sup>1228</sup>

Asked to state his understanding of what the Community Bank itself was doing in terms of ensuring the propriety of sales activity, without providing any details Mr. Julian responded:

So the Community Bank was taking measures to evaluate and enhance its channel for usability, to ensure that the products offered met the customers' needs. They were evaluating product offering -- "they" being the Community Bank was evaluating product offerings, pricing. Various activities with respect to sales practices.<sup>1229</sup>

Asked how he knew in November 2014 these types of activities were occurring at the Community Bank, Mr. Julian stated:

Through the enhanced business monitoring that was taking place by -- by the line of business audit group, specifically Paul McLinko and his team, as well as through my engagement in various different discussions at the

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<sup>1222</sup> Tr. (Julian) at 6596; R. Ex. 20604.

<sup>1223</sup> R. Ex. 20604 at 3-4.

<sup>1224</sup> Tr. (Julian) at 6599; R. Ex. 7138; R. Ex. 7136.

<sup>1225</sup> Tr. (Julian) at 6600; R. Ex. 7138 at 22.

<sup>1226</sup> R. Ex. 7183 at 22.

<sup>1227</sup> Tr. (Julian) at 6600.

<sup>1228</sup> Tr. (Julian) at 6600.

<sup>1229</sup> Tr. (Julian) at 6601.

committee level and board level and one-on-one discussions with the line of business management.<sup>1230</sup>

As was true with the August 2014 Quarterly Report,<sup>1231</sup> there was no reference to the failure of either WFAS, Mr. McLinko (or the CBO audit team), or the Community Bank to identify the root cause of sales practices misconduct by Community Bank team members reported by the Times article; indeed there was no reference to *any* efforts being attempted by WFAS with regard to those issues. Much of the narrative in the November 2014 Quarterly Report is substantially the same as what was presented in the August 2014 Quarterly Report.<sup>1232</sup>

### **WFAS's Presentation to the A&E Committee: February 24, 2015**

Mr. Julian identified the minutes and WFAS's submissions for the February 24, 2015 A&E Committee meeting.<sup>1233</sup> He testified that the Committee approved the Audit Plan and Audit Charter for 2015, and through leading questioning by his attorney during direct examination indicated that over the "20 or 30" meetings he had each year he had "extensive opportunity to interact with the Board members concerning" the WFAS quarterly summaries.<sup>1234</sup>

Nothing in the Minutes presented red flags regarding sales practices misconduct by team members of the Community Bank. To the contrary, under Mr. McLinko's direction, the Internal Auditor's Update stated, "overall the Company's systems of control are well managed".<sup>1235</sup> Nothing in the Board's minutes approving either the WFAS Charter or the 2015 Audit Plan indicated concerns had been brought to their attention regarding sales practices misconduct.<sup>1236</sup> Similarly, the minutes are silent with respect to any key policy or procedure changes in the 2015 Audit Plan relating to controls testing or business monitoring related to sales practices misconduct.<sup>1237</sup>

### **WFAS Audit Engagement Report: Community Banking – Regional Banking (RB-SOCR)**

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<sup>1230</sup> Tr. (Julian) at 6601.

<sup>1231</sup> R. Ex. 6584 at 20.

<sup>1232</sup> *Id.*: "Community Banking risk remains heightened related to reputation and regulatory change. Ongoing media and regulatory scrutiny place additional pressure to ensure customers have a positive experience in all channels including stores, call centers, digital channels, and ATMs. This includes meeting the technology needs of the millennial generation as well as competing with non-bank entities. The risk trend is stable, and Community Bank has taken appropriate measures to continuously evaluate and enhance channel usability to meet the needs of the customer. Additionally, Community Banking continues to evaluate product offerings, pricing, and sales strategies to ensure customers are obtaining the products and services that help them achieve their financial goals."

<sup>1233</sup> Tr. (Julian) at 6646-59; R. Ex. 8414 (Minutes); R. Ex. 604 (2015 Audit Plan); R. Ex. 7988 (transmittal email); R. Ex. 1518 (WFAS Fourth Quarter Summary, proffer only).

<sup>1234</sup> Tr. (Julian) at 6657; R. Ex. 8414 at 2.

<sup>1235</sup> R. Ex. 8414 at 1.

<sup>1236</sup> *Id.* at 2.

<sup>1237</sup> R. Ex. 604 at 29-30.

## March 30, 2015

Through its Audit Engagement Report of March 30, 2015, WFAS notified the Community Bank that the quality assurance functions of the Regional Banking Store Operations Control Review (SOCR) and its Business Banking Operations Control Review (BOCR) needed improvement.<sup>1238</sup> Prior to this time WFAS “use[d] the results of SOCR/BOCR as part of our Leverage Program in determining annual audit coverage.”<sup>1239</sup> Its March 30, 2015 report included reviews of Governance and Structure; Review Execution; Independence/Objectivity; Competency; and Management Reporting.<sup>1240</sup>

In addition, the audit program included “five processes specifically reviewed by the SOCR/BOCR team.” These processes “correlate to the WFAS processes of move money, account setup, service customers and accounts, receiving/posting payments, and manage physical security.”<sup>1241</sup> The audit report noted, however, that the review “did not test the effectiveness of the store controls but rather assessed if the QA function is performed as intended.”<sup>1242</sup>

While finding controls related to SOCR/BOCR’s governance, structure, independence and objectivity “are adequate to ensure appropriate coverage of business operational and regulatory risks,” WFAS found “accuracy and completeness of program execution and supervisory review ‘Needs Improvement’ to ensure testing is sufficient, relevant, and reliable.”<sup>1243</sup> The fact that impact and severity of the issue was rated by WFAS as “High” indicated the auditor’s judgment that the issue “needs a higher level of senior management attention with an increased urgency to address it.”<sup>1244</sup>

The auditors noted in particular “issues regarding sampling, missed errors (*i.e.*, errors identified by WFAS, but not by SOCR/BOCR), inadequate workpaper documentation, inadequate supervision and review of work papers, and ineffective methods used to evidence and provide feedback to QAAs.”<sup>1245</sup> Based on these findings, going forward from March 2015, at Mr. McLinko’s recommendation WFAS “began performing its own testing and eventually designed processes to do in-branch work itself.”<sup>1246</sup>

Mr. Julian testified that up to this point, WFAS “leveraged the work that SOCR and BOCR was [*sic*] doing with respect to SOCR and BOCR actually going into the stores and into

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<sup>1238</sup> R. Ex. 523 at 2.

<sup>1239</sup> *Id.*

<sup>1240</sup> *Id.*

<sup>1241</sup> *Id.*

<sup>1242</sup> *Id.*

<sup>1243</sup> *Id.*

<sup>1244</sup> Tr. (Julian) at 6668-69.

<sup>1245</sup> R. Ex. 523 at 2.

<sup>1246</sup> Tr. (Julian) at 6670.



the banking centers to perform control testing”; while WFAS would only “audit the governance that those groups were employing to perform those activities.”<sup>1247</sup> He testified that up to this point, WFAS “wasn’t personally or specifically going into the branches or the banking centers to perform the work, where Audit was leveraging the work of those two units.”<sup>1248</sup>

When asked why WFAS used the work of the SOCR and BOCR units rather than directly and independently going into Community Bank’s branches and stores, Mr. Julian responded only that “that’s the practice that had been employed” when he came on board as Chief Auditor.”<sup>1249</sup> Without offering any supporting documentation establishing what he actually knew about this mode of audit coverage, he said “based on what I knew, [I] didn’t have any concerns about leveraging their activities, because I knew that [WFAS] was assessing their work and concluding that [WFAS] could rely on their work.”<sup>1250</sup>

Mr. Julian described this approach as “an opportunity to leverage work that was going on already” by the first line of defense, adding, “it wouldn’t have made a lot of sense for Audit to duplicate that work”.<sup>1251</sup> Asked on direct examination whether Wells Fargo was unique in leveraging in-store first line of defense functions like SOCR and BOCR, Mr. Julian responded, again without supporting documentation, that “probably 50/50. Some of the peer banks chose to do that work themselves, meaning within their audit group. . . . [but] the majority of the larger banks, the three or four sort of mega banks at the time were generally more aligned with [WFAS] in that practice.”<sup>1252</sup>

Asked on direct examination whether WFAS Audit relied on other first line of defense testing functions, Mr. Julian responded, again without any supporting documentation and without reference to IIA standards regarding audit independence:

Absolutely. Throughout the -- I'm sorry. Excuse me. Throughout the company, there were a number of different testing activities that went on, not just in the first line, but also in the second line -- excuse me -- where audit would rely on those activities. Corporate investigations, as we discussed, is another activity that rather than audit performing the investigations themselves, they would rely on corporate investigations to perform that work and would be able to leverage it. So there were a number of different activities that Wells Fargo Audit Services would leverage with respect to control testing and control-type activities.<sup>1253</sup>

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<sup>1247</sup> Tr. (Julian) at 6663.

<sup>1248</sup> Tr. (Julian) at 6663.

<sup>1249</sup> Tr. (Julian) at 6663.

<sup>1250</sup> Tr. (Julian) at 6663.

<sup>1251</sup> Tr. (Julian) at 6664.

<sup>1252</sup> Tr. (Julian) at 6665-66.

<sup>1253</sup> Tr. (Julian) at 6666.

## WFAS's Presentation to the A&E Committee: April 17, 2015

In direct examination, Mr. Julian identified documents that had been prepared for and presented during the April 17, 2015 A&E Committee meeting.<sup>1254</sup> During this testimony, Mr. Julian did not describe presentations he made during the meeting, although the Chief Auditor's Report in included in the minutes.<sup>1255</sup> Instead, he spoke of testimony and documents by Jim Richards, who he said was responsible "overall for the Financial Crimes area" and "had also taken responsibility for Corporate Investigations."<sup>1256</sup>

The line of questioning focused on steps being taken by Mr. Richards relating to team member resignations or terminations based on "confirmed fraud."<sup>1257</sup> Mr. Julian opined that Mr. Richards through his presentations to the A&E Committee was "conveying that he had questions with respect to the data" regarding resignations and terminations of team members.<sup>1258</sup> Mr. Julian testified that Mr. Richards "was stating that he wasn't able to reconcile, if you will . . . team member terminations or resignations with respect to confirmed fraud with that of the SAR information that he was familiar with."<sup>1259</sup>

Relevant to the issues presented but not discussed during Mr. Julian's direct examination, however, are the statements presented to the Committee as recorded in the Chief Auditor's Report.<sup>1260</sup> Mr. Julian's report to the Committee was relevant for what was *absent* from that report: Nothing in the comments attributed to Mr. Julian, WFAS, or the CBO concerned sales practices misconduct or the WFAS efforts to determine the efficacy of Community Bank's risk-management controls testing regarding such misconduct.<sup>1261</sup>

The minutes reflect a report by Mark Links, identified by Mr. Julian as "a direct report of mine who had responsibility for providing audit oversight over corporate risk and had responsibility for the process by which the ERMA was conducted."<sup>1262</sup> Here again, Mr. Links' report to the Committee is relevant for what was absent from the WFAS 2014 Enterprise Risk Management Assessment.<sup>1263</sup>

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<sup>1254</sup> Tr. (Julian) at 6617-82; R. Ex. 9232 (Meeting minutes); R. Ex. 9665 (1Q2015 Status Report of the BSA Officer & Financial Crimes Risk Management (FCRM)).

<sup>1255</sup> Tr. (Julian) at 6617-82.

<sup>1256</sup> Tr. (Julian) at 6672-81; R. Ex. 9665.

<sup>1257</sup> Tr. (Julian) at 6672-74.

<sup>1258</sup> Tr. (Julian) at 6674

<sup>1259</sup> Tr. (Julian) at 6675.

<sup>1260</sup> R. Ex. 9232 at 5.

<sup>1261</sup> *Id.*

<sup>1262</sup> Tr. (Julian) at 6681; R. Ex. 9232 at 5.

<sup>1263</sup> R. Ex. 9232 at 5; R. Ex. 8524.

The Assessment reported that the “Enterprise Risk Management” needed improvement.<sup>1264</sup> Notwithstanding the failure thus far of WFAS to identify any root causes for the sales practices misconduct activity in the Community Bank, the report was silent regarding audit activity relating to Community Banking and continued to rate its first line of defense “Satisfactory” for Operational Risk and Compliance Risk.<sup>1265</sup>

Mr. Julian denied that these limitations warranted a lower than Satisfactory rating, in these terms: “At the time, I was aware of allegations of sales practices – undue pressure and undue sales pressure, but yet the work was going on to root that out to determine . . . if those were isolated incidents or if they were prevalent across the Community Bank. More importantly, the Community Bank, again, as I mentioned, was aware of the issues. They were addressing the issues.”<sup>1266</sup>

Further, Mr. Julian testified that the Satisfactory rating took into account “the culture of the Community Bank [but] not the culture of their activities specific to sales practices. This takes into account all of the culture across the Community Bank.”<sup>1267</sup> Notwithstanding the lack of understanding by Mr. McLinko or Mr. Julian to the root cause of the sales practices misconduct at the Community Bank, Mr. Julian testified that he “had no information that would cause” him to disagree with the Assessment awarding Community Bank a “Strong” rating for Culture.<sup>1268</sup>

Mr. Julian testified that the Assessment was based on the “bottoms up” process coming from the team led by Mr. McLinko.<sup>1269</sup> He said “sales practices risk is one type of risk activity that the first and the second line had governance activities over” and that “it was necessary to rely and appropriate to rely on the line of business audit groups who were much closer to the organization that they were assessing.”<sup>1270</sup>

Neither the Assessment nor Mr. Links’ presentation identified any WFAS’s efforts at addressing risk practices attributable to sales practices misconduct in the Community Bank that warranted presentation to the Committee.<sup>1271</sup>

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<sup>1264</sup> Tr. (Julian) at 6683; R. Ex. 8524 at 2.

<sup>1265</sup> R. Ex. 8524 at 3. The Assessment noted “opportunities for improvement” at the Community Bank for Credit Risk, including leveraged lending – activity not related to the present enforcement action.

<sup>1266</sup> Tr. (Julian) at 6689-90; see also “22-03-07 Respondents’ Amended Revised Errata Days 9 -38” at page 52. Ordered through Second Supplemental Order Regarding Hearing Transcript Errata.

<sup>1267</sup> Tr. (Julian) at 6690.

<sup>1268</sup> Tr. (Julian) at 6690.

<sup>1269</sup> Tr. (Julian) at 6690-91.

<sup>1270</sup> Tr. (Julian) at 6691-92.

<sup>1271</sup> Tr. (Julian) at 6686; R. Ex. 9232 at 5.

Mr. Julian's Counsel asked whether Mr. Julian thought at that time the Community Bank should receive a lower risk management rating, and Mr. Julian responded "No."<sup>1272</sup>

Elaborating on this response, Mr. Julian testified:

Well, because information I had received at the time, first starting back – all the way back to the L.A. Times article where team members were displaced, as I've stated before, the controls are what identified the behavior that resulted in team members being displaced. And, therefore, the controls, based on that, were working. I also knew that as a result of the allegations that had occurred, there was a significant amount of work [going] on within the Community Bank to address sales practices allegations and issues that were raised. Based on the information that I had, that work was being performed diligently in good faith. Part of rating a control environment is . . . assessing whether or not management's aware of an issue and also whether or not management is taking the appropriate steps to address the issue. At this time, based on the information I had seen and heard, I felt that the rating was appropriate based on that information.<sup>1273</sup>

Substantial, probative, and preponderant evidence in the record established, however, that the referenced team members were not "displaced" – they were *fired* by the hundreds each year during the relevant period.

#### **WFAS's Presentation to the A&E Committee: May 4, 2015**

Mr. Julian identified the minutes from the A&E Committee's May 4, 2015, and acknowledged that he presented WFAS's First Quarter 2015 Report (which had been distributed to Committee members in advance of the meeting).<sup>1274</sup> There is no mention in the meeting minutes of any action being recommended or taken with respect to WFAS taking steps to determine the efficacy of controls that had been discussed by Ms. Tolstedt during the April 28, 2015 meeting of the Board's Risk Committee.<sup>1275</sup>

When presented during his direct testimony with a copy of the WFAS First Quarter 2015 Report, Mr. Julian identified no part of that report that was responsive to issues presented during the April 28, 2015 Risk Committee meeting.<sup>1276</sup> Further, Mr. Julian identified nothing during his direct testimony suggesting WFAS or Mr. McLinko had taken any steps to determine whether Community Bank's Risk Management Team had implemented effective controls testing

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<sup>1272</sup> Tr. (Julian) at 6687.

<sup>1273</sup> Tr. (Julian) at 6687-88.

<sup>1274</sup> Tr. (Julian) at 6697-6700; R. Ex. 20620 (Minutes of the A&E May 4, 2015 Committee meeting) at 3; R. Ex. 8510 (WFAS First Quarter 2015 Summary); R. Ex. 8552 (transmittal email).

<sup>1275</sup> Tr. (Julian) at 6694; OCC Ex. 1101-R.

<sup>1276</sup> Tr. (Julian) at 6697.

regarding the known risks related to team member sales practices misconduct at the Community Bank.<sup>1277</sup>

### **WFAS's Responses to the City of Los Angeles Complaint – May 4, 2015**

On May 4, 2015, acting on behalf of the State of California, the Los Angeles City Attorney filed suit in the Superior Court for the County of Los Angeles, naming as Defendants both WF&C and Wells Fargo Bank, N.A.<sup>1278</sup> The suit sought equitable relief and civil penalties against the Defendants for violations of the California Unfair Competition Law for Gaming and for Failure to Provide Notice of Data Breach.<sup>1279</sup>

In its lead allegation, the City presented the following narrative:

For years, Wells Fargo & Company and Wells Fargo Bank, National Association (collectively “Wells Fargo”) have victimized their customers by using pernicious and often illegal sales tactics to maintain high levels of sales of their banking and financial products. The banking business model employed by Wells Fargo is based on selling customers multiple banking products, which Wells Fargo calls “solutions.” In order to achieve its goal of selling a high number of “solutions” to each customer, Wells Fargo imposes unrealistic sales quotas on its employees, and has adopted policies that have, predictably and naturally, driven its bankers to engage in fraudulent behavior to meet those unreachable goals. As a result, Wells Fargo’s employees have engaged in unfair, unlawful, and fraudulent conduct, including opening customer accounts, and issuing credit cards, without authorization. Wells Fargo has known about and encouraged these practices for years. It has done little, if anything, to discourage its employees’ behavior and protect its customers. Worse, on the rare occasions when Wells Fargo did take action against its employees for unethical sales conduct, Wells Fargo further victimized its customers by failing to inform them of the breaches, refund fees they were owed, or otherwise remedy the injuries that Wells Fargo and its bankers have caused. The result is that Wells Fargo has engineered a virtual fee-generating machine, through which its customers are harmed, its employees take the blame, and Wells Fargo reaps the profits.<sup>1280</sup>

Noteworthy for the purposes of this Recommendation are the following allegations:

From Complaint, ¶ 4:

Wells Fargo boasts about the average number of products held by its customers, currently approximately six bank accounts or financial products

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<sup>1277</sup> Tr. (Julian) at 6696-6701.

<sup>1278</sup> R. Ex. 168.

<sup>1279</sup> *Id.* at 1.

<sup>1280</sup> *Id.* at 3.

per customer. Wells Fargo seeks to increase this to an average of eight bank accounts or financial products per account holder, a company goal Wells Fargo calls the “Gr-eight” initiative.<sup>1281</sup>

From Complaint, ¶5:

Wells Fargo quotas are difficult for many bankers to meet without resorting to the abusive and fraudulent tactics described further below. . . . Those failing to meet daily sales quotas are approached by management, and often reprimanded and/or told to “do whatever it takes” to meet their individual sales quotas. Consequently, Wells Fargo managers and bankers have for years engaged in practices called “gaming.” Gaming consists of, among other things, opening and manipulating fee-generating customer accounts through often unfair, fraudulent, and unlawful means, such as omitting signatures and adding unwanted secondary accounts to primary accounts without permission.<sup>1282</sup>

From Complaint, ¶6.

Wells Fargo’s gaming practices have caused significant stress to, and hardship and financial losses for, its customers. Specifically, Wells Fargo has (a) withdrawn money from customers’ authorized accounts to pay for the fees assessed by Wells Fargo on unauthorized accounts opened in customers’ names; (b) placed customers into collections when the unauthorized withdrawals from customer accounts went unpaid; (c) placed derogatory information in credit reports when unauthorized fees went unpaid; (d) denied customers access to their funds while Wells Fargo stockpiled account applications; and (e) caused customers to purchase identity theft protection.<sup>1283</sup>

From Complaint, ¶8.

While Wells Fargo has ostensibly terminated a small number of employees who have engaged in gaming, other employees have been rewarded for these practices, and even promoted, perpetuating the problem. Moreover, Wells Fargo has continued to impose the same companywide goals of attaining as many accounts as possible at any expense, thereby fostering the practice of gaming. Wells Fargo thus puts its employees between a rock and a hard place, forcing them to choose between keeping their jobs and opening unauthorized accounts.<sup>1284</sup>

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<sup>1281</sup> *Id.* at 4.

<sup>1282</sup> *Id.*

<sup>1283</sup> *Id.* at 5.

<sup>1284</sup> *Id.*

The Complaint alleged violations of specific state laws. These included willfully obtaining personal identifying information for unlawful purposes – including obtaining or attempting to obtain credit, goods, or services without the consent of that person;<sup>1285</sup> being a party to a fraudulent conveyance;<sup>1286</sup> knowingly accessing and without permission using data to execute a scheme to defraud or wrongfully obtain money,<sup>1287</sup> and knowingly accessing and without permission making use of customer information.<sup>1288</sup>

The Complaint alleged specific *unfair* business acts, including violations of “established public policy of the State of California which, among other things, seeks to ensure that: all monetary contracts are duly authorized by each party; all bank accounts are authorized and agreed to by the customer in whose name the bank account is opened; residents of the state are not harmed in their credit reports by acts not actually performed, or debts not actually incurred by that resident; personal information of an individual is not improperly obtained and used for an unlawful purpose; and that when personal information is obtained without authority, that the person whose information was obtained is informed immediately.”<sup>1289</sup>

The Complaint alleged specific *fraudulent* business practices, including using misrepresentations, deception, and concealment of material information to view customers’ personal information, open unauthorized accounts in its customers’ names, and then fail to reveal to the customers that their personal information was compromised.<sup>1290</sup>

When initially asked during direct examination whether he actually saw the Complaint around the time it was filed, Mr. Julian testified “I don’t recall if I did or didn’t.”<sup>1291</sup> After his Counsel refreshed his recollection by showing him a copy of the OCC’s email to him dated May 6, 2015 with the subject “L.A. Times Article” accompanied by his own email to Mr. McLinko also on May 6, 2015, where Mr. McLinko responded that he would “be happy to provide additional color,” Mr. Julian amended his response testifying that indeed, “Mr. Linskens had emailed me requesting a meeting to discuss the L.A. Times article and the City of L.A. lawsuit.”<sup>1292</sup>

Shortly after Mr. Julian received Mr. Linskens’ May 6, 2015 email, Mr. McLinko sent an email to Mr. Julian reporting that through Mike DeClue, the OCC “indicated they were

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<sup>1285</sup> R. Ex. 168 at 16, ¶55, citing California Business and Professions Code § 17200, et seq., and Penal Code section 530.5, subdivision (a).

<sup>1286</sup> R. Ex. 168 at 16, ¶55, citing Penal Code section 531.

<sup>1287</sup> R. Ex. 168 at 16, ¶55, citing Penal Code section 502, subdivision (c)(1).

<sup>1288</sup> R. Ex. 168 at 16, ¶55, citing 15 United States Code 680, et seq. and rules and regulations promulgated thereunder.

<sup>1289</sup> R. Ex. 168 at 17, ¶56.

<sup>1290</sup> R. Ex. 168 at 17-18, ¶56.

<sup>1291</sup> Tr. (Julian) at 6711.

<sup>1292</sup> Tr. (Julian) at 6712; R. Ex. 168 (Complaint); R. Ex. 8663 (email).

comfortable with our audit coverage (from the work they did as part of the review of the Community Bank [Group Risk Officer – Claudia Russ Anderson] function) and wanted to see a timeline of our audit activities (from 2013 forward).” Mr. McLinko attached to the email a one-page timeline that had been provided to the OCC “in the past in another form”.<sup>1293</sup>

Mr. Julian described the one-page document as “communicating to the OCC the various work that Audit had performed related to sales coverage”.<sup>1294</sup> He testified that the document was from the OCC’s February 2015 examination, and identified the document as “WFAS Community Bank sales practice coverage covering 2013 to 2015”.<sup>1295</sup> Mr. Julian testified, however, that he would not have reviewed each of the audits listed in this document, because “my practice was to review those audits that reached a ‘needs improvement’ or an ‘unsatisfactory’ audit rating versus reviewing those that received an ‘effective’ audit rating.”<sup>1296</sup>

Mr. Julian was shown the WFAS Community Bank Sales Coverage report for February 2015 prepared by Mr. McLinko and Bart Deese, and testified that he would have reviewed the report during communications with Mr. McLinko and Mr. Deese.<sup>1297</sup> He said the coverage report described both audit work (including rated audit reports and control testing) and business monitoring, and that when he reviewed the report it “appeared to be thorough, appropriate level of coverage on the issues that I knew and the risks that I knew.”<sup>1298</sup> He denied, however, that the coverage report included all of the business monitoring that WFAS was performing related to sales practices in the wake of the L.A. Times articles.<sup>1299</sup> He said, for example, that it did not reflect the “the business monitoring that I participated in, in my role as Chief Auditor.”<sup>1300</sup> Through his testimony, however, Mr. Julian offered no substantial documentary evidence supporting the inference that Mr. Julian performed *any* business monitoring in his role as Chief Auditor.

### **Impact of the OCC’s “Heightened Standards”**

Mr. Julian identified the OCC’s “Guidelines Establishing Heightened Standards for Certain Large Insured National Banks”<sup>1301</sup> Effective in November 2014, Mr. Julian stated the Standards did not change Audit’s responsibilities for conducting root cause analysis.<sup>1302</sup> He said

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<sup>1293</sup> Tr. (Julian) at 6713-16; R. Ex. 8654 at 1.

<sup>1294</sup> Tr. (Julian) at 6716-17; R. Ex. 19393.

<sup>1295</sup> Tr. (Julian) at 6717.

<sup>1296</sup> Tr. (Julian) at 6718.

<sup>1297</sup> Tr. (Julian) at 6718-19; R. Ex. 8656.

<sup>1298</sup> Tr. (Julian) at 6719.

<sup>1299</sup> Tr. (Julian) at 6721.

<sup>1300</sup> Tr. (Julian) at 6721.

<sup>1301</sup> Tr. (Julian) at 6368; OCC Ex. 931.

<sup>1302</sup> Tr. (Julian) at 6368; OCC Ex. 931 at 18-19.



that Audit “isn’t a roving root cause detector,” and described WFAS’s responsibility with respect to root causes – before and after the Heighten Standards became effective – “was to identify root cause to the extent . . . an issue was identified in the course of its audit work, in carrying out its Audit Plan. That’s consistent with what the Heighten Standards here articulate.”<sup>1303</sup>

The Standards, however, do not limit Audit’s role to determining the root causes of issues identified only in the course of WFAS’s audit work. Pertinent to this analysis is the description of the role and responsibilities of Internal Audit presented in the Heighten Standards:

3. Role and Responsibilities of Internal Audit. In addition to meeting the standards set forth in appendix A of part 30, **internal audit should ensure that the covered bank's risk governance framework complies with these Guidelines and is appropriate for the size, complexity, and risk profile of the covered bank.** In carrying out its responsibilities, internal audit should:

(a) Maintain a complete and current inventory of all of the covered bank's material processes, product lines, services, and functions, and **assess the risks, including emerging risks, associated with each, which collectively provide a basis for the audit plan described in paragraph II.C.3.(b) of these Guidelines;**

(b) **Establish and adhere to an audit plan that is periodically reviewed and updated that takes into account the covered bank's risk profile, emerging risks, and issues, and establishes the frequency with which activities should be audited.** The audit plan should require internal audit to evaluate the adequacy of and compliance with policies, procedures, and processes established by front line units and independent risk management under the risk governance framework. Significant changes to the audit plan should be communicated to the board's audit committee;

(c) Report in writing, conclusions and material issues and recommendations from audit work carried out under the audit plan described in paragraph II.C.3.(b) of these Guidelines to the board's audit committee. **Internal audit's reports to the audit committee should also identify the root cause of any material issues and include:**

(i) **A determination of whether the root cause creates an issue that has an impact on one organizational unit or multiple organizational units within the covered bank; and**

(ii) **A determination of the effectiveness of front line units and independent risk management in identifying and resolving issues in a timely manner;**

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<sup>1303</sup> Tr. (Julian) at 6368-69.

(d) Establish and adhere to processes for independently assessing the design and ongoing effectiveness of the risk governance framework on at least an annual basis. The independent assessment should include a conclusion on the covered bank's compliance with the standards set forth in these Guidelines; [Note 3: The annual independent assessment of the risk governance framework may be conducted by internal audit, an external party, or internal audit in conjunction with an external party.]

**(e) Identify and communicate to the board's audit committee significant instances where front line units or independent risk management are not adhering to the risk governance framework;**

(f) Establish a quality assurance program that ensures internal audit's policies, procedures, and processes comply with applicable regulatory and industry guidance, are appropriate for the size, complexity, and risk profile of the covered bank, are updated to reflect changes to internal and external risk factors, emerging risks, and improvements in industry internal audit practices, and are consistently followed;

(g) Develop, attract, and retain talent and maintain staffing levels required to effectively carry out its role and responsibilities, as set forth in paragraphs II.C.3.(a) through (f) of these Guidelines;

(h) Establish and adhere to talent management processes that comply with paragraph II.L. of these Guidelines; and

(i) Establish and adhere to compensation and performance management programs that comply with paragraph II.M. of these Guidelines.<sup>1304</sup>

Thus, under Appendix D, WFAS, Mr. McLinko, and Mr. Julian had the responsibility to ensure that Internal Audit's reports to the WF&C A&E Committee “identify the root cause of any material issues” and must include both a “determination of whether the root cause creates an issue that has an impact on one organizational unit or multiple organizational units within the covered bank,” and a determination of “the effectiveness of front line units and independent risk management in identifying and resolving issues in a timely manner.”<sup>1305</sup>

Mr. Julian’s opinion that “Audit’s responsibility is to identify the root cause to the extent that Audit identifies those issues in the course of its audit work”<sup>1306</sup> is not supported by the authority cited in his testimony – and is directly inconsistent with that authority. It is irrelevant whether at any time during the relevant period – particularly after the issuance to the A&E

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<sup>1304</sup> 12 C.F.R. § Pt. 30, App. D.

<sup>1305</sup> *Id.*

<sup>1306</sup> Tr. (Julian) at 6369.

Committee of the January 2014 ERMC report – any member of the A&E Committee or the Board directed Mr. Julian or WFAS to determine the root cause of the sales conduct issue.<sup>1307</sup>

By the November 10, 2014 effective date of Appendix D, Mr. McLinko and Internal Audit under Mr. Julian’s direction had an affirmative obligation to identify the root cause of *any* material issue, through an analysis that included both a determination of whether the root cause creates an issue that has an impact on one organizational unit or multiple organizational units within Wells Fargo Bank, N.A.; and a determination of the effectiveness of front line units and independent risk management in identifying and resolving issues in a timely manner.

It also is irrelevant that Mr. Julian understood in January 2014 that others at Wells Fargo were taking action concerning the issues raised in the L.A. Times articles.<sup>1308</sup> On this point, Mr. Julian testified that “Corporate Risk was . . . directed by the Risk Committee to lead the effort with respect to investigating the issues raised” by the articles.<sup>1309</sup> He testified that through “all of 2014 into 2015, probably up until the time that the five MRAs were issued by the OCC,” Corporate Risk was “directed to work with the Community Bank in addressing the issues, which included determining or identifying root cause, to size and scope the issues.”<sup>1310</sup>

Mr. Julian testified that in addition to the work of Corporate Risk, there was a “core team” that was working to “understand the underlying issues and the allegations that had been made with respect to sales practices.”<sup>1311</sup> He said he had no say in who should be on the core team, and that he personally was not part of the team.<sup>1312</sup>

Mr. Julian testified that beyond the work of the core team and Corporate Risk, the Community Bank itself “was working to understand the underlying issues that were identified in the L.A. Times articles. They were looking to understand the control or to look at the controls and, to the extent possible, enhance the controls.”<sup>1313</sup> He said this work “started late 2013 after the L.A. Times article and continued as well into 2015,” and the Community Bank also was “looking at sales goals to the extent those played a part in any of the sales practices matter.”<sup>1314</sup>

Asked what importance he assigned to the work of Corporate Risk, the core team, and Community Bank, Mr. Julian testified:

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<sup>1307</sup> See Tr. (Julian) at 6370.

<sup>1308</sup> Tr. (Julian) at 6370.

<sup>1309</sup> Tr. (Julian) at 6371.

<sup>1310</sup> Tr. (Julian) at 6371.

<sup>1311</sup> Tr. (Julian) at 6371.

<sup>1312</sup> Tr. (Julian) at 6372.

<sup>1313</sup> Tr. (Julian) at 6372-33.

<sup>1314</sup> Tr. (Julian) at 6372-73; see also “22-03-07 Respondents’ Amended Revised Errata Days 9 -38” at page 46. Ordered through Second Supplemental Order Regarding Hearing Transcript Errata.

Well, at the time, we knew that team members had been terminated for misconduct. We knew through articles that there were allegations of sales pressure. And so as chief auditor, what I'm looking for is: Is the business unit aware of the issue? Are they reacting, in my opinion, appropriately and in good faith to address the issue? And based on all the work that I knew that was going on at the time that I was hearing was going on at the time, it provided me comfort, if you will, or confidence, I should say, that the Community Bank was aware of it and a significant amount of resources both in the Community Bank as well as within corporate risk were being applied to address the issue.<sup>1315</sup>

Asked whether, after the L.A. Times articles were published, Mr. Julian directed Audit to set out to change any controls at the Community Bank, Mr. Julian said, “no” claiming that doing so “would have been inappropriate, given Audit’s role.”<sup>1316</sup> His sole reasoning for not taking such action was that “Audit had to ensure that it maintained its independence. And to do that, Audit’s prohibited by the professional standards from being involved in implementing controls within the organization.”<sup>1317</sup> Nothing in the professional standards cited by Mr. Julian, however, prevented Audit from conducting control testing over the existing risk management controls in place in the Community Bank’s first line of defense, to determine the efficacy of those controls.

Instead of determining whether control changes were warranted at the Community Bank, Mr. Julian directed WFAS to continue its “business monitoring with respect to the work that was being done to assure that the work that had been tasked by the Board” to Corporate Risk and the Community Bank was being done as directed by the Board.<sup>1318</sup> In this context, Mr. Julian said “business monitoring” “comprised a number of different activities that WFAS employed with the purpose of ensuring or assuring that WFAS was aware of the activity going on, that we could monitor the work that was being performed while it was being performed by the business unit or by Corporate Risk in this instance.”<sup>1319</sup> At no point in his testimony did he identify the type of business monitoring he was referring to, nor did he identify any documents that reflected the course of such monitoring.<sup>1320</sup>

Mr. Julian testified that after the L.A. Times published the articles, WFAS engaged in “business monitoring” with both the line of business (here, the Community Bank) as the First

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<sup>1315</sup> Tr. (Julian) at 6374.

<sup>1316</sup> Tr. (Julian) at 6374-75.

<sup>1317</sup> Tr. (Julian) at 6375.

<sup>1318</sup> Tr. (Julian) at 6375-76.

<sup>1319</sup> Tr. (Julian) at 6376-77.

<sup>1320</sup> See R. Ex. 12281 at 53-54: there were five types of business monitoring audit activities: Continuous Risk Assessment (CRA), Risk-Assessable Business Unit (RABU) Risk Review, Issue Validation, Call/Awareness Program, and Leverage; and each had a documentation requirement.

Line of Defense, and with the Second Line of Defense – Corporate Risk.<sup>1321</sup> Such monitoring involved “discussions, participating in meetings with the line of business” and with Corporate Risk, “to understand what work they were doing, to assure that it was being performed at the right level and with the right urgency given the risk.”<sup>1322</sup> Mr. Julian, however, offered no documentary evidence memorializing these discussions.

### **WFAS’s Noteworthy Risk Issues - February 2015**

Once again, the Noteworthy Risk Issues in February 2015 made no mention of sales practices misconduct by team members at the Community Bank.<sup>1323</sup> Once again, copying verbatim from prior Issues statements, the following narrative was presented:

**Sales Conduct, Practices and the Consumer Business Model.** With heightened focus on consumer customers, management is discussing the risks associated with sales practices, our cross sell strategy, and team member conduct. Ensuring we are providing products that provide real benefit to the customer, are sold in the appropriate manner with the proper sales incentives, and are delivered with high operational excellence is key in this environment to reducing our risk.<sup>1324</sup>

The February 2015 Issues statement added that “the CFPB issued a consent order related to inappropriate marketing and referral practices between Wells Fargo home mortgage consultants and Genuine Title, now a defunct title company. Management has taken strong corrective action as a result of this issue. In addition, we are working to build out additional second line of defense oversight of Sales Practices.”<sup>1325</sup> There was, however, no mention of business monitoring or controls testing related to the issues presented by Mr. Bacon’s reporting or the L.A. Times articles.

### **WFAS’s Presentation to the Board’s Risk Committee: April 28, 2015**

Mr. Julian testified that he attended all but the end of the Board’s Risk Committee meeting held on April 28, 2015.<sup>1326</sup> He was present for the presentation by Carrie Tolstedt, who provided “an overview of the Community Bank’s Group Risk Management practices.”<sup>1327</sup> Asked how he felt during the presentation, Mr. Julian responded that while it “appeared to be at a very high level,” he was “[n]ot sure that it was fully responsive to what at least I understood the

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<sup>1321</sup> Tr. (Julian) at 6377-78.

<sup>1322</sup> Tr. (Julian) at 6378.

<sup>1323</sup> OCC Ex. 1098.

<sup>1324</sup> *Id.* at 2; see also R. Ex. 19357 (ERMC Memo to WF&C Board of Directors and Operating Committee, January 22, 2014, at 1.

<sup>1325</sup> OCC Ex. 1098 at 2.

<sup>1326</sup> Tr. (Julian) at 6694; OCC Ex. 1101-R.

<sup>1327</sup> Tr. (Julian) at 6695.

Committee’s intents were for getting information.”<sup>1328</sup> He added that after the meeting he heard, he thinks from Mr. Loughlin, “the Committee members weren’t pleased.”<sup>1329</sup>

According to the minutes, during that part of the her presentation which Mr. Julian attended, Ms. Tolstedt represented that the “high inherent risk level within the business” should be attributed to “a number of factors, including the size, turnover, experience level and distributed nature of the group’s team members, the high volume of transactions, and the mass market segment supported by the business.”<sup>1330</sup>

Ms. Tolstedt explained that the Community Bank “manages risk by using a multi-layered approach that is supplemented by ongoing monitoring and continuous efforts to enhance risk management practices.”<sup>1331</sup> She discussed areas of focus, including “products and services training efforts for team members, the adoption of a simpler product set that is easily understood by customers, the monitoring of metrics, and the impact of performance management systems and compensation plans on business conduct.”<sup>1332</sup>

Nothing in her presentation suggested that WFAS provided credible challenge to the risk management measures Ms. Tolstedt described during this meeting. She reported, “investigations are undertaken to conduct a root cause analysis of conduct risk matters and in some cases the investigations may result in the termination of team members.”<sup>1333</sup> Further, she noted that the business-conduct risk team “conducts a final root cause analysis to evaluate whether new controls or team member communications are needed and products and services are reviewed to evaluate potential areas where risk may arise.”<sup>1334</sup> There is nothing in the minutes suggesting WFAS had undertaken or had plans to undertake an analysis to determine if the Community Bank’s testing controls effectively addressed the identification of root causes for sales practices misconduct within the Community Bank.

Ms. Tolstedt reported that the Community Banking risk management team “regularly reviews sales reports and that if an unusual increase in sales activity for a particular product is identified, then the team conducts an investigation with the support of product specialist partners.”<sup>1335</sup> There is no suggestion that WFAS provided any support with respect to testing controls employed by the Community Bank’s Risk Management Team.

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<sup>1328</sup> Tr. (Julian) at 6695.

<sup>1329</sup> Tr. (Julian) at 6695.

<sup>1330</sup> OCC Ex. 1101-R at 1-2.

<sup>1331</sup> *Id.* at 2.

<sup>1332</sup> *Id.*

<sup>1333</sup> *Id.*

<sup>1334</sup> *Id.*

<sup>1335</sup> *Id.*

Ms. Tolstedt noted that “during a recent regulatory examination,” the OCC rated Community Banking’s oversight of sales practices as “generally effective” but “did identify the need for formal documentation of the risk management framework and associated policies as a matter requiring attention (MRA).”<sup>1336</sup> There is no indication WFAS made any inquiry upon receipt of the MRA to determine the need to audit Community Bank’s risk management program in response to the MRA.

Ms. Tolstedt reported that “over the years” “changes and other enhancements to business practices and organizational structure” included “the decision to move the reporting of the business conduct risk team to the Group Risk Officer,” which Ms. Tolstedt reported “enhanced oversight practices”.<sup>1337</sup> There is no indication that WFAS ever determined whether this change to the Community Bank’s business structure was an effective enhancement with regard to the Community Bank’s risk management processes.

Ms. Tolstedt reported that when investigations are concluded and when the termination of a team member’s employment is warranted, “the termination often is based on a violation of Company policy rather than any specific customer impact and that the business seeks to utilize systems to aid in the control of these risks.”<sup>1338</sup> There is no indication that WFAS audited the systems referred to during the relevant period in order to determine the efficacy of those systems in addressing risks in the Community Bank related to sales practices misconduct.

During Mr. Julian’s First Quarter Report to the A&E Committee during its May 4, 2015 meeting, the minutes make no mention of the exchange between Ms. Tolstedt and members of the Risk Committee.<sup>1339</sup>

### **WFAS’s Noteworthy Risk Issues - May 2015**

The May 2015 WFAS Noteworthy Risk Issues report included the statement that:

Sales Practices continues to be a significant risk to the Company. In April 2015, Community Banking received an MRA from the OCC noting the lack of a formal governance framework over sales practices. In addition, the city of Los Angeles has filed a lawsuit alleging that improper sales practices and sales goals harmed customers.<sup>1340</sup>

Then, copying and pasting from the February 2015 Noteworthy Risk Issues report, the report stated:

Ensuring we are providing products that provide real benefit to the customer, are sold in the appropriate manner with the proper sales incentives, and are

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<sup>1336</sup> *Id.* at 2.

<sup>1337</sup> *Id.* at 3.

<sup>1338</sup> *Id.*

<sup>1339</sup> R. Ex. 20620 at 3.

<sup>1340</sup> R. Ex. 538 at 1.

delivered with high operational excellence is key in this environment to reducing our risk.<sup>1341</sup>

The report concludes with the following: “We are working to build out additional second line of defense oversight of Sales Practices. Community Banking has launched a project to specifically address the OCC’s feedback, and Corporate Risk is currently outlining an enhanced governance approach over sales practices.”<sup>1342</sup>

### **WFAS’s Response to the OCC’s May 20, 2015 Request for Information**

Immediately following the May 19, 2015 Risk Committee meeting, the OCC through Examiner Grover sought information from Mr. Julian.<sup>1343</sup> Examiner Grover recalled “several meetings with various departments within the organization over the past few weeks to discuss Sales Practices.”<sup>1344</sup> After specifically noting that he met with Mr. McLinko and Bart Deese during the Community Banking Operational Risk exam in February 2015 to “discuss audit coverage of Sales Practices,” Examiner Grover asked Mr. Julian to provide “a written response covering WFAS’s perspective and enterprise-wide coverage of Sales Practices since 2013.”<sup>1345</sup>

Specifically, Examiner Grover sought responses to the following by no later than May 27, 2015:

1. How did WFAS incorporate the results from the Significant Investigation Notification (SIN) dated October 9, 2013 into its audit coverage of Sales Practices within Community Banking?
2. Did WFAS test any accounts to determine customer harm?
3. Does WFAS test and evaluate trend in metrics (Sales Quality, Customer/Household Growth and Retention, Team Member, and Customer Experience)?
4. What, if any, are the lessons learned from WFAS perspective given Sales Practices litigation facing the bank?
5. What is WFAS’ coverage strategy of Sales Practices on an enterprise-wide basis? Does WFAS envision any changes in strategy given recent Sales Practices litigation?<sup>1346</sup>

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<sup>1341</sup> R. Ex. 538 at 1; see also OCC Ex. 1098 at 2; and R. Ex. 19357 (ERMC Memo to WF&C Board of Directors and Operating Committee, January 22, 2014, at 1.

<sup>1342</sup> R. Ex. 538 at 1.

<sup>1343</sup> Tr. (Julian) at 6731-32; R. Ex. 9136.

<sup>1344</sup> R. Ex. 9136 at 2.

<sup>1345</sup> *Id.*

<sup>1346</sup> *Id.* at 2-3.



Mr. Julian did not personally provide responses to these questions.<sup>1347</sup> Instead, he “forwarded this information, this request to my Audit leadership and asked each of them to weigh in with response to the questions.”<sup>1348</sup>

When asked after reviewing the email exchange what was his understanding of the OCC’s opinion of WFAS audit coverage related to sales practices, Mr. Julian responded, “That it was adequate.”<sup>1349</sup>

Elaborating on this answer, Mr. Julian testified:

I believe it was Paul McLinko who had communicated to me that he had had a communication with the OCC, I think it was Mike Declue specifically, who had communicated to him that based on their work, "theirs" being the OCC, that they felt audit's coverage of sales practices was adequate -- I believe adequate. I forget the exact word he used.<sup>1350</sup>

On May 26, 2015, Mr. McLinko presented draft responses to Mr. Julian.<sup>1351</sup> On May 27, 2015, Mr. Julian presented responses to Examiner Grover’s questions, based on the draft provided by Mr. McLinko.<sup>1352</sup>

Regarding the question concerning how WFAS incorporated the results from the October 9, 2013 SIN, Mr. Julian described WFAS “audit methodology” in general and stated, “the Community Banking (CB) audit team interacts with Corporate Investigations in a number of ways throughout the year . . . to understand cases/trends, etc.”<sup>1353</sup> He stated that when the SIN was issued, “we were auditing the RB Sales Quality group and discussed the SIN with Corporate Investigations.”<sup>1354</sup>

He added,

While not specifically a result of the SIN, we included audits of cross sell activities into the 2014 audit plan. To carry out these audits, we formed a cross functional team (WBR, CLG, CB, Wholesale) within WFAS to coordinate the audit activities. This team continues to meet, expanding our discussions to sales practices. One specific output of these discussions was including an audit of the Regional Banking Account Opening and Closing in

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<sup>1347</sup> Tr. (Julian) at 6733.

<sup>1348</sup> Tr. (Julian) at 6734.

<sup>1349</sup> Tr. (Julian) at 6732.

<sup>1350</sup> Tr. (Julian) at 6733.

<sup>1351</sup> Tr. (Julian) at 6734; R. Ex. 367.

<sup>1352</sup> Tr. (Julian) at 6735-36; R. Ex. 414.

<sup>1353</sup> R. Ex. 414 at 1.

<sup>1354</sup> *Id.*

the 2015 annual audit plan; with audit planning beginning on May 1, 2015.<sup>1355</sup>

When responding to Examiner Grover's question whether WFAS tested any accounts to determine customer harm, Mr. Julian responded, "We did not specifically test any accounts for customer harm related to this SIN."<sup>1356</sup>

When responding to the question regarding whether WFAS tests and evaluates trends in metrics, Mr. Julian responded that WFAS reviews "sales integrity monitoring and reporting, along with customer polling", and reviews "various Corporate Investigations reporting".<sup>1357</sup>

When responding to the question regarding what lessons WFAS learned given the sales practices litigation facing the Bank, Mr. Julian responded that litigation is one "potential input", leading WFAS to make "various adjustments to our approach beginning in 2013" including, for example, the Cross Sell audit included in the 2014 annual audit plan, and the Regional Bank Account Opening and Closing Audit that was included in the 2015 annual audit plan.<sup>1358</sup> He also stated WFAS "will monitor the implementation of CB's response to the [first line of defense] Risk Management Sales Practices MRA and implement changes to the audit coverage where needed," while also "reviewing our coordination with the Corporate Investigations group" and "adjust where appropriate."<sup>1359</sup>

When responding to the question regarding WFAS's coverage strategy of Sales Practices on an enterprise-wide basis, Mr. Julian stated WFAS "will monitor the development and roll-out" of the implementation of the Risk Framework, and "anticipate[s] performing an ERMA in the future," along with monitoring the roll out of new policies, including "Complaints, C2C, UDAAP" as appropriate.<sup>1360</sup> He also provided a copy of WFAS's coverage of the Community Bank's Sales Practices since 2013, which Mr. McLinko had earlier sent to Mr. Julian.<sup>1361</sup>

### **Supervisory Letter WFC 2015-36 - June 26, 2015: Five MRAs**

Through a June 26, 2015 Supervisory Letter, the OCC's Examiner in Charge for Wells Fargo Bank, N.A., Bradley Linskens, reported to the Bank's CEO, that "Wells Fargo's management and oversight of Enterprise Sales Practices is weak and needs to improve."<sup>1362</sup> Mr. Julian testified that he understood the Letter was "prompted by the City of Los Angeles

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<sup>1355</sup> R. Ex. 414 at 1.

<sup>1356</sup> *Id.*

<sup>1357</sup> *Id.* at 2.

<sup>1358</sup> *Id.*

<sup>1359</sup> *Id.*

<sup>1360</sup> *Id.*

<sup>1361</sup> *Id.*; see Tr. 6717; R. Ex. 19393, WFAS Community Bank Sales Practices Coverage 2013-2015.

<sup>1362</sup> OCC Ex. 1239 at 2.

lawsuit.”<sup>1363</sup> Mr. Julian testified that Wells Fargo took “very seriously” the issues raised by that lawsuit.<sup>1364</sup> When asked on direct examination how this observation factored into his view of his professional obligations with regard to sales practices issues at that time, Mr. Julian responded without actually answering the question:

Well, I was aware that the Board and management were obviously aware of the sales practices issue. They had been made aware of it since early 2014 that there was a significant amount of work going on with respect to sales practices across both first and second lines of defense as well as within Audit Services. So there was just a significant amount of activity going on.<sup>1365</sup>

The Supervisory Letter contained five MRAs, requiring the attention of all three lines of defense.<sup>1366</sup>

In the MRA titled “**Enterprise Sales Practices – Corporate**” the OCC stated the following concern:

Wells Fargo’s strong emphasis on “cross-sell”, combined with inadequate controls and oversight, promoted inappropriate employee behavior that is still being quantified and may yet be occurring. Internal assessments lacked reasonable independence and did not consider customer harm.<sup>1367</sup>

The OCC identified the following cause related to this concern: “Corporate emphasis on product sales and ‘cross-selling’ without an appropriate control or oversight structure.”<sup>1368</sup>

Notwithstanding that this concern addressed the *efficacy* of controls and the lack of independence for internal assessments and controls, when asked on direct examination whether WFAS had any responsibilities with regard to this MRA, Mr. Julian responded “No.”<sup>1369</sup> This answer was directly contradicted by Mr. Loughlin’s commitment that “WFAS will be engaged with the various LOBs as they develop and implement corrective actions to the Enterprise Sales Practices MRAs.”<sup>1370</sup>

Through his August 10, 2015 response to Mr. Linskens, Mr. Loughlin committed to the OCC that the scope of WFAS’s work would include:

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<sup>1363</sup> Tr. (Julian) at 6738-39.

<sup>1364</sup> Tr. (Julian) at 6740.

<sup>1365</sup> Tr. (Julian) at 6740.

<sup>1366</sup> Tr. (Julian) at 6744; OCC Ex. 1239 at 3-9.

<sup>1367</sup> OCC Ex. 1239 at 6.

<sup>1368</sup> *Id.*

<sup>1369</sup> Tr. (Julian) at 6745.

<sup>1370</sup> OCC Ex. 705 at 11.

Issue monitoring and validation, reviewing governance processes and enhanced policy, monitoring of projects/initiatives to enhance Enterprise Sales Practices compliance, and obtaining an understanding of key activities and functions performed to ensure compliance with enterprise sales practices along with their sustainability. WFAS anticipates quarterly status reports will be prepared, beginning the fourth quarter of 2015 and continue to our first ERMA.<sup>1371</sup>

Mr. Julian described WFAS's role in "issue monitoring and validation":

So part of Wells Fargo Audit Services' work was, to the extent that issues -- that could be audit issues, that could be self-identified issues, meaning business unit identified them, it could be regulatory issues such as MRAs. To the extent as that work was being performed to remediate those issues by the responsible business unit, Wells Fargo Audit Services would monitor progress to that work to assure that the business unit -- responsible business unit was -- was working in good faith and with the right level of urgency to address the issues. And once the work was completed, once the business unit identified that they had satisfied that issue, Wells Fargo Audit Services would come in and validate that through various forms. Typically it was through testing, to go in and test that -- let's say it was a control that was put in place -- to test that that control was actually effective.<sup>1372</sup>

In the MRA titled "**Enterprise Sales Practices – Second Line of Defense**" the OCC stated the following concern:

Wells Fargo does not have an Enterprise Sales Practices oversight program. The bank's approach is heavily reliant on decentralized first line of defense identification and escalation of potential issues.<sup>1373</sup>

The OCC identified the following cause related to this concern: "Although identified as an area needing attention, management focused on higher priorities based on available resources (*i.e.*, the build-out of operational and liquidity risk frameworks)."<sup>1374</sup>

When asked on direct examination whether this MRA was in any way directed at WFAS, Mr. Julian responded, "No" and that it did not include WFAS in any way, and that it was

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<sup>1371</sup> *Id.*

<sup>1372</sup> Tr. (Julian) at 6881.

<sup>1373</sup> OCC Ex. 1239 at 6.

<sup>1374</sup> *Id.*

directed only “to the second line of defense.”<sup>1375</sup> He repeated this answer when asked what corrective actions the OCC examiners directed WFAS to perform pursuant to this MRA.<sup>1376</sup>

Unaddressed through this line of questioning was Mr. Julian’s responsibility for corrective actions apart from his role as the head of WFAS’s Internal Audit group. In his testimony, Mr. Julian denied that WFAS had been tasked through MRA#2 with taking corrective actions related to the reasonableness of the incentive compensation program for enterprise sales activities.<sup>1377</sup> Throughout his tenure as Chief Auditor, however, Mr. Julian was a member of the WF&C Incentive Compensation Steering Committee, which had oversight responsibilities regarding incentive compensation programs enterprise-wide.<sup>1378</sup>

Through Wells Fargo’s August 10, 2015 response to MRA#2, Mr. Loughlin committed to implementing a “process for enhancing evaluation of sales practices risk as related to incentive compensation design and administration and related performance management practices.”<sup>1379</sup> He told the OCC that the “ICC will provide oversight around the design and administration of the sales incentive plans and will report to the HRC regarding risk management practices in this area.”<sup>1380</sup>

Apart from his role as a member of the Incentive Compensation Committee, as Chief Auditor Mr. Julian also served as a member of the Enterprise Risk Management Committee throughout the relevant period.<sup>1381</sup> Under the Committee’s Charter, the purpose of the Committee was to oversee “the management of all risks across Wells Fargo, with emphasis on credit, market, institutional, and operational risks.”<sup>1382</sup>

Under MRA#2, the OCC required WF&C to “[r]eassess both the EthicsLine and customer complaints investigative process, establish full independence from the first line, and ensure referrals and complaints are reviewed in a timely manner.”<sup>1383</sup> Mr. Julian denied that WFAS was tasked with this responsibility, testifying – through leading questioning by his Counsel on direct examination – that the second line of defense took meaningful steps to reassess the EthicsLine and customer complaints investigative processes pursuant to this MRA.<sup>1384</sup>

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<sup>1375</sup> Tr. (Julian) at 6745.

<sup>1376</sup> Tr. (Julian) at 6814.

<sup>1377</sup> Tr. (Julian) at 6821.

<sup>1378</sup> OCC Ex. 1722 at 1.

<sup>1379</sup> OCC Ex. 705 at 7.

<sup>1380</sup> *Id.*

<sup>1381</sup> Tr. (Julian) at 6059; R. Ex. 438 at 1.

<sup>1382</sup> Tr. (Julian) at 6261-62; R. Ex. 438 at 1.

<sup>1383</sup> OCC Ex. 1239 at 7.

<sup>1384</sup> Tr. (Julian) at 6822; see also “22-03-07 Respondents’ Amended Revised Errata Days 9 -38” at page 53. Ordered through Second Supplemental Order Regarding Hearing Transcript Errata.

Unaddressed by this response is Mr. Julian's role as a member of the WF&C Ethics Committee throughout the relevant period.<sup>1385</sup> While WFAS was not charged directly with responsibilities under MRA#2, Mr. Julian was a member of a committee that bore a direct responsibility under this MRA.<sup>1386</sup>

To much the same effect, Mr. Julian testified that WFAS was not tasked with conducting "a root cause analysis of sales integrity violations and present the data and assessment to executive management and Risk Committee of the Board."<sup>1387</sup> According to Mr. Julian, "Mike Loughlin was directed specifically to work with the first line of defense to investigate and determine the root cause of sales integrity violations."<sup>1388</sup> However, Mr. Julian introduced no substantial evidence establishing that Mr. Loughlin was ever specifically directed to determine the root cause of sales integrity violations in a way that precluded Mr. Julian as Chief Auditor from having the responsibility to do the same.<sup>1389</sup>

In his August 10, 2015 response to MRA#2, Mr. Loughlin reported to the OCC that while "Corporate HR is the owner of incentive compensation policies and is responsible for the oversight of incentive compensation risk management efforts," Corporate HR "partners with Enterprise Risk" to ensure "incentive compensation risks (including reputational issues and potential customer harm related to sales practices and employee conduct" are adequately understood and appropriately addressed."<sup>1390</sup>

Mr. Julian testified that in response to MRA #2, WF&C's Corporate Risk Group published a Sales Practices Risk Governance Document dated November 2015.<sup>1391</sup> Mr. Julian said he was not personally involved in drafting the document and testified that it describes the "oversight unit" – the "second line of defense groups who were involved or had accountabilities with respect to providing oversight to sales practices risk management."<sup>1392</sup> He testified, however, that Audit is not reflected anywhere in this document,<sup>1393</sup> and did not discuss during direct examination his responsibilities as a member of either the Incentive Compensation Committee or the ERMCM regarding MRA #2.<sup>1394</sup>

The November 2015 Sales Practices Risk Governance Document stated that WF&C was:

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<sup>1385</sup> R. Ex. 12528 at 3.

<sup>1386</sup> Tr. (Julian) at 6822.

<sup>1387</sup> Tr. (Julian) at 6823; R. Ex. 705 at 6.

<sup>1388</sup> Tr. (Julian) at 6823.

<sup>1389</sup> Tr. (Julian) at 6823.

<sup>1390</sup> OCC Ex. 705 at 7.

<sup>1391</sup> Tr. (Julian) at 6816; R. Ex. 11373.

<sup>1392</sup> Tr. (Julian) at 6817.

<sup>1393</sup> Tr. (Julian) at 6818.

<sup>1394</sup> Tr. (Julian) at 6818.

“[m]aintaining an independent internal audit function that is primarily responsible for adopting a systematic, disciplined approach to evaluating the effectiveness of sales practices risk management, control and governance processes and activities, as well as ensuring that this Sales Practices Risk Governance Document adheres to relevant regulatory guidelines and is appropriate for Wells Fargo’s size and risk profile.”<sup>1395</sup>

Through this Governance Document, WF&S defined “credible challenge” as the “communication of an alternate view, opinion, or strategy developed through expertise and professional judgment to challenge business or enterprise strategies, policies, products, practices and controls.”<sup>1396</sup>

According to the Governance Document, Group Risk Officers (GROs), who led the Group Risk organizations embedded in the Company’s sales practices risk-generating Groups, were to exercise credible challenge through various means, including by raising concerns to Group management and escalating issues to CERG [Corporate Enterprise Risk Group] in a timely manner, in particular its SPO [Sales Practices Oversight] unit, in addition to certain components of the Chief Administrative Office, the Law Department, and certain Corporate Risk functions.”<sup>1397</sup>

Further, the Governance Document requires “all team members to escalate sales practices risk issues that necessitate specific reporting or decision making (particularly as it relates to remedial actions) to a higher level of the management or committee structure for consideration.”<sup>1398</sup> The Governance Document identified specific sales practices risk escalation events and the escalation model – so, for example, sales practices that are compensation-related were to be escalated through the escalation path outlined in the ICRM policy; and from there to the Sales Practices Oversight unit established through the Governance Document; and from there to the Head of Enterprise Risk; and from there to the ERMC, and then to the Risk Committee.<sup>1399</sup>

Without elaboration, Mr. Julian testified that while the Governance Document was designed “as a forward-looking document talking about what actions and activities and responsibilities, many of the practices that were – had been in place prior to this document were embedded or embodied into this, so it wasn’t all new.”<sup>1400</sup> Through leading questioning by his Counsel during direct examination, Mr. Julian testified that the Governance Document

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<sup>1395</sup> R. Ex. 11373 at 7.

<sup>1396</sup> *Id.* at 9.

<sup>1397</sup> *Id.*

<sup>1398</sup> *Id.* at 21.

<sup>1399</sup> *Id.* at 22, Figures 3 and 4.

<sup>1400</sup> Tr. (Julian) at 6820-21.

references the fact that Corporate Risk was establishing a new approach with regard to sales practices risk at this time.<sup>1401</sup>

According to the Governance Document, customer complaints and Unfair, Deceptive, or Abusive Acts or Practices (UDAAP) issues were to be escalated through the path outlined in the RCRM Policy, internal fraud through the path outlined in the Financial Crimes Risk Functional Framework, ethical issues through the Reputation Risk Framework – and all proceed from there to the Sales Practices Oversight Unit, using the same path as that used for incentive compensation issues.

At the enterprise level, Mr. Julian had a duty to assure the adequacy of the enterprise’s risk management – to assure that reputation risk was effectively managed and the Bank’s brand was protected. Mr. McLinko had that same duty with respect to the Community Bank. Thus as a member of the ERMC, all of these issues would be presented to Mr. Julian as a member of that Committee, and through this process Mr. McLinko had a clear escalation path via Mr. Julian.<sup>1402</sup>

Also in the MRA titled “**Enterprise Sales Practices – Second Line of Defense**” the OCC stated the following concern regarding “**Complaints**”:

Extended timelines to implement Regulatory Compliance Risk Management’s (RCRM) revised Enterprise Complaints Management Policy (Policy), published in May 2014, is not scheduled to take until year-end 2016. This implementation plan appears excessive given the importance to the bank of an enterprise program.<sup>1403</sup>

The OCC identified the following cause related to this concern: “A decentralized complaints process, multiple complaints systems, and a need to capture verbal complaints systematically will require an extended period of time.”<sup>1404</sup>

When asked on direct examination whether he understood this MRA to be directed at WFAS, Mr. Julian responded, “No, it was not” and that this MRA was to be directed to “the group that was responsible for overseeing the complaint process” and identified that group as the RCRM in the second line of defense.<sup>1405</sup> He said that this MRA did not direct WFAS to perform any action, and when asked whether he personally received customer complaints during the relevant time period, Mr. Julian responded that he did not.<sup>1406</sup>

Mr. Julian testified that the second line of defense “developed a program to, again – to more centralize the intake process for customer complaints as well as enhance the reporting of

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<sup>1401</sup> Tr. (Julian) at 6912.

<sup>1402</sup> R. Ex. 11373 at 22, Figure 4.

<sup>1403</sup> OCC Ex. 1239 at 7.

<sup>1404</sup> *Id.*

<sup>1405</sup> Tr. (Julian) at 6745-46; 6823.

<sup>1406</sup> Tr. (Julian) at 6819; 6824.



customer complaints.”<sup>1407</sup> He said they “also evaluated the adequacy of the controls and built in controls that were necessary in the building out of that process and program.”<sup>1408</sup> He said nothing, however, about any steps being taken by Audit to determine the efficacy of efforts by the second line of defense to determine the root cause of the sales practices misconduct problem associated with the Community Bank.

In the MRA titled “**Community Bank Group – Sales Practices**” the OCC rescinded the *Community Bank Risk Management – Sales Practices MRA* issued in Supervisory Letter 2015-07 on April 3, 2015, replacing that Letter with this MRA.

The present MRA stated the following concern:

The Community Bank (CB) Group lacks a formalized governance process to oversee Sales Practices and does not have an effective oversight and testing of branch (store) sales practices.<sup>1409</sup>

The OCC identified the following cause related to this concern: “Current governance processes are managed separately within the CB group and none address actual ‘in branch’ (store) monitoring of employee sales practices.”<sup>1410</sup>

When asked on direct examination whom he understood this MRA to be directed at, Mr. Julian denied that WFAS had been directed to act with respect to this MRA and responded:

To the Community Bank risk management group. It was very common for MRAs to be directed to specific businesses or specific lines of business and not imply that Wells Fargo Audit Services was responsible for addressing the MRA or necessarily criticism of Wells Fargo services with respect to that MRA.<sup>1411</sup>

According to Mr. Julian, “the risk management function within the Community Bank was tasked with enhancing its oversight and quality assurance and testing programs with respect to sales practices within the branch stores.”<sup>1412</sup> Through leading questioning by his Counsel during direct examination, Mr. Julian testified that the OCC examiners “didn’t task WFAS with establishing effective oversight and the testing or quality assurance function of branch store sales practices.”<sup>1413</sup>

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<sup>1407</sup> Tr. (Julian) at 6824.

<sup>1408</sup> Tr. (Julian) at 6825.

<sup>1409</sup> OCC Ex. 1239 at 8.

<sup>1410</sup> *Id.*

<sup>1411</sup> Tr. (Julian) at 6747; 6825.

<sup>1412</sup> Tr. (Julian) at 6825-26.

<sup>1413</sup> Tr. (Julian) at 6826.

Mr. Julian acknowledged that this MRA required the Community Bank to establish “effective oversight and a testing/quality assurance function of branch (store) sales practices.”<sup>1414</sup> Asked through leading questioning on direct examination if he knew whether the first line of defense took meaningful steps to perform its commitment under this MRA provision, Mr. Julian responded, without providing any details, “they enhanced their program and their governance policies and quality assurance functions.”<sup>1415</sup>

Similarly, Mr. Julian acknowledged the MRA required the Community Bank to describe, “the referral process and assigning responsibility for compliance with CB’s sales integrity policy,” and testified – again without providing details – that they “applied a significant amount of resources to address this issue and built out the program.”<sup>1416</sup>

Asked through leading questioning on direct examination whether his knowledge of these corrective actions was a result of business monitoring activities that he was engaged in, Mr. Julian testified:

That both Wells Fargo Audit Services was engaged in and, therefore, through my discussions with Wells Fargo Audit Services folks, my leadership team and others, I was being updated on actions being taken. I was being provided periodic updates of the progress being made. I also personally was in various meetings where the actions or the progress being made was discussed. And so it was both my personal engagement from that level as well as engagement of WFAS's business monitoring.<sup>1417</sup>

In MRA #5, titled “**Audit**,” the OCC stated the following concern:

Wells Fargo Audit Services (WFAS) did not identify the issues noted in this Supervisory Letter and past coverage did not provide an enterprise view of sales practices.<sup>1418</sup>

The OCC identified the following cause related to this concern: “WFAS coverage included various aspects of sales practices in individual audits, but did not aggregate these aspects into an enterprise view.”<sup>1419</sup> It required WFAS to “[r]eassess their coverage of sales practices and provide an enterprise view (i.e., Enterprise Risk Management Assessment (ERMA) of Enterprise Sales Practices.”<sup>1420</sup>

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<sup>1414</sup> Tr. (Julian) at 6826; OCC Ex. 705 at 10.

<sup>1415</sup> Tr. (Julian) at 6826.

<sup>1416</sup> Tr. (Julian) at 6826-27.

<sup>1417</sup> Tr. (Julian) at 6828.

<sup>1418</sup> OCC Ex. 1239 at 8.

<sup>1419</sup> *Id.* at 9.

<sup>1420</sup> *Id.*

In the Supervisory Letter, EIC Linskens stated:

There has been and continues to remain an overall lack of transparency at the first line of defense regarding past investigations and ongoing control and monitoring processes. There also exists only limited monitoring and oversight by the second (Corporate Risk, Human Resources, Compliance, and Legal) and third lines of defense. . . . [WFAS'] related coverage included 12 audits addressing elements of sales practices between 2013 and 2015. However, no significant issues were identified or escalated as a result of that work, and the group has not completed a comprehensive review of sales practices across the enterprise.<sup>1421</sup>

Mr. Julian testified that he understood the reference to there being “twelve audits” was to the coverage information provided in the WFAS Community Bank Sales Practices Coverage 2013-2015 report Mr. Julian sent to the OCC in response to Examiner Grover’s request for information.<sup>1422</sup> Without disputing the conclusions reached in the Supervisory Letter, Mr. Julian testified that before the issuance of the June 26, 2015 Letter, none of the OCC’s Examiners had communicated any criticism of Audit’s coverage of sales practices issues regarding the Community Bank.<sup>1423</sup>

Mr. Julian testified that he understood the MRA regarding Audit required that WFAS “reassess the coverage related to sales practices,” and that in this context “coverage” meant “the work that Audit was doing with respect to auditing sales practices, risk.”<sup>1424</sup> He added that until the June 2015 Supervisory Letter, no one from the OCC suggested that WFAS should reassess their coverage of sales practices, nor did anyone express any concerns about WFAS’s failure to perform an ERMA for Sales Practices.<sup>1425</sup>

Through MRA #5, WFAS was charged with reassessing their coverage of sales practices “and provide an enterprise view (*i.e.*, Enterprise Risk Management Assessment (ERMA) of Enterprise Sales Practices.”<sup>1426</sup> Although this commitment required an assessment of all the lines of business, when asked during direct examination who he understood were the accountable executives tasked with overseeing WFAS’s commitments to this enterprise-wide task, Mr. Julian did not include himself in his answer, responding instead that Mr. McLinko and Mark Links were responsible for overseeing these commitments.<sup>1427</sup> Mr. McLinko at that time was the

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<sup>1421</sup> OCC Ex. 1239 at 2.

<sup>1422</sup> Tr. (Julian) at 6743; R. Ex. 19393, WFAS Community Bank Sales Practices Coverage 2013-2015.

<sup>1423</sup> Tr. (Julian) at 6744.

<sup>1424</sup> Tr. (Julian) at 6748.

<sup>1425</sup> Tr. (Julian) at 6779-80.

<sup>1426</sup> Tr. (Julian) at 6830; OCC Ex. 705 at 11.

<sup>1427</sup> Tr. (Julian) at 6830.

Executive Audit Director assigned to the Community Bank, and Mr. Links was the Executive Audit Director “over the corporate risk function”.<sup>1428</sup>

According to Mr. Loughlin’s response to the MRA #5, “WFAS will be engaged with the various LOBs as they develop and implement corrective actions to the Enterprise Sales Practices MRAs.”<sup>1429</sup>

Mr. Julian testified that WFAS responded to this task in the following way:

So WFAS was engaged in dialogue with the various first and second line of defense folks who were tasked with implementing the responses to the MRA No. 1 through 4 to fully understand what those groups were doing and to building out the risk management framework, to building out the governance, to changing controls and processes, to understand all of that so that then Wells Fargo Audit Services could then reassess Wells Fargo Audit Service’s coverage in light of all of those changes that were going on. At the same time, there were two third parties that were engaged, Accenture and PwC. So Wells Fargo Audit Services was engaged to understanding the work that those two groups were doing, to the extent that that work should influence that Wells Fargo Audit Services was doing. And assessing through all of that its enterprise risk management view of sales practices.<sup>1430</sup>

Mr. Julian testified during direct examination that at no point in connection with the June 26, 2015 Supervisory Letter did any OCC examiner express concerns about his personal conduct as Chief Auditor, nor state to him that WFAS’s failure to identify the issues noted in the Supervisory Letter was unsafe or unsound, nor that it rose to the level of being reckless.<sup>1431</sup>

Through leading questioning by his Counsel during direct examination, Mr. Julian testified that in his view, given the information that he knew at the time and given his role as Chief Auditor, he satisfied his professional duties, notwithstanding that WFAS did not identify the issues in the June 26, 2015 Supervisory Letter prior to the issuance of the letter.<sup>1432</sup> Through leading questioning, Mr. Julian testified that no provision of the IIA Standards required him to direct WFAS to provide an enterprise view of sales practices prior to June of 2015.<sup>1433</sup>

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<sup>1428</sup> Tr. (Julian) at 6830.

<sup>1429</sup> OCC Ex. 705 at 11.

<sup>1430</sup> Tr. (Julian) at 6831; see also “22-03-07 Respondents’ Amended Revised Errata Days 9 -38” at page 53. Ordered through Second Supplemental Order Regarding Hearing Transcript Errata.

<sup>1431</sup> Tr. (Julian) at 6780.

<sup>1432</sup> Tr. (Julian) at 6781.

<sup>1433</sup> Tr. (Julian) at 6782.

Mr. Julian noted that the Supervisory Letter included a report that Corporate Risk “identified in early 2014 the need to establish a second line of defense framework for Sales Practices.”<sup>1434</sup>

Asked what that was referring to, Mr. Julian testified:

So prior to the L.A. Times article back in 2013 and the escalation of sales practices risk -- corporate risk didn't have a risk framework, if you will, for evaluating and providing governance over sales practices. And as the sales practices matter became communicated and was being worked on, Corporate Risk determined that they should develop a framework specific to sales practices risk.<sup>1435</sup>

According to Mr. Julian in response to leading questioning by his Counsel during direct examination, this meant the second line of defense – Corporate Risk – “owned” the responsibility for building out the risk framework.<sup>1436</sup>

This response fails to address the requirement expressed by Mr. Loughlin that the scope of WFAS’s responsibilities under MRAs #2 and #5 included “issue monitoring and validation, reviewing governance processes and enhanced policy, monitoring of projects/initiatives to enhance Enterprise Sales Practices compliance, and obtaining an understanding of key activities and functions performed to ensure compliance with enterprise sales practices along with their sustainability.”<sup>1437</sup>

Asked during direct examination to describe what he observed in terms of the Bank management’s efforts to implement the corrective actions described in the June 2015 Supervisory Letter, Mr. Julian responded in generalities: “Corrective actions were identified. Various plans were developed to address the issues. Again, a significant amount of resources. Really no money spared, no resources spared to address the issues.”<sup>1438</sup>

Mr. Loughlin, Chief Risk Officer for WF&C, provided a more detailed description of the Bank’s responses to the Supervisory Letter, presented through a letter to EIC Linskens dated August 10, 2015.<sup>1439</sup> Nowhere in his response did Mr. Loughlin dispute the factual claims presented through the Supervisory Letter, nor did he disagree that the actions required by the OCC were warranted.<sup>1440</sup>

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<sup>1434</sup> Tr. (Julian) at 6741; OCC Ex. 1239 at 2.

<sup>1435</sup> Tr. (Julian) at 6741; see also “22-03-07 Respondents’ Amended Revised Errata Days 9 -38” at page 52. Ordered through Second Supplemental Order Regarding Hearing Transcript Errata.

<sup>1436</sup>Tr. (Julian) at 6741.

<sup>1437</sup> OCC Ex. 705 at 11.

<sup>1438</sup> Tr. (Julian) at 6786-87.

<sup>1439</sup> Tr. (Julian) at 6805-06; OCC Ex. 705.

<sup>1440</sup> OCC Ex. 705 at 1-12.

Mr. Loughlin identified specific actions relating to the functions of WF&C’s Incentive Compensation Risk Management (ICRM) Program, which was managed by Corporate Human Resources and was “overseen by the Company’s Incentive Compensation Committee”, which committee include Mr. Julian.<sup>1441</sup> Mr. Loughlin reported that key ICRM Program enhancements would include developing and implementing “methodology to incorporate sales practices risk metrics/outcomes as an input into incentive compensation decisions for the Sales Practices Group”, and expanding the ICRM governance framework “to include broader review of sales roles and evaluations of sales practices, including leveraging the oversight roles of the ICC [the Company’s Incentive Compensation Committee] and HRC [the Human Resources Committee].”<sup>1442</sup>

In addition, WF&C engaged a consultant, Accenture, to complete an independent review of Enterprise Sales Practices, with particular focus on the Community Bank, Home Lending, and “certain activities of Wells Fargo Advisors.”<sup>1443</sup> Among the scope of Accenture’s work in this engagement was a review of “Controls and Monitoring, including Ethics Line”.<sup>1444</sup>

WF&C entered into a separate independent review with another consultant, PricewaterhouseCoopers (PwC) “to complete an independent review that will assess quantification of potential customer harm related to the specific allegations in the Los Angeles litigation as well as a review to assess any broader enterprise concerns.”<sup>1445</sup>

Mr. Loughlin reported that Corporate HR “in partnership with key stakeholders” would develop protocols to identify “whether any inappropriate behavior involving the sale of bank products by a bank employee and resulting in the termination of employment has the potential for customer harm.”<sup>1446</sup> He reported that the lines of business, along with the Bank’s Law Department and Regulatory Compliance Risk Management (RCRM) partners, will determine the existence of, and appropriate remediation for any customer harm.”<sup>1447</sup> He specifically indicated that responsive action would include “partnering with Corporate Risk, [WFAS], and other key stakeholders to develop appropriate reporting” of “handling the review of team member misconduct resulting in termination”.<sup>1448</sup>

Asked through leading questioning by his Counsel during direct examination whether Corporate HR was taking meaningful action in response to the June 2015 Supervisory Letter and

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<sup>1441</sup> OCC Ex. 705 at 2.

<sup>1442</sup> *Id.* at 3.

<sup>1443</sup> *Id.*

<sup>1444</sup> *Id.* at 4.

<sup>1445</sup> *Id.*

<sup>1446</sup> *Id.*

<sup>1447</sup> *Id.*

<sup>1448</sup> *Id.*

its five MRAs, Mr. Julian responded “Yes. I felt their response was appropriate and that they were taking action to implement the response.”<sup>1449</sup>

Asked to describe how Corporate HR and WFAS were “partnering” in response to the MRAs, Mr. Julian responded, “Mostly working with WFAS as WFAS would monitor and assess the reporting that was being developed. They were getting advice, consultation, if you will, from WFAS to the extent that WFAS had a view whether it was responsive and appropriate reporting.”<sup>1450</sup> Mr. Julian offered no documentation supporting this statement, and testified that he himself was not personally providing the services he attributed to WFAS.<sup>1451</sup>

Mr. Loughlin reported that WF&C would establish “an anonymous survey, testing, and analysis program (in store) to ensure our store team members are exhibiting appropriate sales and service conduct.”<sup>1452</sup> After identifying Ms. Russ Anderson as the accountable executive, Mr. Loughlin reported that “[k]ey risk metrics to support analysis of effective sales practices activities will be developed by December 31, 2015” and that the Community Bank would “leverage the [Community Bank] Risk Management Committee to report, monitor and escalate sales practices activities and issues to the second line of defense and WFAS as appropriate.”<sup>1453</sup>

In response to MRA #5 (Audit Coverage), Mr. Loughlin identified Mr. McLinko and Mark Links as the accountable executives, and reported that WFAS “will evaluate the current sales practice audit coverage and commit to develop a comprehensive audit approach.”<sup>1454</sup> He committed WFAS to understanding the scope of both the Accenture and PwC analyses “to understand the scope of their coverage as it relates to Wells Fargo’s approach to Enterprise Sales Practices and assessing potential customer harm for allegations of inappropriate behavior, respectively.”<sup>1455</sup>

Mr. Julian testified that an email exchange between Mr. McLinko and Mr. Julian constituted evidence of Mr. McLinko’s work regarding the Accenture and PwC engagements.<sup>1456</sup> In the exchange, Kris Klos inquired to Accenture email addressees regarding the Accenture engagement letter, the scope of the engagement, and applicable deadlines; and Jean Veta responded from an Accenture email address to Wells Fargo addressees.<sup>1457</sup>

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<sup>1449</sup> Tr. (Julian) at 6812.

<sup>1450</sup> Tr. (Julian) at 6812-13.

<sup>1451</sup> Tr. (Julian) at 6813.

<sup>1452</sup> OCC Ex. 705 at 10.

<sup>1453</sup> *Id.*

<sup>1454</sup> *Id.* at 11.

<sup>1455</sup> *Id.*

<sup>1456</sup> Tr. (Julian) at 6810-11; R. Ex. 9937.

<sup>1457</sup> R. Ex. 9937 at 4.

There is one message from Mark Links indicating that Mr. McLinko “is going to be the lead from a WFAS perspective. I have added him to the daily meetings.”<sup>1458</sup> In his July 8, 2015 email to Ms. Klos, Mr. McLinko inquired regarding the scope of the engagement regarding whether the Accenture engagement addresses customer harm; and a second email, dated July 9, 2015, from Mr. McLinko to Mr. Julian where Mr. McLinko reported that a “separate request will be put out to several firms for the review of customer harm”.<sup>1459</sup> Mr. Julian testified that this exchange “was referring to the customer harm work that PwC ultimately performed.”<sup>1460</sup>

Mr. Loughlin did not limit WFAS’s responsibilities to WFAS itself. He reported that WFAS also was to engage “with the various [lines of business] as they develop and implement corrective actions to the Enterprise Sales Practices MRAs.”<sup>1461</sup> He described the scope of WFAS’s response as including “issue monitoring and validation, reviewing governance processes and enhanced policy, monitoring of projects/initiatives and functions performed to ensure compliance with enterprise sales practices along with their sustainability.”<sup>1462</sup>

Mr. Loughlin reported WFAS “will review the existing audit universe, which is based upon Risk Adjusted Business Units (RABUs), and ensure that these three areas [Corporate Investigations, Corporate Customer complaints, and EthicsLine processes] have been included in the audit universe.”<sup>1463</sup>

In his letter of August 10, 2015, Mr. Loughlin committed to the OCC that WFAS would “evaluate the current complaints audit coverage and commit to develop a comprehensive audit approach.”

Elaborating, Mr. Loughlin reported the following:

WFAS anticipates incorporating these enhancements as part of our 2016 audit plan process and will update our coverage when additional information is available. Similar to Corporate Investigations and Ethics Line, the audit team responsible for the audit of corporate customer complaints will analyze the data that is produced from this group to determine the best way to incorporate relevant information into the appropriate LOB audits. WFAS anticipates completion by the end of the first quarter of 2016.<sup>1464</sup>

Mr. Julian identified Standard Audit Practice Program: Sales Practices – 1<sup>st</sup> Line of Defense” dated September 2015, developed primarily by Kathy Sheng, who was leading a Sales

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<sup>1458</sup> R. Ex. 9937 at 2.

<sup>1459</sup> *Id.* at 1.

<sup>1460</sup> Tr. (Julian) at 6811.

<sup>1461</sup> OCC Ex. 705 at 11.

<sup>1462</sup> *Id.*

<sup>1463</sup> *Id.*

<sup>1464</sup> *Id.* at 12.



Practices Audit Group.<sup>1465</sup> He testified that in response to MRA #5, WFAS “undertook to develop a standard audit program that could be leveraged by the various audit groups throughout [WFAS] as they were performing audits to assure that they were appropriately considering sales practice risk as a risk”.<sup>1466</sup> Although he testified that the audit program “was a high priority,” he had nothing to do at the creation “level of detail” of the Program, but “certainly at the level of understanding the intent of the document.”<sup>1467</sup>

The Sales Practices Audit Program included a list of detailed test procedures, including assessments of whether there are any trends seen from reviews of complaint and EthicsLine data that need to be examined further, and an assessment of whether any internal investigations or employee relations investigations occurred.<sup>1468</sup>

The Program called for the identification of key committees within the organizational structure, looking for evidence that the committee is “fulfilling the key components” of the committee’s charter.<sup>1469</sup> The Program called for a review of sales practices training programs to determine if the training “accurately depicts Wells Fargo’s culture and Visions & Values.”<sup>1470</sup>

The Audit Program also identified potential controls – including Risk Identification, Risk Control, Risk Appetite, Ethical Culture, Vision & Values, Risk Management Credence, and Risk Management Influence.<sup>1471</sup>

Within the list labeled “Monitor and Report,” the Audit Program included reviewing sales practices risk monitoring and reporting to look for evidence “that appropriate feedback has been provided to the second-line of defense for continuous improvement,” to include “escalations, communications of trends, emerging risks, or suggested improvements for risk framework.”<sup>1472</sup> It also required the evaluation of the effectiveness of the testing program, and included monitoring to determine whether “adequate processes exist to identify and monitor emerging risks of inappropriate or improper sales practices relevant to Group, line of business or legal entity levels”.<sup>1473</sup>

Mr. Julian testified that issue monitoring and validation required WFAS to “monitor progress to that work to assure that the business unit” was “working in good faith and with the

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<sup>1465</sup> Tr. (Julian) at 6836.

<sup>1466</sup> Tr. (Julian) at 6834; R. Ex. 11817.

<sup>1467</sup> Tr. (Julian) at 6836-37.

<sup>1468</sup> R. Ex. 11817 at 1.

<sup>1469</sup> *Id.* at 2.

<sup>1470</sup> *Id.* at 2-3.

<sup>1471</sup> *Id.* at 1.

<sup>1472</sup> *Id.* at 5.

<sup>1473</sup> *Id.*

right level of urgency to address the issues.”<sup>1474</sup> He testified that “once the work was completed, once the business unit identified that they had satisfied that issue, [WFAS] would come in and validate that through various forms. Typically, it was through testing . . . to test that that control was actually effective.”<sup>1475</sup>

Where Mr. Loughlin reported that WFAS would be responsible for “reviewing governance processes and enhanced policy,” Mr. Julian testified that this required WFAS to “assess those governance processes and policies” developed or enhanced in addressing MRAs #1 through 4 “being developed or enhanced across both the first and second line of defense.”<sup>1476</sup>

Mr. Loughlin included in his response the commitment that the Enterprise Risk Management Audit Team will include and ERMA for Sales Practices (which at the time had been identified as Cross-Functional Risk).<sup>1477</sup> “As Wells Fargo’s management is developing and implementing proposed corrective actions to the MRAs noted in the Supervisory Letter, we anticipate that the first ERMA for Sales Practices will be in 1Q of 2017, for the year 2016.”<sup>1478</sup> Mr. Julian confirmed that “the enterprise risk management assessment did not previously include sales practices as a specific enterprise risk management assessment category,” but rather than confirm that an ERMA for Sales Practices for 2016 would be presented in 2017; Mr. Julian testified that WFAS was “assessing how to and if it should include an enterprise risk management assessment of sales practices specifically.”<sup>1479</sup>

Mr. Loughlin committed that “WFAS will evaluate the current complaints audit coverage and commit to develop a comprehensive audit approach. WFAS anticipates incorporating these enhancements as part of our 2016 audit plan process”.<sup>1480</sup> Similarly, Mr. Loughlin committed that WFAS “will review our audit coverage” over Corporate Investigations and Ethics Line, “to ensure that all appropriate processes are included” in the audits; and would do the same regarding customer complaints.<sup>1481</sup>

Finally, the Audit Program provided for testing and validating the controls – to include considering “testing a sample of the key controls for effectiveness,” reviewing the program to test “the associated controls for compliance with the applicable laws and regulations,” and

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<sup>1474</sup> Tr. (Julian) at 6881.

<sup>1475</sup> Tr. (Julian) at 6881.

<sup>1476</sup> Tr. (Julian) at 6881-82; OCC Ex. 705 at 11.

<sup>1477</sup> OCC Ex. 705 at 11.

<sup>1478</sup> *Id.*

<sup>1479</sup> Tr. (Julian) at 6884.

<sup>1480</sup> OCC Ex. 705 at 12.

<sup>1481</sup> Tr. (Julian) at 6885-86; OCC Ex. 705 at 11-12.

determining whether the issues were presented to the appropriate audience and that the reports were distributed to the appropriate audience.<sup>1482</sup>

Mr. Julian testified that he knew WFAS fulfilled its commitment to engage with the various lines of business – that they developed and implemented corrective actions in response to the June 2015 MRAs, because there was “formal reporting that went out with respect to” WFAS’s assessment of the activities going on, and because he “had ongoing dialogues with [WFAS] teams, both leadership team as well as project teams, the sales practices audit group that I had developed. So numerous conversations.”<sup>1483</sup> He testified that WFAS’s validation work with respect to MRAs Nos. 1 through 4 took place “mostly in 2016-2017”, but “a bit of it began late 2015 to the extent that any controls were changed, you know, that could be validated, meaning they went through the sustainability period.”<sup>1484</sup>

Through leading questioning by his Counsel during direct examination, Mr. Julian testified that he believed that the WFAS audit team responded to the issues raised in MRA #5 in good faith and that the team intended to promptly implement corrective actions.<sup>1485</sup> He also testified through leading questioning that prior to the 2016 Consent Order between Wells Fargo Bank and the OCC, he never received any negative feedback from the OCC regarding WFAS’s remediation efforts in response to the MRAs.<sup>1486</sup>

### **July 13, 2015 Report of Examination on Risks Present at Wells Fargo Bank, N.A.**

In the July 13, 2015 Report of Examination (ROE), the OCC through Bradley Linskens as Examiner in Charge and Ron Pasch as Deputy Comptroller, identified the need to proactively control reputational risks through “more effective compliance and operational risk programs.”<sup>1487</sup>

Elaborating on this point, the ROE included the following:

Two recent example [including Los Angeles sales practices lawsuit] involved employee misconduct, actual or alleged, on a scale that is difficult to reconcile with management’s perceptions of the risk culture within the firm. While we continue to assess the LA lawsuit, which alleges branch misconduct resulting in customer harm, our early findings suggest management should have responded more proactively to independently investigate the initial allegations. Management needs to ensure that matters such as these are fully and transparently investigated, harmed customers are remediated, bank

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<sup>1482</sup> R. Ex. 11817 at 6.

<sup>1483</sup> Tr. (Julian) at 6883

<sup>1484</sup> Tr. (Julian) at 6884.

<sup>1485</sup> Tr. (Julian) at 6886-87.

<sup>1486</sup> Tr. (Julian) at 6888-89.

<sup>1487</sup> R. Ex. 10015 at 5.

employees are properly trained, incentive programs do not encourage the alleged behavior, and controls are in place to identify and resolve potential or emerging issues.<sup>1488</sup>

As noted by Mr. Julian during direct examination, the OCC described Internal Audit as “Effective” adding, “we can rely on its work in most areas.”<sup>1489</sup> Responding to leading questioning by his Counsel during direct examination, Mr. Julian testified that this was consistent with the feedback that he received from the OCC on or about July 13, 2015.<sup>1490</sup>

Asked during direct examination what steps were taken after the Bank received Supervisory Letter WFC 2015-26, Mr. Julian responded:

Senior-level resources across all three lines of defense were tasked with developing responses to the MRAs. A senior-level person within corporate risk was tasked with coordinating the response. And, again, a significant amount of resources were applied to developing an appropriate response to the MRAs.<sup>1491</sup>

He identified an email chain that began with the OCC’s email transmitting the June 26, 2015 Supervisory Letter to CEO John Stumpf, with copies to Mr. Julian and Ms. Russ Anderson among others.<sup>1492</sup> It ended with two email messages from Mr. Julian, the first, sent on June 29, 2015 to Mr. McLinko and Mark Links, included the statement “I am going to schedule a meeting – who should be included – we will need to discuss our approach to this and how/who/where it should be led.”<sup>1493</sup> The second, sent after receipt of Mr. McLinko’s email answering initially who should participate in the meeting, said only “Should I have asked ‘who shouldn’t be included,’” followed by a happy face emoji.<sup>1494</sup>

Mr. Julian described attending a meeting the purpose of which was to allow Mr. Julian to “understand in more detail the OCC’s concerns as well as the OCC’s expectations for Wells Fargo to develop responses and to develop actions to address the issues raised.”<sup>1495</sup> He also acknowledged the responsibility WFAS would have for “ongoing monitoring and assessment of the responses that the business units, the various owners of the owners of the other four – or accountable folks of the other four MRAs.”<sup>1496</sup>

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<sup>1488</sup> R. Ex. 10015 at 5.

<sup>1489</sup> Tr. (Julian) at 6785-86; R. Ex. 10015 at 5.

<sup>1490</sup> Tr. (Julian) at 6786.

<sup>1491</sup> Tr. (Julian) at 6787.

<sup>1492</sup> Tr. (Julian) at 6788; R. Ex. 1039 at 4.

<sup>1493</sup> R. Ex. 1039 at 2.

<sup>1494</sup> *Id.* at 1.

<sup>1495</sup> Tr. (Julian) at 6789.

<sup>1496</sup> Tr. (Julian) at 6789-90.

Mr. Julian testified that Mr. McLinko, as the Executive Audit Director over the Community Bank, would be the point person for WFAS's response, as the Community Bank had "the predominant amount of sales practices effort" referred to in the MRA.<sup>1497</sup> Mr. Julian offered evidence of his overseeing Mr. McLinko's response to the Supervisory Letter, in the form of a one-page email from Mr. McLinko on July 28, 2015, sent to Mr. Julian and a dozen other Wells Fargo email addresses.<sup>1498</sup> Mr. Julian testified that Mr. McLinko's report through this email was "directly in response to the MRA No. 5 that was directed to Audit."<sup>1499</sup>

Through the message, Mr. McLinko noted "[g]ood progress on the responses to all MRAs so far" but declined to provide copies of those responses because the "current status" of those responses was that they were "in varying stages of completeness."<sup>1500</sup> He added that "[a]s it relates to the WFAS MRA, the only feedback we have received has been on style and formatting; nothing substantial at this point. Tomorrow, Kathy [Sheng] and I are meeting to develop a proposed go forward strategy to track progress against management's agreed upon actions and target dates for the 4 MRAs (one of our deliverables)."<sup>1501</sup>

As further evidence of Mr. Julian's response to the Supervisory Letter and its five MRAs, Mr. Julian identified a one-page email, again from Mr. McLinko and again addressed to several Wells Fargo email addresses, dated July 31, 2015.<sup>1502</sup> Through leading questioning presented by his Counsel during direct examination, Mr. Julian testified that this correspondence reflected that Mr. McLinko continued to meet with members of the OCC, that "they were comfortable with the actions that Audit was going to take," and that Mr. McLinko continued after this email to keep Mr. Julian in the loop as WFAS developed its plan for responding to the MRA.<sup>1503</sup>

Through leading questioning, Mr. Julian was able to testify that Mr. McLinko continued to have discussions with the OCC about WFAS's planned response to the June 2015 MRAs, and that the OCC "continued to be comfortable with the actions" of WFAS.<sup>1504</sup> Mr. Julian testified through leading questioning that at no time did any response from the OCC include feedback indicating that the examiners were uncomfortable in any way with WFAS's proposed response.<sup>1505</sup>

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<sup>1497</sup> Tr. (Julian) at 6790.

<sup>1498</sup> Tr. (Julian) at 6791; R. Ex. 10072.

<sup>1499</sup> Tr. (Julian) at 6791.

<sup>1500</sup> R. Ex. 10072 at 1.

<sup>1501</sup> *Id.*

<sup>1502</sup> Tr. (Julian) at 6793; R. Ex. 10100.

<sup>1503</sup> Tr. (Julian) at 6794.

<sup>1504</sup> Tr. (Julian) at 6794-95.

<sup>1505</sup> Tr. (Julian) at 6795.

Through the July 31, 2015 email from Mr. McLinko, the recipients were put on notice that Mr. McLinko identified the “accountable executives responsible for the parts of the response,” but that – because the response identified respondents at the level of Executive Audit Directors, the response “did not include” Mr. Julian although Mr. McLinko wrote that this could change at Mr. Julian’s direction, if “[Mr. Julian would] like us to put your name for all of it (it’s easy to change).”<sup>1506</sup>

Notwithstanding Mr. Julian’s testimony to the contrary, Mr. McLinko identified areas with which the OCC Examiners had concerns. One area appeared to be an area about which Mr. McLinko had no immediate answer:

Kathy [presumably Sheng] and I met with Jenny and Chris of the OCC on Thursday afternoon to review the draft. They asked some clarifying questions but appeared to be comfortable with the actions we were going to take. I’d say the biggest concern they had was the type of work we’re doing as the business develops and implements the corrective actions (4<sup>th</sup> full paragraph of the response) and the reporting of the work. We told them we’ll determine that once we get into the work itself. They seemed happy with the answer (Kath, if you feel otherwise please speak up). Also from the discussion, we did add a sentence about the current complaints work were [*sic*] doing (with Mark L’s guidance).<sup>1507</sup>

#### **WFAS’s Presentation to the A&E Committee: July 28, 2015**

Mr. Julian identified the minutes of the WF&C A&E Committee meeting of July 28, 2015, which meeting he said he attended.<sup>1508</sup> He also identified the WFAS Second Quarter 2015 Summary that was submitted to members of the Committee in advance of the meeting.<sup>1509</sup>

The minutes of the July 28, 2015 meeting include a summary of Mr. Julian’s report to the Committee.<sup>1510</sup> The minutes are silent with respect to *any* issues regarding sales practices misconduct attributed to team members of the Community Bank.<sup>1511</sup> The Report identified two engagements as “Unsatisfactory” – Specialized Lending Services & Trust, and Unix Security – neither of which identified either the Community Bank or sales practices misconduct.<sup>1512</sup> It identified 40 rated projects or initiatives for 2Q15 – none of which concerned first- or third-line

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<sup>1506</sup> R. Ex. 10100 at 1.

<sup>1507</sup> *Id.*

<sup>1508</sup> Tr. (Julian) at 6800; R. Ex. 20486.

<sup>1509</sup> Tr. (Julian) at 6801-02; R. Ex. 10038 (Summary), which appears to be a color version of the black and white version of the Summary found at OCC Ex. 2157; R. Ex. 10067 (transmittal email).

<sup>1510</sup> R. Ex. 20486 at 1-2.

<sup>1511</sup> *Id.* at 2.

<sup>1512</sup> *Id.* at 3.

of defense risk management controls related to sales practices misconduct by team members at the Community Bank.<sup>1513</sup>

In his testimony about the contents of the July 2015 Summary, Mr. Julian asserted that the written Summary “communicated that the risk in the Community Bank remained heightened and increasing related to reputational and regulatory environment, specifically calling out the issuance to the City of Los Angeles lawsuit related to alleged improper sales practices, the issuance of the OCC report related to enterprise sales practices.”<sup>1514</sup>

The written July 2015 Summary included the following:

### **Community Banking**

Risk in Community Banking remains heightened and increasing related to reputation and regulatory environment. Ongoing media and regulatory scrutiny place additional pressure on management to ensure customers have a positive experience in all channels. This was especially evident in the second quarter with the recent issuance of the city of Los Angeles lawsuit alleging improper sales practices, along with the issuance of the OCC report related to enterprise sales practices. WFAS will be working with management as they develop their formal responses to the issues. In addition, we will monitor corrective actions related to enterprise sales practices, including those impacting Community Banking, and adjust our audit plan as warranted. The efforts of Community Banking, along with the large number of corporate initiatives impacting the business, continue to be a challenge and strain existing resources.<sup>1515</sup>

This Summary closely aligns with the Summary presented in August 2014, which described the risk trend as “stable.”<sup>1516</sup> With no reference to the failure of either WFAS or the Community Bank to identify the root cause of sales practices misconduct by Community Bank team members reported by the Times article, the August 2014 Quarterly Report included the following:

Community Banking risk remains heightened related to reputation and regulatory change. Ongoing media and regulatory scrutiny place additional pressure to ensure customers have a positive experience in all channels including stores, call centers, digital channels, and ATMs. This includes meeting the technology needs of the millennial generation as well as competing with non-bank entities.

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<sup>1513</sup> R. Ex. 10038 at 12.

<sup>1514</sup> Tr. (Julian) at 6911.

<sup>1515</sup> OCC Ex. 2157 at 25.

<sup>1516</sup> R. Ex. 6584 at 20.

The risk trend is stable, and Community Banking has taken appropriate measures to continuously evaluate and enhance channel usability to meet the needs of the customer. Additionally, Community Banking continues to evaluate product offerings, pricing, and sales strategies to ensure customers are obtaining the products and services that help them achieve their financial goals.<sup>1517</sup>

In the “mid-year review,” the Second Quarter 2015 Summary recognized that the “audit plan is dynamic throughout the year,” and avers “WFAS performs a mid-year review as part of our audit methodology to ensure our audit plan remains focused on key and/or emerging risk areas and adequate resources are available to complete the audit plan.”<sup>1518</sup>

Notwithstanding that neither Internal Audit nor the first or second lines of defense had identified one or more root causes for the sales practices misconduct issues raised by Mr. Bacon’s reporting, the 2013 L.A. Times articles, or the 2015 city of Los Angeles lawsuit, the Second Quarter 2015 Summary stated “WFAS management is comfortable with progress to date towards the original plan presented at the February 24, 2015, A&E Committee meeting.”<sup>1519</sup>

Notwithstanding that the 2015 Summary expressly found that “WFAS needs to reassess their coverage of sales practices at an enterprise level and develop an Enterprise Risk Management Assessment (ERMA) process for sales practices,”<sup>1520</sup> the mid-year review reported only the need to “expand focus on activities such as consent order remediation, BSA/AML, Volker, regulatory reporting, and cybersecurity,” but made no mention of the need to test the efficacy of first- and second-line of defense controls in place at the Community Bank relating to sales practices misconduct issues.<sup>1521</sup>

Mr. Julian identified the 2015 Performance Assessment he received from Mr. Quigley, who was at that time Chair of the WF&C A&E Committee.<sup>1522</sup> Mr. Julian testified that Mr. Quigley provided a review of Mr. Julian’s performance, including with respect to regulatory expectations.<sup>1523</sup> Mr. Quigley reported that within the context of regulatory expectations, the OCC “has determined that WFAS has met their expectations of the Heightened Standards”, and that “none of our peer bank Audit functions has as favorable ratings on the four components.”<sup>1524</sup> Mr. Julian testified that during this performance review Mr. Quigley expressed no concerns with

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<sup>1517</sup> *Id.* at 20.

<sup>1518</sup> OCC Ex. 2157 at 36.

<sup>1519</sup> *Id.*

<sup>1520</sup> *Id.* at 43.

<sup>1521</sup> *Id.* at 36.

<sup>1522</sup> Tr. (Julian) at 6939; R. Ex. 20762.

<sup>1523</sup> Tr. (Julian) at 6940-41; R. Ex. 20762 at 2.

<sup>1524</sup> R. Ex. 20762 at 2.



respect to sales practices issues.<sup>1525</sup> Nothing in the record, however, suggests that by the time this Assessment was written Mr. Julian had disclosed to Mr. Quigley that neither he nor any of his subordinates at WFAS would identify the true scope and extent of, nor the root cause of, sales practices misconduct by the Community Bank's team members.

#### **WFAS's Presentation to the A&E Committee: November 17, 2015**

Mr. Julian identified the minutes of the November 17, 2015 meeting of the WF&C A&E Committee, and confirmed that he made a presentation during that meeting.<sup>1526</sup> He testified that he made presentations both with regard to the WFAS Third Quarter 2015 Summary report and the OCC's findings from its annual exam.<sup>1527</sup>

The minutes of the November 17, 2015 A&E concerning the Chief Auditor's Report make no reference to any presentation by Mr. Julian regarding the efficacy of risk-management controls in the Community Bank's first line of defense regarding sales practices misconduct relating to team members of the Community Bank.<sup>1528</sup> He testified that his discussion with the Committee members concerning "the status of the 2015 Internal Audit Plan" and "areas of focus" took place in executive session.<sup>1529</sup>

The minutes regarding what was discussed during executive session do not reflect any content relating to audits underway or planned regarding sales practices misconduct by Community Bank team members.<sup>1530</sup> The only entry reflecting the discussion during executive session stated, "The Committee met in executive session with representatives of KPMG and discussed the 2015 PCAOB inspection report and KPMG's response and the status of the 2015 audit."<sup>1531</sup> Inasmuch as Mr. Julian was not a member of the Committee and the minutes make no reference to his being present during the session, there is no substantial evidence supporting Mr. Julian's testimony regarding any discussion during this part of the Committee meeting relating to issues material to this enforcement action.<sup>1532</sup>

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<sup>1525</sup> Tr. (Julian) at 6941.

<sup>1526</sup> Tr. (Julian) at 6922-23; R. Ex. 11908.

<sup>1527</sup> Tr. (Julian) at 6923.

<sup>1528</sup> R. Ex. 11908 at 5.

<sup>1529</sup> Tr. (Julian) at 6924.

<sup>1530</sup> R. Ex. 11908 at 5.

<sup>1531</sup> *Id.* at 7.

<sup>1532</sup> *Id.*

Mr. Julian testified that his administrative assistant sent on his behalf the WFAS Third Quarter 2015 Summary, dated November 17, 2015 to the OCC.<sup>1533</sup> The record reflects, however, that the Summary was not sent until the day after the Committee met.<sup>1534</sup>

The Third Quarter 2015 Summary reported “recurring themes with increasing risk trend,” including the “lack of transparent risk identification”.<sup>1535</sup> Specifically, “Management across the various OCGs and lines of defense are not accurately and transparently recording applicable risks and control deficiencies.”<sup>1536</sup> Further, the Summary reported deficiencies in knowledge and skill: “While many business functions supporting mitigation of key risks continue to increase staffing levels, issues continue to surface resulting from staff that lack sufficient skill, training, and knowledge.”<sup>1537</sup>

Without identifying the Community Bank (or any other line of business), the Summary identified as a theme the ineffective first line of defense testing and monitoring, “WFAS continues to report issues that point to an oversight or lack of credible challenge from first line of defense testing and monitoring. Many issues relate to required testing functions that are in place but are not testing all key attributes or are not providing effective challenge to the business when identifying issues.”<sup>1538</sup>

The results of WFAS engagements with Operating Committee Groups (OGC) included a report reflecting that the OCC issued a Supervisory Letter on June 26, 2015 that included “five MRAs covering all lines of defense (one specific to Community Banking).”<sup>1539</sup> Through the 3Q15 Summary WFAS committed to working with “various teams/workstreams to monitor corrective actions impacting Community Banking, and adjust our audit plan as warranted.”<sup>1540</sup> WFAS also reported that it would “participate in validating the corrective actions once management has completed remediation.”<sup>1541</sup>

Repeating one part of the Summary from WFAS’s Second Quarter 2015 Summary, the Third Quarter 2015 Summary reports that the “efforts of Community Banking with sales practices, along with the large number of corporate initiatives impacting the business, continue to

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<sup>1533</sup> Tr. (Julian) at 6925; OCC Ex. 2228.

<sup>1534</sup> Tr. (Julian) at 6926; R. Ex. 11351 at 1.

<sup>1535</sup> OCC Ex. 2228 at 19.

<sup>1536</sup> *Id.*

<sup>1537</sup> *Id.*

<sup>1538</sup> *Id.* at 20.

<sup>1539</sup> *Id.* at 24.

<sup>1540</sup> *Id.*

<sup>1541</sup> *Id.*

be a challenge and strain existing resources.”<sup>1542</sup> There is, however, nothing in Mr. Julian’s testimony indicating that the Summary from either the Second or Third Quarter included a request by either Mr. Julian or Mr. McLinko for additional WFAS resources to meet such strain.

Mr. Julian noted that during a meeting of the WF&C Risk Committee held on February 22, 2016, *i.e.*, the day before the A&E Committee met, Corporate Risk prepared for that Committee a Noteworthy Risk Issues report.<sup>1543</sup> Through leading questioning by his Counsel during direct examination, Mr. Julian testified that as of February 2016 he was not aware of any other information regarding sales practices that needed to be, but had not been, escalated to the Board of Directors.<sup>1544</sup> Nothing in the Noteworthy Risk Issues indicated that neither WFAS nor the Community Bank had identified, disclosed, or escalated, the root cause of issues related to ineffective controls related to sales practices misconduct by team members of the Community Bank.<sup>1545</sup>

### **WFAS’s Presentation to the A&E Committee: February 23, 2016**

Mr. Julian identified WFAS’s Fourth Quarter 2015 Summary presented to the WF&C A&E Committee on February 23, 2016, testifying specifically about the “Audit Coverage and Update” section describing “Sales Conduct, Practices and Business Model”.<sup>1546</sup> From the 147-page Summary, Mr. Julian identified the following language, which is found in the section titled “3.9.1 ERMC “Noteworthy Risks””.<sup>1547</sup> The entry in the Quarterly Summary relating to Community Banking stated, “Within Community Banking, the Regional Banking – Account Opening Audit is nearing completion and is being coordinated with Wells Fargo’s counsel. The focus of the review is account opening and sales practices.”<sup>1548</sup> According to Mr. Julian, this statement was a reference to what became the March 18, 2016 WFAS Regional Banking – Account Opening Audit.<sup>1549</sup>

Mr. Julian also identified the WFAS 2016 Audit Plan, dated February 23, 2016, which he said he presented to the A&E Committee during the February 23, 2016 Committee meeting.<sup>1550</sup> He testified, “the plan is a bottoms-up and top-down type of planning approach that a number of

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<sup>1542</sup> OCC Ex. 2228 at 25. See OCC Ex. 2157 at 25: “The efforts of Community Banking, along with the large number of corporate initiatives impacting the business, continue to be a challenge and strain existing resources.”

<sup>1543</sup> Tr. (Julian) at 6956; OCC Ex. 687.

<sup>1544</sup> Tr. (Julian) at 6957.

<sup>1545</sup> OCC Ex. 687 at 3.

<sup>1546</sup> Tr. (Julian) at 6874-75; R. Ex. 11995 at 64.

<sup>1547</sup> Tr. (Julian) at 6875; R. Ex. 11995 at 63-64.

<sup>1548</sup> R. Ex. 11995 at 64.

<sup>1549</sup> Tr. (Julian) at 6875.

<sup>1550</sup> Tr. (Julian) at 6944; R. Ex. 12031.

[WFAS] folks are engaged in.”<sup>1551</sup> His own role was “assuring there was a methodology for developing the plan was in place and being followed,” as well as “having various dialogues with senior leadership with respect to their individual plans as well as the overall plan.”<sup>1552</sup> He offered no documentary evidence establishing what he did to assure there was a methodology for developing any such plan, nor establishing the nature or timing of these dialogues, nor did he identify any participants in those dialogues.

The Audit Plan reflected that sales practices was one of eleven “primary areas of focus” and according to Mr. Julian WFAS carried out the work set out in the Plan.<sup>1553</sup> Through leading questioning by his Counsel on direct examination, Mr. Julian testified that increases in control testing reflected in the Plan were consistent with the June 2015 MRA response.<sup>1554</sup> He said the A&E Committee approved the Audit Plan and the Plan was shared with the entire Wells Fargo Board of Directors, the OCC, and other regulators.<sup>1555</sup> The record reflects that the Plan was shared with the OCC at 5 p.m. on the day of the A&E Committee meeting.<sup>1556</sup> He testified that no one from the OCC ever raised any concerns with him about WFAS’s coverage of sales practices in the 2016 Audit Plan.<sup>1557</sup>

The minutes of the February 23, 2016 A&E Committee meeting indicate that during his presentation of the 2016 Audit Plan, Mr. Julian did not mention sales practices misconduct issues relating to the Community Bank; that he “commented on the areas of focus, including cyber security, consent orders, and regulatory compliance, and the types of engagements, including control testing and business monitoring.”<sup>1558</sup> Mr. Julian is reported as saying the Plan “includes an increase in staffing levels and responded to Committee members’ questions regarding the adequacy of resources and the increase in staffing over the past four years.”<sup>1559</sup> There is no indication that Mr. Julian expressed the view that resources were strained.<sup>1560</sup>

With respect to sales practices being an “area of focus,” the Audit Plan reported, “WFAS continues to monitor the business actions to address the MRAs related to Sales Practices.”<sup>1561</sup> The report stated WFAS “will review both the Accenture and PricewaterhouseCoopers’ (PwC)

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<sup>1551</sup> Tr. (Julian) at 6945.

<sup>1552</sup> Tr. (Julian) at 6945-46.

<sup>1553</sup> R. Ex. 12031 at 13-15.

<sup>1554</sup> Tr. (Julian) at 6947.

<sup>1555</sup> Tr. (Julian) at 6948; R. Ex. 11996 (transmittal email).

<sup>1556</sup> R. Ex. 11996.

<sup>1557</sup> Tr. (Julian) at 6949.

<sup>1558</sup> R. Ex. 12389 at 2.

<sup>1559</sup> *Id.*

<sup>1560</sup> *Id.*

<sup>1561</sup> R. Ex. 12031 at 14.

final reports and incorporate learnings from these reports to enhance our audit plan throughout 2016.”<sup>1562</sup> There is no reference to audit activity involving controls testing – only business monitoring.<sup>1563</sup>

The minutes reflect the Committee’s approval of the WFAS 2016 Charter, which Mr. Julian presented during the Committee meeting.<sup>1564</sup> That Charter included a provision that states the Chief Auditor reports functionally to the Chairman of the A&E Committee and administratively to the CEO, and along with the staff of the internal audit department has the responsibility to “ensure effective actions are taken to strengthen reported control weakness or uncontrolled risks.”<sup>1565</sup>

The minutes reflect Mr. Julian presented WFAS’s Fourth Quarter 2015 Summary.<sup>1566</sup> That Summary reported WFAS “continues to monitor the business actions to address the MRAs related to Sales Practices.”<sup>1567</sup> It reported that a “Sales Practices Standard Audit Program (SAP) has been developed” and “a Sales Practices Coverage Strategy document is being finalized.”<sup>1568</sup> It reported, “as part of the 2016 plan, we will issue the ERMA opinion for Sales Practices in 1Q17.”<sup>1569</sup> The record reflects that a copy of this Summary was provided to the OCC by Mr. Julian’s staff at 5 p.m. on the day of the Committee meeting.<sup>1570</sup>

Mr. Julian was asked to recall testimony from Examiner Smith to the effect that after the June 2015 Supervisory Letter, the Regional Banking – Account Opening Audit was the only audit looking at account opening; and upon inquiry he responded, “Well, again, that’s just not correct.”<sup>1571</sup> Asked why he would say that, he responded “there was significant activity after the – after the Supervisory Letter date, both, as we’ve reviewed, business monitoring as well as control testing as well as project auditing”, positing that “around 100,000 hours” of audit work had been planned with regard to sales practices issues around that time.<sup>1572</sup> In this response, however, Mr. Julian presented no documentary evidence supporting his averment regarding business monitoring, control testing, or project auditing.

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<sup>1562</sup> R. Ex. 12031 at 14.

<sup>1563</sup> *Id.*

<sup>1564</sup> Tr. (Julian) at 6950; R. Ex. 425.

<sup>1565</sup> R. Ex. 425 at 2.

<sup>1566</sup> Tr. (Julian) at 6952; R. Ex. 11995.

<sup>1567</sup> R. Ex. 11995 at 5.

<sup>1568</sup> *Id.*

<sup>1569</sup> *Id.*

<sup>1570</sup> Tr. (Julian) at 6955; R. Ex. 11994.

<sup>1571</sup> Tr. (Julian) at 6876.

<sup>1572</sup> Tr. (Julian) at 6876.

Through leading questioning by his Counsel during direct examination, Mr. Julian testified that in light of all the work he discussed during his testimony, the March 2016 WFAS Regional Banking – Account Opening Audit “added no value with respect specifically to sales practices” because “sales practices activity was scoped out of that audit; therefore it wasn’t intended to add value with respect to sales practices.”<sup>1573</sup> He testified that these Summary findings told him that “the controls [at the Community Bank] were continuing to work and that the enhancements to the processes and controls were also having a difference.”<sup>1574</sup> This testimony identified no controls, however, so the record does not support Mr. Julian’s claim that the Community Bank’s enhancements or controls were making a difference.

The year-to-date case trends were more specific, indicating that from Core Committee reviews, there were nine sales practices cases opened, 94 resulting terminations involving “6 or more terminations outside of LA-OC, 3 or more in LA-OC (2 cases)”.<sup>1575</sup> The report states that sales practices case activity went from a high of 775 cases in 2Q14, to a low of 540 in 3Q15.<sup>1576</sup>

### **Community Banking Enterprise Risk Management Assessment (ERMA) - 2015 (issued March 8, 2016)**

On March 8, 2016, WFAS, through Mr. McLinko, issued its 2015 Community Banking Enterprise Risk Management Assessment.<sup>1577</sup> Mr. Julian identified the Assessment, but testified he was not a recipient of the ERMA because “[t]his was a specific line of business enterprise risk management assessment, and so typically I wouldn’t be copied” on it.<sup>1578</sup> He testified that the process of developing the Community Bank ERMA was led by Mr. McLinko and was “bottoms up” where “each line of business prepared their line of business ERMAs” – so “this was a result of that work that they prepared and were presenting it to their respective line of business management.”<sup>1579</sup> Mr. Julian denied having any role in creating the Community Bank’s ERMA.<sup>1580</sup> He testified that he “would have had discussions with Paul, possibly including his team, as they were developing . . . this line of business ERMA . . . so I would have had dialogue. I don’t know that I would have necessarily received and reviewed this.”<sup>1581</sup>

The Assessment reports that it is “designed to evaluate the adequacy of risk management within CB for those risks that could impact their ability to effectively meet their business

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<sup>1573</sup> Tr. (Julian) at 6877.

<sup>1574</sup> Tr. (Julian) at 6920.

<sup>1575</sup> R. Ex. 13775 at 3.

<sup>1576</sup> *Id.* at 4: 1Q14 - 770, 2Q14 - 775, 3Q14 - 711, 4Q14 -660, 1Q15 - 665, 2Q15 - 626, 3Q15 540.

<sup>1577</sup> OCC Ex. 750.

<sup>1578</sup> Tr. (Julian) at 6958.

<sup>1579</sup> Tr. (Julian) at 6959.

<sup>1580</sup> Tr. (Julian) at 6960.

<sup>1581</sup> Tr. (Julian) at 6960.

objective.”<sup>1582</sup> The overall assessment was that “risk management practices are effective in anticipating and escalating issues and emerging risks, as necessary.”<sup>1583</sup> The Assessment found that “[m]odel risk processes and controls are effectively designed, implemented, and have demonstrated sustainability during 2015.”<sup>1584</sup>

The Assessment included commentary regarding the five MRAs then pending:

In 2015, the OCC issued five MRAs related to enterprise sales practices covering all lines of defense; one of which was issued specifically to Community Banking. In addition, two of the MRAs have corrective action components that specifically relate to incentive compensation. Management recognizes the significance of these issues and their impact on reputation. Since mid-2013, CB has been on a multi-year journey to evolve their model for product and service delivery. Progress continues to be made in these areas. Management has also begun multiple initiatives to address the Sales Practices MRAs. These include, but are not limited to enhanced Store Operations and Control Review (SOCR) questions, implementation of mystery shopping, customer-complaint policy implementation and enhanced performance management plans. In addition, management is expanding sales practices oversight in areas such as enhanced reporting, trending, ethics line procedures, training and risk management (e.g., Regional Services, RB Compliance and Operational Risk, and Sales & Service Conduct and Oversight teams, Conduct Risk Committee, etc.). Combined these activities have a positive impact on the risk management environment.<sup>1585</sup>

The Assessment included notice that Wells Fargo “deferred its 2015 annual risk self-assessment completed by the first line of defense.”<sup>1586</sup> Elaborating, the Assessment reported, “2015 was a year of significant change and transition for the Company with the implementation of various functional frameworks, significant initiatives across Corporate Risk including Compliance, BSA/AML, and Operational Risk as well as technology changes used to support the self-assessment process.”<sup>1587</sup> The stated rationale included the following:

An objective of the 2015 risk self-assessment effort was to align it with the Corporate Risk Management Framework. Functional frameworks, a critical element in defining the first line responsibilities for the key risk types, continued to be developed and implemented throughout 2015. There were

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<sup>1582</sup> OCC Ex. 750 at 1.

<sup>1583</sup> *Id.*

<sup>1584</sup> *Id.* at 2.

<sup>1585</sup> *Id.*

<sup>1586</sup> *Id.* at 23.

<sup>1587</sup> *Id.*

also other significant initiatives across Corporate Risk that created a high level of change across the organization. It was determined that there would be more value in doing the first line risk-self-assessment when the functional frameworks were further matured, and the initiatives were further implemented.<sup>1588</sup>

### **WFAS's Presentation to the A&E Committee: April 25, 2016**

Mr. Julian testified that he made a presentation during the A&E Committee's April 25, 2016 meeting, and identified the minutes from that meeting.<sup>1589</sup> The minutes reflect that Mr. Julian "commented on the positive trends for the month, including a decline in the number of open MRAs and no MRAs that were reopened."<sup>1590</sup> The minutes reflect that Mark Links "presented a report on the [WFAS] 2015 Enterprise Risk Management (ERM) Assessment" but nothing in the minutes indicated that Board members were presented with the recently issued 2015 Community Banking Enterprise Risk Management Assessment.<sup>1591</sup> Mr. Julian testified that Mr. Links was an Executive Audit Director with primary audit oversight of Corporate Risk, who "headed up the overall process for developing the enterprise-wide ERMA assessment."<sup>1592</sup>

The 2015 ERMA that Mr. Links presented to the A&E Board on April 25, 2016 concluded that as of December 31, 2015, Enterprise Risk Management at WF&C "Needs Improvement" under a rating system using three ratings – Satisfactory, Needs Improvement, and Weak.<sup>1593</sup> In its report on Organizational Risk, the Assessment found "the second line of defense needs to continue implementing new governance requirements. Challenges remain for the first line of defense in oversight, risk identification, risk assessment, operational risk, testing, and program maturity/sustainability, as shown by High related issues and regulatory concerns (i.e., MRAs and MRIAs). First line of defense operational risk management practices are evolving and work remains to align practices with the enhanced framework."<sup>1594</sup>

Asked to describe his role in the development of the 2015 enterprise-wide ERMA, Mr. Julian stated he "would have engaged with individuals, such as Paul McLinko and others who were EADs, with respect to their individual line of business ERMA's, and then engaged in discussions with the audit management group as the enterprise-wide view was being consolidated."<sup>1595</sup>

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<sup>1588</sup> OCC Ex. 750 at 23.

<sup>1589</sup> Tr. (Julian) at 6961; R. Ex. 20631.

<sup>1590</sup> R. Ex. 20631 at 4.

<sup>1591</sup> Tr. (Julian) at 6965; R. Ex. 20631 at 4-5.

<sup>1592</sup> Tr. (Julian) at 6965.

<sup>1593</sup> R. Ex. 1144 at 2.

<sup>1594</sup> *Id.* at 2-3.

<sup>1595</sup> Tr. (Julian) at 6967.



Mr. Julian identified a Sales Practices MRA Status Update dated April 29, 2016 from Mr. McLinko and others to Claudia Russ Anderson and others providing a summary of corrective actions relating to the five MRAs issued in 2015.<sup>1596</sup> The Update included in its “highlights” section that “management developed a dashboard to track the corrective action plan and progress.”<sup>1597</sup> The Update also noted that “Management has extended due dates on four corrective actions related to the independent evaluation of allegations of inappropriate behavior, risk appetite metrics, root cause analysis of sales integrity violations, and identifying complaints involving UDAP. These corrective actions are associated with MRAs 1, 2, and 3.”<sup>1598</sup> Mr. Julian offered no explanation for why these deadlines were extended or how these extensions affected risk management in the Community Bank.

Regarding MRA #2, which addressed second line of defense enterprise-wide sales practices oversight, the Update reported a *second* due-date extension on the corrective action to “conduct a root cause analysis of sales integrity violations”.<sup>1599</sup> “In 4Q15, due date was changed to 3/31/16, and has now been revised to 8/31/16. Management reassessed the strategy and determined that additional time was needed to ensure that the end result provides value and contributes to improved processes for sales practices risk management.”<sup>1600</sup>

The Update further reported that because “[c]ompletion of the traceability matrix is contingent upon the independent [Sales Practices Risk] assessments, as well as the root cause analysis of sales integrity violations,” the due date for conducting the integration of Sales Practices risk assessments and completing traceability to corrective actions was revised, from 6/30/16 to 8/31/16.”<sup>1601</sup>

Regarding MRA #3 (Complaints), the Update reported the Corporate Risk validation, which would have included an “appropriate mitigation plan to track, manage, and report customer complaints” which originally was 3/31/16, was *extended* to 5/31/16 “in order to review the frameworks to ensure alignment across multiple policy and reporting requirements.”<sup>1602</sup>

Through leading questioning by his Counsel during direct examination, Mr. Julian testified that at the time he received the April 29, 2016 Update, he was satisfied with WFAS’s

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<sup>1596</sup> Tr. (Julian) at 6973; R. Ex. 1062 (Memo); R. Ex. 12478 (transmittal email from Paul McLinko to David Julian).

<sup>1597</sup> R. Ex. 1062 at 1.

<sup>1598</sup> *Id.* at 2.

<sup>1599</sup> *Id.* at 3.

<sup>1600</sup> *Id.*

<sup>1601</sup> *Id.*

<sup>1602</sup> *Id.*

progress on its validation and remediation work in response to the MRAs.<sup>1603</sup> Nothing in this answer provided reasons for Mr. Julian’s satisfaction.

Asked whether he agreed with the ratings reported in the 2015 ERMA, Mr. Julian responded, “I had no reason not to, based on information I knew at the time.”<sup>1604</sup> Notwithstanding the lack of root cause determinations related to the issues raised by Mr. Bacon and those regarding the Community Bank following the 2013 L.A. Times articles and the City of Los Angeles’ 2015 lawsuit, the Assessment found the first line of defense in Community Banking was “Satisfactory”.<sup>1605</sup>

Mr. Julian did not dispute that the 2015 ERMA does not state that sales practices misconduct was systemic; instead, he testified that the ERMA “wasn’t specific to sales practices at all. It was specific to the overall state of risk management within Wells Fargo Corporation [*sic*]”.<sup>1606</sup> He added that at this time, WFAS “didn’t have a basis for drawing an overall ERMA assessment on sales practices risk management.”<sup>1607</sup> Unclear from this answer is whether its failure to identify or report the root cause of sales practices misconduct was the reason WFAS did not have a basis for drawing an overall assessment on sales practices risk management.

Mr. Julian also did not dispute that the 2015 ERMA does not state that there were significant risk management or control breakdowns within the Community Bank.<sup>1608</sup> He responded that “the ERMA provides an overall rating, for instance, of Community Bank’s risk management; not just taking – not just a rating of one – one risk-type activity. It was a reflection of all the risk management across the Community Bank.”<sup>1609</sup>

Without challenging the underlying premise that the 2015 ERMA lacked information material to the issues presented by the L.A. Times articles and the 2015 city of Los Angeles lawsuit, through leading questioning by his Counsel during direct examination Mr. Julian testified that the 2015 ERMA was not the only means by which he was communicating with the A&E Committee concerning the sales practices situation at the Community Bank.<sup>1610</sup>

The minutes reflect that in his Internal Audit Update, Mr. Julian “reported on issue management trends and the regulators’ perception that the Committee is not receiving enough information about past due and protracted issues and issues with revised dates. Committee

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<sup>1603</sup> Tr. (Julian) at 6974.

<sup>1604</sup> Tr. (Julian) at 6968.

<sup>1605</sup> R. Ex. 1144 at 3.

<sup>1606</sup> Tr. (Julian) at 6969.

<sup>1607</sup> Tr. (Julian) at 6969.

<sup>1608</sup> Tr. (Julian) at 6969.

<sup>1609</sup> Tr. (Julian) at 6969-70.

<sup>1610</sup> Tr. (Julian) at 6970.

members and management discussed the circumstances surrounding past due and protracted issues and the information provided to the Committee.”<sup>1611</sup>

Mr. Julian identified the WFAS First Quarter 2016 Summary, presented to the A&E Committee for its April 25, 2016 meeting and presented to the OCC on July 22, 2016 (delivered along with the Second Quarter A&E Summary).<sup>1612</sup>

Through the First Quarter 2016 Summary presented to the A&E Committee on April 25, 2016, WFAS reported:

WFAS continues to monitor the business actions to address the MRAs related to Sales Practices. Validation is in progress on corrective actions related to Visions and Values, independent review of Wells Fargo’s Enterprise Sales Practices approach, Enterprise Sales Practices Risk Governance Framework, and Sales Practices Risk Governance Document. Overall, the business is on track to complete the necessary corrective actions to address the MRAs. WFAS issued the 4Q15 Sales Practices quarterly report and continues to execute the 2016 coverage approach for sales practices.<sup>1613</sup>

Mr. Julian identified WFAS’s Sales Practices Coverage Strategy, updated May 2016.<sup>1614</sup> He said this update “provides an overview of how [WFAS] would provide sales practices coverage.”<sup>1615</sup> Through leading questioning by his Counsel during direct examination, Mr. Julian opined that the strategy document was a significant milestone in WFAS’s response to the June 2015 Sales Practices MRAs.<sup>1616</sup>

Through the Coverage Strategy, WFAS reported that as the third line of defense, it is “responsible for executing a systematic and disciplined approach to evaluate and improve the effectiveness of Wells Fargo’s risk management, control and governance processes.”<sup>1617</sup> It identified the Enterprise Risk Management (ERM) audit team, within the Corporate Risk audit team, as “the coverage owner for Sales Practices risk for WFAS.”<sup>1618</sup> It distinguishes the responsibilities between it and the specific line of business audit teams:

Although the specific LOB audit teams are responsible for audit execution for RABUs where Sales Practices risk applies, ERM audit team is responsible for coordinating and providing guidance to other audit teams. ERM audit

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<sup>1611</sup> R. Ex. 20631 at 5.

<sup>1612</sup> Tr. (Julian) at 6963, 6993-94; R. Ex. 406 (1Q16 WFAS Summary); R. Ex. 13098 (transmittal email).

<sup>1613</sup> R. Ex. 406 at 6.

<sup>1614</sup> Tr. (Julian) at 6975; R. Ex. 1095.

<sup>1615</sup> Tr. (Julian) at 6975.

<sup>1616</sup> Tr. (Julian) at 6976.

<sup>1617</sup> R. Ex. 1095 at 2.

<sup>1618</sup> *Id.*

team is responsible for coordinating WFAS audit coverage including . . . [p]roviding audit coverage of Second Line of Defense (SLOD), Sales Practices Oversight under Corporate Enterprise Risk Management . . . [and] [a]ttending scope meetings for audits covering Sales Practices to share information and provide guidance to promote consistent coverage of Sales Practices.<sup>1619</sup>

The Coverage Strategy described the audit approach for the first line of defense in these terms, as related to Community Banking:

Community Banking (CB) sales practices have historically been covered in several RABUs (e.g., Regional Banking, Wells Fargo Virtual Channels Digital and Contact Centers, Business Banking, etc.), along with BMP [Business Monitoring Program]. Coverage has included testing controls over sales quality, account opening and incentive compensation across a variety of line of business audits based on risk and corresponding horizon. Coverage for CB incentive compensation has migrated in the last year to align with the WFAS division approach managed by the FCA team. In addition, CB coverage has also included testing in areas such as consumer complaints and cross sell metric reporting.<sup>1620</sup>

The Coverage Strategy reported that CB audit coverage for 2016 “will include a combination of control testing, business monitoring and validation activities.”<sup>1621</sup> Coverage included monitoring and tracking “CB progress on corrective actions for the Sales Practices OCC MRAs (MRA #4 and the CB portion of MRA #3) and will perform validation testing according to established timelines.”<sup>1622</sup> This audit work included “initiatives related to enhanced SOCR (Store Operations Control Review) testing, implementation of mystery shopping, expanded sales practices oversight, etc.”<sup>1623</sup>

### **WFAS Regional Bank Sales Practices Coverage Report to the OCC – June 2016**

Mr. Julian identified a report titled WFAS Regional Sales Practices Coverage dated June 2016, and stated that Mr. McLinko presented the report to members of the OCC on June 14, 2016.<sup>1624</sup> Mr. Julian testified the report was “intended to convey the significant amount of work that had been going on within the [WFAS] group related to sales practices within the Regional

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<sup>1619</sup> R. Ex. 1095 at 2-3.

<sup>1620</sup> *Id.* at 4.

<sup>1621</sup> *Id.*

<sup>1622</sup> *Id.*

<sup>1623</sup> *Id.* at 5.

<sup>1624</sup> Tr. (Julian) at 6979-81; R. Ex. 12822 (6/1/16 email from MR. JULIAN to OCC – Crosthwaite and Linskens – to arrange a conference call); R. Ex. 12890 (6/14/16 email from McLinko to OCC – Linskens et al. – transmitting report); R. Ex. 12891 (WFAS Regional Bank Sales Practices Coverage June 2016).

Bank.”<sup>1625</sup> Through leading questioning by his Counsel during direct examination, Mr. Julian testified that the audit group was reporting on its “audit of controls” and describing that the group was “providing assessments of governance activities and monitoring work that would have gone on.”<sup>1626</sup>

Mr. McLinko testified that the Community Bank was “developing the processes around automating the process of customer consent” and that with respect to the opening of a deposit product, the process of money movement, and the process of opening a credit card account all were in fact processes that could be audited.<sup>1627</sup> Similarly, Mr. McLinko confirmed that the slide regarding “Governance” reflected that ensuring sales goals are adjusted for fluctuations in staffing levels is a process that could be audited, and that the audit team “could audit the control processes” around implementing new incentive compensation processes.<sup>1628</sup>

Mr. McLinko identified a June 1-3, 2016 email chain between Mr. Julian and himself, along with OCC Examiners Linskens and Crosthwaite.<sup>1629</sup> In this exchange, at Mr. Julian’s suggestion, the addressees were invited to schedule time to discuss “Sales Practices as a topic”.<sup>1630</sup> Examiner Crosthwaite responded by accepting the suggestion, and in response Mr. Julian arranged for the meeting to take place on June 14, 2016.<sup>1631</sup>

Mr. Deese then provided the OCC Examiners and the other distributees with information from Ms. Russ Anderson’s reports, “Wendy Tazelaar[,] and team”:

Credit Card consent was implemented as of 5/21[/2016].

Consent for non credit card products will be implemented in Q4 2016.

Money Movement consent . . . the processes below were put into the system effective 5/21[/2016]:

1. New account open – Account transfer funding . . . the customer’s electronic signature will be required on the PIN pad prior to the transfer to fund an account. If the PIN pad is unavailable, the customer may complete the funding process at the teller line, through Online Banking, Wells Fargo ATM, Mobile or Phone Bank.
2. Future and/or reoccurring transfers . . . the customer’s signature will be required prior to establishing, maintaining or deleting a future or reoccurring

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<sup>1625</sup> Tr. (Julian) at 6982.

<sup>1626</sup> Tr. (Julian) at 6982-83.

<sup>1627</sup> Tr. (McLinko) at 8835-36; R. Ex. 12891 at 4.

<sup>1628</sup> Tr. (McLinko) at 8836-37R. Ex. 12891 at 3.

<sup>1629</sup> Tr. (McLinko) at 8837; OCC Ex. 1016.

<sup>1630</sup> OCC Ex. 1016 at 2.

<sup>1631</sup> *Id.* at 1.

transfer between two or more accounts for the same customer. Customer signatures may be captured electronically or manually.

3. Federal direct deposit . . . the customer’s signature will be required prior to establishing a direct deposit for Federal benefits such as Social Security. Customer signatures may be captured electronically or manually.<sup>1632</sup>

Through leading questioning by his Counsel during direct examination, Mr. Julian testified that the activities describing governance-related audit coverage was part of WFAS’s response to the June 2015 sales practices MRAs.<sup>1633</sup> The report identified three audit processes that were taking place both onsite and remotely – enhancement of the “onboarding and training of team members,” implementing “complaints process changes and enhanced reporting,” and ensuring “sales goals are adjusted for fluctuations in staffing levels”.<sup>1634</sup> A fourth process, implementing “new incentive compensation processes,” was performed remotely.<sup>1635</sup>

The report identified three audit processes relating to “authorization,” which Mr. Julian stated meant processes related to “obtaining consent for various products from customers.”<sup>1636</sup> Through leading questioning by his Counsel during direct examination, Mr. Julian testified that this audit coverage was part of WFAS’s response to the June 2015 sales practices MRAs.<sup>1637</sup>

The report identified seven audit processes relating to oversight, which according to Mr. Julian referred to “the oversight activities that were going on within the Regional Bank and . . . Community Bank’s governance activities where they – those groups were responsible for providing oversight. This is work that [WFAS] did to assess the appropriateness of that oversight and the effectiveness of it.”<sup>1638</sup> Mr. Julian testified that a governance group “would issue policies.”<sup>1639</sup>

Mr. Julian testified that WFAS would work with the “process owners to assure that those processes were implemented, that those processes and controls that were built out in the first line, that they were being adhered to.”<sup>1640</sup> He said the oversight group “would, again, be performing -- they themselves within the first line of business would be performing monitoring activities. They might be doing some testing activities. And it was a part of the risk management

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<sup>1632</sup> Tr. (McLinko) at 8838; OCC Ex. 1016 at 1. See Tr. (Russ Anderson) at 9820; OCC Ex. 934 for documentation regarding Wendy Tazelaar as a reporting member of Ms. Russ Anderson’s unit and its “Clarity Initiative”. *Id.* at 2.

<sup>1633</sup> Tr. (Julian) at 6983.

<sup>1634</sup> R. Ex. 12891 at 3.

<sup>1635</sup> *Id.*

<sup>1636</sup> Tr. (Julian) at 6984; R. Ex. 12891 at 4.

<sup>1637</sup> Tr. (Julian) at 6984.

<sup>1638</sup> Tr. (Julian) at 6984; R. Ex. 12891 at 5-6.

<sup>1639</sup> Tr. (Julian) at 6984.

<sup>1640</sup> Tr. (Julian) at 6984-85.

framework within the first line to manage the sales practices activities.”<sup>1641</sup> He said SOCR was an example of both a testing and an oversight function.<sup>1642</sup>

Mr. Julian testified that Mr. McLinko’s June 14, 2016 presentation to the OCC about WFAS’s activities around sales practices at the Regional Bank was “directly responsive and appropriate to respond to the MRA that Audit had received with respect to sales practices.”<sup>1643</sup> He said no one from the OCC raised any concerns about the presentation, nor did they raise any concerns about WFAS’s responses to the June 2015 MRAs.<sup>1644</sup>

### **Supervisory Letter WFC 2016-36: OCC Review of Enterprise Sales Practices**

On July 18, 2016, the OCC through Bradley Linskens as Examiner in Charge, Large Bank Supervision, issued Supervisory Letter WFC 2016-36, providing WF&C with the OCC’s review of enterprise sales practices.<sup>1645</sup> Through this Supervisory Letter, the OCC noted that in June 2015 the OCC identified “a number of deficiencies in internal controls and monitoring processes at the first, second, and third lines of defense that resulted in improper and imprudent sales practices.”<sup>1646</sup>

Following the issuance of the June 2015 Supervisory Letter, the OCC reported reviewing the Regulatory Compliance Risk Management’s (RCRM) analysis of sales practices complaints related to products sold in branches; a sample of sales integrity cases from Corporate Investigations that resulted in employee terminations; a sample of employee sales integrity allegations made to the Bank’s employee EthicsLine and investigated by the Community Bank’s Sales and Service Conduct Oversight Team (SSCOT); Accenture’s review of sales practices in Community Banking, among other lines; and PwC’s independent reviews of customer harm associated with inappropriate sales behavior.<sup>1647</sup>

Upon such review, the OCC concluded the Bank “engaged in unsafe or unsound banking practices based on findings in SL 2015 and further supported by our reviews” of the additional information noted above.<sup>1648</sup> It found “[a]ggressive sales pressure,” along with the “lack of adequate risk management oversight, fostered inappropriate and possibly fraudulent behavior by employees.”<sup>1649</sup> It found “evidence of sales pressure and inappropriate behavior resulting from

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<sup>1641</sup> Tr. (Julian) at 6985.

<sup>1642</sup> Tr. (Julian) at 6985-86.

<sup>1643</sup> Tr. (Julian) at 6986.

<sup>1644</sup> Tr. (Julian) at 6986.

<sup>1645</sup> Tr. (Julian) at 6987; OCC Ex. 805.

<sup>1646</sup> OCC Ex. 805 at 1, citing OCC Supervisory Letter 2015-36 (SL 2015).

<sup>1647</sup> OCC Ex. 805 at 1-2.

<sup>1648</sup> *Id.* at 2.

<sup>1649</sup> *Id.*

the Bank’s lack of sound risk management policies, procedures, and controls related to its sales practices.”<sup>1650</sup>

Enterprise culture was reported in these terms:

For decades, the Bank’s Vision and Values statement emphasized “cross-selling” – the process of offering customers the products and services they need to help them succeed financially. While cross-selling itself may not be a supervisory concern, the practice at the Bank was not properly governed, which led to excessive pressure on employees to sell more products to meet sales goals and achieve financial incentives.

In addition, the risks from these sales practices were not adequately managed. Evidence reveals that many times cross-selling was done without considering whether the products were appropriate for or even wanted by the customer. The Accenture assessment also confirmed aggressive sales goals and inappropriate supervisory practices in the CB. These concerns included sales goals that put undue pressure on front-line employees, as well as incentive compensation programs that often were misaligned with local branch traffic, staff turnover and customer demand.<sup>1651</sup>

The 2016 report found SL 2015 “highlighted a number of weaknesses in internal controls and management information systems including a lack of robust first, second and third lines of defense risk management programs.”<sup>1652</sup>

Notwithstanding these findings regarding the third line of defense, when asked through leading questioning by his Counsel during direct examination whether the OCC examiners stated to him or others that they believed he personally failed in any respect, or whether in connection with the 2016 Supervisory Letter that the OCC believed any actions by WFAS rose to the level of being unsafe, unsound, or reckless, Mr. Julian responded, “no, they did not.”<sup>1653</sup> He made no attempt to reconcile this answer with the finding in the Report that “the Bank’s risk management of its sales practices . . . are unsafe and unsound.”<sup>1654</sup>

The 2016 Letter reported, “[t]he practice of opening deposit accounts without authorization, the practice of moving funds without customer consent (simulated funding) and the failure to timely refund or remediate fees charged are considered unsafe or unsound banking practices.”<sup>1655</sup> It noted the issues presented in the 2015 Letter still had not been resolved:

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<sup>1650</sup> *Id.*

<sup>1651</sup> *Id.*

<sup>1652</sup> *Id.* at 3.

<sup>1653</sup> Tr. (Julian) at 6987.

<sup>1654</sup> OCC Ex. 805 at 2.

<sup>1655</sup> *Id.* at 3.



Our review of a sample of Ethics Line referrals reflects allegations of inappropriate and unethical behavior and suggests there still may be too much pressure on store employees to meet sales goals. Noted themes from the allegations we reviewed were sales pressure, taking advantage of protected classes (*e.g.*, age/elderly), and the selling of unwanted deposit or credit products, particularly credit cards. Our limited samples of customer complaints as well as the OCC’s Customer Assistance Group (CAG) and CFPB complaints, identified similar themes and further evidence that the Bank engaged in the unsafe and unsound practice of failing to adequately monitor and control sales practices to prevent such inappropriate employee behavior.<sup>1656</sup>

The OCC identified the root causes of the “widespread and unauthorized opening of credit card accounts without consent” included “excessive sales pressure and the absence of a control process that required documentation of explicit customer consent.”<sup>1657</sup>

Mr. Julian identified the response by Mr. Loughlin, presented in a letter dated July 29, 2016.<sup>1658</sup> Through this letter, Mr. Loughlin asserted Wells Fargo Bank, N.A., “risk management of sales practices and the specifically identified issues in the Supervisory Letter were not, and are not, unsafe or unsound.”<sup>1659</sup> Mr. Loughlin used the definition of “unsafe or unsound practice” as “any action or omission, which is contrary to generally accepted standards of prudent operation, the possible consequences of which, if continued, would be abnormal risk or loss or damage to an institution, its shareholders, or the agencies administering the insurance funds.”<sup>1660</sup>

Mr. Loughlin did not dispute that sales practices misconduct occurred: “We are deeply committed to our customers, and we acknowledge and regret that some customers were negatively impacted by the sales practices identified in the Supervisory Letters.”<sup>1661</sup> According to Mr. Loughlin, however, “the identified sales practice issues do not present an abnormal risk of loss to the Bank or its shareholders, were self-identified, and the Bank has taken significant corrective action both independently and in response to the 2015 Supervisory Letter.”<sup>1662</sup>

Through leading questioning by his Counsel during direct examination, Mr. Julian testified that at the time Mr. Loughlin sent the July 29, 2016 letter, he opined that based on the information available to him at the time, that Wells Fargo Bank, N.A., had made significant

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<sup>1656</sup> OCC Ex. 805 at 4.

<sup>1657</sup> *Id.*

<sup>1658</sup> Tr. (Julian) at 7003; R. Ex. 1192.

<sup>1659</sup> R. Ex. 1192 at 1.

<sup>1660</sup> *Id.*, quoting *In the Matter of Patrick Adams*, OCC AA-EC-11-50 and OCC Policies and Procedures Manual (“PPM”) 5000-7 (February 26, 2016). This is the standard being applied in this enforcement action.

<sup>1661</sup> R. Ex. 1192 at 1.

<sup>1662</sup> *Id.* at 1-2.

progress on MRA action items and fundamentally improved the Bank's sales practices risk oversight.<sup>1663</sup>

The letter reports, "a key principle of the Incentive Compensation Risk Management (ICRM) Program is that incentive compensation should balance risk and financial reward in a manner that does not provide team members with an incentive to exhibit inappropriate sales conduct."<sup>1664</sup>

The letter continues:

Corporate HR, through the ICRM Program and in partnership with the appropriate Enterprise Risk and Compliance functions including Sales Practices Oversight ('SPO'), the Law Department, and others, continues to evaluate sales practice risk in connection with the design and administration of incentive compensation as well as related performance management practices within the LOBs, including team member sales goals.<sup>1665</sup>

Mr. Julian did not dispute Mr. Loughlin's representation that as of the issuance of this letter, neither WFAS nor any other entity at Wells Fargo Bank, N.A. had determined the root cause of the issues presented by the 2013 L.A. Times articles or the 2014 City of Los Angeles lawsuit. Mr. Loughlin reported, "SPO is currently conducting the root cause [of sales integrity violations] analysis and will provide an update to executive management and the Risk Committee. This analysis is being developed by reviewing the results and recommendations of the independent reviews as well as through discussions with senior leaders in both the first and second lines of defense."<sup>1666</sup>

Mr. Julian did not dispute that through the OCC's 2015 Supervisory Letter, regulators had reported, "WFAS did not independently identify the sales practices issues noted in the 2015 Supervisory Letter, and that prior audit coverage did not provide an Enterprise view of sales practices."<sup>1667</sup> Instead, through leading questioning by his Counsel during direct examination, Mr. Julian asserted that WFAS had diligently worked to address the OCC's concerns and had made significant progress in its MRA remediation work.<sup>1668</sup> Nothing in this responsive testimony identified any documentary evidence to support this factual claim, and the record as a whole does not support the claim.

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<sup>1663</sup> Tr. (Julian) at 7003.

<sup>1664</sup> R. Ex. 1192 at 6.

<sup>1665</sup> *Id.*

<sup>1666</sup> *Id.* at 12.

<sup>1667</sup> *Id.* at 17.

<sup>1668</sup> Tr. (Julian) at 7003-04.

## **WFAS's Presentation to the A&E Committee: July 26, 2016**

Mr. Julian identified the WFAS Second Quarter 2016 Summary presented to the A&E Committee on July 26, 2016.<sup>1669</sup> The 2Q16 Summary reported, "Risk in Community Banking remains heightened and increasing related to reputation and the regulatory environment. While management continues to hire risk management talent, including the Group Chief Compliance Officer, the large number of initiatives impacting the business continues to be a challenge and strain existing resources."<sup>1670</sup>

This language closely tracks what was reported in WFAS's July 28, 2015 Summary. ("The efforts of Community Banking, along with the large number of corporate initiatives impacting the business, continue to be a challenge and strain existing resources."<sup>1671</sup>) It also closely tracks the Third Quarter 2015 Summary, which reported that the "efforts of Community Banking with sales practices, along with the large number of corporate initiatives impacting the business, continue to be a challenge and strain existing resources."<sup>1672</sup> There is, however, nothing Mr. Julian's responsive testimony indicating that the Summary from the Second Quarter 2016, or any Summary posted in 2015, included a request for additional WFAS resources to meet such strain.<sup>1673</sup>

Mr. Julian also identified the minutes from the July 26, 2016 A&E Committee meeting.<sup>1674</sup> The minutes reflect that during the Second Quarter Chief Auditor Report Mr. Julian "commented on the tension caused by the regulators' inference that a higher number of unsatisfactory audits indicate a stronger internal audit department."<sup>1675</sup> Mr. Julian testified that in a prior meeting, where he believes the full Board and the OCC participated, the OCC – probably Brad Linskens – told the Board and the Audit Committee that the OCC "felt that it was a positive, if you will, that [WFAS] was issuing a higher number of unsatisfactory-rated audits. And I didn't agree with that in totality, and I wanted to make sure that the A&E Committee understood my perspective on that."<sup>1676</sup>

Mr. Julian rationalized that "any audit function could perform their work effectively and not have any unsatisfactory audits, meaning the controls they were testing were effective."<sup>1677</sup>

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<sup>1669</sup> Tr. (Julian) at 6991; R. 408.

<sup>1670</sup> R. Ex. 408 at 25.

<sup>1671</sup> OCC Ex. 2157 at 25.

<sup>1672</sup> OCC Ex. 2228 at 24-25. See OCC Ex. 2157 at 25: "The efforts of Community Banking, along with the large number of corporate initiatives impacting the business, continue to be a challenge and strain existing resources."

<sup>1673</sup> Tr. (Julian) at 6991-92.

<sup>1674</sup> Tr. (Julian) at 6994; R. Ex. 13540.

<sup>1675</sup> R. Ex. 13540 at 3.

<sup>1676</sup> Tr. (Julian) at 6995; R. Ex. 13540 at 3.

<sup>1677</sup> Tr. (Julian) at 6995.

He added that he wanted to make sure WFAS team members “didn’t think that they were going to be measured by issuing unsatisfactory or more negative-rated audit reports,” and didn’t want them “thinking the harder graders they were, the better they looked.”<sup>1678</sup> He said it would “have been easy to just issue negative audit rated reports even if they weren’t deserved or appropriate” just to “have the regulators think better of them.”<sup>1679</sup>

The minutes reflect, “WFAS is coordinating on” a project formalizing the process for approving and closing audit issues, with Corporate Risk, “which is working on similar policies for the second line of defense.”<sup>1680</sup> Apart from Mr. Julian’s Chief Auditor report, the Global Ethics and Integrity Report reflected that Ms. Meuers “responded to Committee members’ questions regarding the percentage of sales practices allegations related to account opening and consent and the concentration of sales practices allegations in certain states.”<sup>1681</sup> The minutes are silent, however, regarding WFAS’s response to Supervisory Letter WFC 2016-36, which had provided WF&C with the OCC’s review of enterprise sales practices.<sup>1682</sup>

Mr. Julian identified the July 26, 2016 Head of Global Ethics & Integrity Report by Christine Meuers<sup>1683</sup> Through her report, Ms. Meuers cautioned that while sales incentive allegations reported through the Ethics Line had decreased, “Internal Investigations’ (II) sales practices misconduct case load is up (39%) with increases coming from the use of proactive monitoring tools.”<sup>1684</sup> For the period January 1 – May 31, there were 19,544 total reported Ethics Line allegations in 2015, and 19,223 allegations in 2016.<sup>1685</sup>

Over the prior year from January 1 to May 31, there was a 9% increase in EthicsLine Reports received during the same period.<sup>1686</sup> The report reflected of the top five EthicsLine Reports received, 46% (1,839) were for Sales Practices.<sup>1687</sup> *44% of the internal investigations of EthicsLine Reports led to “Confirmed Fraud/Policy Violations,” and 82% of EthicsLine allegations related to Community Banking.*<sup>1688</sup> The report reflects that “Texas and California have the highest raw numbers of allegations, but Idaho and Nevada have the highest allegations

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<sup>1678</sup> Tr. (Julian) at 6995-96; see also “22-03-07 Respondents’ Amended Revised Errata Days 9 -38” at page 56. Ordered through Second Supplemental Order Regarding Hearing Transcript Errata.

<sup>1679</sup> Tr. (Julian) at 6996.

<sup>1680</sup> R. Ex. 13540 at 3.

<sup>1681</sup> *Id.* at 4.

<sup>1682</sup> Tr. (Julian) at 6987, 6997; R. Ex. 13540 at 4; OCC Ex. 805.

<sup>1683</sup> Tr. (Julian) at 7000-01.

<sup>1684</sup> R. Ex. 14173 at 2.

<sup>1685</sup> *Id.* at 5.

<sup>1686</sup> *Id.* at 7.

<sup>1687</sup> *Id.*

<sup>1688</sup> *Id.*

per 100 team members,” and the “majority of all team member allegations were in California, Texas, Arizona and Virginia for the period January 1 – May 31, 2016.”<sup>1689</sup>

Despite the breadth and reach of these allegations across the country, Mr. Julian opined without support from the record that the distribution was “disproportionate” and could not be “systemic” because “for it to be systemic, it would need to be widespread, meaning, in my words, proportionally distributed across the area of review, in this case, across the footprint.”<sup>1690</sup>

Contrary to this opinion, the Global Ethics & Integrity Report provides substantial, reliable, and preponderant evidence that sales practices misconduct by Community Bank’s team members was widespread and systemic.

### **Sales Practices MRA Status Update – July 29, 2016**

Mr. Julian identified a Sales Practices MRA Status Update dated July 29, 2016 from Mr. McLinko and others to Claudia Russ Anderson and others, which provided a summary of corrective actions relating to the five MRAs issued in 2015.<sup>1691</sup> He testified that WFAS team members provided updates as the report was being prepared, and he “had communications with them as to the conclusions drawn here.”<sup>1692</sup> He added, however, that the update “was specifically with respect to the work that the first and second line were responsible for doing with respect to MRA No. 1 through 4,” and that he did none of the work that led to the generation of this Status Update.<sup>1693</sup>

The Status Update reflected, “key corrective actions are not scheduled to be completed until the fourth quarter 2016”, resulting in an Overall Rating of “Yellow”.<sup>1694</sup> In this context, Yellow indicated “potential risk of schedule delay or missed milestones”, “incomplete action plans to address issues”, “implementation plan requires improvement to fully mitigate risks”, “identified environmental factors (internal or external) have the potential to impact the timely implementation of this effort.”<sup>1695</sup>

One of the “key milestones,” relating to the sales practice oversight by the second line of defense, was to “[e]stablish initial risk appetite metrics for Community Banking”.<sup>1696</sup> Through the Status Update, WFAS reported that it now “believes that a complaint metric should be

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<sup>1689</sup> R. Ex. 14173 at 6.

<sup>1690</sup> Tr. (Julian) at 7001-02.

<sup>1691</sup> Tr. (Julian) at 7004; R. Ex. 13164 (Memo).

<sup>1692</sup> Tr. (Julian) at 7005.

<sup>1693</sup> Tr. (Julian) at 7005-06.

<sup>1694</sup> R. Ex. 13164 at 1.

<sup>1695</sup> *Id.* at 5.

<sup>1696</sup> *Id.* at 3.

included in order to effectively assess Sales Practices risk within Community Banking” but described other initial metrics presented through the Update “are a good starting point.”<sup>1697</sup>

Another bulleted point relating to MRA #2 and the second line of defense was to “[r]eassess EthicsLine and customer complaints investigative processes.”<sup>1698</sup> The Update reported, “[p]lanning for the Ethics Line audit is scheduled to start in July 206 [sic].”<sup>1699</sup> The Update reported that as “part of the overall planning for this audit, we will determine our testing approach as specifically related to the validation of EthicsLine portion of this corrective action. WFAS is also developing our validation testing approach for the customer complaints investigative process.”<sup>1700</sup>

With respect to MRA #5 directed at WFAS, the Status Update identified only two corrective actions: that Management “must reassess their coverage of sales practices and provide an enterprise view” and must “include Internal Investigations (formerly Corporate Investigations) and Corporate Customer complaints and EthicsLine processes in the audit universe and provide an audit opinion on each.”<sup>1701</sup>

While WFAS reported that as of June 30, 2016, 22 audits covering aspects of Sales Practices “are in progress,” only three audit reports had been published, none of which directly pertain to Community Banking.<sup>1702</sup> The Update also reported that WFAS was “progressing towards a consistent process for analysis of Complaint and Internal Investigations (including EthicsLine) data during audit planning.”<sup>1703</sup> The Update was silent, however, with respect to when WFAS expected to meet the stated goals.<sup>1704</sup>

### **Risk Committee, Noteworthy Risk Issues – August 15, 2016**

Mr. Julian identified the report from CRO Mike Loughlin reflecting Noteworthy Risk Issues as of August 15, 2016.<sup>1705</sup> Regarding the Risk Issue of “Sales Conduct, Practices and Business Model,” the report stated as follows:

Management continues to strengthen oversight of Sales Practices in all three lines of defense, including continuing to build teams in the first and second

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<sup>1697</sup> R. Ex. 13164 at 3.

<sup>1698</sup> *Id.*

<sup>1699</sup> *Id.*

<sup>1700</sup> *Id.*

<sup>1701</sup> *Id.* at 6.

<sup>1702</sup> *Id.*; “The audit reports were CLG’s HL Production Sales, CLG’s Credit Card Sales, Originations and Underwriting, and Wholesale’s CTS-New Business.” CLG presumably refers to Consumer Lending Group. See OCC Ex. 2107 at 22 (WFAS 2014 Audit Plan; Coverage by audit team).

<sup>1703</sup> R. Ex. 13164 at 6.

<sup>1704</sup> *Id.*

<sup>1705</sup> Tr. (Julian) at 7007; OCC Ex. 2180.

lines of defense focused on sales practices. The Head of Sales Practices Oversight within Corporate Enterprise Risk completed hiring of three managers devoted to oversight of sales practices risk across the enterprise. The Sales Practices Oversight unit risk managers are coordinating with other second-line of defense partners to complete a schedule of oversight activities. An initial Key Risk indicator report will be available in 3Q-2016 to provide insight into risk profile measures for Community Bank and the Enterprise. The Head of Community Banking Sales and Service Conduct Risk continues building a governance structure and processes to ensure a holistic view of sales practices risk. Accomplishments such as the recent hire of several key leadership positions and finalization of enhancements to reporting frameworks are important steps towards strengthening the program. Regulatory scrutiny remains high.<sup>1706</sup>

Mr. Julian did not dispute any of the report's contents, and testified through leading questioning by his Counsel during direct examination that as of August 2016 he was not aware of any other information regarding sales practices risk that needed to be but had not been escalated to the Wells Fargo Board of Directors.<sup>1707</sup> This answer does not suggest that he escalated any issue to the Wells Fargo Board of Directors, notwithstanding his understanding of the issues presented to him and Mr. McLinko through Mr. Bacon, through the L.A. Times articles, or through the claims presented in the City of Los Angeles lawsuit. As of August 2016, neither Mr. Julian nor Mr. McLinko had identified and escalated to the A&E Committee the root cause of team member sales practices misconduct.

### **Podium Day – September 8, 2016**

Through leading questioning by his Counsel during direct examination, Mr. Julian identified September 8, 2016, as the day the OCC Consent Order and L.A. City Attorney lawsuit settlement regarding sales practices were announced, with significant media reaction.<sup>1708</sup> He recalled, “[t]here was a significant amount of activity, discussions, dialogues going on around that day.”<sup>1709</sup>

In the wake of the activity and media attention relating to the Podium Day settlement announcements, Mr. Julian engaged in a series of email messages to Paul McLinko and others.<sup>1710</sup> Starting the chain, Mr. Julian wrote to Mr. McLinko (as EAD of Community Banking's audit group within WFAS), Joel Schipper (as EAD “with Audit oversight for the Wholesale Bank), Mark Weintraub (as EAD with Audit oversight for Consumer Lending

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<sup>1706</sup> OCC Ex. 2180 at 3.

<sup>1707</sup> Tr. (Julian) at 7007-08.

<sup>1708</sup> Tr. (Julian) at 7008-09.

<sup>1709</sup> Tr. (Julian) at 7008.

<sup>1710</sup> Tr. (Julian) at 7009-13; R. Ex. 875, R. Ex. 876.

activities), and Howard Anderman (as EAD with Audit oversight for Wealth, Brokerage and Retirement).<sup>1711</sup>

In his first September 11, 2016 email (at 3 p.m. CST) to these four WFAS Executive Audit Directors, Mr. Julian asked “How would we answer the question[: ‘]What has WFAS done to determine if we have sales practices issue in the other businesses?[']”

At 4:49 p.m. EST Mr. Weintraub responded, providing a summary of audit functions relating to “the sales for the mortgage business this year using (actually piloting) the sales practices audit program that was developed in response to the [C]ommunity [B]ank issues.”<sup>1712</sup> He wrote, “Most of the CCS products are sold or referred through the [C]ommunity [B]ank, though there are central call centers as well.”<sup>1713</sup> He reported on “Dealer business sales,” “sales, marketing and customer rewards coverage across CLG,” the “direct auto business,” and a “team that has begun data analysis of the CFPB complaints data”.<sup>1714</sup>

Mr. McLinko wrote at 4:13 a.m. on September 12, 2016 that Mr. Weintraub “provided a well-rounded response to your questions.”<sup>1715</sup> He noted “[w]e have a centralized working group that is coordinating our coverage of Sales Practices” and “developed a sales practices coverage strategy for 2016” as well as a “Sales Practices Standard Audit Program which all teams all [*sic*] using to test sales practices.”<sup>1716</sup>

Mr. Anderman wrote at 7:40 a.m. on September 12, 2016, “Sales Practices risks have traditionally been incorporated into WIM [Wealth and Investment Management] audit coverage, being a long-standing retail securities industry and regulatory focus”.<sup>1717</sup> He added, “[c]overage has included testing controls over cross selling, account opening, and incentive compensation across a variety of lines of business audits based on risk and corresponding horizon.”<sup>1718</sup> He reported that WIM audit coverage for 2016 “will be executed within each RABU and will include a combination of control testing, business monitoring, and validation activities. WIM Audit, together with WFAS Audit Teams, will monitor progress on enterprise-wide corrective actions for the Sales Practices OCC MRAs and will establish enhanced monitoring of sales related complaints, EthicsLine and Internal Investigations.”<sup>1719</sup>

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<sup>1711</sup> Tr. (Julian) at 7010-11; R. Ex. 875 at 5.

<sup>1712</sup> Tr. (Julian) at 7012; R. Ex. 875 at 5.

<sup>1713</sup> R. Ex. 875 at 5.

<sup>1714</sup> *Id.*

<sup>1715</sup> Tr. (Julian) at 7012; R. Ex. 875 at 4.

<sup>1716</sup> R. Ex. 875 at 4.

<sup>1717</sup> Tr. (Julian) at 7012; R. Ex. 875 at 3.

<sup>1718</sup> R. Ex. 875 at 3.

<sup>1719</sup> *Id.*



Upon his receipt of these responses, in a September 12, 2016 email sent at 8:54 CST, Mr. Julian wrote, “I could use some help with this question: Where was audit while this activity was taking place. To be honest, I’m not sure how to answer this but am sure the AE Committee will and should be asking. Any thoughts would be welcomed.”<sup>1720</sup>

To this, Kimberly Bordner (whom Mr. Julian described as “a direct report of mine . . . sort of a chief operating officer for Audit”<sup>1721</sup>) responded within the hour, “Let me check to see if we have done any retrospective review work in addition to the go forward enhancements made to our coverage. If we haven’t performed a formal retrospective review, I think we should.”<sup>1722</sup>

To this, Howard Anderman responded, “in October of 2015 Accenture produced reports on Sales Practices for Community Bank, WIM, CLG, and for the Enterprise.”<sup>1723</sup> He wrote that on October 27 [presumably 2015] the Board of Directors received these reports and “[t]he work Paul, Kathy and others have been engaged in (developing the Sales Practices Standard Audit Program, etc.) took into consideration these reviews.”<sup>1724</sup>

Later that morning Mark Links responded by writing, “[t]he LA lawsuit was considered alternative practice under the Retrospective Review process. WFAS does its own retrospective review on MRAs when received. The OCC Sales Practice MRAs may have been assessed through that process.”<sup>1725</sup>

Four minutes after Mr. Links sent his email to Mr. Anderman, Ms. Bordner, Mr. Julian, Mr. McLinko, Mr. Weintraub, and Mr. Schipper, Mr. Julian wrote (at 10:53 on September 12, 2016): “Agree with everyone’s comments but, it still doesn’t answer the question – Where was Audit?”<sup>1726</sup>

Mr. McLinko responded to Mr. Julian with, “David, I’m putting together an answer for you now.”<sup>1727</sup>

Mr. Julian was asked by his Counsel, “What time period were you referring to when you asked your Executive Audit Directors and Ms. Bordner the question, “Where was Audit while this activity was taking place?” Although his response is not consistent with the context set forth above, Mr. Julian responded, “Really pre-2013. I had a fair understanding and good understanding of all of the work that had been going on since the L.A. Times article, and the

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<sup>1720</sup> R. Ex. 875 at 3.

<sup>1721</sup> Tr. (Julian) at 7013.

<sup>1722</sup> R. Ex. 875 at 3.

<sup>1723</sup> *Id.* at 2.

<sup>1724</sup> *Id.*

<sup>1725</sup> *Id.* at 1.

<sup>1726</sup> *Id.*

<sup>1727</sup> *Id.*

audit leaders had provided me some further update, but I also wanted to just understand where Au[dit] was prior to that.”<sup>1728</sup>

Nothing in the email chain spanning September 11 and 12, 2016 either suggested or expressly stated that Mr. Julian’s question concerned a specific period, nor that he was seeking information regarding Audit’s work *prior* to 2013. Certainly none of the responses presented through this email chain indicated the respondents believed the question concerned pre-2013 Audit activity. The record thus supports a finding that Mr. Julian was being deceptive in his sworn testimony about the meaning of this quote, and that the purpose of this deception was to deflect blame and minimize the significance of his email message.

Similarly, Mr. Julian explained why he wrote that he agreed with “everyone’s comments, but still doesn’t answer the question – where was audit?” When asked why he thought the responses thus far did not answer his question, Mr. Julian testified:

Well, again, I was -- most of the responses I received was covering [*sic*] work that audit had done in part in 2013 that Community Bank had done that I was familiar with, but also work across Wells Fargo Audit Services that had been performed sort of post L.A. Times article. And, again, I wanted to have an understanding, a historical understanding of prior to those periods as well.<sup>1729</sup>

Nothing in the email exchange, however, suggests the question presented through his email to these EADs sought information about WFAS’s actions preceding 2013. There is no credible evidence supporting Mr. Julian’s response to the question put to him by his attorney. To the contrary, preponderant evidence establishes that this testimony was misleading, and that Mr. Julian understood the true nature of the question he presented in the email exchange was his request to be told about WFAS’s audit efforts directed at sales practices misconduct by Community Bank team members between 2013 and the present.

Along the same lines, Mr. Julian identified a compilation of email messages that begins with the same three messages already discussed – from Mr. Julian at 3 p.m. on September 11, 2016, then Mr. Weintraub’s response at 4:49 p.m., followed by Mr. McLinko’s response from 4:13 a.m. on September 12, 2016, followed by Mr. Anderman’s 7:40 a.m. response, then Mr. Julian’s September 12, 2016, 9:54 a.m. request for help with the questions stated above, followed by a response from Mr. McLinko at 11:12 a.m. CST and a separate response from Mr. Links dated September 13, 2016.<sup>1730</sup>

Mr. McLinko’s response “is related to the Stores as in the Call Centers, all Sales are recorded, which gives us the ability to select samples from the recordings and test for consent, etc.”<sup>1731</sup> Specifically with respect to the Stores (*i.e.*, Bank branch offices), Mr. McLinko

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<sup>1728</sup> Tr. (Julian) at 7013.

<sup>1729</sup> Tr. (Julian) at 7015.

<sup>1730</sup> R. Ex. 876.

<sup>1731</sup> *Id.* at 1.

identified a set of audit activities, *all of which depended on data gathered not by WFAS but instead by the first line of defense:*

- In many ways, we have leveraged the Store Operations Control Review (SOCR), which is part of the ILOD. SOCR goes into every store every year and performs a variety of functions, one being a review of account opening documentation and signatures. Every two years we test the program by going into a sample of stores and re-performing the work the SOCR team does. Several years back we raised a moderate rated issue as it relates to the documentation supporting the process (not that they weren't performing the work). Audit validation of the corrective actions failed the issue and at that time we raised it to a high rated issue.
- Because of that fail, we added an account opening to our plan in 2015. We announced the audit and then the LA lawsuit happened. As a result, the scope of the audit was changed and put under ACP.
- We have also tested for new account documentation in an audit called Deposit Products Support Services. This audit would review for account documentation and customer signature.
- We have also tested the Sales and Services Conduct Oversight Team, which is the group that was part of researching the sales practices issues back in 2013. That led to the investigation and subsequent TM firings; that led to the LA lawsuit.
- In 2014, we tested incentive plans in coordination with Andrew's team. During that audit we tested: Consumer Connection (WFCC), Personal Banker 1/Assistant Store Mgr. (Regional Banking), and RBPB/Private Banker (Regional Banking) incentive plans.

In short, over the years, we have relied on the SOCR program. Once we failed SOCR issue validation, during annual audit planning in 2014, we added a Regional Banking account-opening audit to the 2015 audit plan which is mentioned above.

In addition:

- As you're aware, [C]omplaints has been an issue at the top of the house with continued rollout of the program, thus we're beginning to be able to utilize that information (which was also part of our response to the MRA).
- The new technology that captures customer consent for deposits, credit cards and unsecured lines of credit just went live recently which we are testing as part of the MRA validation.
- A retrospective review for this topic was performed in response to the OCC's MRA's [*sic*].

In a nutshell this covers what we've done.<sup>1732</sup>

Although this response did not provide a “historical understanding of prior to” 2013 (which is what Mr. Julian swore was the reason for his question, “Where was Audit?”), Mr. Julian testified that he found Mr. McLinko’s response “helpful.”<sup>1733</sup> He then testified that he was looking for a “refresher with respect to all of the work across [WFAS] that had been being performed, and this was in addition to all the other responses, just additional information.”<sup>1734</sup>

Through leading questioning by his Counsel during direct examination, Mr. Julian testified that Mr. McLinko’s explanation of the Community Bank’s sales practices coverage was consistent with what Mr. McLinko had told him back in March of 2013 when he presented Mr. Julian with the so-called one-pager.<sup>1735</sup>

### **September 13, 2016: WF&C Eliminated All Sales Goals and Sales Incentives for Retail Banking Team Members**

Through leading questioning by his Counsel during direct examination, Mr. Julian recalled that on September 13, 2016, Wells Fargo & Company announced that it would eliminate all sales goals and sales incentives for retail banking team members.<sup>1736</sup> He testified further that throughout the relevant period he lacked the authority to eliminate those goals and incentives.<sup>1737</sup>

### **September 13, 2016: Mr. Julian Removes Paul McLinko as EAD for the WFAS Community Bank Audit Group**

In an email sent to Mr. McLinko, who at the time was vacationing in France, Mr. Julian wrote that the OCC was “pushing hard” to “ensure that the leaders of the work in every business group engaged is ‘independent’ of the past work.”<sup>1738</sup> Mr. Julian wrote, “As a result of the Senate hearings there is renewed energy by the OCC and they are coming out strong.”<sup>1739</sup> He said he had “several conversations related to our work on the Sales Practices CO’s [*sic*]” and was “thinking about how we (WFAS) should make this worker [*sic*] broader to ensure all the work being done across WFAS is coordinated and challenged.”<sup>1740</sup>

Mr. Julian said the OCC “acknowledged that the work you and Kathy have done to date is very good. However, they do not feel it should sit in the Community Banking Audit Group. At

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<sup>1732</sup> R. Ex. 876 at 1-2.

<sup>1733</sup> Tr. (Julian) at 7016.

<sup>1734</sup> Tr. (Julian) at 7016.

<sup>1735</sup> Tr. (Julian) at 7016.

<sup>1736</sup> Tr. (Julian) at 7020.

<sup>1737</sup> Tr. (Julian) at 7020-21.

<sup>1738</sup> R. Ex. 1481 at 1.

<sup>1739</sup> *Id.*

<sup>1740</sup> *Id.*

the same time, I feel that we need a full-time focus on this at the Director level reporting directly to me.”<sup>1741</sup>

As a result, Mr. Julian told Mr. McLinko, “I am going to ask Deb Anderson to take the lead on all things Sales Practices (coordination, not execution) for the next 3-5 months. I am going to ask Kathy to stay in the role she is playing – ‘reporting’ up to Deb. Again, sorry for dropping this in email but the regulators want to see demonstrable change immediately by all groups – others like Loughlin are being told to reconsider some of their lead folks as well.”<sup>1742</sup>

Mr. Julian denied reassigning Sales Practices-related audit work because he lost confidence in Mr. McLinko and denied he had any reason at that time to question Mr. McLinko’s independence.<sup>1743</sup>

### **Supervisory Letter WFC 2016-40: Annual Audit Rating Examination of WFAS**

Mr. Julian identified the November 9, 2016 Supervisory Letter WFC 2016-40 as the OCC’s letter to Jim Quigley related to the OCC’s annual audit rating of WFAS.<sup>1744</sup> After noting the OCC rated WFAS “Satisfactory” Mr. Julian acknowledged that the OCC stated, “they were concerned that Internal Audit did not identify any of the sales practices issues.”<sup>1745</sup>

The Supervisory Letter reported, “Management needs to take an enterprise view of audit in this area and redesign a more comprehensive and effective program that addresses incentive compensation, complaints, terminations, and branch testing.”<sup>1746</sup> It noted that in September 2016, a Consent Order was issued as a result of unsafe and unsound banking practices related to Wells Fargo’s Enterprise Sales Practices, and that WFAS “conducted a number of audits in the Community Bank but did not identify nor escalate any of the systemic issues regarding sales pressures, complaints, terminations, or fraudulent activity.”<sup>1747</sup>

The Supervisory Letter found that WFAS’s approach for incentive compensation “needs improvement.”<sup>1748</sup> “The Finance & Corporate Activities (FCA) audit team has provided enterprise-wide coverage of incentive compensation, but the scope of transaction testing was primarily limited to covered employees.”<sup>1749</sup> The Supervisory Letter directed that “FCA coverage of incentive compensation should be expanded to ensure appropriate testing at both the

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<sup>1741</sup> R. Ex. 1481 at 1.

<sup>1742</sup> *Id.* at 2.

<sup>1743</sup> Tr. (Julian) at 7023.

<sup>1744</sup> Tr. (Julian) at 7031; OCC Ex. 2142,

<sup>1745</sup> Tr. (Julian) at 7031.

<sup>1746</sup> OCC Ex. 2142 at 1.

<sup>1747</sup> *Id.* at 2.

<sup>1748</sup> *Id.*

<sup>1749</sup> *Id.*

enterprise and LOB levels, including both covered and non-covered employees.”<sup>1750</sup> The OCC also directed WFAS to “[i]ncorporate all pertinent incentive compensation related audit findings in the HR Enterprise Risk Management Assessment (ERMA).”<sup>1751</sup>

The Supervisory Letter noted that while the A&E Committee “is guided by a sound committee charter and is comprised of independent directors who possess the financial acumen and professional stature to provide effective oversight and challenge of internal and external audit activities,” the overall rating was downgraded from Strong to Satisfactory because “Internal Audit did not identify key issues related to sales practices and the A&E Committee did not provide effective challenge over related ethics, fraud, termination, and complaint reporting.”<sup>1752</sup>

### **November 28, 2016 Noteworthy Risk Issues presented to the Risk Committee**

Mr. Julian identified the Noteworthy Risk Issues report presented to the Risk Committee at its November 28, 2016 meeting.<sup>1753</sup> Through leading questioning by his Counsel during direct examination Mr. Julian testified that as of the date of the report he was not aware of any other information regarding sales practices risk that needed to be but had not been escalated to the Board of Directors.<sup>1754</sup> Among the information Mr. Julian and Mr. McLinko both were aware of but did not disclose in this report was the ineffectiveness of risk management controls by the Community Bank’s first line of defense and their respective and collective failure to identify the root cause of sales practices misconduct issues identified by Mr. Bacon, the L.A. Times articles, and the City of Los Angeles lawsuit.

Included in the report is a reference to Management strengthening its oversight over all three lines of defense, and that “[v]olumes and dispositions of allegations and customer complaints are being closely monitored since announcing the settlement [on] September 8th. Additionally, conduct risk was elevated to a key risk type in the annual review of the Risk Coverage Statement, approved in September.”<sup>1755</sup>

### **WFAS’s Presentation to the A&E Committee: November 29, 2016**

Mr. Julian identified the minutes of the November 29, 2016 meeting of the A&E Committee and the WFAS Third Quarter 2016 Summary, and testified that he made the presentation reflected under the headings Third Quarter Chief Auditor Report and Significant

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<sup>1750</sup> OCC Ex. 2142 at 2.

<sup>1751</sup> *Id.* at 3.

<sup>1752</sup> *Id.*

<sup>1753</sup> Tr. (Julian) at 7034; R. Ex. 15407.

<sup>1754</sup> Tr. (Julian) at 7035.

<sup>1755</sup> R. Ex. 15407 at 2.

MRIAs/MRAs.<sup>1756</sup> Other than identifying the two documents, however, Mr. Julian offered no testimony regarding the minutes or the Summary.<sup>1757</sup>

Through the meeting minutes, Mr. Julian is reported to have “commented on the projects and initiatives being tracked by WFAS and said he remains concerned about the ability to meet due dates given the volume of projects.”<sup>1758</sup> Mr. Julian is reported to have said the OCC “continued to rate WFAS Satisfactory but had downgraded three of the components, including the Committee’s rating, from Strong to Satisfactory.”<sup>1759</sup>

The minutes reflect that in response to a Committee member’s “question about the factors contributing to the Committee’s lower rating” Mr. Julian “[redacted] and commented on the findings of the Consumer Financial Protection Bureau (CFPB), which do not include an overall rating.”<sup>1760</sup> The minutes do not indicate that Mr. Julian actually answered the question presented by the Committee member regarding the factors that contributed to the A&E Committee’s lower rating.<sup>1761</sup>

The Third Quarter 2016 Summary reported that “[a]s a result of the recent Sales Practices consent orders, WFAS will be accountable for assessing, monitoring, testing, and reporting on the company’s progress towards fulfilling the requirements under the consent orders, as well as addressing findings directed to us.”<sup>1762</sup> For the third quarter, “WFAS maintained a Yellow status<sup>1763</sup> for the overall Sales Practices effort. Key drivers for the rating include concerns around sustainability of the actions, two failed corrective action validations, and the overall impact of the consent orders to the in process action plans.”<sup>1764</sup>

Regarding Community Banking, the Summary reported that risk in Community Banking “remains heightened and significantly increasing related to reputation and the regulatory environment.”<sup>1765</sup>

The Summary included a report following the events that became public on Podium Day:

In early September 2016, Wells Fargo reached settlements with the OCC, CFPB, and Office of the Los Angeles City Attorney over allegations of

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<sup>1756</sup> Tr. (Julian) at 7036; R. Ex. 15940 at 12-13 (minutes); R. Ex. 1137 (WFAS Third Quarter 2016 Summary); R. ex. 15515 (transmittal email).

<sup>1757</sup> Tr. (Julian) at 7036-41.

<sup>1758</sup> R. Ex. 15940 at 12.

<sup>1759</sup> *Id.* at 13.

<sup>1760</sup> *Id.*

<sup>1761</sup> *Id.* at 12-13.

<sup>1762</sup> *Id.* at 5.

<sup>1763</sup> *I.e.*, the intermediate status between Green and Red.

<sup>1764</sup> R. Ex. 1137 at 6.

<sup>1765</sup> *Id.* at 23.

improper Sales Practices. The primary concerns noted a need to enhance risk governance and processes, including incentive compensation and customer complaints, and remediation of customer harm. In addition, WFAS has committed to revising our testing and monitoring program.

Within 60 days from the date of the OCC consent order, WFAS was required to submit a plan which includes the actions necessary and appropriate to address the consent order. The plan was submitted with the comprehensive Wells Fargo corrective action plan on November 4, 2016. Within 90 days, WFAS will review and revise existing testing and monitoring programs to include an enterprise view of Sales Practices including: Corporate Investigations, Corporate Customer Complaints, and EthicsLine processes. Also, within 120 days of completion of the Reimbursement Plan, WFAS will conduct a Reimbursement Review to assess compliance with the terms of the Reimbursement Plan.<sup>1766</sup>

Specific to Incentive Compensation, WFAS “is currently examining a sample of 2015 Incentive Compensation Plans” that were identified “to have Sales Practices Risk to evaluate compliance with the ICRM framework”, and has “expanded the scope of our testing procedures to further assess 2016 compensation outcomes in the Community Bank, including the incorporation of risk information.”<sup>1767</sup>

Specific to EthicsLine, “testing includes examining and assessing the design effectiveness of the reassessment of EthicsLine processes as noted as part of the Sales Practices MRAs.” WFAS has “expanded the scope of our process design work and testing procedures” to “incorporate end-to-end testing across the various research groups to assess investigations and dispositions.”<sup>1768</sup>

Specific to the Complaints Management Program, WFAS “downgraded the prior quarter’s rating [from Yellow to Red] based on the compressed timeline to complete remaining deliverables associated with Service Complaints and Third Party Service Provider Complaints by year-end, coupled with challenges related to oversight of workstreams, inconsistencies in evidencing completion of deliverables, due date extensions, and increased regulatory focus on this project.”<sup>1769</sup>

### **WFAS’s Enterprise Risk Management Assessment – April 27, 2017**

Through its Enterprise Risk Management Assessment covering 2016 Sales Practices Enterprise Risk Management, WFAS defined “sales practices risk” as “the risk of customer harm, reputational damage, financial loss, litigation, and regulatory non-compliance associated

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<sup>1766</sup> R. Ex. 1137 at 42.

<sup>1767</sup> *Id.* at 43.

<sup>1768</sup> *Id.*

<sup>1769</sup> *Id.* at 5, 43-44.



with sales practices.”<sup>1770</sup> “Sales practices” refers to “actions and/or activities related to promoting or selling a financial product or service, including all actions and activities intended to retain existing customers.”<sup>1771</sup>

Mr. Julian identified the Enterprise Risk Management Assessment, through which WFAS concluded, “as of December 31, 2016, Enterprise Risk Management (ERM) for Sales Practices Risk is **Weak**”, where such assessment ratings are Satisfactory, Needs Improvement, or Weak.<sup>1772</sup> He denied authoring the Assessment, testifying that it was “authored under the leadership of Deb Anderson.”<sup>1773</sup>

The Assessment defined a “Weak” rating thus:

The design is not adequate and lacks sufficient support[.] Enterprise risk management is not effective and does not balance risk with reward[.] Evidence does not exist and is not sufficient to be conclusive[.] Enterprise risk management is not communicated, understood, or adhered to[.]<sup>1774</sup>

Asked for his understanding of the Weak rating, Mr. Julian testified:

Predominantly driven by that there was inability still to capture an overall view of sales practices risk across the company, so the company had not yet developed that comprehensive capture -- ability to capture. The office of the -- sorry. The Office of Ethics still needed build out. While it was formed, it still needed a significant amount of built out and oversight, and also with respect to the enhancements that needed to be continued to be developed and executed on with respect to sales practices activities.<sup>1775</sup>

Through leading questioning by his Counsel during direct examination, Mr. Julian testified that this did not mean that progress had not been made in responding to the sales practices issues that had been raised through the June 2015 MRAs – “it just recognized that there was still . . . a significant amount of additional work to be done.”<sup>1776</sup>

While the record includes Mr. Julian’s understanding of the Weak rating – that the rating was based on the “inability still to capture an overall view of sales practices risk across the company,” the Assessment itself reflects additional material concerns led to the rating.

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<sup>1770</sup> R. Ex. 16103 at 1, n. 2.

<sup>1771</sup> *Id.*.

<sup>1772</sup> Tr. (Julian) at 7048; R. Ex. 16103 at 1.

<sup>1773</sup> Tr. (Julian) at 7049.

<sup>1774</sup> R. Ex. 16103 at 20.

<sup>1775</sup> Tr. (Julian) at 7051; see also 22-03-07 Respondents’ Amended Revised Errata Days 9 -38” at page 57. Ordered through Second Supplemental Order Regarding Hearing Transcript Errata.

<sup>1776</sup> Tr. (Julian) at 7051-52.

The weak rating is predominately driven by three factors. First, Wells Fargo is currently lacking the capability to capture an overall view of sales practices risk across the Company. Second, the recently formed Office of Ethics, Oversight and Integrity (EOI) needs time to further build out and demonstrate effective oversight. Third, effectiveness and sustainability on the recently implemented enhancements remains to be demonstrated.<sup>1777</sup>

In reporting on “Complaints, Team Member Allegations and Internal Investigations”, the Assessment noted that there continued to be a need “for an enterprise view and reporting of all complaints to senior management and the Board (e.g., including ‘service complaints’ that are resolved same-day without escalation).”<sup>1778</sup>

As late as 2017, the Assessment reported:

Efforts are underway for some businesses to fully comply with the policy requirement for capturing third party service provider complaints, for reporting service complaint trends and root cause analysis to COG [Complaints Oversight Group], and for addressing complaint backlogs in consumer-focused areas that increased in Q4 2016. As such, the Complaints Management Policy implementation project is in ‘red’ (*i.e.*, off-track) status. Certain exceptions to the policy have been approved (*e.g.*, certain CL [Consumer Lending] businesses exclude disputes from Complaint Management & [O]versight, unless a wrongdoing is asserted), but more transparency and documentation is needed for an independent party to understand all approved exceptions logged by RCRM [Regulatory Compliance Risk Management].<sup>1779</sup>

Similarly, the Assessment found that Team Member Allegations processes, including EthicsLine, are rated “Weak” where that rating is defined thus: “The design is not adequate and lacks sufficient support; Enterprise risk management is not effective and does not balance risk with reward; Evidence does not exist and is not sufficient to be conclusive; [and] Enterprise risk management is not communicated, understood, or adhered to.”<sup>1780</sup>

For the purposes of ERMA, Team Member allegations include intake channels such as the EthicsLine that is administered by a third party and the respective research groups. The recently concluded 2016 Team Member Allegations and EthicsLine audit noted considerable work needed in the areas of oversight and reporting; allegations inventory; retaliation monitoring process; allegation research timeliness, process documentation and follow-

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<sup>1777</sup> R. Ex. 16103 at 1.

<sup>1778</sup> *Id.* at 15.

<sup>1779</sup> *Id.*

<sup>1780</sup> R. Ex. 16103 at 4, 20.

up procedures; and monitoring of the EthicsLine third party. Although numerous changes have been made both before and after the sales practices regulatory issues came to light, more time is needed to demonstrate sustainability. Thus, the overall development of Wells Fargo's allegations practices remains at an early stage.<sup>1781</sup>

The Assessment included a report on culture, including the following:

“Tone at the top” is a key to both culture setting and delivery throughout Wells Fargo. Policy changes as a result of sales practices issues and root cause analysis will involve senior leadership. These changes and other cultural expectations are often communicated through emails, Teamworks and Town Hall meetings. While the Board is expressing the right tone at the top, it is imperative to ensure that team members at all levels of the organization are understanding the intended message.<sup>1782</sup>

Mr. McLinko testified that the Assessment was “meeting the commitment that WFAS made in response to . . . MRA #5 in that WFAS would complete a Sales Practices ERMA . . . in this time frame.”<sup>1783</sup> He testified that this assessment was solely for assessing risk management for sales practices, and that WFAS had never conducted an ERMA specifically for risk assessment relating to sales practices.<sup>1784</sup>

Mr. McLinko was asked why WFAS decided to complete a Sales Practices ERMA for the first time in 2016, and, without acknowledging any role the MRAs had in identifying the need for such an assessment, he responded:

It was -- first of all, the way the risk management function was evolving within Wells Fargo, various components of the risk management -- risk management were being rolled out, and at the times that they were being rolled out and assessments were being performed on those. Since the sales practices framework had just been rolled out, the sales practices -- or the risk management assessment could be performed at that time.<sup>1785</sup>

Under Mr. McLinko's direction, the CBO audit team rated Community Banking's First Line of Defense sales practices processes and controls as Weak “given sustainability and effectiveness of a number of those controls have not had time to be fully assessed.”<sup>1786</sup>

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<sup>1781</sup> R. Ex. 16103 at 4.

<sup>1782</sup> *Id.* at 7.

<sup>1783</sup> Tr. (McLinko) at 8330.

<sup>1784</sup> Tr. (McLinko) at 8330-31.

<sup>1785</sup> Tr. (McLinko) at 8331.

<sup>1786</sup> Tr. (McLinko) at 8333; OCC Ex. 1878 at 12.

The narrative supplied by Mr. McLinko and the CBO audit team did not discuss the failure of the Community Bank's First Line of Defense to identify root causes for sales practices misconduct. Instead, it reported on "several changes during 2016 in response to the OCC's MRA's [*sic*]":<sup>1787</sup>

Senior management announced the removal of product sales goals in branches and call centers as of October 1, 2016, and assessed the impacts to incentive plans. 2017 incentive plans have been finalized. In addition, management has assessed further corrective actions resulting from the CFPB and OCC consent orders as well as the Los Angeles settlement. Specifically, in Q4 2016, CB management addressed the initial requirements of the consent orders and settlement including employee training, customer notifications and build out of processes such as mediation. Three new organizational positions were also created to focus customer experience and building analytical capabilities. As noted above, management has and continues to take multiple actions to address sales practices risk; however, most of these actions are still in process of build-out and/or early implementation and have not exhibited effectiveness or sustainability at this time.<sup>1788</sup>

Mr. McLinko testified that his role in drafting the Assessment was to review the draft prepared by his team regarding the Community Banking section appearing in the First Line of Defense section of the Assessment.<sup>1789</sup> He testified that members of his team determined the "Weak" rating, and that the rating was based on finding "the Community Bank was still in the process of developing their internal controls around sales practices. And the ones that they – even had been put in still hadn't been . . . proved to be sustained at that point. So it was based on a number of items like that."<sup>1790</sup>

In response to a request from the regulators, WFAS included in this ERMA an assessment of "Complaints, Team Member Allegations and Internal Investigations as these processes are an integral part of effective sales practices risk management."<sup>1791</sup> As of December 31, 2016, WFAS concluded the complaints processes across the enterprise "Need Improvement" based on this narrative:<sup>1792</sup>

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<sup>1787</sup> OCC Ex. 1878 at 12.

<sup>1788</sup> *Id.*

<sup>1789</sup> Tr. (McLinko) at 8332-33; OCC Ex. 1878 at 12.

<sup>1790</sup> Tr. (McLinko) at 8333.

<sup>1791</sup> OCC Ex. 1878 at 15.

<sup>1792</sup> *Id.* "Needs Improvement" is defined: "The design is not fully adequate or lacks sufficient support[.] Enterprise risk management is not fully effective or does not balance risk with reward[.] Evidence is minimal and may not be fully sufficient[.] Enterprise risk management is not consistently communicated, understood, or adhered to[.]" *Id.* at 20.

The Needs Improvement rating is driven by the need for an enterprise view and reporting of all complaints to senior management and the Board (e.g. including “service complaints” that are resolved same-day without escalation). Efforts are underway for some businesses to fully comply with the policy requirement for capturing third party service provider complaints, for reporting service complaint trends and root cause analysis to COG, and for addressing complaint backlogs in consumer-focused areas that increased in Q4 2016. As such, the Complaints Management Policy implementation project is in “red” (i.e. off-track) status. Certain exceptions to the policy have been approved (e.g. certain CL businesses exclude disputes from Complaint Management & oversight, unless a wrongdoing is asserted), but more transparency and documentation is needed for an independent party to understand all approved exceptions logged by RCRM.<sup>1793</sup>

The 2016 ERMA also found the “Team Member Allegations processes are rated Weak” based on the 2016 Team Member Allegations and EthicsLine audit.<sup>1794</sup> This audit “featured expanded testing on an enterprise basis and addressed regulatory issues related to sales practices for the EthicsLine area.”<sup>1795</sup> The audit “included testing of the intake of allegations through the action taken regardless of the group researching the allegations (e.g., Internal Investigations, SSCOT and Virtual Channel Conduct Oversight Teams (VCCOT) and Employee Relations).”<sup>1796</sup>

The Assessment noted, “there are multiple workstreams around team member allegation processes”, adding, “[s]ome work has already resulted in enhancements to the risk management practices”.<sup>1797</sup> The Assessment recommended “improvements to the risk management practices around the EthicsLine and allegations processes that are commensurate with Wells Fargo’s priority of rebuilding trust and stakeholder expectations.”<sup>1798</sup>

Included in the narrative of issues, the Assessment found “[t]he oversight and reporting over the team member allegations process needs to be strengthened, as we noted the following components were lacking: root cause analysis of allegations, actionable data and reporting over EthicsLine allegations, and oversight of the research groups’ resolution recommendation and escalation processes.”<sup>1799</sup>

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<sup>1793</sup> OCC Ex. 1878 at 15.

<sup>1794</sup> *Id.* at 16.

<sup>1795</sup> *Id.*

<sup>1796</sup> *Id.*

<sup>1797</sup> *Id.* at 17.

<sup>1798</sup> *Id.*

<sup>1799</sup> *Id.*

The 2016 Assessment found that enterprise risk management for Internal Investigations “Needs Improvement.”<sup>1800</sup> The Assessment reported that Internal Investigations “is responsible for investigating allegations of misconduct by internal team members or managed resources involving a possible violation of law, acts of dishonesty, breach of trust, significant violation of the Code of Ethics or the Information Security Policy.”<sup>1801</sup>

Further, the Assessment reported:

Regional Banking Sales and SSCOT or VCCOT refer sales practices related cases to Internal Investigations. SSCOT and VCCOT are responsible for obtaining sales information for sales practice related referrals, polling customers to verify that the customers opened the account(s) in question, and referring team members to Internal Investigations based on criteria documented in the SSCOT/VCCOT Service Level Agreement (SLA). Other LOBs submit sales practices referrals to Internal Investigations via the EthicsLine or other LOB referral sources.<sup>1802</sup>

The scope of WFAS’s audit of Internal Investigations “included a design of control assessment over SSCOT/VCCOT SLA; training, reporting quality review, and reporting [sic].”<sup>1803</sup> WFAS effectiveness testing included “separate samples for sales practices and other case types (no case, no SAR, SAR); data analytics for event and case timeliness; and Investigations Controlled Electronically (ICE) user access.”<sup>1804</sup>

Noteworthy in the audit findings was this narrative regarding risk exposure:

WFAS testing referenced above has identified issues which led to unmitigated risks and additional risk exposure. Specifically, Managers/District Managers are allowed to witness the team member investigative interviews increasing the risk of employees not speaking freely, undue influence, and potential opportunities for retaliation against team members. Testing also identified inappropriate system access to investigations in ICE, potentially compromising sensitive SAR related information, and other execution errors impacting SARs filing completeness. WFAS further identified issues related to enhancing SSCOT referral escalation processes and performing an annual review of the SSCOT SLA. The root cause of these issues are primarily driven by a combination of

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<sup>1800</sup> OCC Ex. 1878 at 17.

<sup>1801</sup> *Id.*

<sup>1802</sup> *Id.*

<sup>1803</sup> *Id.* at 18.

<sup>1804</sup> *Id.*

increasing volumes, design flaws, and resource constraints (people and technology).<sup>1805</sup>

Mr. McLinko testified that he had no responsibility for or role in drafting the “Complaints, Team Member Allegations and Internal Investigations” sections of this Assessment.<sup>1806</sup> He testified further, however, that the risk assessments and ratings presented in the 2016 Sales Practices Enterprise Risk Management Assessment all were based on information available to the auditors at the time the audit report is prepared, because you cannot “rate something that you don’t know about”.<sup>1807</sup>

In a response similar to that provided by Mr. Julian, when Mr. McLinko was asked through leading questioning by his Counsel during direct examination whether the “Weak” rating for Community Banking risk management over sales practices meant that the CBO’s prior assessments regarding Community Banking’s risk management were unreliable or false, Mr. McLinko responded, “no”.<sup>1808</sup>

Explaining why not, Mr. McLinko testified:

Because as the ERMA process evolved over the years, the methodology changed along with those -- with those processes. So what was included, what was excluded, et cetera. So the methodologies that were – that were in place at the time of those ERMAs that were prepared and the ratings that were produced by those ERMAs met the criterias [*sic*] and met the definitions for the rating criteria, so they were accurate.<sup>1809</sup>

Through its Executive Summary, the 2016 Sales Practices Risk Management ERMA provided “an enterprise view of sales practices risk” and was intended to “support effective and timely identification and management of sales practices risk.”<sup>1810</sup> The Summary reported, “[e]xtensive effort is needed to build a comprehensive risk assessment to understand where sales practices risk lies, including the list of products, distribution channels, legal entities, and associated incentive compensation and performance management.”<sup>1811</sup>

Elaborating on this point, the Summary reported:

Sales practices is a high risk area, with significant impact to Wells Fargo’s reputational risk. Following the sales practices settlements in late 2016, management demonstrated commitment to root cause analysis, issue

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<sup>1805</sup> OCC Ex. 1878 at 18.

<sup>1806</sup> Tr. (McLinko) at 8331-32.

<sup>1807</sup> Tr. (McLinko) at 8335.

<sup>1808</sup> Tr. (McLinko) at 8334.

<sup>1809</sup> Tr. (McLinko) at 8334.

<sup>1810</sup> OCC Ex. 1878 at 2.

<sup>1811</sup> *Id.*

resolution and ongoing monitoring. Major actions have included key leadership changes, elimination of product sales goals for retail bankers, enhancement of oversight and controls, and increased communication from the CEO and executive leadership.<sup>1812</sup>

The Summary also reported that the Second Line of Defense for sales practices, including “SPO, COG [Complaints Oversight Group], GEI, Financial Crimes Risk Management (FRCM) and other relevant functions including Corporate Human Resources, Regulatory Compliance Risk Management (RCRM), GRO, and Government and Community Relations” is rated “Weak”.<sup>1813</sup> The Summary reported that the rating “stems from the magnitude and complexity of the actions remaining to build and sustain an effective sales practices risk management program.”<sup>1814</sup>

In the Summary regarding the Second Line of Defense for sales practices, the auditors reported:

The Program establishes a foundation for risk management; however, enhancements are needed in key areas such as escalations, reporting, and clarity of roles and responsibilities. The escalation process through SPO [Sales Practices Oversight] needs to be formalized, with improved clarity and definition of trigger events for escalating. Additionally, an effective systems and data foundation does not exist at this time in order to timely and accurately aggregate and analyze sales practice risk across Wells Fargo. Both SPO and the Sales Practices Data Community of Practice have independently begun report development, but coordination and clear role and responsibilities are needed to ensure an effective process while avoiding duplication.<sup>1815</sup>

### **IOCC Supervisory Letter WFC 2016-49: Sales Practices Governance and Reporting Review**

Through a Supervisory Letter dated September 21, 2017, the OCC summarized the results of its Sales Practice Governance and Reporting review that began in November 2016.<sup>1816</sup> Describing SL 2015-36 (issued June 2015) as the baseline for the 2017 Letter, the OCC reflected that in June 2015 the OCC had concluded “that sales practices oversight was weak and in need of improvement.”<sup>1817</sup> The 2015 Letter included five MRAs across each of the three lines of defense,

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<sup>1812</sup> OCC Ex. 1878 at 2.

<sup>1813</sup> *Id.*

<sup>1814</sup> *Id.*

<sup>1815</sup> *Id.* at 3.

<sup>1816</sup> Tr. (Julian) at 7062; OCC Ex. 1689 at 1.

<sup>1817</sup> OCC Ex. 1689 at 1.



and “highlighted a number of breakdowns in governance, risk management, incentive compensation, reporting, and controls.”<sup>1818</sup>

The 2017 Letter noted that in July 2016, the OCC issued SL 2016-36, “citing the sales practices activities as unsafe or unsound.”<sup>1819</sup> Drawing from data gathered through independent consultant reports and the ongoing work of its examiners, the OCC “identified that aggressive sales pressure combined with a lack of adequate risk management oversight resulted in unsafe or unsound practices.”<sup>1820</sup> This work led in September 2016 to the Sales Practices Consent Order, which was announced in conjunction with the CFPB Consent Order and the Bank’s settlement with the Los Angeles City Attorney.<sup>1821</sup>

Subsequent to the issuance of the 2016 Consent Order, the OCC sought to assess “who at the executive management level knew about sales practices issues, when they became aware of the problems, and what if any actions these individuals took to address or escalate the issues to the Board and the [OCC].”<sup>1822</sup> The 2017 Letter considered Board committee meeting packages, Community Bank committee meeting packages, EthicsLine and customer complaints, termination notes, Suspicious Activity Reports, and over 400,000 emails.<sup>1823</sup>

Through this assessment, the OCC evaluated “who was held accountable for the unsafe or unsound and/or lack of adequate supervision or escalation.”<sup>1824</sup> The assessment leading to the 2017 Letter focused on Community Banking, which the OCC found was “responsible for retail sales and branch operations”.<sup>1825</sup> It also evaluated the role of the Board of Directors and the former CEO; along with the Law Department, Human Resources, Audit, and Corporate Risk, “given their oversight and/or control function responsibilities.”<sup>1826</sup> The assessment also evaluated employee terminations, EthicsLine allegations, and claims of retaliation.<sup>1827</sup>

In its supporting comments, the Letter identified the failure of former CEO John Stumpf to provide effective oversight of Community Banking.<sup>1828</sup> It reported, “the CB management team implemented aggressive sales goals and a poorly designed incentive compensation program

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<sup>1818</sup> OCC Ex. 1689 at 1.

<sup>1819</sup> *Id.* at 2.

<sup>1820</sup> *Id.*

<sup>1821</sup> *Id.*

<sup>1822</sup> *Id.*

<sup>1823</sup> *Id.* at 1.

<sup>1824</sup> *Id.* at 2.

<sup>1825</sup> *Id.*

<sup>1826</sup> *Id.*

<sup>1827</sup> *Id.*

<sup>1828</sup> *Id.* at 6.

which resulted in the widespread unethical activity, significant customer harm and reputational damage to the bank.”<sup>1829</sup>

The Letter noted the following in the history of the material issues:

In June of 2013, as a result of an increasing number of whistleblower emails regarding sales practices to the CEO, the Sales and Service Conduct Oversight Team (SSCOT) in the first line of defense launched an investigation into allegations of simulated funding in LA and Orange County (LA/OC). The bank initially terminated 30 employees in the LA/OC area and then launched a larger investigation across the company into simulated funding. As a result of the investigation, the bank terminated approximately 230 team members in total throughout 2014. None of this information was escalated to the OOC or the Board in 2013 or 2014. In February 2015, the OCC conducted a CB examination with a focus on sales practices governance to follow up on the claims of sales pressure. Multiple interviews were conducted with [Carrie] Tolstedt, [Claudia] Russ Anderson (Group Risk Officer), [Jason] MacDuff (Head of Strategic Planning) and a number of her direct reports. There was no mention of the 230 terminations related to simulated funding, or the larger issue of sales practices related terminations across the company.

In April 2015, Tolstedt presented to the Risk Committee of the Board on sales practices for the first time. There was no mention of the LA/OC investigation or the numbers of team members terminated on an annual basis. The focus was on the “Evolving Model” – the end to end improvement process developed to address some sales practices concerns. Just one month later, Tolstedt was again asked to present in response to the LA lawsuit that was filed on May 4, 2015. Her presentation focused only on the 230 terminated as a result of the LA/OC investigation with no mention of the larger body of terminations related to sales integrity issues. The root cause of the problem was summarized as a few rogue employees violating bank policy and the risk management team being aggressive in detecting and terminating team members engaging in conduct that violated CB policies. There was no mention of the history behind sales pressure, unattainable product goals, whistleblower complaints, SOX matters, or related class action lawsuits.

Tolstedt and Russ Anderson pushed back on the second and third lines of defense and were resistant to challenge and oversight by these groups. Tolstedt never voluntarily escalated sales practices issues, and when she did present at the Board level, the presentations were high level and viewed by many Board members as misleading. There was also a culture, pattern, and practice in the CB of redacting, minimizing and deleting material information

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<sup>1829</sup> OCC Ex. 1689 at 7.

that went to the Board or regulators. In an email exchange between Russ Anderson, Tolstedt, and various members of the Law Department on May 16, 2015, there were conversations about what to include in the Board presentation. A phone meeting was held later that evening and a decision was made to delete termination data from the presentation, which showed the CB was terminating one percent of team members annually. The same package was presented to the OCC as a part of our request [for] information for the May 2015 review, and CB leadership never provided this termination data despite OCC requests. In interviews with Russ Anderson, she stated to the OCC that sales pressure was not an underlying issue for increased turnover and terminations.<sup>1830</sup>

Specifically relating to Audit, the Letter reported the following:

WFAS had a clear view across the organization of the issues arising from sales practices due to work in Compliance, Community Banking, Compensation, Human Resources, and other related areas. WFAS became aware of sales practices irregularities and concerns as early as 2012. At that time, the head of Corporate Investigations sent the Chief Auditor (CA) an email regarding the increasing trend in sales integrity violations and complaints and highlighted concerns with the CB Group Risk Officer minimizing the information. The CA was also copied on a number of whistleblower complaints and served as a member of the Conduct Risk Committee that met quarterly in 2012 and 2013 to address these issues. In addition, WFAS regularly received reports showing an increasing number of sales practice-related issues including SAR filings and Ethics Line complaints before the L.A. Times Article in 2013. In spite of this visibility, WFAS did not accurately identify or escalate the issues around sales practices to the Board in a timely manner.

It is apparent that WFAS' focus was control testing to assess the effectiveness of processes and not on assessing the broader systemic issues including culture, compensation, and sales goals.

WFAS' coverage of sales practices was ineffective, evidenced by the fact that all twelve audits covering sales practices between 2013 and 2015 were rated as effective. Also, there was no independent audit coverage of branch activities; instead, the audit team relied heavily on the CB (first line) to assess branch controls. We found evidence that audit leadership lacked adequate independence from the CB. In one instance, the CB Executive Audit Director told the CB GRO not to discuss culture with the OCC and was briefing the CB GRO on a meeting with the OCC. [REDACTED]

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<sup>1830</sup> OCC Ex. 1689 at 7-8.

[REDACTED] The audit planned for May 2015 was not issued until March 2016 and was rated effective with only one issue. An overall rating of effective was given despite the results of the Accenture and PwC reports issued in October 2015 and February 2016, which cited significant deficiencies. WFAS must ensure that it maintains adequate independence to ensure a robust enterprise function.<sup>1831</sup>

In its conclusions, the OCC reported the following:

Since at least early 2011, Wells Fargo's (WF) executive and senior management teams failed to adequately address widespread sales practices issues originating in CB [Community Banking], and the Board of Directors failed in their oversight duties by inadequately challenging senior leadership. CB management enforced an aggressive sales culture that resulted in team members selling unwanted products to customers and opening unauthorized accounts. The former CEO was slow to react, depending instead on Wells Fargo's strong market perception, exceptional financial performance, and overall balance sheet strength. He failed to properly supervise the head of the CB and did not address known problems with leadership in that Group over an extended period of time. Additionally, the decentralized corporate structure, most notably within Corporate Risk and HR, exacerbated the problem and provided the CB with undue independence and limited accountability.

The control functions also failed in their responsibilities. Executives in the Law Department, HR, Corporate Risk and Audit were aware of sales practices issues at least as early as 2011 through whistleblower complaints and adverse sales integrity metrics, but did not escalate the situation to the Board or regulators in a timely manner. Management and the Board need to move much more quickly to identify and address critical issues. The Law Department and Corporate Risk must work more closely together to understand the broader risks contained in systemic legal issues and to ensure that the root cause of the issues are appropriately analyzed.

Escalation to and transparency with the Board of Directors and OCC is poor and must improve. CB management repeatedly failed to properly escalate the growing concerns around sales practices to the Board of Directors and the OCC. We found that CB management, primarily the head of CB and the Group Risk Officer, along with the Law Department and HR, engaged in a pattern and practice of minimizing and downplaying termination information

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<sup>1831</sup> OCC Ex. 1689 at 12-13.

and redacting information from OCC requests, ERMIC presentations, and employee exit interviews and surveys.

Unsafe or unsound sales practices have been identified in a number of areas within the bank, indicating that while the most significant problems were in the CB, the culture of poor behavior went beyond just the CB. Issues have been identified in Insurance, Merchant Services, and Private Banking. We also identified several instances of potential retaliation when team members escalated issues. Management needs to ensure that the new Sales Practices Governance and Oversight function captures sales practices activity across the company and addresses supervision, escalation and governance committees to ensure new products and incentive compensation plans are properly structured. Investigations are ongoing in a number of these areas and management should continue to keep the OCC apprised of findings and ensure remediation plans are consistent where appropriate and approved by a designated Board Committee.<sup>1832</sup>

### **OCC Requirements for a Heightened Standards Safety and Soundness Plan**

In a letter dated July 28, 2015, the OCC through its Examiner in Charge for Large Bank Supervision, Bradley Linskens, reported that it had determined that Wells Fargo Bank, N.A. “has failed to satisfy the safety and soundness standards contained in the OCC Guidelines Establishing Heightened Standards for Certain Large Insured National Banks”.<sup>1833</sup> The letter noted that enforcement actions and MRAs existed to address some of the weaknesses in the Bank’s compliance program, “recent compliance-related issues noted by various regulatory agencies, including the OCC, indicate significant actions remain to establish a fully effective compliance program.”<sup>1834</sup>

Two requirements directly required action by WFAS Internal Audit. In “Risk Assessment, Risk Appetite, and Testing”, the Bank was required to implement “a reliable compliance risk assessment and testing program” that would assess “compliance risk across material lines of business” and test line of business programs to “ensure timely corrective action by [lines of business]”.<sup>1835</sup> “The program should consider the distinct roles and responsibilities of front line units, RCRM, and Internal Audit and ensure independent evaluations and testing are conducted with an appropriate scope, coverage, and frequency by individuals with the requisite knowledge, skills, and abilities.”<sup>1836</sup>

The OCC noted here that while the

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<sup>1832</sup> OCC Ex. 1689 at 2-3.

<sup>1833</sup> OCC Ex. 2060 at 1.

<sup>1834</sup> *Id.*

<sup>1835</sup> *Id.* at 2.

<sup>1836</sup> *Id.*

primary basis for finding that the Bank is not in compliance with Appendix D relates to deficiencies in the Bank’s RCRM [Regulatory Compliance Risk Management], the Part 30 Plan must take into consideration the interdependencies of all three lines of defense to ensure that weaknesses in front line risk management or Internal Audit practices don’t undermine the effectiveness of actions taken to improve RCRM.<sup>1837</sup>

Internal Audit was specifically directed to “[s]taff the compliance audit function with respect to both the experience level and number of the individuals employed”, develop audit programs “that test the first lines of defense compliance with high-risk laws and regulations”, develop an audit strategy that “regularly assesses the effectiveness of the second line of defense (RCRM)”, and report “Internal Audit identified deficiencies to the Bank’s Audit and Examination Committee, along with the severity of the deficiencies and the corrective actions.”<sup>1838</sup>

### **Delegation of Duties by Mr. Julian to the WFAS Leadership Team**

Mr. Julian justified his failure to participate in the scoping of WFAS audits, the scheduling of those audits, and the allocation of resources for those audits, in these terms:

It would have been impossible for me, as Chief Auditor, one person, to be engaged in the planning, scoping, resource allocations of, as I mentioned, 200 to 300 audits a year in addition to all the other audit work that was going on. It wouldn't have allowed me to perform what I felt were my -- the appropriate responsibilities as Chief Auditor of Wells Fargo Corporation [*sic*].<sup>1839</sup>

Mr. Julian further justified this approach by stating that he “had confidence in the Wells Fargo Audit Services leadership team and the methodologies that were employed.”<sup>1840</sup> It should be noted, however, that elsewhere in his testimony Mr. Julian expressed concerns regarding the WFAS leadership team - specifically that upon assuming the duties of Chief Auditor, he “didn’t feel there was a very robust review from a top-down.”<sup>1841</sup>

He testified that he was further concerned that “you can build up a bottoms-up approach and actually potentially not cover or not address significant risks or risk areas that the company was focused on just by mistake, if you will.”<sup>1842</sup> Nothing in the record presents a basis to find the skills and qualifications of the same leadership team that gave rise to Mr. Julian’s concerns had somehow been adequately addressed to justify Mr. Julian’s confidence in them during his tenure.

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<sup>1837</sup> OCC Ex. 2060 at 2, n. 1.

<sup>1838</sup> *Id.* at 2.

<sup>1839</sup> Tr. (Julian) at 6014.

<sup>1840</sup> Tr. (Julian) at 6016.

<sup>1841</sup> Tr. (Julian) at 6004.

<sup>1842</sup> Tr. (Julian) at 6004.

In Mr. Julian's opinion, neither he nor Mr. McLinko had any responsibility for ensuring the accuracy of an individual audit.<sup>1843</sup> When asked what responsibilities he had during the relevant period for assuring the completeness of an individual audit, he said he had no such responsibility.<sup>1844</sup> In his view, "[i]t would have been impossible for me to carry out my role as Chief Auditor of Wells Fargo Corporation [*sic*] and at the same time be engaged in that level of detail with respect to that kind of work."<sup>1845</sup> Although he offered no evidence to support the factual claim, Mr. Julian testified that the OCC's bank examination team was aware of his practice of delegating these responsibilities, and raised no concerns to him about the need to change this approach.<sup>1846</sup>

Because of this approach, under Mr. Julian's leadership at WFAS the same employees who were responsible for determining the accuracy of a specific audit were also involved in determining the completeness of the audit.<sup>1847</sup>

Mr. Julian testified that the only responsibility he had for reading individual WFAS audit reports during the relevant period was to read those audit reports that had a "less than satisfactory audit rating."<sup>1848</sup> As a result, Mr. Julian did not read any audit reports that indicated satisfactory findings. Nothing in the record, however, supports Mr. Julian's assertion that he had no duty to read reports that indicated satisfactory findings.

Notwithstanding Mr. Julian's observation upon starting his work as Chief Auditor that there was not "a very robust review" from the "top-down",<sup>1849</sup> Mr. Julian elected to rely heavily on the WFAS "methodologies in the planning, scoping, [and] executing of the audit work."<sup>1850</sup> He noted in particular the Quality Assurance Group within WFAS, which he averred was "independent of any of those line of business audit groups" who "assessed the performance against the professional standards, looked at individual audits to provide assurance that the audit groups were executing the work in accordance with the professional standards."<sup>1851</sup> He asserted the Quality Assurance Group would take into account WFAS' policies and procedures and would assess "performance against the various industry standards, the OCC and any Federal Reserve standards that were applicable."<sup>1852</sup>

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<sup>1843</sup> Tr. (Julian) at 6018.

<sup>1844</sup> Tr. (Julian) at 6018.

<sup>1845</sup> Tr. (Julian) at 6018.

<sup>1846</sup> Tr. (Julian) at 6025.

<sup>1847</sup> Tr. (Julian) at 6018-19.

<sup>1848</sup> Tr. (Julian) at 6019.

<sup>1849</sup> Tr. (Julian) at 6004.

<sup>1850</sup> Tr. (Julian) at 6020.

<sup>1851</sup> Tr. (Julian) at 6021.

<sup>1852</sup> Tr. (Julian) at 6070.

Mr. Julian stated that he did not lead the Quality Assurance Group, but that it was instead led by “a senior person within [WFAS].”<sup>1853</sup> He said there were “permanent members of the team” and there were “rotational positions where at times we would move in certain individuals from Wells Fargo lines of business audit groups” to “bring a fresh perspective with respect to current work being performed.”<sup>1854</sup> There is no evidence, however, establishing the level of skills and experience that can be attributed to any of the members of this Group, nor has the Group’s charter been presented, if in fact it had one during the relevant period.

Mr. Julian identified a written report titled “Wells Fargo Audit Services – Audit Engagement Report; State of Audit Quality for the eighteen months ended June 30, 2013.”<sup>1855</sup> The Report was prepared by the WFAS Quality Assurance Group, which was led at that time by Brad Miller.<sup>1856</sup> The Group provided Mr. Julian with internal quality assessments, and during the relevant period the Group’s conclusions were that “throughout that [period] the work was being performed in accordance with the applicable professional standards.”<sup>1857</sup>

Little weight can be given to this Report or to its findings, however, as there is no evidence that the Quality Assurance Group was chartered to provide, or actually provided services relevant to, issues relating to sales practices misconduct relating to the Community Bank during the relevant period.<sup>1858</sup> Little weight can also be given to the 2014 Report of the Quality Assurance Group<sup>1859</sup> or the 2016 Report of the Quality Assurance Group,<sup>1860</sup> because again there is no charter establishing the credentials and scope of the Group’s mission and no evidence that the Report reflects determinations that were made independent of the WFAS management.

In addition, and apart from the Quality Assurance Group described above (and without specifying when this took place), Mr. Julian testified that early during his tenure he formed a group “made up of senior leaders across Wells Fargo Audit Services,” to whom he delegated the responsibility for reviewing audit reports prior to issuance.<sup>1861</sup> He averred that with “another set of eyes outside of the specific line of business audit group,” this would provide assurance that “the conclusions drawn were reasonable and appropriate.”<sup>1862</sup> And he asserted that “[t]o the extent that that group had concerns about any audit rating or challenges, they would have either

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<sup>1853</sup> Tr. (Julian) at 6070.

<sup>1854</sup> Tr. (Julian) at 6071.

<sup>1855</sup> Tr. (Julian) at 6072; R. Ex. 4399

<sup>1856</sup> Tr. (Julian) at 6072.

<sup>1857</sup> Tr. (Julian) at 6071.

<sup>1858</sup> See R. Ex. 4399 at Appendix A, reflecting the majority of internal core engagement reviews concerned 2012.

<sup>1859</sup> Tr. (Julian) at 6074-75; R. Ex. 7164.

<sup>1860</sup> Tr. (Julian) at 6077-79; R. Ex. 12075.

<sup>1861</sup> Tr. (Julian) at 6021.

<sup>1862</sup> Tr. (Julian) at 6021.



had that audit team or audit leadership group bring those to me so that I was aware of them”.<sup>1863</sup> Because of the work of this group, Mr. Julian felt the “added assurance that the work was being done appropriately, and therefore, effective rated audits weren’t really – reviewing them weren’t [*sic*] really a good use of my time based on the confidence I had in the execution of the work.”<sup>1864</sup>

In addition, Mr. Julian described a Director Level Review Program that was to “assure that the - the audit directors that were being included in these reviews, that their work was being done in accordance with the standards.”<sup>1865</sup> He testified that these reviews “just gave me additional comfort that not only is the overall audit program working in accordance with the applicable standards, but individual director level work was going on as well, consistent with the standards.”<sup>1866</sup> This testimony did not include reference to documentary evidence that would support Mr. Julian’s taking comfort in the overall audit program.

Mr. Julian identified an April 20, 2015 report of the Director Level Review Program of a review performed by Mr. McLinko as the EAD who was responsible for the Third Line of Defense for the Community Bank line of business.<sup>1867</sup> The report examined the five sub-processes subject to quality assessment: audit execution, issue management, plan and staff management, AMP tool management, and regulatory activities, and included the conclusion that in the Community Bank, “the five processes generally conforms to the IIA Standards for Professional Practices of the Internal Audit”.<sup>1868</sup>

Included in the Director Level Review report for 2015, the reporting team “reviewed one Enterprise Risk Management Assessment (ERMA) engagement and had documentation concerns around the evidence supporting the ERMA testing approach and the exclusion of conclusions reached.”<sup>1869</sup> No corrective action was reported – only that “QA knows the ERMA process is dynamic in nature and guidance is continually updates [*sic*].”<sup>1870</sup> Without identifying what changes followed or how effective those changes have been, the report stated only that “QA understands the CBO team has since made modifications to these processes.”<sup>1871</sup>

The report also evidences a continuing problem within senior managers at WFAS (including EAD McLinko) regarding weaknesses in issue management, [REDACTED]

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<sup>1863</sup> Tr. (Julian) at 6021-22.

<sup>1864</sup> Tr. (Julian) at 6022.

<sup>1865</sup> Tr. (Julian) at 6080.

<sup>1866</sup> Tr. (Julian) at 6080-81.

<sup>1867</sup> Tr. (Julian) at 6081; R. Ex. 9357.

<sup>1868</sup> Tr. (Julian) at 6083; R. Ex. 9357 at 2.

<sup>1869</sup> R. Ex. 9357 at 5.

<sup>1870</sup> *Id.*

<sup>1871</sup> *Id.*

[REDACTED]

[REDACTED]

[REDACTED]

In the 2015 Director Level Review (which covered January 1, 2013 to September 22, 2014), “QA noted some initial observations around the quality of the validation and status updates as well as the documentation necessary to allow workpapers to stand on their own and allow for third party reperformance,” including “[d]isposition of exceptions as non-reportable without identification of root cause to determine if errors are systemic in nature,” and a concern that documentation “lacked sufficient details for sample selection and population validation.”<sup>1877</sup>

Little weight can be given to the conclusions appearing in the 2015 Director Level Review. Notwithstanding the re-emergence of these previously identified issues, Mr. McLinko concluded that WFAS’s Quality Assurance Director Level review warranted a finding that each of the five processes being examined “generally conforms” to IIA and WFAS standards.

Despite the weaknesses evidenced by the lack of successful improvement over issues presented by the regulators in July 2013, and despite Mr. Julian’s awareness of the need to address those weaknesses, Mr. Julian testified that the 2015 Director Level Review report

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<sup>1872</sup> R. 740 at 6.

<sup>1873</sup> R. Ex. 740 at 2.

<sup>1874</sup> *Id.*

<sup>1875</sup> *Id.*

<sup>1876</sup> *Id.* at 5.

<sup>1877</sup> Tr. (Julian) at 6083; R. Ex. 9357 at 5.

“provided me a level of comfort that detailed work was done to assess Paul’s work and that his work generally conforms with the standards that were applicable.”<sup>1878</sup>

What is clear from the record is that at no time during the relevant period did the Internal Quality Assurance function ever raise even a red flag that WFAS had failed to conform to IIA Standards or raise concerns about WFAS’ work around the sales practices misconduct risk at the Community Bank.<sup>1879</sup> This is true notwithstanding the third-party reports published by the L.A. Times in late 2013 regarding abusive practices at the Community Bank.

### **Reports of OCC Examinations**

Without providing details about its provenance, Mr. Julian identified a “Core Assessment” dated as of September 30, 2013 detailing “Progress under Heightened Expectations”.<sup>1880</sup> Mr. Julian did not indicate the author(s) or source(s) of the Core Assessment, but testified that it is “specific to Wells Fargo & Company, the holding company Charter. And it’s [*sic*] progress under Heightened Expectations.”<sup>1881</sup>

The Assessment further identified “Significant Hindrances” in the Audit Function, including the need to improve in two areas: continuing to “strengthen the talent and skillsets of audit management team and staff”, and the need to “[e]xecute a dynamic audit plan that provides comprehensive coverage of material risks and issues in a timely manner.”<sup>1882</sup> The Assessment included this in its reporting of the significant hindrances to achieving an “A” Rating for each Heightened Expectation:

The substantive areas needing improvement to achieve a strong audit rating are:

Provide sufficient evidence of audit’s independent risk assessments, transparency of audit coverage with an emphasis on high-risk areas, credible challenge, and influence over the line of business risk management practices in the direction of strong across the risk spectrum.<sup>1883</sup>

Further, the September 2013 Assessment emphasized the “sanctity of the charter” when identifying the “most substantive goals for meeting this [Heightened Expectations]”.<sup>1884</sup> Those goals were stated as “the successful building out of a comprehensive enterprise-wide risk

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<sup>1878</sup> Tr. (Julian) at 6085; see also 22-03-07 Respondents’ Amended Revised Errata Days 9 -38” at page 42. Ordered through Second Supplemental Order Regarding Hearing Transcript Errata.

<sup>1879</sup> Tr. (Julian) at 6085-86.

<sup>1880</sup> Tr. (Julian) at 6214; R. Ex. 5357.

<sup>1881</sup> Tr. (Julian) at 6214.

<sup>1882</sup> R. Ex. 5357 at 4.

<sup>1883</sup> *Id.*

<sup>1884</sup> *Id.* at 5.

management framework and a fully effective Internal Audit function that identify and escalate risks, and provide credible challenge.”<sup>1885</sup>

The Assessment found that, *inter alia*, two key gaps prevented WF&C from reaching those goals: first, there was a need to “[i]mplement a formalized long-term strategic planning process and framework for ensuring consistency amongst various lines of business and business groups and address Board goals, objectives, and provide accountability”.<sup>1886</sup>

Second, there was the need to continue “ongoing initiatives to strengthen Internal Audit, which include but are not limited to attracting and retaining talent, providing credible challenge, issue resolution, expanding audits horizontally across functional business lines to capture associated risks, and stability at the chairmanship level of the Audit and Examination Committee.”<sup>1887</sup>

### **OCC’s February 2015 Examination of Community Bank**

Mr. Julian testified he received and read Supervisory Letter WFC 2015-07, the OCC through Examiner in Charge Bradley K. Linskens reported to Carrie Tolstedt, Community Bank’s Senior Executive Vice President, findings from the OCC’s February 2015 examination of Community Bank.<sup>1888</sup> Through this report, although rating Community Bank’s operational risk management “effective” and thus awarding its highest rating, the OCC found that the “[l]ack of a comprehensive governance framework exposes CB to heightened reputation risk and possible negative publicity. Without a formalized structure, it is difficult to demonstrate compliance with the firm’s values and goals while meeting strategic and financial objectives.”<sup>1889</sup>

The February 2015 Exam prompted the OCC to require the Community Bank to “establish an overarching framework and formalize current practices in policy.”<sup>1890</sup> To address existing deficits the OCC issued an MRA requiring the Community Bank’s policies and framework to, *inter alia*, define “escalation protocols and address the timing and reporting of information of CB’s sales activities to the CB Risk Management Committee” and define “appropriate sales practices and alignment with corporate values, goals, and mission statements.”<sup>1891</sup> The Community Bank was expressly required to “[d]ocument compensation and incentive plans along with processes used to identify and prevent inappropriate sales conduct

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<sup>1885</sup> R. Ex. 5357 at 5.

<sup>1886</sup> *Id.*

<sup>1887</sup> *Id.*

<sup>1888</sup> Tr. (Julian) at 6643; R. Ex. 654.

<sup>1889</sup> R. Ex. 654 at 3.

<sup>1890</sup> *Id.*

<sup>1891</sup> *Id.*

[and] [o]utline sales expectations for CB employees consistent with monitoring incentives for sales misconduct and employee turnover.”<sup>1892</sup>

The Examination report states that “GRO Russ Anderson agreed to address the corrective actions”, apparently without disagreeing with the findings.<sup>1893</sup>

While WFAS could not *set* Community Bank’s risk appetite and could not *design* the internal controls for the Community Bank, it was responsible for the *testing* of the controls in order to assure the Community Bank’s compliance with the Bank’s risk appetite. WFAS was required to assure the testing of the risks that were being managed, and was required to assure the effectiveness of those controls against the stated risk appetite of the Bank. **As Chief Auditor and as Executive Audit Director for Community Bank, respectively, the failure of Mr. Julian and Mr. McLinko between 2013 and 2015 to promptly escalate the Community Bank’s failure to set a risk appetite, under the facts presented, constituted an unsafe or unsound banking practice and constituted a breach of the fiduciary duties Mr. Julian and Mr. McLinko owed to the Bank.**

#### **Audit Engagement Report – Regional Bank Account Opening; March 18, 2016**

The record reflects that the A&E Committee received WFAS’s Fourth Quarter 2015 Summary, dated February 26, 2016.<sup>1894</sup> After identifying the Summary, Mr. Julian testified that in the section entitled “Sales Conduct, Practices, and Business Model,” there is a reference to the audit work that would become WFAS’s March 18, 2016 Regional Bank Account Opening Audit Engagement Report.<sup>1895</sup> The Quarterly Report stated, “Within Community Banking, the Regional Banking – Account Opening Audit is nearing completion and is being coordinated with Wells Fargo’s counsel. The focus of the review is account opening and sales practices.”<sup>1896</sup>

During direct examination, Mr. Julian was asked by his Counsel whether at the time WFAS issued the Fourth Quarter Summary he knew the scope of the Regional Bank Account Opening Audit had been changed, Mr. Julian responded that he “was not aware of that.”<sup>1897</sup>

Mr. Julian acknowledged through leading questioning by his Counsel during direct examination that before the report was issued in March 2016, he learned the scope of the audit had been narrowed.<sup>1898</sup> He gave the following explanation regarding how he learned about the narrowing:

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<sup>1892</sup> R. Ex. 654 at 3.

<sup>1893</sup> *Id.*

<sup>1894</sup> Tr. (Julian) at 6875; R. Ex. 11995.

<sup>1895</sup> Tr. (Julian) at 6875; R. Ex. 11995 at 64.

<sup>1896</sup> R. Ex. 11995 at 64.

<sup>1897</sup> Tr. (Julian) at 6875-76.

<sup>1898</sup> Tr. (Julian) at 6869.

I met with Paul McLinko just prior to the Regional Bank account-opening audit being issued, as it was being drafted and issued for issuance. And Paul met with me to discuss it, just knowing the sensitivity around Regional Bank account opening, to provide me an overview of the audit and the work. And in that meeting, the rating, as you see on this, was effective. And in that meeting, I questioned Paul, in general, you know, how can we give an effective rating over Regional Bank account opening in light of what we know or have heard about sales practices in that area? And at that time, Paul described to me the process that he and his team went through to define the scope for this audit.<sup>1899</sup>

Mr. Julian testified that this response “seemed reasonable and made sense to me, knowing all the work that was going on by the first and second line within the Regional Bank specific to the sales practices misconduct. Scoping out that work out of this audit made sense to me at the time.”<sup>1900</sup> He added to this answer with the following testimony, when asked whether he thought WFAS could have added value by having a broader scope to that audit:

No. Actually not. Because the purpose of -- one of the primary purposes of audit performing control testing is to determine if controls are working as intended and to identify any current or potential control issues. In this case, sales practice misconduct and the risk of that had been escalated by me, but escalated back in 20- -- you know, late 2013, early 2014, there was a significant amount of work going on by the first and second line as well as Wells Fargo Audit Services monitoring all that work. It really would have been redundant, if you will, for audit to go in, test control activities related to sales practices that the bank already was aware of. It wouldn't have added any value. Nothing would have changed as a result of audit doing that work to confirm, if you will, that the risk is there. I mean, a lot of work was already going on within it.<sup>1901</sup>

Asked why WFAS should not have canceled or delayed the audit, Mr. Julian responded:

When you look at the scope of the audit, notwithstanding that work was going on specific to identifying to the extent that there was sales practice misconduct activity going on as defined in this case, but the processes and the controls that were being tested in the Regional Bank account opening extended far beyond the consent, if you will, issues that were being investigated by first and second line. The process, once an account is opened or a customer walks in, wants an account, there's a whole process for assuring

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<sup>1899</sup> Tr. (Julian) at 6869; see also “22-03-07 Respondents’ Amended Revised Errata Days 9 -38” at page 54. Ordered through Second Supplemental Order Regarding Hearing Transcript Errata.

<sup>1900</sup> Tr. (Julian) at 6870.

<sup>1901</sup> Tr. (Julian) at 6870-71.

that that account is appropriately boarded, meaning put into the system, put into the reporting, identified, and customer information is provided to the customer. All those activities were still very relevant to the millions of accounts that were being opened appropriately. So it was important to still test those controls while excluding specifically the work that was going on within -- related to sales practice misconduct that was going on -- the work going on in the first and second line.<sup>1902</sup>

Mr. Julian testified that prior to the Report being issued in March 2016, he discussed the scope of the audit with Mr. McLinko, including the fact that Mr. McLinko had revised how the scope of the audit would be reflected in the report.<sup>1903</sup>

Through leading questions by his Counsel during direct examination, Mr. Julian testified that he never suspected that Mr. McLinko narrowed the scope of the Regional Bank Account Opening Audit because he was afraid or concerns about what that audit would find.<sup>1904</sup> According to Mr. Julian, “the risk . . . had been identified. A significant amount of work was already ongoing.”<sup>1905</sup>

Notwithstanding this testimony, Mr. Julian later testified that at no point did he make any assurances to WF&C based on the findings of the Regional Bank Account-Opening Audit, and acknowledged that the information in the March 2016 Report was not escalated to Board members.<sup>1906</sup> He justified this by stating, “that Audit was rated ‘Effective,’ and so there would have been nothing of significance to escalate to the Board.”<sup>1907</sup>

Mr. Julian added that he had no concerns that Board members were falsely assured about the state of sales practices in the Community Bank as the result of the Effective rating reported in March 2016 because,

[t]he Board was fully aware of all the work. They had received the MRAs. They had received management’s response. They were aware of all the activity that was going on with respect to addressing the MRAs. So this Audit wouldn’t have had or shouldn’t have had any implication in their thinking about the amount of effort going on and still needed to go on with respect to sales practices.<sup>1908</sup>

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<sup>1902</sup> Tr. (Julian) at 6871-72; see also “22-03-07 Respondents’ Amended Revised Errata Days 9 -38” at page 54. Ordered through Second Supplemental Order Regarding Hearing Transcript Errata.

<sup>1903</sup> Tr. (Julian) at 6872.

<sup>1904</sup> Tr. (Julian) at 6872.

<sup>1905</sup> Tr. (Julian) at 6872.

<sup>1906</sup> Tr. (Julian) at 6877.

<sup>1907</sup> Tr. (Julian) at 6877.

<sup>1908</sup> Tr. (Julian) at 6878.

Mr. Julian added that he never heard any Wells Fargo Board members express a concern that they were falsely assured by the March 2016 Regional Bank Account-Opening Audit.<sup>1909</sup>

The March 18, 2016 Audit Engagement Report rated as Effective the Regional Bank's Account Opening.<sup>1910</sup> This rating reflected WFAS's opinion that "the Originate and Set Up Account and User Access processes and controls are effective to manage corresponding risks."<sup>1911</sup> It reported that the "scope of the audit focused on the system of internal controls related to banker execution for originating and setting up demand deposit accounts (DDA), credit card, and direct auto loans within the stores. We also included a review of processes and controls relating to user access provisioning and maintenance for StoreVision Platform (SVP)."<sup>1912</sup>

Through leading questioning by his Counsel during direct examination, Mr. Julian testified that given Mr. McLinko's explanation of how the revised scope of the audit would be reflected in the report, Mr. Julian was comfortable with the Effective rating.<sup>1913</sup> He elaborated, without adding any material information:

Based on my understanding of the scope of work, I had confidence in the audit group performing the work that they would perform the work in line with the scope and come to an appropriate conclusion as to the effectiveness of the controls with respect to the work that was done around the scope.<sup>1914</sup>

#### **Evidence of Non-conformance with IIA Standards between 2012 and 2017<sup>1915</sup>**

IIA Standard 1130 requires that if independence or objectivity is "impaired in fact or appearance, the details of the impairment must be disclosed to appropriate parties."<sup>1916</sup> The 2017 EQA found that "[w]hile it may happen informally, WFAS does not have a formal procedure to notify the audit entity, senior management and/or the Audit & Examination Committee of an impairment."<sup>1917</sup>

IIA Standard 1210 requires that internal auditors "possess the knowledge, skills, and other competencies needed to perform their individual responsibilities."<sup>1918</sup> The 2017 EQA found that "a comprehensive understanding of each of Wells Fargo's business lines is critical for

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<sup>1909</sup> Tr. (Julian) at 6878.

<sup>1910</sup> R. Ex. 382 at 1.

<sup>1911</sup> *Id.* at 2.

<sup>1912</sup> *Id.*

<sup>1913</sup> Tr. (Julian) at 6873.

<sup>1914</sup> Tr. (Julian) at 6873.

<sup>1915</sup> See R. Ex. 16653 at 32, which describes the areas of improvement from the 2012 EQA report.

<sup>1916</sup> R. Ex. 16653 at 24.

<sup>1917</sup> *Id.*

<sup>1918</sup> *Id.* at 25.



WFAS personnel to meet stakeholder expectations and fulfill its mission.”<sup>1919</sup> From stakeholder interviews, PwC concluded that WFAS staff members “did not demonstrate a higher level of understanding of Wells Fargo’s business”.<sup>1920</sup> The record above supports a similar finding regarding Mr. Julian’s understanding of the limitations of WFAS and CBO’s audit function regarding risk management controls that were put in place by the Community Bank’s first line of defense between 2013 and 2015.

IIA Standard 2420 requires that communication “must be accurate, objective, clear, concise, constructive, complete, and timely.”<sup>1921</sup> The 2017 EQA found that stakeholders reportedly “expressed a desire to be: [m]ade aware of potential emerging risks, [m]ade aware of potential audit issues sooner, and [p]rovided more tactical/action oriented recommendations.”<sup>1922</sup>

IIA Standard 1220 provides that “[i]n exercising due professional care internal auditors must consider the use of technology-based audit and other data analysis techniques.”<sup>1923</sup> PwC reported that during interviews for the 2017 review, “several IA stakeholders expressed a desire for WFAS to further expand its use of technology and data analytics. It was noted that WFAS was in the process of establishing a centralized data analytics team which will be managed [by a] newly appointed executive audit director (EAD).”<sup>1924</sup>

#### **Evidence of Non-conformance with Industry Standards and Practices (November 30, 2017)<sup>1925</sup>**

In its 2017 Assessment of WFAS’ Alignment with Industry Standards and Practices, PwC reported that the “expectations placed on WFAS by stakeholders have and will continue to increase. Wells Fargo’s designation as a global systemically important financial institution (G-SIFI) demands that all of the Bank’s key assurance functions, specifically Internal Audit, operate at optimal performance.”<sup>1926</sup> The 2017 Assessment compared WFAS against “industry practices and regulatory and supervisory guidance”. Regulatory standards included “FRB SR 13-1 and the specific internal audit requirements within FRB SR 15-18, FRB SR 11-7, and the OCC’s Heightened Standards.”<sup>1927</sup>

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<sup>1919</sup> R. Ex. 16653 at 25.

<sup>1920</sup> *Id.*

<sup>1921</sup> *Id.* at 26.

<sup>1922</sup> *Id.*

<sup>1923</sup> *Id.* at 27.

<sup>1924</sup> *Id.*

<sup>1925</sup> *Id.* at 39, reporting the findings are based on information made available to PwC through October 31, 2017.

<sup>1926</sup> R. Ex. 16653 at 40.

<sup>1927</sup> *Id.*

SR13-01 required internal auditors receive a minimum of 40 hours of training in a given year.<sup>1928</sup> WFAS Team Member Development Policy required 40 hours of training per year for all audit personnel, but “data analytics team members are currently exempt from the monitoring related to this policy.”<sup>1929</sup>

SR13-01 required internal audit to “ensure a review takes place and appropriate action is taken after an adverse event.”<sup>1930</sup> The Standard required internal audit to “evaluate management’s analysis of the reasons for the event and whether the adverse event was the result of a control breakdown or failure, and identify the measures that should be put in place to prevent a similar event from occurring in the future.”<sup>1931</sup> The 2017 Assessment found that in their reporting to the Audit and Examination Committee of the Board, WFAS “only includes ‘reportable’ lessons learned.” The Assessment recommended that WFAS “enhance the board reporting of lessons learned to include ‘non-reportable’ enhancements (e.g., changes to audit scope, timing, test procedures).”<sup>1932</sup>

SR13-01 required internal audit to evaluate “the reasonableness of established limits and perform[] sufficient testing to ensure that management is operating within risk tolerance limits and other restrictions.”<sup>1933</sup> The 2017 Assessment noted, “WFAS does not consistently consider limits across the enterprise” when performing individual audits.<sup>1934</sup> “WFAS is not testing to ensure limits are reasonable for the level of business activity being performed by the audit entity.”<sup>1935</sup> The Assessment further found that WFAS is not “consistently testing the business’ ability to operate within their established limits, or the related escalation processes if limits are broken.”<sup>1936</sup> Further, the Assessment found WFAS was not “evaluating management’s aggregation of limits to consider the impact limits may have on risk tolerances.”<sup>1937</sup>

### **Escalation of Issues within WFAS**

Each of the WFAS Executive Audit Directors reported directly to Mr. Julian.<sup>1938</sup> He testified that he would, on a “routine basis,” meet with each EAD, “just to have dialogue about

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<sup>1928</sup> R. Ex. 16653 at 45.

<sup>1929</sup> *Id.*

<sup>1930</sup> *Id.* at 47.

<sup>1931</sup> *Id.*

<sup>1932</sup> *Id.*

<sup>1933</sup> *Id.* at 52.

<sup>1934</sup> *Id.*

<sup>1935</sup> *Id.*

<sup>1936</sup> *Id.*

<sup>1937</sup> *Id.*

<sup>1938</sup> Tr. (Julian) at 6022.

the work that they were doing, what they were seeing within their audit group.”<sup>1939</sup> He said he also met “at least monthly, if not bimonthly,” with “the leadership team” to talk about “issues that each one was aware of in their own group to share dialogue amongst the whole group.”<sup>1940</sup> He did not couple this testimony with any references to documentary evidence that would support these averments.

Mr. Julian testified that one of the objectives of the quarterly meetings between WFAS and Corporate Risk was to discuss the Noteworthy Risk Reports created during the Enterprise Risk Management Committee (ERMC) meetings.<sup>1941</sup> Mr. Julian identified the July 2014 Noteworthy Risk Issues memo as the product one such discussion.<sup>1942</sup> Through leading questioning by his Counsel on direct examination, Mr. Julian testified that those discussions were one of the ways in which members on his team, including Mr. McLinko, escalated to Mr. Julian and to the ERMC their views on emerging and significant risks.<sup>1943</sup>

### **The CBO’s Duties under the WFAS Audit Charter**

WFAS’s CBO under Mr. McLinko had the duty to provide an independent assurance and advisory function to A&E. Through its assurance and advisory work, Mr. Julian, WFAS, Mr. McLinko, and each EAD, were required to help the Bank accomplish its objectives by bringing a systematic and disciplined approach to evaluate and improve the effectiveness of enterprise governance, risk management, and control processes across the enterprise.

Mr. Julian offered as evidence the WFAS Audit Charter describing the “mission and purpose and scope and work” of WFAS.<sup>1944</sup> Although he offered no authority to support this proposition, he testified that the Audit Charter imposed no additional professional responsibilities on WFAS beyond those required by the IIA Standards, asserting,<sup>1945</sup> “the IIA Standards were the professional standards by which Wells Fargo Audit Services needed to conduct itself.”<sup>1946</sup> He asserted that the WFAS Audit Charter served only to provide “clarity with respect to the IIA Standards.”<sup>1947</sup>

### **Features of the 2014 WFAS Audit Charter**

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<sup>1939</sup> Tr. (Julian) at 6023.

<sup>1940</sup> Tr. (Julian) at 6023.

<sup>1941</sup> Tr. (Julian) at 6900; see e.g. Noteworthy Risk Issues – July 2014, OCC Ex. 1103.

<sup>1942</sup> Tr. (Julian) at 6590; OCC Ex. 1103.

<sup>1943</sup> Tr. (Julian) at 6901.

<sup>1944</sup> Tr. (Julian) at 6026-28, OCC Ex. 2087, approved by the WF&C A&E Committee on 2/26/2013 (see Resp. Ex. 20591, minutes of the A&E Committee meeting of February 26, 2013).

<sup>1945</sup> Tr. (Julian) at 6029.

<sup>1946</sup> Tr. (Julian) at 6029.

<sup>1947</sup> Tr. (Julian) at 6029.

Included in the 2014 Audit Charter was the express requirement that WFAS assure that the “operational risk is effective so that risk of loss resulting from inadequate or failed internal processes, people and systems or from external events is adequately controlled.”<sup>1948</sup> The Charter was not limited to a statement of what WFAS was required to “assure”; it also required that WFAS “[e]nsure effective corrective actions are taken to strengthen reported control weaknesses or uncontrolled risks.”<sup>1949</sup>

Nothing in the 2014 Charter prevented WFAS from changing the Plan upon cause shown, but the Charter did require WFAS to “[c]ommunicate adjustments to the audit plan timely to the Audit & Examination Committee”.<sup>1950</sup> Further, by the end of 2013, WFAS was required in its 2014 Audit Report to provide “annual individual opinions/assessments of credit, market, and operations risk management” from 2013.<sup>1951</sup>

### **The Role of IIA Standards in the WFAS Audit Charter**

The record does not support the factual premise espoused by Mr. Julian that the WFAS Audit Charter’s purpose was to provide “clarity” with respect to the IIA Standards. The WFAS Audit Charter provided that WF&C’s Internal Auditing Department “is an independent, objective assurance and consulting activity designed to add value and improve an organization’s operations. It helps an organization accomplish its objectives by bringing a systematic, disciplined approach to evaluate and improve the effectiveness of risk management, control and governance processes.”<sup>1952</sup>

The Charter provided that the Internal Audit Department “recognizes the IIA’s mandatory definition of Internal Audit and will adhere to the *International Standards for the Professional Practice of Internal Auditing* and the Code of Ethics of the Institute of Internal Auditors.”<sup>1953</sup> There is no suggestion in the WFAS Audit Charter, however, that its purpose is tied in any way to providing “clarity” to IIA standards. The source of controlling standards for WFAS throughout Mr. McLinko’s term as the Community Bank’s EAD for WFAS was the WFAS Audit Charter – which recognizes the existence and applicability of IIA Standards – nothing more, and nothing less.

Pursuant to the WFAS Audit Charter, the mission and purpose of Internal Audit was to serve as a “provider of independent, objective assurance and consulting services delivered through a highly competent and diverse team.”<sup>1954</sup> As a business partner, Internal Audit was required to help the Company accomplish its objectives by bringing a systematic disciplined

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<sup>1948</sup> R. Ex. 423 at 2.

<sup>1949</sup> *Id.*

<sup>1950</sup> *Id.* at 3.

<sup>1951</sup> *Id.* at 2.

<sup>1952</sup> OCC Exhibit 2087 at 4, n.1

<sup>1953</sup> *Id.* at 3.

<sup>1954</sup> *Id.* at 1.

approach to evaluate and improve the effectiveness of risk management, control, and governance processes.<sup>1955</sup>

Through its assurance and consulting work, Audit:

- Conducts tests and provides conclusive reporting regarding the health of the risk management and internal control structure within the Company.
- Advises management on risk based management practices and controls in the design of new business products/processes. This includes timely involvement in product and system development, operations changes, and strategic initiatives to ensure risks are identified at an early stage.
- Functions as a change agent to ensure risk issues are escalated and resolved.
- Functions as a source of talent and a training ground for other areas in the Company.<sup>1956</sup>

The role of WFAS was to perform audit work designed to provide assurance to management and to the Board that the controls that management oversaw were working as intended or as designed. WFAS was expected to serve as a change agent to ensure risk issues were identified, escalated, and resolved. Under Mr. McLinko's direction the CBO had direct engagement with the various lines of Community Banking business and was expected to assure the Bank that these lines of business were addressing the risks associated with the line of business, that the lines of business escalated reportable issues by bringing the issues to the attention of senior management where appropriate, and by ultimately resolving the issues so identified.

### **Leveraging Audit Functions through the First and Second Lines of Defense**

Mr. Julian testified that in order for the Bank's internal controls to work effectively, "you had to have all three lines of defense doing the work they're accountable to do."<sup>1957</sup> Relying on language in the Audit Charter that Internal Audit should function as "a business partner,"<sup>1958</sup> Mr. Julian asserted Internal Audit could "work together" with the First and Second Lines of Defense "to ensure that there was appropriate communications and dialogue going on."<sup>1959</sup>

The record does not reflect that Mr. Julian ever shared with the OCC, the Chair of the WF&C A&E Committee, or the members of the WF&C Board of Directors this assertion – the assertion that WFAS Internal Auditors could "rely on" the work performed by the First and

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<sup>1955</sup> OCC Exhibit 2087 at 1.

<sup>1956</sup> *Id.* (2013); R. Ex. 423 at 1 (2014)

<sup>1957</sup> Tr. (Julian) at 6033.

<sup>1958</sup> OCC Ex. 2087 at 1.

<sup>1959</sup> Tr. (Julian) at 6033.

Second Lines of Defense while still maintaining the independence required under the Audit Charter.

### **The Role of the Chief Auditor and WFAS as Change Agents**

Mr. Julian acknowledged that within the WFAS Audit Charter was the requirement that Internal Audit “[f]unctions as a change agent to ensure risk issues are escalated and resolved.”<sup>1960</sup> He attributed the “first and foremost responsibil[ity]” for the change agent function was with “the Audit Group who had day-in and day-out engagement with the various lines of business or their respective line of business”.<sup>1961</sup> Those members of WFAS, according to Mr. Julian, had the responsibility to “assure that the line of business was addressing the risks, escalating where appropriate and ultimately resolving the issues that were identified.”<sup>1962</sup>

### **Describing the Scope of WFAS Internal Audit’s Work**

The WFAS Audit Charter stated that the scope of Internal Audit work was “to determine if the Company’s risk management, systems of control, and governance processes are adequate and functioning as intended.”<sup>1963</sup> Mr. Julian opined that this meant that through the course of Internal Audit’s work, “Audit was responsible for assuring that -- in an overview, that the controls were working as intended, that there were governance processes in place to manage the risk that the business unit was accountable for managing.”<sup>1964</sup>

Asked to explain what it meant to “assure” in this context, Mr. Julian replied thus:

Well, so audit would perform work, whether it be control testing, whether it be monitoring activities, to provide assurance that management was addressing the issue or that the control was working appropriately. I think, as we talked earlier, audit wasn't providing 100 percent guarantee that every control worked appropriately or that audit identified every control where it wasn't working appropriately. But to provide an assurance based on a scope and level of work audit was doing.<sup>1965</sup>

The Charter called for WFAS to employ “a dynamic audit program” in order to accomplish its mission.<sup>1966</sup> Under the Charter, WFAS was expected to assure that the Board’s Governance system “is adequately designed in compliance with regulatory requirements.”<sup>1967</sup>

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<sup>1960</sup> OCC Ex. 2087 at 1.

<sup>1961</sup> Tr. (Julian) at 6035.

<sup>1962</sup> Tr. (Julian) at 6035-36; see also “22-03-07 Respondents’ Amended Revised Errata Days 9 -38” at page 41. Ordered through Second Supplemental Order Regarding Hearing Transcript Errata.

<sup>1963</sup> OCC Ex. 2087 at 1 (2013); R. Ex. 423 at 1 (2014).

<sup>1964</sup> Tr. (Julian) at 6036.

<sup>1965</sup> Tr. (Julian) at 6037.

<sup>1966</sup> OCC Ex. 2087 at 1.

<sup>1967</sup> *Id.*

This included assuring that the Board adheres to “key governance documents” and is receiving “appropriate, accurate, and timely information.”<sup>1968</sup>

The Charter imposed upon WFAS and Mr. McLinko the obligation to assure that “Corporate Governance functions and processes provide adequate direction and oversight.”<sup>1969</sup>

### **Internal Audit’s Duties Regarding Appropriate Culture in the Organization**

WFAS was required to assure that “[a]n appropriate culture has been established, understood, and consistently complied with across the organization.”<sup>1970</sup> Mr. Julian asserted that this meant, “the company had its vision and values, and Audit was to assure that those vision and values were appropriately understood throughout the organization, that there was an appropriate tone at the top by management and by risk owners with respect to managing risks.”<sup>1971</sup> He added that the provision required that Audit assure that “there was appropriate training and awareness, again, of the vision and values and the culture that was expected through those vision and values.”<sup>1972</sup>

Mr. Julian testified that Internal Audit under his direction assessed the risk culture across the enterprise in 2013 “through dialogue with the various risk owners.”<sup>1973</sup> As an example, he stated, “to the extent the audit would execute work and identify issues or potential issues and communicate those to the business unit, was the business unit responsive in addressing those? Did they provide the right level of resources and urgency depending on the nature of the issue? Or did they ignore it?”<sup>1974</sup> Through this answer, however, Mr. Julian identified *no audit work* that was actually designed to identify the efficacy of the Community Bank’s controls regarding sales practices misconduct issues or related potential risk issues, nor any evidence that WFAS communicated those issues to the business unit.

Elaborating on this response, Mr. Julian stated: “Audit was looking to see that there was appropriate risk culture within their risk tolerance and that the dialogue was one of understanding that the business unit owned the risk and they take appropriate actions to address the risk.”<sup>1975</sup>

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<sup>1968</sup> OCC Ex. 2087 at 1.

<sup>1969</sup> *Id.*

<sup>1970</sup> *Id.*

<sup>1971</sup> Tr. (Julian) at 6038.

<sup>1972</sup> Tr. (Julian) at 6038.

<sup>1973</sup> Tr. (Julian) at 6038.

<sup>1974</sup> Tr. (Julian) at 6038.

<sup>1975</sup> Tr. (Julian) at 6039

WFAS Internal Audit was required to assure that “[o]bjectives align with the Company’s mission and an appropriate risk appetite.”<sup>1976</sup> Under the Charter, Mr. McLinko was required to assure that communication systems are in place “to share information with stakeholders,” including employees, customers, shareholders, and community government.<sup>1977</sup>

### **Internal Audit’s Duties Regarding the Design of Risk Management Systems**

Under the WFAS Audit Charter, Internal Audit was required to assure that the enterprise-wide risk-management system “is adequately designed to ensure risks, including emerging risks, are appropriately identified and managed, and risk approvals, acceptances, and escalations are appropriately administered.”<sup>1978</sup>

According to Mr. Julian, this meant that,

In addition to testing control environments, Audit would also assess the design of the control environment to assure that the control environment that was designed and implemented by the risk owner was appropriately designed, that it took into consideration information, such as emerging risks, risk approval, risk acceptance, so that the risk management system took into account all that was designed in accordance with that.<sup>1979</sup>

In the WFAS Audit Plan for 2013, in the section titled “Ongoing Risk Identification and Response,” the Plan provides that after WFAS presented its dynamic plan to the A&E Committee, “an ongoing risk identification process is in place to respond to changes in strategic risk factors, risk profiles and as enterprise events occur.”<sup>1980</sup>

The Plan required “Audit leadership” (which would include both Mr. Julian and Mr. McLinko) to remain “informed of enterprise and [Risk Assessable Business Unit, or RABU<sup>1981</sup>] activities,” and that such leadership “adjust[] resource deployment to areas of heightened importance, showing signs of control stress, or those that could deteriorate in the future.”<sup>1982</sup>

The 2013 Plan also provided that new or emerging risks that may impact multiple [Operating Committee Group, or OCGs<sup>1983</sup>] “or could result in substantial reputational damage, criticism by regulators or the media, significant financial impacts, legal ramification or

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<sup>1976</sup> OCC Ex. 2087 at 1 (2013); R. Ex. 423 at 1 (2014).

<sup>1977</sup> OCC Ex. 2087 at 1.

<sup>1978</sup> OCC Ex. 2087 at 1 (2013); R. Ex. 423 at 1 (2014).

<sup>1979</sup> Tr. (Julian) at 6039-40; see also “22-03-07 Respondents’ Amended Revised Errata Days 9 -38” at page 4. Ordered through Second Supplemental Order Regarding Hearing Transcript Errata.

<sup>1980</sup> R. Ex. 3560 at 26.

<sup>1981</sup> *Id.* at 39.

<sup>1982</sup> *Id.* at 27.

<sup>1983</sup> *Id.* at 39, stating the OGC consists of the CEO’s direct reports, indicating that this is “the highest level in the WFC organization structure.”



interference with the normal operations of the business are escalated to the [Audit Management Committee<sup>1984</sup>] for further evaluation.”<sup>1985</sup>

In the case where new or emerging risks may impact multiple Bank OCGs or could result in substantial reputational damage, or could result in criticism by regulators or the media, or could lead to significant financial impacts, legal ramification or interference with the normal operations of the business, those risk were to be escalated, which is to say that both Mr. Julian and Mr. McLinko were required to bring those risks to the attention of the WF&C Audit Management Committee for further evaluation.

The 2013 Plan provides that “[b]usiness monitoring” is a “vital part of the ongoing risk identification activity”, and states that such monitoring “includes continuous risk assessments, analyses of business reporting and metrics, and issue follow-up. It also includes a call/awareness program from a variety of internal and external sources to keep apprised of new and emerging risks.”<sup>1986</sup>

As distinct from business monitoring, the Plan also described the role of results taken from testing groups:

WFAS uses results from risk management/control testing groups when certain criteria are met, e.g., independence, competence, supervision, authoritative reporting, and timely issue follow-up, to inform its ongoing assessment of enterprise risk and potentially reset the [Risk Assessable Business Unit]-process last coverage date.<sup>1987</sup>

### **Internal Audit’s Duties Regarding the Management of Reputation Risk**

With respect to WFAS’s duty to assure the adequacy of the enterprise’s risk management, WFAS and Mr. McLinko both were expressly required to assure that “[r]eputation risk is effectively managed and the company’s brand protected.”<sup>1988</sup>

According to Mr. Julian, “reputation risk was a byproduct of the effectiveness from Audit's perspective. At least reputation risk with respect to a control environment of the management of risk was a byproduct of how well functioning the controls worked.”<sup>1989</sup> Internal Audit’s role was “assuring that controls were working,” that they were “designed appropriately

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<sup>1984</sup> R. Ex. 3560 at 39.

<sup>1985</sup> *Id.* at 27.

<sup>1986</sup> *Id.*

<sup>1987</sup> *Id.*

<sup>1988</sup> OCC Ex. 2087 at 1.

<sup>1989</sup> Tr. (Julian) at 6040.

and working as intended”.<sup>1990</sup> If so, then “that would help to manag[e] the reputational risk of a control breakdown and, therefore, creating a negative reputation issue.”<sup>1991</sup>

Under the Audit Charter, WFAS Internal Audit was required to assure that “[s]ignificant financial, managerial, and operating information is accurate, reliable, and timely.”<sup>1992</sup> It was required to assure that “[s]ignificant legislative or regulatory issues impacting the organization are recognized and addressed appropriately.”<sup>1993</sup> Each of the issues and Matters Requiring Attention that were presented to the Bank through the OCC’s Supervisory Letter of June 26, 2015 involved regulatory issues affecting the Bank.<sup>1994</sup>

### **Internal Audit’s Duties Regarding Compensation Programs**

Under the Audit Charter, WFAS was required to assure that the organization’s compensation programs “incent appropriate and desired behavior.”<sup>1995</sup> Mr. Julian testified that “[i]t was important that compensation programs incented the appropriate and desired behavior, specifically within risk and reward”.<sup>1996</sup> He said, “Audit’s role with respect to that was to assure that there was an appropriate governance model providing oversight on the compensation programs that were implemented and managed by the various lines of business.”<sup>1997</sup>

Mr. Julian asserted that the role of WFAS regarding the governance model “was to make sure there was an appropriate governance model in the development of those, meaning . . . were the people who should be designing them designing them? Was there the right level of people engaged in the design of them? [Were] there review programs in place, governance structure to assure that by both the First and the Second Line?”<sup>1998</sup>

Under the WFAS Audit Charter, Internal Audit was required to assure that the organization’s policies were sound and strong, and “employees’ actions are in compliance with the policies, standards, procedures, and applicable laws and regulations.”<sup>1999</sup>

Mr. Julian testified that as Internal Audit was performing its testing of controls, “it was important to test against in compliance [*sic*] with the various policies, standards, procedures,

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<sup>1990</sup> Tr. (Julian) at 6040.

<sup>1991</sup> Tr. (Julian) at 6040.

<sup>1992</sup> OCC Ex. 2087 at 1 (2013); R. Ex. 423 at 2 (2014).

<sup>1993</sup> OCC Ex. 2087 at 1.

<sup>1994</sup> See OCC Ex. 1239.

<sup>1995</sup> OCC Ex. 2087 at 1.

<sup>1996</sup> Tr. (Julian) at 6041.

<sup>1997</sup> Tr. (Julian) at 6041.

<sup>1998</sup> Tr. (Julian) at 6042.

<sup>1999</sup> OCC Ex. 2087 at 1 (2013); R. Ex. 423 at 1 (2014).

applicable rules, oversight the management of that risk. So audit would test compliance with those various policies or standards that the business unit developed.”<sup>2000</sup>

Asked on direct examination whether, during 2013, he had any reason for concern to believe WFAS was failing to perform appropriately and competently the work described in the Scope of Work section of the WFAS Audit Charter, Mr. Julian responded, “No.”<sup>2001</sup> He added however, that WFAS could not “directly manage each of the items” discussed during this testimony.<sup>2002</sup> He said to do so would “impede on WFAS’s independence and objectivity in executing its work.”<sup>2003</sup>

Instead of “directly manag[ing]” the items in the Audit Charter’s Scope of Work section discussed to this point, Mr. Julian testified that the responsibility of WFAS Internal Audit was to “assure that the company had designed appropriate controls, built appropriate business governance, activities, and tested to assure that governance practices and controls were working as intended.”<sup>2004</sup> He testified, however, that he personally was not responsible for executing each of the items identified in the WFAS Audit Charter’s Scope of Work section.<sup>2005</sup> Instead, the responsibility for performing the work reflected in the Scope of Work section was borne by the “various audit line of business groups.”<sup>2006</sup> This presumably included the CBO under Mr. McLinko’s leadership.

Pursuant to the Scope of Work in the WFAS Audit Charter, Internal Audit was required to assure that the organization’s technology “supports achievement of the Company’s goals and objectives”,<sup>2007</sup> was required to assure that the organization’s programs, plans, and objectives are achieved and its resources are protected adequately,<sup>2008</sup> and was required to assure that “[q]uality assurance and continuous improvement are fostered in the organization’s control process”.<sup>2009</sup>

The WFAS Audit Charter expressly provided that the need for changes in an audit plan may become clear during the implementation of audits. Thus, “[o]pportunities for improving management profitability and the organization’s reputation may be identified during audits, and communicated to the appropriate level of management.”<sup>2010</sup>

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<sup>2000</sup> Tr. (Julian) at 6042-43.

<sup>2001</sup> Tr. (Julian) at 6043

<sup>2002</sup> Tr. (Julian) at 6032.

<sup>2003</sup> Tr. (Julian) at 6043.

<sup>2004</sup> Tr. (Julian) at 6044.

<sup>2005</sup> Tr. (Julian) at 6044.

<sup>2006</sup> Tr. (Julian) at 6044.

<sup>2007</sup> OCC Ex. 2087 at 1.

<sup>2008</sup> *Id.*

<sup>2009</sup> *Id.*

<sup>2010</sup> *Id.* at 2 (2013); R. Ex. 423 at 2 (2014).

Given the dynamic nature of the scope of WFAS audits, changes that may be detected during the implementation of an individual audit or an annual Audit Plan could create opportunities for improving management profitability and the organization’s reputation. Such opportunities could arise when there was a deficit in risk management – when something was *ineffective or not working as intended*.

These opportunities for improvement were then supposed to be communicated – escalated – to the appropriate level of management by Mr. Julian (at the enterprise level) and by Mr. McLinko (for the Community Bank). Because the issue of sales practices misconduct arose during the relevant period, both Mr. Julian and Mr. McLinko had the fiduciary duty to bring the issue of sales practices misconduct to the relevant level of management. This included the duty to bring the relevant issue to the committees Mr. Julian and Mr. McLinko served on – regardless of whether their service was as a voting member or a non-voting member.

Under the WFAS Charter, the Chief Auditor “shall be accountable to the Management Committee and the Audit & Examination committee” with the responsibility to develop and employ a dynamic audit plan to be submitted to the A&E Committee for its review and approval, “using an appropriate risk-based methodology, including any risks or control concerns identified by management ensuring it effectively responds to and addresses new and emerging risks/hot topics in a timely (rapid) fashion.”<sup>2011</sup> Under the WFAS Audit Charter, the staff of the Internal Audit department of WFAS, including Mr. McLinko, had the same responsibility.<sup>2012</sup>

Under the WFAS Charter, Mr. Julian and Mr. McLinko each had the responsibility to develop and employ a plan that included any risks or control concerns identified by management ensuring it effectively responds to and addresses new and emerging risks or hot topics in a timely fashion. By early 2013, Corporate Investigations had identified risks arising from an increasing number of sales practices misconduct cases by Community Bank team members, and had provided information about those risks to Ms. Russ Anderson, Mr. Julian and Mr. McLinko. These risks needed to be addressed through the dynamic audit plan.

Under the WFAS Charter, the Chief Auditor “shall be accountable to the Management Committee and the Audit & Examination committee” with the responsibility to provide “periodic information on the status and results of the audit plan and the sufficiency of department resources”;<sup>2013</sup> the responsibility to “communicate adjustments to the audit plan timely” to the A&E Committee;<sup>2014</sup> the responsibility to “[c]omplete the audit plan, as approved, including as appropriate any special tasks or projects” requested by management and the A&E Committee;<sup>2015</sup> the responsibility to employ a professional and highly talented audit staff “with the knowledge, skills, expertise, and experience to provide credible and critical challenge

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<sup>2011</sup> OCC Ex. 2087 at 2 (2013); R. Ex. 423 at 2 (2014).

<sup>2012</sup> OCC Ex. 2087 at 2.

<sup>2013</sup> *Id.*

<sup>2014</sup> *Id.*

<sup>2015</sup> *Id.*

regarding management actions and decisions and to meet the requirements of this Charter”;<sup>2016</sup> the responsibility to issue periodic reports to the A&E Committee “summarizing results of audit activities”;<sup>2017</sup> the responsibility to keep the A&E Committee “informed of emerging trends and successful practices in internal auditing”;<sup>2018</sup> the responsibility to provide “significant measurement goals and results” to the A&E Committee;<sup>2019</sup> the responsibility to “[c]oordinate with and provide oversight of other control and monitoring functions (risk management, compliance, security, legal, ethics, environmental, external audit)”;<sup>2020</sup> the responsibility to “[c]onsider the scope of work of the external auditors and regulators, as appropriate, for the purpose of providing optimal audit coverage to the organization at a reasonable overall cost”;<sup>2021</sup> Under the WFAS Audit Charter, Mr. McLinko and the staff of the CBO also had the same responsibility.<sup>2022</sup>

Under the WFAS Charter, Mr. Julian (at the enterprise level) and Mr. McLinko (for the Community Bank) had the authority to leverage control and monitoring efforts when appropriate.

Despite the requirement that audit perform independently of the risk-management activities of the Bank’s lines of business,<sup>2023</sup> Mr. Julian testified that to the extent those control activities were being performed by the first and second lines of defense appropriately and reasonably, then there were opportunities for Audit to “leverage” – piggy-back off – that work.<sup>2024</sup> In such cases, Audit under Mr. Julian would not necessarily have WFAS perform the same kind of work that these control functions in the first or second lines of defense were doing – he and Mr. McLinko would defer to the work being done under the direction of the first line of defense – Ms. Tolstedt, and by Group Risk Officer Ms. Russ Anderson, without exercising credible challenge as the Bank’s third line of defense.<sup>2025</sup>

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<sup>2016</sup> OCC Ex. 2087 at 2.

<sup>2017</sup> *Id.*

<sup>2018</sup> *Id.*

<sup>2019</sup> *Id.*

<sup>2020</sup> *Id.*

<sup>2021</sup> *Id.*

<sup>2022</sup> *Id.*

<sup>2023</sup> See, *Id.* at 3.

<sup>2024</sup> Tr. (Julian) at 6051; see also “22-03-07 Respondents’ Amended Revised Errata Days 9 -38” at page 42. Ordered through Second Supplemental Order Regarding Hearing Transcript Errata.

<sup>2025</sup> Tr. (Julian) at 6051; see also “22-03-07 Respondents’ Amended Revised Errata Days 9 -38” at page 42. Ordered through Second Supplemental Order Regarding Hearing Transcript Errata.

Mr. Julian opined that this authority also permitted WFAS, Mr. McLinko, and the CBO auditors to leverage – and thus not independently perform – work that was being done, or would be done in the future, by the OCC.<sup>2026</sup>

Under the WFAS Charter, the Chief Auditor “shall be accountable to the Management Committee and the Audit & Examination committee” with the responsibility to “[l]everage other control and monitoring functions’ efforts when appropriate.”<sup>2027</sup> Under the WFAS Audit Charter, Mr. McLinko and the staff of the CBO also had the same responsibility.<sup>2028</sup>

Mr. Julian testified that he understood this accountability in these terms:

An organization the size of Wells Fargo, again, the concept of Three Lines of Defense is that risk is being managed within the First and the Second Line. And by "being managed," there's a number of control activities that are going on within the First and Second Line of Defense. And to the extent those control activities were being performed, in Audit's view, "appropriately and reasonably," then there were opportunities for audit to leverage that work and, therefore, not necessarily go in -- go in and perform the same kind of work that these control functions in the first or second line were doing. That's true also with the OCC, as I mentioned before, to the extent that we could leverage work that they had done or were going to do.<sup>2029</sup>

Under the WFAS Charter, Mr. McLinko and the CBO “shall be accountable to the Management Committee and the Audit & Examination committee” with the responsibility to “[e]nsure effective corrective actions are taken to strengthen reported control weaknesses or uncontrolled risks”;<sup>2030</sup> the responsibility to “[a]ssist in the investigation of significant suspected fraudulent activities within the organization” and notify management and the A&E Committee of the results.<sup>2031</sup>

Under the WFAS Charter, Mr. Julian (at the enterprise level) and Mr. McLinko (for Community Banking) both had the responsibility to ensure effective corrective actions were timely taken to strengthen reported control weaknesses or uncontrolled risks. Both also were required to assist in the investigation of significant suspected fraudulent activities within the organization.<sup>2032</sup> Sales practices misconduct by Community Bank team members included

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<sup>2026</sup> Tr. (Julian) at 6051; see also “22-03-07 Respondents’ Amended Revised Errata Days 9 -38” at page 42. Ordered through Second Supplemental Order Regarding Hearing Transcript Errata.

<sup>2027</sup> OCC Ex. 2087 at 2.

<sup>2028</sup> *Id.*

<sup>2029</sup> Tr. (Julian) at 6051; see also “22-03-07 Respondents’ Amended Revised Errata Days 9 -38” at page 42. Ordered through Second Supplemental Order Regarding Hearing Transcript Errata.

<sup>2030</sup> OCC Ex. 2087 at 2 (2013); R. Ex. 423 at 2 (2014).

<sup>2031</sup> OCC Ex. 2087 at 2.

<sup>2032</sup> *Id.*

fraudulent activity and indicated both weaknesses in risk management controls and the presence of uncontrolled risks related to such misconduct.

Under the WFAS Charter, Mr. McLinko “shall be accountable to the Management Committee and the Audit & Examination committee” with the responsibility to “[e]mploy a Quality Assurance and Improvement Plan that covers all aspects of the internal audit activity and continuously monitors its effectiveness.”<sup>2033</sup>

In furtherance of these responsibilities, the WFAS Audit Charter expressly permitted Mr. McLinko and the CBO team to have “unrestricted access to all functions, records, property, and personnel.”<sup>2034</sup>

Mr. Julian testified that this provision meant that “[i]n the course about its work, to the extent Audit deemed it necessary to have access to certain information to execute its work, Audit had the authority to ask for and receive that information.”<sup>2035</sup>

While WFAS auditors were not authorized to perform any operational duties for the organization or its affiliates, this limitation did not apply to operational duties performed by Corporate Security (later Corporate Investigations).<sup>2036</sup> In addition, while not authorized to direct the activities of any organization employee not employed by the internal auditing department, Mr. Julian, Mr. McLinko and their respective staff members were expressly authorized to direct such employees who have been appropriately assigned to auditing teams or to otherwise assist the internal auditors.<sup>2037</sup>

In furtherance of these responsibilities, the WFAS Audit Charter expressly permitted Mr. McLinko to have “full and free access” to the A&E Committee.<sup>2038</sup>

In furtherance of these responsibilities, the WFAS Audit Charter expressly permitted Mr. McLinko to “[a]llocate resources, set frequencies, select subjects, determine scopes of work, and apply the techniques required to accomplish audit objectives.”<sup>2039</sup>

In furtherance of these responsibilities, the WFAS Audit Charter expressly permitted Mr. McLinko to obtain “the assistance of personnel in units of the organization where internal audit performs audits, as well as other specialized services from within or outside the organization, to accomplish audit objectives”.<sup>2040</sup>

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<sup>2033</sup> OCC Ex. 2087 at 2.

<sup>2034</sup> *Id.* at 3.

<sup>2035</sup> Tr. (Julian) at 6052.

<sup>2036</sup> OCC Ex. 2087 at 2.

<sup>2037</sup> *Id.* at 2-3.

<sup>2038</sup> *Id.* at 3.

<sup>2039</sup> *Id.*

<sup>2040</sup> *Id.*

In furtherance of these responsibilities, the WFAS Audit Charter expressly did not authorize Mr. McLinko to [p]erform “any operational duties for the organization or its affiliates,” except for Corporate Security.<sup>2041</sup>

Mr. Julian testified that he understood this provision to not authorize Internal Audit “to perform operational activities to manage risk, to implement risks, to perform any type of operational activities with respect to the businesses.”<sup>2042</sup> The purpose of this provision, Mr. Julian stated, “was to assure that Audit maintained its independence and objectivity with respect to professional standards.”<sup>2043</sup>

### **Community Bank Senior Leadership Knew the Unlawful and Unethical Misconduct was Widespread and that Sales Goals and Pressure Were the Root Cause**

Beginning as early as 2002, when a group of employees was fired from a branch in Fort Collins, Colorado, for sales gaming, Community Bank senior leadership became aware that employees were engaged in unlawful and unethical sales practices, that gaming conduct was increasing over time, and that these practices were the result of onerous sales goals and management pressure to meet those sales goals.<sup>2044</sup>

That information was reported to Community Bank senior leadership by multiple channels.<sup>2045</sup> Those channels included Wells Fargo’s internal investigations unit, the Community Bank’s own internal sales quality oversight unit, and managers leading the Community Bank’s geographic regions, as well as regular complaints by lower-level employees and Wells Fargo customers reporting serious sales practices violations.<sup>2046</sup>

For example, in 2005 a corporate investigations manager described the problem as “spiraling out of control.”<sup>2047</sup> This reporting continued through 2016, and generally emphasized increases in various forms of sales practices misconduct.<sup>2048</sup> By 2012, certain of the RBEs and their direct reports, Regional Presidents, were regularly raising objections about the sales plans.<sup>2049</sup>

These objections included objections regarding the levels at which the plans were set, the types and categories of products for which they incented sales, the accompanying pressure, the resulting no- or low-value accounts, and unlawful and unethical sales practices at the Community

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<sup>2041</sup> OCC Ex. 2087 at 3.

<sup>2042</sup> Tr. (Julian) at 6053.

<sup>2043</sup> Tr. (Julian) at 6053.

<sup>2044</sup> EC MSD Ex. 1, Ex. A at ¶19.

<sup>2045</sup> *Id.* at ¶20.

<sup>2046</sup> *Id.*

<sup>2047</sup> *Id.*

<sup>2048</sup> *Id.*

<sup>2049</sup> *Id.* at ¶21.



Bank.<sup>2050</sup> These complaints specifically articulated that the sales goals were too high and incited Community Bank employees to sell a significant number of low quality or valueless duplicate products, sometimes through misconduct.<sup>2051</sup> Similar complaints continued to be made until 2016.<sup>2052</sup>

In November 2013, a member of the senior staff wrote, “I really question the value of adding growth to secondary checking in regions that have very high rates to begin with. Based on what we know about the quality of those accounts it seems like we would want to keep their secondary DDA flat or down . . . .”<sup>2053</sup> A year earlier, another senior staff member suggested eliminating any incentive payments tied to accounts that never funded, debit cards that were never used, and more than one demand deposit account per customer per day.<sup>2054</sup>

### **Community Bank Senior Leadership Exacerbated the Sales Practices Problem and Concealed Material Facts**

Even though Community Bank employees often did not meet the sales goals—or met them by selling products and accounts customers neither wanted nor needed—Community Bank senior leadership increased the sales plans nearly every year through 2013.<sup>2055</sup> Pressure to meet those ever-increasing plans also increased during this time period.<sup>2056</sup>

Even after 2012, when Wells Fargo began regularly retroactively lowering goals during the sales year in recognition that the goals were unachievable, employees still largely missed the lowered goals, an indication that they continued to be too high.<sup>2057</sup> Despite knowledge of the widespread sales practices problems, including the pervasive illegal and unethical conduct tied to the sales goals, Community Bank senior leadership failed to take sufficient action to prevent and reduce the incidence of unlawful and unethical sales practices.<sup>2058</sup>

Certain Community Bank leaders also impeded scrutiny of sales practices by Wells Fargo’s primary regulator, the Office of the Comptroller of Currency (“OCC”).<sup>2059</sup> During OCC examinations in February and May 2015, the OCC was given information that minimized the

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<sup>2050</sup> *Id.*

<sup>2051</sup> *Id.*

<sup>2052</sup> *Id.*

<sup>2053</sup> *Id.* at ¶22.

<sup>2054</sup> *Id.*

<sup>2055</sup> *Id.* at ¶24.

<sup>2056</sup> *Id.*

<sup>2057</sup> *Id.*

<sup>2058</sup> *Id.* at ¶25.

<sup>2059</sup> *Id.* at ¶27.

amount of sales pressure within the Community Bank and the size and scope of Wells Fargo's sales practices problem.<sup>2060</sup>

On numerous occasions, Community Bank senior leadership also made statements and gave assurances to the Company's management and Board of Directors that minimized the scope of the sales practices problem and led key gatekeepers to believe the root cause of the issue was individual misconduct rather than the sales model itself.<sup>2061</sup> Until approximately 2015, Community Bank senior leadership viewed negative sales quality and integrity as a necessary byproduct of the increased sales and as merely the cost of doing business.<sup>2062</sup> They nonetheless failed to advise key gatekeepers of the significant risks that the nonneeds-based selling posed to the Company.<sup>2063</sup>

### **Scope of the Unlawful and Unethical Misconduct**

Between 2011 and 2016, tens of thousands of employees were the subject of allegations of unethical sales practices.<sup>2064</sup> During this period, the Company referred more than 23,000 employees for sales practices investigation and terminated over 5,300 employees for customer-facing sales ethics violations, including, in many cases, for falsifying bank records.<sup>2065</sup> Thousands of additional employees received disciplinary action short of termination or resigned prior to the conclusion of the Company's investigations into their sales practices.<sup>2066</sup>

Almost all of the terminations and resignations were of Community Bank employees at the branch level, rather than managers outside of the branches or senior leadership within the Community Bank.<sup>2067</sup> From 2002 to 2016, Wells Fargo opened millions of accounts or financial products that were unauthorized or fraudulent.<sup>2068</sup> During that same time period, Wells Fargo employees also opened significant numbers of additional unneeded, unwanted, or otherwise low value products that were not consistent with Wells Fargo's purported needs-based selling model.<sup>2069</sup>

Wells Fargo collected millions of dollars in fees and interest to which the Company was not entitled, harmed the credit ratings of certain customers, and unlawfully misused customers'

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<sup>2060</sup> *Id.* at ¶27.

<sup>2061</sup> *Id.* at ¶28.

<sup>2062</sup> *Id.*

<sup>2063</sup> *Id.*

<sup>2064</sup> *Id.* at ¶30.

<sup>2065</sup> *Id.*

<sup>2066</sup> *Id.*

<sup>2067</sup> *Id.* at ¶31.

<sup>2068</sup> *Id.* at ¶32.

<sup>2069</sup> *Id.*

sensitive personal information (including customers' means of identification).<sup>2070</sup> In general, the unauthorized, fraudulent, unneeded, and unwanted accounts were created as a result of the Community Bank's systemic sales pressure and excessive sales goals.<sup>2071</sup>

### **Impact of Sales Practices Misconduct on Cross-Sell Disclosures**

Accounts and financial products opened without customer consent or pursuant to gaming practices were included by the Company in the Community Bank cross-sell metric until such accounts were eventually closed for lack of use.<sup>2072</sup> When Community Bank senior leadership set employee sales goals at a level to achieve year-over-year sales growth, it rarely took into consideration that the base level of sales included accounts or financial products resulting from unlawful misconduct or gaming.<sup>2073</sup> This had the effect of imposing additional pressure on employees to continue gaming practices.<sup>2074</sup>

Like the accounts and financial products lacking customer consent, accounts and financial products that were never or seldom used by customers were also included by the Company in the Community Bank cross-sell metric until such accounts were eventually closed for lack of use, at which time those accounts were removed from the cross-sell metric.<sup>2075</sup> In some cases (like checking or savings accounts), the unused accounts were closed relatively quickly (usually within 90 days if unfunded), but in other cases (like debit cards, the largest product category included in the cross-sell metric, or bill pay, another large contributor to cross-sell), the unused accounts remained open without activity for up to four years.<sup>2076</sup>

From 2012 to 2016, Wells Fargo failed to disclose to investors that the Community Bank's sales model had caused widespread unlawful and unethical sales practices misconduct that was at odds with its investor disclosures regarding needs-based selling and that the publicly reported cross-sell metric included significant numbers of unused or unauthorized accounts.<sup>2077</sup>

By the end of 2013, the cross-sell metric had grown by .11 since the prior year.<sup>2078</sup> However, .04 of that growth resulted from the addition of global remittance, and the remaining growth was attributable to an increase in accounts and financial products that had been inactive

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<sup>2070</sup> *Id.*

<sup>2071</sup> *Id.*

<sup>2072</sup> *Id.* at ¶33.

<sup>2073</sup> *Id.*

<sup>2074</sup> *Id.*

<sup>2075</sup> *Id.* at ¶34.

<sup>2076</sup> *Id.*

<sup>2077</sup> *Id.* at ¶35.

<sup>2078</sup> *Id.* at ¶36.

for at least 365 days.<sup>2079</sup> Nonetheless, WFC's FY 2013 Form 10-K, filed February 2014, touted that the Community Bank had achieved record cross-sell over the prior year.<sup>2080</sup>

Nonetheless, despite the addition of a new product, by late 2013 and early 2014, quarter-over-quarter growth in the cross-sell metric had flattened, significantly because of a slowdown in sales growth as a result of, among other things, the Community Bank's belated efforts to impose increased controls to curb misconduct resulting from aggressive sales goals.<sup>2081</sup>

Community Bank executives knew that the metric included many products that were not used by customers. Wells Fargo's inclusion of the word "used" to describe the accounts was therefore misleading.<sup>2082</sup> Several months after changing its disclosure that described how the cross-sell metric was calculated to characterize the metric as "products used," Community Bank senior leadership began to develop an alternative metric to capture products that had been used.<sup>2083</sup> The Community Bank referred to this metric internally as "active cross-sell."<sup>2084</sup>

In developing the active cross-sell metric, Community Bank senior leadership recognized that as many as ten percent of accounts included in the cross-sell metric had not been used within the previous 12 months.<sup>2085</sup> The Community Bank considered releasing this alternative metric to investors, but never did so, in part because of concerns raised that its release would cause investors to ask questions about Wells Fargo's historical sales practices.<sup>2086</sup>

Following the Company's announcement of the September 2016 settlements with the OCC, the Consumer Financial Protection Bureau, and the City of Los Angeles that confirmed publicly for the first time the scale of the sales practices misconduct within the Community Bank, as well as the widespread media and political criticism of the Company that resulted, Wells Fargo's stock experienced three significant stock drops that translated into an approximately \$7.8 billion decrease in market capitalization.<sup>2087</sup>

### **Bank Examiner Analyses**

Pursuant to the OCC's Uniform Rules of Practice and Procedure, if the contents of a report of examination or reports of supervisory activity or visitation contain relevant, material,

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<sup>2079</sup> *Id.* at ¶36.

<sup>2080</sup> *Id.*

<sup>2081</sup> *Id.* at ¶37.

<sup>2082</sup> *Id.* at ¶40.

<sup>2083</sup> *Id.* at ¶41.

<sup>2084</sup> *Id.*

<sup>2085</sup> *Id.*

<sup>2086</sup> *Id.*

<sup>2087</sup> *Id.* at ¶42.

and reliable evidence that is not unduly repetitive, the evidence is admissible to the fullest extent authorized by the Administrative Procedure Act and other applicable law.<sup>2088</sup>

National Bank Examiner for the OCC Elizabeth Candy became the Corporate Risk Team Lead on the OCC's Wells Fargo supervision team in March 2018 and continues to serve in this role.<sup>2089</sup> As the Corporate Risk Team Lead, she was and is responsible for planning, coordinating, and monitoring supervisory activities, and leading examinations and reviews of the Bank.<sup>2090</sup> She drafts and reviews reports of examinations, Supervisory Letters, and Conclusion Memos and oversees the preparation of such documents by other team members.<sup>2091</sup> She also drafts and reviews progress reports for Enforcement Actions and Matters Requiring Attention (MRAs).<sup>2092</sup>

Her job involves assessing the adequacy of those Bank functions and establishing the OCC's supervision strategy for those areas.<sup>2093</sup> She is also responsible for evaluating the adequacy of, and safety and soundness of, risk management and corporate governance functions, including the role of the Bank's Board of Directors, management committee structure, and policies and procedures.<sup>2094</sup> She also identifies and evaluates systemic risks and trends, analyze data and reporting, and participates in discussions with bank management throughout the OCC's supervisory activities.<sup>2095</sup>

She assumed responsibility as the Acting Enterprise Risk Management Team Lead on August 16, 2020. In this role, she assesses the adequacy of Bank management and the Board.<sup>2096</sup> Her responsibilities include evaluating the following areas of the Bank: enterprise risk management, audit, internal controls, incentive compensation, legal, and human resources.<sup>2097</sup> She oversees an examination team in Large Bank Supervision focused on various risk areas and serves as an advisor to the Examiner-in-Charge and other OCC officials.<sup>2098</sup> She provides analysis and advice on the planning and conduct of examinations and reviews, preparation of reports of examination and Supervisory Letters, and presentations of findings and

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<sup>2088</sup> 12 C.F.R. § 19.36.

<sup>2089</sup> EC MSD Ex. 269 (Report of NBE Candy) at ¶10.

<sup>2090</sup> *Id.*

<sup>2091</sup> *Id.* at ¶11.

<sup>2092</sup> *Id.* at ¶10.

<sup>2093</sup> *Id.*

<sup>2094</sup> *Id.*

<sup>2095</sup> *Id.*

<sup>2096</sup> *Id.* at ¶11.

<sup>2097</sup> *Id.*

<sup>2098</sup> *Id.*

recommendations to senior management at the Bank and the OCC.<sup>2099</sup> She meets with and communicates regularly with senior Bank management, OCC staff, and other Bank regulators to discuss supervisory conclusions, share information, and resolve concerns.<sup>2100</sup>

Examiner Candy has twelve years of professional examiner experience at the OCC, including extensive experience in the supervision of community, midsize, and large banks, problem banks, application of safety and soundness principles to bank operations, corporate governance, risk management, and controls.<sup>2101</sup> She joined the OCC in 2008, was an examiner in Midsize and Community Bank Supervision with the OCC for six years, from June 2008 through April 2014, before transferring to the OCC's Large Bank Supervision.<sup>2102</sup> During her tenure there, she participated in over 100 midsize and community bank examinations, as well as examinations of large banks, including Wells Fargo.

In her positions with Midsize and Community Bank Supervision at the OCC, Examiner Candy served as both Acting Examiner-in-Charge and Examiner-in-Charge for multiple problem banks with significant control, compliance, Bank and Secrecy Act ("BSA"), asset quality, and management deficiencies. These were banks with a composite rating of "3" or worse under the Uniform Financial Institutions Rating System of the Federal Financial Institutions Examination Council.<sup>2103</sup>

Examiner Candy reported that she holds the following opinions as a National Bank Examiner.<sup>2104</sup>

From no later than 2002 until October 2016, the Community Bank pursued a business model premised on unreasonable sales goals coupled with extreme pressure on its employees to meet these goals.<sup>2105</sup> Leadership focused on increasing the cross-sell ratio year over year at all cost, instead of ensuring that Wells Fargo customers received only the products they wanted, needed, and requested.<sup>2106</sup> The pressure included the threat of disciplinary action and termination as well as actual termination for failure to meet the unreasonable goals and contributed to hostile working conditions with managers sometimes embarrassing employees or forcing them to work overtime.<sup>2107</sup>

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<sup>2099</sup> EC MSD Ex. 269 (Report of NBE Candy) at ¶11.

<sup>2100</sup> *Id.*

<sup>2101</sup> *Id.* at ¶3.

<sup>2102</sup> *Id.*

<sup>2103</sup> *Id.*

<sup>2104</sup> EC MSD Ex. 269 (Report of NBE Candy) at page 6.

<sup>2105</sup> *Id.* at ¶16.

<sup>2106</sup> *Id.*

<sup>2107</sup> *Id.*

In addition, the Community Bank's controls were severely deficient and intentionally so.<sup>2108</sup> This business model was recklessly unsafe or unsound and resulted in a severe and systemic sales practices misconduct problem.<sup>2109</sup> (The term "sales practices misconduct," as used in her report, refers to the practices of Bank employees issuing a product or service to a customer without the customer's consent, transferring customer funds without the customer's consent, or obtaining a customer's consent by making false or misleading representations.)<sup>2110</sup>

Sales practices misconduct, or issuing products to customers without their consent or obtaining the customer's consent by making false or misleading representations, is an unsafe or unsound banking practice and violates laws and regulations. Those laws and regulations include: 18 U.S.C. §§ 656 (theft/misapplication by bank employee), 1005 (false entries), 1028(a)(7) (identity theft), and 1344(2) (bank fraud); 15 U.S.C. § 45(a) (unfair or deceptive acts and practices); 12 C.F.R. § 1030.4(a) (Regulation DD/Truth in Savings); and 12 C.F.R. § 1026.12(a) (Regulation Z/Truth in Lending).<sup>2111</sup>

The incentive compensation program and plans in the Community Bank were deficient in both design and implementation, as well as testing, oversight, and challenge, and resulted in employees engaging in sales practices misconduct over the course of fourteen years. This was recklessly unsafe or unsound and exposed the Bank to increased operational, compliance, regulatory, legal, reputational and financial risks.<sup>2112</sup>

The Bank's controls to prevent and detect sales practices misconduct were inadequate and the Bank's risk management of its sales practices and the sales practices themselves, were recklessly unsafe or unsound.<sup>2113</sup>

Sales practices misconduct was pervasive in the Community Bank and involved tens of thousands, if not hundreds of thousands, of Bank employees issuing millions of products to customers without their consent.<sup>2114</sup>

It took a massive and prolonged failure by Respondents for the sales practices misconduct problem to become as severe and pervasive as it was and last as long as it did.<sup>2115</sup> The Respondents knew, or should have known, that sales practices misconduct in the

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<sup>2108</sup> EC MSD Ex. 269 (Report of NBE Candy) at ¶16.

<sup>2109</sup> *Id.*

<sup>2110</sup> *Id.* at ¶16 (a).

<sup>2111</sup> *Id.* at ¶17.

<sup>2112</sup> *Id.* at ¶18.

<sup>2113</sup> *Id.* at ¶19.

<sup>2114</sup> *Id.* at ¶20.

<sup>2115</sup> *Id.* at ¶21.

Community Bank was widespread, systemic, and the high-pressure environment and aggressive sales goals contributed to the root cause.<sup>2116</sup>

In 2014, National Bank Examiner Jennifer Crosthwaite participated in a number of examinations related to Incentive Compensation, Compliance, and Operational Risk and issued Supervisory Letters highlighting issues in each area.<sup>2117</sup> In February 2015, she and the Operations and Compliance Team Leads examined the Community Bank’s governance processes with a focus on sales practices.<sup>2118</sup> The result of the February 2015 examination was an April 2015 Supervisory Letter including an MRA on sales practices governance.<sup>2119</sup>

During the February 2015 exam, Examiner Crosthwaite was told that only 20 or 30 people had been terminated in connection with an investigation that was limited geographically to Los Angeles/Orange County.<sup>2120</sup> After the City of Los Angeles filed its lawsuit against the Bank for sales practices related misconduct in May 2015, she led a targeted examination of the Community Bank specifically related to the allegations in the lawsuit.<sup>2121</sup>

In conjunction with the examiners from the Operations and Compliance group, the ERM examiners examined the Community Bank, sampled a number of EthicsLine and customer complaints, and reviewed termination files and notes.<sup>2122</sup> It was during this period that she learned, for the first time, that over 230 individuals had been terminated across the Bank (not just in Los Angeles/Orange County) for engaging in simulated funding and changing customer phone numbers.<sup>2123</sup> This 230 number was drastically higher than what the Bank had previously reported to the OCC during the February 2015 exam.<sup>2124</sup> She then realized that the sales practices problem

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<sup>2116</sup> EC MSD Ex. 269 (Report of NBE Candy) at ¶21.

<sup>2117</sup> EC MSD Ex. 268 (Report of NBE Crosthwaite) at ¶9. Examiner Crosthwaite has been the Enterprise Risk Management Team Lead for Wells Fargo since May 2013. In that role, she directs a team of between eight and ten OCC examiners and oversee supervisory efforts at Wells Fargo in the areas of Corporate Risk, Audit, Legal, Human Resources, Reputation Risk, Strategic Risk, Model Risk, Counterparty Credit Risk, and International Risk. Among other things, she regularly meets with Bank senior management to cover key current topics, emerging risks, and issues identified through the OCC’s ongoing examination work, and provides clear and detailed feedback to the Bank in the form of Supervisory Letters. She also assists the Examiner-In-Charge in providing input into the Quarterly Management Report, the annual Report of Exam (“ROE”), the Quarterly Risk Assessments, and the supervisory strategies of the Bank. She serves as an expert advisor for the field examining staff of Large Bank Supervision (“LBS”) and as an advisor to the Examiner-in-Charge (“EIC”), the Deputy Comptroller for LBS, and other OCC officials. She participated in the OCC’s examinations and investigations of the Bank’s sales practices. Id. at ¶2.

<sup>2118</sup> EC MSD Ex. 268 (Report of NBE Crosthwaite) at ¶9.

<sup>2119</sup> *Id.*

<sup>2120</sup> *Id.* at ¶10.

<sup>2121</sup> *Id.*

<sup>2122</sup> *Id.*

<sup>2123</sup> *Id.*

<sup>2124</sup> *Id.*



was more severe and pervasive than what management, including Respondents, had communicated to the OCC.<sup>2125</sup> She learned that sales practices was much more than just simulated funding and phone number changes.<sup>2126</sup>

Some examples of other types of sales practices misconduct that the OCC’s examiners discovered were: opening unauthorized deposit accounts (and in some instances 40 or 50 accounts for one individual), issuing multiple credit and debit cards without consent, and targeting the deceptive practices on protected classes.<sup>2127</sup>

Community Bank Management also had a practice of pushing two checking and two savings accounts on customers (known as the “2 for 2” campaign).<sup>2128</sup> Examiners reviewed over 300 EthicsLine complaints and a sizeable number of customer complaints, which provided detailed accounts of pervasive unsafe or unsound and fraudulent sales practices misconduct.<sup>2129</sup> The Bank’s EthicsLine is a 24-hour hotline and website program that serves as the primary method for employees to anonymously voice complaints, including reporting possible violations of the Bank’s Code of Ethics, violations of law, and suspicious conduct involving other employees.<sup>2130</sup>

The examination resulted in a Supervisory Letter with five MRAs that addressed the three lines of defense (the Community Bank, Corporate Risk, and Internal Audit), incentive compensation, and complaint systems.<sup>2131</sup> The Supervisory Letter highlighted the aggressive sales culture and lack of effective Bank oversight, controls, and supervision.<sup>2132</sup> It also highlighted that there was a lack of transparency in the front-line Community Bank leadership team.<sup>2133</sup> This Supervisory Letter required the Bank to assess root cause and hire an independent consultant to assess customer harm. The Bank retained Accenture and PricewaterhouseCoopers (“PwC”) for this work, respectively.<sup>2134</sup>

Throughout the targeted examination in May 2015, the EIC and Examiner Crosthwaite informed the Bank’s Chief Corporate Risk Officer that the OCC did not want Respondent Russ Anderson taking the lead on providing information to the OCC.<sup>2135</sup> The EIC and Examiner

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<sup>2125</sup> *Id.*

<sup>2126</sup> *Id.*

<sup>2127</sup> *Id.*

<sup>2128</sup> *Id.*

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<sup>2130</sup> *Id.*

<sup>2131</sup> *Id.*

<sup>2132</sup> *Id.*

<sup>2133</sup> *Id.*

<sup>2134</sup> *Id.*

<sup>2135</sup> *Id.* at ¶11.

Crosthwaite requested that the independent Corporate Risk function of the Bank take the lead on coordinating responses to OCC information requests, on scheduling meetings, and on ensuring that the OCC received all such requested information.<sup>2136</sup> They made this request because the information that the Community Bank had provided to the OCC previously was not consistent with the information in the City of Los Angeles lawsuit.<sup>2137</sup> At this time, based upon Examiner Crosthwaite’s interactions throughout early 2015, she was very concerned that Community Bank leadership, and specifically Respondent Russ Anderson, was not fully transparent in meetings with OCC examiners.<sup>2138</sup>

In July 2015, the OCC commented on sales practices in its annual Report of Examination (“ROE”),

The Bank needs to proactively control reputational risks through more effective compliance and operational risk programs. This included a reference to our continued assessment of the LA lawsuit, which alleges branch misconduct resulting in customer harm, our early findings suggest management should have responded more proactively to independently investigate the initial allegations. Management needs to ensure that matters such as these are fully and transparently investigated, harmed customers are remediated, bank employees are properly trained, incentive programs do not encourage the alleged behavior, and controls are in place to identify and resolve potential or emerging issues.<sup>2139</sup>

In February 2016, the OCC received the results of the PricewaterhouseCoopers (PwC) report, which confirmed that sales practices misconduct was occurring on systemic scale and affected more than 1.5 million customer accounts.<sup>2140</sup> The PwC report, combined with the Accenture findings, confirmed the systemic nature of sales practices misconduct.<sup>2141</sup>

The OCC issued a Supervisory Letter in July 2016, finding that the sales practices misconduct problem at Wells Fargo was unsafe or unsound.<sup>2142</sup> The July 2016 Supervisory Letter ultimately supported the Sales Practices Consent Order issued against the Bank in September 2016.<sup>2143</sup> By August 2017, the number of accounts that had been opened between January 2009

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<sup>2136</sup> EC MSD Ex. 268 (Report of NBE Crosthwaite) at ¶11.

<sup>2137</sup> *Id.*

<sup>2138</sup> *Id.*

<sup>2139</sup> *Id.* at ¶12.

<sup>2140</sup> *Id.* at ¶13.

<sup>2141</sup> *Id.*

<sup>2142</sup> *Id.*

<sup>2143</sup> *Id.*

and September 2016 in a manner consistent with simulated funding had ballooned to 3.5 million customer accounts.<sup>2144</sup>

Examiner Candy opined that through their actions and inactions, each Respondent engaged in recklessly unsafe or unsound practices that enabled the sales practices misconduct problem to exist and continue. Each Respondent also breached his/her fiduciary duties.<sup>2145</sup>

As the Group Risk Officer for the Community Bank, Respondent Russ Anderson had a primary responsibility to properly identify, quantify and control all risks in the Community Bank's operations.<sup>2146</sup> Audit—that is, Respondents Julian and McLinko—had a responsibility to ensure incentive compensation plans were designed and operated in accordance with Bank policy, evaluate risk and controls and ensure it was adequately managed and escalated, advise whether the Community Bank was operating in conformance with laws and regulations, or identify and detail significant or systemic problems in audit reports.<sup>2147</sup> None of the Respondents, each of whom held leadership roles in those departments, adequately performed their responsibilities with respect to the sales practices misconduct problem.<sup>2148</sup> Examiner Candy opined that all three Respondents failed in their responsibilities.<sup>2149</sup>

Examiner Candy opined that Respondent Russ Anderson failed to execute her risk management, control, and escalation responsibilities as the Group Risk Officer, the Chairperson of the Community Bank Risk Management Committee, and under the Bank's own policies;<sup>2150</sup> and that her conduct was recklessly unsafe or unsound and was done in disregard of or evidenced a conscious indifference to a known or obvious risk of substantial harm.<sup>2151</sup> Examiner Candy opined that Respondent Russ Anderson's conduct constituted a breach of her fiduciary duty.<sup>2152</sup>

Examiner Candy opined that Respondent Russ Anderson's failure to escalate the sales practices misconduct problem was recklessly unsafe or unsound and constituted a breach of her fiduciary duty,<sup>2153</sup> and that her false, misleading, and incomplete reporting to the Enterprise Risk Management Committee, the Board, and the OCC was recklessly unsafe or unsound and constituted a breach of her fiduciary duty.<sup>2154</sup>

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<sup>2144</sup> EC MSD Ex. 268 (Report of NBE Crosthwaite) at ¶¶13, 52.

<sup>2145</sup> EC MSD Ex. 269 (Report of NBE Candy) at ¶22.

<sup>2146</sup> *Id.* at ¶23.

<sup>2147</sup> *Id.*

<sup>2148</sup> *Id.*

<sup>2149</sup> *Id.*

<sup>2150</sup> *Id.* at ¶24.

<sup>2151</sup> *Id.*

<sup>2152</sup> *Id.*

<sup>2153</sup> *Id.* at ¶25.

<sup>2154</sup> *Id.* at ¶26.

Examiner Candy opined that Respondent Russ Anderson violated laws and regulations, including by causing, participating in, counseling, or aiding and abetting the following violations: 18 U.S.C. §§ 656 (theft/misapplication by bank employee), 1001(a) (false statements), 1005 (false entries), 1028(a)(7) (identity theft), 1344(2) (bank fraud), and 1517 (obstruction of bank exam); 15 U.S.C. § 45(a) (unfair or deceptive practices); 12 C.F.R. § 1030.4(a) (Regulation DD/Truth in Savings); and 12 C.F.R. § 1026.12(a) (Regulation Z/Truth in Lending).<sup>2155</sup>

Examiner Candy opined that Respondent Russ Anderson's violations of laws and regulations, unsafe or unsound practices, and breaches of fiduciary duties involved personal dishonesty and demonstrated a willful or continuing disregard for the safety or soundness of the Bank.<sup>2156</sup>

### **Respondents Julian and McLinko**

Examiner Candy opined that Respondent Julian and Respondent McLinko each recklessly engaged in an unsafe or unsound practice by failing to plan and manage audit activity within the Community Bank that would detect and document the ongoing sales practices misconduct problem and identify corrective action to remediate and resolve it.<sup>2157</sup> She noted that audits performed under their leadership gave "Effective" ratings to areas touching on sales practices, failed to include appropriate scope or sufficient testing, and this continued to be the case until the elimination of sales goals in the Community Bank.<sup>2158</sup> In Examiner Candy's opinion, this conduct constituted breaches of their fiduciary duties.<sup>2159</sup>

Examiner Candy opined that Respondent Julian recklessly engaged in an unsafe or unsound practice by failing to accurately assess and appropriately incorporate risk events in incentive compensation recommendations for material risk takers and executives at the Bank from 2014 through 2016.<sup>2160</sup>

Examiner Candy opined that each of the Respondents' unsafe or unsound practices were part of a pattern of misconduct, resulted in pecuniary gain or other benefit to each of the Respondents, and caused significant loss to the Bank.<sup>2161</sup> In her opinion, civil money penalties ("CMP") in the amount assessed against each Respondent are appropriate. In her opinion, higher

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<sup>2155</sup> EC MSD Ex. 269 (Report of NBE Candy) at ¶27.

<sup>2156</sup> *Id.* at ¶28.

<sup>2157</sup> *Id.* at ¶32.

<sup>2158</sup> *Id.*

<sup>2159</sup> *Id.*

<sup>2160</sup> *Id.* at ¶33.

<sup>2161</sup> *Id.* at ¶34.

CMPs against each Respondent than those presented through the Notice of Charges are consistent with and supported by the evidence.<sup>2162</sup>

### **Incentive Compensation Program in the Community Bank Failed to Balance Risk and Reward**

Examiner Candy participated in the OCC's May 2015 ongoing supervisory activity of the Bank's sales practices that resulted in Supervisory Letter (SL) 2015-36.<sup>2163</sup> The review was prompted by the City of Los Angeles lawsuit filed against Wells Fargo on May 4, 2015. SL 2015-36 specified that the OCC's review focused on the events in 2013 that led to the initial employee terminations for sales practices, the investigation of employee misconduct that followed, and overall changes in governance intended to improve the Bank's practices.<sup>2164</sup> The Operating Committee consisted of the Chief Executive Officer and his direct reports.<sup>2165</sup> SL 2015-36 concluded that the Bank's management and oversight of Enterprise Sales Practices risk was weak and needed to improve.<sup>2166</sup>

SL 2015-36 also concluded that "[t]here also exists only limited monitoring and oversight by the second (Corporate Risk, Human Resources, Compliance, and Legal) and third lines of defense [Audit.]"<sup>2167</sup> SL 2015-36 specifically noted, "Cross-selling, if not properly governed, can lead to excessive sales pressure on employees to meet sales goals and achieve financial incentives. Incentive compensation is a key factor in motivating employee behavior and should be reevaluated across all sales activities enterprise-wide given these events."<sup>2168</sup> SL 2015-36 required the Bank to review compensation programs to protect against incenting inappropriate behavior.<sup>2169</sup>

The OCC uses Matters Requiring Attention (MRAs) to communicate concern about a bank's deficient practices to a bank's board of directors and management.<sup>2170</sup> An MRA is a significant supervisory action and must be taken seriously and addressed by bank management.<sup>2171</sup>

All incentive compensation plans at the Bank, including the Community Bank, were required to comply with the Bank's Incentive Compensation Risk Management Policy ("ICRM

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<sup>2162</sup> EC MSD Ex. 269 (Report of NBE Candy) at ¶35.

<sup>2163</sup> *Id.* at ¶37.

<sup>2164</sup> *Id.*

<sup>2165</sup> *Id.*

<sup>2166</sup> *Id.*

<sup>2167</sup> *Id.*

<sup>2168</sup> *Id.*

<sup>2169</sup> *Id.*

<sup>2170</sup> *Id.* at ¶38.

<sup>2171</sup> *Id.* at ¶41.

Policy”) dated July 13, 2011,<sup>2172</sup> and amended on November 27, 2012.<sup>2173</sup> The ICRM Policy was the primary policy that governs the Bank’s incentive compensation arrangements.<sup>2174</sup>

The Bank’s ICRM Policy “applies to any Wells Fargo business that pays team members under an incentive compensation arrangement. It covers both domestic and international team members in all jurisdictions where Wells Fargo does business.”<sup>2175</sup>

The ICRM Policy states:

The purpose of the Incentive Compensation Risk Management Policy is to help ensure that Wells Fargo’s incentive compensation arrangements are aligned with appropriate risk taking – which is to balance short-term performance goals with the long-term strength and stability of the company.<sup>2176</sup>

The amended ICRM Policy issued on November 28, 2012 states:

Incentive-based compensation arrangements should balance risk and financial rewards in a manner that does not provide our team members with an incentive to take inappropriate risks that could lead to material financial, operational, or reputational risk for the company.<sup>2177</sup>

Generally accepted standards of prudent operation and the Bank’s own ICRM Policy required incentive compensation arrangements to balance risk and reward in a manner that does not encourage team members to expose Wells Fargo to imprudent risks.<sup>2178</sup>

The Wells Fargo Risk Management Framework also emphasized the importance of a sound incentive compensation program.<sup>2179</sup> It states:

Wells Fargo’s incentive-based compensation practices balance risk and financial reward in a manner that incentivizes team members to take appropriate risks they understand and avoid taking risks they do not understand or that exceed risk appetite. To this end, the Incentive Compensation Risk Management (ICRM) program was developed to manage risk in incentive-

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<sup>2172</sup> EC MSD Ex. 269 (Report of NBE Candy) at ¶41, citing Wells Fargo & Co., Incentive Compensation Risk Management Policy (July 13, 2011) (OCC-WF-SP-05434513).

<sup>2173</sup> EC MSD Ex. 269 (Report of NBE Candy) at ¶41, citing Fargo & Co., Incentive Compensation Risk Management Policy (July 13, 2011) (OCC-WF-SP-05434513).

<sup>2174</sup> EC MSD Ex. 269 (Report of NBE Candy) at ¶42.

<sup>2175</sup> *Id.* at ¶43.

<sup>2176</sup> *Id.*

<sup>2177</sup> *Id.*

<sup>2178</sup> *Id.* at ¶44.

<sup>2179</sup> *Id.* at ¶45.

based compensation arrangements throughout Wells Fargo. The ICRM principles and requirements are fundamental and strictly adhered to, guiding both general and tailored compensation practices. The balance of risk and reward is, and always will be, a top priority.<sup>2180</sup>

The Human Resources Committee of the Board received a presentation on the ICRM Policy in February 2012. The presentation stated, “[t]he ICRM Program has been broadened to be the single risk management program for all incentive compensation related matters across the enterprise.”<sup>2181</sup>

After determining Community Bank’s incentive compensation practice did not conform to the Bank’s own ICRM Policy and Fraud Risk Management Framework, Examiner Candy conducted additional review of sales goals.<sup>2182</sup> During this review, she discovered that from 2002 through 2016, the sales goals in the Community Bank were unreasonable.<sup>2183</sup> They were unreasonable in part because they could not be met by reasonable and diligent efforts and incentivized employees to engage in sales practices misconduct—improper, unethical, and illegal activity—to meet them.<sup>2184</sup>

The Community Bank’s sales model was predicated on double-digit annual sales growth over the prior year’s sales performance, a concept known as “run rate.”<sup>2185</sup> The current year’s sales plan served as the baseline for each successive year’s sales goals, and sales goals were increased each year.<sup>2186</sup> So, for example: the Community Bank’s 2012 sales plan derived from the 2011 sales performance, and required team members to sell a greater number of products and services than they had sold in 2011; by extension, the Bank’s 2013 sales plan was derived from the Bank’s 2012 sales performance, which required team members to sell a greater number of products and services than they had sold in 2012.<sup>2187</sup>

However, sales practices misconduct artificially inflated the run rate, making sales goals increasingly unattainable every year.<sup>2188</sup> The Community Bank’s sales run rate was tainted by sales practices misconduct; each year’s sales performance numbers reflected products and

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<sup>2180</sup> EC MSD Ex. 269 (Report of NBE Candy) at ¶45, citing Wells Fargo Bank, N.A., Wells Fargo Risk Management Framework, at 10-11 (July 2014) (OCC-WF-SP-04791987).

<sup>2181</sup> EC MSD Ex. 269 (Report of NBE Candy) at ¶46, citing Wells Fargo Bank, N.A., *Incentive Compensation Risk Management Program 2011 Program Update*, Human Resources Committee, at 2 (Feb. 28, 2012) (OCC-WF-SP-07644598).

<sup>2182</sup> EC MSD Ex. 269 (Report of NBE Candy) at ¶48.

<sup>2183</sup> *Id.*

<sup>2184</sup> *Id.*

<sup>2185</sup> *Id.*

<sup>2186</sup> *Id.*

<sup>2187</sup> *Id.*

<sup>2188</sup> *Id.*

services that were opened for and issued to customers without their knowledge and consent or obtained through false statements and misrepresentations. This made it even harder to achieve the sales goals through legal and ethical means in every subsequent year.<sup>2189</sup>

The Independent Directors of the Board of Wells Fargo & Company, the Bank's holding company, conducted an investigation to understand the root cause of improper sales practices in the Community Bank ("Board Report").<sup>2190</sup> The Board Report explained the run rate as such: "[t]he problem built on itself: attaining growth when the prior year's sales included a large number of low quality accounts meant that even more low quality accounts had to be opened to hit the increased target."<sup>2191</sup>

The Board Report found that the Community Bank's sales goals were "untenable," "unrealistic," and "unattainable."<sup>2192</sup> The Board Report found that, even after the Community Bank made mid-year downward adjustments to sales goals in 2013 and 2014, "they were still set at an unachievable level."<sup>2193</sup> These findings are consistent with Examiner Candy's own conclusions based on her supervisory work and evidence she reviewed during the investigation and litigation.<sup>2194</sup>

In October 2015, Accenture, a firm hired by the Bank in response to MRAs issued by the OCC in June 2015, issued a report.<sup>2195</sup> The report stated, "despite recent reductions in store sales goals," employees "continue to feel pressure to meet sales targets that many team members perceive to be unreasonable, and this may occur at the potential expense of sales quality."

Accenture also observed based on its review that even in 2015, "sales goals have not been met since 2013 (even after accounting for adjustment made throughout the year to improve achievement rates)."<sup>2196</sup> However, even though sales goals were lowered in 2013, sales practices misconduct in the Community Bank continued to be significant (as discussed in this report), employees still could not meet sales goals, further highlighting that they were unreasonable.<sup>2197</sup>

## **The Board of Directors' Sales Practices Investigation Report**

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<sup>2189</sup> EC MSD Ex. 269 (Report of NBE Candy) at ¶48.

<sup>2190</sup> *Id.*, citing Independent Directors of the Board of Wells Fargo & Company, Sales Practices Investigation Report (Apr. 10, 2017), available at <https://www08.wellsfargomedia.com/assets/pdf/about/investor-relations/presentations/2017/board-report.pdf> [hereinafter Board Report].

<sup>2191</sup> EC MSD Ex. 269 (Report of NBE Candy) at ¶48, citing *Board Report* at 41.

<sup>2192</sup> EC MSD Ex. 269 (Report of NBE Candy) at ¶49, citing *Board Report* at 5, 19, 39.

<sup>2193</sup> EC MSD Ex. 269 (Report of NBE Candy) at ¶49, citing *Board Report* at 45.

<sup>2194</sup> EC MSD Ex. 269 (Report of NBE Candy) at ¶49.

<sup>2195</sup> *Id.* at ¶50.

<sup>2196</sup> *Id.*, citing Accenture, *Wells Fargo Sales Practices Assessment – Community Banking Sales Practices Report: Observations and Recommendations* (Oct. 2015) (OCC-SP1140359).

<sup>2197</sup> EC MSD Ex. 269 (Report of NBE Candy) at ¶50.



On April 10, 2017, the Independent Directors of the Board of Wells Fargo issued its Sales Practices Investigation Report (“Board Report”).<sup>2198</sup> Examiner Tanya Smith was the Bank’s Acting Examiner-in-Charge at the time.<sup>2199</sup> The Board Report found that the “root cause of sales practice failures was the distortion of the Community Bank’s sales culture and performance management system, which, when combined with aggressive sales management, created pressure on employees to sell unwanted or unneeded products to customers and, in some cases, to open unauthorized accounts.”<sup>2200</sup> It continued: “the only way definitively to address the broken sales model and the root cause of sales practice abuses was to emphasize other metrics for performance and to abandon exerting pressure through sales goals and sales-driven incentive programs.”<sup>2201</sup>

The Board Report identified deficiencies in the Law Department, Audit, and Community Bank Risk. The Board Report found:

Russ Anderson’s performance fell far short of what was expected and required of the senior risk officer in the Community Bank. Russ Anderson failed to adequately assess and advocate for changes in the business practices

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<sup>2198</sup> EC MSD Ex. 280 (Independent Directors of the Board of Wells Fargo & Company, Sales Practices Investigation Report, dated April 17, 2017).

<sup>2199</sup> Examiner Smith is the current Examiner-in-Charge of Wells Fargo Bank, N.A., Sioux Falls, South Dakota in Large Bank Supervision at the Office of the Comptroller of the Currency. She became Wells Fargo’s Acting Examiner-in-Charge in March 2017 and has served as its permanent Examiner-in-Charge since July 2017. As Wells Fargo’s Examiner-in-Charge, she manages a team of approximately 80 OCC examiners and other employees covering all aspects of the Bank’s daily supervision. Her supervisory responsibilities include establishing regulatory and supervisory expectations on major programs through discussions with the Chief Executive Officer and other senior executives, providing clear feedback on progress against Enforcement Actions and Matters Requiring Attention, evaluating the Bank’s systems and controls to determine the Risk Assessment and CAMELS ratings, preparing the Report of Examination and the annual comprehensive risk assessment (“CORE”), and regularly communicating with the Board about supervisory findings and priorities. Among other things, she is responsible for developing and supporting the supervisory strategy for this large, complex, multinational institution with multiple risk, regulatory, and control deficiencies, including those related to legal, audit, compliance, risk, governance, and sales practices. From March 2017 onwards, she participated in the OCC’s examinations and investigation of the Bank’s sales practices. She has over 27-years of professional experience at the OCC, the Federal Deposit Insurance Corporation (“FDIC”), and the International Monetary Fund (“IMF”), including extensive experience in the supervision of large, complex, multinational banks. EC MSD Ex. 267 (Report of Examiner Smith) at ¶¶1-3.

<sup>2200</sup> EC MSD Ex. 267 (Report of NBE Smith) at ¶51, quoting Independent Directors of the Board of Wells Fargo & Company, Sales Practices Investigation Report, at 8 (Apr. 10, 2017) (“Board Report”), available at <https://www08.wellsfargomedia.com/assets/pdf/about/investorrelations/presentations/2017/board-report.pdf>.

<sup>2201</sup> EC MSD Ex. 267 (Report of NBE Smith) at ¶51, quoting Independent Directors of the Board of Wells Fargo & Company, Sales Practices Investigation Report, at 8 (Apr. 10, 2017) (“Board Report”), available at <https://www08.wellsfargomedia.com/assets/pdf/about/investorrelations/presentations/2017/board-report.pdf>.

that resulted in sales integrity violations. She also did not adequately address customer harm arising from improper sales practices.<sup>2202</sup>

Between 2011 and 2016, Wells Fargo Audit Services (“Audit”) conducted periodic audits that touched on sales practice issues within the Community Bank. These audits generally found that processes and controls designed to detect, investigate and remediate sales practice violations were effective at mitigating sales practice-related risks. In addition to auditing these detective functions, Audit also reviewed the Community Bank’s compensation plans and found that their design did not promote unethical behavior.<sup>2203</sup>

Notwithstanding the growing awareness of the reputational risk associated with mass terminations, and the fact that many of these incidents involved unauthorized products or accounts, the perception persisted in the Law Department that sales integrity issues involved ‘gaming’ the Community Bank’s incentive programs and not conduct affecting customers. That led them to underestimate the need to escalate and more directly manage sales integrity issues.<sup>2204</sup>

Respondent Julian was a member of the Operating Committee at the time the Board Report was issued and had the opportunity to review and correct any factual errors in the report prior to its issuance.<sup>2205</sup> Examiner Smith interacted with Respondent Julian at the time of the Board Report’s issuance, asked him for his feedback on the Board Report, and does not recall him expressing *any* concerns about the accuracy of the report or any disagreement with any of its findings or conclusions.<sup>2206</sup>

Examiner Smith opined that Respondents’ current assertion that the Bank fabricated or exaggerated its sales practices problem in the Board Report is implausible on its face.<sup>2207</sup> In her 27 years of professional experience as a bank examiner, Examiner Smith has never observed or

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<sup>2202</sup> Independent Directors of the Board of Wells Fargo & Company, Sales Practices Investigation Report, at 8 (Apr. 10, 2017) (“Board Report”), available at <https://www08.wellsfargomedia.com/assets/pdf/about/investorrelations/presentations/2017/board-report.pdf> at 49.

<sup>2203</sup> Independent Directors of the Board of Wells Fargo & Company, Sales Practices Investigation Report, at 8 (Apr. 10, 2017) (“Board Report”), available at <https://www08.wellsfargomedia.com/assets/pdf/about/investorrelations/presentations/2017/board-report.pdf> at 91.

<sup>2204</sup> EC MSD Ex. 267 (Report of NBE Smith) at ¶52, quoting Independent Directors of the Board of Wells Fargo & Company, Sales Practices Investigation Report, at 8 (Apr. 10, 2017) (“Board Report”), available at <https://www08.wellsfargomedia.com/assets/pdf/about/investorrelations/presentations/2017/board-report.pdf> at 75.

<sup>2205</sup> EC MSD Ex. 267 (Report of NBE Smith) at ¶53.

<sup>2206</sup> *Id.*

<sup>2207</sup> *Id.* at ¶54.

even heard of any board exaggerating a significant problem to the extreme detriment to the institution.<sup>2208</sup>

In addition, in this instance the Board engaged outside counsel to independently look at the facts and circumstances that form the basis of the final report.<sup>2209</sup> Examiner Smith's team reviewed a number of documents and interview notes that the outside counsel gathered as part of the Board investigation and found the work and the conclusions to be credible, comprehensive, and not exaggerated.<sup>2210</sup> Examiner Smith reported that the OCC's examination work and the subsequent investigation revealed that the sales practices misconduct problem was even worse than what was detailed in the Board Report.<sup>2211</sup>

On February 21, 2020, the Bank agreed to pay \$3 billion to resolve criminal and civil investigations with the Department of Justice and the Securities and Exchange Commission into sales practices "involving the opening of millions of accounts without customer authorization."<sup>2212</sup> Wells Fargo agreed that the factual statements contained within the Statement of Facts to the Deferred Prosecution Agreement ("DOJ Statement of Facts") are true and accurate. The DOJ Statement of Facts described the sales goals as "onerous" and "aggressive."<sup>2213</sup>

In her report, Examiner Candy noted the following:

Corporate culture refers to the norms and values that drive behaviors within an organization. An appropriate corporate culture for a bank is one that does not condone or encourage imprudent risk taking, unethical behavior, or the circumvention of laws, regulations, or safe and sound policies and procedures in pursuit of profits or business objectives. Office of the Comptroller of the Currency, Comptroller's Handbook, Safety and Soundness, Corporate and Risk Governance at 13 (July 2016).<sup>2214</sup>

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<sup>2208</sup> EC MSD Ex. 267 (Report of NBE Smith) at ¶54.

<sup>2209</sup> *Id.*

<sup>2210</sup> *Id.*

<sup>2211</sup> *Id.*

<sup>2212</sup> EC MSD Ex. 269 (Report of NBE Candy) at ¶51, quoting Press Release 20-035, U.S. Dep't of Justice, Central District of California, Wells Fargo Agrees to Pay \$3 Billion to Resolve Criminal and Civil Investigations into Sales Practices Involving the Opening of Millions of Accounts Without Customer Authorization (Feb. 21, 2020), <https://www.justice.gov/usao-cdca/pr/wells-fargo-agrees-pay-3-billion-resolvecriminal-and-civil-investigations-sales>.

<sup>2213</sup> EC MSD Ex. 269 (Report of NBE Candy) at ¶50, citing Press Release, U.S. Attorney's Office for the Central District of California, Wells Fargo Agrees to Pay \$3 Billion to Resolve Criminal and Civil Investigations into Sales Practices (Feb. 21, 2020); Wells Fargo Deferred Prosecution Agreement and Exhibit A, Statement of Facts (Feb. 20, 2020).

<sup>2214</sup> EC MSD Ex. 269 (Report of NBE Candy) at ¶52.

Based on her work in the supervision of the Bank and evidence she reviewed during the investigation and litigation, Examiner Candy concluded that employees engaged in sales practices misconduct because they feared disciplinary action up to and including termination if they did not meet the unreasonable sales goals and that this environment and aggressive sales culture existed in the Community Bank from 2002 through 2016.<sup>2215</sup> Employees also engaged in sales practices misconduct to earn incentive compensation.

Based on her training, experience, and commission as a National Bank Examiner, Examiner Candy reported that incentive compensation arrangements require effective oversight, governance, controls, and risk management and she concluded that the incentive compensation plans in the Community Bank overemphasized unreasonable sales goals and did not appropriately balance financial risk and reward.<sup>2216</sup> The incentive compensation arrangements in the Community Bank incentivized employees to engage in sales practices misconduct.<sup>2217</sup> The incentive compensation arrangements also incentivized store or branch managers to encourage, or turn a blind eye to, sales practices misconduct.<sup>2218</sup>

At the Bank, incentive compensation and performance management went hand in hand. The sales and incentive plans were commonly referred to as 50/50 plans because there was an expectation that only half the regions would be able to meet them. Although in theory incentive compensation arrangements should reward superior performance and employees should not suffer employment consequences for failing to achieve incentive compensation goals, in practice this is not what happened in the Community Bank.<sup>2219</sup>

For employees, failure to meet sales goals under the incentive compensation plans carried with it both the risk of not obtaining incentive compensation and poor performance reviews, including the risk of disciplinary action and termination.<sup>2220</sup> As the Board Report concluded, “performance management and incentive plans added significant additional risk to the sales model.”<sup>2221</sup> Moreover, promotions and advancement within the Community Bank were based primarily on employees’ ability to generate sales and meet the unreasonable sales goals.<sup>2222</sup> This contributed to the high-pressure culture within the Community Bank and gave the impression

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<sup>2215</sup> EC MSD Ex. 269 (Report of NBE Candy) at ¶53

<sup>2216</sup> *Id.* at ¶54.

<sup>2217</sup> *Id.*

<sup>2218</sup> *Id.*

<sup>2219</sup> *Id.*

<sup>2220</sup> *Id.*

<sup>2221</sup> *Id.*, citing Board Report at 27.

<sup>2222</sup> EC MSD Ex. 269 (Report of NBE Candy) at ¶55.

that the Bank and senior management valued sales at all cost – including above ethics and the customer’s best interest.<sup>2223</sup>

The incentive compensation plans rewarded employees for sales of secondary products (e.g., a second checking or savings account or additional debit cards).<sup>2224</sup> An outsized portion of conduct risk was associated with sales of secondary products. As the Bank acknowledged in the DOJ Statement of Facts, “[m]illions of secondary accounts and products were opened from 2002 to 2016, and many of these were never used by customers.”<sup>2225</sup> The Board Report explained that Community Bank

[r]egional leadership was unsuccessful in having their concerns about secondary checking accounts addressed even as late as 2015. In that year, one regional leader wrote an email continuing to advocate the removal of secondary accounts from incentive compensation plans, saying he and other leaders should “fight the good fight every year – especially since I think one day we will be asked why it was part of the goal process to begin with.”<sup>2226</sup>

The Board Report found that incentive compensation “contributed to problematic behavior by over-weighting sales as against customer service or other factors.”<sup>2227</sup> Based on an extensive investigation, the Board Report determined that “the only way definitively to address the broken sales model and the root cause of sales practice abuses was to emphasize other metrics for performance and to abandon exerting pressure through sales goals and sales-driven incentive programs.”<sup>2228</sup> The Board Report described the incentive compensation program as “misaligned” and in January 2017, the Bank put in place a new incentive program that focused on customer service rather than selling products.<sup>2229</sup> Examiner Candy’s conclusions match those found in the Board Report.<sup>2230</sup>

It is Examiner Candy’s opinion as a National Bank Examiner that the incentive compensation program and plans in the Community Bank were deficient in both design and implementation and resulted in employees engaging in sales practices misconduct.<sup>2231</sup> This was

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<sup>2223</sup> EC MSD Ex. 269 (Report of NBE Candy) at ¶55.

<sup>2224</sup> *Id.* at ¶56.

<sup>2225</sup> *Id.*, citing Press Release, U.S. Attorney’s Office for the Central District of California, Wells Fargo Agrees to Pay \$3 Billion to Resolve Criminal and Civil Investigations into Sales Practices (Feb. 21, 2020); Wells Fargo Deferred Prosecution Agreement and Exhibit A, Statement of Facts (Feb. 20, 2020).

<sup>2226</sup> EC MSD Ex. 269 (Report of NBE Candy) at ¶57, citing *Board Report* at 41 n.17.

<sup>2227</sup> EC MSD Ex. 269 (Report of NBE Candy) at ¶58, citing *Board Report* at 7

<sup>2228</sup> EC MSD Ex. 269 (Report of NBE Candy) at ¶58, citing *Board Report* at 8.

<sup>2229</sup> EC MSD Ex. 269 (Report of NBE Candy) at ¶58, citing *Board Report* at 8.

<sup>2230</sup> EC MSD Ex. 269 (Report of NBE Candy) at ¶58.

<sup>2231</sup> *Id.* at ¶59.

recklessly unsafe or unsound and exposed the Bank to increased operational, compliance, regulatory, legal, reputational and financial risks.<sup>2232</sup>

The Incentive Compensation Steering Committee, later renamed the Incentive Compensation Committee (“ICC”), was responsible for overseeing the ICRM policy, processes, and outcomes and for reporting to the Human Resources Committee of the Board regarding ICRM practices and outcomes.<sup>2233</sup> The ICC was responsible for providing “oversight around the design and outcomes of the Business Line incentive plans, and lead[ing] Wells Fargo’s enterprise efforts to enhance incentive compensation practices throughout the Company.”<sup>2234</sup> Respondent Julian was a member of the ICC from 2012 through October 2016.<sup>2235</sup>

Examiner Candy opined that Respondent Julian recklessly engaged in unsafe or unsound practices through his failings with respect to incentive-compensation risk management, governance, and oversight as members of the ICC.<sup>2236</sup> The ICRM Policy states that incentive-based compensation arrangements should “balance risk and financial rewards in a manner that does not provide team members with an incentive to take inappropriate risks that could lead to material financial, operational, or reputational risk for the company.”<sup>2237</sup> The incentive compensation plans in the Community Bank encouraged employees to take inappropriate risks, risk that Respondent Julian and others were responsible for understanding, managing, overseeing, and escalating as members of the ICC.<sup>2238</sup> Respondent Julian’s failures with respect to incentive-compensation risk management exposed the Bank to abnormal risk of loss and resulted in actual loss.<sup>2239</sup>

### **The Community Bank’s Controls were Inadequate**

Examiner Candy participated in the May 2015 ongoing supervisory activity that resulted in SL 2015-36.<sup>2240</sup> During that review, she performed work to better understand the Bank’s controls related to sales practices.<sup>2241</sup> She reviewed customer and employee complaints and

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<sup>2232</sup> EC MSD Ex. 269 (Report of NBE Candy) at ¶59.

<sup>2233</sup> *Id.* at ¶65.

<sup>2234</sup> *Id.*

<sup>2235</sup> *Id.*

<sup>2236</sup> *Id.*

<sup>2237</sup> EC MSD Ex. 269 (Report of NBE Candy) at ¶66, citing Incentive Compensation Risk Management Policy (July 13, 2011) (OCC-WF-SP-05434513); Incentive Compensation Risk Management Policy (Nov. 27, 2012) (OCC-WF-SP-07258277).

<sup>2238</sup> EC MSD Ex. 269 (Report of NBE Candy) at ¶66.

<sup>2239</sup> *Id.*

<sup>2240</sup> *Id.* at ¶67.

<sup>2241</sup> *Id.*

identified themes from those complaints.<sup>2242</sup> Based on her work on the May 2015 review, she concluded that the Community Bank had a problem with sales practices misconduct and identified weakness in the Bank's controls.<sup>2243</sup> However, she did not have clear visibility into the extent, severity, and duration of the sales practices misconduct problem until further supervisory work and Examiner Candy's participation in the investigation.<sup>2244</sup>

SL 2015-36 notes that "[o]f the 2,856 sales integrity cases [in 2014], 43% involved lack of customer consent for a product."<sup>2245</sup> She noted that in her work sampling customer complaints, "in many cases there was no method to prove customer consent in the form of a signature for either the deposit or credit card product."<sup>2246</sup> Based on her review of employee complaints made through the Bank's EthicsLine, Examiner Candy identified the following themes: sales pressure; taking advantage of a protected classes (e.g., age/elderly); and the selling of unwanted deposit or credit products.<sup>2247</sup> Review of customer complaints revealed similar themes.<sup>2248</sup> She found the complaints to be credible, and found that the Community Bank did not have adequate controls to proactively identify these types of misconduct, nor did they complete adequate follow-up or investigation of the allegations.<sup>2249</sup>

The May 2015 review resulted in the issuance of five MRAs.<sup>2250</sup> One of the MRAs identified deficiencies in the Bank's controls over complaints.<sup>2251</sup> The review determined that the Bank did not have an effective customer complaint process and required management to reassess the customer complaint process "since it is critical to promoting compliance with laws and regulations and reducing reputation risk."<sup>2252</sup> One of the MRAs also identified deficiencies in Audit's coverage of sales practices, finding that "no significant issues were identified or escalated as a result of [Audit's] work, and the group has not completed a comprehensive review of sales practices across the enterprise."<sup>2253</sup>

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<sup>2242</sup> EC MSD Ex. 269 (Report of NBE Candy) at ¶67.

<sup>2243</sup> *Id.*

<sup>2244</sup> *Id.*

<sup>2245</sup> *Id.*, citing OCC Supervisory Letter WFC 2015-36 (June 25, 2015) (OCC-WF-SP-07084578).

<sup>2246</sup> EC MSD Ex. 269 (Report of NBE Candy) at ¶67, citing OCC Supervisory Letter WFC 2015-36 (June 25, 2015) (OCC-WF-SP-07084578) at 3.

<sup>2247</sup> EC MSD Ex. 269 (Report of NBE Candy) at ¶68, citing OCC Supervisory Letter WFC 2015-36 (June 25, 2015) (OCC-WF-SP-07084578), at 3.

<sup>2248</sup> EC MSD Ex. 269 (Report of NBE Candy) at ¶68.

<sup>2249</sup> *Id.*

<sup>2250</sup> *Id.* at ¶69.

<sup>2251</sup> *Id.*

<sup>2252</sup> *Id.*, citing OCC Supervisory Letter WFC 2015-36 (June 25, 2015) (OCC-WF-SP-07084578) at 4.

<sup>2253</sup> *Id.*, citing OCC Supervisory Letter WFC 2015-36 (June 25, 2015) (OCC-WF-SP-07084578) at 2.

After the OCC issued the five MRAs in June 2015, the OCC continued its review of sales practices risk, ultimately issuing SL 2016-36 on July 18, 2016.<sup>2254</sup> Examiner Candy participated in the ongoing review that culminated in the issuance of SL 2016-36.<sup>2255</sup> SL 2016-36 documents the following conclusions, with which she agrees:

The practice of opening deposit accounts without authorization, the practice of moving funds without customer consent (simulated funding) and the failure to timely refund or remediate fees charged are considered unsafe or unsound banking practices.<sup>2256</sup>

The widespread and unauthorized opening of credit card accounts without consent . . . is considered an unsafe or unsound banking practices. The root causes include excessive sales pressure and the absence of a control process that required documentation of explicit customer consent.<sup>2257</sup>

Aggressive sales pressure, coupled with lack of adequate risk management oversight, fostered inappropriate and possibly fraudulent behavior by employees. This behavior included the opening of unwanted deposit and credit card accounts and the practice of moving funds without customer consent (simulated funding), which resulted in customer harm, hundreds of terminated employees. . . .<sup>2258</sup> In addition, the risks from these sales practices were not adequately managed.”<sup>2259</sup>

Our own review of incentive compensation programs and sales goals confirmed the aggressive sales pressure. For example, Gold, Silver, and Bronze programs were in place to encourage employees to meet sales goals, with Gold requiring 13 daily ‘solutions’ or products sold per day.<sup>2260</sup>

Weaknesses in internal controls and management information systems including a lack of robust first, second and third lines of defense risk management programs.<sup>2261</sup>

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<sup>2254</sup> EC MSD Ex. 269 (Report of NBE Candy) at ¶70, citing OCC Supervisory Letter WFC 2016-36 (July 18, 2016) (OCC-WF-SP-07169362).

<sup>2255</sup> EC MSD Ex. 269 (Report of NBE Candy) at ¶70.

<sup>2256</sup> *Id.*

<sup>2257</sup> *Id.*

<sup>2258</sup> *Id.*

<sup>2259</sup> *Id.*

<sup>2260</sup> *Id.*

<sup>2261</sup> *Id.*



## The Evolution of Controls

In general, the Bank relied on three mechanisms to identify employees who engaged in sales practices misconduct: (1) employee reported allegations through the EthicsLine, to Human Resources, or to management, when the report was deemed sufficiently credible to warrant further review; (2) customer complaints, only if subsequent “polling” of other customers of the same employee revealed other similar incidents of misconduct; and (3) “proactive monitoring,” which involved the use of data analytics to identify patterns of “red flag” sales activity.<sup>2262</sup> The first two detection methods were reactive and relied on another employee or a customer becoming aware of improper activity and reporting it.<sup>2263</sup> The third detection method was, in Examiner Candy’s opinion, inadequate as it only identified patterns of activity for certain types of misconduct.<sup>2264</sup>

In an email dated August 3, 2012, the former Head of Sales Quality, Cindy Walker, acknowledged that the controls relied on employees and customers reporting misconduct rather than active monitoring to detect misconduct:

The Sales Quality (SQ) business model has always been predicated upon being “reactive” by design. That is, researching and vetting incoming EthicsLine allegations, Phone Bank allegations and the like. Monitoring and/or additional reporting activities would not necessarily be effective or in scope considering the business intent.<sup>2265</sup>

During her supervisory review, Examiner Candy found that SSCOT’s research process was not robust nor effective, and ultimately many allegations were not properly investigated as a result.<sup>2266</sup> Bank documents show that between 2012 and 2013, the Sales and Service Conduct Oversight Team (SSCOT– SSCOT was formerly known as Sales Quality), a group within the Community Bank that reported to Respondent Russ Anderson, began “proactively monitoring” some types of sales practices misconduct, including changes to customer phone numbers in the Bank’s system and a practice the Bank referred to as “simulated funding.”<sup>2267</sup> The activity that the Bank described as “simulated funding” involves a banker making fraudulent or unauthorized transfers of money from one account to another without the customer’s consent to make it appear as if the customer had funded the account.<sup>2268</sup>

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<sup>2262</sup> EC MSD Ex. 269 (Report of NBE Candy) at ¶72.

<sup>2263</sup> *Id.*

<sup>2264</sup> *Id.*

<sup>2265</sup> *Id.* at ¶73, citing email from Marty Weber to Michael Bacon et. al. (Aug. 8, 2012) (OCC-WF-SP-06076695).

<sup>2266</sup> EC MSD Ex. 269 (Report of NBE Candy) at ¶74.

<sup>2267</sup> *Id.* at ¶75.

<sup>2268</sup> *Id.*

Bank documents show that in the summer and fall of 2013, SSCOT conducted an analysis to detect simulated funding and phone number changes in the Los Angeles/Orange County and then across the Regional Bank footprint, using criteria to identify “extreme outlier” activity.<sup>2269</sup> For conduct likely exhibiting simulated funding, SSCOT used criteria of 50 or more accounts in five months or more than 10 percent of total accounts opened in four months, where the account was funded with a single transfer of funds from an existing accounts to a new account, and then transferred back to the originating accounts within 1 day, with no further activity in the new account.<sup>2270</sup> The practical effect of using this methodology was that if activity exhibiting simulated funded was done to 49 accounts in five months, it was not detected through proactive monitoring.<sup>2271</sup>

This proactive monitoring was used to identify only egregious patterns of red flag activity for simulated funding and led to an initial round of investigation and termination of approximately 30 employees in fall 2013, some of whom complained to the Los Angeles Times.<sup>2272</sup> In October 2013, the Los Angeles Times reported, “the pressure to meet sales goals was intense at Wells Fargo. At times, managers required workers to stay in the branch after the close of business, calling their friends and family members, if they failed to open enough accounts during the day.”<sup>2273</sup> In December 2013, the Los Angeles Times published a second article identifying that the sales practices misconduct was not limited to Los Angeles:

To meet quotas, employees have opened unneeded accounts for customers, ordered credit cards without customers’ permission and forged client signatures on paperwork. . . . These conclusions emerge from a review of internal bank documents and court records, and from interviews with 28 former and seven current Wells Fargo employees who worked at bank branches in nine states, including California.<sup>2274</sup>

### **Pause on Proactive Monitoring**

Following the Los Angeles Times articles, SSCOT “paused” proactive monitoring until July 2014, purportedly to allow the Community Bank to identify and address the root cause of the misconduct.<sup>2275</sup> It was evident that the misconduct was widespread and continued monitoring

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<sup>2269</sup> EC MSD Ex. 269 (Report of NBE Candy) at ¶76.

<sup>2270</sup> *Id.*

<sup>2271</sup> *Id.*, citing email from David Otsuka to Debra Patterson et. al. (Nov. 18, 2013) (OCC-WF-SP-06925140); Email from Glen Najvar to Michael Moore et. al. (Sept. 13, 2013) (OCC-WF-SP-08387599).

<sup>2272</sup> EC MSD Ex. 269 (Report of NBE Candy) at ¶77.

<sup>2273</sup> *Id.*

<sup>2274</sup> *Id.*

<sup>2275</sup> *Id.* at ¶78.

could inundate the Community Bank with investigations and terminations.<sup>2276</sup> However, by 2013 the root cause of sales practices misconduct was well known by the Community Bank, the Law Department, and Audit.<sup>2277</sup>

The Community Bank paused proactive monitoring for approximately seven months, from December 2013 through July 2014.<sup>2278</sup> Based on her review of the evidence, Examiner Candy opined that at the time the Community Bank instituted the pause on proactive monitoring, the root cause had been well known within the Bank.<sup>2279</sup> Many Bank witnesses testified that no one ever suggested any cause for employees to engage in sales practices misconduct other than the pressure on employees to meet sales goals in order to keep their jobs, and to a lesser extent to earn incentive compensation.<sup>2280</sup>

From her review of Bank documents during the investigation and litigation, Examiner Candy opined that the pause on proactive monitoring was intended to limit the number of terminations for sales practices misconduct to avoid reputational harm to the Bank from negative publicity.<sup>2281</sup> In her opinion as a National Bank Examiner, this was not a prudent nor acceptable reason to pause proactive monitoring.<sup>2282</sup>

### **Controls Following the Pause**

In July 2014, SSCOT resumed proactive monitoring for simulated funding, applying a new criteria of identifying employees in the 99.99th percent (top 0.01 percent) of Bank team members who met “red flag” activity for simulated funding in one month.<sup>2283</sup> Based on Bank documents, approximately 30,000 employees exhibited characteristics of “red flag” activity for simulated funding in one month.<sup>2284</sup> However, due to the 99.99th percent threshold SSCOT used to identify potential simulated funding, SSCOT identified only 3 employees per month (i.e., 0.01 percent of 30,000 Community Bank team members) for investigation.<sup>2285</sup> The Community Bank

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<sup>2276</sup> EC MSD Ex. 269 (Report of NBE Candy) at ¶78, citing Email from Christine Meuers to Hope Hardison et. al. (Dec. 2, 2013) (OCC-WF-SP-07373388).

<sup>2277</sup> EC MSD Ex. 269 (Report of NBE Candy) at ¶78.

<sup>2278</sup> EC MSD Ex. 269 (Report of NBE Candy) at ¶80, citing Email from Paula Herzberg to Rebecca Rawson et. al. (Sept. 13, 2016) (OCC-WF-SP-07687489).

<sup>2279</sup> EC MSD Ex. 269 (Report of NBE Candy) at ¶81.

<sup>2280</sup> *Id.*

<sup>2281</sup> *Id.* at ¶82.

<sup>2282</sup> *Id.*

<sup>2283</sup> *Id.* at ¶83, citing Email from Deanna Lindquist to Crystal Silva et. al. (Oct. 22, 2015) (OCC-WF-SP-07916406); Email from Glen Najvar to David Otsuka (July 7, 2014) (OCC-WF-SP-08205606).

<sup>2284</sup> EC MSD Ex. 269 (Report of NBE Candy) at ¶84.

<sup>2285</sup> *Id.*

referred to these employees as “outliers.”<sup>2286</sup> Examiner Candy opined that this was grossly insufficient – opining that only reviewing 0.01 percent of the “red flag” activity in any given month is nowhere near a sufficient control for identifying potential simulated funding.<sup>2287</sup>

Beyond simulated funding, SSCOT used 99.99th percent as its threshold for proactive monitoring for the vast majority of sales activity monitored.<sup>2288</sup> In April 2015, the Community Bank’s threshold was lowered slightly to detect employees in the 99.95th percentile of activity that was a red flag for simulated funding.<sup>2289</sup> The 99.95th percent threshold involved an employee engaging in approximately 10.3 monthly occurrences of red flag activity for simulated funding.<sup>2290</sup> Lowering the threshold monitoring criteria slightly to the 99.95th percentile resulted in the identification of approximately 15 to 18 employees engaging in simulated funding per month.<sup>2291</sup> However, the Bank’s data shows that 45 percent of employees had at least one instance of red flag activity for simulated funding per month.<sup>2292</sup>

OCC National Bank Examiner Gregory Coleman reported that during the May 2015 Risk Committee meeting, Board members expressed concerns about the adequacy of the high threshold that had been used in the 2013 investigation, namely the requirement that employees had made 50 or more telephone number changes to trigger review.<sup>2293</sup> Examiner Coleman

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<sup>2286</sup> EC MSD Ex. 269 (Report of NBE Candy) at ¶84.

<sup>2287</sup> *Id.*

<sup>2288</sup> *Id.* at ¶85.

<sup>2289</sup> *Id.* at ¶86, citing Email from Deanna Lindquist to Crystal Silva et. al. (Oct. 22, 2015) (OCC-WF-SP-07916406); Email from Paula Herzberg to Rebecca Rawson et. al. (Sept. 13, 2016) (OCC-WF-SP-07687489).

<sup>2290</sup> EC MSD Ex. 269 (Report of NBE Candy) at ¶86, citing Email from David Otsuka to Rebecca Rawson et. al. (Sept. 21, 2015) (OCC-SP0613052).

<sup>2291</sup> EC MSD Ex. 269 (Report of NBE Candy) at ¶86, citing Email from Deanna Lindquist to Crystal Silva et. al. (Oct. 22, 2015) (OCC-WF-SP-07916406).

<sup>2292</sup> EC MSD Ex. 269 (Report of NBE Candy) at ¶86, citing Email from David Otsuka to Rebecca Rawson et. al. (Sept. 21, 2015) (OCC-SP0613052).

<sup>2293</sup> EC MSD Ex. 257 (Report of NBE Coleman) at ¶90 citing Strother Tr. 28:7-24 (December 18, 2018), OCC-SP00047742. Gregory J. Coleman is a Deputy Comptroller of Large Bank Supervision for the OCC. He became a commissioned National Bank Examiner in 1994 and Federal Thrift Regulator in 2013. As Deputy Comptroller of Large Bank Supervision, he is responsible for effectively supervising a portfolio of 8 financial institutions totaling \$2.8 trillion in assets, as well as leading, mentoring, and managing a staff of 170 examiners and support personnel. Among other things, his responsibilities include setting examination strategy and overseeing the OCC’s supervision and personnel management for the institutions in his portfolio. He also reviews and confirms the OCC’s findings and conclusions on safety and soundness, legal and regulatory violations, and fiduciary duty expectations, and deliver such findings to the directors and senior management of the institutions he oversees. From approximately September 2015 to September 2019, he was the Deputy Comptroller of Large Bank Supervision responsible for overseeing the supervision of Wells Fargo Bank, N.A. Sioux Falls, South Dakota (“Wells Fargo” or “Bank”). Even after the management of the Bank moved out of his portfolio, he continued to participate in the OCC’s investigation of the Bank’s sales practices and receive periodic updates on the investigation status, consistent with the role of a senior manager. He has thirty-one years of professional experience at the OCC and Promontory

reported that despite these concerns about Community Bank thresholds, Respondent Russ Anderson, who presented at the meeting, failed to advise the Risk Committee of the 99.99 and 99.95 percent thresholds then being used to identify other types of misconduct.<sup>2294</sup>

In April 2015, an SSCOT manager who reported directly to Respondent Russ Anderson shared with Respondent Russ Anderson Facebook posts from a former Bank branch manager.<sup>2295</sup> The posts stated, “[Wells Fargo management] have created a toxic atmosphere of sales goals that forces employees to sell products [customers] don’t want. They literally say ‘every customer needs a credit card.’ . . . If there is ever a company as disgusting and unethical as this one, I dare you to find it.”<sup>2296</sup>

Examiner Smith reported that she is aware of several meetings where Respondent Russ Anderson was not transparent with the OCC’s examination team.<sup>2297</sup> For example, Examiner Smith reported that notwithstanding her obvious knowledge about sales pressure, including terminations for not meeting sales goals, Respondent Russ Anderson told the OCC at a February 10, 2015 meeting, “no one loses their job because they did not meet sales goals.”<sup>2298</sup> And she told examiners during a May 14, 2015 meeting with the OCC that interviews with employees “did not lead to a conclusion about sales pressure,” that she does not “hear” about pressure from personal bankers “at all,” and that “people are positive and pleased.”<sup>2299</sup>

Examiner Smith reported that as early as November 2008, Respondent Russ Anderson was informed the “vast majority of customer consent sales integrity cases are directly related” to the fact that no customer signature is required for opening accounts.<sup>2300</sup> Yet, according to Examiner Smith, the Community Bank continued to permit employees to issue products without a signature requirement.<sup>2301</sup>

Examiner Smith reported that although Respondent Russ Anderson was aware of the risks posed to the Bank by sales practices misconduct, the SSCOT, under her supervision,

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Financial Group, including extensive experience in the government and private sector in the supervision and risk management of large, complex financial institutions. EC MSD Ex. 257 (Report of NBE Coleman) at ¶¶1-4, 6.

<sup>2294</sup> EC MSD Ex. 257 (Report of NBE Coleman) at ¶90, citing Minutes of the Meeting of the Risk Committee of the Board of Directors of Wells Fargo & Company held on May 19, 2015, OCC-WF-SP-08676318.

<sup>2295</sup> EC MSD Ex. 267 (Report of NBE Smith) at ¶111.

<sup>2296</sup> EC MSD Ex. 267 (Report of NBE Smith) at ¶111, quoting E-mail from Rawson to Russ Anderson, FYI ONLY | FW: SNJ FACEBOOK POSTS (RP & AP NAMED) (OCCWF-SP-04792164).

<sup>2297</sup> EC MSD Ex. 267 (Report of NBE Smith) at ¶112.

<sup>2298</sup> EC MSD Ex. 267 (Report of NBE Smith) at ¶112, citing Conclusion Memorandum, Community Bank Operational Risk Exam: Cross Sell/Sales Practices (Feb. 19, 2015) (OCC-SP0125161).

<sup>2299</sup> EC MSD Ex. 267 (Report of NBE Smith) at ¶112, quoting Meeting Notes, Discussion with CB GRO Claudia Russ Anderson surrounding Sales Practices (May 14, 2015) (OCC-SP0067064).

<sup>2300</sup> EC MSD Ex. 267 (Report of NBE Smith) at ¶113, quoting E-mail from Pyles to Russ Anderson, RE: SS&D Parking Lot File Pickup Notification (OCC-WF-SP-05012541).

<sup>2301</sup> EC MSD Ex. 267 (Report of NBE Smith) at ¶114.

employed a proactive monitoring threshold for simulated funding designed to capture only “extreme outliers” or the worst of the worst offenders.<sup>2302</sup> She reported that Respondent Russ Anderson had previously assented to a months-long pause in 2013 and 2014 of the only proactive monitoring the Bank was doing to identify simulated funding.<sup>2303</sup> She reported that the Bank lacked the means to proactively identify many other types of sales practices misconduct, including the issuance of unauthorized debit cards.<sup>2304</sup>

Examiner Smith reported that notwithstanding her knowledge about the inadequacy of the Bank’s sales practices controls, for which she was directly responsible, Respondent Russ Anderson was involved in the preparation and presentation of the May 2015 memorandum to the Risk Committee of the Board of Directors that stated the Bank’s sales practices controls were “robust.”<sup>2305</sup> The memo stated that the root cause of sales practices misconduct was “intentional team member misconduct,” and that there was “a dramatic reduction in inappropriate practices in the past year,” without disclosing the high thresholds SSCOT used to identify wrongdoers.<sup>2306</sup> The memorandum was also provided to the OCC.<sup>2307</sup>

Examiner Smith opined that Respondent Russ Anderson engaged in violations of law, unsafe or unsound practices, and breaches of her fiduciary duty by failing to ensure that the Bank adequately managed sales practices risk, which allowed the Bank’s sales practices misconduct problem to continue unabated for many years, and failed in performing the most basic elements of her job.<sup>2308</sup>

Examiner Smith further opined that Respondent Russ Anderson engaged in violations of law, unsafe or unsound practices, and breaches of her fiduciary duty by misleading and providing false information to the Board of Directors and the OCC and obstructing the OCC’s examination process; that Respondent Russ Anderson recklessly engaged in the aforementioned unsafe or unsound practices, and that Respondent Russ Anderson’s violations, practices, and breaches

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<sup>2302</sup> EC MSD Ex. 267 (Report of NBE Smith) at ¶115, quoting E-mail from Rawson to Russ Anderson, FOR REVIEW | FW: SIM FUNDING & Phone Change outliers for OTHER AREAS—PROPOSED E-MAIL PART 3 (Oct. 25, 2013) (OCC-WF-SP-07037285).

<sup>2303</sup> EC MSD Ex. 267 (Report of NBE Smith) at ¶115, citing E-mail from Russ Anderson to Callahan et al. Sales Quality work (Jan. 30, 2014) (OCC-SP00009142).

<sup>2304</sup> EC MSD Ex. 267 (Report of NBE Smith) at ¶115.

<sup>2305</sup> *Id.* at ¶116, quoting Memorandum from Strother to Risk Committee WFC Board of Directors, Board Risk Committee Agenda Item (May 19, 2015) (OCC-WF-SP-07083821).

<sup>2306</sup> EC MSD Ex. 267 (Report of NBE Smith) at ¶117, quoting Memorandum from Strother to Risk Committee WFC Board of Directors, Board Risk Committee Agenda Item (May 19, 2015) (OCC-WF-SP-07083821) at 3, 5.

<sup>2307</sup> EC MSD Ex. 267 (Report of NBE Smith) at ¶118.

<sup>2308</sup> *Id.*

constituted a pattern of misconduct, involved personal dishonesty, and demonstrated a willful and continuing disregard for the Bank's safety and soundness.<sup>2309</sup>

In late 2016, in response to an OCC MRA and the work of consultant PricewaterhouseCoopers regarding the volume of accounts that had likely been affected by simulated funding, the Bank's Financial Crimes Risk Management department conducted its own analysis of potential simulated funding.<sup>2310</sup> This analysis concluded that from May 2011 through July 2015, "387,000 accounts were opened by 41,000 Team Members that were more likely than not simulated funding."<sup>2311</sup>

Examiner Candy reported that the Bank's SSCOT continued to use the 99.95th percentile threshold until sales goals were eliminated in October 2016.<sup>2312</sup> She opined that using the 99.95th percentile, although slightly better than the 99.99th percentile, is also grossly insufficient given the amount of "red flag" activity.<sup>2313</sup>

### **The Bank's Controls to Prevent and Detect Sales Practices Misconduct were Inadequate**

Examiner Candy reported that effective internal controls provide bankers and examiners reasonable assurance that bank operations are efficient and effective, risk management systems are effective, and the bank complies with banking laws and regulations, internal policies, and internal procedures.<sup>2314</sup> She added that senior management is supposed to oversee and provide leadership and direction for the communication and monitoring of control policies, practices, and processes.<sup>2315</sup>

Examiner Candy opined that the Bank's controls to prevent and detect sales practices misconduct were inadequate and the Bank's risk management of its sales practices and the sales practices themselves were recklessly unsafe or unsound.<sup>2316</sup> She reported that designing and implementing controls reasonably designed to prevent and detect misconduct or illegal activity is a critical part of effective risk management and internal controls,<sup>2317</sup> adding that generally accepted standards of prudent operation require banks to manage risks and implement and

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<sup>2309</sup> EC MSD Ex. 267 (Report of NBE Smith) at ¶¶119-20.

<sup>2310</sup> EC MSD Ex. 257 (Report of NBE Coleman) at ¶66

<sup>2311</sup> EC MSD Ex. 257 (Report of NBE Coleman) at ¶66, quoting FCRM Report at 1, OCC-WF-SP-08515940.

<sup>2312</sup> EC MSD Ex. 269 (Report of NBE Candy) at ¶87.

<sup>2313</sup> *Id.*

<sup>2314</sup> EC MSD Ex. 269 (Report of NBE Candy) at ¶88, citing Office of the Comptroller of the Currency, Comptroller's Handbook, Internal Control at 2 (Jan. 2001).

<sup>2315</sup> EC MSD Ex. 269 (Report of NBE Candy) at ¶88, citing Office of the Comptroller of the Currency, Comptroller's Handbook, Internal Control at 2, 16 (Jan. 2001).

<sup>2316</sup> EC MSD Ex. 269 (Report of NBE Candy) at ¶89.

<sup>2317</sup> *Id.*

maintain controls reasonably designed to prevent and detect misconduct.<sup>2318</sup> She reported that ineffective sales practices risk management increases the potential of financial loss, litigation, regulatory risk, reputational damage, conduct risk, and operational and compliance risks.<sup>2319</sup>

As explained in the OCC's Corporate and Risk Governance, Comptroller's Handbook:

A responsible corporate culture and a sound risk culture are the foundation of an effective corporate and risk governance framework and help form a positive perception of the bank. A bank that fails to implement effective corporate and risk governance principles and practices may hinder the bank's competitiveness and adversely affect the bank's ability to establish new relationships and services or to continue servicing existing relationships. Departures from effective corporate and risk governance principles and practices cast doubt on the integrity of the bank's board and management. History shows that such departures can affect the entire financial services sector and the broader economy.<sup>2320</sup>

Examiner Candy opined that in addition to its inadequate detective controls, the Bank's controls to prevent sales practices misconduct were insufficient.<sup>2321</sup> For example, the Bank did not require a customer signature—*i.e.*, evidence of customer consent—to open a debit card.<sup>2322</sup> The Bank began requiring a customer signature to open a credit card only in 2015.<sup>2323</sup> On November 3, 2008, the former Head of Sales Quality wrote the following email to Respondent Russ Anderson:

Many of our product groups in the early 90's lobbied to remove the signature requirements because they slowed down the account opening process and carried a back room cost of filing and storing the paper application. The vast majority of customer consent sales integrity cases are directly related to this issue. This is why we have been pressing so hard for PIN or E-Signature Consent on ALL product sales. If we had a requirement that all product or services had one or the other, then most of our consent issues would become moot.<sup>2324</sup>

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<sup>2318</sup> EC MSD Ex. 269 (Report of NBE Candy) at ¶89.

<sup>2319</sup> *Id.*

<sup>2320</sup> *Id.* at ¶88, quoting Office of the Comptroller of the Currency, Comptroller's Handbook, Safety and Soundness, Corporate and Risk Governance at 3 (July 2016).

<sup>2321</sup> EC MSD Ex. 269 (Report of NBE Candy) at ¶90.

<sup>2322</sup> *Id.*

<sup>2323</sup> *Id.*

<sup>2324</sup> *Id.*, quoting Email from Tyson Pyles to Claudia Russ Anderson (Nov. 3, 2008) (OCC-WF-SP-05012541).



The Head of SSCOT, who reported to Respondent Russ Anderson, testified that the Bank's systems enabled employees to engage in sales practices misconduct.<sup>2325</sup> Rebecca Rawson explained in sworn testimony that the Bank's systems allowed employees to issue debit and credit cards to customers without their signatures or consent, which she determined was a control failure:

Q Okay. So I take it the bank had a policy that you should not issue credit cards or debit cards without the customer's consent?

A Correct.

Q All right. But the system allowed team members to actually issue credit cards and debit cards without the customer's consent or the customer's signature?

A I think that is right.

Q Okay. And you view that as a failure in controls?

A I think that is fair.<sup>2326</sup>

Based on the evidence that she reviewed, Examiner Candy opined that the Bank's controls to detect sales practices misconduct were also insufficient.<sup>2327</sup> She reported that a bank should investigate transactions that it considers a "red flag" for misconduct,<sup>2328</sup> adding that is particularly true where, as here, the suspected misconduct constitutes illegal and even criminal activity.<sup>2329</sup>

Examiner Candy reported that the Bank's use of the term "simulated funding" to refer to the activity described in this report does not change the fact that the activity constitutes fraud and falsification of bank records as well as a violation of 15 U.S.C. § 45(a) (Unfair and Deceptive Acts and Practices or UDAP).<sup>2330</sup> She reported that other types of sales practices misconduct similarly constitute illegal and criminal activity, for example opening a savings account without customer authorization involves falsifying bank records and UDAP.<sup>2331</sup>

Examiner Candy reported that the evidence shows that SSCOT determined that every month approximately 30,000 employees, or 45 percent of its employees, engaged in an activity that the Bank itself considered to be a "red flag" for illegal behavior.<sup>2332</sup> Examiner Candy

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<sup>2325</sup> EC MSD Ex. 269 (Report of NBE Candy) at ¶90.

<sup>2326</sup> *Id.* at ¶91, quoting Rawson Tr. 50:11-19 (July 26, 2018).

<sup>2327</sup> EC MSD Ex. 269 (Report of NBE Candy) at ¶92.

<sup>2328</sup> *Id.*

<sup>2329</sup> *Id.*

<sup>2330</sup> *Id.*

<sup>2331</sup> *Id.*

<sup>2332</sup> *Id.* at ¶93.

reported, however, that the Bank investigated only 3 employees per month during the period it was using the 99.99 percent threshold, and only approximately 15-18 employees per month when the Bank used the 99.95 percent threshold.<sup>2333</sup> Examiner Candy opined that this is far too few.<sup>2334</sup>

Examiner Candy was the lead OCC examiner who reviewed the Bank's earnings for three years and was responsible for understanding the drivers of the enterprise and the major business line income and expense streams.<sup>2335</sup> She understood that at least one of the justifications for the chosen thresholds was that the Bank believed it lacked resources to investigate additional misconduct and expanding the thresholds would yield many false positives.<sup>2336</sup> Examiner Candy opined that neither rationale is appropriate, and both demonstrate that the Bank did not have adequate risk management over sales practices.<sup>2337</sup>

Examiner Candy opined that the lack of resources to conduct necessary investigations is simply not an excuse for any bank, let alone a bank with the size and resources of Wells Fargo.<sup>2338</sup> She noted that Wells Fargo was posting record earnings quarter after quarter during that period.<sup>2339</sup> Moreover, she reported, a simple phone call to the customer asking whether he or she opened an account, moved a certain amount of money into it, and then moved back the same amount within one day and conducted no further activity on the new account, could suffice to investigate the issue.<sup>2340</sup>

Examiner Candy determined that the chosen thresholds were intentionally restrictive so as to allow the Bank to manage the *outcome* (that is, manage the number of employees identified), not the *risk*.<sup>2341</sup> She reported that the restrictive thresholds limited the number of investigations and terminations for sales practices misconduct, rather than managing the risk.<sup>2342</sup> And she opined that that is not consistent with prudent and effective risk management.<sup>2343</sup>

Examiner Candy opined that the fact that the Bank was identifying more "red flag" activity than it had the capacity to investigate is a strong indicator that there was a serious and

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<sup>2333</sup> EC MSD Ex. 269 (Report of NBE Candy) at ¶93.

<sup>2334</sup> *Id.*

<sup>2335</sup> *Id.* at ¶94.

<sup>2336</sup> *Id.*

<sup>2337</sup> *Id.*

<sup>2338</sup> *Id.*

<sup>2339</sup> *Id.*

<sup>2340</sup> *Id.*

<sup>2341</sup> *Id.*

<sup>2342</sup> *Id.*

<sup>2343</sup> *Id.* at ¶95.

systemic sales practices misconduct problem in the Community Bank.<sup>2344</sup> She reported that this is particularly so given the narrow criteria used to identify “red flag” activity (involving back-and-forth movement of funds between accounts within 24 hours, which in Examiner Candy’s view is not indicative of customer-authorized activity).<sup>2345</sup>

Moreover, she opined that the evidence indicates that the Community Bank lacked the ability to identify the following types of sales practices misconduct using data analytics (and thus relied on reactive channels only to detect such misconduct): bundling; pinning; sandbagging; and the opening of unauthorized debit cards and credit cards.<sup>2346</sup>

Examiner Candy reported that the detected “red flag” activity, the majority of which the Bank chose not to investigate, did not even come close to reflecting the full universe of sales practices misconduct at the Bank.<sup>2347</sup> She noted that the Bank determined each month 30,000 of its employees engaged in an activity that was a red flag for just one of the various types of sales practice misconduct, and she opined that this should have alerted Bank leadership, including the Group Risk Officer and Audit, that there was a serious and systemic problem with sales practices misconduct in the Community Bank’s model.<sup>2348</sup>

Examiner Candy opined that this should have alerted them that the problem was not attributable to rogue employees but to the Community Bank’s business model and operations.<sup>2349</sup> She reported that rather than changing the profitable model, the Bank investigated three employees per month, and later fifteen to eighteen employees, out of the 30,000 employees identified per month who engaged in the “red flag” activity.<sup>2350</sup>

Examiner Candy reported that authoritative sources within the Bank knowledgeable on the red flag activity and the detection methodologies gave testimony that shows the Bank’s detection approach was inappropriate.<sup>2351</sup>

For example, the head of SSCOT, testified as follows:

Q I take it you would agree that the Bank's analysis shows that about 45 percent of the employees engaged in red flag activity, is that correct?

A Correct.

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<sup>2344</sup> *Id.*

<sup>2345</sup> EC MSD Ex. 269 (Report of NBE Candy) at ¶95.

<sup>2346</sup> *Id.*

<sup>2347</sup> *Id.*

<sup>2348</sup> *Id.*

<sup>2349</sup> *Id.*

<sup>2350</sup> *Id.*

<sup>2351</sup> *Id.* at ¶96.

Q All right. And you also agree that the Bank was only investigating 18 of those? A Correct.

Q All right. And you thought that was problematic?

A Correct.

Q And Ms. Sperle, the head of corporate investigation, also thought it was problematic?

A I believe she did.<sup>2352</sup>

The Head of SSCOT admitted that the proactive monitoring demonstrated that the Bank's other two reactive methods for detecting sales practices misconduct (methods that relied on employees and customers reporting misconduct) were ineffective.<sup>2353</sup> That is because the reactive methods generally failed to identify even the "worst of the worst" actors, who then triggered the 99.99% and 99.95% thresholds.<sup>2354</sup> Accordingly, it follows that the reactive controls were also ineffective in detecting employees who engaged in the red flag activity with less frequency given that they did not detect even the most egregious offenders.<sup>2355</sup>

Specifically, the Head of SSCOT testified as follows:

Q And for the most part, the number of people that met that threshold had not been caught by the Bank's other methods for identifying misconduct?

A Correct.

Q All right. So, if these other methods were not effective in identifying people who are at the top fraction of the top one percent of people engaged in the misconduct, it would fall into a mathematical certainty that they really would not be effective if people engaged in this misconduct who are in the 50th percentile or 60th percentile, correct?

A Correct.<sup>2356</sup>

Examiner Candy reported that the Bank had better systems and tools to detect employees who did not meet sales goals than it did employees who engaged in sales practices misconduct.<sup>2357</sup> She reported that the risk of termination for employees who did not meet sales goals far exceeded that of being investigated and terminated for sales practices misconduct.<sup>2358</sup>

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<sup>2352</sup> EC MSD Ex. 269 (Report of NBE Candy) at ¶96, quoting Rawson Tr. 188:3-16 (July 26, 2018).

<sup>2353</sup> EC MSD Ex. 269 (Report of NBE Candy) at ¶97.

<sup>2354</sup> *Id.*

<sup>2355</sup> *Id.*

<sup>2356</sup> *Id.*, quoting Rawson Tr. 211:7-20 (July 26, 2018).

<sup>2357</sup> EC MSD Ex. 269 (Report of NBE Candy) at ¶98.

<sup>2358</sup> *Id.*

She found that the Community Bank management had the ability to track sales at a very granular level and would call the branches multiple times a day with an update on sales activity.<sup>2359</sup>

Examiner Candy reported that this contrasted sharply with the insufficient and infrequent sales quality and proactive monitoring reporting.<sup>2360</sup> She opined that the high pressure and aggressive sales goal business model contributed to an environment with high inherent risk for compliance.<sup>2361</sup> She reported that despite this, Respondent Russ Anderson failed to implement sufficient preventative and detective controls, which ultimately pushed the residual risk to unacceptable levels.<sup>2362</sup>

As an example, Examiner Candy noted that Loretta Kay Sperle, the former Head of Corporate Investigations, testified before the OCC that there was a significant likelihood that an employee's manager would know if the employee failed to meet her sales goals because the Community Bank tracked that; by contrast, the chances that an employee would be caught for issuing an unauthorized product or service were very small.<sup>2363</sup>

She testified:

Q Okay. So if [employees] were doing it when nobody is watching, and they don't do it enough to trigger the outlier thresholds that you've had, the chances of them getting caught is very small?

A Yes. I would agree.<sup>2364</sup>

### **The Bank's Controls Were Intentionally Inadequate**

Based on Bank documents and sworn testimony that Examiner Candy reviewed, she concluded that the Bank's senior leaders did not want to identify and terminate additional employees for sales practices misconduct, beyond those identified through the reactive methods and the restrictive proactive monitoring methodology described above, in part because of the negative publicity that terminations were expected to generate.<sup>2365</sup>

Examiner Candy reported that ongoing mass terminations would have undermined the Bank's arguments that were presented to the Board and OCC examiners: (1) the misconduct was caused by "bad apple" employees engaging in intentional misconduct, as opposed to a defect in the business model, and (2) corrective measures implemented by the Community Bank were

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<sup>2359</sup> *Id.* at ¶98.

<sup>2360</sup> *Id.*

<sup>2361</sup> *Id.*

<sup>2362</sup> *Id.*

<sup>2363</sup> *Id.*

<sup>2364</sup> *Id.*, quoting Loretta Kay Sperle Tr. 158:15-20 (February 13, 2018) (EC MSD Ex. 299).

<sup>2365</sup> EC MSD Ex. 269 (Report of NBE Candy) at ¶99.

effectively resolving the problem.<sup>2366</sup> She opined that Respondent Russ Anderson’s failure to implement effective controls, and the failure to identify employees engaged in sales practice misconduct to reduce terminations or to manage reputation risk, was unsafe or unsound and was inconsistent with the role of a Group Risk Officer.<sup>2367</sup>

Examiner Candy reported that the Bank’s former Director of Investigations and Chief Security Officer Michael Bacon saw common schemes indicative of misconduct that could have easily been detected if the Bank had looked for them.<sup>2368</sup> She reported that in 2012 or 2013, he advocated for proactive monitoring of other types of sales practices activities, such as: employees or customers with excessive accounts (*e.g.*, hundreds of accounts) registered to the same address; college credit cards issued to non-college students; and Bank employees with inappropriate business accounts.<sup>2369</sup> She reported that the former Chief Security Officer testified that he offered suggestions for proactive monitoring primarily to Respondent Russ Anderson, but also to Operating Committee members.

Examiner Candy reported that in his testimony, Mr. Bacon stated that there was resistance to more investigations due to fear of finding more misconduct that would lead to additional terminations.<sup>2370</sup> She reported that the former Chief Security Officer testified that the “lack of being proactive” was a “reoccurring theme” and he informed Respondent Russ Anderson that the employees identified and terminated for sales practices misconduct were the “tip of the iceberg.”<sup>2371</sup> She reported that he emphasized to her and others that a decline in terminations did not necessarily indicate less misconduct because the Bank was not proactive.<sup>2372</sup>

The former Chief Security Officer testified before the OCC that Community Bank senior leadership, including Respondent Russ Anderson, “absolutely” wanted to minimize terminations even if there was strong evidence that the employee engaged in sales practices misconduct.<sup>2373</sup>

James Richards, the Head of the Bank’s Financial Crimes Risk Management (“FCRM”) department, testified before the OCC, “using a percentage threshold does not necessarily address the actual risk. So if you’re pulling down a two percent or .01 percent or .05 percent that’s managing the output more than it is managing the risk.”<sup>2374</sup> He testified that he explained this to

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<sup>2366</sup> EC MSD Ex. 269 (Report of NBE Candy) at ¶99.

<sup>2367</sup> *Id.*

<sup>2368</sup> *Id.*, citing Michael Bacon Tr. 120:7-127:19 (May 4, 2018) (EC MSD Ex. 295).

<sup>2369</sup> EC MSD Ex. 269 (Report of NBE Candy) at ¶100.

<sup>2370</sup> *Id.*, citing Bacon Tr. 120:7-127:19 (May 4, 2018).

<sup>2371</sup> *Id.* quoting Bacon Tr. 105:25-106:19; 121:23-122:15 (May 4, 2018).

<sup>2372</sup> EC MSD Ex. 269 (Report of NBE Candy) at ¶100, citing Bacon Tr. 105:25-106:19; 121:23-122:15 (May 4, 2018).

<sup>2373</sup> EC MSD Ex. 269 (Report of NBE Candy) at ¶100, quoting Bacon Tr. 61:16-63:13 (May 4, 2018).

<sup>2374</sup> EC MSD Ex. 269 (Report of NBE Candy) at ¶100, quoting James Richards Tr. 139:3-140:17 (May 4, 2018) (EC MSD Ex. 298).

Respondent Russ Anderson and offered members of his analytics team to assist SSCOT's monitoring, but she refused. He testified that Respondent Russ Anderson responded that if "SSCOT changed or dramatically changed their monitoring thresholds that they would have, and I can't recall her phrase, but many, many more identified team members than they could reasonably handle."<sup>2375</sup>

### **Magnitude of Sales Practices Misconduct**

Examiner Candy reported that the OCC's investigation revealed that the scope of misconduct dramatically exceeded what has been publicly reported even during the September 2016 Congressional inquiries, what was reported to the Board in real time, and what was disclosed to the OCC during its examinations.<sup>2376</sup> Examiner Candy opined that given the business model in the Community Bank, the duration of the sales practices misconduct problem, and the quality of the preventative and detective controls for sales practices misconduct, a significant number of Community Bank customer-interfacing employees engaged in sales practices misconduct.<sup>2377</sup>

Examiner Candy reported that in August 2017, Bank consultant PricewaterhouseCoopers determined that Bank employees opened approximately 3.5 million potentially unauthorized accounts between January 2009 and September 2016.<sup>2378</sup> She reported that Bank documents show that as of January 2016, the Community Bank allowed employees to have approximately 30 percent of the new accounts they opened to remain unfunded; they would still be eligible to receive sales credit for the unfunded accounts.<sup>2379</sup> She reported that it is likely that some employees would only engage in simulated funding if they had exhausted other types of misconduct (which the Bank did not have the capabilities to proactively detect) but were still unable to meet their goals.<sup>2380</sup> Thus, only employees who had exhausted other opportunities to invent sales but were still short on sales goals were most likely to resort to "simulated funding."<sup>2381</sup>

Examiner Candy noted that in the DOJ Statement of Facts, the Bank itself admitted to the volume of sales practices misconduct:

The Community Bank's onerous sales goals and accompanying management pressure led thousands of its employees to engage in: (1) unlawful conduct to attain sales through fraud, identity theft, falsification of bank records, and (2) unethical practices to sell products of no or low value to the customer, while

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<sup>2375</sup> EC MSD Ex. 269 (Report of NBE Candy) at ¶100, quoting Richards Tr. 146:5-149:24 (May 1, 2018).

<sup>2376</sup> EC MSD Ex. 269 (Report of NBE Candy) at ¶101.

<sup>2377</sup> *Id.*

<sup>2378</sup> *Id.* at ¶102.

<sup>2379</sup> *Id.* at ¶107.

<sup>2380</sup> *Id.*

<sup>2381</sup> *Id.*

believing that the customer did not actually need the account and was not going to use the account.<sup>2382</sup>

Millions of secondary accounts and products were opened from 2002 to 2016, and many of these were never used by customers.<sup>2383</sup>

Between 2011 and 2016, tens of thousands of employees were the subject of allegations of unethical sales practices. During this period, the Company referred more than 23,000 employees for sales practices investigation and terminated over 5,300 employees for customer-facing sales ethics violations, including, in many cases, for falsifying bank records. Thousands of additional employees received disciplinary action short of termination or resigned prior to the conclusion of the Company's investigations into their sales practices.<sup>2384</sup>

From 2002 to 2016, Wells Fargo opened millions of accounts or financial products that were unauthorized or fraudulent.<sup>2385</sup>

Millions of non-Wells Fargo-employee customer accounts reflected a Wells Fargo email address as the customer's email address, contained a generic and incorrect customer phone number, or were linked to a Wells Fargo branch or Wells Fargo employee's home address.<sup>2386</sup>

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<sup>2382</sup> EC MSD Ex. 269 (Report of NBE Candy) at ¶110, quoting Press Release, U.S. Attorney's Office for the Central District of California, Wells Fargo Agrees to Pay \$3 Billion to Resolve Criminal and Civil Investigations into Sales Practices (Feb. 21, 2020); Wells Fargo Deferred Prosecution Agreement and Exhibit A, Statement of Facts (Feb. 20, 2020), at A-1 through A-16, ¶ 15 (Feb. 21, 2020) (Bank admitting to criminal violations resulting from sales practices misconduct, the root cause, scope, and duration of the problem, and the knowledge of Community Bank senior leadership).

<sup>2383</sup> EC MSD Ex. 269 (Report of NBE Candy) at ¶110, quoting Press Release, U.S. Attorney's Office for the Central District of California, Wells Fargo Agrees to Pay \$3 Billion to Resolve Criminal and Civil Investigations into Sales Practices (Feb. 21, 2020); Wells Fargo Deferred Prosecution Agreement and Exhibit A, Statement of Facts (Feb. 20, 2020) ¶ 17.

<sup>2384</sup> EC MSD Ex. 269 (Report of NBE Candy) at ¶110, quoting Press Release, U.S. Attorney's Office for the Central District of California, Wells Fargo Agrees to Pay \$3 Billion to Resolve Criminal and Civil Investigations into Sales Practices (Feb. 21, 2020); Wells Fargo Deferred Prosecution Agreement and Exhibit A, Statement of Facts (Feb. 20, 2020) ¶ 30.

<sup>2385</sup> EC MSD Ex. 269 (Report of NBE Candy) at ¶110, quoting Press Release, U.S. Attorney's Office for the Central District of California, Wells Fargo Agrees to Pay \$3 Billion to Resolve Criminal and Civil Investigations into Sales Practices (Feb. 21, 2020); Wells Fargo Deferred Prosecution Agreement and Exhibit A, Statement of Facts (Feb. 20, 2020) ¶ 32.

<sup>2386</sup> EC MSD Ex. 269 (Report of NBE Candy) at ¶110, quoting Press Release, U.S. Attorney's Office for the Central District of California, Wells Fargo Agrees to Pay \$3 Billion to Resolve Criminal and Civil Investigations into Sales Practices (Feb. 21, 2020); Wells Fargo Deferred Prosecution Agreement and Exhibit A, Statement of Facts (Feb. 20, 2020) ¶ 16.



Examiner Candy reported that “millions” of non-Wells Fargo-employee customer account documents were not delivered to the customer but were sent to the team member or Bank premises indicates both the immense magnitude of the misconduct and the inadequate controls.<sup>2387</sup> She opined that this demonstrates the systematic nature of the misconduct and the detrimental impact of the high sales goals and high-pressure business model.<sup>2388</sup> She added that in an October 2013 email, a senior Community Bank executive stated, “Basically we are closing about 90% of the accounts we open within 12 months. Not something to broadcast but ‘something’ is going on.”<sup>2389</sup>

Examiner Candy reported that anecdotal evidence also illustrated the pervasiveness of sales practices misconduct.<sup>2390</sup> She found that every customer-interfacing employee had a powerful motive and opportunity to engage in sales practices misconduct.<sup>2391</sup> She found the motive arose from fear of disciplinary action up to and including termination if they did not meet the unreasonable sales goals, or the desire to earn incentive compensation.<sup>2392</sup> She also found that the opportunity arose from the inadequate controls as detailed in this report.<sup>2393</sup> Given this motive and opportunity, the Bank’s own data and analysis, the duration of sales practices misconduct, and her experience, training, and commission as a National Bank Examiner, it is Examiner Candy’s opinion and conclusion that sales practices misconduct was pervasive in the Community Bank and involved tens of thousands, if not hundreds of thousands, of Bank employees issuing millions of products to customers without their consent.<sup>2394</sup>

### **Background on Bank Supervision Generally**

Examiner Coleman reported that the OCC supervises the largest banks and thrifts subject to its supervision within the Large Bank Supervision division (“LBS”).<sup>2395</sup> Within the OCC, an institution supervised by LBS is referred to as a “large bank.”<sup>2396</sup> The OCC has “resident” teams of LBS examiners stationed on-site at each large bank. Those examiners, led by an examiner-in-charge, supervise the institution and regularly assess different areas of a bank, including various

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<sup>2387</sup> EC MSD Ex. 269 (Report of NBE Candy) at ¶111.

<sup>2388</sup> *Id.*

<sup>2389</sup> *Id.* at ¶112, quoting Email from Laura Schulte to Shelly Freeman (Oct. 18, 2013) (OCC-WF-SP-05365262).

<sup>2390</sup> EC MSD Ex. 269 (Report of NBE Candy) at ¶113.

<sup>2391</sup> *Id.* at ¶114.

<sup>2392</sup> *Id.*

<sup>2393</sup> *Id.*

<sup>2394</sup> *Id.*

<sup>2395</sup> EC MSD Ex. 257 (Report of NBE Coleman) at ¶13.

<sup>2396</sup> *Id.*

components of its safety and soundness, risk management, and compliance with laws and regulations.<sup>2397</sup>

Examiner Coleman reported that the OCC uses a risk-based approach to determine its supervision strategy, prioritizing higher-risk activities and functions of the banks to assess the banks' safety and soundness and operation in compliance with applicable laws and regulations. Supervisory strategies are set in advance for each fiscal year.<sup>2398</sup>

The OCC supervisory process relies on transparency and open communication for its effectiveness. OCC examiners request information from bank management at the inception of each supervisory activity in order to assess the area under examination, and the OCC expects bank management to provide accurate and complete information in response to such requests.<sup>2399</sup> Further, the effectiveness of the supervisory process requires that bank management be transparent about examination-related risks, issues, and problems for areas being examined by the OCC.<sup>2400</sup>

Examiner Coleman reported that although the OCC has a dedicated staff of examiners assigned to each large bank, the number of OCC examiners is dwarfed by the number of control function staff at each large bank, including the bank's risk management, compliance, legal, and audit personnel, among others.<sup>2401</sup> The number of OCC examiners assigned to Wells Fargo between 2010 and 2016 generally ranged from 60 to 85 dedicated examiners. By way of comparison, Wells Fargo had more than 1,400 people in its audit department, more than 1,000 in its law department, and several thousand staff across its risk management function.<sup>2402</sup> Each of those control function units or departments has an important role in ensuring the safe and sound operation of the Bank and its compliance with laws and regulations.<sup>2403</sup>

Examiner Coleman reported that one of the ways the OCC and financial institutions refer to effective risk management within an institution is by reference to a framework known as the three lines of defense.<sup>2404</sup> He reported that this framework is well laid out in OCC guidance:

The three lines of defense model explains governance and roles among the bank's business units, support functions, and the internal audit function from a risk management perspective. First line of defense risk management activities take place at the frontline units where risks are created. The second

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<sup>2397</sup> EC MSD Ex. 257 (Report of NBE Coleman) at ¶13.

<sup>2398</sup> *Id.* at ¶14.

<sup>2399</sup> *Id.* at ¶15.

<sup>2400</sup> *Id.*

<sup>2401</sup> *Id.* at ¶16.

<sup>2402</sup> *Id.*

<sup>2403</sup> *Id.*

<sup>2404</sup> *Id.* at ¶17.

line of defense risk management activities occur in an area or function separate from the frontline unit, sometimes referred to as independent risk management. It oversees and assesses frontline units' risk management activities.

The internal audit function is often referred to as the third line of defense in this model. In its primary responsibility of providing independent assurance and challenge, the internal audit function assesses the effectiveness of the policies, processes, personnel, and control systems created in the first and second lines of defense.<sup>2405</sup>

Examiner Coleman reported that it is the responsibility of all three lines of defense to keep the Board of Directors informed of the Bank's risk management practices to allow the Board to provide credible challenge to management's recommendations and decisions.<sup>2406</sup>

### **Respondents Julian and McLinko Failed to Perform their Auditing Responsibilities with Respect to the Sales Practices Misconduct Problem**

According to the Office of the Comptroller of the Currency, Comptroller's Handbook, Internal and External Audits, an internal audit function is responsible for auditing activities to determine the Bank's compliance with laws, regulations, and established bank policies and procedures.<sup>2407</sup> "Internal audit provides an objective, independent review of bank activities, internal controls, and management information systems to help the board and management monitor and evaluate internal control adequacy and effectiveness."<sup>2408</sup> "Effective internal and external audit programs are also a critical defense against fraud and provide vital information to the board of directors about the effectiveness of the internal control system."<sup>2409</sup> Effective audit programs should "[h]elp maintain or improve the effectiveness of bank risk management processes, controls, and corporate governance."<sup>2410</sup> "Internal audit programs are a bank's primary mechanism for assessing controls and operations and performing whatever work is

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<sup>2405</sup> EC MSD Ex. 257 (Report of NBE Coleman) at ¶17, quoting Comptroller's Handbook, Internal and External Audits at 2 (December 2016), OCC-SP1107962.

<sup>2406</sup> EC MSD Ex. 257 (Report of NBE Coleman) at ¶17, citing Wells Fargo Risk Management Framework, Published July 2014, OCC-WF-SP-04791987.

<sup>2407</sup> EC MSD Ex. 269 (Report of NBE Candy) at ¶129, citing Office of the Comptroller of the Currency, Comptroller's Handbook, Internal and External Audits, at 7 (Apr. 2003).

<sup>2408</sup> EC MSD Ex. 269 (Report of NBE Candy) at ¶130, quoting Office of the Comptroller of the Currency, Comptroller's Handbook, Internal Control at 1 (Jan. 2001).

<sup>2409</sup> EC MSD Ex. 269 (Report of NBE Candy) at ¶130, quoting Comptroller's Handbook, Internal and External Audits at 1 (Apr. 2003).

<sup>2410</sup> EC MSD Ex. 269 (Report of NBE Candy) at ¶130.

necessary to allow the board and management to accurately attest to the adequacy of the bank's internal control system.”<sup>2411</sup>

Respondent Julian was the Chief Auditor.<sup>2412</sup> The chief auditor is responsible for internal audit's control risk assessments, audit plans, audit programs, and audit reports.<sup>2413</sup>

Respondent McLinko was responsible for audits of the Community Bank. This included audits covering incentive compensation, risk management, and controls.<sup>2414</sup>

Examiner Candy opined that Respondent Julian and Respondent McLinko each recklessly engaged in an unsafe or unsound practice by failing to plan and manage audit activity within the Community Bank that would detect and document the ongoing sales practices misconduct problem and identify corrective action to remediate and resolve it.<sup>2415</sup> The same conduct constituted breaches of their fiduciary duties.<sup>2416</sup>

Generally accepted standards of prudent operation require internal auditors to exhibit independence from the business line both in terms of operation and judgment<sup>2417</sup> and “understand a bank's strategic direction, objectives, products, services, and processes to conduct [its auditing] activities.”<sup>2418</sup> Although Examiner Candy reported that she did not have anywhere near complete visibility into the sales practices misconduct issues in the Community Bank during the May 2015 examination, which was only a few weeks long, based on the information she reviewed she determined that there were weaknesses in risk management and controls.<sup>2419</sup>

Respondents Julian and McLinko had unrestricted access to all functions, records, property, and personnel in the Bank, and WFAS's practice was to discuss problem areas and trends with Corporate Investigations, the unit that investigated sales integrity issues at the Bank.<sup>2420</sup> Respondents Julian and McLinko also had considerably more information about the sales practices misconduct problem than OCC examiners, and had full authority to perform audits and issue corrective actions (known as issues and remediations for Wells Fargo Audit).<sup>2421</sup>

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<sup>2411</sup> EC MSD Ex. 269 (Report of NBE Candy) at ¶130, quoting Office of the Comptroller of the Currency, Comptroller's Handbook, Internal and External Audits at 7-8 (April 2003)

<sup>2412</sup> EC MSD Ex. 269 (Report of NBE Candy) at ¶131.

<sup>2413</sup> *Id.*

<sup>2414</sup> *Id.* at ¶132.

<sup>2415</sup> *Id.* at ¶133.

<sup>2416</sup> *Id.* at ¶133.

<sup>2417</sup> EC MSD Ex. 268 (Report of NBE Crosthwaite) at ¶74.

<sup>2418</sup> EC MSD Ex. 269 (Report of NBE Candy) at ¶134, quoting Office of the Comptroller of the Currency, Comptroller's Handbook, Internal and External Audits, at 12 (Apr. 2003).

<sup>2419</sup> EC MSD Ex. 269 (Report of NBE Candy) at ¶134.

<sup>2420</sup> EC MSD Ex. 268 (Report of NBE Crosthwaite) at ¶75.

<sup>2421</sup> EC MSD Ex. 269 (Report of NBE Candy) at ¶134.

They also had significantly more personnel at their disposal, yet did not identify sales practices concerns in any meaningful way in any audit.<sup>2422</sup> Instead, all of the audits touching on sales practices indicated that the processes and controls were effective.<sup>2423</sup>

Respondent Julian and Respondent McLinko each were responsible for understanding the Community Bank's business model, the risks the model posed to the Bank, and the effectiveness of controls to detect and prevent the materialization of such risks.<sup>2424</sup> As set forth above, the risk management framework at the Bank had significant deficiencies and the controls were inadequate to prevent and detect sales practices misconduct.<sup>2425</sup>

Respondent Julian had a significant number of personnel at his disposal and the authority to examine any line of business at the Bank, including the Community Bank.<sup>2426</sup> It is Examiner Crosthwaite's opinion that both Respondent Julian and Respondent McLinko should have employed his resources and authority to identify and escalate the sales practices misconduct problem much earlier in a manner that could have lessened the severity and duration of the sales practices problem.<sup>2427</sup>

There was a significant control breakdown in the Community Bank, one that Respondent Julian previously acknowledged in his sworn statement.<sup>2428</sup> None of the deficiencies was identified in any audit while the sales practices misconduct problem existed at the Bank from the beginning of each Respondent's tenures as Chief Auditor and Executive Audit Director, respectively.<sup>2429</sup>

Examiner Crosthwaite expected Respondents Julian and McLinko to provide the OCC clear and direct information about issues that present serious risks to the Bank.<sup>2430</sup> She opined that Respondents Julian and McLinko never provided such information to the OCC related to the Bank's systemic sales practices misconduct problem.<sup>2431</sup>

### **Respondents Julian and McLinko Were Aware of the Sales Practices Problem**

Respondents Julian and McLinko received regular reporting about the extent of the systemic problem from multiple informational channels, including the committees they were

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<sup>2422</sup> EC MSD Ex. 269 (Report of NBE Candy) at ¶134.

<sup>2423</sup> *Id.*

<sup>2424</sup> *Id.*

<sup>2425</sup> *Id.*

<sup>2426</sup> EC MSD Ex. 268 (Report of NBE Crosthwaite) at ¶76

<sup>2427</sup> *Id.*

<sup>2428</sup> EC MSD Ex. 269 (Report of NBE Candy) at ¶134.

<sup>2429</sup> *Id.*

<sup>2430</sup> EC MSD Ex. 268 (Report of NBE Crosthwaite) at ¶79.

<sup>2431</sup> *Id.*

members of.<sup>2432</sup> Examiner Crosthwaite recalled the Chief Security Officer testifying that he was confident that all members of the TMMEC, including Respondent Julian, were fully aware of the seriousness, extent and root cause of the sales practices misconduct issue because he told them about all aspects of the problem in detail.<sup>2433</sup>

He testified as follows:

I am confident because we dedicated an hour and went through a very formal -- albeit an informal setting -- presentation and general discussion whereby all -- all participants acknowledged the existence of the -- of the pressure and the goals, and shared individual stories about such.<sup>2434</sup>

The contemporaneous documents Examiner Crosthwaite reviewed during the February 2017 email review support the Chief Security Officer's testimony.<sup>2435</sup> In August 2013, he provided information to the members of the TMMEC that sales integrity was the second largest investigation case type and that the number of investigations into sales integrity violations had increased from 2011 to 2012.<sup>2436</sup> The Committee consisted "of senior executives who share responsibility for the appropriate management of team member misconduct and internal fraud matters" and "was formed to look at issues more broadly across the company rather than individual situations."<sup>2437</sup> Its purpose was to "provide a forum for Wells Fargo executive management to provide leadership, oversight and direction related to team member misconduct and internal fraud risk management."<sup>2438</sup>

In March 2013, Respondent Julian wrote to Respondent McLinko that Michael Bacon, the Chief Security Officer and Head of Corporate Investigations "is presenting some data and Community Banking has a lot of issues [related to team member fraud] each year[.]"<sup>2439</sup>

In August 2013, Mr. Bacon again sent the members of the TMMEC information showing that, in 2012, about half of the 7,000+ EthicsLine complaints investigated by Corporate Investigations related to sales integrity violations and that the number of sales integrity cases had increased from 2012 to 2013.<sup>2440</sup>

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<sup>2432</sup> EC MSD Ex. 268 (Report of NBE Crosthwaite) at ¶80.

<sup>2433</sup> *Id.*

<sup>2434</sup> *Id.*

<sup>2435</sup> *Id.* at ¶81.

<sup>2436</sup> *Id.*

<sup>2437</sup> *Id.*

<sup>2438</sup> Quoting Team Member Misconduct Executive Committee Charter, at 1 (May 2012) (OCC-WF-SP-07038231).

<sup>2439</sup> EC MSD Ex. 268 (Report of NBE Crosthwaite) at ¶82.

<sup>2440</sup> *Id.* at ¶83.

Mr. Bacon specifically highlighted the following misconduct considerations for the TMMEC, stating:

- Does practice or process create a need or an opportunity for misconduct?
- Are controls allowing too much opportunity?
- Is the LOB [Line of Business] creating an environment whereby the TM [Team Member] must commit misconduct?
- Too much opportunity or too much personal or business pressure can sway most anyone.<sup>2441</sup>

Respondent Julian himself admitted in his sworn statement before the OCC that he was informed of the sales practices misconduct problem by various sources, including Corporate Investigations, the TMMEC, the Ethics Committee, and news articles, beginning in 2012.<sup>2442</sup>

Mr. Bacon reported to the Ethics Committee, including Respondent Julian, in August 2013 that “Sales Integrity issues are most prevalent – there needs to be continued focus in this area” and that most EthicsLine reports are “associated with Sales Integrity Issues.”<sup>2443</sup> Respondents Julian and McLinko read the 2013 Los Angeles Times articles and were, in Examiner Crosthwaite’s opinion, therefore aware that the allegations of sales practices misconduct were widespread across multiple states.<sup>2444</sup>

In an April 9, 2014 Enterprise Risk Management Committee meeting, Community Bank leadership informed the committee, including Respondent Julian, that one to two percent of Community Bank employees (1,000 to 2,000) were terminated each year for sales practices-related wrongdoing.<sup>2445</sup>

The Enterprise Risk Management Committee oversees the management of all types of risk across Wells Fargo.<sup>2446</sup> Enterprise Risk Management Committee members, including Respondent Julian, were responsible for understanding and evaluating risk, addressing escalated issues, and providing active oversight of risk mitigation.<sup>2447</sup> The Enterprise Risk Management Committee could escalate any issue to the Operating Committee or the CEO and reported quarterly to the Operating Committee and Risk Committee of the Board of Directors.<sup>2448</sup>

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<sup>2441</sup> EC MSD Ex. 268 (Report of NBE Crosthwaite) at ¶83.

<sup>2442</sup> *Id.* at ¶84.

<sup>2443</sup> *Id.*

<sup>2444</sup> *Id.*

<sup>2445</sup> *Id.*

<sup>2446</sup> *Id.* at ¶94.

<sup>2447</sup> *Id.*

<sup>2448</sup> Citing Wells Fargo, Risk Management Framework, 2<sup>nd</sup> Edition (July 2014) (OCC-WF-SP-04791987).

The Enterprise Risk Management Committee identified for the Board sales practices as a significant enterprise risk beginning in January 2014; however the description of the risk was lacking in that it provided no information about the root cause, scope, or duration of the sales practices misconduct problem.<sup>2449</sup> It did not describe the problem as systemic.<sup>2450</sup> It merely stated that management is discussing the risk and that addressing the risk is key.<sup>2451</sup>

Examiner Smith reported that information provided to the Board should give directors a complete and accurate overview of the Bank's condition, activities, and issues.<sup>2452</sup> Management is responsible for being transparent and providing sufficient information to allow the directors to ask questions and challenge management.<sup>2453</sup> Examiner Smith opined that the Enterprise Risk Management Committee's identification of sales practices as a significant risk in January 2014 did not constitute adequate escalation, was not sufficiently transparent, and Respondent Julian did not adequately address the risk of sales practices misconduct on the Bank.<sup>2454</sup>

The Ethics Committee was responsible for the content of the Code of Ethics, which contained a section on sales incentive programs, and overseeing the policy and interpretation of the Code.<sup>2455</sup> The Code provides, "Steering a customer to an inappropriate or unnecessary product to receive sales credit harms the customer; it is an unacceptable practice . . . Any form of 'gaming' to receive compensation, to meet sales goals, or for any other reason is in direct violation of company policy and this Code."<sup>2456</sup>

The members of the Ethics Committee, including Respondent Julian, regularly received information about the sales practices misconduct problem.<sup>2457</sup> For example, the minutes of the August 22, 2013 meeting state the Community Bank has the most EthicsLine complaints at the Bank with "most associated with Sales Integrity Issues."<sup>2458</sup> The minutes further state: "Sales Integrity issues are most prevalent – there needs to be continued focus in this area."<sup>2459</sup>

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<sup>2449</sup> EC MSD Ex. 267 (Report of NBE Smith) at ¶95.

<sup>2450</sup> *Id.*

<sup>2451</sup> *Id.*, citing Memo from the Enterprise Risk Management Committee, Significant Enterprise Risks (Jan. 22, 2014) (OCC-WFSP-08672449).

<sup>2452</sup> EC MSD Ex. 267 (Report of NBE Smith) at ¶95.

<sup>2453</sup> *Id.*, citing The Director's Book: Role of Directors for National Banks and Federal Savings Associations, at 40 (July 2016).

<sup>2454</sup> EC MSD Ex. 267 (Report of NBE Smith) at ¶95.

<sup>2455</sup> *Id.* at ¶100.

<sup>2456</sup> *Id.*, quoting Wells Fargo Team Member Code of Ethics and Business Conduct (OCC-WF-SP-04455174).

<sup>2457</sup> EC MSD Ex. 267 (Report of NBE Smith) at ¶101.

<sup>2458</sup> *Id.*

<sup>2459</sup> *Id.*, quoting Ethics Committee Meeting Minutes (Aug. 22, 2013) (OCC-WF-SP-06727216).



Examiner Smith opined that Respondent Julian took no meaningful actions in response to receiving information that thousands of employees each year submitted EthicsLine complaints (*i.e.* the complainants were blowing the whistle) about sales practices misconduct at the Bank, despite the facts that: (1) sales practices misconduct was a violation of the Code of Ethics and they were responsible for it; and (2) they were supposed to provide leadership, oversight, and direction related to sales practices misconduct as members of the Team Member Misconduct Executive Committee.<sup>2460</sup>

Examiner Smith opined that Respondent Julian failed to fulfill their respective responsibilities as members of the Enterprise Risk Management Committee, Ethics Committee, and Team Member Misconduct Executive Committee.<sup>2461</sup> It was her opinion that Respondent Julian’s failures perpetuated the existence of the Bank’s sales practices misconduct problem and constituted unsafe or unsound practices and breaches of their fiduciary duties,<sup>2462</sup> and recklessly engaged in the aforementioned unsafe or unsound practices.<sup>2463</sup>

Respondents Julian and McLinko also received information that the Community Bank and the Group Risk Officer, Ms. Russ Anderson, was unable or unwilling to adequately address the sales practices issues.<sup>2464</sup> In July 2012, the Chief Security Officer informed Respondents Julian and McLinko that the Community Bank’s data “continues to highlight a concerning trend in the area of sales integrity” and that Community Bank Group Risk Officer Claudia Russ Anderson was “minimizing the negative information being submitted to executive management.”<sup>2465</sup>

The Chief Security Officer detailed the concerning data “from the increase in EthicsLine reports, to the increase in executive complaint letters/OCC referrals, and increases in confirmed fraud, thus, we need to continue to escalate this issue with senior leadership.”<sup>2466</sup> The Chief Security Officer emphasized that the “data continues to point to a very negative trend” and that Respondent Russ Anderson “often challenges the Audit and [Corporate Security] A&E reporting verbiage.”<sup>2467</sup>

Respondent McLinko testified before the OCC that based on all the information he reviewed, including the data, analysis, and modeling, it was evident that thousands of Bank employees issued millions of products and services without customer consent:

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<sup>2460</sup> EC MSD Ex. 267 (Report of NBE Smith) at ¶102.

<sup>2461</sup> *Id.* at ¶103.

<sup>2462</sup> *Id.*

<sup>2463</sup> *Id.* at ¶104.

<sup>2464</sup> EC MSD Ex. 268 (Report of NBE Crosthwaite) at ¶87.

<sup>2465</sup> *Id.*

<sup>2466</sup> *Id.*

<sup>2467</sup> *Id.*

Q [by Enforcement Counsel]: Okay. And based on what you have seen and all the information you gathered, those thousands of Wells Fargo employees have issued millions of products and services without customers' consent?

MR. CRUDO [Counsel for Mr. McLinko]: [Objection as to] Foundation.

A [by Mr. McLinko]: Based upon the data that was produced, on the filing of the data analysis that's done, and the modeling, yes.<sup>2468</sup>

Respondent McLinko served on the Community Banking Risk Management Committee from at least 2014 until August 2016.<sup>2469</sup> The CBRMC was responsible for understanding the Community Bank's "operational risk profile and [] work[ing] with management across Community Banking to ensure risks are managed effectively."<sup>2470</sup> Respondent McLinko explained in an email he drafted for Respondent Julian that "audit['] methodology includes contacting Corporate Investigations at the beginning of each audit to determine if there are any cases/trends related to the area under review."<sup>2471</sup>

In January 2011, Mr. Bacon informed Respondent McLinko: "Community Bank sales integrity issue has resulted in two arrests."<sup>2472</sup> This is highly unusual but reinforces the fact that this type of activity is unlawful and certainly poses a significant reputation risk to our company."<sup>2473</sup>

In February 2011, Corporate Investigations met with Audit and informed auditors on case volumes and trends related to sales practices, including the number of terminations and cases and that, "customer consent" was the number one issue.<sup>2474</sup> Corporate Investigations also informed Audit that some of the Community Bank's controls with respect to sales practices amounted to "the fox guarding the hen house."<sup>2475</sup>

In July 2011, Mr. Bacon again informed Respondent McLinko, "[s]ales Integrity cases continue to surge."<sup>2476</sup> In July 2012, he again informed Respondent McLinko that the Bank's data "continues to highlight a concerning trend in the area of [s]ales [i]ntegrity – from the increase in EthicsLine reports, to the increase in executive complaint letters/OCC referrals, and

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<sup>2468</sup> EC MSD Ex. 268 (Report of NBE Crosthwaite) at ¶88.

<sup>2469</sup> *Id.* at ¶89.

<sup>2470</sup> *Id.*

<sup>2471</sup> *Id.* at ¶90.

<sup>2472</sup> *Id.* at ¶91.

<sup>2473</sup> *Id.*

<sup>2474</sup> *Id.* at ¶92.

<sup>2475</sup> *Id.*

<sup>2476</sup> *Id.* at ¶93.

increases in confirmed fraud” and that Respondent Russ Anderson “minimiz[ed] the negative information being submitted to executive management.”<sup>2477</sup> Mr. Bacon concluded: “we need to continue to escalate this issue with senior leadership” and stated the data “continues to point to a very negative trend.”<sup>2478</sup>

In January 2013, an auditor who reported to Respondent McLinko told him that sales integrity “is still [the Chief Security Officer’s] #1 concern.”<sup>2479</sup> In that same email, the auditor wrote, “I questioned [Mr. Bacon] as to whether they had discussed root cause for some of the items listed above and was it related to sales pressure. He said he felt a lot of it was related to the sales goals and pressure. He feels there’s an issue that [Regional Bank] is trying to work through but not a lot of people want to address it with [Respondent Tolsted].”<sup>2480</sup>

Respondent McLinko also was aware of the Los Angeles Times articles at the end of 2013. Mr. Bacon emailed him the first article and explained it was a “big deal[.]”<sup>2481</sup>

Examiner Crosthwaite reported that Respondent Julian himself asked his staff in a September 2016 email about sales practices misconduct: “Where was audit while this activity was taking place? To be honest, I’m not sure how to answer this but am sure the A[udit and] E[xamination] Committee will and should be asking.”<sup>2482</sup> Respondent Julian testified that he never received a “good answer about where was audit.”<sup>2483</sup>

Examiner Crosthwaite opined that Respondent Julian could offer no reasonable explanation for Audit’s failure to detect and escalate the sales practices misconduct problem.<sup>2484</sup> She further reported that this is consistent with Bank documents that show Respondent Julian did not receive an acceptable answer when he asked his staff, including Respondent McLinko, in September 2016: “where was audit while this activity was taking place?”<sup>2485</sup> She reported that no one, including Respondent McLinko, responded with any of the arguments that Respondents Julian and McLinko now advance in the present litigation.<sup>2486</sup>

Examiner Candy opined that Respondent Julian’s and Respondent McLinko’s respective conduct subjected the Bank to abnormal risk or loss or damage to the Bank.<sup>2487</sup> She opined that

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<sup>2477</sup> EC MSD Ex. 268 (Report of NBE Crosthwaite) at ¶94.

<sup>2478</sup> *Id.*

<sup>2479</sup> *Id.* at ¶95.

<sup>2480</sup> *Id.*

<sup>2481</sup> *Id.* at ¶96.

<sup>2482</sup> *Id.* at ¶97.

<sup>2483</sup> *Id.*

<sup>2484</sup> *Id.*

<sup>2485</sup> *Id.*

<sup>2486</sup> *Id.*

<sup>2487</sup> EC MSD Ex. 269 (Report of NBE Candy) at ¶135.

their respective failures to detect sales practices issues in a timely and fulsome manner and review sales practices created undue legal, compliance, and reputational risks, and risk of customer and team member harm – the very risks that Audit was supposed to be auditing.<sup>2488</sup> She opined that the failure to identify the problem in any audit also perpetuated the problem and caused actual loss to the Bank.<sup>2489</sup>

### **Respondent Julian’s and Respondent McLinko’s Respective Conduct in Failing to Fulfill Their Job Responsibilities was Recklessly Unsafe or Unsound Conduct**

Examiner Coleman reported that the Bank has three lines of defense that are responsible for identifying, measuring, monitoring, and controlling risk.<sup>2490</sup> He reported that the first line of defense is composed of the Bank’s risk-generating business units like the Community Bank.<sup>2491</sup> The second line of defense is composed of the Bank’s independent risk management functions such as Corporate Risk.<sup>2492</sup> Wells Fargo Audit Services (“WFAS” or “Audit”) is the third line of defense.<sup>2493</sup>

Examiner Coleman reported that as the third line of defense, the internal audit function assesses the effectiveness of the policies, processes, personnel, and control systems created in the first and second lines of defense, citing the 2003 and 2016 Internal and External Audits Handbook.<sup>2494</sup>

Examiner Crosthwaite reported that the evaluation of controls was within the purview of Audit’s responsibilities:

The effectiveness of internal controls is assessed through the bank’s risk reviews (often second line of defense) and audit program (third line of defense) . . . Audit programs are the independent control function that verifies the effectiveness of the bank’s risk management system. Unlike risk reviews, audit managers and the board should make decisions regarding the audit program to maintain appropriate independence.<sup>2495</sup>

Examiner Hudson reported that the primary responsibility of the internal audit function is to provide independent assurance and challenge.<sup>2496</sup> She reported that as the third line of defense, the internal audit function assesses the effectiveness of the policies, processes, personnel, and

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<sup>2488</sup> EC MSD Ex. 269 (Report of NBE Candy) at ¶135.

<sup>2489</sup> *Id.*

<sup>2490</sup> EC MSD Ex. 257 (Report of NBE Coleman) at ¶18.

<sup>2491</sup> *Id.*

<sup>2492</sup> *Id.*

<sup>2493</sup> *Id.*

<sup>2494</sup> *Id.*

<sup>2495</sup> EC MSD Ex. 268 (Report of NBE Crosthwaite) at ¶98.

<sup>2496</sup> EC MSD Ex. 270 (Report of NBE Hudson) at ¶28,

control systems created in the first and second lines of defense.<sup>2497</sup> She reported that the fact that under Respondent McLinko’s leadership Audit had not conducted a comprehensive review of sales practices and control systems concerned her, because it raised questions about Audit’s ability to detect risk, which is an important aspect of Audit’s role.<sup>2498</sup>

During a February 9, 2015 call, Respondent Russ Anderson reported to the OCC that the Community Bank group risk function had a “good partnership with Audit.”<sup>2499</sup> This statement also raised concerns for Examiner Hudson regarding Respondent McLinko’s independence in his role as the Executive Audit Director.<sup>2500</sup> This statement and the prior interjection of Ms. Russ Anderson on the audit call raised concerns for Examiner Hudson regarding the independence of the Audit function generally.<sup>2501</sup>

Internal audit, according to Examiner Hudson, is required to maintain independence both in appearance and in fact and not be influenced by the lines of business that internal audit is supposed to be auditing.<sup>2502</sup> A lack of independence by an audit function is concerning as it could result in strategic decisions that increase business line risks through ineffective policies, procedures, and controls contrary to the bank’s risk appetite.<sup>2503</sup>

Based on her experience, training, and commission as a National Bank Examiner, and her participation and interaction with Audit in the February 2015 Exam, Examiner Hudson opined that Audit lacked independence.<sup>2504</sup> She opined that Audit’s failure to be fully independent posed an elevated risk to the Bank because it affected Audit’s ability to detect and document risks and required corrective actions, and therefore hindered the Bank’s ability to fully address risk.<sup>2505</sup>

From her participation and interaction with Audit in the February 2015 Exam, Examiner Hudson opined that she did not believe that Audit, under Respondents McLinko’s and Julian’s leadership, acted with appropriate professional skepticism toward the Community Bank and its managers.<sup>2506</sup>

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<sup>2497</sup> EC MSD Ex. 270 (Report of NBE Hudson) at ¶28, citing Comptroller’s Handbook, Internal and External Audits (Apr. 2003) (OCC-SP0103885).

<sup>2498</sup> EC MSD Ex. 270 (Report of NBE Hudson) at ¶29.

<sup>2499</sup> *Id.* at ¶30.

<sup>2500</sup> *Id.*

<sup>2501</sup> *Id.*

<sup>2502</sup> *Id.*, citing Office of the Comptroller of the Currency, Comptroller’s Handbook, Internal and External Audits, at 23 (April 2003).

<sup>2503</sup> EC MSD Ex. 270 (Report of NBE Hudson) at ¶30.

<sup>2504</sup> *Id.* at ¶31.

<sup>2505</sup> *Id.*

<sup>2506</sup> *Id.* at ¶32.

## **Respondents Julian and McLinko Awarded the Community Bank the Highest Possible Audit Ratings While its Team Members Engaged in Widespread and Systemic Sales Practices Misconduct**

Examiner Smith reported that well-planned, properly structured auditing programs are essential to effective risk management and internal control systems.<sup>2507</sup> She reported that effective internal and external audit programs are also a critical defense against fraud and provide vital information to the board of directors about the effectiveness of internal control systems.<sup>2508</sup> She reported that this was underscored by the fact that the head of Audit reported directly to the Board through the Audit & Examination Committee.<sup>2509</sup>

Examiner Smith reported that the scope of Audit's work "is to determine if the Company's risk management, systems of controls, and governance processes are adequate and functioning as intended."<sup>2510</sup> She reported that Respondent Julian and his staff, including Respondent McLinko, were responsible for escalating significant weakness and deficiencies in internal controls, risk management, and governance to the Audit & Examination Committee of the Board of Directors weaknesses.<sup>2511</sup> She reported that Audit's work was critical "to improve the effectiveness of [the Bank's] risk management, control and governance processes, their adherence to relevant regulatory guidelines, and appropriateness for Wells Fargo's size, business mix, and risk profile."<sup>2512</sup>

In July 2012, Michael Bacon, the Chief Security Officer and Head of Corporate Investigations informed Respondents Julian and McLinko: "[O]ur data continues to highlight a concerning trend in the area of Sales Integrity – from the increase in EthicsLine reports, to the increase in executive complaint letters / OCC referral, and increases in confirmed fraud, thus, we need to continue to escalate this issue with senior leadership. Our data continues to point to a very negative trend."<sup>2513</sup>

Mr. Bacon also informed Respondent Julian in the email that Respondent Russ Anderson, the Community Bank's Group Risk Officer, was "minimizing" the seriousness of the

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<sup>2507</sup> EC MSD Ex. 267 (Report of NBE Smith) at ¶121.

<sup>2508</sup> *Id.*

<sup>2509</sup> *Id.*

<sup>2510</sup> *Id.* at ¶122.

<sup>2511</sup> *Id.*

<sup>2512</sup> *Id.*, quoting Wells Fargo, Risk Management Framework, 2nd Edition (July 2014) (OCC-WF-SP-04791987); Wells Fargo Audit Services, Second Quarter 2014 Summary, at 8 (Aug. 4, 2014) (OCC-SP0811518).

<sup>2513</sup> EC MSD Ex. 267 (Report of NBE Smith) at ¶123, quoting E-mail from Bacon to McLinko, Julian et al., HIGHLY CONFIDENTIAL - review & discard - FW: Follow-up - Regional Banking Cash Negotiables Investigations Key Activity Report thru 2Q (OCC-WF-SP-06076643).

problem to executive management.<sup>2514</sup> In January 2013, Mr. Bacon informed Audit, including Respondent McLinko, that sales integrity was still his #1 concern.<sup>2515</sup> During the February 9, 2015 Call, Audit told the OCC, “no significant coverage gaps were identified” concerning Audit’s coverage of the Community Bank.<sup>2516</sup> That was Audit’s conclusion that was communicated to the OCC.<sup>2517</sup>

Respondent Julian informed the OCC in May 2015, “Our audit methodology includes contacting Corporate Investigations at the beginning of each audit to determine if there are any cases/trends related to the area under review.”<sup>2518</sup> Respondent Julian admitted in his sworn testimony that any competent auditor would have followed up on the information that he and his Audit group in fact received in real time.<sup>2519</sup> Respondent Julian also admitted that if an auditor received such information and failed to investigate further, then such an auditor would not be doing his job.<sup>2520</sup> Examiner Smith agreed with Respondent Julian’s assessment on this point.

Examiner Smith reported that notwithstanding all the information Respondents Julian and McLinko received about sales practices misconduct in the Community Bank, Audit did not follow up on the information, and as a result, continued to award the Community Bank the highest possible ratings year after year.<sup>2521</sup> She opined that Respondent Julian’s and Respondent McLinko’s failure to identify and escalate the systemic sales practices misconduct problem, including their failure to document the significant sales practices risk management and internal controls weaknesses in any audit report, perpetuated the existence of the Bank’s sales practices misconduct problem for many years and was an unsafe or unsound practice and breach of their fiduciary duty.<sup>2522</sup>

She further opined that that Respondent Julian failed to adequately supervise the Audit Department and failed to escalate issues to his direct supervisor, the Chair of the Audit and

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<sup>2514</sup> EC MSD Ex. 267 (Report of NBE Smith) at ¶123, quoting E-mail from Bacon to McLinko, Julian et al., HIGHLY CONFIDENTIAL - review & discard - FW: Follow-up - Regional Banking Cash Negotiables Investigations Key Activity Report thru 2Q (OCC-WF-SP-06076643).

<sup>2515</sup> EC MSD Ex. 267 (Report of NBE Smith) at ¶124, citing Email from Deese to McLinko, Recap of Meeting with Bacon (Jan. 3, 2013) (OCC-WF-SP-08880999).

<sup>2516</sup> EC MSD Ex. 270 (Report of NBE Hudson) at ¶32, citing Meeting Notes from Kevin Swanson to Karin Hudson (Feb. 9, 2015) (OCC-SP0333218).

<sup>2517</sup> EC MSD Ex. 270 (Report of NBE Hudson) at ¶32.

<sup>2518</sup> EC MSD Ex. 267 (Report of NBE Smith) at ¶125, quoting E-mail from Julian to Grover et al., Audit Coverage of Sales Practices (OCC-WF-SP-06969110).

<sup>2519</sup> EC MSD Ex. 267 (Report of NBE Smith) at ¶126, quoting Sworn Statement of Respondent Julian at 167:18-171:4; 263:6-22 (May 31, 2018) (OCC-SP00046063).

<sup>2520</sup> EC MSD Ex. 267 (Report of NBE Smith) at ¶126, citing Sworn Statement of Respondent Julian at 167:18-171:4; 263:6-22 (May 31, 2018) (OCC-SP00046063).

<sup>2521</sup> EC MSD Ex. 267 (Report of NBE Smith) at ¶127.

<sup>2522</sup> *Id.* at ¶128.

Examination Committee, thereby ensuring that the Board was not made aware of the issues by the independent third line of defense.<sup>2523</sup> Examiner Smith opined that these failures perpetuated the existence of the sales practices misconduct problem and constituted unsafe or unsound practices and breaches of his fiduciary duty.<sup>2524</sup>

She further opined that Respondents Julian and McLinko recklessly engaged in the aforementioned unsafe or unsound practices.<sup>2525</sup>

Examiner Hudson reported that as part of scoping OCC examinations, examiners review previous audit reports.<sup>2526</sup> As with other examinations, the OCC reviewed previous audit reports during the February 2015 Exam with respect to Audit's coverage of cross sell and sales practices in the Community Bank.<sup>2527</sup> Based on Examiner Hudson's training and experience as a National Bank Examiner reviewing internal audit programs, audit should conduct a risk assessment and devise an audit scope and testing that would accurately identify and document risk in audit reports.<sup>2528</sup>

Examiner Hudson reported that Audit testing should incorporate areas that pose risk to the Bank and accurately and completely assess such risks and recommend corrective action.<sup>2529</sup> From her participation in the February 2015 Exam and review of audit reports, Examiner Hudson concluded that none of Audit's reports covered sales practices in the manner one would have expected given the significant risks, nor did the reports identify any concerns with the sales model and its impact on employee misconduct and employee terminations.<sup>2530</sup>

Examiner Crosthwaite reported that in July 2015, the OCC communicated to the Bank that it had failed to satisfy the safety and soundness standards contained in the OCC's Guidelines Establishing Heightened Standards for Certain Large Insured National Banks.<sup>2531</sup> She reported that through this communication, the OCC highlighted deficiencies with Audit and required Respondent Julian to, among other things, "develop audit programs that test the first line of defense compliance with high risk laws and regulations and report internal audit identified deficiencies to the Bank's Audit and Examination Committee along with the severity of the deficiency and the corrective actions."<sup>2532</sup>

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<sup>2523</sup> EC MSD Ex. 267 (Report of NBE Smith) at ¶129.

<sup>2524</sup> *Id.*

<sup>2525</sup> *Id.* at ¶130.

<sup>2526</sup> *Id.* at ¶32.

<sup>2527</sup> *Id.*

<sup>2528</sup> *Id.*

<sup>2529</sup> *Id.*

<sup>2530</sup> *Id.*

<sup>2531</sup> EC MSD Ex. 268 (Report of NBE Crosthwaite) at ¶99

<sup>2532</sup> *Id.*



Examiner Crosthwaite opined that it was recklessly unsafe or unsound for the Respondents Julian and McLinko to continue awarding the Community Bank the highest possible audit rating, even after the sales practices misconduct problem was the subject of two Los Angeles Times articles in the Fall of 2013; after the City of Los Angeles filed a lawsuit against the Bank in May of 2015; and after the OCC issued five Matters Requiring Attention with respect to sales practices on June 2015.<sup>2533</sup>

In support of this opinion, Examiner Crosthwaite specifically noted the following:

a. During all the years that Respondents Julian and McLinko served in their respective positions, Audit consistently rated the Community Bank as effective—the highest possible grade.

b. WFAS and Respondents Julian and McLinko issued these “effective” ratings even when they received information indicating that the sales practices problem had grown to an unmanageable level.

c. WFAS rated the Regional Banking and Business Banking Compliance Program as “effective” in December 2013, when the Los Angeles Times published its second article on the Bank’s sales practices.

d. In June 2015, the OCC issued five MRAs related to sales practices. One MRA required Audit to “reassess their coverage of sales practices and provide an enterprise view.” In response to the MRA, Audit indicated that it was committed to maintaining independence and developing a comprehensive audit approach with respect to sales practices. The response to the MRA designated Respondent McLinko as the “accountable executive.”

The commitments for which Respondent McLinko was the “accountable executive” included being “engaged with the various LOBs (lines of business) as they develop and implement corrective actions to the Enterprise Sales Practices MRA’s. . . . Issue monitoring and validation, reviewing governance processes and enhanced policy, monitoring of projects/initiatives to enhance Enterprise Sales Practices compliance, and obtaining an understanding of key activities and functions performed to ensure compliance with enterprise sales practices along with their sustainability.” Notwithstanding all of the commitments which Audit made, and for which Respondent McLinko was the “accountable executive,” the Community Bank audit team under Respondent McLinko’s leadership continued to award high ratings to the Community Bank.

e. WFAS Audit rated the Community Bank’s internal controls for customer account opening as “effective” as late as March 2016, after the Los Angeles City Attorney’s lawsuit and the OCC’s issuance of five MRAs from

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<sup>2533</sup> EC MSD Ex. 268 (Report of NBE Crosthwaite) at ¶100.

the OCC.” During my time as ERM Lead, WFAS never rated the Community Bank as anything less than “effective” until 2017, following public backlash over the Bank’s sales practices.<sup>2534</sup>

Examiner Crosthwaite opined that the Chief Auditor should know whether Community Bank’s internal controls were adequate, whether any business operations in Community Bank were causing violations of laws, regulations, or Bank policies, and whether management was taking appropriate steps to address control deficiencies.<sup>2535</sup> Although the extent of the sales practices misconduct problem, as is illustrated by PwC’s estimation of 3.5 million potentially unauthorized accounts, was alarming, it should not have been a surprise to senior executives such as Respondents Julian and McLinko who had regular and immediate access to sales integrity data.<sup>2536</sup>

Examiner Crosthwaite reported that Respondent Julian was responsible for ensuring that WFAS performed its duties objectively and independent of the lines of business.<sup>2537</sup> She opined that Respondent Julian failed to meet the expectations the OCC set and communicated for all internal auditors.<sup>2538</sup> She reported that despite knowledge about Respondent Russ Anderson’s lack of transparency and the Community Bank’s failure to address the sales practices problem, Respondents Julian and McLinko both failed to challenge the Community Bank in any capacity.<sup>2539</sup>

Examiner Crosthwaite reported that in his role as Chief Auditor, Respondent Julian was required to assess executive compensation and recommend reduction or negative impacts to compensation if there were deficiencies in risk management or other executive misconduct.<sup>2540</sup> She reported that Respondent Julian acknowledged, “Audit provided information in connection with annual incentive compensation risk memoranda and that memoranda were provided to the Human Resources Committee of the Board.”<sup>2541</sup> Examiner Crosthwaite reported that Respondent Julian was asked to consult and determine whether there needed to be any impacts to executive compensation due to sales practices misconduct, and thereafter assessed a rating of “satisfactory” for sales practices in 2014, 2015, and 2016.<sup>2542</sup>

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<sup>2534</sup> EC MSD Ex. 268 (Report of NBE Crosthwaite) at ¶100.

<sup>2535</sup> *Id.* at ¶101.

<sup>2536</sup> *Id.*

<sup>2537</sup> *Id.* at ¶102.

<sup>2538</sup> *Id.*

<sup>2539</sup> *Id.*

<sup>2540</sup> *Id.* at ¶103.

<sup>2541</sup> *Id.* at ¶103.

<sup>2542</sup> *Id.* at ¶104.

Examiner Crosthwaite reported that “Satisfactory” was the highest possible assessment. She reported that Respondent Julian did not recommend any impacts to Respondent Tolstedt’s compensation due to sales practices contrary to real-time information he had received about the sales practices misconduct problem.<sup>2543</sup> Examiner Crosthwaite opined that these ratings inaccurately signaled to the CEO and the Board that the Community Bank’s management over sales practices risk was appropriate and should have no negative impact on senior management’s incentive compensation.<sup>2544</sup> She opined that it was recklessly unsafe or unsound for Respondent Julian to maintain the level of compensation for senior executives he knew or should have known contributed to the problem.<sup>2545</sup>

Examiner Crosthwaite opined that Respondent Julian breached his fiduciary duty and engaged in an unsafe or unsound practice by failing to accurately assess and appropriately incorporate risk events in incentive compensation recommendations for material risk takers and executives at the Bank from 2014 through 2016.<sup>2546</sup> She also expressed the concern that although the Community Bank’s problems have been common knowledge for many years, Respondents Julian and McLinko deny the existence of any serious or systemic problem with sales practices misconduct in the Community Bank even now.<sup>2547</sup>

Examiner Candy concluded that Respondents Julian and McLinko disregarded known and obvious risk of substantial harm to the Bank caused by sales practices misconduct.<sup>2548</sup> She opined that both Respondents failed to act appropriately to address or mitigate risk of substantial harm to the Bank, irrespective of the information and data supplied to them about the extent and root cause of the problem over the course of their tenures.<sup>2549</sup>

It is Examiner Candy’s opinion as a National Bank Examiner that Respondent Julian recklessly engaged in an unsafe or unsound practice by failing to accurately assess and appropriately incorporate risk events in incentive compensation recommendations for material risk takers and executives at the Bank from 2014 through 2016.<sup>2550</sup> She reported that annual memoranda from 2014 through 2016 rated the Community Bank’s risk management in connection with sales practices as “satisfactory,” the highest possible assessment.<sup>2551</sup> It also is

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<sup>2543</sup> EC MSD Ex. 268 (Report of NBE Crosthwaite) at ¶104.

<sup>2544</sup> *Id.*

<sup>2545</sup> *Id.* at ¶105.

<sup>2546</sup> *Id.* at ¶106.

<sup>2547</sup> *Id.* at ¶107.

<sup>2548</sup> EC MSD Ex. 269 (Report of NBE Candy) at ¶136.

<sup>2549</sup> *Id.*

<sup>2550</sup> *Id.* at ¶137.

<sup>2551</sup> *Id.*

her opinion that Respondent Julian's and Respondent McLinko's practices and breaches constituted a pattern of misconduct.<sup>2552</sup>

### **Each Respondent Received Personal Gain or Other Benefit from Their Misconduct**

Examiner Candy opined that each Respondent's misconduct conferred personal gain or other benefit to them.<sup>2553</sup> As explained above, she reported that the sales practices misconduct problem persisted because its root cause, the unreasonable goals and extreme pressure, also was the very basis for the financial success of the business model.<sup>2554</sup> She reported that the Community Bank was the largest line of business at the Bank and was the driver of growth for the Bank and the key to its publicly touted cross-sell success.<sup>2555</sup>

Examiner Candy opined that as senior executives at the Bank, Respondents reaped the benefits of that success in the form of compensation, substantial bonuses, and long-term equity awards.<sup>2556</sup> She reported that as WFC's share price increased during their tenures, so did their effective compensation.<sup>2557</sup> Further, she reported that cash bonuses were also substantial and linked to both the Respondents' individual performance as well as the performance of the bank.<sup>2558</sup>

Examiner Smith reported that Respondents' improper actions and inactions allowed the Bank's impermissible, but profitable, sales model to continue for many years.<sup>2559</sup> As senior executives of the Bank, they benefitted financially from the unsafe and unsound business model that their misconduct preserved and perpetuated because their compensation was based in part on the Bank's financial performance.<sup>2560</sup> Upon these findings, Examiner Smith opined that the Respondents received financial gain or other benefits by reason of their misconduct.<sup>2561</sup>

### **Respondents' Misconduct Caused Financial Losses and Reputational Damage to the Bank as Well as Harm to its Customers and Employees**

Examiner Candy reported that when the sales practices scandal was publicized, the Bank suffered and continues to suffer massive financial loss and reputational damage.<sup>2562</sup> Examiner

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<sup>2552</sup> EC MSD Ex. 269 (Report of NBE Candy) at ¶138.

<sup>2553</sup> *Id.* at ¶211.

<sup>2554</sup> *Id.* at ¶212.

<sup>2555</sup> *Id.*

<sup>2556</sup> *Id.* at ¶213.

<sup>2557</sup> *Id.*

<sup>2558</sup> *Id.*

<sup>2559</sup> EC MSD Ex. 267 (Report of NBE Smith) at ¶146.

<sup>2560</sup> *Id.*

<sup>2561</sup> *Id.* at ¶147.

<sup>2562</sup> EC MSD Ex. 269 (Report of NBE Candy) at ¶214.

Smith reported that the sales practices misconduct problem caused enormous and ongoing financial losses and other damage to Wells Fargo.<sup>2563</sup> She reported that a former CEO of Wells Fargo estimated the total financial impact of sales practices misconduct on the Bank to be in the “tens of billions of dollars.”<sup>2564</sup>

Examiner Smith reported that the Bank has to date paid roughly \$3.83 billion in fines and penalties to the OCC, CFPB, City Attorney of Los Angeles, the U.S. Department of Justice, the Securities and Exchange Commission, and state Attorneys General to settle sales practices-related matters.<sup>2565</sup> She reported that the Bank has paid roughly \$622 million in civil settlements related to sales practices and expended at least \$160 million in payments to law firms and consultants in connection with sales practices.<sup>2566</sup>

Examiner Smith reported that the Bank also incurred significant expenses to rehabilitate its image and rebuild trust with its customers.<sup>2567</sup> She reported that in 2018, the Bank launched a marketing and outreach campaign, “Re-Established,” that cost the Bank hundreds of millions of dollars.<sup>2568</sup> She reported that on February 2, 2018 the Board of Governors of the Federal Reserve imposed an “asset cap” on Wells Fargo, which she opined has had a significant financial impact on the Bank by limiting the Bank’s ability to increase in asset size.<sup>2569</sup>

In its public announcement of the action, the Federal Reserve noted that the asset cap was being imposed in response “to recent and widespread consumer abuses and other compliance breakdowns by Wells Fargo”<sup>2570</sup> and that it would remain in effect until WFC sufficiently

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<sup>2563</sup> EC MSD Ex. 267 (Report of NBE Smith) at ¶148.

<sup>2564</sup> *Id.*, quoting Sworn Statement of Timothy Sloan at 260:8-261:3 (July 11, 2019) (OCC-SP00048394).

<sup>2565</sup> EC MSD Ex. 267 (Report of NBE Smith) at ¶148, citing Wells Fargo & Company, Form 10-Q, at 124-25 (Aug. 4, 2020), available at <https://www08.wellsfargomedia.com/assets/pdf/about/investor-relations/sec-filings/2020/second-quarter-10q.pdf>; Wells Fargo & Company, Form 10-Q, at 124-25 (Nov. 3, 2016), available at <https://www08.wellsfargomedia.com/assets/pdf/about/investor-relations/sec-filings/2016/third-quarter-10q.pdf>.

<sup>2566</sup> EC MSD Ex. 267 (Report of NBE Smith) at ¶148, citing Wells Fargo & Company, Form 10-Q, at 124-25 (Aug. 4, 2020), available at <https://www08.wellsfargomedia.com/assets/pdf/about/investor-relations/sec-filings/2020/second-quarter-10q.pdf>; and Declaration of Scott W. Champion (Apr. 24, 2018) (OCC-WF-SP-06584570).

<sup>2567</sup> EC MSD Ex. 267 (Report of NBE Smith) at ¶148.

<sup>2568</sup> *Id.*, citing Sworn Statement of Hope Hardison at 36:14-38:18 (Aug. 16, 2018).

<sup>2569</sup> EC MSD Ex. 267 (Report of NBE Smith) at ¶148, citing Order to Cease and Desist Issued Upon Consent Pursuant to the Federal Deposit Insurance Act, as Amended, In re Wells Fargo & Co., Docket No. 18-007-B-HC (Feb. 2, 2018) (FRB); EC MSD Ex. 658 (Report of Dr. Pocock) at ¶58.

<sup>2570</sup> EC MSD Ex. 658 (Report of Dr. Pocock) at ¶58 citing Federal Reserve Board of Governors, Press Release (Feb. 2, 2020), available at <https://www.federalreserve.gov/newsevents/pressreleases/enforcement20180202a.htm>.

improves its governance and risk management.<sup>2571</sup> She reported that as of the date of November 20, 2020, the asset cap remained in place.<sup>2572</sup>

Examiner Smith reported that the asset cap imposed on WFC is one of, if not the, costliest penalties ever.<sup>2573</sup> She reported that from February 2, 2018 through December 31, 2019:

- a. WFC's stock price declined by 16.0 percent;
- b. JPMorgan's stock price increased by 22.0 percent;
- c. Bank of America's stock price increased by 10.2 percent;
- d. Citigroup's stock price increased by 3.7 percent; and
- e. The S&P 500 Financials sector index increased by 5.0 percent.<sup>2574</sup>

Dr. Pocock reported that his stock analysis demonstrates that WFC far outperformed its peers for many years prior to September 8, 2016, and significantly underperformed its peers ever since that day.<sup>2575</sup> He opined that it would not be reasonable nor plausible to attribute this to a coincidence.<sup>2576</sup>

Examiner Smith reported that the Company's stock price has significantly lagged its peers since September 8, 2016, the date of the sales practices settlements with the OCC, CFPB, and City Attorney of Los Angeles.<sup>2577</sup> Examiner Smith also opined that the Bank subsequently suffered immense reputational damage as a result of the sales practices misconduct problem.<sup>2578</sup>

### **The Importance of the Community Bank to WFC**

WFC is a financial holding company and a bank holding company registered under the Bank Holding Company Act of 1956.<sup>2579</sup> WFC's principal business is to act as a holding company for its subsidiaries.<sup>2580</sup> As of December 31, 2019, Wells Fargo Bank, N.A. was WFC's

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<sup>2571</sup> EC MSD Ex. 658 (Report of Dr. Pocock) at ¶58.

<sup>2572</sup> *Id.*

<sup>2573</sup> *Id.*, citing American Banker, Wells Fargo asset cap is now one of the costliest bank penalties, (Aug. 24, 2020), available at <https://www.americanbanker.com/articles/wells-fargo-asset-cap-is-now-one-of-the-costliest-bank-penalties>.

<sup>2574</sup> EC MSD Ex. 267 (Report of NBE Smith) at ¶58.

<sup>2575</sup> *Id.* at ¶65.

<sup>2576</sup> *Id.*

<sup>2577</sup> *Id.* at ¶148.

<sup>2578</sup> *Id.* at ¶149.

<sup>2579</sup> EC MSD Ex. 658 (Report of Dr. Pocock) at ¶44, citing Wells Fargo & Co., Annual Report (Form 10-K) at 1 (Feb. 27, 2020).

<sup>2580</sup> EC MSD Ex. 658 (Report of Dr. Pocock) at ¶44, citing Wells Fargo & Co., Annual Report (Form 10-K) at 1 (Feb. 27, 2020).

principal subsidiary with assets of \$1.7 trillion, or 89 percent of WFC's assets.<sup>2581</sup> WFC admitted that the Community Bank "contributed more than half (and in some years more than two-thirds) of the Company's revenue from 2007 through 2016."<sup>2582</sup>

Not only did the Bank generate more than half of WFC's revenue, it also provided important synergies to all parts of the corporation.<sup>2583</sup> "The Community Bank also made referrals to other units in WFC regarding mortgages, lines of credit, credit cards, investment products (including brokerage products), insurance products, safe deposit boxes and a variety of other banking products."<sup>2584</sup>

The Bank and the OCC's Wells Fargo examination team concluded that while the cross-sell business model was the root cause of unacceptable levels of misconduct, it was also financially beneficial and increased WFC's stock price.<sup>2585</sup>

The scope of the scandal was publicized with the September 8, 2016 Announcement of the OCC's and CFPB's enforcement actions against the Bank.<sup>2586</sup> However, the Bank and OCC examiners concluded that the Bank suffered, and continues to suffer, reputational and financial harm that adversely affected WFC's stock price.<sup>2587</sup>

In testimony before the OCC, the Bank's former CEO, Timothy Sloan, testified about the financial impact of the sales practices misconduct scandal on the Bank as follows:

Q Overall, what's the best estimate that you have on the total financial impact of the sales practices scandal on the company or the bank?

A Oh it would be in the tens of billions of dollars, when you add -- the most significant impact was one that we were referring to earlier, and that was the impact of the stock price. We really missed out on recovery.<sup>2588</sup>

The stock price analysis Dr. Pocock performed provides significant evidence that the Bank and OCC examiners are correct with respect to both propositions.<sup>2589</sup> Dr. Pocock found that the Bank and its senior managers benefitted greatly from the impermissible but profitable

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<sup>2581</sup> EC MSD Ex. 658 (Report of Dr. Pocock) at ¶44, citing Wells Fargo & Co., Annual Report (Form 10-K) at 1 (Feb. 27, 2020).

<sup>2582</sup> EC MSD Ex. 658 (Report of Dr. Pocock) at ¶45, citing Deferred Prosecution Agreement at A-1.

<sup>2583</sup> EC MSD Ex. 658 (Report of Dr. Pocock) at ¶46.

<sup>2584</sup> *Id.*, citing Deferred Prosecution Agreement at A-2/

<sup>2585</sup> EC MSD Ex. 658 (Report of Dr. Pocock) at ¶47.

<sup>2586</sup> *Id.* at ¶48.

<sup>2587</sup> *Id.*

<sup>2588</sup> *Id.* at ¶49, quoting Sworn Statement of Timothy Sloan at 260:8-16 (July 11, 2019) (OCC-SP00048394).

<sup>2589</sup> EC MSD Ex. 658 (Report of Dr. Pocock) at ¶50.

cross-sell business model during the many years that the model was in effect.<sup>2590</sup> He also found, however, that the Bank suffered, and continues to suffer, staggering reputational and financial harm following the public disclosure of the Bank’s sales practices misconduct on September 8, 2016 and the scandal that ensued.<sup>2591</sup>

From his analysis, Dr. Pocock opined that there is significant evidence that the Bank and its senior managers benefitted greatly from preserving and implementing the profitable but impermissible cross-sell business model for over fourteen years, and that the Bank suffered, and is still suffering, great reputational and financial harm from the scandal, that the impermissible cross-sell business model caused.<sup>2592</sup>

Examiner Smith reported that the sales practices misconduct problem has also led to volatility in the membership of the Board of Directors and of individuals in senior executive management positions.<sup>2593</sup>

Examiner Smith reported that in 2017, the Bank fell to last place in a bank reputation survey conducted by American Banker/Reputation Institute.<sup>2594</sup> According to the American Banker, the Bank’s reputation score “went into free fall . . . [and was] by far the lowest of any bank.”<sup>2595</sup> The Bank’s own research showed that its favorability ratings significantly trailed its peers and that it remained “near the bottom” in terms of trust.<sup>2596</sup>

Examiner Smith reported that the sales practices misconduct problem also had negative business impacts on the Bank. As Ms. Mack testified, the scandal hampered the ability of the Community Bank to attract customers.<sup>2597</sup>

Examiner Smith reported that the sales practices misconduct problems are ongoing<sup>2598</sup> and have led to significant customer harm and breaches of customer trust.<sup>2599</sup> She also reported that the sales model also had a significant impact on Bank employees.<sup>2600</sup> She opined that the intentionally unreasonable sales goals and extreme pressure to meet those goals led employees to

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<sup>2590</sup> EC MSD Ex. 658 (Report of Dr. Pocock) at ¶50.

<sup>2591</sup> *Id.*

<sup>2592</sup> *Id.* at ¶66.

<sup>2593</sup> EC MSD Ex. 267 (Report of NBE Smith) at ¶150.

<sup>2594</sup> *Id.* at ¶151.

<sup>2595</sup> *Id.*

<sup>2596</sup> *Id.*, quoting 2017 reputation survey: Banks avoid the Wells Fargo drag, American Banker, Sean Sposito, (Jun. 27, 2017) available at <https://www.americanbanker.com/news/2017-bank-reputation-survey>, last accessed November 16, 2022.

<sup>2597</sup> EC MSD Ex. 267 (Report of NBE Smith) at ¶152, quoting Mack Tr. at 241:16-242:1.

<sup>2598</sup> EC MSD Ex. 267 (Report of NBE Smith) at ¶153.

<sup>2599</sup> *Id.* at ¶154.

<sup>2600</sup> *Id.* at ¶155.



engage in violations of laws (including criminal laws pertaining to fraud, identity theft, and the falsification of bank records), regulations, and Bank policy, and the Bank fired more than 5,300 employees for engaging in sales practices misconduct between 2011 and 2015.<sup>2601</sup> She reported that during that same period, over 8,100 employees were terminated from not meeting sales goals.<sup>2602</sup> Examiner Smith opined that all of the Community Bank's employees over a 14-year period were victimized by intentionally unreasonable goals and extreme pressure to meet those goals.<sup>2603</sup>

From these findings, Examiner Smith opined that Respondents' misconduct caused the Bank to suffer material financial loss and reputational damage.<sup>2604</sup> It is also her opinion that the Bank has yet to recover from the reputational damage caused by sales practices, and that the reputational harm as well as the improper sales practices resulted in actual or prospective prejudice to the Bank's depositors.<sup>2605</sup>

### **Assessment of Civil Money Penalties**

Examiner Smith reported that Respondents Russ Anderson, Julian, and McLinko were among the most senior officers of Wells Fargo, one of the largest financial institutions in the world.<sup>2606</sup> She opined that each Respondent had a unique and important responsibility with respect to the Bank's longstanding, widespread, and systemic sales practices misconduct problem.<sup>2607</sup> She reported that each Respondent knew about the problem and its root cause.<sup>2608</sup> She opined that notwithstanding this knowledge, each Respondent failed in his or her respective responsibilities.<sup>2609</sup> She opined that they failed to identify, escalate, and address the sales practices misconduct problem continuously and repeatedly for years.<sup>2610</sup> In Examiner Smith's opinion, these failures resulted in the opening of millions of unauthorized accounts, and billions

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<sup>2601</sup> EC MSD Ex. 267 (Report of NBE Smith) at ¶155, citing Consent Order, In re Wells Fargo Bank, N.A., No. 2016-CFPB-0015 (Sept. 8, 2016) (CFPB), available at [https://files.consumerfinance.gov/f/documents/092016\\_cfpb\\_WFBconsentorder.pdf](https://files.consumerfinance.gov/f/documents/092016_cfpb_WFBconsentorder.pdf); Statement of John G. Stumpf, Chairman and Chief Executive Officer, Wells Fargo & Co., Hearing before the Committee on Banking, Housing, and Urban Affairs, U.S. Senate, 114th Congress (Sept. 20, 2016) (OCC-SP0111168).

<sup>2602</sup> EC MSD Ex. 267 (Report of NBE Smith) at ¶155, citing E-mail from Matthews to Huss, USE THIS VERSION: Updated with totals: Data Request: terms due to sales performance (Sept. 27, 2016) (OCC-SP00034166).

<sup>2603</sup> EC MSD Ex. 267 (Report of NBE Smith) at ¶155.

<sup>2604</sup> *Id.* at ¶156.

<sup>2605</sup> *Id.* at ¶157.

<sup>2606</sup> *Id.* at ¶159.

<sup>2607</sup> *Id.*

<sup>2608</sup> *Id.*

<sup>2609</sup> *Id.*

<sup>2610</sup> *Id.*

of dollars of financial losses and massive reputational damage to the Bank.<sup>2611</sup> She opined that each of the Respondent’s received financial benefit as a result of the Bank’s improper sales model.<sup>2612</sup>

Examiner Candy opined that each Respondent had insight into the sales practices misconduct problem, giving rise to responsibilities that required them to take action to minimize and address the associated risks, and required that they use their authority and stature to effectuate change.<sup>2613</sup> She opined that none of the Respondents fulfilled their important responsibilities and that their conduct and failures perpetuated the sales practices misconduct problem and enabled ongoing illegal activity at the Bank.<sup>2614</sup>

Examiner Candy reported that the OCC considers a number of statutory and interagency factors in determining the amount of a civil money penalty (“CMP”) to assess to an individual.<sup>2615</sup> These include: (1) the size of the financial resources and good faith of the person; (2) the gravity of the violation; (3) the history of previous violations; (4) such other matters as justice may require; (5) evidence that the violations were intentional or committed with disregard of the law or consequences to the institution; (6) the duration and frequency of the misconduct; (7) the continuation of the misconduct after the respondent was notified or, alternatively, its immediate cessation and correction; (8) the failure to cooperate with the agency in effecting early resolution of the problem; (9) concealment of the misconduct; (10) any threat of loss, actual loss, or other harm to the institution, including harm to the public confidence in the institution, and the degree of such harm; (11) the respondent’s financial gain or other benefit from the misconduct; (12) any restitution paid by the respondent for the losses; (13) any history of previous misconduct, particularly where similar to the actions under consideration; (14) previous criticism of the institution or individual for similar actions; (15) presence or absence of a compliance program and its effectiveness; (16) tendency to engage in violations of law, unsafe or unsound practices or breaches; and (17) the existence of agreements, commitments, orders or conditions imposed in writing intended to prevent violations.<sup>2616</sup>

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<sup>2611</sup> EC MSD Ex. 267 (Report of NBE Smith) at ¶159.

<sup>2612</sup> *Id.*

<sup>2613</sup> EC MSD Ex. 269 (Report of NBE Candy) at ¶217

<sup>2614</sup> *Id.*

<sup>2615</sup> *Id.* at ¶215, citing 1818(i)(2)(G); and Federal Financial Institutions Examination Council’s (FFIEC) “Interagency Policy Regarding the Assessment of Civil Money Penalties by the Federal Financial Institutions Regulatory Agencies” transmitted in OCC Bulletin 1998-32, “Civil Money Penalties: Interagency Statement” (July 24, 1998).

<sup>2616</sup> EC MSD Ex. 257 (Report of NBE Coleman) at ¶119, citing 12 U.S.C. § 1818(i)(2)(G) and Interagency Policy Regarding the Assessment of Civil Money Penalties by the Federal Financial Institutions Regulatory Agencies, 63 Fed. Reg. 30227, (June 3, 1998).

In his review of these factors, Examiner Coleman noted that Title 12 U.S.C 1818(i) permits the assessment of a CMP on a per-violation and per-day basis.<sup>2617</sup> Title 12 U.S.C. 1818(i)(2)(B) authorizes the OCC to assess a CMP of “of not more than \$25,000 for each day during which such violation, practice, or breach continues.”<sup>2618</sup> Examiner Coleman opined that each Respondent engaged in a repeated pattern of reckless unsafe and unsound practices and breaches of their fiduciary duties over a period of many years, and calculated that even if the OCC were to assess Respondents based on a single violation over a single year, the maximum CMP would exceed \$18 million.<sup>2619</sup>

Examiner Crosthwaite reported that the OCC considers a number of statutory and interagency factors in determining the amount of a civil money penalty (“CMP”) to assess to an individual.<sup>2620</sup> She reported that one such factor is the Respondent’s ability to pay the CMP. She reported that there is no evidence that any of these Respondents lack the financial resources to pay the assessed CMP or a greater amount.<sup>2621</sup>

Examiner Crosthwaite reported that each Respondent had many opportunities to submit a personal financial statement or other evidence showing that their financial resources should mitigate the CMP but each chose not to.<sup>2622</sup> She reported that as a result, the OCC assumes the Respondents have the ability to pay CMPs in the assessed amounts.<sup>2623</sup> Even without relying on that assumption, from her review of the Respondents’ compensation information received from the Bank, Examiner Crosthwaite opined that each of the Respondents has the ability to pay the CMPs in the assessed amounts.<sup>2624</sup>

Examiner Coleman noted the assessed CMPs or even higher CMPs are appropriate to serve the purpose of deterrence.<sup>2625</sup> He reported that an important purpose of a CMP is to function as a deterrent.<sup>2626</sup> Examiner Coleman reported that each Respondent was a senior

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<sup>2617</sup> EC MSD Ex. 257 (Report of NBE Coleman) at ¶127.

<sup>2618</sup> *Id.*, noting that 12 C.F.R. § 19.240 provides for annual adjustments to this amount for inflation. “The current Tier 2 CMP maximum is \$51,222 per violation per day. The per-day maximum for violations that occurred between December 6, 2012 and November 2, 2015 is \$37,500.” *Id.*

<sup>2619</sup> EC MSD Ex. 257 (Report of NBE Coleman) at ¶127.

<sup>2620</sup> EC MSD Ex. 268 (Report of NBE Crosthwaite) at ¶131, citing 12 U.S.C. § 1818(i)(2)(G) and interagency policy.

<sup>2621</sup> EC MSD Ex. 268 (Report of NBE Crosthwaite) at ¶131.

<sup>2622</sup> *Id.*

<sup>2623</sup> *Id.*

<sup>2624</sup> *Id.*

<sup>2625</sup> EC MSD Ex. 257 (Report of NBE Coleman) at ¶130.

<sup>2626</sup> *Id.*, citing OCC PPM 5000-7, Civil Money Penalties (November 13, 2018) at 3 (“A CMP may serve as a deterrent to future violations, unsafe or unsound practices, and breaches of fiduciary duty, by the IAP or institution against which the CMP is assessed and by other IAPs and institutions.”)

executive within the Bank, accepted significant responsibility, and was well compensated.<sup>2627</sup> Given the duration and scope of sales practices misconduct problem, Examiner Coleman opined that significant penalties are necessary to deter these Respondents or others in the industry from similar misconduct.<sup>2628</sup> Examiner Coleman asserted that if CMPs are insufficient, bank officers might reasonably conclude that ignoring the harm caused by a profitable business model is the prudent and profitable course of action.<sup>2629</sup> He asserted that CMPs must be high enough to change that calculation; to encourage other bank executives to identify significant problems and escalate and address them, even if doing so may be unwelcome to their colleagues or senior management.<sup>2630</sup>

Upon consideration of all of the statutory and interagency factors, Examiner Candy opined that the CMPs in the assessed amounts are appropriate.<sup>2631</sup> Specifically, Examiner Candy opined that a CMP of at least \$5,000,000 against Respondent Russ Anderson is warranted, a CMP of at least \$2,000,000 against Respondent Julian is warranted, and a CMP of at least \$500,000 against Respondent McLinko is warranted.<sup>2632</sup> Further, she opined that *higher* CMPs against each Respondent are consistent with and supported by the evidence.<sup>2633</sup>

#### Findings of Fact

1. At all relevant times Wells Fargo Bank, N.A., Sioux Falls, South Dakota (“Bank”) is a national banking association within the meaning of 12 U.S.C. § 1813(q)(1)(A) and an “insured depository institution” as defined in 12 U.S.C. § 1813(c)(2).<sup>2634</sup>
2. Respondent Paul McLinko was employed by the Bank within six years of the filing of the Notice of Charges. Pursuant to 12 U.S.C. § 1813(u), Respondent Julian is an “institution-affiliated party” of the Bank.<sup>2635</sup>
3. The OCC is the “appropriate Federal banking agency” as that term is defined in 12 U.S.C. § 1813(q) and is authorized to initiate and maintain cease and desist and civil money penalty actions against Respondent McLinko pursuant

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<sup>2627</sup> EC MSD Ex. 257 (Report of NBE Coleman) at ¶130.

<sup>2628</sup> *Id.*

<sup>2629</sup> *Id.*

<sup>2630</sup> *Id.*

<sup>2631</sup> EC MSD Ex. 269 (Report of NBE Candy) at ¶216.

<sup>2632</sup> *Id.*

<sup>2633</sup> *Id.*

<sup>2634</sup> Respondent Claudia Russ Anderson’s Amended Answer (“Russ Anderson Amended Answer”) at ¶1) and Response to Enforcement Counsel’s Statement of Material Facts (ECSMF) at No. 1; (MSD-1 and MSD-343 at 19 (the Bank’s Board stipulating the Bank is a “national banking association” and an “insured depository institution”))

<sup>2635</sup> SD Order at 161-64; Tr. at 8458 (McLinko); McLinko Am. Answer at ¶¶ 439, 442; OCC Exh. 1710 at 0015; OCC Exh. 1713 at 0015; OCC Exh. 1714 at 0017; OCC Exh. 1715 at 0017; OCC Exh. 2321 at 0007, 0020.

to 12 U.S.C. § 1818(b) and (i). (12 U.S.C. § 1813(q)).<sup>2636</sup>

4. For purposes of the Notice of Charges, the term “sales practices misconduct” was defined as the practices of Bank employees issuing a product or service to a customer without the customer’s consent, transferring customer funds without the customer’s consent, or obtaining a customer’s consent by making false or misleading representations.<sup>2637</sup>
5. The Bank utilized different terminology over the years to describe employee misconduct that encompassed sales practices misconduct and other ethical violations, such as “sales integrity violations,” “sales incentive program violations,” and “gaming.”
6. The Bank’s Sales Quality Manual from August 2008 defined “Sales Quality” as follows. “‘Sales Quality’ is a broader term that captures all sales and referral related issues that impact customer satisfaction as well as profitability of the sale/referral for Wells Fargo. Examples could range from general product design considerations and trends to Bankers failing to disclose fees while selling a solution<sup>2638</sup> to the most serious ethical violations.”<sup>2639</sup>
7. The Bank’s Sales Quality Manual from August 2008 defined “Sales Integrity” as follows: “‘Sales Integrity’ is a narrower term used to specifically describe the subset of Sales Quality concerns that are related to unethical and/or illegal behavior on the part of individuals while selling to our customers. Sales integrity issues involve the manipulation and/or misrepresentation of sales or referrals and reporting of sales and referrals in an attempt to receive compensation or to meet sales goals. Unethical sales behavior has far-reaching impacts. It impacts customer relationships, damages relationships between Team Members, and leads to loss of revenue and reputation for the company.”<sup>2640</sup>
8. The June 2010 Corporate Security Policy Manual categorized its “sales integrity violations” case type into the following subtypes: Customer Consent, False Entries/CIP Violations, Fictitious Customer, Online Banking, Product Manipulation, Funding Manipulation, Reassignment of Sales Credit, Referrals, and Other. All sales integrity violations subtypes were listed as “656 - Defalcation/Embezzlement, and/or 18 USC 1001 & 1005, False entries/records, USA Patriot Act (CIP issues).”<sup>2641</sup>

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<sup>2636</sup>MSD-343 at 19 (the Bank’s Board stipulating the Bank is the “appropriate federal banking agency”).

<sup>2637</sup> Russ Anderson Amended Answer ¶ 4, Julian Amended Answer ¶ 4; McLinko Amended Answer ¶ 4.

<sup>2638</sup> Within the Community Bank, the term “solution” referred to Bank products and services that could be opened, issued, or provided by Bank employees, including, but not limited to deposit accounts, debit and credit cards, online bill pay and other Bank services.

<sup>2639</sup> MSD-10 at 5.

<sup>2640</sup> *Id.*

<sup>2641</sup> MSD-423 at 7-9.

9. The Bank's Sales Quality Manual from July 2014 defined sales integrity violations as "manipulations and/or misrepresentations of sales, service or referrals and reporting of sales, service or referrals in an attempt to receive compensation or to meet sales and service goals."<sup>2642</sup>
10. In a November 2012 email, Bart Deese explained the distinction between sales quality and sales integrity to Respondent McLinko as follows: "I have heard Sales Quality and Sales Integrity used interchangeably across [Community Bank]. When I think SQ/SI, I think of them together in regards to a banker trying to manipulate incentive compensation plans by recording inappropriate sales (e.g. adding debit cards to customers without consent, creating bogus accounts, etc.)."<sup>2643</sup>
11. The term "gaming" within the Bank mirrored the definition of sales integrity violations. "Sales gaming may be classified as the manipulation and/or misrepresentation of sales or sales reporting to receive or attempt to receive compensation, or to meet or attempt to meet sales goals."<sup>2644</sup> Specified types of gaming, included the following:
  - (a) "Selling products to existing customers without their knowledge (i.e. debit cards) or booking more expensive DDA products above what an actual customer requested and without their knowledge.
  - (b) Listing bogus sales referrals by use of current customer SSN's when they were never present.
  - (c) Misrepresenting products by not disclosing additional fee income items like overdraft protection.
  - (d) Signing customers up for on-line banking and bill pay without their knowledge.
  - (e) Management supplying tellers and bankers with SSN's from the Hogan system to be used as bogus referrals.
  - (f) Opening unfunded DDA's without customer knowledge and waiving fees (zero balance account auto-closes within 90 days but the sales goal is registered).
12. Altering or falsifying documents translating to increased sales (i.e.; phony referrals).<sup>2645</sup>
13. A "sales incentive program violation" is defined as the "manipulation and/or

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<sup>2642</sup> Russ Anderson Amended Answer ¶ 33; McLinko Amended Answer ¶ 33; MSD-9 at 5.

<sup>2643</sup> MSD-479.

<sup>2644</sup> MSD-2 at 1, 3.

<sup>2645</sup> MSD-557.

misrepresentation of sales or sales reporting in an attempt to receive compensation or meet sales goals. Includes inappropriate sales.”<sup>2646</sup>

14. A “case” or an “investigation” as used by the Bank’s Corporate Investigations group “is defined as an allegation of team member misconduct involving a possible violation of law or a code of ethics policy violation or information security policy violation, which has resulted in a financial loss and/or exposure or represents a significant compliance or reputational risk.”<sup>2647</sup>
15. A “systemic” problem, as used herein, refers to a problem that is inherent in the business model, operations, or culture of a bank as opposed to a problem that can be solved by terminating employees engaged in wrongdoing.
16. The Community Bank was and is the Bank’s largest line of business and houses the Bank’s retail branch network.<sup>2648</sup>
17. The Community Bank referred to its products and services as “solutions.”<sup>2649</sup>
18. The Community Bank referred to its employees as “team members.”<sup>2650</sup>
19. The Community Bank referred to its branches as “stores.”<sup>2651</sup>
20. Sales practices misconduct violated laws and regulations and harmed the Bank’s customers.<sup>2652</sup>
21. Sales practices misconduct was pervasive and widespread within the Community Bank.<sup>2653</sup>
22. During the time period relevant to the issues presented in the Notice of Charges the root cause of sales practices misconduct was the Community Bank’s business model, which imposed undue pressure on employees to meet unreasonable sales goals.<sup>2654</sup>
23. That the Bank’s controls to both prevent and detect sales practices misconduct

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<sup>2646</sup> MSD-381 at 6.

<sup>2647</sup> MSD-526 at 47; MSD-523 at 51.

<sup>2648</sup> Russ Anderson Amended Answer ¶ 2; MSD-1 at 20-21 ¶ 4; Julian Amended Answer ¶ 2; McLinko Amended Answer ¶ 2; MSD-1 at 20 ¶ 4.

<sup>2649</sup> MSD- 653 (Pyles Tr.) at 96:5-96:9; MSD-350 (Ramage Tr.) at 37:24-38:2; MSD-579 (Schulte Tr.) at 71:14-72:13.

<sup>2650</sup> MSD-266 (Russ Anderson Dep. Tr.) at 165:1-3.

<sup>2651</sup> MSD-1 at 21 ¶ 5.

<sup>2652</sup> See Russ Anderson SOF ¶¶ 257-275; 459-489; Julian and McLinko SOF ¶¶ 214-231.

<sup>2653</sup> See Russ Anderson SOF ¶¶ 214-256; Julian and McLinko SOF ¶¶ 169-213.

<sup>2654</sup> See Russ Anderson SOF ¶¶ 48-68, 124-146; Julian and McLinko SOF ¶¶ 31-116.

were inadequate.<sup>2655</sup>

24. None of Respondents' expert witnesses concludes or opines on whether the Community Bank had a systemic sales practices misconduct problem, the root cause thereof, how long that lasted, the magnitude of the problem, or how widespread it was.<sup>2656</sup>
25. None of Respondent Julian's expert witnesses concludes or opines that the sales goals in the Community Bank were reasonable.<sup>2657</sup>
26. None of Respondent Julian's expert witnesses concludes or opines that the pressure was reasonable.<sup>2658</sup>
27. None of Respondent Julian's expert witnesses concludes or opines that controls to prevent sales practices misconduct were adequate.<sup>2659</sup>
28. None of Respondent Julian's expert witnesses concludes or opines that controls to detect sales practices misconduct were adequate.<sup>2660</sup>
29. In sworn testimony before the OCC during its investigation, Respondent Julian agreed there was a systemic problem with sales practices misconduct at the Bank, and the root cause of the problem was unattainable sales goals and severe

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<sup>2655</sup> See Russ Anderson SOF ¶¶ 150-213; Julian and McLinko SOF ¶¶ 117-168.

<sup>2656</sup> See MSD-264 (Farrell Expert Report) at 5; MSD-262 (Abshier Expert Report) at 5; MSD-281 (Wilcox Expert Report) at 11; MSD-265A (Farrell Dep. Tr.) at 52:18-22; MSD-263A (Abshier Dep. Tr.) at 44:18-25, 50:15-51:12; MSD-282A (Wilcox Dep. Tr.) at 40:11-41:11; MSD-271 (Ploetz Expert Report) at 4; MSD-283A (Julian Deal Expert Report) at 8; MSD-283B (McLinko Deal Expert Report) at 8; MSD-285 (Jarrett Expert Report) at 6; see also MSD-282A (Wilcox Dep. Tr.) at 40:11-41:16; MSD-272A (Ploetz Dep. Tr.) at 16:16-22:4; MSD-286B (Jarrett Dep. Tr.) at 580:3-584:3; MSD-284A (Deal Dep. Tr.) at 116:3-119:9.

<sup>2657</sup> See MSD-271 (Ploetz Expert Report) at 4; MSD-283A (Julian Deal Expert Report) at 8; MSD-285 (Jarrett Expert Report) at 6; see also MSD-282A (Wilcox Dep. Tr.) at 40:20-23; MSD-286B (Jarrett Dep. Tr.) at 581:10-25; MSD-284A (Deal Dep. Tr.) at 118:10-17; MSD-272A (Ploetz Dep. Tr.) at 19:13-10.

<sup>2658</sup> See MSD-271 (Ploetz Expert Report) at 4; MSD-283A (Julian Deal Expert Report) at 8; MSD-283B (McLinko Deal Expert Report) at 8; MSD-285 (Jarrett Expert Report) at 6; see also MSD-282A (Wilcox Dep. Tr.) at 40:24-41:3; MSD-286B (Jarrett Dep. Tr.) at 582:3-18; MSD-284A (Deal Dep. Tr.) at 118:18-119:9; MSD-272A (Ploetz Dep. Tr.) at 21:9-21.

<sup>2659</sup> See MSD-271 (Ploetz Expert Report) at 4; MSD-283A (Julian Deal Expert Report) at 8; MSD-283B (McLinko Deal Expert Report) at 8; MSD-285 (Jarrett Expert Report) at 6; see also MSD-282A (Wilcox Dep. Tr.) at 41:4-7; MSD-286B (Jarrett Dep. Tr.) at 583:15-584:6; MSD-284A (Deal Dep. Tr.) at 122:9-19; MSD-272A (Ploetz Dep. Tr.) at 21:22-22:4.

<sup>2660</sup> See MSD-271 (Ploetz Expert Report) at 4; MSD-283A (Julian Deal Expert Report) at 8; MSD-283B (McLinko Deal Expert Report) at 8; MSD-285 (Jarrett Expert Report) at 6; see also MSD-282A (Wilcox Dep. Tr.) at 41:4-7; MSD-286B (Jarrett Dep. Tr.) at 582:20-583:13; MSD-284A (Deal Dep. Tr.) at 122:9-19; MSD-272A (Ploetz Dep. Tr.) at 21:22-22:4.



pressure on employees to meet them.<sup>2661</sup>

30. Mr. Julian now knew that the Bank gave its employees unreasonable sales goals.<sup>2662</sup> He also agreed with the OCC's assertion that, based on what was now known it would be obvious that there would be systemic sales practices misconduct.<sup>2663</sup>

31. Respondent Julian testified as follows:

Q: And as you know and as I've said earlier, our investigation is focused on the sales practice issues. And so, let me ask you: Hindsight is 20/20. Let me ask you based on what you know now today. Here we are on May 31st, 2018. Do you now believe that there was a systemic problem with sales practice misconduct at Wells Fargo? And let me define what I mean by 'systemic.' By 'systemic' I mean a problem that is inherent in the system, the business model, the culture of the bank as opposed to a problem that could be solved by terminating some individuals who are doing things they shouldn't do. With that definition, do you now believe that there was a significant systemic problem at Wells Fargo with sales practice misconduct?

A: I do.

...

Q. Is it fair to say that sitting here today based on the work that Wells Fargo's Audit Group has done, you can confidently say that Wells Fargo had systemic problem with sales practice misconduct that existed at least since 2011 where the data from Pricewaterhouse was looked at?

A. Yes. I'm just trying to differentiate the question between that – the – just the prior one. So the answer I think would be very –

Q. Yes.

A. – the same as – expanding on the same as I just said.

Q: Okay. And based on the work that Wells Fargo Audit Group did, the root cause of the sales practice misconduct was -- at least in large part --- that the goals were unattainable or unreasonable, and the pressure to meet those unattainable goals was severe. Is that fair to say?

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<sup>2661</sup> Julian Amended Answer ¶ 12; MSD-278 (Julian Tr.) at 25:1-27:3; 35:5-36:2, 40:23-41:9.

<sup>2662</sup> MSD-278 at 121:4-7.

<sup>2663</sup> Julian's ECSFM at No. 32, quoting MSD-278 at 121:20-122:5, 122:15-25.

A: Yes, I -- I -- I think that's how I would characterize it.<sup>2664</sup>

32. Respondent Julian agreed under oath that the Community Bank's sales practices problem was longstanding, and the problem that existed in the Bank up until 2016 when the Bank eliminated the sales goals.<sup>2665</sup>

33. In sworn testimony before the OCC during its investigation, Respondent McLinko testified the Community Bank had a systemic problem with sales practices misconduct, the root cause of which was pressure on employees to meet unreasonable sales goals.<sup>2666</sup>

34. In sworn testimony before the OCC during its investigation, Respondent McLinko testified as follows:

Q Let's leave it within the community bank. Do you believe that the community bank had a systemic problem with sales practice misconduct?

A From everything that I've read, in the regional bank part of the community bank, yes.

Q All right. And when you say the regional bank, what does that include?

A That's the branch environment.

Q All right. So it's all the branches in all the regions of the country?

A That's right. Yes, correct.

Q Okay. And do you have a belief on what is the cause of this problem at the bank?

MR. CRUDO: Foundation.

THE WITNESS: Based upon everything that I've read, as of now, the different reports that were issued, I would say that the sales goals and incentive processes were certainly two areas that contributed significantly to the issue, the pressure for the sales goals.<sup>2667</sup>

35. In sworn testimony before the OCC during its investigation, Respondent McLinko testified that his conclusions about the systemic nature of the sales practice misconduct problem were based on the voluminous data and comprehensive analyses reflected in the reports of the Bank's third party

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<sup>2664</sup> Julian Amended ¶ 12, 18; MSD-278 (Julian Tr.) at 24:23-25:16; 35:5-36:2.

<sup>2665</sup> MSD-278 at 200:15-19 (May 31, 2018).

<sup>2666</sup> McLinko Amended Answer ¶ 3; MSD-276 (McLinko Tr.) at 54:7-55:2, 95:19-24.

<sup>2667</sup> MSD-276 (McLinko Tr.) at 54:7-55:2.

consultants engaged to review the sales practices problem, as well as information detailed in the April 2017 Sales Practices Investigation Report published by the Independent Directors of the Board of Wells Fargo & Company, the Bank's holding company.<sup>2668</sup>

36. In sworn testimony before the OCC during its investigation, Respondent McLinko testified before the OCC that sales goals and incentives contributed significantly to the Community Bank's systemic problem with sales practices misconduct.<sup>2669</sup>
37. In sworn testimony before the OCC during its investigation, Respondent McLinko agreed in sworn testimony that the Community Bank's sales practices misconduct problem existed from at least 2004 until October 2016.<sup>2670</sup>
38. Employees engaged in numerous types of sales practices misconduct, including:
  - (a) opening and issuing unauthorized checking and savings accounts, debit cards, and credit cards;
  - (b) transferring customer funds between accounts without customer consent, a practice the Bank refers to as "simulated funding";
  - (c) misrepresenting to customers that certain products were available only in packages with other products, known as "bundling";
  - (d) enrolling customers in online banking and online bill-pay without consent, known as "pinning";
  - (e) delaying the opening of requested accounts and other products to the next sales reporting period, known as "sandbagging"; and
  - (f) accessing and falsifying personal customer account information without authorization such as customer phone numbers, home addresses, and email addresses.<sup>2671</sup>
39. In sworn testimony before the OCC, the Bank's former CEO John Stumpf testified, "learning the things I've learned here the last few days, I would agree, it was a systemic problem. . . ."

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<sup>2668</sup> MSD-276 (McLinko Tr.) at 56:8- 57:2; 57:16-21.

<sup>2669</sup> McLinko Amended Answer ¶ 19; 70; MSD-276 (McLinko Tr.) at 54:7-55:2.

<sup>2670</sup> MSD- 276 at 58:24-59:7, 93:17-22 (Mar. 2, 2018).

<sup>2671</sup> McLinko Amended Answer ¶ 8; Russ Anderson Amended Answer ¶ 8; MSD-22; MSD-23; MSD-108; MSD-225; MSD-1; MSD-2; MSD-297 (Richards Tr.) at 87:7-90:3; MSD-295 (Bacon Tr.) at 188:19-189:10; MSD-544 (Weber Tr.) at 82:24-84:12; MSD-585 (Herzberg Tr.) at 119:13-15) (McLinko Amended Answer ¶ 8; see also Russ Anderson Amended Answer ¶ 8; MSD-22; MSD-23; MSD-108; MSD-225; MSD-1; MSD-2; MSD-297 (Richards Tr.) at 87:7-90:3; MSD-295 (Bacon Tr.) at 188:19-189:10; MSD-544 (Weber Tr.) at 82:24-84:12); MSD-585 (Herzberg Tr.) at 119:13-15.

40. In sworn testimony before the OCC, the Bank's former Chief Risk Officer Michael Loughlin testified that he was "trying to translate [Enforcement Counsel's definition of systemic] into a simple phrase like widespread" and did not believe the bank had a widespread issue until at least 2015, after reviewing a report "generated by corporate investigations."<sup>2672</sup>
41. In sworn testimony before the OCC, the Bank's former Chief Administrative Officer, Hope Hardison testified that "sometime in 2013" she became "worried that there was a root cause that . . . they weren't acknowledging," and that as late as 2014, the Enterprise Risk Management Committee "didn't believe there was a root cause issue to be solved" and that the Bank's response "to this problem was slow and incremental, and ultimately not effective until 2016."<sup>2673</sup>
42. In sworn testimony before the OCC, Patricia Callahan, the Bank's former Chief Administrative Officer in charge of the Corporate Human Resources function, testified that the incentive plans were "too aggressive," "basic performance plans were also probably too aggressive in terms of how many of whatever people needed to click off to get satisfactory performance and keep their jobs" and "there was a perception that there was just too much pressure in the branches", but averred that at the time "when the L.A. Times articles came out" that she "thought that the root cause was probably a few different things."<sup>2674</sup>
43. In sworn testimony before the OCC, the Bank's former Head of Corporate Enterprise Risk Karl ("Keb") Byers testified that sales goals in the Community Bank "were too high and there was pressure in the system. And there was an overemphasis on solutions versus quality of sale" and, when asked whether he believed the Community Bank had a systemic problem with "sales practices misconduct," without his memory being refreshed, and without access to the evidence, he responded "Sure" and "I think that sounds very reasonable."<sup>2675</sup> Mr. Byers also testified that, by the time he appreciated the scope of sales practices misconduct, "it was pretty late. . . to be perfectly honest it just wasn't prior to the September 8th, 2016 [Consent Order] announcement" and that both he and "the second line" thought "the first line [] was making progress and making improvement."<sup>2676</sup>
44. Michael Bacon, Chief Security Officer and Head of Corporate Investigations until September 2014 testified before the OCC that he realized in 2004 that the Bank had a systemic problem with sales practices misconduct, and the problem

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<sup>2672</sup> Julian's ECSFM at No. 47, quoting MSD- 290A (Loughlin Inv. Tr.) at 49:6-52:23.

<sup>2673</sup> Julian's ECSFM at No.48.

<sup>2674</sup> Julian's ECSFM at No. 49, quoting MSD-291 at 87:18-88:17 (Callahan Inv. Tr.).

<sup>2675</sup> Julian's ECSFM at No. 50, quoting MSD- 382 at 132:2-132:16.

<sup>2676</sup> Julian's ECSFM at No. 50, quoting MSD-382 at 132:17- 133:4.

persisted until he left the Bank in 2014. He testified that “it was my view and continues to be my view that senior leaders in the roles that should have addressed it simply didn’t do their job[,]” including Respondent Russ Anderson.<sup>2677</sup>

45. The Bank’s former Head of Financial Crimes Risk Management James Richards, who succeeded Mr. Bacon in taking over the Corporate Investigations function, testified before the OCC that the Community Bank had a systemic problem with sales practices misconduct and what he “observed was that there were team members that felt pressure from senior management, sales goals related pressure and that those team members committed sales practices related misconduct as a result.” Mr. Richards further testified that the Community Bank tracked whether employees were meeting sales goals on a daily basis and if employees failed to meet sales goals they would suffer adverse employment consequences up to and including termination.<sup>2678</sup>
46. In sworn testimony before the OCC during its investigation, former General Counsel James Strother testified the Community Bank’s sales goals were a major contributing factor to the Bank’s sales practices misconduct problem:

[I]n hindsight knowing what I know today, it’s clear that those goals were either the major contributing factor to the problems that we had, and certainly a major contributing factor to it, and that the bank, as a whole, and the Community Bank, in particular, should have recognized earlier that the amount of bad behavior that was resulting, either because of, or partly because of those goals, or mainly because of those goals, was unacceptable and it should have been changed.<sup>2679</sup>
47. In her declaration, the Bank’s former Regional President for Los Angeles and Lead Regional President for Florida Shelley Freeman stated “sales practices misconduct was a systemic problem in that it resulted from the Community Bank’s incentive plans and high sales goals, coupled with a lack of oversight and controls. [S]ales practices misconduct had occurred throughout the Bank’s geographic footprint, with higher concentrations in certain parts of the country.”<sup>2680</sup>
48. Lisa Stevens and Laura Schulte, Regional Bank Executives reporting to Carrie Tolstedt, held the belief that the Community Bank had a “systemic” sales

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<sup>2677</sup> MSD-295 (Bacon Tr.) at 25:12-26:23; see also *id.* at 17:21-20:19; MSD-296A (Bacon Dep. Tr.) at 222:6-24; 224:2-225:9; 226:1-15; MSD-296B (Bacon Dep. Tr.) at 433:13-434:14.

<sup>2678</sup> (MSD-297 (Richards Tr.) at 234:5-19).

<sup>2679</sup> MSD-288A (Strother Tr.) at 110:6-16.

<sup>2680</sup> MSD- 199 (Freeman Decl.) at ¶¶ 6-7.

practices misconduct problem.<sup>2681</sup>

49. In April 2017, the Independent Directors of the Board of Wells Fargo & Company, the Bank's holding company ("Company"), issued a Sales Practices Investigation Report ("Board Report").<sup>2682</sup> The Bank accepted the findings of the Board Report "as a critical part of [its] journey to rebuild trust."<sup>2683</sup>
50. Based on 100 interviews of Bank employees and review across 35 million documents, the Board Report concluded that "[t]he root cause of sales practice failures was the distortion of the Community Bank's sales culture and performance management system, which, when combined with aggressive sales management, created pressure on employees to sell unwanted or unneeded products to customers and, in some cases, to open unauthorized accounts."<sup>2684</sup>
51. Further, the Board Report pointed out Community Bank senior management's failure to recognize the sales model as the root of the problem: "[t]hey ... failed to adequately consider that low quality accounts could be indicative of unauthorized accounts. It was convenient instead to blame the problem of low quality and unauthorized accounts and other employee misconduct on individual wrongdoers and poor management in the field rather than on the Community Bank's sales model."<sup>2685</sup>
52. As part of a Deferred Prosecution Agreement the Bank entered into after the Department of Justice concluded its investigation regarding the Bank's sales practices, the Bank admitted, accepted, and acknowledged as true the following facts:
  - (a) "The Community Bank's onerous sales goals and accompanying management pressure led thousands of its employees to engage in: (1) unlawful conduct to attain sales through fraud, identity theft, and the falsification of bank records, and (2) unethical practices to sell products of no or low value to the customer, while believing that the customer did not actually need the account and was not going to use the account";
  - (b) "Despite knowledge of the widespread sales practices problems, including the pervasive illegal and unethical conduct tied to the sales goals, Community Bank senior leadership failed to take sufficient action to prevent and reduce the incidence of unlawful and unethical sales

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<sup>2681</sup> MSD-546 (Stevens Tr.) at 201:1-10; 207:5-17; MSD-579 (Schulte Tr.) at 95:3-14; 99:1-7.

<sup>2682</sup> Russ Anderson Amended Answer ¶ 21; MSD-280). (Julian Amended Answer ¶ 21; McLinko Amended Answer ¶ 21; MSD-280.

<sup>2683</sup> MSD-326 at 5.

<sup>2684</sup> MSD-280 at 2.

<sup>2685</sup> *Id.* at 5.

practices”; and

- (c) From 2002 to 2016, Wells Fargo opened millions of accounts or financial products that were unauthorized or fraudulent. During that same time period, Wells Fargo employees also opened significant numbers of additional unneeded, unwanted, or otherwise low value products that were not consistent with Wells Fargo’s purported needs-based selling model. Wells Fargo collected millions of dollars in fees and interest to which the Company was not entitled, harmed the credit ratings of certain customers, and unlawfully misused customers’ sensitive personal information (including customers’ means of identification). In general, the unauthorized, fraudulent, unneeded, and unwanted accounts were created as a result of the Community Bank’s systemic sales pressure and excessive sales goals.<sup>2686</sup>

53. The Community Bank imposed unreasonable sales goals on its employees until October 2016, including when Respondent Julian served as Chief Auditor of the Bank and Respondent McLinko served as Executive Audit Director of the Community Bank.<sup>2687</sup>

54. Among the claims unresolved prior to the start of the evidentiary hearing was Enforcement Counsel’s claim stating the following:

The Bank internally and publicly identified a metric known as “cross-sell” which related to the number of products sold per household.<sup>2688</sup> The cross-sell ratio was a measure of products sold per customer household, as a perceived driver of future revenue. The more products sold to existing households, the more money the Bank expected to earn from each relationship and the less likely those customers would exit their relationship with the Bank confuses the cross-sell metric with sales practices.<sup>2689</sup>

55. During the hearing, any ambiguity regarding (1) whether the Bank publicly

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<sup>2686</sup> MSD-1 at 25, 30, 31 ¶¶ 15, 25, 32.

<sup>2687</sup> MSD-50 (“In retrospect, we missed some clear indications that our goals were unrealistic, making the problem worse than it should’ve been.”); MSD-131; MSD-269 (NBE Candy Expert Report) at ¶¶ 48-51; MSD-268 (NBE Crosthwaite Expert Report) at ¶¶ 43a-g; MSD-257 (NBE Coleman Expert Report) at ¶¶ 56, 69, 106; MSD-267 (NBE Smith Expert Report) at ¶¶ 67-85; MSD-349 (Schumacher Tr.) at 30:12-33:3, 35:4-20, MSD-82; MSD-581 (Clegg Tr.) at 44:1-46:6, 84:8-11; MSD-300 (Rawson Tr.) at 237:2-7; MSD-582 (Sotoodeh Tr.) at 61:20-62:7, 73:21-74:12; MSD-577 (Foley Tr.) at 134:19-135:9, 163:17-19; MSD-546 (Stevens Tr.) at 72:23-73:5; MSD-579 (Schulte Tr.) at 50:12-16; MSD-290B (Loughlin Tr.) at 304:3-14; MSD-297 (Richards Tr.) at 191:5-20; MSD-289A (Sloan Tr.) at 79:3-80:25.

<sup>2688</sup> Russ Anderson Amended Answer ¶¶ 6, 59; Julian Amended Answer ¶ 6; McLinko Amended Answer ¶ 6.

<sup>2689</sup> Enforcement Counsel’s MSD at Enforcement Counsel’s Statement of Material Fact (Russ Anderson) No. 71 and (Julian and McLinko) No. 68.

identified the cross-sell metric as a perceived driver of future income; (2) whether the metric related to the number of products sold per household; and (3) whether the metric related to sales practices and thus to sales practices misconduct was resolved through preponderant evidence establishing each of these three factual premises.

56. The first claim – that the Bank internally and publicly identified a metric known as “cross-sell” which related to the number of products sold per household – was not disputed, as each Respondent confirmed the claim in their amended answers.<sup>2690</sup>
57. The next claim was that the cross-sell ratio was a measure of products sold per customer household, as a perceived driver of future revenue. Mr. Julian asserted that the factual premise as stated by Enforcement Counsel confused the cross-sell metric with sale practices.<sup>2691</sup> He asserted the cross-sell metric “was a key metric tracking the number of products per household and was reviewed by the Retail Bank Cross-Sell Steering Committee for data integrity.”<sup>2692</sup>
58. Testimony during the hearing resolved any confusion or ambiguity: As Deputy Comptroller Coleman explained, the cornerstone of the Community Bank’s business strategy was “selling more bank products to customers”.<sup>2693</sup> The Community Bank developed their own “cross-sell metric so they could track the number of products that they sold.”<sup>2694</sup> Through this testimony, Deputy Comptroller Gregory established the relationship between the Bank’s business model and the metric used to determine the success of that model.
59. Susan Nelson, a Human Resources manager and later one of its Business Partner Leaders in the Community Bank, testified in a pre-hearing deposition.<sup>2695</sup> Responding to questioning by Mr. McLinko’s attorney, she agreed that she understood that when discussing either sales practice misconduct or sales integrity, that would, using the description provided to her by the attorney, be referring to the practice of an employee providing a service or product to a customer without the customer’s consent or

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<sup>2690</sup> Russ Anderson Amended Answer ¶¶ 6, 59; Julian Amended Answer ¶ 6; McLinko Amended Answer ¶ 6.

<sup>2691</sup> Julian’s ECSFM at ¶68, citing DJ0576 at 1-2 OCC-SP0913943. See also Russ Anderson’s ECSFM at ¶ 71 and McLinko ECSFM at ¶68, incorporating Mr. Julian’s response.

<sup>2692</sup> MSD-548 (Nelson Tr., Jan. 31, 2018) at 116.

<sup>2693</sup> Tr. (Coleman) at 246.

<sup>2694</sup> *Id.*

<sup>2695</sup> MSD-548 (Nelson Tr. January 31, 2018).



knowledge, or transferring funds from one account to another without the customer's consent.<sup>2696</sup>

60. Ms. Nelson testified that it was "the Wells Fargo way" to increase sales goals every year:

A: . . . I can confirm that goals did go up every year.

Q: Okay. Okay. And how are you able to confirm that goals went up every year?

A: It was the Wells Fargo way. (Laughter.) Double digit, year over year, increasing goals.

\* \* \*

I would say in more recent years, it wasn't double digits. Listening to my businesses talk, I think it was less than ten percent, probably anywhere from one to nine percent, depending on the business, my guess is. . . . I'm going to say possibly in late . . . 2008, 2009" the "double digit pace kicked down."<sup>2697</sup>

61. The Board Report found that, even after the Community Bank lowered sales goals mid-year in 2013 and 2014, "they were still set at an unachievable level," and described the Community Bank's sales goals as "untenable," "unrealistic," and "unattainable."<sup>2698</sup>

62. Multiple senior regional leaders in the Community Bank testified that the Community Bank's sales goals were unreasonable.<sup>2699</sup>

63. The Bank's former Chief Risk Officer Michael Loughlin testified that he had no doubt that the sales goals in the Community Bank were unreasonable:

Q: And did you at some point conclude that the goals in Community Bank – well, let me put it this way; sitting here today, do you have any doubt in your mind that Community Bank's sales goals were unreasonable?

A: I don't have any doubt.<sup>2700</sup>

A former regional leader Jeffrey Schumacher provided the following sworn testimony to the OCC about the impact of the sales goals:

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<sup>2696</sup> MSD-548 (Nelson Tr.) at 9.

<sup>2697</sup> Julian's ECSFM at No. 71.

<sup>2698</sup> MSD-280 at 5, 19, 44-45; see also MSD-199 (Freeman Decl.) at 2 ("I believed the sales goals were too high . . . despite the fact that the Community Bank at that time had been retroactively reducing sales goals . . .").

<sup>2699</sup> See, e.g., MSD-546 (Stevens Tr.) at 72:23- 73:5; MSD-579 (Schulte Tr.) at 50:12-51:9; MSD-349 (Schumacher Tr.) at 36:3-25; MSD-575 (Lee Tr.) at 87:13-16; MSD-576 (Perry Tr.) at 35:2-9; MSD-577 (Foley) Tr. 62:23-63:5; see also MSD-199 (Freeman Decl.) at 2, 5-6.

<sup>2700</sup> MSD-290B (Loughlin Tr.) at 303:13-18.

Q: Okay. You also eluded [sic] to some emails that you sent, and some statements you made to others that high goals, that the goals were so unreasonable or aggressive that they are likely to cause that behavior. At least that's what I understood you to say. Is that what happened?

A: Yes.

Q: Okay. And why did you think that these unreasonable goals that you were assigned would lead to bad behavior?

A: Well, because people need jobs. I mean, they have families to feed, they have people that depend on them. And you know, the goals were part, the sales goals were part of their incentive plan which was how much extra money they made. And it was part of their performance review, which was obviously could determine whether they stay with the company. And so for a long period of time, sales were a pretty big part of what Wells Fargo did. And I actually, the common term was solutions are king. And I think senior management projected that. And so when sales goals are aggressive, I think that creates a lot of pressure on someone that's trying to keep their job and keep their family and it's a lot of pressure to make those goals. . . .<sup>2701</sup>

64. Respondent McLinko testified that sales goals within the Community Bank were unreasonable. Specifically, he testified:

Q: All right. From reading this and from what you now know from everything, do you have a belief as to whether these sales goals that Wells Fargo set for members of the community bank were unreasonable?

MR. CRUDO: Foundation.

A: Again, yes, based upon what I know now and reading this, they were certainly very difficult to attain.<sup>2702</sup>

Respondent Julian testified that the Community Bank's sales goals were unreasonable. Specifically, he testified:

Q: Okay. So, it's fair to say that you now know that the bank gave its employees unreasonable sales goals. Is that correct?

A: Yes.<sup>2703</sup>

65. The Community Bank maintained "an incentive compensation system that was poorly designed, poorly monitored and managed and allowed to remain in place too

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<sup>2701</sup> MSD-349 (Schumacher Tr.) at 36:3-25 (emphasis added).

<sup>2702</sup> McLinko Amended Answer ¶ 5.

<sup>2703</sup> MSD-278 (Julian Tr.) at 121:4-7.

long.”<sup>2704</sup>

66. The incentive compensation plans in the Community Bank were based upon and consisted of unreasonable sales goals.<sup>2705</sup>
67. The Bank’s Incentive Compensation Risk Management Policy, adopted in 2011, governed all incentive compensation plans, including those in the Community Bank, but did not impose oversight responsibilities on the Head of the Community Bank, the Community Bank Group Risk Officer, and the Law Department.<sup>2706</sup>
68. From the early 2000s during Respondent Russ Anderson’s tenure as the Group Risk Officer and until sales goals were eliminated in the Community Bank effective October 1, 2016, employees in the retail branch network of the Community Bank faced significant pressure to meet sales goals.<sup>2707</sup>
69. The Community Bank tracked employees’ sales performance on a daily and at times

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<sup>2704</sup> MSD-6; see also MSD-5; MSD-289A (Sloan Tr.) at 79:3-80:25.

<sup>2705</sup> MSD-5; MSD-6; MSD-213 (SL 2015-36) at 2 (“Cross-selling, if not properly governed, can lead to excessive sales pressure on employees to meet sales goals and achieve financial incentives. Incentive compensation is a key factor in motivating employee behavior and should be reevaluated across all sales activities enterprise-wide given these events.”); MSD-280 (Board Report) at 23, 29, 31-33, 57, 78, 84 (“The Community Bank did not drop teller referral goals, and, while it lowered overall sales goals slightly for 2013, it did not revise the sales goals embedded in the eligibility thresholds for incentive compensation until 2014 (and then only slightly).”); MSD-570 (SL 2016-36); MSD-600 (SL-2016-49) at 1, 3, 7 (“the CB management team implemented aggressive sales goals and a poorly designed incentive compensation program which resulted in the widespread unethical activity, significant customer harm and reputational damage to the bank.”); MSD-651 (SL 2016-35); MSD-343 (Sales Practices Consent Order); MSD-269 (NBE Candy Expert Report) at ¶¶ 37-59; MSD-382 (Byers Tr.) at 231:20-232:6; MSD-199 (Freeman Decl.) at ¶ 8, 17; MSD-411 (Raphaelson Decl.) at ¶¶ 5, 14, 15, 16, 19, 20, 23.

<sup>2706</sup> Russ Anderson Amended Answer ¶ 150; MSD-211; MSD-212; MSD-224 at 10, 24; McLinko Amended Answer ¶ 150; Julian Amended Answer ¶ 150; MSD-211; MSD-212; MSD-224 at 10, 24.

<sup>2707</sup> MSD-266 (Russ Anderson Dep. Tr.) at 32:17-33:9, 61:16-63:23, 78:18-79:17; MSD-268 (NBE Crosthwaite Expert Report) at ¶¶ 44, 46; MSD-580 (Henderson Tr.) at 131:18- 132:19 (describing call nights whereby employees who did not meet sales goals had to stay overtime to make calls in order to get sales); MSD-382 (Byers Tr.) at 231:20-232:6; MSD-128; MSD-129; MSD-81 (“We have a lot of markets and regions that are significantly below minimum standards, and you have to believe there is unbearable pressure. In light of that, you have to predict there will be more gaming.”); MSD-141; MSD-142; MSD-158 at 4 (“Make your goals at any cost to the team member or customer – this is our environment.”); MSD-159; MSD- 160; MSD-296A (Bacon Dep. Tr.) at 222:1-24, 225:20-226:3, MSD-296B (Bacon Dep. Tr.) at 180:17-181:9, 190:12-192:15, 200:4-202:24); MSD-544 (Weber Tr.) at 20:16-23:10, 27:20-32:8, 50:18-52:7, 146:23-148:4, 151:1-152:3 (Dec. 21, 2017); MSD-294 (Wipprecht Tr.) 35:1-38:3, 79:7-14, 94:1-21, 112:6-19; MSD-549 (Holliday Tr.) at 51:19-52:9, 69:14-71:22); MSD-73; MSD-74; MSD-75 (“...I do know gaming has everyone’s attention at the moment. We’ve been preaching it for ten years largely ignored . . .”); MSD-76 (October 21, 2005 email from an Investigations Manager stating: “We have seen a recent surge in complaints regarding on-line banking enrolling, bill-pay enrollment and ordering debit cards without customer consent or knowledge. I don’t know what’s going on but I think we need to address the issue, as it is spiraling out of control.”); MSD-581 (Clegg Tr.) at 50:3-12; 51:14-21, 81:4-82:7; MSD-287B (Otsuka Tr.) at 9:15-19; MSD-546 (Stevens Tr.) at 88:2-9, 111:5-18; MSD-582(Sotoodeh Tr.) at 81:16-82:2, 106:14-24, 107:3-10; MSD-579 (Schulte Tr.) at 71:9-11, 93:21-94:1.

hourly basis.<sup>2708</sup>

70. Incentive compensation and promotional opportunities in the Community Bank depended on an employee's ability to meet sales goals.<sup>2709</sup>
71. From 2011 through third quarter 2016, the Bank terminated approximately 8,520 employees for sales performance issues, including failure to meet sales goals.<sup>2710</sup>
72. The Board Report found that Community Bank's sales-performance stack rankings and its determination of employees' incentive compensation and promotional opportunities relative to sales goals, created an "intense pressure to perform. . . ." <sup>2711</sup>
73. Employees remained under significant pressure to meet unreasonable sales goals even in September 2016, a month before the sales goals in the Community Bank were officially eliminated.<sup>2712</sup>
74. In an email dated October 5, 2016, Hope Hardison, the former Chief Administrative Officer and Head of Corporate Human Resources wrote the following: "Don't say there was nothing wrong with our culture. At least in the case of parts of the Community Bank, to suggest so just ignores a reality that everyone knows there was insane pressure on people to produce 'widgets' new account sales. That is a reality people know, and we will hear more about in the media as former team member exposes' will show."<sup>2713</sup>
75. During his May 2018 sworn statement, Respondent Julian testified that, "having seen the information, read the various reports, read the – what's out there in the public, read team members' allegations, read customer complaints, it – it's clear to me that we had a culture within the general bank, within the retail bank at Wells Fargo that was putting goal-oriented, undue -- my words -- undue pressure on team members to reach goals that either were unattainable or were very challenging to be able to reach, and it put pressure on the culture of not only setting goals that

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<sup>2708</sup> MSD-549 (Holliday Tr.) at 25:7-27:25, 59:11-18; MSD-541 (J. Freeman Tr.) 76:20-77:12; MSD-350 (Ramage Tr.) at 33:13-36:18; MSD-199 (Freeman Decl.) at ¶ 10; MSD- 411 (Raphaelson Decl.) at ¶ 21.

<sup>2709</sup> MSD-266 (Russ Anderson Dep. Tr. ) at 22:13-23:3; MSD-349 (Schumacher Tr.) at 40:25-44:11; MSD-549 (Holliday Tr.) at 28:3-23; MSD-579 (Schulte Tr.) at 97:8-15; MSD-591 (Najvar Tr.) at 305:1– 308:2; MSD-350 (Ramage Tr.) at 112:1-113:4; MSD-595 (Vasquez Tr.) at 37:5-10, 98:12-18; MSD-508).

<sup>2710</sup> MSD-44.

<sup>2711</sup> MSD-280 (Board Report) at 20.

<sup>2712</sup> MSD-103; MSD-83 ("For the day, volume was up 177% over YTD daily volume and Sales Practice allegations almost doubled. I just read the 19 sales practice allegations and at least 50% are exactly 'pressure and gaming' related. It made my hair curl"); MSD-293A (Hardison Tr.) at 148:7-160:18 (testifying that employees were complaining about pressure and gaming for many years and reflected what was actually going on in the Community Bank for many years)); CRA-148; MSD-472 (Mack Tr.) at 179:19-181:9.

<sup>2713</sup> MSD-77; MSD-293A (Hardison Tr.) at 134:4- 137:11; McLinko Amended Answer ¶ 134.

appeared to have been in a number of appearances unattainable.”<sup>2714</sup>

76. Similarly, during his March 2018 sworn statement, Respondent McLinko testified: “There was certainly the pressure of the goals and that sort of stuff, sales goals.”<sup>2715</sup>
77. Corporate Investigations was a department within the Bank responsible for investigating employee misconduct.<sup>2716</sup>
78. Employees investigated for engaging in sales practices misconduct expressed to investigators in Corporate Investigations that they committed the misconduct because of sales pressure and fear that they could and would be fired for failing to meet sales goals. Multiple senior leaders in Corporate Investigations testified before the OCC that employees who engaged in sales practices misconduct did so because of significant pressure to meet unreasonable sales goals.<sup>2717</sup>
79. Through the summary disposition process, the parties identified a factual dispute regarding whether controls to prevent and detect sales practices misconduct were inadequate. Testimony taken during the evidentiary hearing constituted preponderant evidence establishing that controls from both the first and third lines of defense were inadequate and neither prevented nor detected sales practices misconduct.
80. With respect to the first line of defense, as GRO Ms. Russ Anderson was responsible for implementing proactive and sound risk-management practices and reinforcing the risk culture throughout the Community Bank.<sup>2718</sup> As Chair of the Community Bank’s Risk Management Committee and pursuant to the Bank’s Risk Management Framework, Ms. Russ Anderson was responsible for understanding the Community Bank’s risk profile and working with management across the Community Bank to ensure risks were effectively managed.<sup>2719</sup>
81. As a member of the Community Bank’s Internal Fraud Committee, Ms. Russ Anderson was responsible for managing internal fraud risks related to business practices and processes, and for developing appropriate controls to mitigate such risks.<sup>2720</sup> Taking these responsibilities into account, NBE Candy identified the inadequacies of these

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<sup>2714</sup> MSD-278 (Julian Tr.) at 25:4-26:11.

<sup>2715</sup> MSD-276 (McLinko Tr.) at 125:11-13.

<sup>2716</sup> Russ Anderson Amended Answer, ¶ 50; Julian Amended Answer ¶ 50; McLinko Amended Answer ¶ 50.

<sup>2717</sup> MSD-544 (Weber Tr.) 21:24-23:20; MSD-299 (Sperle Tr.) at 67:4-25, 139:10-140:1, 146:1-13, 162:8-25; MSD-294 (Wipprecht Tr.) 38:23-39:25; MSD-297 (Richards Tr.) at 79:11-80:22; MSD-581 (Clegg Tr.) at 44:1-46:6. OCC Exh. 2340 at ¶ 118; OCC Exh. 2335 at ¶ 109; OCC Exh. 0102 at 0025; OCC Exh. 2407 at ¶ 106.

<sup>2718</sup> OCC Exh. 2340 at ¶ 118; OCC Exh. 2335 at ¶ 109; OCC Exh. 0102 at 0025; OCC Exh. 2407 at ¶ 106.

<sup>2719</sup> OCC Exh. 0660 at 0001; R Exh. 11556 at 0001; Tr. at 9769-9770 (CRA).

<sup>2720</sup> OCC Exh. 2340 at ¶ 120; OCC Exh. 1272 at 0003, 0005; R Exh. 06313 at 0003, 0005; Tr. at 9548 (CRA).

controls and Ms. Russ Anderson's role:

Q (by Enforcement Counsel): What, if any, conclusions did you reach about the adequacy of the Bank's controls to prevent sales practices misconduct from 2013 to 2016?

A (by NBE Candy): From reviewing documents and testimony, I have concluded that from 2013 to 2016, this relevant time period, that the controls to prevent sales practices misconduct were inadequate.

Q: Why?

A: There's a number of reasons for that. The most basic way to explain it is if a customer -- I mean, if an employee wanted to open up an unauthorized account, he or she could. If they wanted to open up an unauthorized credit card, he or she could. If he wanted to open up an unauthorized checking account, move money in and out of that account to make it appear funded and then take the money out, he could or she could. During this entire time, the preventative controls were not effective to prevent these, this sort of misconduct to happen, and we know that, both from confirmed cases of sales practice misconduct and fraud, as well as from other analyses that show the, the potential magnitude of the problem at the Community Bank.

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Q: How, if at all, is Ms. Russ Anderson responsible for the inadequate controls to prevent sales practices misconduct as the Group Risk Officer?

A: As the group risk officer for the Community Bank during this period, it was absolutely her responsibility to implement adequate preventative controls. You know, like I discussed earlier, the bank was pursuing a risky business model, as well as the fact that there's just risk inherent in, in offering products and services to customers. As the Group Risk Officer charged with ensuring that risk management was effective, which includes preventative controls, it was her responsibility to implement adequate preventative controls.

Q: What controls to prevent sales practices misconduct should Ms. Russ Anderson have instituted during her tenure as the Group Risk Officer?

A: There's a number of things. I can't give an exhaustive list, but probably the most important thing that she could have done to prevent sales practice misconduct was to advocate for fundamental changes to the business model. Wells Fargo's Community Bank chose to have unreasonable sales goals and unbearable pressure to meet those sales goals.

Changing that model was by far, advocating and incredibly challenging that model, was one of the most effective things she could have done to prevent sales practice misconduct from occurring. Also, she could have advocated for

a formal policy that team members could not be terminated for failing to meet sales goals. The fact that people could risk termination if they did not meet the unreasonable goals did drive some of the misconduct. So that would have been another effective thing to do.

And in terms of her responsibilities with incentive compensation risk management, there's also a number of things she could do. She could have advocated for not giving credit for unfunded accounts or not giving credit for duplicate accounts. You know, I've seen people who have had 50-plus checking accounts unnecessarily. She could have advocated for not giving credit to accounts that appeared to be simulated funding. Or she could have advocated for just taking the sales goals out of the incentive compensation plan.

But other than those three, there's a number of things she could have done for preventing the misconduct from ever happening, including things such as requiring signatures prior to opening up accounts, including things such as having text message or e-mail confirmations, you know, when you're opening an account that you are authorizing it. Again, this is not exhaustive, but there's, there's a number of things that she should have implemented as Group Risk Officer to prevent sales practice misconduct.<sup>2721</sup>

82. With respect to the third line of defense and Mr. Julian's responsibilities, the record reflects that Mr. Julian was responsible for developing and employing dynamic audit plans using an appropriate risk-based methodology and for ensuring that that the plans effectively and timely responded to and addressed new and emerging risks and hot topics.<sup>2722</sup> He was also responsible for reviewing, approving, and completing the audit plans and the execution of WFAS' audit work and was authorized to allocate WFAS' resources to accomplish its objectives.<sup>2723</sup>
83. To effectively perform its duties and protect the Bank, Internal Audit must ensure that risks are assessed appropriately and evaluated at proper intervals, plan its audits accordingly, and perform the audits required.<sup>2724</sup> When he became Chief Auditor, the OCC told him that to meet the OCC's heightened expectations, WFAS's audit plans had to "reflect and include significant risks."<sup>2725</sup>
84. When asked to describe the risks that are posed to a bank when its audit department does not effectively articulate the control environment through their audit reporting,

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<sup>2721</sup> Tr. (Candy) at 1065-69.

<sup>2722</sup> OCC Exh. 2088 at 0002.

<sup>2723</sup> OCC Exh. 2090 at 0075; OCC Exh. 2091 at 0098; OCC Exh. 2092 at 0120; OCC Exh. 2093 at 0111; R Exh. 17746 at 0002, 0004.

<sup>2724</sup> OCC Exh. 1938R at 0023.

<sup>2725</sup> Tr. (Julian) at 6095.

NBE Candy responded:

So the risks are quite substantial when an audit department does not escalate risks properly to -- to the Audit and Examination Committee or to the other -- to the board more generally. And the risks -- when audit does not share that there are significant issues in the internal control environment, that effectively doesn't give the Audit and Examination Committee and the broader board an understanding of the independent look at the -- at the internal control and the risk governance environment of the bank.

And that is actually what the board is expecting from the audit -- the audit group. They want to hear the independent views, because these are the views that are sort of free from, you know, any first or second line, if you will, possibly spin -- I'm sorry. That's a rather loose way to put it. But, in essence, you're looking at the audit group to go in, do the work, and come out with its views completely separate from the work that's being done in the first and second lines of defense. They're going to have their own opinions.

So without providing that, then you get into issues like compliance risk. You get into issues reputation risk. Certainly that's quite critical. You get into fraud. You get into -- and a lack of views around fraud -- financial risk. Strategic risk. Did I mention compliance risk? And then, obviously litigation risk is another subset. So there's a number of risks when audit does not properly inform the board of its views on the internal control environment and the overall risk governance framework.<sup>2726</sup>

85. Deputy Comptroller Coleman opined that Mr. McLinko engaged in unsafe and unsound practices related to the failure to identify inadequacies in prevention and detection controls that were in place in the Community Bank. He described Mr. McLinko's responsibilities in these terms:

So as an internal auditor, you would have the obligation and responsibility to understand those strategies and then understand any risks that are associated with those strategies and what compensating controls were put in place. As an auditor, you would want to design an audit scope and an audit program that would review that activity, determine if those compensating controls were effective, and if not, identify those specific issues and escalate those issues to either your direct supervisor within the audit division or to ensure that the board was aware of those issues.<sup>2727</sup>

Continuing, Mr. Coleman testified:

Based upon his responsibilities as the audit director for the Community Bank

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<sup>2726</sup> Tr. (NBE Smith) at 3877-79.

<sup>2727</sup> Id. at 247.



and the responsibilities that come with that position in providing assurance to the Board that there were effective controls, that he had performed a risk assessment as it related to the activities of the Community Bank and conducted audits with an appropriate scope relative to those business activities and where he found deficiencies those issues were escalated to the Board.

\* \* \*

So during that time from 2013 to 2016 [Mr. McLinko] was at least made aware of the sales practice issues through the publication of stories in the L.A. Times. And from that information, he could have used that to set up audit work that would focus in on the issues as it related to sales practice misconduct to help determine the root cause of those issues and provide Board information on what needed to be done to remediate those issues.<sup>2728</sup>

86. From no later than 2004 until 2016, the controls to prevent and detect sales practices misconduct were inadequate.<sup>2729</sup>

87. The Bank's systems did not prevent employees from engaging in sales practices misconduct. The Bank's Head of SSCOT, Rebecca Rawson, who reported to Respondent Russ Anderson, provided the following sworn testimony about the deficiencies in controls to prevent sales practices misconduct:

A: . . . And also looking at controls within our operations, so the systems that are used by the bankers, so store vision platform. And if we say a signature is required, or whatever by policy, why does the system not prevent the banker from going against policy? So in other words, making it harder for someone to get something -- for a banker to get it wrong.

Because I think in that point in time, we have policies and procedures that stated X, but the system really could just allow you to proceed.

Q: Okay.

A: So I think that is what I think about with the root cause a little bit.

Q: I see. Again, I will tell you what I got from your testimony, and please correct me if I misunderstood you.

A: Okay.

Q: At the Community Bank, I take it there was a significant problem with controls that are supposed to detect and prevent sales practice misconduct? Is

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<sup>2728</sup> Id. at 242.

<sup>2729</sup> MSD-269 (Expert Report of NBE Elizabeth Candy); MSD-267 (Expert Report of Tanya K. Smith, NBE, CFA); MSD-92; MSD-297 (Richards Tr.) at 175:21-178:13; MSD-300 (Rawson Tr.) at 49:5-50:22; 211:21-212:2; MSD-92 ("With the recent sales practices matter, we have recognized the consumer and customer impact, reputational impact, legal and regulatory impact of conduct risk. Fragmented, complex controls spread across the company have not proven to be effective."); MSD-643A (DiCristofaro Tr.) at 109:18-21; MSD-472 (Mack Tr.) at 111:3-112:8; MSD-59.

that fair to say?

A: I do not know if it would be -- it depends in how you define the system.

Q: Okay.

A: If the system is a control. I think we should have -- this is my opinion. We should have built into our systems places where it stops the team member from advancing if they are not acting in accordance with policy. Q: Okay. So I take it the bank had a policy that you should not issue credit cards or debit cards without the customer's consent?

A: Correct.

Q: All right. But the system allowed team members to actually issue credit cards and debit cards without the customer's consent or the customer's signature?

A: I think that is right.

Q: Okay. And you view that as a failure in controls? A: I think that is fair.<sup>2730</sup>

88. Community Bank employees across its nationwide branch network used a Bank system known as the Store Vision Platform ("SVP") to open and issue products and services for bank customers.<sup>2731</sup>

89. SVP required bank employees to enter or confirm customers' personal data and select options within the platform to open or issue any product or service.<sup>2732</sup>

90. Bank policies required Bank employees to obtain express consent from customers prior to opening accounts or services, where such consent could be through a variety of means, including pins, signatures, and verbal consent.<sup>2733</sup>

91. SVP did not require Community Bank employees to obtain evidence of customer consent, such as a customer signature, before they could open or issue credit cards, debit cards, lines of credit, or certain other products and services, or transfer customer funds; and Respondent Russ Anderson explained in 2015 that the Bank "will process [a credit card] application without a signature (since it is not required by law) unless the applicant is under the age of 21 . . . . So, if the customer complains [that a card was unauthorized] and there is not a signature there isn't anything we 'do' about it."<sup>2734</sup>

92. Until approximately 2014, it was an acceptable practice for Community Bank employees

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<sup>2730</sup> MSD-300 (Rawson Tr.) at 49:5-50:22; 211:21-212:2; see also MSD-150 ("Lines of Credit, Cards, and ancillary services such as online, bill pay, rewards, etc. do not require signatures and thus are hard to track internally.").

<sup>2731</sup> MSD-200 (Hughes Decl.) at 1; MSD-596 at 3.

<sup>2732</sup> MSD-200 (Hughes Decl.); MSD-596.

<sup>2733</sup> Julian's ECSFM at No., citing MSD-010 at 5; MSD-009 at 7.

<sup>2734</sup> MSD-66; MSD-150; MSD-229; MSD-356.

to open accounts over the phone and not obtain customer signature.<sup>2735</sup>

93. Not until approximately 2016 were Bank systems modified to require evidence of customer consent before Community Bank employees could issue credit cards or transfer funds in customer accounts.<sup>2736</sup> Consent capture for non-credit card products had not yet been implemented as of May 2016.<sup>2737</sup> Up until March 2018, customer signatures still were not required to obtain a debit card.<sup>2738</sup>
94. Community Bank leaders, including Respondent Russ Anderson, knew that the vast majority of customer-consent sales integrity cases were related to the Community Bank's failure to capture evidence of customer consent.<sup>2739</sup>
95. In spring and summer 2012, the Community Bank piloted a program that would require explicit customer consent before allowing bankers to issue debit cards to customers.<sup>2740</sup> On June 28, 2012, Respondent Russ Anderson received a PowerPoint presentation explaining the "[p]ositive impacts of store pilot for consumer and business debit cards" included: "Strong customer preference per market research"; (2)"Banker feedback that debit consent screen flow and process easy to adopt, and represents a sales quality improvement"; and (3) "Lifts in debit card fraud activation and POS [point of sale] activation – especially where customer provides consent electronically (on the signature pad)."<sup>2741</sup> She was also informed, "Debit card 'lack of consent' contributes more than fair share of enterprise quality issues and corrective actions."<sup>2742</sup>
96. In a Supervisory Letter issued on June 26, 2015 to the Bank, the OCC stated: "[o]ur sampling of customer complaints noted in many cases there was no method to prove customer consent in the form of a signature for either the deposit or credit card product."<sup>2743</sup>
97. Another preventative control that the Community Bank failed to institute was awarding sales credit to employees only for accounts that customers use. This was Accenture's

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<sup>2735</sup> MSD-65.

<sup>2736</sup> MSD-356.

<sup>2737</sup> MSD-356; MSD-598.

<sup>2738</sup> MSD-655 at 6-7 ("signatures are still not required to obtain a debit card.").

<sup>2739</sup> MSD-58); MSD-59; MSD-60; MSD-150.

<sup>2740</sup> MSD-229.

<sup>2741</sup> *Id.* at 3.

<sup>2742</sup> *Id.* at 4; see also *id.* at 7 (noting that "Debit explicit consent has strong customer appeal.").

<sup>2743</sup> MSD- 213 (SL 2015-36) at 3; see also MSD-570 (SL 2016-36) at 4 ("The root causes include excessive sales pressure and the absence of a control process that required documentation of explicit customer consent").

first recommendation to the Community Bank in October 2015.<sup>2744</sup>

98. There were four primary mechanisms the Bank employed to detect sales practices misconduct. Three were reactive tools that relied on employees or customers to surface problems: 1) a whistleblower hotline known as the EthicsLine established for employees to raise concerns about behavior that may violate the Bank's Code of Ethics, or any laws, rules or regulations, 2) employee complaints sent directly to senior management or others within the Bank, and 3) customer complaints. The fourth tool involved using data analytics to detect activity indicative of certain sales practices misconduct, referred to as "proactive monitoring." The Bank did not begin employing proactive monitoring until around 2012; before then, the primary way the Bank detected sales practices misconduct was if a customer or a Bank employee reported it.<sup>2745</sup>

99. The Bank's former Head of Corporate Investigations Loretta Sperle testified before the OCC that there was nearly a 100% chance an employee's boss would know if she failed to meet her sales goals. By contrast, the chances were very small that an employee would be caught for issuing an unauthorized product or service. Ms. Sperle testified:

Q: Okay. So if [employees] were doing it when nobody is watching, and they don't do it enough to trigger the outlier thresholds that you've had, the chances of them getting caught is very small?

A: Yes. I would agree.

100. Although the EthicsLine was one of the Community Bank's mechanisms for detecting sales practices misconduct, Community Bank employees did not consistently use the EthicsLine to report issues. In its 2015 independent review of sales practices, Accenture reported, based on its interviews of over 300 Community Bank employees, that "[m]any bankers stated that ethics issues are usually escalated through management and rarely escalated through the Ethics Line," and "some Service Managers and Bankers stated that they do not utilize the Ethics Line as they fear retribution or that it may not be anonymous."<sup>2746</sup> Sales integrity-related EthicsLine complaints were referred to Community

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<sup>2744</sup> MSD-51 at 12 ("Reward team members based more on positive customer outcomes (e.g., account utilization) with less emphasis on solutions sold."). "As of January 2016, the Community Bank allowed employees to have approximately 30 percent of the new accounts they opened to remain unfunded; they would still be eligible to receive sales credit for the unfunded accounts." (MSD-269 (NBE Candy Expert Report) at ¶ 107c; MSD-647); see also MSD-295 (Bacon Tr.) at 121:15-125:1 (suggestions of preventative controls).

<sup>2745</sup> Russ Anderson Amended Answer ¶ 92; MSD-290A (Loughlin Tr.) 236:1-13; MSD- 300 (Rawson Tr.) at 86:2-88:15, 213:2-8; MSD-299 (Sperle Tr.) at 41:6-42:2, 53:13-19.

<sup>2746</sup> MSD-51 at 41; see also *id.* at 11.

Bank's Sales Quality team, later known as SSCOT.<sup>2747</sup>

101. Sales Quality/SSCOT referred only a small percentage of the EthicsLine complaints to the Bank's Corporate Investigations group for investigation. Sales Quality imposed various preliminary thresholds including, among other things, polling of other customers of the accused employee, to determine which allegations to send to Corporate Investigations for investigation. An employee accused of sales practices misconduct might only be referred to Corporate Investigations if telephone "polling" of other customers of the same employee revealed other incidents, or "substantiations," of similar misconduct.<sup>2748</sup>
102. The Bank's former CEO John Stumpf testified before the OCC, "As I sit here today looking back, there were a number of outreaches by team members that were informing the company and senior leadership about these issues. And I wish we would have moved faster on those". He took responsibility that he personally should have moved faster, and testified that employees did all they could to complain about the unreasonable sales goals to Bank senior leadership in numerous ways over many years, by calling the EthicsLine, sending emails, holding protests, and approaching newspapers. He further stated that the senior leadership team and not the employees, is to blame for the Bank not moving fast enough to address the sales practices misconduct problem.<sup>2749</sup>
103. According to the Community Bank's former Chief Compliance Officer, who reported to Respondent Russ Anderson, the "Community Bank did not have an adequate system to track customer complaints from 2011 until [his] departure in 2015. Specifically:
- a. Retail branches lacked the technology to track customer complaints in a consistent manner;
  - b. Complaints that were tracked were captured via disparate systems and inputted into various spreadsheets; and
  - c. The Community Bank did not have a centralized repository for customer complaints."<sup>2750</sup>

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<sup>2747</sup> MSD-381 at 15.

<sup>2748</sup> MSD-245 at 9; MSD-381; MSD-122 ("Generally speaking, if there are fewer than 3 polling substantiations, there's no referral to Investigations."); MSD-93 ("No single LOB [Line of Business] or Second Line of Defense 'owns' EthicsLine/Sales Integrity/Sales Practices, and Corporate Investigations only sees a sliver of these.") (emphasis added); MSD-297 (Richards Tr.) at 226:18-229:20; MSD-591 (Najvar Tr.) at 142:24-144:25; MSD-75; MSD-150; MSD-151 at 1 ("There are lots of situations where we do polling. Generally speaking, if the team member denied the conduct and there was just one polling confirmation, we're not likely to terminate (and it might not even get sent to Investigations."); MSD-245.

<sup>2749</sup> MSD-8B (Stumpf Tr.) at 401:9-402:6.

<sup>2750</sup> MSD-56 (Christoff Decl.).

104. The Community Bank did not consistently capture customer complaints from customers affected by sales practices misconduct. When Accenture conducted its 2015 independent review of sales practices within the Community Bank, it found in its interviews of over 300 Community Bank employees that “team members . . . do not have a clear understanding of what constitutes a customer complaint and frequently do not capture or document complaints for further analysis.” Accenture’s review “did not identify a clear and consistent process or governance model to ensure all customer complaints are captured, monitored, addressed, and reported across all stores within the Community Bank.”<sup>2751</sup>

105. Of the customer complaints Community Bank Sales Quality/SSCOT captured, lack of consent was the most common customer complaint type. Accenture “review[ed] all SSCOT cases with ‘an element of a customer complaint’ provided by SSCOT.” Its review “revealed that ‘Consent’ is the greatest case type (68%). The remaining case types are related to ‘Account Openings’ (14%) and case types that are a combination of the consent and account opening case types.”<sup>2752</sup>

106. Lack of consent had been the greatest customer complaint type since long before Accenture conducted its review in 2015. A September 5, 2007 presentation by the Sales Quality Team, the predecessor to SSCOT, showed that by 2007, the Bank as a whole was receiving 25,000-48,000 “Customer Calls Annually Stating ‘Did Not Request’” (i.e. lack of consent) for certain Bank products.<sup>2753</sup> The presentation explained: “The content of these calls is very similar to content in [approximately] 50% of the formal EthicsLine/HR allegations that Sales Quality allegations currently processes.”<sup>2754</sup> The presentation depicted an iceberg, representing the Bank was only detecting the tip of the iceberg of sales practices misconduct.<sup>2755</sup>

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<sup>2751</sup> MSD-51 at 10.

<sup>2752</sup> Julian’s ECSFM at No. 138 citing MSD-51 at 43.

<sup>2753</sup> MSD-51 at 7.

<sup>2754</sup> *Id.*

<sup>2755</sup> *Id.*; MSD-539 (Dement Tr.) at 159:20-163:20.

## Watch List: Issues Reported Across Regional Banking

WELLS FARGO

❖ **Potential scope of Sales Quality issues companywide is larger than SQ Team allegation volumes**

- Product groups approached Sales Quality regarding direct customer calls alleging lack of consent
- SQ asked each group to size, and given information on volumes, implemented alternative processes
- With data accumulated, surfacing issue now with intent to educate, further the case for signatures, and manage potential risks
- Comparing calls and cases is not a 1 to 1 comparison, as some portion of calls would relate to same bankers or same stores



Product	# of Customer Calls Annually Stating "Did Not Request"	Type of Issue
Credit Card & Combo Rewards	25,000-48,000*	Consent
Credit Cards	8,700	Consent
Overdraft Protection	3,800	Consent
Debit Card Rewards	850	Consent
Personal Lines	500	Consent
Loan Documentation Issues	100	Procedure
Chking/Svngs. Debit. Online	???	
Total Previously Undocumented	38,650 +	
<small>*Range depends on whether you consider accts open ~5 mths or ~6 mths</small>		
Total Annual SQ Cases	~1,800	Consent & Procedure

❖ The content of these calls is very similar to content in ~50% of the formal Ethicsline/HR allegations that Sales Quality allegations currently processes.

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107. The presentation separately stated that the primary allegations handled by the Sales Quality Team “continue to be customer consent issues and account opening procedural issues” and that sales quality allegations were occurring across the Bank geography wide.<sup>2756</sup>

108. In a Supervisory Letter issued on June 26, 2015 to the Bank, the OCC cited a Matter Requiring Attention (“MRA”) related to the Bank’s complaint management systems.<sup>2757</sup>

109. The group within the Community Bank that performed proactive monitoring was SSCOT, which reported to Respondent Russ Anderson beginning from 2012 through 2016.<sup>2758</sup>

110. SSCOT proactively monitored for simulated funding and phone number changes.<sup>2759</sup>

111. The practice that the Bank referred to as simulated funding involved

<sup>2756</sup> MSD- 72 at 3-4 (emphasis added).

<sup>2757</sup> MSD-213 at 4, 7-8.

<sup>2758</sup> Russ Anderson Amended Answer ¶ 260; Julian Amended Answer ¶ 260; McLinko Amended Answer ¶ 260.

<sup>2759</sup> Russ Anderson Amended Answer ¶ 97; Julian Amended Answer ¶ 260; McLinko Amended Answer ¶ 260.

- the unauthorized transfer of customer funds between one customer account and another, unauthorized customer account.<sup>2760</sup>
112. The Community Bank did not proactively monitor other types of sales practices misconduct, including pinning, bundling, sandbagging, and the issuance of unauthorized debit and credit cards.<sup>2761</sup>
113. In the summer and fall of 2013, SSCOT conducted an analysis to detect instances of simulated funding and of employees changing customer phone numbers without customer authorization in Los Angeles/Orange County, and then across the regional footprint.<sup>2762</sup>
114. For the Los Angeles/Orange County and then regional footprint analysis, Respondent Russ Anderson approved SSCOT applying the following methodology to identify employees who, based on data analytics, exhibited activity that was a red flag for simulated funding: “account X was opened, account X was funded by virtue of an auto transfer from account Y, within one day funds were auto transferred from Account X back to account Y leaving account X with a \$0 or possibly a negative balance,” and “account X had no further funding activity within [] 60 day[s].”<sup>2763</sup>
115. After applying this methodology for identifying red flag simulated funding activity, SSCOT then referred for investigation only those employees who were “extreme outliers” for simulated funding (e.g., those who met the following restrictive criteria): “50 or more instances of the above activity occurring over the five month period review OR Four of the five months reflected 10+ accounts involved in this activity and 10% or more of checking/savings sales was involved in this activity.”<sup>2764</sup>
116. For the Los Angeles/Orange County and then regional footprint analysis, SSCOT identified employees who engaged in “potential falsification of customer phone numbers (possibly to circumvent 11Ways to Wow Customer Surveys)” by identifying instances in which a “Customer’s existing phone number was changed by 1-3 digits.”<sup>2765</sup> After applying this methodology, SSCOT then referred for investigation only those employees “having greater than 50 examples of unique phone number changes” in a three-month

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<sup>2760</sup> MSD-297 (Richards Tr.) at 82:4-84:4.

<sup>2761</sup> MSD-300 (Rawson Tr.) at 79:16-83:17; MSD-297 (Richards Tr.) at 96:6- 97:19; MSD-299 (Sperle Tr.) at 56:10-62:3.

<sup>2762</sup> MSD-105; MSD-106; MSD-107; MSD-155 at 4.

<sup>2763</sup> MSD-105 (emphasis in original); MSD-106; MSD-107; (“...the fact that the accounts only had one deposit and one withdrawal with no additional transactions ultimately resulting in a zero balance seems unusual”); MSD-265 (Farrell Dep. Tr.) at 369:16-370:24.

<sup>2764</sup> MSD-105 (emphasis added); MSD-106; MSD-107.

<sup>2765</sup> MSD-105; MSD-106; MSD-107.



period.<sup>2766</sup>

117. On October 18, 2013, Corporate Investigations sent Respondent Russ Anderson a Significant Investigation Notification.<sup>2767</sup> Respondent McLinko's direct report Bart Deese received the Significant Investigation Notification from Corporate Investigations.<sup>2768</sup> Mr. Deese provided Respondent McLinko with an updated Significant Investigation Notification on November 1, 2013.<sup>2769</sup> The Significant Incident Notification stated, "Corporate Investigations has deemed this case significant based on the number of team members impacted and the specific misconduct identified."<sup>2770</sup>
118. The Significant Investigation Notification noted that 177 bankers were identified for possible simulated funding.<sup>2771</sup> The allegation was that "Simulated funding falsified entries were made to meet individual and store sales goals."<sup>2772</sup> Individuals with "the most egregious simulated funding numbers were to be interviewed first."<sup>2773</sup> The criteria for identifying employees with the most egregious simulated funding numbers was the criteria of "50 or more accounts opened in 1 month or 10% of total accounts opened in a 4 month period."<sup>2774</sup> Those individuals with the most egregious phone number changes were also interviewed.<sup>2775</sup>
119. The Significant Investigation Notification Respondent Russ Anderson received contained the following key findings based on the investigation of employees with the most egregious simulated funding numbers: "[k]nowing their actions were against wfb [Wells Fargo Bank] policy[;] [t]o meet quarterly sales goals; following manager and/or prior manager's guidance[;] [l]earned from observing/talking to other team members[;] [h]ad customer's [sic] fund accounts with a \$50 deposit and then withdraw from atm[;] [a]ttempt to contact customer with unfunded accounts but would resort to auto transfers w/o customer consent to meet goals timely[.]"<sup>2776</sup>
120. As Corporate Investigations explained, "The SIN and IDEA notifications are

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<sup>2766</sup> MSD-105; MSD-106; MSD-107.

<sup>2767</sup> MSD-108.

<sup>2768</sup> *Id.*

<sup>2769</sup> MSD-333.

<sup>2770</sup> MSD-108 at 2.

<sup>2771</sup> *Id.*

<sup>2772</sup> *Id.* at 3 (emphasis added).

<sup>2773</sup> *Id.*

<sup>2774</sup> *Id.*

<sup>2775</sup> *Id.*

<sup>2776</sup> *Id.*

designed to ensure that the investigative findings are appropriately shared with all appropriate key stakeholders. The goal of the SIN and IDEA is to ensure all key stakeholders are aware of the issue and that they review for possible follow-up specific to their role and responsibility within the organization. A primary role for each LOB [line of business] Group Risk Officer is to mitigate risks and acts of TM [team member] misconduct and fraud are a key part of these risks.”<sup>2777</sup>

121. The analysis from SSCOT in the summer and fall of 2013 to identify employees engaged in egregious patterns of simulated funding and phone number changes led to an initial round of investigations that resulted in terminations of approximately 35 employees in the fall of 2013, followed by a footprint-wide investigation of similar conduct across the Regional Bank.<sup>2778</sup>
122. On October 3, 2013, the *Los Angeles Times* published an article under the headline, “Wells Fargo Fires Workers Accused of Cheating on Sales Goals.” The article reported that the Bank had fired 30 employees in the Los Angeles region for “open[ing] accounts that were never used and attempt[ing] to manipulate customer-satisfaction surveys.” The article further reported “the pressure to meet sales goals was intense” and that there were cases of forged customer signatures and accounts opened without customer knowledge.<sup>2779</sup>
123. On December 21, 2013, the *Los Angeles Times* published a second article, with the headline: “Wells Fargo’s Pressure-Cooker Sales Culture Comes at a Cost.” The article stated it was based on interviews with 28 former and seven current employees across nine states. This article reported that employees were threatened with termination if they failed to meet their sales goals.<sup>2780</sup>
124. Respondents Julian and McLinko were both aware of the October 2013 and December 2013 Los Angeles Times articles about the Community Bank’s sales practices.<sup>2781</sup>
125. The pause on the Community Bank’s proactive monitoring of simulated funding and phone number changes did not end until July 2014, in that SSCOT did not begin to refer cases generated from the proactive monitoring reports to Corporate Investigations until then.<sup>2782</sup> There was no lookback conducted of potential simulated funding and phone number changes that occurred prior to

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<sup>2777</sup> MSD-221 at 2.

<sup>2778</sup> Russ Anderson Amended Answer ¶ 99; MSD-114 at 2-3.

<sup>2779</sup> Russ Anderson Amended Answer ¶ 100; MSD-331 (email forwarding Oct. 2013 LA Times Article) (Russ Anderson asking Mr. Bacon for “some context” because she “wasn’t aware of this situation”); MSD-56 (Christoff Decl.) at ¶ 16.

<sup>2780</sup> Russ Anderson Amended Answer ¶ 101; MSD-111.

<sup>2781</sup> Julian Amended Answer ¶ 55, 102; McLinko Amended Answer ¶ 55, 102; MSD-531 (a colleague warning Respondent McLinko that “it poses reputation risk to the firm”).

<sup>2782</sup> MSD-115 at 2, 3.

- April 2014.<sup>2783</sup>
126. When SSCOT resumed proactive monitoring of simulated funding in July 2014, the Community Bank used a threshold that identified for further investigation only the top 0.01% of employees who engaged in “red flag” simulated funding activity. The other 99.99% of employees engaging in “red flag” activity were not referred for investigation as a result of the proactive monitoring.<sup>2784</sup>
127. SSCOT’s application of the 99.99% threshold beginning in July 2014 identified approximately 30,000 employees per month who exhibited activity that was a red flag for simulated funding. SSCOT referred for investigation only the top 0.01% of those employees who had the most activity indicative of simulated funding, or 3 employees per month. In other words, SSCOT referring for investigation only 1 out of every 10,000 employees who exhibited red flag activity for simulated funding.<sup>2785</sup>
128. The “extreme outlier” employees identified for further investigation through SSCOT’s proactive monitoring of simulated funding had not been previously identified and terminated through the Bank’s other reactive detective means, such as the EthicsLine or customer complaints.<sup>2786</sup>
129. From April 2015 through October 2016, SSCOT lowered the threshold slightly to refer for investigation those employees at or above the 99.95th percentile of activity that was a red flag for simulated funding. SSCOT’s proactive monitoring of simulated funding never looked beyond the most egregious offenders.<sup>2787</sup>
130. Lowering the threshold to the 99.95<sup>th</sup> percentile resulted in the identification and referral of approximately 15 to 23 employees per month.<sup>2788</sup>
131. The 99.95% percent threshold captured employees who had on average 10.3

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<sup>2783</sup> MSD-115.

<sup>2784</sup> Russ Anderson Amended Answer ¶ 104; MSD-116 at 3; MSD-300 (Rawson Tr.) at 91:21-94:22, 177:2-22; MSD-602 (Bernardo Tr.) at 109:12-112:25, 115:3-116:2.

<sup>2785</sup> MSD-116 at 3; see also MSD-300 (Rawson Tr.) at 176:17-179:11.

<sup>2786</sup> MSD- 300 (Rawson Tr.) at 90:18-91:20.

<sup>2787</sup> Russ Anderson Amended Answer ¶ 106; MSD- 116 at 3; MSD-115 at 3 (describing the evolution of thresholds); MSD-300 (Rawson Tr.) at 158:24-163:3 225:11-22 (testifying that plan to expand thresholds was not approved); Russ Anderson Dep. Tr. 229:6-17, 225:4-22; MSD-299 (Sperle Tr.) at 110:20-111:1 (testifying that SSCOT continued using the 99.95 threshold for identifying simulated funding, even in 2016); MSD-118; MSD-119; MSD-121.

<sup>2788</sup> MSD-603; MSD-116 at 3; MSD-119 at 1-2 (noting that application of the 99.95% captures the “more egregious behavior”); MSD- 122; MSD-300 (Rawson Tr.) at 169:7-172:10, 213:16-23; MSD-299 (Sperle Tr.) at 170:9- 171:13.

occurrences of red flag activity for simulated funding each month.<sup>2789</sup>

132. The Bank's former Head of Financial Crimes Risk Management James Richards explained to Respondent Russ Anderson that "applying percentage based, purely percentage based thresholds allows you to manage to the output from those thresholds rather than to manage to the underlying risk or underlying activity that you're monitoring. It allows you to manage the output."<sup>2790</sup>

133. As part of the Bank's February 2020 Deferred Prosecution Agreement with the U.S. Department of Justice related to its sales practices, the Bank admitted, accepted, and acknowledged as true the following:

- Gaming conduct and the practice of pushing unnecessary accounts on customers began in at least 2002 and became widespread over time, lasting through 2016, when the community Bank eliminated product sales goals for its employees.
- From 2002 to 2016, Wells Fargo opened millions of accounts or financial products that were unauthorized or fraudulent. During that same time period, Wells Fargo employees also opened significant numbers of additional unneeded, unwanted, or otherwise low-value products that were not consistent with Wells Fargo's purported needs-based selling model. Wells Fargo collected millions of dollars in fees and interest to which the Company was not entitled, harmed the credit ratings of certain customers, and unlawfully misused customers' sensitive personal information (including customers' means of identification).
- Millions of non-Wells Fargo-employee customer accounts reflected a Wells Fargo email address as the customer's email address, contained a generic and incorrect customer phone number, or were linked to a Wells Fargo branch or Wells Fargo employee's home address.
- Millions of secondary accounts and products were opened from 2002 to 2016, and many of these were never used by customers.<sup>2791</sup>

134. Respondent McLinko testified in March 2018 that thousands of Wells Fargo employees issued millions of products and services without customers' consent:

Q All right. You -- I think that based on everything you've read, that central report, the PricewaterhouseCooper report, and your audit work, do you believe now that, over the years, let's say from 2009 to 2016, thousands of

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<sup>2789</sup> MSD-119; MSD-300 (Rawson Tr.) at 165:11-19.

<sup>2790</sup> MSD-297 (Richards Tr.) at 146:11-148:20.

<sup>2791</sup> MSD-1 at 27, 31 ¶¶ 17-18, 32.

Wells Fargo employees issued products and services to customers without the customers' consent?

A Based upon everything that I've read, that's correct.

Q: Okay. And based on what you have seen and all the information you gathered, those thousands of Wells Fargo employees have issued millions of products and services without customers' consent?

MR. CRUDO: Foundation.

THE WITNESS: Based upon the data that was produced, on the filing of the data analysis that's done, and the modeling, yes.<sup>2792</sup>

135. The Bank's former Chief Risk Officer testified that "the sales practice problem as described in this 2004 [Investigation Report] is essentially the same problem that existed at the bank up until the elimination of sales goals in the fall of 2016."<sup>2793</sup>
136. After publication of the 2016 Consent Orders with the OCC and CFPB and settlement with the City of LA, a regional leader in California forwarded negative media coverage of the Bank's sales practices "crisis", commenting that the "[o]nly thing this article is missing is that [the sales practices crisis] wasn't created over the span of 5 years – this was created since 2002!"<sup>2794</sup>
137. The Bank's former Head of Corporate Investigations Loretta Sperle agreed in sworn testimony that given the Community Bank's business model and the controls that existed at the Bank, every customer-facing employee had a daily temptation and opportunity to cheat. She testified before the OCC that given the amount of pressure that existed at the Bank, it would not be surprising "that there is going to be a high percentage of people that will cheat."<sup>2795</sup>
138. Bankers received sales credit for unfunded accounts.<sup>2796</sup>
139. As of December 2015, the Bank had approximately 12.4 million accounts that had been inactive for the last 12 months, including nearly 7 million debit cards (approximately 18% of all debit cards accounts had been inactive for the last 12 months).<sup>2797</sup>

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<sup>2792</sup> McLinko Amended Answer ¶ 8; SS at 124:1-18.

<sup>2793</sup> MSD-290B (Loughlin Tr.) at 332:22-333:7.

<sup>2794</sup> MSD-550.

<sup>2795</sup> MSD- 299 (Sperle Tr.) at 160:16-163:4; see also MSD-269 (NBE Candy Expert Report) at ¶ 108, 114; MSD-581 (Clegg Tr.) at 46:11-48:13; MSD-223 at OCC-WF-SP-06963006 ("Focus on 'business practices & business processes' (are they creating need or opportunity)").

<sup>2796</sup> MSD-243; MSD-269 (NBE Candy Expert Report) at ¶ 107(c) ("the Community Bank allowed employees to have approximately 30 percent of the new accounts they opened to remain unfunded; they would still be eligible to receive sales credit for the unfunded accounts."

<sup>2797</sup> MSD-604.

140. Debit card accounts were a “major contributor” to customer consent cases and represented an “outsize portion of conduct risk.”<sup>2798</sup>
141. Debit cards generally represented about 25% of all solutions sold by the Community Bank each year.<sup>2799</sup> For example, in 2013, approximately 10.3 million consumer and business debits cards were sold, which comprised about 24.1% of total solutions sold that year.<sup>2800</sup>
142. Respondents’ only expert to opine on the PwC work admitted he has done no analysis to confirm or quantify false negatives related to the PwC data (i.e. unauthorized accounts in fact affected by simulated funding that were excluded from PwC’s estimate of potentially unauthorized accounts), though he testified “it seems very likely that there would be, you know, false – some false negatives.”<sup>2801</sup>
143. Audit relied on PwC’s sales practices work and did not conduct its own analysis of the scope of the sales practices. Audit noted that its work on the identification of customers and associated financial harm for the customer account analysis and the historical complaints analysis was complete: “For the customer account analysis, based on our assessment of the implementation of the analytical approach by PwC to identify potentially impacted customers, and the identification of the associated reimbursement amounts, we are reasonably confident that the work is accurate and complete.”<sup>2802</sup>
144. Respondent McLinko testified that the model used by PwC was “probably substantially correct.”<sup>2803</sup>
145. A report distributed to regional leaders on July 2, 2013 showed that “11.26% of accounts that are funded in West Coast are done so using simulated funding (vs 6.82% for regional banking [nationwide]) and approx[imately] 60% of those accounts are closed within 90 days.”<sup>2804</sup>
146. The former Head of Corporate Investigations Michael Bacon testified that the senior leadership in the Community Bank wanted to minimize terminations even with strong evidence that an employee engaged in sales integrity

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<sup>2798</sup> MSD-239; MSD-60 (“This furthers my view that debit cards should be one of our primary areas of focus . . . It’s a major contributor in cases involving both Tellers and PBs [Personal Bankers], and it’s the primary factor in customer consent allegations. Also, as we noted in previous conversations, the debit card can be a ‘doorway’ to additional unethical sales (online, billpay, rewards.)”); see also MSD-18; MSD-23; MSD-46; MSD-61; MSD-62; MSD-63 (discussing that “an outsize portion of conduct risk is related to” issuance of secondary checking and secondary debit cards); MSD-64; MSD-150.

<sup>2799</sup> MSD-605; MSD-606; MSD-607; MSD-608.

<sup>2800</sup> MSD-608.

<sup>2801</sup> MSD-282A (Wilcox Dep. Tr.) at 125:12-126:10.

<sup>2802</sup> MSD-347; MSD-413 at 14.

<sup>2803</sup> MSD-276 (McLinko Tr.) at 124:20-125:4.

<sup>2804</sup> MSD-227.

- violations.<sup>2805</sup>
147. From January 2011 through March 2016, the Bank terminated over 5,300 employees for engaging in improper sales practices.<sup>2806</sup> Improper sales practices included:
- (a) Opening any account without the consumer's consent;
  - (b) Transferring funds between a consumer's accounts without the consumer's consent;
  - (c) Applying for any credit card without the consumer's consent;
  - (d) Issuing any debit card without the consumer's consent;
  - (e) Enrolling any consumer in online-banking services without the consumer's consent.
148. SSCOT outlined the criteria for simulated funding monitoring. In a May 11, 2015 analysis, Paula Bernardo presented a chart showing the Simulated Funding outlier criteria as it existed in 2014.<sup>2807</sup> From the Sales Quality Proactive Monitoring Plan report, Ms. Russ Anderson's subordinate reported that Sales Quality was continuing previously established monitoring that defined outliers as the top "99.99 percentile of team members participating in each activity except Low Debit Card Activations" – and specifically included identified those activities as including instances of "missing signatures" and low debit card activations.<sup>2808</sup>
149. According to Kathlyn Farrell, Ms. Russ Anderson's expert witness, use of the 99.99 (and later 99.95) percentile for this monitoring model only caught the worst offenders of simulated funding, so only a small percentage of employees, i.e., only the top .01 percent of employees with potential simulated funding activity would be identified for investigation.<sup>2809</sup>
150. According to NBE Candy, these two thresholds were not disclosed to the OCC during the May 2015 examination.<sup>2810</sup> Through her subsequent investigation, after familiarizing herself with how the thresholds had been used, NBE Candy concluded that the reports provided by Ms. Russ Anderson's subordinate supported the conclusion that using the 99.99 percent threshold, "over 30,000 team members per month engaged in at

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<sup>2805</sup> MSD-295 (Bacon Tr.) at 62:8- 25.

<sup>2806</sup> MSD-52; MSD-661 at 96.

<sup>2807</sup> MSD-116 at 3.

<sup>2808</sup> R. Ex. 17391 at 1.

<sup>2809</sup> Tr. (Farrell) at 10515-16.

<sup>2810</sup> Tr. (Candy) at 1079.

least one instance of activity that was indicative of simulated funding.”<sup>2811</sup>  
She found that only three to six team members were actually referred to Corporate Investigations for simulated funding.<sup>2812</sup>

151. When asked how she knew that approximately 30,000 employees exhibited red flag activity for simulated funding per month, NBE Candy responded:

A few different ways. One is understanding what the threshold means. So when they used a 99.99 percent threshold, that means they’re not going to look at 99.99 percent; they are looking at, or Ms. Russ Anderson’s group was looking at the .01 percent of that, of team members that engaged in that behavior. So one, it is simple math.

When you take to six number of people that they were referring to corporate investigations and apply the facts that they're looking at, that .01, that will get you between 30,000 and 60,000 team members per month that engaged in activity indicative of simulated funding. And it's not a surprise that that number varies because this is measured on a monthly basis, so it's not going to be the same month to month.

But also I have reviewed documentation from the bank that has confirmed that during this time period about 45 percent of Community Bank employees had, were engaging in the red flag activity for simulated funding. At this time there was roughly 70,000 customer-facing people in the Community Bank, which also translates to that 30,000 figure.

Lastly, in Ms. Rebecca [Rawson’s] testimony, who was the head of SSCOT during this period, she testified to, you know, knowledge of that 45 percent of team members were engaging in activity that was a red flag for simulated funding, and she confirmed the methodology that I have described today.<sup>2813</sup>

152. Preponderant evidence established that SSCOT’s application the 99.99% threshold beginning in July 2014 identified approximately 30,000 employees per month who exhibited activity that was a red flag for simulated funding. Only 1 out of every 10,000 employees were referred for further investigation.<sup>2814</sup>

153. Of all the issues Bank employees could report to the EthicsLine (the whistleblower hotline), the most common issue was sales integrity, ultimately

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<sup>2811</sup> Tr. (Candy) at 1080.

<sup>2812</sup> *Id.* at 1080; (Report of NBE Candy) at 9, 84, 93, and 95(a).

<sup>2813</sup> Tr. (Candy) at 1081-82.

<sup>2814</sup> MSD-116 at 3.



- comprising more than half of all EthicsLine complaints.<sup>2815</sup>
154. An investigator testified that there were a “multitude of ways” employees engaged in sales practices misconduct: “Oh, simulated funding, opening accounts for nonexistent people, opening accounts for deceased people, opening multiple checking accounts where a person should only have one, if that. It would depend on the emphasis during that time period.”<sup>2816</sup>
155. Audit, including Respondents Julian and McLinko, had certain oversight responsibilities with respect to incentive compensation, risk, compliance, and/or preparing audit reports.<sup>2817</sup>
156. According to the *Comptrollers Handbook on Internal and External Audits*, “Well-planned, properly structured auditing programs are essential to effective risk management and adequate internal control systems. Effective internal and external audit programs are also a critical defense against fraud and provide vital information to the board of directors about the effectiveness of internal control systems.”<sup>2818</sup>
157. According to the *Comptrollers Handbook on Internal and External Audits* “Internal audit programs are a bank’s primary mechanism for assessing controls and operations and performing whatever work is necessary to allow the board and management to accurately attest to the adequacy of the bank’s internal control system.”<sup>2819</sup> The handbook continues: “Internal auditors must understand a bank’s strategic direction, objectives, products, services, and processes to conduct these activities. The auditors then communicate findings to the board of directors or its audit committee and senior management.”<sup>2820</sup>
158. Wells Fargo Audit Services was the Bank’s third line of defense.<sup>2821</sup>
159. The responsibilities of WFAS were set forth in its charter. According to its charter, “The scope of internal audit work is to determine if the Company’s risk management, systems of control, and governance processes are adequate and functioning as intended.”<sup>2822</sup>

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<sup>2815</sup> MSD-3 at 52; MSD-161-168; MSD-430 at 15 (“Over 50% of [EthicsLine] calls were related to sales integrity.”); MSD-324 at 5 (showing that sales integrity cases made up 48% of EthicsLine cases).

<sup>2816</sup> MSD-581 (Clegg Tr.) at 47:9-48:1.

<sup>2817</sup> Julian Amended Answer ¶ 16.

<sup>2818</sup> MSD-273 at 10.

<sup>2819</sup> *Id.*; *see id.* at 12 (“The primary role of internal auditors is to independently and objectively review and evaluate bank activities to maintain or improve the efficiency and effectiveness of a bank’s risk management, internal controls, and corporate governance.”)

<sup>2820</sup> MSD-273 at 12.

<sup>2821</sup> Julian Amended Answer ¶ 388; McLinko Amended Answer ¶ 388.

<sup>2822</sup> MSD-422B (2012) at 3; MSD-422C (2013) at 3; MSD-422D (2014) at 1; MSD-422E (2015) at 24; Julian Amended Answer ¶ 388; McLinko Amended Answer ¶ 388.

160. WFAS's charter further states that Audit "[c]onducts tests and provides conclusive reporting regarding the health of the [Bank's] risk management and internal control structure" and "[f]unctions as a change agent to ensure risk issues are escalated and resolved."<sup>2823</sup>

161. WFAS's charter further states that Audit performs work to assure:

- (a) "Corporate Governance functions and processes provide adequate direction and oversight;"
- (b) "An appropriate culture has been established, understood, and consistently complied with across the organization;"
- (c) "The risk management system is adequately designed to ensure risks, including emerging risks, are appropriately identified and managed, and risk approvals, acceptances, and escalations are appropriately administered;"
- (d) "Operational risk is effective so that risk of loss resulting from inadequate or failed internal processes, people and systems or from external events is adequately controlled;"
- (e) "Fraud risk management is effectively managed and the company's customers and internal resources are protected;"
- (f) "Reputation risk is effectively managed and the company's brand protected;"
- (g) "Compensation programs incent appropriate and desired behavior;" and
- (h) "Policies are sound/strong and employees' actions are in compliance with the policies, standards, procedures, and applicable laws and regulations."<sup>2824</sup>

162. Respondent Julian testified before the OCC: "Audit's role is to come in and to assess the adequacy of those controls to ensure that . . . they're working as appropriate. And if not, then to provide . . . comment, provide issues, raise concerns to management, raise concerns to the Board[.]"<sup>2825</sup>

163. The Bank had a Fraud Risk Management Policy. With respect to WFAS's fraud risk management responsibilities, the Bank's Fraud Risk Management Policy states that WFAS "[p]rovides independent evaluation of the fraud controls that management has designed and implemented, including direct

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<sup>2823</sup> MSD-422B (2012) at 3; MSD-422C (2013) at 3; MSD-422D (2014) at 1; MSD-422E (2015) at 24.

<sup>2824</sup> MSD-422C (2013) at 3; MSD-422D (2014) at 1; MSD-422E (2015) at 24; Julian Amended Answer ¶ 390; McLinko Amended Answer ¶ 390.

<sup>2825</sup> MSD-278 (Julian Tr.) at 21:18-22:23; Julian Amended Answer ¶ 391; McLinko Amended Answer ¶ 391; see MSD-413 at 1.

- business controls” and “[p]erforms direct audits of business fraud programs and controls.”<sup>2826</sup>
164. The Bank also had a Responsible Business Policy. The policy stated that “WFAS carries out its responsibilities as risk management’s ‘third line of defense’ by auditing for UD(A)AP and “[r]eferring suspected violations of law or regulation to the Law Department and Business Compliance” and “Providing independent evaluations of [UD(A)AP] controls.”<sup>2827</sup>
165. WFAS had significant resources to satisfy its essential auditing responsibilities with respect to risk management and control. For example, in 2014, WFAS’s annual budget was around \$120 million, it had 941,000 planned audit hours, 753 approved FTEs, and 555 audit engagements.<sup>2828</sup>
166. As Chief Auditor, Respondent Julian reported directly to the Audit and Examination Committee of the Board (“Audit and Examination Committee”) and administratively to the Chief Executive Officer (“CEO”) and oversaw the work of Audit.<sup>2829</sup> As Respondent Julian testified: “the reason I report to the -- to the chair of the Audit Committee is because I am assessing and providing criticism on the entire company. That includes the CEO. So I need or have the independence to be able – and the confidence to be able to criticize, if I had an occasion, the CEO knowing that he wouldn’t then turn around and fire me for it.”<sup>2830</sup>
167. Respondent Julian was a member of the Operating Committee, a group of the most senior executives of the Bank, including the CEO and Carrie Tolsted.<sup>2831</sup>
168. Respondent Julian was a member of the Bank’s Enterprise Risk Management Committee. The committee’s charter stated the committee was responsible for “understand[ing] and evaluat[ing] risk, address[ing] escalated issues, and provid[ing] active oversight of risk mitigation.” The Enterprise Risk Management Committee could escalate any issue to the Operating Committee or the CEO, and reported quarterly to the Operating Committee and Risk Committee of the Board.<sup>2832</sup>
169. Respondent Julian was a member of the Bank’s Team Member Misconduct Executive Committee (“TMMEC”).<sup>2833</sup> The TMMEC charter stated that the

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<sup>2826</sup> MSD-238 at 7.

<sup>2827</sup> MSD- 306 at 13.

<sup>2828</sup> MSD-636 at 3, 20; MSD-637 at 18-19.

<sup>2829</sup> Julian Amended Answer ¶¶ 9, 381, 382, 391, 392; MSD-278 (Julian Tr.) at 65:13-21.

<sup>2830</sup> MSD-278 (Julian Tr.) at 65:13-21.

<sup>2831</sup> Julian Amended Answer ¶¶ 11, 383.

<sup>2832</sup> Julian Amended Answer ¶ 155; MSD-435.

<sup>2833</sup> Julian Amended Answer ¶¶ 157, 383.

“committee consists of senior executive who share responsibility for the appropriate management of team member misconduct and internal fraud matters” and the “purpose of the Team Member Misconduct Executive Committee is to provide a forum for Wells Fargo executive management to provide leadership, oversight and direction related to team member misconduct and internal fraud risk management.”<sup>2834</sup>

170. Respondent Julian was a member of the Bank’s Ethics Committee. The 2013 “Wells Fargo’s Risk Management Framework” stated that “[t]he Ethics Committee is responsible for administering and interpreting the Wells Fargo Code of Ethics and Business Conduct, as well as approving its content.”<sup>2835</sup>

171. Respondent Julian was a member of the Bank’s Incentive Compensation Steering Committee, later renamed the Incentive Compensation Committee.<sup>2836</sup> The Incentive Compensation Committee charter stated that the committee “is chartered to . . . provide oversight around the design and outcomes of the business line incentive plans, and lead Wells Fargo’s enterprise efforts to enhance incentive compensation practices throughout the Company.”<sup>2837</sup>

172. As one of Mr. Julian’s direct reports, Respondent McLinko had access to each of the committees on which Mr. Julian served, irrespective of whether such service was as a voting or non-voting member.

173. At his deposition in this proceeding, Respondent Julian could not remember attending any Incentive Compensation Committee meetings. He could not remember the committee issuing any policy statements or reviewing any compensation plans, and did not know whether the committee had criticized any individual incentive compensation plans.<sup>2838</sup>

174. Similarly, Ken Zimmerman, the Community Bank’s representative on the Incentive Compensation Committee could not recall serving on the Incentive Compensation Committee, even though he believed he would have remembered it “[b]ecause it looks like it’s kind of a big deal.”<sup>2839</sup>

175. In or around October 2018, the Bank placed Respondent Julian on administrative leave.<sup>2840</sup>

176. Respondent Julian retired from the Bank in or around October 2019.<sup>2841</sup>

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<sup>2834</sup> Julian Amended Answer ¶ 157; MSD-417.

<sup>2835</sup> Julian Amended Answer ¶ 159; 383; MSD-418 at 2.

<sup>2836</sup> MSD-279 (Julian Dep. Tr.) at 36:18-23; MSD-421 at 27-28; MSD-687; MSD-712.

<sup>2837</sup> Julian Amended Answer ¶ 153; (MSD-421 at 24.

<sup>2838</sup> MSD-279 (Julian Dep. Tr.) at 37:11-41:15.

<sup>2839</sup> MSD-583B (Zimmerman Tr.) at 505:4-506:12.

<sup>2840</sup> Julian Amended Answer ¶ 384.

<sup>2841</sup> Julian Amended Answer ¶ 385.

177. In his post-hearing brief, Respondent McLinko asserted that Enforcement Counsel had failed to prove that he was an officer of the Bank from June 10, 2014 to June 26, 2014, and after June 26, 2015. This assertion lacks a factual basis and is rejected.
178. The Notice of Charges included the factual claim that from approximately 2011 to 2017 Mr. McLinko “was an Executive Audit Director at the Bank, responsible for auditing the Community Bank.”<sup>2842</sup> In his amended answer, Mr. McLinko admitted this was true, responding that he held the title of Executive Audit Director at the Bank “from approximately late 2008 to at least 2018” and that, with the exception of an approximately six-month period during 2012, he was “an Executive Audit Director for the Community Bank from approximately 2011 to 2017” with “responsibilities for overseeing the auditing of the Community Bank.”<sup>2843</sup>
179. Preponderant evidence has established that Mr. McLinko is an institution-affiliated party and that throughout the relevant period Mr. McLinko was an Executive Audit Director for the Community Bank from the fourth quarter of 2010 to 2017 and had responsibilities for overseeing the auditing of the Community Bank.<sup>2844</sup>
180. From March 2012 to 2018, Respondent McLinko reported to Respondent Julian.<sup>2845</sup>
181. During his tenure as Executive Audit Director for the Community Bank between 2010 and 2017, Respondent McLinko had responsibilities concerning “oversight of the audits performed by WFAS’s Community Bank & Operations Group, which included setting the audit strategy, reviewing and approving draft audit reports, complying with Audit’s charter, and providing credible challenge to Community Bank management, as necessary.”<sup>2846</sup>
182. As EAD, Respondent McLinko had responsibilities concerning “oversight of the Community Bank’s audit team’s execution of their duties consistent with Audit’s responsibilities” and “the accuracy and completeness of the Community Bank’s audits.”<sup>2847</sup>
183. Respondent McLinko was a member of the Community Bank’s Internal Fraud Committee, which received reporting from Corporate Investigations regarding, in part, sales integrity cases and investigations related to lack of

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<sup>2842</sup> Notice of Charges at ¶439.

<sup>2843</sup> Amended Answer of Respondent Paul McLinko to Notice of Charges at ¶439.

<sup>2844</sup> McLinko Amended Answer ¶ 439.

<sup>2845</sup> Julian Amended Answer ¶ 440, McLinko Amended Answer ¶ 440.

<sup>2846</sup> McLinko Amended Answer ¶ 444.

<sup>2847</sup> McLinko Amended Answer ¶¶ 445-46.

- customer consent for products and services.<sup>2848</sup>
184. By no later than February 2015, Respondent McLinko was a member of the Community Banking Risk Management Committee.<sup>2849</sup> The Committee was responsible for understanding the Community Bank’s risk profile and to ensure risks were managed effectively. Specifically, the committee identified and evaluated current and emerging material risks, determined whether appropriate balances exist between risk and reward, and identified exposures that may change the operational risk portfolio.<sup>2850</sup>
185. The Community Banking Risk Management Committee also was to ensure risk appetite was considered throughout the new product planning processes, strategic decision-making, and business practices process by each appropriate line of business. The committee served “as the primary management-level forum for the consideration of the highest priority risk issues resident in Community Banking . . . and support and assist Wells Fargo’s Enterprise Risk Management Committee (ERMC) in carrying out its risk oversight responsibilities.”<sup>2851</sup>
186. By at least October 2015, Respondent McLinko was a member of the Community Banking Conduct Risk Oversight Committee.<sup>2852</sup> The Committee was established to understand Community Bank’s risk profile and work to provide visibility and transparency into business line strategy, progress, risks, and future opportunities to ensure sales practices risk are managed effectively. The Committee defined sales practices as: “risk of customer harm, reputational damage, financial loss, litigation, and regulator non-compliance associated with sales practices” within Community Bank.<sup>2853</sup>
187. The Community Banking Conduct Risk Oversight Committee was accountable for: “1. Identify[ing] and evaluate[ing] current and emerging material risks and examine trends appropriate for conduct risk oversight. Assess[ing] strategic implications for business objectives and sales practices risk management. 2. Review[ing] conduct risk activities, including: cross-selling, the drive to meet financial targets (including, potentially, sales goals) and key behavioral motivators (including incentive compensation arrangements and team member recognition and rewards practices) as well as important HR processes (including recruitment and training and performance

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<sup>2848</sup> McLinko Amended Answer ¶ 449.

<sup>2849</sup> MSD-307 at 40 (showing Respondent McLinko as a member of the Community Bank Risk Management Committee)

<sup>2850</sup> MSD-307 at 36; McLinko Amended Answer ¶¶ 161, 255.

<sup>2851</sup> MSD-307 at 36.

<sup>2852</sup> MSD-309 at 4; MSD-338 at 4.

<sup>2853</sup> MSD-309 at 1; MSD-338 at 1.

- management) for, in particular, customer-facing team members.”<sup>2854</sup>
188. Respondent McLinko retired from the Bank on or around April 2019.<sup>2855</sup>
189. Respondent Julian also received information showing that there were sales integrity cases in every region in the Community Bank and that customer consent cases were the most common sales-integrity case type.<sup>2856</sup>
190. Corporate Investigations (also called Corporate Security) prepared quarterly updates that were included in WFAS’s quarterly reports to the Audit and Examination Committee of the Board.<sup>2857</sup> In Audit’s February 2012 report to the Audit and Examination Committee, Corporate Security noted a 44% increase in Suspicious Activity Report (“SAR”) filings in 2011 related to team member misconduct and attributed the increases in part to “sales integrity issues involving a possible violation of law.” Corporate Investigation’s report also noted 42% of all EthicsLine reports were referred to the Community Bank’s Sales Quality Team (i.e. they were related to possible sales integrity violations).<sup>2858</sup>
191. During the April 2012 Ethics Committee meeting, Head of Corporate Investigations Michael Bacon provided a written presentation to the Ethics Committee that showed that over 90% of EthicsLine reports in 2011 related to Community Banking and the vast majority of EthicsLine cases referred to Corporate Investigations related to sales integrity violations. Specifically, it showed that Corporate Investigations opened 1,339 sales integrity violations cases from EthicsLine complaints in 2010 and opened 1,220 sales integrity violations cases from EthicsLine complaints in 2011.<sup>2859</sup>
192. Respondent Julian testified to the OCC during its investigation:
- Q. Once Mr. McLinko and yourself got this email is there any excuse for audit not to investigate further to see whether what Mr. Bacon is pointing to is a serious issue or not?
- A. Yes. Again, I am not sure what Paul would have or did do in this. I can’t say that he didn’t. We get, not an excuse, we cover a broad range.
- This was one example where it appears Michael is raising a concern that ultimately turned out to be a valid concern. Whether it was looked into by Paul or not at that time I am not sure, but –

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<sup>2854</sup> MSD-309 at 1; MSD-338 at 1.

<sup>2855</sup> McLinko Amended Answer ¶ 441.

<sup>2856</sup> See, e.g., MSD-420 at 9.

<sup>2857</sup> MSD-279 (Julian Dep. Tr.) at 204:15-207:1.

<sup>2858</sup> MSD-425 at 3-4.

<sup>2859</sup> MSD-506 at 8, 10.

Q. Okay. I'm sorry.

A. So you used the word "excuse," I'm not sure I am in the excuse making. I mean it's clear we didn't do enough based on what I know now to investigate.

Q. No, I understand that historically you don't know what, if anything, Mr. McLinko did in response to getting to this email, is that correct?

A. I don't recall, yes, what he would have did or didn't do.

Q. Okay, all right. My question is not like a historical question on what Mr. McLinko or anybody in audit did or didn't do, my question is more about what you would expect a competent audit department or competent auditor to do. If a competent auditor gets an email like this from corporate investigation, what should they do?

A. Again, depending on the overall context, but they should look further into to see if the concerns raised by, in this case, Michael Bacon were valid and relevant or not relevant valid concerns.<sup>2860</sup>

193. The TMMEC presentation listed misconduct governance supporting policies and processes, including:

- (a) "Comprehensive Team Member Misconduct/Fraud Investigations Program (includes routine reporting of results, escalation or risks/control breakdowns/systemic issues, partnering with audit, and components specific to strategic internal fraud testing and ongoing internal fraud assessments);"
- (b) Senior Leader / Operating Committee / A&E / GRO & Audit escalation processes;" and
- (c) "Investigative Key Activity reporting to all key stakeholders, LOB Internal Fraud Committees, GEVPS, and Audit & Examination Committee."<sup>2861</sup>

194. The TMMEC presentation provided an update on the establishment of Internal Fraud Committees within each line of business, including the Community Bank. The update provided: "[a]s stated within the Corporate Fraud Policy, the primary responsibility for adequate response to investigation results lies with LOB senior leaders, GROs, and LOB specific internal fraud committee members" and "LOB [Internal Fraud Committee] membership includes, but [is] not limited to . . .

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<sup>2860</sup> Julian Amended Answer ¶ 402; MSD-278 (Julian Tr.) at 166:19-168:5; 168:6-170:19).

<sup>2861</sup> MSD-436 at 7.



*Audit.*<sup>2862</sup>

195. The presentation further showed the TMMEC that sales integrity violations was the second-most common Corporate Investigations case type and that sales integrity violations were at 3,108 for 2012, up from 2,992 in 2011. It also showed that the vast majority of Corporate Investigation cases in both 2011 and 2012 originated in the Community Bank.<sup>2863</sup>
196. In the February 26, 2013 WFAS Fourth Quarter 2012 Summary to the Audit and Examination Committee, Corporate Security reported that sales integrity violations and related falsifications were one of the top four case types and had increased 4% over the prior year's volume. The report explained that the increase could be partly attributed to enhanced monitoring and detection, and a slight increase in misconduct in some regions.<sup>2864</sup>
197. The October 3, 2013 *Los Angeles Times* article stated that the Bank "fired about 30 branch employees in the Los Angeles region who the bank said had opened accounts that were never used and attempted to manipulate customer-satisfaction surveys." According to the article, a Bank spokesperson explained that "[t]he employees were trying to take shortcuts to meet sales goals." The article also stated that one of the fired employees said, "in some cases signatures were forged and customers had accounts opened in their names without their knowledge" and "the pressure to meet sales goals was intense at Wells Fargo."<sup>2865</sup>
198. On December 21, 2013, the *Los Angeles Times* published an article titled "Wells Fargo's Pressure-Cooker Sales Culture Comes at a Cost." The article stated it was based on interviews with 28 former and seven current employees across nine states and reported that "To meet quotas, employees have opened unneeded accounts for customers, ordered credit cards without customers' permission and forged client signatures on paperwork" and employees were threatened with termination if they failed to meet their sales goals.<sup>2866</sup>
199. Respondent Julian testified to the OCC during its investigation that after he read the 2013 *Los Angeles Times* articles, he started "thinking that, gosh, is there a problem" with Community Bank sales practices misconduct.<sup>2867</sup>
200. Corporate Security's update in the February 25, 2014 WFAS Fourth Quarter 2013 Summary to the Audit and Examination Committee explained that a

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<sup>2862</sup> MSD-436 at 10.

<sup>2863</sup> *Id.* at 11.

<sup>2864</sup> MSD-523 at 51.

<sup>2865</sup> MSD-331.

<sup>2866</sup> Julian Amended Answer ¶ 101; MSD-111 at 1-2). Respondent Julian was aware of the article. (Julian Amended Answer ¶ 55, 102; 404.

<sup>2867</sup> Julian Amended Answer ¶ 405.

“case is defined as an allegation of team member misconduct involving a possible violation of law or a code of ethics policy violation or information security policy violation, which has resulted in a financial loss and/or exposure or represents a significant compliance or reputational risk.” It further stated that “The major case types that increased year-over-year include Sales Integrity up 5%” and that “43% [of EthicsLine complaints] were referred to Community Bank Sales Quality” (i.e. related to sales practices).<sup>2868</sup>

201. On February 28, 2014, Respondent Julian received a “Corporate Investigations 2013 Year End Update/2014 Priorities” slide deck for the Head of Corporate Investigations’ presentation to the Audit Management Committee on March 3, 2014. The presentation showed sales integrity violations as the number two case type for both 2012 and 2013, with 3,167 and 3,330 respectively.<sup>2869</sup>
202. On March 4, 2014, Respondent Julian received a 2013 year-end update from Head of Corporate Investigations Michael Bacon as part of his TMMEC membership. The report showed that sales integrity violations were the second highest case type at the Bank in 2012 and 2013, with 3,330 sales integrity violations cases YTD in 2013 compared with 3,167 sales integrity violations cases YTD in 2012.<sup>2870</sup> The report also reflected that the vast majority of EthicsLine complaints related to the Community Bank<sup>2871</sup> and that 3,653 of 8,535 (42.8%) EthicsLine reports in 2013 were referred to Sales Quality (i.e. related to sales practices) compared with 3,739 of 8,354 (44.7%) in 2012.<sup>2872</sup>
203. At the April 9, 2014 Enterprise Risk Management Committee meeting, Community Bank leadership, including Respondent Russ Anderson, informed the committee that one to two percent of the Community Bank employees (1,000-2,000) were terminated each year for sales practices-related wrongdoing.<sup>2873</sup>
204. The Corporate Security update in WFAS’s May 5, 2014 First Quarter 2014 Summary to the Audit and Examination Committee stated that, of the 2,168 total EthicsLine complaints received in YTD 1Q14, 46% were referred to Community Bank Sales Quality (i.e. were related to sales practices).<sup>2874</sup>
205. Corporate Security’s update in WFAS’s August 4, 2014 Second Quarter 2014 Summary to the Audit and Examination Committee stated that sales integrity

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<sup>2868</sup> MSD-526 at 47-48, 51.

<sup>2869</sup> MSD-335 at 4.

<sup>2870</sup> MSD-447 at 4.

<sup>2871</sup> *Id.*

<sup>2872</sup> *Id.* at 7.

<sup>2873</sup> MSD-28 at 1; Julian Amended Answer ¶¶ 164, 271, 398; McLinko Amended Answer ¶ 164, 271, 398.

<sup>2874</sup> MSD-451 at 52.

was one of Corporate Investigations' major case types<sup>2875</sup> and 42% of the 4,536 total EthicsLine received YTD in 2Q14 "were referred to Community Bank Sales Quality" (i.e. were related to sales practices).<sup>2876</sup>

206. The Corporate Security update in WFAS's November 18, 2014 Third Quarter 2014 Summary to the Audit and Examination Committee stated that 40% of the 6,700 EthicsLine complaints received 3Q14 YTD were "referred to Community Bank Sales Quality" (i.e. were related to sales practices).<sup>2877</sup>
207. The Corporate Security update in WFAS's February 24, 2015 WFAS Fourth Quarter 2014 Summary to the Audit and Examination Committee stated that 39% of the 8,707 EthicsLine complaints received 4Q14 YTD were referred to Community Bank Sales Quality (i.e. were related to sales practices).<sup>2878</sup>
208. On May 4, 2015, the City Attorney of Los Angeles sued the Bank in connection with the Community Bank's sales practices. The Complaint, which was consistent with the information Respondents Julian had received over the years related to the Bank's salepractices, alleged the following:

For years, Wells Fargo & Company and Wells Fargo Bank, National Association (collectively "Wells Fargo") have victimized their customers by using pernicious and often illegal sales tactics to maintain high levels of sales of their banking and financial products. The banking business model employed by Wells Fargo is based on selling customers multiple banking products, which Wells Fargo calls "solutions." In order to achieve its goal of selling a high number of "solutions" to each customer, Wells Fargo imposes unrealistic sales quotas on its employees, and has adopted policies that have, predictably and naturally, driven its bankers to engage in fraudulent behavior to meet those unreachable goals.

As a result. Wells Fargo's employees have engaged in unfair, unlawful, and fraudulent conduct, including opening customer accounts, and issuing credit cards, without authorization. Wells Fargo has known about and encouraged thesepractices for years. It has done little, if anything, to discourage its employees' behavior and protect its customers.

Worse, on the rare occasions when Wells Fargo did take action against its employees for unethical sales conduct, Wells Fargo further victimized its customers by failing to inform them of the

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<sup>2875</sup> MSD-397 at 64.

<sup>2876</sup> *Id.* at 68.

<sup>2877</sup> MSD-398 at 69.

<sup>2878</sup> MSD-400 at 79.

breaches, refund fees they were owed, or otherwise remedy the injuries that Wells Fargo and its bankers have caused.

The result is that Wells Fargo has engineered a virtual fee-generating machine, through which its customers are harmed, its employees take the blame, and Wells Fargo reaps the profits.<sup>2879</sup>

209. On May 4, 2015, Respondent Julian received a *Los Angeles Times* article titled, “L.A. Sues Wells Fargo, alleging ‘unlawful and fraudulent conduct,’” which described the allegations in the City Attorney of Los Angeles lawsuit.<sup>2880</sup>

210. On October 4, 2013, Respondent McLinko was forwarded the October 3, 2013 *Los Angeles Times* Article, “Wells Fargo Fires Workers Accused of Cheating on Sales Goals,” from the Head of Corporate Investigations. The Head of Corporate Investigations wrote that the article was a “big deal and very interesting.”<sup>2881</sup>

211. October 4, 2013 *Los Angeles Times* article stated that the Bank “fired about 30 branch employees in the Los Angeles region who the bank said had opened accounts that were never used and attempted to manipulate customer-satisfaction surveys.” According to the article, a Bank spokesperson explained that “[t]he employees were trying to take shortcuts to meet salesgoals.” The article also stated that one of the fired employees said, “in some cases signatures were forged and customers had accounts opened in their names without their knowledge” and “the pressure to meet sales goals was intense at Wells Fargo.”<sup>2882</sup>

212. On November 1, 2013, Bart Deese (a direct report of Respondent McLinko) forwarded Respondent McLinko a Significant Investigation Notification he received from Corporate Investigations about the investigation that gave rise to the October 2013 *Los Angeles Times* article. The notification stated that: the allegation was that “[s]imulated funding falsified entries were made to meet individual and store sales goals;” twenty employees “with the most egregious simulated funding numbers were to be interviewed first” and that the “Criteria for egregious [was] 50 or more accounts opened in 1 month or 10% of total accounts opened in a 4 month period” that met the simulated funding criteria; and the investigation found that employees engaged in simulated funding “[t]o meet quarterly sales goals” despite “[k]nowing their actions were against [Bank] policy.”<sup>2883</sup>

213. After the *Los Angeles Times* published its second article about the Bank’s sales

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<sup>2879</sup> MSD-169 at 3.

<sup>2880</sup> MSD-463.

<sup>2881</sup> McLinko Amended Answer ¶¶ 55, 102, 404, 457; MSD-331.

<sup>2882</sup> MSD-331.

<sup>2883</sup> MSD-333 at 3.

practices, *Wells Fargo's Pressure-Cooker Sales Culture Comes at a Cost*, a fellow WFAS corporate risk auditor sent a link to article to Respondent McLinko the and wrote: "I am not sure how much merit there is to this story (L.A. Times), but it poses reputation risk to the firm."<sup>2884</sup>

214. The article stated it was based on interviews with 28 former and seven current employees across nine states and reported that "To meet quotas, employees have opened unneeded accounts for customers, ordered credit cards without customers' permission and forged client signatures on paperwork" and employees were threatened with termination if they failed to meet their sales goals.<sup>2885</sup>
215. On February 28, 2014, Respondent McLinko received a "Corporate Investigations 2013 Year End Update/2014 Priorities" slide deck for the Head of Corporate Investigations' presentation to the Audit Management Committee on March 3, 2014. The presentation showed sales integrity violations as the number two case type for both 2012 and 2013, with 3,167 and 3,330 respectively. Although sales-integrity violation cases are not specifically tied to the Community Bank, the Community Bank comprises of the vast majority of cases: 11,591 cases in Community Bank versus 1,583 in the other lines of business in 2012 and 11,915 cases in Community Bank versus 1,821 in the other lines of business in 2013.<sup>2886</sup>
216. Respondent McLinko received a presentation and agenda for an Internal Fraud Committee meeting. The agenda stated: "Sales Integrity key activity is mixed, but expected to increase due to proactive initiatives" (*i.e.* the Community Bank will identify more sales integrity violations when it increases proactive monitoring). The presentation showed: 740 sales integrity violations cases in 4Q12, 798 in 1Q13, 823 in 2Q13, 822 in 3Q13, and 824 in 4Q13 (*i.e.* 3,267 total sales integrity cases in 2013); and 361 terminations/resignations for sales integrity violations in 4Q12, 335 in 1Q13, 383 in 2Q13, 389 in 3Q13, and 348 in 4Q13 (*i.e.* 1,455 terminations/resignations for sales integrity violations in 2013).<sup>2887</sup>
217. On August 18, 2014, Respondent McLinko received a presentation for an October 2, 2014 Internal Fraud Committee meeting showing: 824 sales integrity violations cases in 2Q13, 822 in 3Q13, 822 in 4Q13, 746 in 1Q14, and 744 in 2Q14; and 386 terminations/resignations for sales integrity violations in 2Q13, 389 in 3Q13, 368 in 4Q13, 381 in 1Q14, and 393 in 2Q14.<sup>2888</sup>

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<sup>2884</sup> MSD-531.

<sup>2885</sup> McLinko Amended Answer ¶ 101; MSD-111 at 1-2. Respondent McLinko was aware of the article; McLinko Amended Answer ¶ 55, 102.

<sup>2886</sup> MSD-335 at 4.

<sup>2887</sup> MSD-336 at 7, 28.

<sup>2888</sup> MSD-614 at 6, 30.

218. According to a February 2015 presentation made to the OCC by Respondent McLinko (and his direct report Bart Deese) on WFAS Community Bank Sales Coverage, WFAS had a “[p]artnership with Corporate Investigations” and interacted with Corporate Investigations in several ways.<sup>2889</sup> For example, WFAS was “[c]opied on all significant cases above established dollar thresholds for review and assessment,” it had “[o]ngoing dialogue throughout the year on open cases (where needed),” and it “[p]articipat[ed] in semi-annual CMBK Internal Fraud Committee Meeting.”<sup>2890</sup> The presentation also noted that WFAS attended “Semi-annual Regional President meetings,” in which “RB – Sales Quality and Corporate Investigations attend and share information.”<sup>2891</sup>
219. Similarly, in a May 27, 2015 email to the OCC, Respondent Julian wrote that WFAS’s “audit methodology includes contacting Corporate Investigations at the beginning of each audit to determine if there are any cases/trends related to the area under review. In addition, the Community Banking (CB) audit team interact with Corporate Investigations in a number of ways throughout the year (e.g., Semi-annual Regional President meetings, Semi-annual CMBK Internal Fraud Committee, Copied on SINs and IDEAs, Ad hoc discussions) to understand cases/trends, etc.”<sup>2892</sup>
220. Like Respondent Julian, Respondent McLinko’s direct reports also received extensive information from both Corporate Investigations and the Community Bank’s Sales Quality team indicating that sales practices misconduct existed throughout the Community Bank, that consent was the number one sales integrity issue, and that the root cause of the misconduct was pressure to meet sales goals.<sup>2893</sup>

The below paragraphs list some of the information Respondent McLinko’s direct reports received.

221. At a July 6, 2010 Regional President meeting (Southwest region) attended by Bart Deese, Corporate Investigations reported, “sales integrity cases continue to increase.”<sup>2894</sup>
222. At a July 7, 2010 Regional President meeting (Carolinas region) attended by Bart Deese, Corporate Investigations reported, “due to a more aggressive sales

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<sup>2889</sup> MSD-476 at 6.

<sup>2890</sup> *Id.*

<sup>2891</sup> *Id.*

<sup>2892</sup> MSD-416; Julian Amended Answer ¶¶ 400, 451; McLinko Amended Answer ¶¶ 400, 451; MSD-369 (providing Respondent Julian with a draft email to send to the OCC).

<sup>2893</sup> SOF ¶¶ 265-418.

<sup>2894</sup> MSD- 615.

culture, sales integrity is going to be a challenge.”<sup>2895</sup>

223. Preponderant evidence adduced during the hearing established that throughout the relevant period, Respondents Julian and McLinko failed to identify the systemic sales practices misconduct problem and the significant sales practices risk management and internal controls weaknesses in any audit report or Enterprise Risk Management Assessment.<sup>2896</sup>
224. Respondents Julian, McLinko, and Russ Anderson failed to identify incentive compensation practices as relating to sales practices and sales practices misconduct.
225. When asked what she found during the 2016 risk management examination, NBE Candy responded that adverse risk events were not adequately incorporated into incentive decisions during the relevant period:

A [Ms. Candy]: You know, for this exam, we were doing it in 2016, and we were basing it off of 2015 compensation decisions. So when we look specifically to sales practices, at this point, you know, it's after the L.A. Times article. It's also after the OCC issued the five letter -- I mean the five MRAs to the bank from the sales practices exam in June of 2015.

There was a lot of knowledge within the bank about the deficiencies in risk management that led to sales practice misconduct occurring. Despite this, there was not adequate incorporation of that as a huge adverse risk event in compensation decisions.

When you specifically looked at people that were identified as accountable for sales, you know, the sales practices issue, they, the lowest they received compensation was 98 percent of their target bonus, up until 120 percent of their target bonus. So they even got above target bonus payments despite this event.

When people are not held accountable, especially through compensation for adverse risk events, it does not; it's not consistent with incentive compensation risk management practices to deter that behavior. You know, furthermore, when we were looking at compensation plans in the Community Bank, we also identified that there was not an adequate process at an individual level and especially manager level to incorporate sales practice misconduct and conduct risk into their compensation as well.

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<sup>2895</sup> MSD-616.

<sup>2896</sup> See SOF ¶¶ 419- 522; MSD-638 (Deese Dep. Tr.) 245:22-251:17.

Q [by Enforcement Counsel]: What role did Mr. Julian have in the annual risk assessment process from 2013 through 2016?

A: Yes, Mr. Julian was, um, an important person in that process.

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You know, he had a seat at the table and, you know, he had a valued opinion on his, um, both the result of audits that had been done, you know, other work audit has done, as well as his general opinion of, of the senior leaders at the bank.

Q: Take a look at page 5 of the supervisory letter. Was Mr. Julian, the chief auditor of the bank, one of the executives copied on your supervisory letter? A: He was.

Q: Okay. To your knowledge, were the deficiencies with the incentive compensation plans that you identified in this supervisory letter in November 2016 previously identified by any of the respondents in this case?

A: They were not. And frankly that's a problem.

Q Why? A So as we've talked about the last few days about heightened standards and risk governance framework and the purpose of the three lines of defense, as the first line of defense they are responsible for managing and identifying the risks.

So in this case, you know, risks got posed by the incentive compensation plan. The second line of defense should be credibly challenging that and overseeing it. And then the third line of defense is also critical, because they're the last, you know, the last stop within the bank and should be adequately providing oversight and testing to ensure compliance.

So when the OCC has to go in and identify an issue, that really demonstrates failures in all three lines of defense.

Q: Are you familiar with the annual OCC exams covering internal audit?

A: I am.

Q How, if at all, was your work leading the incentive compensation exam that we just discussed, incorporated into the annual audit exam in 2016?

A: Yes, I'd be happy to explain. So as part of this exam, we did also look at audit coverage of, um, incentive compensation, and we found deficiencies in that.



We found both deficiencies from an enterprise perspective and not adequately testing compliance with the policies, but specifically we also found deficiencies in the coverage of testing individual incentive compensation plans in the lines of business, including the Community Bank.

So my incentive compensation exam was going on at the same time as the audit exam. So since the, you know, appropriate recipient of that letter would be Mr. Julian, I included an MRA that I wrote requiring audit to improve their coverage of incentive compensation in that annual audit exam letter.

Q: Ms. Candy, respondents may argue that the incentive compensation plans in the Community Bank were being modified beginning in 2013. What, if anything, did you conclude about any modifications to incentive compensation plans in the Community Bank from 2013 to 2016?

A: I concluded that any modifications made were not sufficient. When we reviewed the 2015 plans, you know, when we reviewed it in 2016 during this exam, we found them still to be unreasonable and driving inappropriate behavior, so it shows any subsequent, you know, tweaks to the plans were not adequate to manage the risk and sales practices misconduct.<sup>2897</sup>

226. Respondent Julian admitted in his Amended Answer that, “As to the allegation in the first sentence that ‘[u]nder Respondent Julian’s leadership, Audit never . . . identified [the sales practices misconduct problem’s] root cause in any audit report,’ admitted that Audit did not discuss the root cause of sales practices misconduct in audit reports, which reports were focused on the testing and assessment of specific controls.”<sup>2898</sup>
227. Respondent Paul McLinko admitted in his Amended Answer that “his 15-Day Letter response states, in part, that: ‘Mr. McLinko did not identify the depth and breadth of the systemic sales practices misconduct that ultimately were revealed in the Board Report.’ Respondent further admits that the Community Bank audit team did not identify in any audit reports what the Notice of Charges alleges is the root cause of the alleged systemic sales practices misconduct problem.”<sup>2899</sup>
228. On February 5, 2015, the Bank provided OCC examiners with a presentation

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<sup>2897</sup> Tr. (Candy) at 1123-28. See also OCC Ex. 2407 (Report of NBE Candy) at ¶128 (regarding Respondents Julian and McLinko), ¶115-16 (regarding Respondent Russ Anderson); OCC Ex. 2335 (Report of NBE Crosthwaite) at ¶31 (regarding Respondents Julian and McLinko), and ¶110-11 (regarding Respondent Russ Anderson).

<sup>2898</sup> Julian Amended Answer ¶ 411.

<sup>2899</sup> McLinko Amended Answer ¶ 411.

prepared by Respondent McLinko and his direct report Bart Deese on “WFAS Community Sales Coverage.” The presentation identified audits that had been completed since 2013 or were expected to be completed in 2015.<sup>2900</sup>

229. On May 27, 2015, Respondents Julian provided OCC examiners with a list detailing WFAS Community Bank Sales Coverage, which identified audits that had been completed since 2013 or were expected to be completed in 2015.<sup>2901</sup>
230. Respondents Julian and McLinko identified the following audits as covering sales practices in 2014: Wells Fargo Customer Connection Account Opening & Fulfillment;<sup>2902</sup> Digital Channels Group Online Sales & Marketing;<sup>2903</sup> Regional Bank SOCR;<sup>2904</sup> Enterprise Incentive Compensation;<sup>2905</sup> and Business Banking Group Accounting & Finance.<sup>2906</sup>
231. Respondents Julian and McLinko identified the following audit as covering sales practices in 2015: RB Account Opening & Closing.<sup>2907</sup>
232. WFAS rated all but one of the audits Respondents Julian and McLinko identified as relating to sales practices issues in the Community Bank as “Effective” or “Satisfactory.”<sup>2908</sup>
233. In addition to audit activities that were scoped to assess a particular area of operations within the Community Bank, the WFAS Community Bank audit team also completed annual Enterprise Risk Management (“ERM”) Assessments of the overall risk management within the Community Bank. Like the audit activities completed during Respondents Julian and McLinko’s tenures, the annual ERM Assessments (or “ERMAs”) reported each year from 2012 to 2016 that the Community Bank had Satisfactory risk management, including management of sales practices risk, and reported Strong or Satisfactory ratings of the Community Bank’s “Governance” and “Culture.”
234. WFAS awarded the Community Bank Effective ratings in other audits that touched on sales practices that were not included on the lists of sales practices-

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<sup>2900</sup> MSD-630.

<sup>2901</sup> MSD-416.

<sup>2902</sup> MSD- 513.

<sup>2903</sup> MSD-514.

<sup>2904</sup> MSD-520.

<sup>2905</sup> MSD-515.

<sup>2906</sup> MSD-516.

<sup>2907</sup> MSD-385.

<sup>2908</sup> Julian Amended Answer ¶ 413 (“Admitted that, between 2012 and 2016, some controls related to sales practices were audited and received ratings of ‘effective’ between 2012 and 2016.”); McLinko Amended Answer ¶ 463 (“Respondent Paul McLinko admits that Audit periodically issued audit reports pertinent to aspects of sales practices misconduct at the Community Bank, certain of which reports provided overall ‘effective’ ratings”); see SOF ¶¶ 439-41, 443, 452-53, 456, 465, 467, 487.

- related audits Respondents Julian and McLinko provided to the OCC.<sup>2909</sup>
235. On April 11, 2011, WFAS issued its audit report on *Regional Bank - Sales, Service & Development*, rating internal controls Effective. The audit assessed controls related to sales quality, incentive-compensation plan administration, incentive-compensation plan design, approval, implementation, and governance, and the control environment quality of risk management.<sup>2910</sup>
236. On March 22, 2012, WFAS issued its audit report on *Regional Banking – HumanResources*, rating internal controls as **Effective**.<sup>2911</sup>
237. On October 26, 2012, WFAS issued its audit report on *Regional Banking Compensation*, rating internal controls as **Effective**. Although the report identified Incentive Compensation Risk Management - Incentive Compensation as a risk, because “[i]nadequate review and execution of [incentive] plan balancing activities could negatively impact Wells Fargo’s safety and soundness, resulting in adverse impact on Wells Fargo’s reputation, regulatory scrutiny, negative market opinion, an increase in cost of capital, and a decrease in share price,” the report concluded that compensation processes were “very robust within both administrative and control functions” and “management has historically focused on and continues to be attentive to the inherent risks associated with incentive compensation.”<sup>2912</sup>
238. On November 26, 2012, after Respondent Russ Anderson learned that WFAS had contacted the OCC regarding an upcoming examination, Respondent Russ Anderson wrote: “[n]ot sure why audit would make this type of inquiry and not cc me as GRO. Help!” Respondent McLinko replied: “You have my assurance that we would never bring anything to the regulators attention without you are [sic] your team being aware (thus preventing a disconnect). No surprises as we agreed.”<sup>2913</sup>
239. On December 18, 2012, Respondent McLinko described a meeting with Respondent Russ Anderson to his direct reports, where he wrote “It’s either my charming personality (not or mimosa’s [sic] in the morning (not on my part) or something else, but had a very good meeting with [Respondent Russ Anderson]... regarding [Respondent Russ Anderson’s] expectations for me at her offsite the first week of January. As the audit lead, she’s looking to partner, for me to get to know her folks better (and vice versa), and hear what the senior risk leaders ... have to say. She also expects me to stay for heavy appetizers and beverages (she needs to twist my arm for that :)).” [also – I specifically brought up audits of Sales

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<sup>2909</sup> MSD-371; MSD-348; MSD-379.

<sup>2910</sup> MSD-371.

<sup>2911</sup> MSD-631.

<sup>2912</sup> Julian Amended Answer ¶¶ 415, 464; McLinko Amended Answer ¶¶ 415, 464; MSD-348.

<sup>2913</sup> MSD-388 (emphasis added).

Quality, Suitability and a slip on my part Integrity. Her only comment was they don't use Integrity as those issues are referred to [the Head of Corporate Investigations]".<sup>2914</sup>

240. On March 4, 2013, Respondent McLinko asked his audit team to put together a presentation in advance of a March 19, 2013 meeting with Carrie Tolstedt and Respondent Russ Anderson. Respondent McLinko directed his team prepare a slide that suggests the Community Bank should consider WFAS as "more of a partner versus an auditor."<sup>2915</sup> The draft PowerPoint presentation that Respondent McLinko's team prepared contained a slide titled "Working Together." The slide stated: "Consider us more a partner than an auditor."
241. On March 7, 2013, WFAS issued its Community Banking Enterprise Risk Management Assessment ("ERMA") for 2012 ("2012 CB ERMA"), concluding that "risk management within Community Banking is Satisfactory trending toward Strong. . . WFAS's evaluation of risk related to Community Banking focused on Operational Risk with an emphasis on . . . sales quality, regulatory compliance, and reputation impacts." Governance, Culture, and Risk Response and Control were rated Strong. Strategy/Objective Setting and Risk Identification, Assessment and Analysis were rated Satisfactory.<sup>2916</sup> At the time, ERMA ratings were Strong, Satisfactory, or Weak.<sup>2917</sup>
242. Regarding Culture, the 2012 CB ERMA noted: "The vision and values of Wells Fargo is evident in the Community Banking culture and their key initiatives continue to focus on the customer." Regarding Risk Response and Control, the ERMA noted: "Community Banking risk management, system of controls, and governance processes are adequate and functioning as intended. Controls across Community Banking are well designed to proactively mitigate risk exposures. This includes use of automated controls and robust policies and procedures to governday-to-day activities within the business segments."<sup>2918</sup>
243. On September 30, 2013, WFAS issued its audit report on *Community Bank - Household Metrics Reporting*, concluding that "[t]he systemic of internal controls for [Community Bank] – Household Metrics Reporting is **Effective**, with no reportable issues. The ~~scope~~ of this audit included re-performance of key metrics (including cross sell). . . ."<sup>2919</sup>
244. On September 30, 2013, WFAS issued its audit report on *Community Bank - Household Metrics Reporting*, concluding that "[t]he systemic of internal controls

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<sup>2914</sup> MSD-389.

<sup>2915</sup> MSD-390.

<sup>2916</sup> MSD-373.

<sup>2917</sup> *Id.* at 1.

<sup>2918</sup> MSD-373.

<sup>2919</sup> MSD-375.

for [Community Bank] – Household Metrics Reporting is Effective, with no reportable issues. The scope of this audit included re-performance of key metrics (including cross sell).<sup>2920</sup>

245. On December 13, 2013, WFAS issued its audit report on *Regional Banking - Sales Quality/ Sales Integrity*. In its report, WFAS concluded, “the system of internal controls with Regional Banking Sales Quality / Sales Integrity is **Effective**. This rating reflects our opinion that controls in place adequately mitigate the risks associated with sales quality allegation, case management, service management and reporting processes. WFAS did identify a moderate-rated issue regarding the need to enhance the training notification process; however, this is not a significant control weakness. The scope of our audit also included a design review of the enhanced proactive monitoring and behavioral trend reporting processes. The overall design is deemed adequate . . . .”<sup>2921</sup>
246. On October 29, 2013, WFAS had provided members of the Community Bank with a draft Issue and Recommendation Memo (“Draft I&R”) in connection with its RB – Sales Quality / Sales Integrity audit. The Draft I&R and cover email described an issue identified during audit regarding enhancing training notifications and “escalation and increased visibility of repeat sales offenders.”<sup>2922</sup> WFAS requested a written response from Community Bank about the audit issue, setting corrective actions and reasonable target dates to complete them, and designating responsible individuals. Neither the Draft I&R nor cover email requested line edits to the Draft I&R itself.<sup>2923</sup>
247. On November 15, 2013, the Community Bank provided line edits to the 2013 Draft I&R, including edits from Respondent Russ Anderson. (MSD- 198). The Draft I&R included language such as “Enhance the training notification process and increased visibility of repeat sales offenders,” which was changed to “Enhance the training notification process and increased visibility of second time training notifications.”<sup>2924</sup>
248. Respondent Russ Anderson changed “The monthly regional sales reports including metrics on cases resulting in training e-mail does not differentiate between first time and repeat offenders” in the original Draft I&R to “The monthly regional sales reports including metrics on cases resulting in training e-mail notifications does not differentiate between first time and second time training notifications.”<sup>2925</sup>

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<sup>2920</sup> MSD-512.

<sup>2921</sup> MSD-376; Julian Amended Answer ¶¶ 416, 465 McLinko Amended Answer ¶¶ 416, 465.

<sup>2922</sup> MSD-503 at 1, 2.

<sup>2923</sup> *Id.*

<sup>2924</sup> MSD-198.

<sup>2925</sup> *Id.*

249. The Risk section of the Draft I&R originally read “Failure to properly monitor training e-mail notifications and escalate/report repeat allegations could lead to inappropriate training practices and increased numbers of repeat offenders of inappropriate sales practices,” but Respondent Russ Anderson changed it to “Failure to properly monitor training e-mail notifications and differentiate between first and second time training notifications could lead to inappropriate training practices and increased numbers of additional allegations.”<sup>2926</sup>
250. WFAS incorporated Respondent Russ Anderson’s edits on the Draft I&R into its final audit engagement report on RB – Sales Quality/Sales Integrity issued on December 16, 2013 and its final Issue and Recommendation Memo.<sup>2927</sup>
251. On December 16, 2013, Bart Deese, Respondent McLinko’s direct report sent the OCC a presentation summarizing audits WFAS completed in 2013. The presentation was titled “Community Bank and TOG Operations and Team Update.” Respondent McLinko was copied on this email and was listed as one of the presenters. Under “2013 Plan Highlights,” the comments for the RB - Sales Quality/ Sales Integrity reads: “Report issued on December 16. Rating was Effective. Review included processes related to monitoring and reporting of questionable sales activity. One moderate issue identified related to the need to enhance the training notification process.” (MSD-366 at 10). Under “2014 Plan Highlights,” the deck lists “CMBK - Cross Sell” as a planned area of audit coverage for 2014.<sup>2928</sup>
252. On December 20, 2013, WFAS issued its audit report on *Business Banking Sales, Service, Product Suitability, and Marketing*, which assessed the marketing and product evaluation processes that are managed within [Business Banking] for use by all business bankers within Business Banking and Regional Banking.” WFAS concluded that “[t]he system of internal control of this engagement scope is **Effective**. This rating reflects our opinion that the product evaluation, marketing, sales customer set up, customer servicing and user access processes and controls are working effectively to manage risk.”<sup>2929</sup>
253. Thereafter the Enterprise Risk Management Committee identified “Sales Conduct, Practices and the Consumer Business Model” for the Board as a “Noteworthy Risk” at least seven times in 2014 and 2015.<sup>2930</sup> Audit updated the Audit and Examination Committee on its activities related to the “Sales Conduct, Practices and the Consumer Business Model” “Noteworthy Risk.”<sup>2931</sup> It provided

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<sup>2926</sup> MSD-198.

<sup>2927</sup> MSD-376 (not using the term “repeat offenders” or “inappropriate sales practices”); MSD-601.

<sup>2928</sup> MSD-366 at 14.

<sup>2929</sup> MSD-518.

<sup>2930</sup> See MSD-395; MSD-396; MSD-532; MSD-533; MSD-534; MSD-535; MSD-536.

<sup>2931</sup> SOF ¶¶ 451, 454, 457-58, 460, 470, 477, 484.

similar reporting to the Operating Committee and the Enterprise Risk Management Committee.<sup>2932</sup>

254. Each year, the Bank's Chief Risk Officer and its Director of Human Resources submitted to the Human Resources Committee of the Board a memorandum summarizing the risk assessment processes and risk outcome evaluations that informed their annual incentive compensation recommendations for senior Bank executives, including Head of the Community Bank Carrie Tolstedt. These memoranda were submitted to the CEO and the Human Resources Committee of the Board, and later provided to the OCC. Corporate Human Resources and Corporate Risk explicitly relied on WFAS's work and findings in preparing annual incentive compensation risk memoranda.<sup>2933</sup> Respondent Julian attended meetings regarding the executive compensation year-end risk review.<sup>2934</sup>
255. In a February 18, 2014 annual incentive-compensation risk memorandum from the Bank's Chief Risk Officer and its Director of Human Resources to the CEO and the Human Resources Committee of the Board, Carrie Tolstedt received a "Satisfactory" assessment related to Sales Quality Monitoring and there was no adjustment to her compensation. A "Satisfactory" assessment indicated: "No adverse impact from management of risk. The individual has taken steps expected to prevent and manage the risk issues."<sup>2935</sup> The memorandum noted that the Chief Risk Officer's and Director of Human Resources' evaluation of risk outcomes was based, in part, on a "holistic review of audit findings related to the business . . . with a focus on the Unsatisfactory and high-risk Needs Improvement audit issues."<sup>2936</sup>
256. On March 31, 2014, WFAS issued a Community Banking Enterprise Risk Management Assessment for 2013 ("2013 CB ERMA"), concluding, "risk management within Community Banking (CB) is **Satisfactory**." Governance and Culture and Strategy and Objective Setting were rated Strong. Risk Identification, Assessment and Analysis and Risk Response and Control were rated Satisfactory.<sup>2937</sup> At the time, ERMA ratings were Strong, Satisfactory, Needs Improvement, or Weak.<sup>2938</sup>
257. Regarding culture, the 2013 CB ERMA concluded: "The vision and values of

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<sup>2932</sup> See, e.g., MSD-536, MSD-719.

<sup>2933</sup> MSD-412; MSD-433; MSD-456); Julian Amended Answer ¶ 425 (admitting that "Audit provided information in connection with annual incentive compensation risk memoranda and that memoranda were provided to the Human Resources Committee of the Board."); MSD-290B (Loughlin Tr.) at 452:16-23.

<sup>2934</sup> MSD-507 at 2, 4.

<sup>2935</sup> MSD-412 at 7.

<sup>2936</sup> *Id.* at 3.

<sup>2937</sup> MSD-378.

<sup>2938</sup> *Id.* at 3.

Wells Fargo is also evident in the CB culture. Key initiatives continue to focus on the customer. Expectations regarding the company's ethical culture are frequently communicated and tangibly demonstrated throughout the Community Bank." Regarding performance management (in Risk Response and Control), the ERMA stated: "Community Banking performance measures are appropriately tied to compensations, incentive, and risk. They are aligned with shareholder interests and the long-term profitability of the company."<sup>2939</sup>

258. At an April 29, 2014 meeting, Respondent Julian informed the Board of Directors that there were "no alarming trends or significant issues to discuss with the Board."<sup>2940</sup>
259. On May 5, 2014, WFAS presented its First Quarter 2014 Summary to the Audit and Examination Committee of the Board. Audit's quarterly report to the Board contained the following update on the "Sales Conduct, Practices and the Consumer Business Model" Noteworthy Risk: "Sales audits are being performed in Wells Fargo Customer Connection and Digital Channels Group in 2014. In addition, an assessment of cross sell audit coverage is included in the Community Banking Audit Plan. Focus of these reviews is on the sales practices and conduct to ensure customers are sold products meeting their financial needs."<sup>2941</sup>
260. Respondent McLinko and his team reviewed and advised on the language WFAS included in its quarterly reports to the Audit and Examination Committee, including regarding the "Sales Conduct, Practices and the Consumer Business Model" "Noteworthy Risk," and even provided draft language to Respondent Russ Anderson for her review and comment.<sup>2942</sup>
261. On May 9, 2014, WFAS issued an audit report on *Community Banking WFCC (Wells Fargo Customer Connection) – Account Opening/Fulfillment*. The audit rated "the system of internal controls within WFCC Account Opening/Fulfillment is **Effective**. Testing . . . noted no significant concerns or reportable issues."<sup>2943</sup>
262. On June 27, 2014, WFAS issued an audit report on *Community Banking – Digital Channels Group (DCG) – Online Sales & Marketing*. The audit concluded, "The system of internal controls within DCG Online Sales and Marketing is Effective. Testing . . . noted no significant concerns or reportable issues."<sup>2944</sup>

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<sup>2939</sup> MSD-378.

<sup>2940</sup> MSD-481 at 6.

<sup>2941</sup> MSD-402 at 31.

<sup>2942</sup> See, e.g., MSD-536, MSD-719.

<sup>2943</sup> MSD-513.

<sup>2944</sup> MSD-514.



263. Although Respondents Julian and McLinko and WFAS implied to the OCC and the Board that its audits of Wells Fargo Customer Connection (call center) and digital channels (online) were related to its Community Bank sales practices coverage and the “Sales Conduct, Practices and the Consumer Business Model” Noteworthy Risk, these audits were scoped to review Community Bank activities in call centers and online channels, and did not look at sales practices in the Regional Banking branches/stores. In any case, WFAS’s audits of these areas were rated **Effective**.<sup>2945</sup>
264. On June 30, 2014, WFAS issued an audit report on *Enterprise Code of Ethics*, the scope of which include the Bank’s “tracking and reporting of complaints and violations.” The audit was rated **Effective**.<sup>2946</sup>
265. On August 1, 2014, WFAS issued its audit report on *Community Banking Business Banking Group – Accounting and Finance* audit rated management of compensation processes and controls as **Effective**.<sup>2947</sup>
266. On August 4, 2014, WFAS presented its Second Quarter 2014 Summary to the Audit and Examination Committee of the Board. Audit’s quarterly report to the Board contained the following update on the “Sales Conduct, Practices and the Consumer Business Model” Noteworthy Risk: “Sales audits were completed within Community Banking in Wells Fargo Customer Connection and the Digital Channels Group. The focus of these reviews was on the sales practices and conduct to ensure customers are sold products meeting their financial needs. Both audits were rated Effective with no reportable issues.”<sup>2948</sup>
267. On November 18, 2014, WFAS presented its Third Quarter 2014 Summary to the Audit and Examination Committee of the Board. Audit’s quarterly report to the Board contained the following update on the “Sales Conduct, Practices and the Consumer Business Model” Noteworthy Risk: “Sales audits were completed within Community Banking in Wells Fargo Customer Connection and the Digital Channels Group. The focus of these reviews was on the sales practices and conduct to ensure customers are sold products meeting their financial needs. Both audits were rated Effective with no reportable issues.”<sup>2949</sup>
268. On December 16, 2014, WFAS issued its audit report on *Regional Bank - Risk Council*. As explained in the audit report, the “Risk Council is a forum of RB Senior Management that meets on a quarterly basis to discuss operational risk topics and breaches for established Enterprise Key Indicators (EKIs). Root cause and corrective action plans for any EKI breaches are

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<sup>2945</sup> See MSD-512; MSD-513; and MSD-514.

<sup>2946</sup> MSD-529 at 2.

<sup>2947</sup> MSD-516 at 2.

<sup>2948</sup> MSD-397 at 52.

<sup>2949</sup> MSD-398 at 56.

researched and monitored by the Risk Council on a quarterly basis to ensure store banker performance meets established standards.” WFAS concluded in its report that “the system of internal controls related to Risk Council organizational structure and EKI monitoring is **Effective**.” The report also rated “Originate and Setup Accounts – EKI Monitoring,” and rated that process Effective as well.<sup>2950</sup>

269. On February 4, 2015, WFAS presented its Fourth Quarter 2014 Summary to the Audit and Examination Committee of the Board. Audit’s quarterly report to the Board contained the following update on the “Sales Conduct, Practices and the Consumer Business Model” Noteworthy Risk: “Sales audits were completed within Community Banking in Wells Fargo Customer Connection and the Digital Channels Group as part of the 2014 Community Banking plan. The focus of these reviews was on the sales practices and conduct to ensure customers are sold products meeting their financial needs. Both audits were rated Effective with no reportable issues. In addition, an assessment of cross-sell audit coverage was also completed as part of the plan with no significant additional coverage warranted. A continued focus on sales practices and conduct will continue in 2015 with account opening audits in both Regional Banking and Business Banking.”
270. On February 9, 2015, Respondent McLinko and his reports met with OCC examiners of WFAS’s Community Bank Sales Coverage. Respondent Russ Anderson attended the meeting as well.<sup>2951</sup> According to OCC examiner Karin Hudson, “Respondent McLinko was unable to respond to many questions around sales practices” at the February 9, 2015 meeting. Additionally, Respondent Russ Anderson interjected during the meeting and stated at the meeting “that the Community Bank group risk function had a ‘good partnership with Audit.’”<sup>2952</sup>
271. The February 16, 2015 annual incentive compensation risk memorandum from the Bank’s Chief Risk Officer and its Director of Human Resources to the CEO and the Human Resources Committee of the Board stated: “As a follow up to issues identified as part of 2013 compensation process for monitoring in 2014, we reviewed the progress against Sales Integrity issue in Community Banking, specifically store level quality processes. We believe appropriate actions were taken to address the issues during the performance year and no compensation adjustment is required for the 2014 cycle.”<sup>2953</sup> The memorandum noted that the Chief Risk Officer’s and Director of Human Resources’ evaluation of risk outcomes was based, in part, on a “holistic review of audit findings related to the business, with a focus on the Unsatisfactory and high-risk Needs Improvement

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<sup>2950</sup> MSD-379.

<sup>2951</sup> MSD-185.

<sup>2952</sup> MSD-270 (NBE Hudson Expert Report) at ¶ 25, 30.

<sup>2953</sup> MSD-433 at 4.

audit issues.”<sup>2954</sup>

272. On February 19, 2015, Respondent McLinko updated Respondent Russ Anderson on another WFAS meeting with the OCC regarding sales and cross-sell, to provide her with additional perspective. In the update, Respondent McLinko described part of the conversation: “I took that opportunity to tell them (after we had emailed them asking them to go to you) to make all such inquiries specifically relating to Community Bank process with you and your team.”<sup>2955</sup>
273. On March 12, 2015, WFAS issued its 2014 Community Banking Enterprise Risk Management Assessment (“2014 CB ERMA”), concluding again that “[r]isk management for Community Banking (CB) is **Satisfactory**. Community Banking risk management processes and controls are designed to identify, manage, monitor, and report on credit, operational, and compliance risk.” Culture and Strategy & Objective Setting were rated Strong. Governance, Risk Response and Control, and Risk Identification, Assessment and Analysis were rated Satisfactory.<sup>2956</sup> At the time, ERMA ratings were Strong, Satisfactory, Needs Improvement, or Weak.<sup>2957</sup>
274. On March 13, 2015, WFAS issued its audit report on *Enterprise Incentive Compensation*, which concluded compensation processes and the overall system of internal control was **Effective**. In the audit, WFAS had “evaluated the end-to-end processes Wells Fargo uses to manage incentive compensation risk. Our scope focused on the ICRM program, key regulatory requirements related to incentive compensation, and [certain] processes put in place.”<sup>2958</sup> The audit report also specified that the Community Bank’s processes and risks related to managing incentive compensation were effective as well.<sup>2959</sup>
275. On March 24, 2015, Respondent McLinko emailed his notes from the Community Bank’s March Risk Management Committee Meeting to his audit team. One discussion topic was the OCC’s examination of the Community Bank’s operational risk and cross sell/ sales practices and the Respondent Russ Anderson’s expectation to receive a couple MRAs from the OCC. Respondent McLinko also noted, “again, [Carrie Tolstedt] and the management team, was very involved in the meeting as noted above. [Carrie Tolstedt] and team set the tone at the top and their understanding of risk. It also is a clear indication of the risk culture that [Carrie Tolstedt] instill[s] in the [Community Bank].”<sup>2960</sup>

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<sup>2954</sup> MSD-433 at 3.

<sup>2955</sup> MSD-399.

<sup>2956</sup> MSD-380 at 3.

<sup>2957</sup> *Id.*

<sup>2958</sup> MSD-515 at 3.

<sup>2959</sup> *Id.* at 14.

<sup>2960</sup> MSD-401.

276. On March 30, 2015, WFAS issued its audit report on *RB – SOCR* (Regional Banking Store Operations Control Review (“SOCR”). In determining annual audit coverage, WFAS leveraged the results of SOCR on-site reviews. WFAS rated the SOCR program **Needs Improvement** because of the accuracy and completeness of program execution and supervisory review.<sup>2961</sup> On February 10, 2015, Respondent McLinko had assured Carrie Tolstedt that the SOCR audit would not be reported to the Board.<sup>2962</sup>
277. Neither the March 30, 2015 RB SOCR audit report nor any other audit report issued during Respondent Julian’s and McLinko’s tenures before October 2016 identified that: the Bank was opening up large numbers of accounts or services without customer consent; the Bank had a systemic problem with sales practices misconduct; the Community Bank’s sales goals were unreasonable; there was undue sales pressure in the Community Bank; or the Bank’s preventative or detective controls regarding sales practices were unsatisfactory or inadequate.<sup>2963</sup>
278. On May 4, 2015, the Los Angeles City Attorney filed a complaint against the Bank alleging it violated the California Unfair Competition Law, Business and Professional Code § 17200 et seq. by engaging in unlawful sales practices.<sup>2964</sup>
279. On May 4, 2015, WFAS presented its First Quarter 2015 Summary to the Audit and Examination Committee of the Board. Audit’s quarterly report to the Board contained the following update on the “Sales Conduct, Practices and the Consumer Business Model” Noteworthy Risk: “Sales audits are planned for Regional Banking and Business Banking in 2015. The focus of these reviews is on the sales practices and conduct to ensure customers are sold products meeting their financial needs.”<sup>2965</sup>
280. In May 2015, the OCC commenced an examination of Enterprise Sales Practices at the Bank, which was prompted by the City of Attorney of Los Angeles lawsuit against the Bank relating to its sales practices. The review “focused on the events in 2013 that led to the initial employee termination, the investigation of employee misconduct that followed, and overall changes in governance intended to improve the bank’s practices.” (MSD-213). The former Examiner-in-Charge of the Bank explained that the purpose of the May 2015 examination was “to find the truth. We were told being one thing by the bank and management, and we were seeing something else” in the City Attorney of

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<sup>2961</sup> MSD-520.

<sup>2962</sup> MSD-368.

<sup>2963</sup> MSD-638 (Deese Dep. Tr.) 245:22-251:17.

<sup>2964</sup> Julian Amended Answer ¶¶ 123, 223; McLinko Amended Answer ¶¶ 123, 223.

<sup>2965</sup> MSD-634 at 59-60.

Los Angeles lawsuit.<sup>2966</sup>

281. According to the Bank's former Examiner-in-Charge Bradley Linskens, Respondent Julian delivered a similar message to the OCC around that time. Mr. Linskens testified that: "I do remember a number of meetings that I had with David, and the message that we received from him during that period was consistent with the other executives, that it was, you know, rogue employees and -- and that, you know, the bank was working to address it -- or had worked to address it. And at that period of time, there was not one executive who was volunteering that it was more significant than a few rogue employees."<sup>2967</sup>
282. On June 26, 2015, the OCC communicated the results of its May 2015 examination of Enterprise Sales Practices in Supervisory Letter WFC 2015-36 ("SL 2015-36"). SL 2015-36 concluded, "Wells Fargo's management and oversight of Enterprise Sales Practices risk is weak and needs to improve."<sup>2968</sup>
283. SL 2015-36 contained five MRAs, covering all three lines of defense: Enterprise Sales Practices - Corporate; Enterprise Sales Practices - Second Line of Defense; Complaints; Community Bank Group - Sales Practices; and Audit Coverage. The Enterprise Sales Practices - Corporate MRA required the Bank to hire an independent third party consultants "to conduct a thorough review of Wells Fargo's approach to Enterprise Sales Practices" and "to ensure all allegations of inappropriate behavior (e.g., gaming, pinning, bundling, etc.) are evaluated and properly remediated."<sup>2969</sup>
284. The concern identified by the OCC in the Community Bank Group - Sales Practices MRA, was that the Community Bank "lacks a formalized governance framework to oversee sales practices and does not have effective oversight and testing of branch (store) sales practices." The MRA explained that inaction "could impact reputation risk and cause customer harm."<sup>2970</sup> The concern identified by the OCC in the Audit Coverage MRA was that "Wells Fargo Audit Services (WFAS) did not identify the issues noted in this Supervisory Letter and past coverage did not provide an enterprise view of sales practices." The MRA explained that inaction "increases compliance, legal, and reputation risks."<sup>2971</sup>
285. On July 28, 2015, the OCC issued a Notice of Deficiency under 12 C.F.R. Part 30 to the Bank because based on deficiencies and weaknesses in all three lines of defense related to the Bank's compliance risk management program, which

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<sup>2966</sup> MSD-302 (Linskens Dep. Tr.) at 147:12-16.

<sup>2967</sup> *Id.* at 119:3-17.

<sup>2968</sup> MSD-213 at 2.

<sup>2969</sup> *Id.* at 3-4, 6-9.

<sup>2970</sup> *Id.* at 8.

<sup>2971</sup> *Id.* at 8-9.

Respondents Julian and McLinko received.<sup>2972</sup> The Part 30 Notice of Deficiency required the Bank to submit a Safety and Soundness Plan to “adequately address all of the deficiencies and weaknesses noted in compliance-related supervisory letters” and must specifically include “[d]evelop[ing] audit programs that test the first lines of defense compliance with high-risk laws and regulations” and “[r]eport[ing] Internal Audit identified deficiencies to the Bank’s Audit and Examination Committee, along with the severity of the deficiencies and the corrective actions.”<sup>2973</sup>

286. On August 10, 2015, the Bank provided a response to SL 2015-36, stating that the Bank “recognize[s] the importance of the concerns discussed in the Supervisory Letter to Wells Fargo and its customers.”<sup>2974</sup> The response named Respondent McLinko as an accountable executive for the Audit Coverage MRA and stated that WFAS was “committed to maintaining independence and implementing the changes needed to address the concerns noted in the MRA” and “evalu[ating] the current sales practices audit coverage and commit to develop a comprehensive audit approach.” WFAS also committed to “engag[ing] with Accenture and PwC to understand the scope of their coverage as it relates to Wells Fargo’s approach to Enterprise Sales Practices and assessing potential customer harm for allegations of inappropriate behavior, respectively. Their review and evaluation will be compared to our current sales practices audit coverage, and enhance coverage where appropriate. WFAS anticipate incorporating the preliminary findings from PwC and Accenture as part of our 2016 audit plan process and will enhance our coverage when additional information is available.”
287. The Bank’s August 10, 2015 response further stated, “WFAS will be engaged with the various LOBs as they develop and implement corrective actions to the Enterprise Sales Practices MRAs. The scope of WFAS’s work will include: issue monitoring and validation, reviewing governance processes and enhanced policy, monitoring of projects/initiatives to enhance Enterprise Sales Practices compliance, and obtaining an understanding of key activities and functions performed to ensure compliance with enterprise sales practices along with their sustainability.”<sup>2975</sup>
288. Accenture’s top recommendation was to “Review the solution sales goals setting at district/store level, and reward team members based more on positive customer outcomes (e.g., account utilization) with less emphasis on solutions

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<sup>2972</sup> MSD-414 at 1-2.

<sup>2973</sup> *Id.* at 2-3.

<sup>2974</sup> MSD-313 at 1.

<sup>2975</sup> *Id.* at 11; Julian Amended Answer ¶¶ 419, 468; McLinko Amended Answer ¶¶ 419, 468.

sold.”<sup>2976</sup> The report noted, “solution sales goals have not been met since 2013 (even after accounting for adjustments made throughout the year to improve achievement rates).”<sup>2977</sup> The Accenture Report warned of the risk that “[n]egative sales practices may occur due to pressure to meet unreasonable sales targets set by senior management, which could lead to adverse customer impact.”<sup>2978</sup>

289. Respondent McLinko testified “in the Accenture report, the volume of interviews that were done, the data that they had gathered on a very large sample of the community bank, they had a very strong basis to come up with their conclusions. So that led me, at least initially to like, there’s a systemic issue here, from that perspective.”<sup>2979</sup>

290. On November 17, 2015, WFAS presented its Third Quarter 2015 Summary to the Audit and Examination Committee of the Board. Audit’s quarterly report to the Board contained the following update on the “Sales Conduct, Practices and the Consumer Business Model” Noteworthy Risk: “As reported last quarter, the OCC issued a supervisory letter on June 26, 2015, that included five MRAs covering all lines of defense. In 3Q15, Wells Fargo management formally responded to the OCC with actions plans for the five issues, which the OCC formally accepted on September 9, 2015. A group within WFAS has been formed to assess and monitor management’s remediation efforts across the enterprise. The WFAS working group, which encompasses all lines of defense audit teams, as well as Risk Management audit teams, has been formed to enhance future audit coverage of Sales Practices, but also of the associated Incentive Compensation, Human Resource, Ethics Line, Complaint Management, and Corporate Investigation functions. A Sales Practices Standard Audit Program is also being created to ensure consistency in audit coverage. In 2017, WFAS will issue the ERMA opinion for Sales Practices for 2016.”<sup>2980</sup>

291. In the February 12, 2016, annual incentive-compensation risk memorandum from the Bank’s Chief Risk Officer and its Director of Human Resources to the CEO and the Human Resources Committee of the Board, sales practices received an Issue Rating of “Improvement Needed” but an “Overall Risk Performance” assessment of “Satisfactory,” the highest rating.<sup>2981</sup> The memorandum did not recommend any incentive compensation adjustments for Head of the Community Bank Carrie Tolstedt. The memorandum noted that the Chief Risk

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<sup>2976</sup> MSD-51 at 4.

<sup>2977</sup> *Id.* at 27.

<sup>2978</sup> *Id.*

<sup>2979</sup> MSD-276 (McLinko Tr.) at 56:8- 19.

<sup>2980</sup> MSD-405 at 63.

<sup>2981</sup> MSD-456 at 8, 13.

Officer's and Director of Human Resources' evaluation of risk outcomes was based, in part, on a "holistic review of audit findings related to the business, with a focus on the Unsatisfactory and high-risk Needs Improvement audit issues."<sup>2982</sup>

292. On March 18, 2016, WFAS issued its Community Banking Enterprise Risk Management Assessment for 2015 ("2015 CB ERMA"), concluding yet again that "Enterprise Risk Management [] for Community Banking [] is Satisfactory." Strategy and Objective Setting, Governance, Culture, Risk Identification, Assessment, and Analysis, and Risk Control and Response were all rated Satisfactory. At the time, ERMA ratings were Satisfactory, Needs Improvement, or Weak, i.e. Satisfactory was the highest possible rating at the time.<sup>2983</sup>
293. With respect to Culture, the 2015 CB ERMA noted, "actions are underway to strengthen sales practices across all channels by fostering a culture that only needs-based and value-add product and service solutions are delivered to customers. Efforts include assessing solutions goals and customer outcomes, enhanced vision and values assessments/reinforcement, additional training, enhanced Ethics Line procedures and cultural benchmark/monitoring." The 2015 CB ERMA also noted that "management is expanding sales practices oversight in areas such as enhanced reporting, trending, ethics line procedures, training and risk management (e.g., Regional Services, RB Compliance and Operational Risk, and Sales & Service Conduct Oversight teams, Conduct Risk Committee, etc.)."<sup>2984</sup>
294. On April 21, 2016, Respondent McLinko sent the following email message to Respondent Russ Anderson:

Hi Claudia,

Not sure if you traveled home yet or not, but if you did, hope it was a good flight. If not, safe travels.

My regulator meeting to discuss the 2016 audit plan was a non-event. We discussed my sales practices audit validation coverage in some detail, along with ERMA (the area where the topic of Risk Culture has been raised). Chris Mosses asked the most questions, but nothing on the culture front. They continue to be very interested in complaints and ethics line, the rollout, the data, and what is done with that data. Chris indicated that she thought she was meeting with you next week. If so, I'm sure the topics will come up. Jenny asked a few questions, but more

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<sup>2982</sup> MSD-456 at 2.

<sup>2983</sup> MSD-384 at 1.

<sup>2984</sup> MSD-384.



on my FTE count and some specifics on my plan.

It just hit me that you and Carrie meet with regulators monthly and culture doesn't come up and I meet with them bimonthly and sometimes in between and the topic is not specifically raised with me (I hear it from my peers). Wonder what that is about?

That's the low lights. I'd appreciate it if you don't mention audit and the risk culture topic together when and if you approach the subject with the regulators.<sup>2985</sup>

295. On July 18, 2016, the OCC communicated the findings from its ongoing review of sales practices at the Bank in Supervisory Letter WFC 2016-36 ("SL 2016-36"), which Respondents Julian and McLinko received.<sup>2986</sup> SL 2016-36 noted that since the issuance of SL 2015-36, the OCC "reviewed additional reports and material prepared by the Bank and third-party consultants as part of our ongoing supervision. . . One of our objectives in reviewing these materials was to determine whether the findings identified instances of unsafe or unsound banking practices. Based on our ongoing review, we have concluded that the Bank's risk management of its sales practices and its sales practices themselves are unsafe or unsound."<sup>2987</sup>

296. Regarding the unsafe or unsound practices, SL 2016-36 elaborated:

- a. "The practice of opening deposit accounts without authorization, the practice of moving funds without customer consent (simulated funding) and the failure to timely refund or remediate fees charged are considered unsafe or unsound banking practices."<sup>2988</sup>
- b. "The widespread and unauthorized opening of credit card accounts without consent . . . is considered an unsafe or unsound banking practice."<sup>2989</sup>
- c. "[T]he Bank engaged in the unsafe or unsound practice of failing to adequately monitor and control sales practices to prevent such inappropriate employee behavior."<sup>2990</sup>
- d. "[T]he Bank engaged in the unsafe or unsound practices of operating

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<sup>2985</sup> McLinko's ECSFM at No. 490, quoting MSD-407.

<sup>2986</sup> MSD-342 at 1.

<sup>2987</sup> *Id.* at 2.

<sup>2988</sup> MSD-570 at 5.

<sup>2989</sup> *Id.* at 6.

<sup>2990</sup> *Id.*

without adequate controls and monitoring over its sales practices.”<sup>2991</sup>

297. The OCC informed the Bank in SL 2016-36 that the “inappropriate sales practices and the lack of adequate risk management over the sales practices referenced in this letter are considered unsafe or unsound banking practices, and the OCC is considering formal enforcement action against the Bank.”<sup>2992</sup>

298. On July 18, 2016, the same day as the OCC issued SL 2016-36 communicating to the Bank that its sales practices and sales practices risk management were unsafe or unsound, Respondent McLinko wrote to Carrie Tolstedt, “congratulations on your retirement. You have been a wonderful partner with WFAS. It’s rare to find a business leader who takes risk management as seriously as you do. I’ve been lucky to work with one of the best; that being you. I, and Wells Fargo, will miss all that you bring on a day to day basis; but also know that I am very happy for you. Keep wearing the Wells Fargo Stagecoach pin.”<sup>2993</sup>

299. On September 7, 2016, Respondent McLinko's direct report asked him whether sales practices was classified as a high risk area. Respondent McLinko replied, “Nope, not even sure who makes that classification.” After discussion about whether sales practices would be considered a high-risk area, Respondent McLinko stated: “the short answer is I don’t see how it can't have a high risk classification, given the impact on the company and the regulatory interest.”<sup>2994</sup>

300. On September 8, 2016, the OCC issued a consent order and assessed a \$35,000,000 civil money penalty to the Bank for deficiencies and unsafe or unsound practices in the Bank’s risk management and oversight of the Bank’s sales practices, and unsafe or unsound sales practices by the Bank.<sup>2995</sup>

301. In the Sales Practices Consent Order, the Comptroller found “that the OCC has identified the following unsafe or unsound sales practices in the Bank’s Community Bank Group,” which the Sales Practices Consent Order referred to as the “unsafe or unsound sales practices”:

- a. “The selling of unwanted deposit or credit card accounts”;
- b. “The unauthorized opening of deposit or credit card accounts”;
- c. “The transfer of funds from authorized, existing accounts to unauthorized accounts (‘simulated funding’)”; and
- d. “Unauthorized credit

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<sup>2991</sup> *Id.*; Julian Amended Answer ¶ 131; McLinko Amended Answer ¶ 131.

<sup>2992</sup> MSD-342 at 7; Julian Amended Answer ¶ 131; McLinko Amended Answer ¶ 131.

<sup>2993</sup> McLinko Amended Answer ¶ 470; MSD-409.

<sup>2994</sup> MSD-362.

<sup>2995</sup> MSD-343.

inquiries”.<sup>2996</sup>

302. In the Sales Practices Consent Order, the Comptroller also found “that the OCC has identified the following deficiencies and unsafe or unsound practices in the Bank’s risk management and oversight of the Bank’s sales practices:”

- a. “The incentive compensation program and plans within the Community Bank Group were not aligned properly with local branch traffic, staff turnover, or customer demand, and they fostered the unsafe or unsound sales practices”;
- b. “The Bank lacked an Enterprise-Wide Sales Practices Oversight Program and thus failed to provide sufficient oversight to prevent and detect the unsafe or unsound sales practices”;
- c. “The Bank lacked a comprehensive customer complaint monitoring process that impeded the Bank’s ability to: (1) assess customer complaint activity across the Bank; (2) adequately monitor, manage, and report on customer complaints; and (3) analyze and understand the potential sales practices risk”;
- d. “The Bank’s Community Bank Group failed to adequately oversee sales practices and failed to adequately test and monitor branch employee sales practices”; and
- e. “The Bank’s audit coverage was inadequate because it failed to include in its scope an enterprise-wide view of the Bank’s sales practices.”<sup>2997</sup>

303. In the Sales Practices Consent Order, the Comptroller further found that by reason of the unsafe or unsound sales practices and unsafe or unsound practices in the Bank’s risk management and oversight of the Bank’s sales practices, “the Bank engaged in reckless unsafe or unsound banking practices that were part of a pattern of misconduct.”<sup>2998</sup>

304. The Sales Practices Consent Order contained actionable articles covering an Enterprise-Wide Risk Review of Sales Practices Risk, an Enterprise-Wide Sales Practices Risk Management and Oversight Program, an Enterprise Complaints Management Policy, Internal Audit, and Customer Reimbursement.<sup>2999</sup>

305. On September 11, 2016, Respondent Julian emailed WFAS’s Executive Audit Directors, including Respondent McLinko, asking, “How would we

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<sup>2996</sup> *Id.*

<sup>2997</sup> MSD-343.

<sup>2998</sup> *Id.* at 3.

<sup>2999</sup> *Id.*

answer the question[:] What has WFAS done to determine if we have sales practices issue in the other businesses?” Several of the Executive Audit Directors responded, including Respondent McLinko, who described, not WFAS activities completed before 2016, but the development of the 2016 sales practices coverage strategy.<sup>3000</sup>

306. In response to another auditor’s inquiry, Mr. McLinko stated:

David,

Mark provided a well-rounded response to your questions. We have a centralized working group that is coordinating our coverage of Sales Practices. Kathy Sheng is leading that group and it included representatives from all LOB audit teams, as well as teams that cover Internal Investigations, Ethics Line and Compensation. We’ve developed sales practices coverage strategy for 2016 (which will be updated in response to the CO) as well as a Sales Practices Standard Audit Program which all teams all [*sic*] using to test sales practices. In addition, and like Mark indicated, all teams are in the initial stages of using the complaints data (is a large complaints initiative at the top of the house) to target testing.

In my absence, Kathy Sheng for the overall sales practices project, and Bart Deese for Community Banking are the key contacts.

Let me know if you have other questions.<sup>3001</sup>

307. On September 12, 2016, Respondent McLinko responded, describing WFAS’s reliance on the Community Bank’s SOCR program; and, after WFAS failed SOCR’s review documentation, the addition of an account opening audit in the 2015 audit plan.<sup>3002</sup>

308. In response to another auditor’s inquiry, Mr. McLinko stated:

My response is related to the Stores as in the Call Centers, all Sales are recorded, which gives us the ability to select samples of sales from the recordings and test for consent, etc.

Regarding the Stores:

- In many ways, we have leveraged the Store Operations Control Review (SOCR) which is part of the ILOD. SOCR goes into every store every year and performs a variety of functions, one being a review of account opening documentation and signatures. Every two years we test: the

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<sup>3000</sup> MSD-469.

<sup>3001</sup> McLinko’s ECSFM at No. 502, quoting MSD-469 at -624.

<sup>3002</sup> MSD-469; MSD-364.

program by going into a sample of stores and re-performing the work the SOCR team does. Several years back we raised a moderate rated issues as it relates to the documentation supporting the process (not that they weren't performing the work). Audit validation of the corrective actions failed the issue and at that time we raised it to a high rated issue.

- Because of that fail, we added an account opening audit: to our plan in 2015. We announced the audit: and then the LA lawsuit happened. As a result, the scope of the audit was changed and put under ACP.
- We have also tested for new account documentation in an audit called Deposit Products Support Services. This audit would review for account documentation and customer signature.
- We have also tested the Sales and Services Conduct Oversight Team, which is the group that was part of researching the sales practices issues back in 2013. That led to the investigation and subsequent TM firings; that led to the LA lawsuit.
- In 2014, we tested incentive plans in coordination with Andrew's team, during that audit we tested: Customer Connection (WFCC), Personal Banker 1/Assistant Store Mgr. (Regional Banking), and RBPB/Private Banker (Regional Banking) incentive plans.

In short, over the years, we have relied on the SOCR program. Once we failed the SOCR issue validation, during annual audit planning in 2014, we added a Regional Banking account-opening audit to the 2015 audit plan which is mentioned above.

In addition:

- As you're aware, complaints has been an issue at the top of the house with continued rollout of the program, thus we're beginning to be able to utilize that: information (which was also part of our response to the MRA).
- The new technology that captures customer consent for deposits, credit: cards and unsecured lines of credit just: went live recently which we are testing as part of the IVRA validation.
- A retrospective review for this topic was performed in response to the OCC MRA's. In a nutshell, this covers what we've done.<sup>3003</sup>

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<sup>3003</sup> McLinko's ECSFM at No. 504, quoting MSD-364 at -513-514.

309. Another Executive Audit Director responded with some suggestions for moving forward and Respondent Julian replied, “I will really need to respond to ‘where was Audit’ and while I’d like to be able to say we tested for activity like this, specifically in the Community Bank, I don’t think we did.”<sup>3004</sup>
310. On September 12, 2016, after receiving Respondent Julian’s question, “Where was audit while this [sales practices] activity was taking place?,” Respondent McLinko sent an instant message to two of his direct reports as shown above, asking, “have we audited new account opening in the past as to customer consent?” His direct reports responded that the first account-opening audit in branches occurred in 2016. Respondent McLinko stated: “something doesn’t add up. [W]e added the account-opening audit to the plan in 2015. [I] would have thought we knew earlier.”<sup>3005</sup>
311. On November 8, 2016, Respondent Julian was interviewed by Shearman & Sterling LLP on behalf of the Oversight Committee of the Board of Directors.<sup>3006</sup> According to the notes from the November 8, 2016 interview, Respondent Julian “stated that Audit first became aware of the need to plan additional audits around [Community Bank’s] sales practice controls in [Community Bank] in late 2013, shortly before the L.A. Times article was published. Audit’s awareness arose in part from data showing an increasing number of sales practice-related issues.”<sup>3007</sup> “He was, however, unaware of SAR and EthicsLine metrics related to sales practices having resulted in a change to any particular audit’s scope.”<sup>3008</sup> “He also stated that he was unaware of Audit having conducted any audit into the ways incentive compensation policies had motivated lower level team members.”<sup>3009</sup> According to the interview notes, Respondent Julian stated, “To the extent Audit had failed to review issues or functions that it should have, he said, this was Audit’s responsibility.”<sup>3010</sup>
312. On April 27, 2017, WFAS issued its 2016 Sales Practices Enterprise Risk Management Assessment for 2016 (“2016 SP ERMA”). The 2016 SP ERMA concluded that Enterprise Risk Management for sales practices risk was Weak, the lowest WFAS audit rating. WFAS defined sales practices risk as sales practices, complaints, team member allegations including EthicsLine, and Internal Investigations. The weak rating was driven by several factors, including the lack of an overall view of sales practices risk across the Bank and the

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<sup>3004</sup> MSD-469.

<sup>3005</sup> MSD-345.

<sup>3006</sup> MSD-501.

<sup>3007</sup> *Id.* at 5.

<sup>3008</sup> *Id.*

<sup>3009</sup> *Id.* at 7.

<sup>3010</sup> *Id.* at 5.

effectiveness and sustainability of the recently implemented enhancements needed to be demonstrated.<sup>3011</sup>

313. The 2016 SP ERMA issued on April 27, 2017 rated the First Line of Defense (i.e., the Community Bank) as Weak due to the need to better understand where sales practices risk reside, the need to implement the Sales Practices Risk Governance Document, and additional time to demonstrate the recently implemented enhancements to demonstrate effectiveness and sustainability.<sup>3012</sup>

The 2016 SP ERMA rated the Second Line of Defense Weak due to the magnitude and complexity of the corrective actions that remained to build and sustain an effective sales practices risk management program.<sup>3013</sup> Finally, the 2016 SP ERMA rated Team Member Allegations processes as Weak and Complaints and Internal Investigations processes as Needs Improvement.<sup>3014</sup>

314. One of the auditors responsible for the 2016 SP ERMA testified that despite the improvements made by the Bank in 2015 and 2016 in response to OCC Matters Requiring Attention, controls and risk management related to sales practices was still weak.

Q: So notwithstanding the risk management and control improvements to address the MRAs from 2015 through 2016, audit still gave sales practices risk a weak rating overall; is that correct?

A: We - - we concluded the overall sales practices risk is weak, as of December 31, 2016.<sup>3015</sup>

315. Respondent Julian testified before the OCC during his May 31, 2018 sworn statement that he would now consider the Community Bank's controls over sales practices misconduct from 2012 to 2016 to be "unsatisfactory," the lowest possible rating that Audit could issue at that time:

Q. Okay. But how about if we limit it to not just work that Audit – and the Audit Group did by itself, but work that the Audit Group did by itself, but work that the Audit Group did in conjunction with other parts of the bank or other consultants? Would you then conclude, based on that – the work that the Audit Group did by itself and in conjunction with other groups – that the controls for sales practice misconduct were unsatisfactory?

A. That the controls – I'm sorry.

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<sup>3011</sup> MSD- 386 at 1.

<sup>3012</sup> *Id.* at 3.

<sup>3013</sup> *Id.* at 2.

<sup>3014</sup> *Id.* at 4.

<sup>3015</sup> MSD-505 (Sheng Dep. Tr.) at 220:23-221:3.

Q. Yes, the controls to manage the risk of sales practice misconduct were unsatisfactory.

A. Based on what I know now, yes.

...

Q. Okay. And if the systems did not prevent employees from issuing credit cards and debit cards without customer signatures, how would you rate the controls?

A. Based on the impact and what we know the controls were unsatisfactory in that way.

Q. Thank you. And unsatisfactory is the lowest grade you can get?

A. Yes, sir.<sup>3016</sup>

316. Respondent Julian testified before the OCC during his May 31, 2018 sworn statement that he would now consider the Community Bank's controls over sales practices misconduct from 2012 to 2016 to be "unsatisfactory," the lowest possible rating that Audit could issue at that time:

Q. Okay. But how about if we limit it to not just work that Audit – and the Audit Group did by itself, but work that the Audit Group did by itself, but work that the Audit Group did in conjunction with other parts of the bank or other consultants? Would you then conclude, based on that – the work that the Audit Group did by itself and in conjunction with other groups – that the controls for sales practice misconduct were unsatisfactory?

A. That the controls – I'm sorry.

Q. Yes, the controls to manage the risk of sales practice misconduct were unsatisfactory.

A. Based on what I know now, yes.

...

Q. Okay. And if the systems did not prevent employees from issuing credit cards and debit cards without customer signatures, how would you rate the controls?

A. Based on the impact and what we know the controls were unsatisfactory in that way.

Q. Thank you. And unsatisfactory is the lowest grade you can get?

A. Yes, sir.<sup>3017</sup>

317. Regarding the email he sent to his team asking "Where was audit?" Respondent

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<sup>3016</sup> Julian Amended Answer ¶ 414; MSD-278 (Julian Tr.) at 37:2-14, 155:22-156:5.

<sup>3017</sup> Julian Amended Answer ¶ 414; MSD-278 (Julian Tr.) at 37:2-14, 155:22-156:5.



Julian testified before the OCC during his 2018 sworn statement as follows:

A: I think I concluded that audit didn't do -- certainly in retrospect -- didn't do the level of work I wish we had done around these issues throughout the process. So I didn't get an answer where was audit. What I discovered is what we did and, in cases, what we didn't do and formed the opinion I discussed earlier that I think we could have done, should have done more, should have done more sooner.

Q Did anybody in your team give you any explanation for why audit did not do what, in fact, it should have done?

A No one gave me an explanation why something wasn't done, but they talked to me about what was done and recognized that other things could have, should have been done, especially, you know, in retrospect, based on seeing information that was available, certain flags such as Michael Bacon's, and things like that. So they didn't give me an answer why they didn't do anything as much as what they did and recognized there's more that could have been done

Q But what you are absolutely sure of now is that audit, in fact, did not do what it should have done with respect to sales practices at the bank; is that fair to say?

A It's fair to say we could have done more, we should have done more.

...

Q Okay. Well, no, I appreciate your efforts, but could have done more could always be the case. You could do a great job and you could have done an even better one. You could do a fabulous job, but, as long as it wasn't perfect, there's room for improvement. Is that what you're telling me?

A No, I don't think I –

Q Okay.

A -- whatsoever.

Q Fine. Therefore, I don't want your answer to be misinterpreted as that. Therefore, you can always do more, but my question is it fair to say that, without a doubt, audit should have done much more than it did with respect to the sales-practice misconduct issue at the bank?

A In retrospect, yes, we should have done more specific to sales practices in relation to that.

Q And the reason you are saying that they should have done more

is because they, in fact, did receive red flags and information that should have caused any competent auditor to do more; is that fair to say?

A In retrospect. Again, you know, taking it all in what we know now, seeing four emails or emails over a long period of time, taking that all into context, certainly, again, I'm going to go back to wish we would have. I'm not saying that audit did enough. I'm not making the excuse that, at the time, we did what was appropriate because we wouldn't be here, we being the company, potentially if we had done more.<sup>3018</sup>

318. Respondent Julian admitted that WFAS under his leadership never identified in any audit report the sales practices misconduct problem's root cause and did not discuss in audit reports the root cause of sales practices misconduct.<sup>3019</sup> Similarly, Respondent McLinko admitted that he and his team did not identify in any audit reports the root cause of the systemic sales practices misconduct problem.<sup>3020</sup>

319. Respondent McLinko testified before the OCC on March 2, 2018 as follows regarding the satisfactory ratings for culture Audit award the Community Bank:

Q: Okay. Based on what you know now, how would you rate the bank's culture in 2015 and 2014?

A: Community bank. I'm not talking about -- Q Community bank, yes.

A: -- the bank as a whole, just to be clear.

Q: Yes, yes. The community bank, absolutely. Community bank.

A: Yes, well, based upon what I know now and what was the information that I've learned, it certainly would not be -- have received what we would qualify as an effective rating or satisfactory rating, whatever the terms are that we had.

Q: It would be unsatisfactory. Right?

A: I -- it certainly would lead -- could lead that way. Yes.<sup>3021</sup>

Respondent McLinko further testified:

Q: Okay. Is it fair to say, though that audit, over the years totally missed the problem in the community bank, the systemic problem with sales practice misconduct?

A: I think that, based on the approach from internal audit, the process, risk, and control that we discussed—in our approach to looking at that—to looking at the leveraging, the SOCR program that we did, and our transactional approach that we took—okay—coming up with those

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<sup>3018</sup> MSD-278 (Julian Tr.) at 261:6-263:22.

<sup>3019</sup> Julian Amended Answer ¶ 411.

<sup>3020</sup> McLinko Amended Answer ¶ 411.

<sup>3021</sup> MSD-276 (McLinko Tr.) at 125:15-126:8.

effective ratings in that approach, we did not identify the sales practices issues that we've all come to see.<sup>3022</sup>

320. In a January 23, 2020 Wells Fargo press release about the OCC's Notice of Charges, the Bank's current CEO stated, "The OCC's actions are consistent with my belief that we should hold ourselves and individuals accountable. They also are consistent with our belief that significant parts of the operating model of our Community Bank were flawed. At the time of the sales practices issues, the Company did not have in place the appropriate people, structure, processes, controls, or culture to prevent the inappropriate conduct. This was inexcusable. Our customers and you all deserved more from the leadership of this Company."<sup>3023</sup>

321. The Community Bank was "Wells Fargo's largest operating segment in terms of revenue," contributing roughly half of the Company's average annual revenue and profits each year.<sup>3024</sup>

322. NBE Crosthwaite opined:

The Community Bank model with the unreasonable goals and the extreme pressure was also a wildly profitable model for the company. So with all that pressure, team members were putting on lots of real accounts and real customers, which ultimately drove up revenue, net income, and quarter after quarter, the bank's performance was going up, and their stock was going up.<sup>3025</sup>

323. The Community Bank's business model was financially profitable for Wells Fargo and was key to its growth and cross-sell success.<sup>3026</sup>

324. From January 1, 2002 through September 8, 2016 (the date of the Sales Practices Consent Order), Wells Fargo's stock price performed "significantly better than the stock price of its peers and the financial services sector."<sup>3027</sup>

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<sup>3022</sup> MSD-276 (McLinko Tr.) at 64:14- 65:1; McLinko Amended Answer ¶ 461.

<sup>3023</sup> MSD-662.

<sup>3024</sup> Julian Amended Answer ¶ 2; MSD-1 at 20 ¶ 4 ("Wells Fargo's largest business unit was the Community Bank, which contributed more than half (and in some years more than two-thirds) of the Company's revenue from 2007 through 2016."); MSD-692 at 50; MSD-693 at 42; MSD-694 at 46; MSD-695 at 44; MSD-696 at 46; MSD-697 at 45; MSD-698 at 53; MSD-658 (Pocock Expert Report) at 9-10 ¶ 44-45).

<sup>3025</sup> Tr. at 2420 (Crosthwaite); OCC Exh. 2335 at ¶¶ 63-64; OCC Exh. 2407 at 28; OCC Exh. 2330 at ¶¶ 105-107.

<sup>3026</sup> MSD-266 (Russ Anderson Dep. Tr.) at 87:16-88:24; see also MSD-294 (Wipprecht Tr.) at 133:4-11; See MSD-658 (Pocock Expert Report) at ¶ 13, 18, 19; MSD-267 (Expert Report of Tanya Smith) at ¶ 72 ("The Bank described the 'cross-sell' as 'its primary strategy' and 'the foundation of our business model.'"); MSD- 304A (Candy Dep. Tr.) at 234:4-13; MSD-649 ("The Community Bank is 'Rome' in our company—all roads lead to and from it."); MSD-692 at 100 ("cross-selling' – is very important to our business model and key to our ability to grow revenue and earnings.").

<sup>3027</sup> MSD-658 (Pocock Expert Report) at 5, 11-14.

325. Mr. Julian initially asserted that he received no additional equity compensation as a result of sales practices misconduct at the Community Bank; and averred that the expert report of Bruce Deal extensively analyzed Mr. Julian's compensation and opined that there is no basis to conclude that he received pecuniary gain due to sales practices misconduct.<sup>3028</sup>

326. There is, however, no requirement that a banker receive additional equity compensation beyond that which he was entitled under the bank's existing compensation program. Retaining employment is, in and of itself, a benefit sufficient to meet the benefit element, where such retention was occasioned by the failure of the head of the bank's third line of defense to effectively challenge inadequate controls put in place by the first line of defense. As NBE Smith testified, Mr. McLinko and Mr. Julian benefitted because they got to keep their jobs. "None of them were doing their jobs. Certainly not to any level of professional expectations, and they were able to retain their jobs."<sup>3029</sup>

327. Preponderant evidence established that both Mr. Julian and Mr. McLinko benefitted by their failure to credibly challenge the risk management practices relating to controls that should have detected and prevented sales practices misconduct at the Community Bank.

328. Deputy Comptroller Coleman opined:

Between 2013 and 2016 respondent Julian was compensated both in terms of salary bonus and stock benefits, and that remuneration was directly tied to the financial performance of -- one of the components was the financial performance of the bank. So, therefore, he benefitted financially from the continued ongoing systemic sales practices misconduct while he served as chief auditor when he had the role and responsibility of identifying that risk and assuring the Board that that risk was properly mitigated by escalating it to the Board.<sup>3030</sup>

329. NBE Candy opined:

[T]he sales practices misconduct problem persisted because its root cause, the unreasonable goals and extreme pressure, were also the very basis for the financial success of the business model. The Community Bank was the largest line of business at the Bank. It was the driver of growth for the Bank and the key to its touted cross-sell success. . . . [McLinko] reaped the benefits of that success in the form of compensation, substantial bonuses, and long-term equity awards. As WFC's share price increased during their tenures, so did their effective compensation. Cash bonuses were also substantial and linked to both

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<sup>3028</sup> Julian's ECSFM at No. 526.

<sup>3029</sup> Tr. (Smith) at 4072; see also OCC Ex. 2377 at ¶54.

<sup>3030</sup> Tr. (Coleman) at 269-70.

their individual performance as well as the performance of the bank.<sup>3031</sup>

330. Preponderant evidence established that Respondent Julian and Respondent McLinko received equity incentive compensation from Wells Fargo that was dependent on or tied to Wells Fargo's financial performance.<sup>3032</sup>
331. Between 2012 and 2016, Respondent McLinko earned approximately \$880,000 in equity compensation in addition to \$2,073,000 in cash compensation (salary and bonus).<sup>3033</sup> Between 2011 and 2017, McLinko's actual total compensation was approximately \$3,664,460. This included approximately \$1,161,460 in actual equity compensation in the form of restricted share rights, approximately \$1,768,750 in salary and \$1,125,000 in cash bonuses.<sup>3034</sup> Between 2013 and 2016, McLinko's actual total compensation was approximately \$2,334,727. This included approximately \$691,727 in actual equity compensation in the form of restricted share rights, \$1,015,000 in salary, and \$628,000 in cash bonuses.<sup>3035</sup>
332. Evidence adduced during the hearing included evidence that had not been available to the Comptroller when the Notice of Charges was issued. First, Mr. Julian and Mr. McLinko filed materially incomplete answers that withheld from this Tribunal the true extent of their knowledge and information pertaining to factual allegations appearing in the Notice.<sup>3036</sup>
333. Next, only after the filing of the Notice of Charges did the Bank admit to opening millions of accounts or financial products that were unauthorized or fraudulent.<sup>3037</sup>
334. Next, during the discovery process testimony from both Mr. Julian and Mr. McLinko was taken. Thereafter, during the hearing, both Mr. Julian and Mr. McLinko provided hearing testimony that was materially inconsistent with their testimony and with the answers they provided in their 15-Day Letters, resulting in conflicts in their testimony unavailable at the time the Notice was filed. For example, Mr. Julian's Response to the 15-Day Letter noted that "with the benefit of hindsight we do not dispute that sales practices violations were widespread and driven by a systemic disconnect between incentives and ethical and legal

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<sup>3031</sup> OCC Exh. 2340 at ¶ 211-213.

<sup>3032</sup> MSD-283A (Julian Expert Report of Bruce Deal) at 12, 20-21; MSD-283B (McLinko Expert Report of Bruce Deal) at 15, 19.

<sup>3033</sup> MSD- 283B (McLinko Expert Report of Bruce Deal) at 17-18.

<sup>3034</sup> SD Order at 581-82; OCC Exh. 2367 at 0015-18; OCC Exh. 2055; OCC Exh. 2941.

<sup>3035</sup> OCC Exh. 2055.

<sup>3036</sup> See, Order Regarding Enforcement Counsel's Motion Concerning the Answers of Respondents Strother, Julia, and McLinko, issued July 16, 2020.

<sup>3037</sup> See OCC Exh. 2327 at 0010, 0027, 0031.

obligations”.<sup>3038</sup> Contradicting this averment, Mr. Julian repeatedly used the hearing to assert he found no evidence of systemic or widespread misconduct driven by incentives.<sup>3039</sup>

335. Next, neither Mr. Julian nor Mr. McLinko provided financial information that had been requested prior to the issuance of the Notice of Charges, thereby forestalling until after the Notice had been issued the process by which their ability to pay a civil penalty could be assessed.

336. Next, there is merit in Enforcement Counsel’s proposition that the increase in the proposed civil money penalty does not constitute retaliation for Respondents’ exercising their right to a hearing.<sup>3040</sup> The increase in the proposed penalty can be wholly attributed to the Respondents “plac[ing] themselves in their self-contradictory position after this litigation began.”<sup>3041</sup> No better example of this exists than Mr. Julian’s incredible assertion that he was not an officer of the Bank, in his attempt to avoid the OCC’s jurisdiction – a claim not made until after the Notice was issued, one that clearly contradicted his prior statements and testimony before the OCC.

337. Next, only through the process leading up to the filing of Enforcement Counsel’s summary disposition motions was it possible to take the full measure of Respondents’ good faith – one of the factors that must be considered when recommending a civil penalty. The record reflects, as described above, substantial evidence of sustained gross neglect by each Respondent, coupled with evidence that each Respondent was motivated by greed and a desire to keep their jobs, which required them to withhold from the Bank’s Board of Directors and its regulators the true scope and nature of the Bank’s highly profitable and seriously unsafe compensation practices.

338. Last, the hearing produced the remarkable and indefensible position by both Mr. Julian and Mr. McLinko asserting that having witnessed the testimony presented neither Respondent could articulate whether incentive compensation through sales goals was the root cause of Community Bank team member sales practices misconduct. This position utterly beggars belief, given the abundance of uncontroverted evidence establishing the relationship between the sales goals and the misconduct.

339. On or about September 8, 2016, the Bank paid a total of \$185 million as part of a stipulated judgment to settle the Los Angeles City Attorney lawsuit, and to pay

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<sup>3038</sup> OCC Ex. 1938 at 22-23 (page 20-21 of the Response).

<sup>3039</sup> Tr. (Julian) at 7072: “Again, I was saying -- in other words, notwithstanding that, I was stating -- not disputing that for the moment, in the -- in the consideration of my statements stating that I acted appropriately and in accordance with the professional standards as chief auditor of Wells Fargo Corporation [sic]. I wasn’t conceding that it was systemic. I was just stating notwithstanding that, irregardless [sic] of most of that, I acted appropriately.”

<sup>3040</sup> See, Enforcement Counsel’s Post-Hearing Reply Brief as to Paul McLinko at 88.

<sup>3041</sup> Id.

civil money penalties assessed by the CFPB and OCC related to the Bank's systemic sales practices misconduct.<sup>3042</sup>

340. The September 2016 announcement of the settlement and subsequent public awareness of the sales practices misconduct problem, which resulted from Respondents' misconduct, significantly damaged the Bank's reputation. The May 2017 results of a corporate reputation tracking study indicated the Bank's favorability rating plummeted 50% between September and October 2016, and by May 2017 had recovered only to 65% of its previous level.
341. The announcement of the September 2016 settlement and subsequent public backlash caused the Bank to change the Community Bank's business model and eliminate product sales goals, effective October 1, 2016.<sup>3043</sup>
342. After the September 8, 2016 settlement announcement, and continuing over the next several years, the Bank suffered a series of other losses related to sales practices misconduct, including civil judgments to settle class action lawsuits, investigations commissioned to root out malfeasance, the costs of advertising campaigns aimed at rehabilitating its reputation, and in February 2020, a \$3 billion settlement with the DOJ and the SEC.<sup>3044</sup>
343. Respondent Julian testified before the OCC in May 2018 as follows: "I'm not saying that audit did enough. I'm not making the excuse that, at the time, we did what was appropriate because we wouldn't be here, we being the company, potentially if we had done more."<sup>3045</sup>
344. Respondent Russ Anderson testified, based on her experience as a senior risk professional with years of experience in the risk business, that when employees engage in various types of sales practices misconduct, they are violating applicable laws and regulations:

Q: Understand. So just so we're clear, you agree that when employees issue a product or service to a customer without the customer's consent, they're violating applicable laws and regulations; correct?

A: I would agree, yes.

Q: Okay. And you also agree that when employees transfer customer funds without customer consent, they're violating applicable laws and regulations; correct?

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<sup>3042</sup> Julian Amended Answer ¶ 132; McLinko Amended Answer ¶ 132; MSD-562.

<sup>3043</sup> MSD-289A (Sloan Tr.) at 251:2-253:6; MSD- 288-B (Strother Tr.) at 49:22-50:10; MSD-8B (Stumpf Tr.) at 228:11-229:16; MSD-563.

<sup>3044</sup> MSD- 293A (Hardison Tr.) at 34:4-36:18; MSD-289A (Sloan Tr.) at 251:2-253:6; MSD-564; MSD-1.

<sup>3045</sup> MSD-278 (Julian Tr.) at 263:18-22; see also id. at 269:12-270:1 ("Certainly I think management would admit that we were too slow to act.")

A: I would agree, yes.<sup>3046</sup>

345. Respondent Russ Anderson's expert witness, Kathlyn Farrell, testified that sales practices misconduct violated UDAP, Regulation Z, Regulation DD, and Truth in Savings Act.<sup>3047</sup> The testimony by Ms. Farrell that was relied upon by Enforcement Counsel is as follows:

Q. Okay. I'm going to read part of this e-mail to you. In -- in the body of the e-mail starting with the third sentence, Ms. Bresee wrote: "To be honest, if the allegations are proven to be correct, they violate a series of laws which are in the talking points we drafted. So, to the extent a team member gives a customer a credit card they didn't want/didn't consent to, it likely violates: UDAAP (OCC), UDAAP," with two As, "(CFPB), TILA, Reg Z, and the Fair" -- "and FCRA. On the deposit side, providing a savings/checking account that a customer didn't want/didn't consent to likely violates: UDAP, UDAAP" with two As, "the Truth in Savings Act, and Reg DD. (As well as similar state laws.)" Do you see that?

A. I do.

Q. Okay. You mentioned previously that whether there were any violations of law as a result of the sales practices misconduct issues crossed your mind; is that right?

A. Yes.

Q. Okay. Does sales practice misconduct, as we defined it earlier, violate UDAP with one A [verbatim]?

A. I think so.

Q. Does sales practice misconduct, as we described it before, violate UDAAP with two As?

A. I think it probably does.

Q. Okay. Does opening an unauthorized account violate TILA?

A. Probably. I'm saying that without looking it up, but I suspect that it does.

Q. Why?

A. Because I don't think you're supposed -- well, now that I think about it, I don't think you're supposed to issue any activated credit card to anybody without their consent. So, yes, if the card was activated before -- you used to could send them out unactivated, but I -- I don't -- so if these were activated, then, yes, it's clearly a violation of Truth in Lending.

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<sup>3046</sup> MSD-266 (Russ Anderson Dep. Tr.) at 122:22-124:19.

<sup>3047</sup> MSD-265 (Farrell Dep. Tr.) at 63:5-66:1.



Q. Does opening an unauthorized credit card account also violate Reg Z?

A. Yes. It would be the same.

Q. Does opening an unauthorized credit card account violate FCRA?

A. That completely would depend upon whether it is reported to the credit bureaus. I have no idea if they did in this case.

Q. Okay. And if they were reported to the credit card bureaus, would there be a violation of the FCRA if there was an unauthorized credit card account opened?

A. I think so.

Q. Does opening an unauthorized deposit account violate the Truth in Savings Act?

A. I would have to look at it.

Q. Does opening an unauthorized deposit account violate Reg DD?

A. Again, I would have to -- to look at that for sure. Those are disclosure laws that are hard to remember. I'm sorry.

Q. Okay. It's all right. If -- if an unauthorized deposit account was opened and the required disclosures weren't made, would that violate Reg DD?

A. Yes, it would.

Q. Would that also violate the Truth in Savings Act?

A. Yes, it would.<sup>3048</sup>

346. As part of its Deferred Prosecution Agreement with the U.S. Department of Justice "to resolve the federal criminal investigation of violations of, among other statutes, Title 18, United States Code, Sections 1005 and 1028A, arising out of Wells Fargo's improper sales practices," the Bank admitted, accepted, and acknowledged as true that the "Community Bank's onerous sales goals and accompanying management pressure led thousands of its employees to engage in: (1) unlawful conduct to attain sales through fraud, identity theft, and the falsification of bank records." Wells Fargo agreed that "the acts and omissions described in the Statement of Facts" attached to the Deferred Prosecution Agreement "are sufficient to establish violations by Wells Fargo of Title 18, United States Code, Sections 1005 and 1028A."<sup>3049</sup>

347. Under the Bank's June 2010 Corporate Security Policy Manual, sales integrity violations, including but not limited to customer consent and funding manipulation cases, were considered to result in violations of 18 U.S.C. §§ 656 (misapplication), 1001 (false statements), and 1005 (false bank entries).<sup>3050</sup>

348. Authoritative sources within the Bank testified about the illegal nature of sales

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<sup>3048</sup> MSD-265 (Farrell Dep. Tr.) at 63:5-66:1.

<sup>3049</sup> MSD-1 (DOJ SOF) at 7, 10, 25.

<sup>3050</sup> MSD-423 at 7-9.

practices misconduct.<sup>3051</sup> For example, James Strother, the Bank's former General Counsel, testified before the OCC that sales practices misconduct violated applicable laws and regulations and that "for sure it is [an] unfair and deceptive practice. There are laws in every state that prohibit that" in addition to federal laws. He agreed under oath that such practices constitute "fraud" and "falsification of bank records" and might constitute identity theft in some states.<sup>3052</sup>

349. Ms. Herzberg, who formerly worked as an examiner for the Office of Thrift Supervision ("OTS") and was a "safety and soundness regulator" and did work in compliance before working at the Bank, gave the following testimony under oath before the OCC:

Q: ...As I understand your testimony, now you believe that sales practice misconduct at the bank was systemic. Is that correct?

A: Yes. Now I believe that.

Q: All right. And you believe the sales practice misconduct at the bank that was systemic also constituted unsafe and unsound banking practices. Is that --

A: Yes.

Q: Okay. And you also believe that the sales practices misconduct at the bank that was systemic also constituted violations of applicable laws and regulations.

A: That's right.

Q: All right. And that includes violations of -- and that includes unsafe and unsound practices, as well as unfair and deceptive practices.

A: Yes.<sup>3053</sup>

Ms. Herzberg also testified as follows:

Q. Regardless of the motivation, the behavior of inputting fake email addresses essentially constitutes falsification of bank records.

A. Yes. Regardless of why they did it. Yes.

Q. Are you familiar with Reg DD?

A. Yes.

Q. Would the behavior also violate Reg DD?

A. Yes. They didn't receive their deposit account disclosures.

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<sup>3051</sup> MSD-544 (Weber Tr.) at 82:13-22, 91:22-93:21; MSD-297 (Richards Tr.) at 84:5-11.

<sup>3052</sup> MSD-288A (Strother Tr.) at 26:19-28:13, 142:25-143:10, 192:23-193:24 (testifying that issuing products and services to customers without their consent "is serious and violates law."); James Strother Amended Answer ¶¶ 141 ("Admitted that sales practices misconduct involved serious misconduct that likely included violations of criminal laws"); MSD-382 (Byers Tr.) at 135:6- 136:5; MSD-297 (Richards Tr.) at 82:4-84:11, 105:4-9 (explaining why simulated funding is improper and that it is a form of fraud), 200:4-201:2, 251:8-15; MSD-599 (Meuers Tr.) at 11:3- 11; MSD-549 (Holliday Tr.) at 69:14-70:9; MSD-149.

<sup>3053</sup> MSD-585 (Herzberg Tr.) at 17:18-19:5, 220:21-222:4, 26:9-27:20, 30:15-32:8.

Yes.<sup>3054</sup>

350. In the Bank's September 2016, CFPB Sales Practices Consent Order, the CFPB concluded that the Bank, by engaging in sales practices misconduct, "engaged in 'unfair' and 'abusive' acts or practices that violate §§ 1031(c)(1), (d)(1), (d)(2)(B), and 1036(a)(1)(B) of the [Consumer Financial Protection Act]. 12 U.S.C. §§ 5531(c)(1), (d)(1), (d)(2)(B), 5536(a)(1)(B)" (UDAAP).<sup>3055</sup>

351. OCC examiners have concluded that sales practices misconduct violates multiple consumer and criminal laws and regulations, including: 18 U.S.C. §§ 656 (theft/misapplication by bank employee), 1005 (false entries), 1028(a)(7) (identity theft), and 1344(2) (bank fraud); 15 U.S.C. § 45(a) (unfair or deceptive acts and practices); 12 C.F.R. § 1030.4(a) (Regulation DD/Truth in Savings); and 12 C.F.R. § 1026.12(a) (Regulation Z/Truth in Lending).<sup>3056</sup>

352. In its Deferred Prosecution Agreement with the U.S. Department of Justice, the Bank further admitted, accepted, and acknowledged as true the following:

- (a) "Employees created false records and forged customers' signatures on account opening documents to open accounts that were not authorized by customers."<sup>3057</sup>
- (b) "After opening debit cards using customers' personal information without consent, employees falsely created a personal identification number ('PIN') to activate the unauthorized debit card. Employees often did so because the Community Bank rewarded them for opening online banking profiles, which required a debit card PIN to be activated."<sup>3058</sup>
- (c) "Employees created false records by opening unauthorized checking and savings accounts to hit sales goals."<sup>3059</sup>
- (d) "Unlawfully misused customers' sensitive personal information (including customers' means of identification)."<sup>3060</sup>

353. Bank policies did not permit employees to open accounts or issue products not

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<sup>3054</sup> MSD-257 (Herzberg Tr.) at 166:18-167:4; 221:14-23.

<sup>3055</sup> MSD-52 (CFPB Consent Order) (citing violations of UDAAP against the Bank for sales practices misconduct).

<sup>3056</sup> MSD-257 (NBE Coleman Expert Report) at 6; MSD-267 (NBE Smith Expert Report) at 7; MSD-268 (NBE Crosthwaite Expert Report) at 7; MSD-269 (NBE Candy Expert Report) at 8.

<sup>3057</sup> MSD-1 at 25.

<sup>3058</sup> *Id.*

<sup>3059</sup> *Id.* at 26.

<sup>3060</sup> *Id.* at 31.

- authorized by a customer or to engage in simulated funding.<sup>3061</sup> Bank employees who confessed to opening unauthorized accounts or engaging in simulated funding admitted they knew it was against Bank policy and ethics guidelines.<sup>3062</sup>
354. To open or issue an unauthorized account, product, or service for a customer, Bank employees generally would have had to enter false information into the Bank's systems.<sup>3063</sup> Bank employees used the Bank's Store Vision Platform ("SVP") "to open accounts for new and existing Bank customers, and the provision to customers of new accounts kits, including electronic new account kits ('eNAK')." <sup>3064</sup>
355. "When opening or issuing an account, product or service for a customer, SVP required Bank employees to indicate in the system whether the customer was present in the branch. If an employee issued a product or service to a customer without customer consent, the employee would have had to indicate that the customer was present when in fact the customer was not present to avoid" appearing on a "report reflecting products and services issued to a customer when the customer was not present." <sup>3065</sup>
356. "When opening a savings or checking account or issuing a debit card to a customer, SVP required Bank employees to enter into the system, as applicable, information related to the nature of the Bank employee's interaction with the customer, the customer request method, the source of funds for the opening deposit, the purpose of the account, the estimated monthly account activity, and whether the customer was present. In situations where employees opened a checking or savings account or issued a debit card for a customer without customer consent, Bank employees would have had to fabricate (or use without consent) some or all of this information in order to open the account or issue the card." <sup>3066</sup>
357. "When opening a savings, checking, or credit card account for a customer, the Bank requires its employees to provide the customer with certain account opening disclosures, either in paper form or electronically via eNAK. SVP required Bank employees to indicate in the system that the required disclosures were provided to the customer; otherwise, SVP would not allow the employee to continue with the account opening process. In situations where Bank employees opened a savings, checking, or credit card account for a customer

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<sup>3061</sup> MSD-9 at 7; MSD-10.

<sup>3062</sup> See, e.g., MSD-108 (concluding that employees engaged in simulated funding to meet sales goals despite knowing it was against Bank policy).

<sup>3063</sup> See MSD-200 (Hughes Decl.).

<sup>3064</sup> *Id.* at 1.

<sup>3065</sup> *Id.* at 1-2.

<sup>3066</sup> *Id.* at 2.

without customer consent, Bank employees would have had to indicate in SVP that the required disclosures were provided to the customer when, in fact, they were not.”<sup>3067</sup>

358. “When opening a credit card account for a customer, SVP required Bank employees to enter into the system the customer’s current income information. In situations where employees opened a credit card account for a customer without customer consent, Bank employees would have had to fabricate (or use without consent) this information.”<sup>3068</sup>

359. “When opening or issuing an account, product or service for a customer, SVP required Bank employees to enter into the system the customer’s identification information, such as a driver’s license number. In situations where employees issued a product or service to an existing customer without customer consent, Bank employees could have populated customer identification information with information previously supplied by the customer.”<sup>3069</sup>

360. In October 2016, the Bank finally eliminated sales goals for Community Bank employees.<sup>3070</sup>

361. In a January 23, 2020 Wells Fargo press release about the OCC’s Notice of Charges, the Bank’s current CEO stated, “The OCC’s actions are consistent with my belief that we should hold ourselves and individuals accountable. They also are consistent with our belief that significant parts of the operating model of our Community Bank were flawed. At the time of the sales practices issues, the Company did not have in place the appropriate people, structure, processes, controls, or culture to prevent the inappropriate conduct. This was inexcusable. Our customers and you all deserved more from the leadership of this Company.”<sup>3071</sup>

362. Sales practices misconduct at the Bank breached its customers’ trust, including but not limited to by opening accounts for customers without customer consent, transferring customer funds without customer consent, and misusing its customers’ personal information to do so.<sup>3072</sup>

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<sup>3067</sup> *Id.* at 4.

<sup>3068</sup> *Id.* at 5.

<sup>3069</sup> *Id.* at 6.

<sup>3070</sup> Russ Anderson Amended Answer ¶ 135; MSD-295 (Bacon Tr.) at 194:10-197:8 (testifying that “it took an act of Congress for the company to change.”; MSD-289A (Sloan Tr.) at 251:2-253:6; MSD-288-B (Strother Tr.) at 49:22-50:10; MSD-8B (Stumpf Tr.) at 228:11- 229:16; MSD-563; (Julian Amended Answer ¶ 135; McLinko Amended Answer ¶ 135. The Head of the Community Bank’s Sales and Service Conduct Oversight Team (“SSCOT”) testified that the Bank’s “elimination of sales goals [in early October 2016] help[ed] dramatically reduce the sales practices problem,” a conclusion she testified was supported by SSCOT’s own data. (MSD-300 (Rawson Tr.) at 66:3- 66:8).

<sup>3071</sup> MSD-662.

<sup>3072</sup> MSD-8A (Stumpf Tr.) at 127:9-14; MSD-567; MSD-568; MSD-569.

363. Sales practices misconduct at the Bank resulted in financial harm to the Bank’s customers, including but not limited to account fees paid by the customer and increased borrowing costs borne by the customer due to a credit score impact.<sup>3073</sup>
364. The Bank has acknowledged that its sales practices misconduct problem resulted in a breach of its customers’ trust and financially harmed its customers. In an August 31, 2017 Wells Fargo press release related to the remediation process, former Bank CEO Tim Sloan said:
- We apologize to everyone who was harmed by unacceptable sales practices that occurred in our retail bank. To rebuild trust and to build a better Wells Fargo, our first priority is to make things right for our customers, and the completion of this expanded third-party analysis is an important milestone. Through this expanded review, as well as the class action settlement, free mediation services, and ongoing outreach and complaint resolution, we’ve cast a wide net to reach customers and address their remaining concerns. Our commitment has never been stronger to build a better bank for our customers, team members, shareholders and communities.<sup>3074</sup>
365. As part of its February 20, 2020 Deferred Prosecution Agreement with the DOJ, the Bank also admitted as true that, as a result of its sales practices misconduct problem from 2002 through 2016, the Bank “collected millions of dollars in fees and interest to which the Company was not entitled, harmed the credit ratings of certain customers, and unlawfully misused customers’ sensitive personal information (including customers’ means of identification).”<sup>3075</sup>
366. The Bank has paid millions of dollars of remediation to its customers to compensate them for harm resulting from its sales practices.<sup>3076</sup>
367. On June 14, 2018, the U.S. District Court for the Northern District of California approved a \$142 million class action settlement in *Jabbari v. Wells Fargo & Co*, No. 15-cv- 02159-VC.<sup>3077</sup>
368. The *Jabbari* settlement class included “All Persons for whom Wells Fargo or Wells Fargo’s current or former subsidiaries, affiliates, principals, officers, directors, or employees opened an Unauthorized Account or submitted an Unauthorized Application, or who obtained Identity Theft Protection Services

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<sup>3073</sup> MSD-543; MSD-663.

<sup>3074</sup> MSD- 664.

<sup>3075</sup> MSD-1 at 31 ¶ 32.

<sup>3076</sup> MSD-542; Julian Amended Answer ¶ 26; MSD-665.

<sup>3077</sup> MSD-665; see also Julian Amended Answer ¶ 173.

- from Wells Fargo during the period from May 1, 2002 to April 20, 2017.”<sup>3078</sup>
369. In a June 15, 2018 Wells Fargo press release about the *Jabbari* settlement, former Bank CEO Tim Sloan stated: “The court’s approval of the broad and far-reaching \$142 million settlement agreement is a significant step forward in making things right for our customers and further restoring trust with all of Wells Fargo’s stakeholders. . . . We are pleased with this decision as it supports our efforts to help customers impacted by improper retail sales practices and ensures they have every opportunity for remediation.”<sup>3079</sup>
370. Under the *Jabbari* settlement, “Claimants will be reimbursed from the Net Settlement Amount for out-of-pocket losses stemming from Unauthorized Accounts and Unauthorized Applications. Such out-of-pocket losses shall consist of two components: (1) increased borrowing cost due to credit score impact as a result of a Credit Analysis Account (‘Credit Impact Damages’); and (2) fees assessed by Wells Fargo in connection with certain Unauthorized Accounts.”<sup>3080</sup>
371. On September 8, 2016, the Bank was fined \$185 million by the OCC, the Consumer Financial Protection Bureau, and the Office of the Los Angeles City Attorney in connection with its sales practices.<sup>3081</sup>
372. On February 2, 2018, the Board of Governors of the Federal Reserve imposed on Wells Fargo an “asset cap” limiting the Bank’s ability to increase in asset size because it “pursued a business strategy that emphasized sales and growth without ensuring that senior management had established and maintained an adequate risk management framework commensurate with the size and complexity of the Firm, which resulted in weak compliance practices.”<sup>3082</sup>
373. The “asset cap” has had a significant adverse financial impact on the Bank.<sup>3083</sup>
374. On October 22, 2018, Wells Fargo was fined \$65 million by the Office of the Attorney General of the State of New York in connection with its sales practices.<sup>3084</sup>
375. On December 28, 2018, the Bank was fined \$575 million by all 50 state Attorneys General and the District of Columbia in connection with its sales

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<sup>3078</sup> MSD-665.

<sup>3079</sup> MSD-666.

<sup>3080</sup> MSD-664.

<sup>3081</sup> MSD-667; MSD-52; MSD-343; MSD-344.

<sup>3082</sup> MSD-668; MSD-679.

<sup>3083</sup> MSD-267 (NBE Smith Expert Report) at ¶ 148(e); MSD-669 (noting the Bank “has missed out on roughly \$4 billion in profits -- and counting -- since the cap was imposed”).

<sup>3084</sup> MSD-670; MSD-673; MSD-678.

- practices and related matters.<sup>3085</sup>
376. By July 11, 2019, when former Bank CEO Tim Sloan testified before the OCC, he estimated the total financial impact of the sales practices scandal on the Bank to be already “in the tens of billions of dollars, when you add -- the most significant impact was one that we were referring to earlier, and that was the impact of the stock price. We really missed out on recovery.”<sup>3086</sup>
377. The Company’s stock price has significantly lagged its peers since September 8, 2016, the date of the sales practices settlements with the OCC, CFPB, and City Attorney of Los Angeles.<sup>3087</sup>
378. The Bank has also expended significant sums of money on lawyers and consultants in connection with its sales practices. From the fourth quarter of 2016 through the first quarter of 2018, the Bank paid legal fees and consulting costs of at least \$169 million related to its sales practices.<sup>3088</sup>
379. The Bank’s 10-Q dated August 2, 2019 includes the following statement: “[T]he Company establishes accruals for legal actions when potential losses associated with the actions become probable and the costs can be reasonably estimated. The high end of the range of reasonably possible potential losses in excess of the Company’s accrual for probable and estimable losses was approximately \$3.9 billion as of June 30, 2019.”<sup>3089</sup>
380. On February 20, 2020, the Bank was fined \$3 billion by the U.S. Department of Justice and U.S. Securities and Exchange Commission in connection with its sales practices.<sup>3090</sup>
381. In a February 21, 2020 Wells Fargo press release related to their \$3 billion Deferred Prosecution Agreement with the DOJ and SEC, the Bank’s CEO said: “The conduct at the core of today’s settlements — and the past culture that gave rise to it — are reprehensible and wholly inconsistent with the values on which Wells Fargo was built. Our customers, shareholders and employees deserved more from the leadership of this Company.”<sup>3091</sup>
382. Wells Fargo’s reputation was significantly impacted as a result of the sales

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<sup>3085</sup> MSD-671; MSD-672.

<sup>3086</sup> MSD-289A (Sloan Tr.) at 260:8-16.

<sup>3087</sup> MSD-658 (Pocock Expert Report) at 5, 13-14; MSD-267 (NBE Smith Expert Report) at 148(f); MSD-289A (Sloan Tr.) at 256:25-257:8; see also MSD-257 (NBE Coleman Expert Report) at ¶ 115.

<sup>3088</sup> MSD-564 (Champion Decl.); MSD-267 (NBE Smith Expert Report) at ¶ 148; MSD-289A (Sloan Tr.) at 255:10-18.

<sup>3089</sup> Julian Amended Answer ¶ 184; McLinko Amended Answer ¶ 184.

<sup>3090</sup> MSD-1 at 1-4; MSD-674.

<sup>3091</sup> MSD-674.



- practices misconduct problem.<sup>3092</sup>
383. According to the Bank’s own research, the Bank’s favorability and trustworthiness scores declined significantly between September and October 2016. As of May 2017, Wells Fargo’s favorability and trustworthiness scores remained “near the bottom.”<sup>3093</sup>
384. In 2017, the Bank fell to last place in a bank reputation survey conducted by the *American Banker*/Reputation Institute. According to the *American Banker*, the Bank’s reputation score “went into free fall . . . [and was] by far the lowest of any bank.” It added, “Wells Fargo’s image is in tatters — and will likely remain so for some time.” Wells Fargo’s declining reputation score was attributed to the sales practices scandal.<sup>3094</sup>
385. In an August 4, 2017 news release, former Wells Fargo CEO Tim Sloan acknowledged the reputational damage resulting from the Bank’s sales practices: “Rebuilding trust became our top priority when I became CEO last October. That’s when we began our recovery from the reputation damage we sustained from unacceptable retail sales practices in the Community Bank.”<sup>3095</sup>
386. In explaining how the Bank’s sales practices misconduct problem “so clearly harmed [the Bank’s] reputation,” former Wells Fargo CEO Tim Sloan testified before the OCC: “Well, prior to [the sales practices scandal], Wells Fargo had a very stellar reputation in terms of serving our customers, serving all of our stakeholders. And because of the mistakes that we made related to sales practices, we saw significant criticism on the part of a number of those stakeholders.”<sup>3096</sup>
387. On May 7, 2018, the Bank launched its “Re-Established” marketing campaign “to emphasize the company’s commitment to re-establish trust with stakeholders and to demonstrate how Wells Fargo is transforming as it emerges from a challenging period in its history.”<sup>3097</sup>
388. The “Re-Established” marketing campaign cost the Bank hundreds of millions of dollars.<sup>3098</sup>
389. The sales practices misconduct problem also negatively affected the Bank’s ability to attract new customers. The current Head of the Community Bank Mary Mack testified on October 26, 2018 that the scandal hampered the ability of the

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<sup>3092</sup> MSD-267 (NBE Smith Expert Report) at ¶ 149; MSD-257 (NBE Coleman Expert Report) at ¶¶ 114, 117; MSD-289A (Sloan Tr.) at 43:15-23; MSD-565; MSD-675.

<sup>3093</sup> MSD- 565.

<sup>3094</sup> MSD-675; Julian Amended Answer ¶ 175.

<sup>3095</sup> MSD-676.

<sup>3096</sup> MSD-289A (Sloan Tr.) at 43:15-23.

<sup>3097</sup> MSD- 677; Julian Amended Answer ¶ 178; McLinko Amended Answer ¶ 178.

<sup>3098</sup> MSD-293A (Hardison Tr.) at 36:14-38:18; MSD-289A (Sloan Tr.) at 254:3-15.

Community Bank to attract customers.<sup>3099</sup> Similarly, former Wells Fargo CEO Tim Sloan testified before the OCC on July 11, 2019 that, as a result of the sales practices scandal, “on the retail side of the bank we clearly haven’t grown as many new customers.”<sup>3100</sup>

#### **4. Cease and Desist**

If, in the opinion of the Office of the Comptroller of the Currency, Mr. McLinko engaged in an unsafe or unsound practice in conducting the business of the Bank, upon sufficient notice and after a hearing the Comptroller may pursuant to 12 U.S.C. § 1818(b)(1) issue and serve upon him an order to cease and desist from any such practice. Proof of misconduct alone entitles the banking regulator to invoke its broad cease and desist enforcement powers.<sup>3101</sup>

Action, or lack of action, is unsafe or unsound if it is contrary to generally accepted standards of prudent operation, the possible consequences of which, if continued, would be abnormal risk or loss or damage to an institution, its shareholders, or the agencies administering the insurance funds.<sup>3102</sup> The objectives of a cease and desist order are twofold: to correct existing conditions and to prevent the recurrence of unsafe or unsound practices and violations of law in the future. An order to cease and desist from abandoned practices is in the nature of a safeguard for the future.<sup>3103</sup>

Preponderant credible evidence presented through the hearing in this matter and as noted above established that Mr. McLinko engaged in conduct that was contrary to generally accepted standards of prudent operation, the possible consequences of which, if continued, would be abnormal risk or loss or damage to an the Bank, its holding company and the holding company’s shareholders, or the agencies administering the insurance funds.

Upon such findings, cause has been shown to recommend the issuance of a cease and desist order against Mr. McLinko as shown in Enforcement Counsel’s Proposed Cease and Desist Order that accompanied their Post-Hearing Brief and Proposed Findings of Fact and Conclusions of Law at Appendix A.

#### **5. Civil Money Penalty**

Through the Notice of Charges, the Comptroller proposed to assess Tier 2 civil money penalties against Mr. McLinko. Tier 1 penalties are available upon sufficient evidence

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<sup>3099</sup> MSD-472 (Mack Tr.) at 241:16-242:1.

<sup>3100</sup> MSD-289A (Sloan Tr.) at 257:18-23.

<sup>3101</sup> *Greene Cnty. Bank v. F.D.I.C.*, 92 F.3d 633, 636 (8th Cir. 1996), quoting *Oberstar v. FDIC*, 987 F.2d 494, 502 (8th Cir.1993).

<sup>3102</sup> 12 U.S.C. § 1818(b)(1).

<sup>3103</sup> *In re \*\*\**, Nos. FDIC-83-252b&c, FDIC-84-49b, FDIC-84-50e, 1985 WL 303871, at \*104 (Aug. 19, 1985); see also *In re \*\*\**, No. OCC-AA-EC-87-106, 1988 WL 427542, at \*29 (Nov. 14, 1988) (final decision) (“[T]he legislative history of section 1818 makes it clear that Congress intended cease and desist orders to prevent future unsafe or unsound practices or violations as well as to correct current problems.”).

establishing that a Respondent violated any law or regulation. Tier 2 penalties are available upon sufficient evidence establishing that the Respondent violated laws or recklessly engaged in unsafe or unsound practices in conducting the Bank's business, or breached any fiduciary duty owed to the Bank, if the violation of law, unsafe practice, or breach of duty was part of a pattern of misconduct, or caused or was likely to cause more than a minimal loss to the Bank, or resulted in pecuniary gain or other benefit to the Respondent.

In this context, conduct is reckless if it is done in disregard of, and evidences a conscious indifference to, a known or obvious risk of a substantial harm. If a Respondent was aware of a risk of substantial harm but did not act to appropriately address or mitigate that risk, or took only perfunctory steps, that conduct is reckless.

Preponderant evidence presented during the hearing and as noted above established that Mr. McLinko continuously, repeatedly, and recklessly engaged in unsafe or unsound practices. The evidence further established that Mr. McLinko breached fiduciary duties that he owed to the Bank, under conditions that constituted a pattern of misconduct, where those conditions were likely to cause and did in fact cause more than a minimal loss to the Bank, while also resulting in pecuniary gain and other benefits to Mr. McLinko, including his continued employment throughout the period where he engaged in unsafe or unsound practices and breached fiduciary duties he owed to the Bank.

Upon such evidence cause has been shown establishing a basis to impose either a Tier 2 civil money penalty upon Mr. McLinko.

For conduct occurring between November 10, 2008 and November 1, 2015, the maximum per day Tier 2 penalty was \$37,500 for each day that the misconduct continued. That penalty was \$51,222 per day from November 2, 2015 to September 30, 2016, and beyond. Given the continuing nature of Mr. McLinko's unsafe and unsound practices, and his breaches of fiduciary duties, cause has been shown supporting a penalty based on conduct that began on January 1, 2013 and continued unabated until September 30, 2016

### **Assessment of Civil Money Penalties**

The OCC considers a number of statutory and interagency factors in determining the amount of a civil money penalty to assess to an individual. These include: (1) the size of the financial resources and good faith of the person; (2) the gravity of the violation; (3) the history of previous violations; (4) such other matters as justice may require; (5) evidence that the violations were intentional or committed with disregard of the law or consequences to the institution; (6) the duration and frequency of the misconduct; (7) the continuation of the misconduct after the respondent was notified or, alternatively, its immediate cessation and correction; (8) the failure to cooperate with the agency in effecting early resolution of the problem; (9) concealment of the misconduct; (10) any threat of loss, actual loss, or other harm to the institution, including harm to the public confidence in the institution, and the degree of such harm; (11) the respondent's financial gain or other benefit from the misconduct; (12) any restitution paid by the respondent for the losses; (13) any history of previous misconduct, particularly where similar to the actions under consideration; (14) previous criticism of the institution or individual for similar actions;

(15) presence or absence of a compliance program and its effectiveness; (16) tendency to engage in violations of law, unsafe or unsound practices or breaches; and (17) the existence of agreements, commitments, orders or conditions imposed in writing intended to prevent violations.

Evidence adduced during the hearing established the following:

(1) *the size of the financial resources and good faith of the person*: The record reflects the absence of good faith on Mr. McLinko's part, where in his underlying conduct prior to the issuance of the Notice of Charges he persistently failed to provide timely material information to the Bank's A&E Committee, its Board of Directors, and the OCC examiners, factors warranting a high penalty.

(2) *the gravity of the violation*: the record reflects the risks of financial loss and harm to the Bank's reputation were aggravating conditions warranting a high penalty.

(3) *the history of previous violations*: there is nothing in the record establishing a history of violations by Mr. McLinko preceding the misconduct alleged in the Notice of Charges.

(4) *such other matters as justice may require*: Mr. McLinko asserted the increased penalty is also contrary to the statutory scheme. In support, he cited the provision in 12 U.S.C. § 1818(i)(2)(E)(i), (G) that requires the OCC to consider statutory mitigation factors prior to assessing the CMP and to provide written notice of such assessment. The record reflects, however, that both Examiner Candy and Deputy Comptroller did consider the statutory mitigation factors prior to assessing the CMP presented in the Notice of Charges. The cited statute does not speak to those instances where through the evidentiary hearing process evidence demonstrates cause for a penalty that is either higher or lower than the penalty presented through the Notice of Charges.

Evidence adduced during the hearing included Mr. McLinko's unfounded assertion that his employment during the relevant period did not fall within the definition of an institution-affiliated party; that he was not throughout the relevant period aware of the root cause of sales practices misconduct by Community Bank team members; and that he did not intentionally and knowingly withhold material information to the OCC and the Board of Directors.

This evidence was not available at the time the Notice of Charges was issued. Having been present and attentive to Mr. McLinko's testimony, I find ample cause has been shown for the \$1.5 million penalty sought by Enforcement Counsel.

(5) *evidence that the violations were intentional or committed with disregard of the law or consequences to the institution*: The record establishes Mr. McLinko's refusal to act in the Bank's interest and his failure to escalate known issues regarding the ineffective risk management controls that were in place in the Community Bank were intentional acts taken in utter disregard to the myriad adverse consequences to the Bank.

(6) *the duration and frequency of the misconduct*: The record establishes a chronic lack of effective audit services by Mr. McLinko throughout a period that began no later than January 2013 and ended only during late 2016.

(7) *the continuation of the misconduct after the respondent was notified or, alternatively, its immediate cessation and correction:* The record reflects Mr. McLinko's failure to provide effective Executive Audit Director services persisted after he received repeated notifications of risk-management control failures and elected to take no effective action to mitigate those control failures.

(8) *the failure to cooperate with the agency in effecting early resolution of the problem:* The record reflects that Mr. McLinko's interactions with the OCC examiners exacerbated the adverse implications of the Community Bank's risk management control failure, through his failure to exercise credible challenge to the Community Bank's first line of defense and failure to properly supervise the WFAS CBO audit team responsible for identifying such failure.

(9) *concealment of the misconduct:* The record reflects Mr. McLinko persistently provided to the Board and to the OCC little or no notice of the ineffectiveness of Community Bank's risk management controls, notwithstanding his position on committees where the mission of those committees mandated disclosure and not concealment of known issues.

(10) *any threat of loss, actual loss, or other harm to the institution, including harm to the public confidence in the institution, and the degree of such harm:* The record reflects significant material losses sustained by the Bank, both financial and reputational losses, that threatened public confidence in the Bank to a significant degree, losses that were directly related to ineffective controls by the Community Bank's first line of defense and were mitigated only when external auditors were employed to quantify the true scope of that harm.

(11) *the respondent's financial gain or other benefit from the misconduct:* The record reflects that Mr. McLinko was able realize financial gain throughout the relevant period because he was permitted to keep his job while not performing the duties of that job, and to profit from the Bank's increased income and value where that value was increased only due to the pervasive sales practices culture that exposed the Bank to financial loss in the long run. Until those risks were exposed, Mr. McLinko was highly compensated as the Executive Audit Director of the Community Bank, allowing him to benefit from his misconduct.

(12) *any restitution paid by the respondent for the losses.* Nothing in the record suggests Mr. McLinko or anyone else has paid restitution for the Bank's losses.

(13) *any history of previous misconduct, particularly where similar to the actions under consideration:* Apart from the significant course of time over which ineffective risk management controls permitted pervasive sales practices misconduct by team members in the Community Bank, the record is silent regarding similar misconduct by Mr. McLinko in any of his previous postings.

(14) *previous criticism of the institution or individual for similar actions:* There is no record of previous criticism of either the Bank or Mr. McLinko apart from the misconduct alleged in the Notice of Charges.

(15) *presence or absence of a compliance program and its effectiveness:* Although there is evidence in the record of the Bank's development of compliance programs after the issuance of five MRAs, one of which directly addressed Audit, the record does not establish effective

compliance programs regarding risk management control failures at the Community Bank during the relevant period, until sales goals were eliminated in 2016.

(16) *tendency to engage in violations of law, unsafe or unsound practices or breaches*: The record reflects Mr. McLinko had a tendency to deny responsibility for audit functions that were clearly his to fulfill, including responsibilities arising out of his membership on critical risk-management committees and the duty to be familiar with materials being presented to him by his audit team and other risk managers at the Bank.

(17) *the existence of agreements, commitments, orders or conditions imposed in writing intended to prevent violations*: The record includes written directives issued by the OCC that were intended to prevent violations, where responses from Mr. McLinko and WFAS could have but did not effectively address those matters requiring attention.

Upon a sufficient showing that each of these factors were considered by the OCC when arriving at such assessments,<sup>3104</sup> and upon a separate review of the evidence presented during the hearing relating to each of these factors, sufficient cause has been shown to recommend the issuance of orders assessing a \$1.5 million civil money penalties against Mr. McLinko.

## **7. Key Factual Findings**

1. Beginning in not later than January 2013, Mr. McLinko had actual notice that controls put in place by Community Bank's first line of defense were not effective against risks related to sales practices misconduct by Community Bank's team members.
2. Between January 2013 and mid-2016, the number of Bank products per household was the key metric through which the Bank benefitted through increased revenue and customer retention. The metric was critical to the Bank's reputation because it was disclosed in SEC filings and was closely watched by investors and analysts.
3. In February 2015 the OCC notified WFAS and Mr. McLinko that between January 2013 and February 2015 oversight of the Community Bank's cross-sell activities lacked transparency and needed to be formalized in a governing framework that describes roles and responsibilities, lines of reporting, escalation protocols, incentive compensation oversight, and quality assurance processes. Further, the OCC noted that the lack of a comprehensive governance framework could expose the Community Bank to heightened reputation risk through negative publicity, and that without a more formal structure it would be difficult to ensure compliance with the Bank's values and goals for achieving customer satisfaction and strategic and financial objectives.
4. Between January 2013 and mid-2016, sales practices violations were widespread and driven by a systemic disconnect between incentives available to team members and team members' ethical and legal obligations.

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<sup>3104</sup> See OCC Ex. 2377 (Declaration of OCC Acting Examiner-in-Charge Tanya K. Smith, March 23, 2021).

5. Between January 2013 and mid-2016, Mr. McLinko failed to identify control deficiencies in Community Bank's incentive compensation programs and the relationship between those programs and sales practices misconduct by Community Bank's team members.
6. Between January 2013 and mid-2016, Mr. McLinko failed to provide credible challenge to the Community Bank's leadership (including Carrie Tolstedt and Ms. Russ Anderson) regarding the Community Bank's risk culture.
7. Between January 2013 and mid-2016, Mr. McLinko failed to take effective measures to determine the root cause of sales practices misconduct by Community Bank's team members.
8. Between January 2013 and mid-2016, Mr. McLinko failed to effectively escalate risk issues related to sales practices misconduct by Community Bank team members and controls over such misconduct.
9. Between late 2013 (with the publication of two L.A. Times articles regarding sales practices pressure and related misconduct by team members of the Community Bank) and mid-2016, Mr. McLinko failed to take meaningful action to escalate known issues regarding controls over sales risk management and sales risk culture in the Community Bank.
10. By late 2013, sales practices misconduct by Community Bank team members was widespread in scope and nature, and persisted as a material risk to the safety and soundness of the Bank throughout 2014 to 2016. Between 2013 and mid-2016, Mr. McLinko persistently and knowingly failed to address known risk-management control failures in the Community Bank, exposing the Bank to financial, reputational, and regulatory risk that exceeded the Bank's risk appetite.
11. Through the independent analysis by PwC commissioned by the Bank in 2015 and completed in 2017, the Bank learned that at least 1.8 million potentially unauthorized accounts were opened between 2013 and 2016; and that simulated funding occurred across the Bank's nationwide branch network and was not limited to Los Angeles or Orange County, California.
12. In 2016, the Bank's Corporate Risk unit determined that as of November 2016, 40,600 team members had potentially engaged in simulated funding and that at the time of this determination there were 19,900 currently employed team members who had potentially engaged in such misconduct.
13. Between 2013 and mid-2016, the risks associated with sales practices misconduct by Community Bank team members exceeded and contravened the Bank's established risk appetite.
14. Throughout 2014 to 2016, Mr. McLinko was aware of the scope and nature of the risk, including regulatory and reputational risk, associated with sales practices misconduct by Community Bank team members, and knew of control failures within Community Bank's first line of defense related to that risk.
15. Throughout 2013 to mid-2016, Mr. McLinko failed to exercise credible challenge to known deficiencies in controls that had been put in place under the direction of Ms. Tolstedt and Ms. Russ Anderson that were supposed to detect and prevent

- sales practices misconduct by Community Bank team members.
16. Between late 2013 and 2016, Mr. McLinko concealed from members of the Bank's Audit & Examination Committee, its Enterprise Risk Management Committee, its Board of Directors, and the OCC examiners the extent of sales practices misconduct being committed by Community Bank team members and the inadequacy of controls related to such misconduct.
  17. Throughout 2013 to 2016, Mr. McLinko failed to take effective measures to identify the root cause of the risks associated with sales practices misconduct by Community Bank's team members.
  18. Throughout 2013 to 2016, Mr. McLinko failed to take sufficient measures to assure that effective preventative and detective controls tied to team member sales practices misconduct were in place at the Community Bank.
  19. Throughout 2013 to 2016, Mr. McLinko failed to effectively supervise WFAS and CBO staff members and failed to provide credible challenge regarding the management of risks associated with team member sales practices misconduct in the Community Bank. **This conduct constituted unsafe or unsound practice and violated fiduciary duties Mr. McLinko owed to the Bank.**
  20. Whether or not a customer realized a financial harm, at a minimum the Bank suffered a reputational injury when a customer learns that an account had been opened that the customer did not want or request.
  21. Although he was aware of reports of sales practices misconduct from across the bank branch system, Respondent McLinko took no steps in early 2013 to determine the true scope and reach of such misconduct, nor did he determine whether Community Bank's first line of defense had effective controls in place that would determine the root cause of such misconduct, nor did he take steps to determine whether the first line of defense had controls to assure the culture in the Community Bank adhered to the Bank's Vision and Values. **Failing to take such steps constituted unsafe or unsound banking practices and violated fiduciary duties Mr. McLinko owed to the Bank.**
  22. Notwithstanding the information supplied to him by Corporate Investigations throughout early 2013, and notwithstanding the absence of any assurance that the risk management controls at the Community Bank were effective with respect to the risks associated with sales practices misconduct, Respondent McLinko failed to provide credible challenge to Mr. Julian's report to the A&E Committee on February 26, 2013, that overall risk management was Generally Effective. **Failing to report the absence of any assurance that those controls were effective constituted unsafe or unsound banking practices and violated fiduciary duties Mr. McLinko owed to the Bank.**
  23. October 3, 2013, the L.A. Times published an article written by E. Scott Reckard under the headline, "WELLS FARGO FIRES WORKERS ACCUSED OF CHEATING ON SALES GOALS". The article reported that the Bank had fired 30 employees in the Los Angeles region for opening accounts that were never used and attempting to manipulate customer-satisfaction surveys. The article



further reported the pressure to meet sales goals was intense and that there were known cases of forged customer signatures and accounts opened without customer knowledge.

24. On December 21, 2013, the L.A. Times published a second article, also by Mr. Reckard, with the headline: “WELLS FARGO’S PRESSURE-COOKER SALES CULTURE COMES AT A COST”. The article stated it was based on interviews with 28 former and seven current employees across nine states. This article reported that employees were threatened with termination if they failed to meet their sales goals.
25. On May 4, 2015, the City Attorney of Los Angeles sued the Bank in connection with the Community Bank’s sales practices. The Complaint alleged the Wells Fargo & Company and Wells Fargo Bank, N.A. had for years victimized their customers by using pernicious and often illegal sales tactics to maintain high levels of sales of their banking and financial products. It alleged the banking business model employed by Wells Fargo was based on selling customers multiple banking products. It alleged that in order to achieve its goal of selling products and services to each customer, Wells Fargo imposed unrealistic sales quotas on its employees, and adopted policies that drove its bankers to engage in fraudulent behavior to meet those unreachable goals.
26. The lawsuit alleged that as a result, Wells Fargo’s employees engaged in unfair, unlawful, and fraudulent conduct, including opening customer accounts, and issuing credit cards, without authorization. It alleged that on the rare occasions when Wells Fargo did take action against its employees for unethical sales conduct, Wells Fargo further victimized its customers by failing to inform them of the breaches, refund fees they were owed, or otherwise remedy the injuries that Wells Fargo and its bankers have caused. It alleged that Wells Fargo had engineered a virtual fee-generating machine, through which its customers were harmed, its employees took the blame, and Wells Fargo reaped the profits.
27. When OCC examiners completed their annual examination of WFAS in September 2015, they required WFAS to test the Community Bank’s first line of defense for compliance with high-risk laws and regulations, develop an audit strategy that regularly assesses the effectiveness of Regulatory Compliance Risk Management (RCRM) as the second line of defense, and report all WFAS-identified deficiencies to the Audit & Examination Committee, with a report to the Committee describing the severity of the deficiencies and the corrective actions associated with the deficiencies.
28. In October 2015, Respondent McLinko’s staff reported to him that in the staff’s opinion, management of the risks associated with the Community Bank’s sales conduct, practices, and the consumer business model needed improvement and presented a high risk of impact to the Bank – and the risk was getting higher. Through this opinion, the WFAS staff indicated the Bank was vulnerable to material or significant losses to current or anticipated earnings, capital, reputation, or regulatory violations. The opinion that this risk management needed

improvement meant that current risk management was not fully effective or did not balance risk and reward.

29. An independent sales practices assessment commissioned by the Board in mid-2015 and shared with Respondent McLinko resulted in an October 2015 report finding the Community Bank's first line of defense did not have a uniform way of evidencing sufficient control over sales practices issues; that many bankers felt pressure to meet sales targets that they perceive to be unreasonable and that this may occur at the potential expense of sales quality; that the Company's Vision and Values were not fully understood or incorporated by team members; that there was no consistent process or governance model to ensure all customer complaints were captured, monitored, addressed and reported across the Community Bank; that eligibility thresholds under the Community Bank's incentive compensation plan may have been misaligned with store traffic and customer demand; and that cases that should be reported through the Company's Ethics Line were not being documented or captured.
30. In September 2015, the Board commissioned an independent analysis of one form of sales practices misconduct – simulated funding – to determine the number of accounts that may have been subject to such activity and to report on the harm – primarily financial harm – related to such activity. The analysis, issued on December 18, 2015, identified two types of harm: primary financial harm, where customers paid account fees directly on the unauthorized account as well as indirectly through the Bank's set-off process; and secondary financial harm, which was defined as net overdraft fees paid by the customer on his or her authorized account from which the simulated funding occurred, or due to the Bank's set-off process.
31. In November 2016, the OCC completed an examination of the Bank's Talent Management and Incentive Compensation programs. Through this examination, the examiners found the Bank's incentive compensation program was weak and in need of improvement. Examiners found weaknesses in the design and execution of compensation and performance management practices, found that management lacked a holistic and cohesive testing, monitoring, and validation strategy that would ensure risks were identified and well controlled. It found that performance management and incentive compensation decisions did not adequately and consistently incorporate adverse risk outcomes or conduct issues. It found that other control functions, including risk, compliance, and audit, should have a more prominent role in incentive compensation design and risk management. It found that these weaknesses exposed the Bank to increased operational, compliance, regulatory, and reputational risks, and were considered unsafe or unsound banking practices.
32. Notwithstanding the fund of information available to him throughout 2013 to 2015, for four years starting in 2013 Respondent McLinko failed to identify control deficiencies in Community Bank's first line of defense, failed to assure that WFAS audit activity would detect and document the efficacy of controls over

ongoing sales practices misconduct issues in the Community Bank, failed to escalate to senior Bank management and the Board issues related to internal control deficiencies in Community Bank's first line of defense, failed to adequately supervise senior leaders of WFAS to assure resources were timely being directed to detect and remediate control deficiencies in the Community Bank, failed to effectively manage internal audit to ensure it added value to the Bank, failed to assure that adequate steps were taken to identify the root cause(s) of sales practices misconduct by Community Bank team members, and failed to assess risks related to customer consent, customer complaints, and incentive compensation between 2013 and 2016. **The failure to take such action constituted unsafe or unsound banking practices and constituted a breach of the fiduciary duties that Mr. McLinko owed to the Bank.**

33. Respondent McLinko's fiduciary duties arose not only because of his position as the WFAS EAD for the Community Bank, but also through the mandates of the committees he was a member of. As a member of these committees, Mr. McLinko had fiduciary responsibilities based on the mission of each committee. His presence on these committees gave him the opportunity and the duty to gather information concerning risk activities. With that information, he had the duty to establish the proper internal audit scope related to those activities. **The failure to gather such information and establish the proper internal audit scope related to those activities constituted unsafe or unsound banking practices and constituted a breach of the fiduciary duties Mr. McLinko owed to the Bank.**
34. As a member of these committees, Respondent McLinko had fiduciary duties that included addressing risk issues that were, or should have been, made known to committee members, escalating the issues where appropriate, and ensuring that the issues were promptly resolved. Notwithstanding the fiduciary duties associated with his membership in these committees, throughout 2013 to 2016 Mr. McLinko persistently failed to present to members of these committees material information regarding the mismanagement of sales practice risk controls by Community Bank's first line of defense. **The failure to present such information constituted unsafe or unsound banking practices and constituted a breach of the fiduciary duties Mr. McLinko owed to the Bank.**
35. Mr. McLinko's failure to take effective steps to identify and address sales practices misconduct in the Community Bank persisted over four years, and expressed itself as a pattern of misconduct, one that included willful neglect of the duty to familiarize himself with the scope and nature of sales practices misconduct by Community Bank's team members and extant controls related to such misconduct, willful failure to disclose through escalation information establishing the root cause of such misconduct, and willful failure to supervise senior audit leaders in WFAS to assure their compliance with regulatory and professional audit standards.
36. Mr. McLinko's failure to take effective steps to identify and address sales practices misconduct in the Community Bank was likely to cause and did cause

more than a minimal loss to the Bank. Those losses included the Bank's payment of civil penalties and criminal fines, and costs the Bank bore to rebuild trust with the holding company's shareholders, customers, the public, and regulators. Those losses and costs continue, as the Bank continues to remediate its present and past customers.

37. Through his failure to disclose the inadequacy of the Community Bank's risk management control processes, sales practice misconduct by Community Bank team members continued throughout 2013 to 2016. During this time, because the problem was unaddressed and hidden from the public and myriad stakeholders, Mr. McLinko was able to retain his employment and receive the benefits of being a highly regarded and compensated member of the Bank's senior officer staff.
38. Although the Community Bank's business model incited misconduct, it was profitable throughout the relevant period, which benefited Mr. McLinko during that same period. In addition to being able to retain his position as the WFAS EAD for the Community Bank, by allowing the misconduct to proliferate Mr. McLinko benefited from bonus payments and stock increases that were directly tied to the Bank's financial performance. As long as the true risks associated with such misconduct were withheld from the Bank's A&E Committee, its Enterprise Risk Management Committee, the Bank's Board of Directors, and the OCC (and other regulators), Mr. McLinko received the material financial and other benefits that came from such non-disclosure uninterrupted month to month from 2013 through 2016.

## **CONCLUSIONS OF LAW**

1. Preponderant evidence presented during the hearing established that Mr. McLinko is an institution-affiliated party, that the Bank is a financial institution as that term is used in the Federal Deposit Insurance Act, and that the OCC is the appropriate Federal regulator authorized to issue cease and desist orders under the FDI Act.
2. Preponderant evidence presented during the hearing established that Mr. McLinko has engaged in unsafe and unsound practices in conducting the business of the Bank, sufficient to warrant the issuance of a cease and desist order as proposed by Enforcement Counsel in their post-hearing brief.
3. Preponderant evidence presented during the hearing established that Mr. McLinko engaged in misconduct by engaging in unsafe or unsound practice, breached fiduciary duties he owed to the Bank; (2) the Bank has suffered and will probably continue to suffer financial loss or other damage by reason of Mr. McLinko's misconduct; that Mr. McLinko's misconduct could have prejudiced and did prejudice the Bank's depositors, and his misconduct resulted in financial gain or other benefit to him; and (3) his misconduct involved both his personal dishonesty and his willful or continuing disregard for the safety or soundness of the Bank.
4. After taking into account each of the statutory and regulatory factors relevant to the assessment of civil money penalties in this context, preponderant evidence

presented during the hearing established cause to assess a \$1.5 million civil money penalty against Mr. McLinko.

5. **Statute of Limitations**<sup>3105</sup>

Mr. McLinko asserted the five-year statute of limitations in 28 U.S.C. § 2462 applies to the civil money penalty action and the cease and desist order.<sup>3106</sup>

Enforcement Counsel have persuasively established that the cited statute does not apply to enforcement actions seeking cease and desist orders.<sup>3107</sup> As such and for the reasons cited in Enforcement Counsel’s Post-Hearing Reply Brief as to Paul McLinko, the assertion is found to be without merit and the affirmative defense is denied as to limitations applicable to cease and desist actions under the Federal Deposit Insurance Act.

Respondents argue the limitations period under Section 2462 is triggered once the elements of a claim are present.<sup>3108</sup> Enforcement Counsel respond that even if cease and desist actions are properly subject to the five-year limitation the continuing nature of Respondents’ action permits this enforcement action, as the misconduct attributed to each Respondent continued from before the five-year period well into the five-year period.

In support of their argument, Respondents cite to *Blanton v. OCC*.<sup>3109</sup> In *Blanton*, the Court of Appeals held:

A claim generally accrues “when the factual and legal prerequisites for

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<sup>3105</sup> Respondent Claudia Russ Anderson’s Proposed Findings of Fact and Conclusions of Law at 149; Respondent Claudia Russ Anderson’s Post-Hearing Reply Brief at 87; Respondent David Julian’s Proposed Findings of Fact and Conclusions of Law at 107; Respondent David Julian’s Post-Hearing Reply Brief at 92; Respondent Paul McLinko’s Proposed Findings of Fact and Conclusions of Law at 119; Respondent Paul McLinko’s Post-Hearing Reply Brief at 92.

<sup>3106</sup> Respondent David Julian’s Proposed Findings of Fact and Conclusions of Law at 107.

<sup>3107</sup> See Enforcement Counsel’s Post-Hearing Reply Brief as to Paul McLinko at 92-93, citing *SEC v. Graham*, 823 F.3d 1357, 1362 (11th Cir. 2016) (“Because injunctions are equitable, forward-looking remedies and not penalties within the meaning of § 2462, we conclude that the five-year statute of limitations is inapplicable to injunctions such as the one the SEC sought in this case.”); See *First Nat’l Bank of Bellaire*, 697 F.2d 674 at 680-81 (5th Cir. 1983) (“Congress designed the Cease and Desist power to give the Comptroller ‘a statutory means of moving quickly and effectively to require adherence to the law and cessation and correction of unsafe or improper practices.’ ... In other words, the Cease & Desist power was envisioned as a means of correcting improprieties and not as a form of punitive relief.”); *In re \*\*\**, Nos. FDIC-83-252b&c, FDIC-84-49b, -50e, 1985 WL 303871, at \*104 (Aug. 19, 1985) (final decision); *In re The Stephens Security Bank*, 1991 WL 789326, at \*4 (FDIC Aug. 9, 1991).

<sup>3108</sup> Respondent David Julian’s Proposed Findings of Fact and Conclusions of Law at 108.

<sup>3109</sup> Respondent David Julian’s Proposed Findings of Fact and Conclusions of Law at 108, citing *Blanton v. OCC*, 909 F.3d 1162, 1171 (D.C. Cir 2018).

filing suit are in place.” *Proffitt v. Fed. Deposit Ins. Corp.*, 200 F.3d 855, 862 (D.C. Cir. 2000) (quoting *3M Co. (Minnesota Min. & Mfg.) v. Browner*, 17 F.3d 1453, 1460 (D.C. Cir. 1994)). Here, an actionable infraction consists of two elements: first, the bank official must “recklessly engage[ ] in an unsafe or unsound [banking] practice”; and second, the reckless practice must be “part of a pattern of misconduct.” 12 U.S.C. § 1818(i)(2)(B)(i)(II), (ii)(I). *For our purposes, then, a claim accrues each time a bank official recklessly engages in an unsafe or unsound banking practice as part of a pattern of misconduct.*

Blanton contends that the OCC's overdraft claim accrued long before June 30, 2010, because the Bank's practice of honoring Campos's overdrafts began before Blanton assumed the CEO role. But the initial onset of the Bank's ongoing (and preexisting) pattern of honoring the overdrafts did not alone trigger the limitations clock. *Rather, each instance of an unsafe or unsound practice triggers a new claim if part of a pattern of misconduct. See Proffitt*, 200 F.3d at 863-64.

As a result, each time the Bank, under Blanton's direction, honored a Campos overdraft without having imposed adequate risk controls, an unsafe or unsound banking practice occurred, continuing the pattern of misconduct and causing a new claim to accrue. It follows that each honored overdraft after June 30, 2010 (there were at least ten) constituted an actionable banking practice as part of a pattern of misconduct. And even though the OCC “might well have brought an action earlier,” its “failure to do so” does not make the claims it elected to bring “untimely.” *Id.* at 864.

Respondents’ conduct as reported above constituted a continuous pattern of inactions, affirmative misconduct, and false and misleading reporting that was inconsistent with their respective risk management and control function responsibilities. Under the continuing violations doctrine, where one of the cognizable effects of Respondents’ respective misconduct has occurred within the limitations period, an action to enforce Section 1818 is timely.<sup>3110</sup>

Under this doctrine, a continuing violation occurs when a defendant creates a situation from which new claims continue to arise, notwithstanding that some of the defendants’ specific acts fell outside the limitations period.<sup>3111</sup> Under the

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<sup>3110</sup> *Proffitt v. Fed. Deposit Ins. Corp.*, 200 F.3d 855, 861 (D.C. Cir. 2000).

<sup>3111</sup> *In re Conover*, Nos. FDIC-13-214e, FDIC-13-217k, 2016 WL 10822038, at \* 21 (Nov. 29, 2016) (final decision) (citing *In re Leuthe*, Nos. FDIC-95-15e, FDIC-95-16k, 1998 WL 438323, at \*5 (June 26, 1998) (final decision)); *Courtney v. La Salle Univ.*, 124 F.3d 499, 505 (3d Cir. 1997) (“[I]n the case of a continuing unlawful practice, every day that the practice continues is a fresh wrong for purposes of the statute of limitations.”).

continuing violations doctrine, the statute of limitations under 28 U.S.C. § 2462 is tolled for a claim that otherwise would be time-barred where the violation giving rise to the claim continues to occur within the limitations period.<sup>3112</sup> I find that from the record now assembled, this is the case for all claims presented against Mr. McLinko. As such, given the facts reported above, the limitations of actions defense raised by Mr. McLinko with respect to the civil money penalty assessment is without merit and is denied.

Finding insufficient factual and legal bases to support the affirmative defense based on 28 U.S.C. § 2462, the defense is without merit and is denied.

### Respondents' Affirmative Defenses

#### Estoppel

Mr. McLinko asserted the Tribunal erred in striking Mr. Julian's affirmative defenses, including the defense of estoppel.<sup>3113</sup> For the reasons articulated in the Tribunal's April 1, 2020 Order Regarding Enforcement Counsel's Motion to Strike Respondents' Affirmative Defenses, the assertion is found to be without merit and the contents of that Order are incorporated by this reference. The parties argue further that, with respect to the evidence presented during the hearing, the OCC provided positive assessments and feedback; that they relied upon that feedback; that the reliance was detrimental; that that the OCC now seeks to deflect blame from the OCC to the Respondents.<sup>3114</sup>

While Respondents are not precluded from the affirmative defense of equitable estoppel, they bear an increased burden in order to prevail on their estoppel claim. "To succeed on a claim of equitable estoppel against the government, a plaintiff must not only prove all the elements of equitable estoppel, but also that the government committed affirmative misconduct." *Charleston Hous. Auth. v. U.S. Dep't of Agric.*, 419 F.3d 729, 739 (8th Cir.2005). Through this affirmative misconduct requirement, "[t]he Supreme Court has imposed a more stringent standard for estopping the government because there is a strong public interest in upholding the rule of law, even where hardship may result to individuals in particular cases." *Wang*, 823 F.2d at 1276. The claimant bears the "heavy burden" of establishing that the government engaged in affirmative misconduct. *Morgan v. Comm'r*, 345 F.3d 563, 566 (8th Cir.2003).

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<sup>3112</sup> *Nat'l Park & Conversation Ass'n, Inc. v. Tenn Valley Auth.*, 502 F.3d 1316, 1322 (11th Cir. 2007).

<sup>3113</sup> Respondent David Julian's Proposed Findings of Fact and Conclusions of Law at 109; Respondent Paul McLinko's Proposed Findings of Fact and Conclusions of Law at 143; Respondent Claudia Russ Anderson's Proposed Findings of Fact and Conclusions of Law at 150.

<sup>3114</sup> Respondent David Julian's Proposed Findings of Fact and Conclusions of Law at 109.

If a claimant satisfies the affirmative misconduct requirement, he then must prove the four traditional elements of estoppel: (1) a “false representation by the government;” (2) government intent to induce the claimant to act on the misrepresentation; (3) a lack of knowledge or inability to obtain true facts on the part of the claimant; and (4) the claimant's “reliance on the misrepresentation to his detriment.”<sup>3115</sup>

Respondents asserted the government engaged in affirmative misconduct by providing “positive assessments and feedback concerning Mr. Julian and WFAS.”<sup>3116</sup> This assertion will not support the affirmative defense relied upon by Respondents.<sup>3117</sup> While the record reflects positive feedback had been provided by the OCC’s examiners, the record also reflects that the basis for that feedback was reporting by Respondents that falsely assured the OCC, the Bank’s A&E committee, and its Board of Directors that Community Bank’s risk management controls over sales practices misconduct was proactive and effective. No reliance on this body of misinformation (supplied by Mr. Julian, Ms. Russ Anderson, and Mr. McLinko directly and through their roles as members of risk management committees) can support an estoppel claim.

Upon these findings, the affirmative defense of estoppel as pleaded and as presented through the evidence adduced during the hearing is without merit and is denied.

#### Constitutional Violations

a. Article II<sup>3118</sup>

Mr. Julian asserted, and Mr. McLinko joined in the assertion, that deference given to examiners under *Sunshine*<sup>3119</sup> violated the Appointments Clause,<sup>3120</sup> and that the presiding ALJ was not validly appointed by the appropriate head of a department and that any subsequent

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<sup>3115</sup> *Rutten v. United States*, 299 F.3d 993, 995 (8th Cir.2002).

<sup>3116</sup> Respondent David Julian’s Proposed Findings of Fact and Conclusions of Law at 109.

<sup>3117</sup> See, *Bartlett v. U.S. Dep’t of Agric.*, 716 F.3d 464, 475–76 (8th Cir. 2013),

<sup>3118</sup> Respondent David Julian’s Post-Hearing Reply Brief at 93-94; Respondent Claudia Russ Anderson’s Proposed Findings of Fact and Conclusions of Law at 150; Respondent Claudia Russ Anderson’s Post-Hearing Reply Brief at 87; Respondent David Julian’s Proposed Findings of Fact and Conclusions of Law at 123-31; Respondent David Julian’s Post-Hearing Reply Brief at 98-99; Respondent Paul McLinko’s Proposed Findings of Fact and Conclusions of Law at 144-47; Respondent Claudia Russ Anderson’s Proposed Findings of Fact and Conclusions of Law at 150; Respondent Claudia Russ Anderson’s Post-Hearing Reply Brief at 87.

<sup>3119</sup> *Sunshine State Bank v. FDIC*, 783 F.2d 1580 (11th Cir. 1986).

<sup>3120</sup> Julian COL ¶¶425-60.



ratification of such appointment does not cure the deficiency. Finding an insufficient factual and legal basis has been advanced in support of this claim, I find the claims raised by Respondents to be without merit and are denied.

b. Article III<sup>3121</sup>

Mr. Julian asserted and Mr. Julian joined in the assertion that this administrative enforcement action is unconstitutional. In support, Mr. Julian cited Respondents' Joint Motion for Summary Disposition on the Basis of Their Appointments, Removal, and Improper Signatory Defenses (May 12, 2020); Respondents' Joint Motion for Summary Disposition on the Basis of Their Article III, Seventh Amendment, and Due Process Defenses (May 12, 2020). The merits of these claims have been addressed by prior orders of this Tribunal, the contents of which are incorporated by reference. Upon this record, the claims raised by Respondents in these motions are denied for the reasons appearing in the record.

c. Discovery

Respondents Julian and McLinko asserted the Tribunal erred by striking their discovery requests seeking information covered by *Brady v. Maryland*.<sup>3122</sup> The merits of these claims were addressed in the Order Regarding Enforcement Counsel's Motion to Strike Portions of Respondent Julian's et al. Fourth Request for Production of OCC Documents (Oct. 28, 2020). Upon this record, the claims raised by Respondents in these motions are denied for the reasons appearing in the record.

d. Summary Disposition

Mr. Julian asserted, and Mr. McLinko joined in the assertion, that the Tribunal erred in entertaining summary disposition and in ruling that Enforcement Counsel had established 356 statements of material fact concerning Mr. Julian and that only twelve of the asserted statements were controverted.<sup>3123</sup> The record includes the analysis of claims presented by the parties, which analysis is incorporated by reference.<sup>3124</sup> Upon this record, the claims raised by Respondents in these motions are denied for the reasons appearing in the record.

e. Pretrial

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<sup>3121</sup> Respondent David Julian's Proposed Findings of Fact and Conclusions of Law at ¶¶461-66.

<sup>3122</sup> Julian COL at ¶ 467.

<sup>3123</sup> Julian COL at ¶¶ 467-74; Respondent David Julian's Post-Hearing Reply Brief at 94-98 Respondent Claudia Russ Anderson's Proposed Findings of Fact and Conclusions of Law at 150 (Due Process Clause, consultation with counsel, Summary Disposition); Respondent Claudia Russ Anderson's Post-Hearing Reply Brief at 87.

<sup>3124</sup> See Order Regarding Enforcement Counsel's Motions for Summary Disposition, issued July 20, 2021.

Mr. Julian asserted, and Mr. McLinko joined in the assertion, that the Tribunal erred in striking certain witnesses and quashing certain subpoenas addressed to those witnesses.<sup>3125</sup> The record includes an analysis of the claims presented by the parties, which analysis is incorporated by reference.<sup>3126</sup> Upon this record, the claims raised by Respondents in these motions are denied for the reasons appearing in the record.

f. The Hearing

Mr. Julian asserted, and Mr. McLinko joined in the assertion, that the Tribunal erred by making an opening statement at the start of the evidentiary hearing, on the ground that the statement constituted evidence of prejudice.<sup>3127</sup> Upon review of the record and finding the statement consisted of findings already entered into the record through the summary disposition process, I find the claim is without merit and is denied.

Mr. Julian and Mr. McLinko asserted error in the order of hearing, including orders regarding when witnesses would be permitted to testify, the import of answers provided, whether the questions sought information beyond the scope of direct examination, examiner competence and credibility, limits on the scope of testimony permitted, the provisional admission of documentary evidence, the admission of evidence for the truth of the matter asserted, the admission of evidence asserted to be not relevant, the admission of expert witness opinions, the admission of summary exhibits, the admission of prior statements, the admission of documents provided by the Bank, the admission of agreements between the Bank and other parties, the admission of certain spreadsheets, the admission of testimony regarding certain audits, the admission of or the exclusion of peer bank reports.<sup>3128</sup>

Upon review of the premises and finding an insufficient factual and legal basis has been presented, I find the claims are without merit and are denied.

g. ALJ Recusal

Mr. Julian asserted and Mr. McLinko joined in the assertion that the ALJ's

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<sup>3125</sup> Julian COL at ¶¶ 475-76.

<sup>3126</sup> Order Regarding EC's Motions to Quash Hearing Subpoenas Directed to Certain OCC Personnel and Strike Them from Respondents' Witness Lists and for Order to Show Cause, issued Aug. 18, 2021.

<sup>3127</sup> Julian COL at ¶ 478.

<sup>3128</sup> Julian COL at ¶ 479-504; Respondent David Julian's Proposed Findings of Fact and Conclusions of Law at 123-31; Respondent David Julian's Post-Hearing Reply Brief at 98-99; Respondent Paul McLinko's Proposed Findings of Fact and Conclusions of Law at 144-47; Respondent Claudia Russ Anderson's Proposed Findings of Fact and Conclusions of Law at 150; Respondent Claudia Russ Anderson's Post-Hearing Reply Brief at 87.

conduct warranted recusal.<sup>3129</sup> The record includes an analysis of the claims presented by the parties, which analysis is incorporated by reference.<sup>3130</sup> Upon this record, the claims raised by Respondents in these motions are denied for the reasons appearing in the record.

h. Seventh Amendment<sup>3131</sup>

Mr. Julian asserted and Mr. McLinko joined in the assertion that the administrative enforcement action violated his Seventh Amendment right to a jury trial, citing in support *Tull v. United States*, 481 U.S. 412, 417, 421-422, 425 (1987); *SEC v. Lipson*, 278 F.3d 656, 662 (7th Cir. 2002); and *Jarkesy v. SEC*, 2022 WL 1563613, at \*4-5 (5th Cir. May 18, 2022). Finding an insufficient factual and legal basis has been advanced to explain and support these claims, I find the claims raised by Respondents to be without merit and are denied.

i. Proposed Recommendation for a New Hearing

Mr. Julian<sup>3132</sup> proposed and Mr. McLinko joined in the proposal that if the Tribunal does not recommend the dismissal of the case against him, the Tribunal should recommend that the Comptroller grant a new hearing.<sup>3133</sup> In support, Mr. Julian incorporated by reference Respondents' Motion for Disqualification Based on Personal Bias and Other Disqualification Under 5 U.S.C. § 556(b) (Oct. 15, 2021) and Respondents' Motion for Reconsideration (May 27, 2022).

I find the premises supporting this assertion to be without merit, for the reasons set forth in the Order Regarding Respondents' Objection Pursuant to 12 U.S.C. 1818(h)(1) and Motion for Reconsideration, issued on September 6, 2021, the Order Regarding Respondents' Motion for Disqualification Based on Personal Bias and Other Disqualifications under 5 U.S.C. § 556(b), issued on November 3, 2021 and the Order Regarding Respondents' Motion for Reconsideration and for Leave to File, issued on July 5, 2022. Incorporating by reference the determinations issued through these orders and finding Respondents have presented an insufficient factual and legal basis in support of the request for a new hearing, the request is denied.

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<sup>3129</sup> Julian COL at ¶¶ 505-08.

<sup>3130</sup> See, Order Regarding Respondents' Motion for Disqualification Based on Personal Bias and Other Disqualification under 5 U.S.C. § 556(b), issued November 3, 2021, and Order Regarding Respondents' Motion for Disqualification Based on Personal Bias and Other Disqualification, issued Nov. 5, 2021.

<sup>3131</sup> Respondent David Julian's Proposed Findings of Fact and Conclusions of Law at 131.

<sup>3132</sup> Ms. Russ Anderson incorporated this claim by reference, see Respondent Russ Anderson's Post-Hearing Reply Brief at 87; as did Mr. McLinko, see Respondent McLinko's Post-Hearing Reply Brief at 1.

<sup>3133</sup> Respondent Julian's Post-Hearing Reply Brief at 100.

6. Proposed Orders

A proposed Cease and Desist Order is attached, accompanied by a proposed Civil Money Penalty assessment against Mr. McLinko.

Date: December 5, 2022

Christopher B. McNeil, JD, PhD  
U.S. Administrative Law Judge  
Office of Financial Institution Adjudication

**CERTIFICATE OF SERVICE**

On October 20, 2022 and December 5, 2022, the Office of Financial Institution Adjudication provided hard drives containing the hearing exhibits and the certified record upon the Hearing Clerk, Office of the Comptroller of the Currency by encrypted hard drive, along with a copy of the index of the certified record, a copy of the index of exhibits, the Executive Summary, and Recommended Decision in OCC AA-EC-2019-72 regarding Respondent Paul McLinko.

Also on December 5, 2022, I served upon the parties by email transmission a copy of the index of the certified record, a copy of the index of exhibits, along with copies of the Executive Summary and Recommended Decision in OCC AA-EC-2019-72, Respondent Paul McLinko, upon:

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**UNITED STATES OF AMERICA**  
**DEPARTMENT OF THE TREASURY**  
**OFFICE OF THE COMPTROLLER OF THE CURRENCY**

In the Matter of

**Paul McLinko**, Former  
Executive Audit Director  
Wells Fargo Bank, N.A.  
Sioux Falls, South Dakota

OCC AA-EC-2019-72

**[PROPOSED] CEASE AND DESIST ORDER AND ORDER FOR THE ASSESSMENT  
OF A CIVIL MONEY PENALTY**

**WHEREAS**, the Office of the Comptroller of the Currency (“OCC”) initiated cease and desist and civil money penalty proceedings against Paul McLinko (“Respondent”), former

Chief Auditor of Wells Fargo Bank, N.A. (“Bank”), pursuant to 12 U.S.C. § 1818(b) and (i), through the issuance of a Notice of Charges for Orders of Prohibition and Orders to Cease and Desist and Notice of Assessments of a Civil Money Penalty dated January 23, 2020 in *In the Matter of Carrie Tolstedt, et al.* (“Notice”) based on Respondent’s conduct related to the Bank’s sales practices misconduct problem;

**WHEREAS**, Respondent timely filed an Answer to the Notice and requested a hearing on February 12, 2020. Respondent filed an Amended Answer on August 7, 2020;

**WHEREAS**, pursuant to 12 U.S.C. §§ 1818(b) and (i) and 12 C.F.R. Part 19, a hearing was conducted before an Administrative Law Judge in Sioux Falls, South Dakota and remotely via videoconference between September 13, 2021 and January 6, 2022. Respondent was given a full opportunity to appear, present evidence, examine and cross-examine witnesses, file proposed findings of fact and conclusions of law, and file post-hearing and reply briefs;

**NOW, THEREFORE**, having considered the evidence presented at said hearing and the record as a whole, the arguments of both parties, and the Recommended Decision issued by the presiding Administrative Law Judge, and pursuant to the authority vested in him by the Federal Deposit Insurance Act, as amended, 12 U.S.C. § 1818, the Comptroller of the Currency (“Comptroller”) hereby issues the following cease-and-desist and civil money penalty orders (“Order”):

## **ARTICLE I**

### **JURISDICTION**

(1) The Bank is an “insured depository institution” as that term is defined in 12 U.S.C. § 1813(c)(2).

(2) Respondent was an officer and employee of the Bank and was an “institution-affiliated party” of the Bank as that term is defined in 12 U.S.C. § 1813(u), having served in such capacity within six (6) years from the date of the Notice. *See* 12 U.S.C. § 1818(i)(3).

(3) The Bank is a national banking association within the meaning of 12 U.S.C. § 1813(q)(1)(A), and is chartered and examined by the OCC. *See* 12 U.S.C. § 1 *et seq.*

(4) The OCC is the “appropriate Federal banking agency” as that term is defined in 12 U.S.C. § 1813(q) and is therefore authorized to initiate and maintain these cease and desist and civil money penalty actions against Respondent pursuant to 12 U.S.C. § 1818(b) and (i).

**ARTICLE II**  
**ORDER TO CEASE AND DESIST**

(1) Whenever Respondent is employed by or is otherwise affiliated with any depository institution as defined in 12 U.S.C. § 1813(c)(1) or otherwise becomes an institution-affiliated party as defined in 12 U.S.C. § 1813(u), Respondent shall:

- (a) Comply fully with all laws and regulations applicable to the depository institution;
- (b) Not engage or participate in any unsafe or unsound practice, as that term is used in Title 12 of the United States Code;
- (c) Fulfill his fiduciary duty of care and act in the best interests of the depository institution at all times;
- (d) Adhere to the depository institution's written charters, policies, procedures, and any other governing documents, or receive written permission from appropriate authorized individuals to do otherwise;
- (e) With respect to any Board or management committee of which he is a member, act diligently, prudently, honestly, and carefully in carrying out his responsibilities;
- (f) Document, at least annually, his title, role, and responsibilities with respect to the depository institution, and produce such documentation to the appropriate Federal banking agency upon request;
- (g) Participate, at least annually, in accredited training regarding audits of sales practices, culture, retail banking, and incentive compensation programs;
- (h) Ensure that any audit he manages, oversees, or supervises is adequately scoped and competently executed, and that reports of such audits identify the root cause of any identified controls breakdown; and
- (i) Ensure that any audit department or team he manages, oversees, or supervises is independent and objective, adequately audits the most significant risks, and completely and accurately reports on the

effectiveness of risk management and controls in audit reports and to the Board.

(2) If Respondent is currently an institution-affiliated party, he shall provide the Chief Executive Officer and Chairman of Board of the institution with a copy of this Order within ten (10) days of issuance of this Order.

(3) Prior to accepting any offer of a position that causes Respondent to become an institution-affiliated party, he shall provide the Chief Executive Officer and Chairman of the Board of the institution with a copy of this Order.

(4) Within ten (10) days of satisfying the requirements of paragraphs (2) and/or (3) of this Article, Respondent shall provide written certification of his compliance to the OCC by mail to Director, Enforcement, Office of the Comptroller of the Currency, 400 7th Street, SW, Washington, DC 20219, or by email to the address provided by the OCC.

(5) If, at any time, Respondent is uncertain whether a situation implicates paragraph (1) of this Article, or if Respondent is uncertain about his duties arising from such paragraph, he shall obtain, at his own expense, and abide by the written advice of counsel regarding his duties and responsibilities with respect to the matter. To comply with this paragraph, Respondent shall engage counsel who is in no way affiliated with the institution; and who has never been subject to any formal sanctions by any Federal banking agency, either by agency order or consent, as disclosed on the banking agencies' websites.

### **ARTICLE III**

#### **ORDER FOR CIVIL MONEY PENALTY**

(1) Respondent shall pay a civil money penalty in the amount of 1.5 Million Dollars (\$1,500,000.00), which shall be paid in full upon the effective date of this Order.

(2) Respondent shall make payment in full via wire transfer, in accordance with instructions provided by the OCC. The docket number of this case (AA-EC-2019-72) shall be referenced in connection with the submitted payment.

**ARTICLE IV**

**CLOSING**

(1) Respondent is prohibited from seeking or accepting indemnification from any insured depository institution for the civil money penalty assessed and paid in this matter.

(2) If, at any time, the Comptroller deems it appropriate in fulfilling the responsibilities placed upon him by the several laws of the United States of America to undertake any action affecting the Respondent, nothing in this Order shall in any way inhibit, estop, bar or otherwise prevent the Comptroller from so doing.

(3) The provisions of this Order are effective at the expiration of thirty (30) days after the service of this Order by the Comptroller, and shall remain effective and enforceable, except to the extent that, and until such time as, any provisions of this Order shall have been stayed, modified, terminated, or set aside in writing by the Comptroller, his designated representative, or a reviewing court.

IT IS SO ORDERED, this \_\_\_\_ day of \_\_\_\_\_, 202\_

\_\_\_\_\_  
Comptroller of the Currency  
Office of the Comptroller of the Currency